OECD Multi-level Governance Studies

Making Decentralisation Work in Chile

TOWARDS STRONGER MUNICIPALITIES



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Foreword

The OECD Regional Development Policy Committee (RDPC) is a leading international forum in the fields of regional, urban, and rural development policy and in multi-level governance. It has led the way in acknowledging the importance of multi-level governance and place-based approaches tailored to local and regional needs. To support the RDPC's leadership in this policy dialogue, the OECD created the Multi-Level Governance Studies series in 2016, focusing both on country and thematic work.

Country reviews provide policy makers and other stakeholders with a diagnosis of the strengths and weaknesses of multi-level governance frameworks; an assessment of the main challenges in subnational finance and public investment management; comparative data and indicators; benchmarks and good practices to promote learning, as well as recommendations on ways to strengthen multi-level governance practices. Thematic reviews focus on priority topics identified by the country, such as decentralisation reforms, public investment, municipal governance, subnational finance and territorial reforms.

The OECD's subnational government database is updated annually and supports the multi-level governance work with data on subnational government structure and finance. Subnational governments - defined as all levels of government below the national level, i.e. administrative regions, states/provinces, counties, and municipalities - are responsible, on average, for 40% of public expenditures in OECD countries and 60% of public investment. In 2014, the OECD adopted the Recommendation on Effective Public Investment across Levels of Government. To help countries implement the Recommendation while also strengthening their multi-level governance practices, an Implementation Toolkit was developed and complements the multi-level governance studies series.

Decentralisation refers to the delegation of responsibilities, political decision making and fiscal powers to lower levels of government. Rather than a clear-cut allocation of roles, many responsibilities are often shared among levels of government, and this requires appropriate multi-level governance systems. For decentralisation to work efficiently, a number of conditions must be met, starting with sufficient and appropriate resources to fulfil new responsibilities but also adequate capacities at the subnational level, proper co-ordination mechanisms, effective monitoring systems and a good balance in the way various policy functions are decentralised. It is, therefore, important to have a systemic and balanced approach.

This report examines the multi-level governance framework in Chile. It provides a diagnosis of the strengths and challenges of the Chilean multi-level governance system and includes comparative data and a set of benchmarks to promote the exchange of good practices and foster learning. It offers recommendations on how to further improve the system, with a particular focus on strengthening and modernising municipalities in the context of Chile's decentralisation reforms.

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Table of contents

Acronyms and abbreviations 17

Executive summary 19

Assessment and recommendations 23

1. Towards a renewed, ambitious and sustainable municipal decentralisation agenda 24
2. Reforming the municipal finance system to meet current and future municipal needs 26
3. Establishing a stronger and more transparent fiscal responsibility framework: The necessary corollary of fiscal decentralisation reform 28
4. Designing more appropriate equalisation mechanisms for better territorial equity and performance 29
5. Modernising human resources management in Chilean municipalities 31
6. Enhancing the quality and efficiency of municipal services to guarantee effective decentralisation 33
7. Reinforcing transparency, accountability and citizen participation practices at the municipal level 34
8. Strengthening strategic co-ordination within and across levels of government in a context of enhanced decentralisation 36

Chapter 1 **The Chilean municipalities in the evolving national multi-governance system** 39

Introduction 40
How is governance organised in Chile? 47
The decentralisation process: Historical overview, recent changes and prospects 54
The role of municipalities in this evolving institutional system 72
References 124

Chapter 2 **The fiscal challenge: Developing Chilean municipalities' financial capacities and accountability** 131

Financial weakness of public engagement and low decentralisation in Chile 133
Trends in municipal finances in Chile 144
The limitations of the mechanisms financing local budgets and potential avenues for improvement 161
Fiscal responsibility framework at the municipal level 206
References 233

Chapter 3 **The equity challenge: Can existing horizontal equalisation mechanisms reduce municipal fiscal disparities?** 239

Introduction: Chile is characterised by strong inter-regional and inter-municipal disparities 240
Inter-municipal financial disparities 245
The FCM and the treatment of inter-municipal disparities 263
Change in FCM operating procedures 278

References 290

Chapter 4 **The management challenge: Strengthening the human capacities and management tools of municipalities** 293

Modernising human resource management in Chilean municipalities 294
Enhancing the quality and efficiency of municipal services in Chile 325
References 348

Chapter 5 **The participatory challenge: Strengthening participatory governance at the local level** 353

Introduction 354
The current state of participatory governance in Chile 357
Participatory governance frameworks, institutions and actors in Chile 362
Adjusting transparency techniques and building accountability for stronger participatory governance 376
Citizen engagement: Activating the local level for stronger participatory governance 390
Conclusion and recommendations 413
Annex 5.A. Guiding principles for open and inclusive policy making 423
References 425

Chapter 6 **Strengthening strategic co-ordination within and across levels of government** 435

Building a coherent multi-level institutional framework 436
Reinforcing multi-level co-ordination and dialogue through adequate instruments 443
Supporting co-operation between municipalities 461
References 482

Figures

Figure 1.1. The singularity of Chile: A very limited and centralised public intervention 42
Figure 1.2. Contribution to national labour productivity growth 2010-2013 44
Figure 1.3. Percentage contribution to national GDP growth 2010-13 44
Figure 1.4. Decentralisation and wealth: comparing the level of subnational expenditure in GDP with the level of GDP per capita 45
Figure 1.5. Organisational chart of the Chilean multi-level governance system 48
Figure 1.6. Historical timeline of decentralisation in Chile 1970-2017 60
Figure 1.7. Decentralisation agenda: Regional and municipal levels 70
Figure 1.8. Average municipal population (number of inhabitants, 2015-2016) 73
Figure 1.9. Median municipal size (number of inhabitants, 2015-2016) 73
Figure 1.10. Average Municipal size in selected Latin American countries (2015) 73
Figure 1.11. Average municipal area in Chile is large compared to other OECD countries (2015-2016) 74
Figure 1.12. Municipalities by population size class in the OECD (% of municipalities, 2015-2016) 75
Figure 1.13. Population by municipality 76
Figure 1.14. Distribution of municipalities in Chile ranked by population density, 2014 78
Figure 1.15. Distribution of population and area by type of region, 2014 78
Figure 1.16. Level of poverty by municipality 80
Figure 1.17. Breakdown of responsibilities across subnational government levels: A general scheme 102

Figure 1.18. Adopting an open-systems perspective 115
Figure 1.19. Chilean municipalities operate in a multi-level governance system undergoing profound changes 117
Figure 2.1. Public expenditure in OECD countries (% of GDP, 2014) 134
Figure 2.2. Public expenditure in OECD countries (USD PPP per capita, 2014) 134
Figure 2.3. Public investment in OECD countries (USD PPP per capita, 2014) 135
Figure 2.4. Public investment in OECD countries (% of GDP, 2014) 135
Figure 2.5. Tax revenue as a % of public revenue in the OECD countries (2014) 136
Figure 2.6. Tax revenue as a % of GDP in the OECD countries (2014) 136
Figure 2.7. Public debt as a % of GDP in the OECD countries (2014) 137
Figure 2.8. Subnational government expenditure per capita in OECD countries (USD PPP, 2014) 138
Figure 2.9. Subnational government expenditure as a % of GDP in OECD countries (2014) .. 138
Figure 2.10. Subnational government expenditure as a % of total public expenditure and as a % of GDP in OECD and selected Latin American countries, 2014 (2013 for Latin American countries) 139
Figure 2.11. Subnational government investment per capita in OECD countries (USD PPP, 2014) 140
Figure 2.12. Subnational government investment as a % of GDP (2014) 140
Figure 2.13. Subnational government investment as a % of public investment in OECD countries and selected Latin American countries (2014) 141
Figure 2.14. Structure of subnational government revenue (%, 2014) 142
Figure 2.15. Subnational tax revenue as a % of GDP in OECD and selected Latin American countries 143
Figure 2.16. Subnational tax revenue as a % of public tax revenue in OECD and selected Latin American countries 143
Figure 2.17. Change in the share of municipal expenditure and revenue in total general government 145
Figure 2.18. Change in municipal and general government expenditure and revenue 1990 – 2015 (constant 2015 CLP, base 100 = 1990) 146
Figure 2.19. Change in municipal expenditure and revenue as a % of GDP over 1990 – 2015 .. 146
Figure 2.20. Change in composition of municipal expenditure 1990-2015 (% of total municipal expenditure) 148
Figure 2.21. Change in composition of municipal expenditure 1990-2015 (constant 2015 CLP, base 100 = 1990) 149
Figure 2.22. Change in structure of municipal revenue 1990-2015 (% of total municipal revenue) 150
Figure 2.23. Breakdown of municipal revenue 1990-2015 (constant 2015 CLP, base 100 = 1990) 150
Figure 2.24. Change in the weight of local expenditure by sector (2011-2015) (% of total expenditure) 153
Figure 2.25. Change in the breakdown of municipal sector expenditure transfers (2011-2015) (Millions of current CLP) 154
Figure 2.26. Change in the structure of expenditure transfers in the municipal sector (2011-2015) (%) 154
Figure 2.27. Investment as a % of total expenditure in 2015 (%) 156
Figure 2.28. Investment by FIGEM category of municipalities (% of total expenditure, 2015) .. 157
Figure 2.29. Change in local government investment as a % of general government 1990-2015 158
Figure 2.30. Change in local government investment as a % of GDP 1990-2015 158

Figure 2.31. Breakdown of revenues in the municipal sector (2015) ... 159
Figure 2.32. Breakdown of revenues in the education sector (2015) ... 159
Figure 2.33. Breakdown of revenues in the health sector (2015) ... 159
Figure 2.34. Fiscal imbalances in the OECD countries in 2014 ... 160
Figure 2.35. Regional and local programmes ... 167
Figure 2.36. Breakdown of permanent own revenue in 2015 (%) ... 168
Figure 2.37. Change in the breakdown of permanent own revenue between 2011 and 2015 (constant billion CLP) ... 169
Figure 2.38. Recurrent taxes on property in the OECD and other Latin American countries (% of GDP, 2014) ... 172
Figure 2.39. Income from municipal licenses* per capita (2015) ... 176
Figure 2.40. Breakdown of subnational debt by type of liabilities (%, 2014) ... 196
Figure 2.41. Breakdown of claims for irregularities in the purchase process by public actors ... 202
Figure 3.1. Gini index of inequality of GDP per capita across TL3 regions, 2000 and 2013 ... 240
Figure 3.2. Regional variation in GDP per capita (as a % of national average), 2013 (TL2) ... 240
Figure 3.3. Regional concentration of GDP, TL3 regions ... 241
Figure 3.4. GDP breakdown by region (2013) ... 242
Figure 3.5. Employment breakdown by region (2014) ... 242
Figure 3.6. Regional GDP per capita (2013, current USD, current PPP) ... 242
Figure 3.7. Relative performance of Chilean regions by well-being dimension ... 243
Figure 3.8. Regional disparities in multi-dimensional living standards are higher than for income alone Coefficient of variation (higher values mean larger disparities), 2012 ... 244
Figure 3.9. Local expenditure of all three sectors per capita and population (log-log scale) (2015) ... 247
Figure 3.10. Local expenditure of all three sectors per capita (2015) ... 248
Figure 3.11. Municipal investment per capita (annual average 2011-2015, constant CLP, value 2015) ... 252
Figure 3.12. Average 2011-2015 municipal investment per capita and per year (constant thousand CLP) compared to municipal population (log) ... 253
Figure 3.13. Territorial tax per capita and population (log-log scale) (2015) ... 254
Figure 3.14. Business licenses per capita and population (log-log scale) (2015) ... 255
Figure 3.15. Factorial axes of differentiation in per capita municipal expenditure by nature (logarithmic transformation) (population INE) ... 257
Figure 3.16. Factorial axes of differentiation in per capita municipal expenditure by area (logarithmic transformation) (population INE) ... 258
Figure 3.17. Factorial axes of differentiation in per capita municipal revenue (logarithmic transformation) (population INE) ... 259
Figure 3.18. Factorial axes of the per capita revenues of the municipalities of the Metropolitan region of Santiago (logarithmic transformation) ... 260
Figure 3.19. Clusters of municipalities of the Metropolitan Region of Santiago based on municipal resources ... 260
Figure 3.20. Local expenditure of all three sectors per capita in the Metropolitan Region of Santiago (2015) ... 262
Figure 3.21 Relation between revenue per capita of the FCM and population (2015) (log-log scale) ... 275
Figure 3.22. Change in municipal revenue inequalities (2001-2015) ... 276
Figure 4.1. Public sector employment as a percentage of total employment, 2009 and 2013 ... 296
Figure 4.2. Distribution of general government employment across levels of government, 2011 ... 297

Figure 4.3. Comparing municipal employees and municipal population (2015) 298
Figure 4.4. Breakdown of staff according to their status in the central government and in the municipal sector 299
Figure 4.5. Breakdown of education and health sector personnel by status, 2015 300
Figure 4.6. Subnational staff expenditure as a share of total public staff expenditure 304
Figure 4.7. Structure of public expenditure at the subnational level, 2014 OECD unitary countries 305
Figure 4.8. Share of expenditure in training in Chilean municipalities (2014 and 2015) 312
Figure 4.9. Level of professionalisation of personal staff (as a %, municipal sector, 2015) 314
Figure 4.10. Progress of the management of municipal services 327
Figure 4.11. Basic services for minimum standards 331
Figure 5.1. One in four young people in the OECD is not at all interested in politics 359
Figure 5.2. Individuals using the Internet to interact with public authorities by type of activity (over the past 12 months), 2014 379
Figure 5.3. OURdata Index: Open, Useful, Reusable Government Data, 2014 383
Figure 5.4. The spectrum of public engagement 391
Figure 5.5. Barriers to partnering with citizens in service delivery (2010) 395
Figure 5.6. Common measurements tool 399
Figure 5.7. Top 10 engagement tools included in municipal ordinances for citizen participation in Chile % (2015) 404
Figure 6.1. Regional Investments 2001-2015 457
Figure 6.2. Timeline of the Project 463
Figure 6.3. Stages of pilot project on metropolitan areas in Concepción 472

Tables

Table 1.1. Type and numbers of subnational governments in the OECD: Country by country, 2014-2015 50
Table 1.2. Chilean regions and municipalities (from most to least populated) 77
Table 1.3. Indigenous communities in OECD countries 106
Table 2.1. Change in the structure of expenditure transfers in the municipal sector (2011-2015) (%) 154
Table 2.2. Changes in the Chilean educational system 155
Table 2.3. From the apparent final distribution to the actual original distribution of municipal tax revenues (2013) 169
Table 2.4. Territorial tax: properties included in taxed properties (2014) 173
Table 2.5. Municipal, education, health and cemeteries budgets 207
Table 2.6. Budget Timeline 208
Table 3.1. Correlation coefficients between expenditure indicator per capita (log value) and population (log value)* (2015) 246
Table 3.2. Revenue sources of the FCM 268
Table 3.3. Ranking of the municipalities according to the dependency ratio on FCM revenue (2015) (%) 277
Table 4.1. Distribution of public employees across levels of government in Chile, 2015 297
Table 5.1. Average number of municipal councillors in select OECD countries, 2015 370
Table 5.2. Municipal matters in which COSOC have had input or participated (2015) 372
Table 5.3. Percentage of civil society organisations active in Chile classified by INCPO1 categories 374
Table 5.4. Examples of engagement aims and mechanisms that support their achievement 409
Table 5.5. Examples of engagement activity outcomes matched to mechanism results 409

Table 5.6. Matching citizen engagement mechanism to outcomes desired……410

Boxes

Box 1.1. Decentralisation, wealth and growth 45
Box 1.2. Deconcentration and decentralisation..... 49
Box 1.3. CORE responsibilities 52
Box 1.4. *Cabildos*, the origins of Chilean municipalities 54
Box 1.5. The first regionalisation process (*primera regionalización*) 57
Box 1.6. The National Municipal Information System (SINIM)..... 63
Box 1.7. An increasing number of stakeholders are promoting decentralisation and regionalisation in Chile 64
Box 1.8. Report of the Presidential Advisory Commission on Decentralisation and Regional Development 68
Box 1.9. Main laws adopted since 2014 concerning the municipal sector 71
Box 1.10. Municipal poverty in Chilean municipalities 79
Box 1.11. The FIGEM typology 81
Box 1.12. Sub-municipal delegations: Some international experiences from the OECD 84
Box 1.13. Municipal exclusive and non-exclusive functions and fundamental attributions..... 86
Box 1.14. Areas of intervention of municipalities in Chile: Approach by the organisation of services 88
Box 1.15. Strong involvement of municipalities in social programmes 90
Box 1.16. Principles of organisation and financing of the education sector through the voucher system..... 93
Box 1.17. Municipalities and the Chilean health system 96
Box 1.18. How to assign education responsibilities across levels of government? The cases of France and Austria 98
Box 1.19. Transferring health responsibilities from municipalities to self-governing regions: The current Finnish reform 100
Box 1.20. Breakdown of responsibilities and functions across subnational government levels 101
Box 1.21. Asymmetric decentralisation: Defining differentiated competences for different municipalities: the case of Colombia, Denmark and Czech Republic 103
Box 1.22. Decentralisation can offer space to design effective policies supporting the development and integration of indigenous communities: The experience of OECD and Chile 106
Box 1.23. Public private partnerships for infrastructure and urban development in Chile..... 113
Box 1.24. Decentralisation reforms: Three closely interconnected dimensions to be considered in an “open-system” perspective 114
Box 1.25. Multi-level governance reforms: Policy makers are faced with a variety of challenges 118
Box 1.26. Ad hoc commissions and committees facilitating the dialogue with stakeholders for designing and implementing multi-level governance reform 120
Box 1.27. Key recommendations for designing and implementing the municipal decentralisation agenda 121
Box 2.1. The relative decrease in municipal education activities 155
Box 2.2. Central government transfers in the education and health sectors 163

Box 2.3. Capital transfers to Chilean regions, municipalities, associations of municipalities, and corporations 166
Box 2.4. Aquaculture and mining licenses 176
Box 2.5. Recommendation of the OECD Council on Effective Public Investment across Levels of Government 183
Box 2.6. Fiscal decentralisation reforms in selected OECD countries: From earmarked grants to general purpose grants 185
Box 2.7. Local public companies in the OECD and Colombia 189
Box 2.8. Land-based financing instruments: Focus on several international practices 190
Box 2.9. Subnational PPPs in Colombia 192
Box 2.10. Accessing credit in the form of loans or bonds : OECD practices at the subnational level 195
Box 2.11. The transformation of the UK Public Works Loan Board 198
Box 2.12. The role of national public development banks in the financing of subnational governments: Takeaways from experiences in OECD and Latin American countries 198
Box 2.13. The development of local government funding agencies in the OECD 200
Box 2.14. Municipal public procurement: A high level of irregularities resulting from a lack of municipal capacities 202
Box 2.15. Key recommendations for improving municipal finance 204
Box 2.16. Recent reforms of subnational government balanced budget rules 211
Box 2.17. Debt and debt service restrictions on subnational governments in selected OECD and Latin America countries 214
Box 2.18. New expenditure ceilings for subnational governments in selected OECD countries 216
Box 2.19. Procedures in case subnational governments fail to meet fiscal rules in selected OECD countries 217
Box 2.20. Reforms to curb the use of unfunded mandates in the United States 220
Box 2.21. Escape clauses and follow-up mechanisms 221
Box 2.22. SINIM budget databases 222
Box 2.23. Examples of municipal classifications for financial management purposes: Colombia and South Africa 225
Box 2.24. Monitoring local government debt and municipalities in financial distress 226
Box 2.25. Auditing local finances in Sweden and France 227
Box 2.26. Key recommendations for a more comprehensive fiscal framework and increased fiscal responsibility 228
Box 3.1. Regional well-being in Chile and OECD countries 243
Box 3.2. Overview of fiscal equalisation systems in OECD countries 264
Box 3.3. How to evaluate the effectiveness of an equalisation system? 269
Box 3.4. Key recommendations for reforming equalisation mechanisms 286
Box 4.1. OECD guidelines for designing, implementing and assessing workforce planning 302
Box 4.2. United Kingdom: Government principles for compensation reform 307
Box 4.3. Chile's Municipal and Regional Training Academy 310
Box 4.4. OECD experience on delegating pay-setting to subnational governments. 320
Box 4.5. Key recommendations for modernising human resource management 324
Box 4.6. Diagnosis of the Quality of Municipal Management 326
Box 4.7. Minimum Service Standards in Indonesia 329

Box 4.8. User charters in healthcare: The Netherlands and the United Kingdom 332
Box 4.9. What does a service charter looks like? The example of Andalucía and Jalisco, Mexico 333
Box 4.10. Model for Quality Municipal Management: A proposal by RIMISP..... 334
Box 4.11. Indicators and incentives: Local Public Service Agreements in the United Kingdom 337
Box 4.12. Performance measurement in Norway, Ontario (Canada) and US cities 338
Box 4.13. Common obstacles to building meaningful performance indicators 340
Box 4.14. Abolition of the Audit Commission (United Kingdom)..... 340
Box 4.15. Digital Municipalities in Chile 342
Box 4.16. Key recommendations for enhancing the quality and efficiency of municipal services in Chile 344
Box 5.1. The "managerial" and "governmental" typologies of local government administration 355
Box 5.2. Chile's Plan for Civic Education in Public Educational Establishments Law No. 20.911 359
Box 5.3. Approaches to promoting greater youth participation in civic life: The United States, Canada and France 361
Box 5.4. Chile's government frameworks and implementation mechanisms to support participatory governance 363
Box 5.5. National councils to support citizen participation 367
Box 5.6. The Economic, Social and Environmental Council in France 368
Box 5.7. Fund for Neighbourhood Development (*Fondo de Desarrollo Vecinal* - FONDEVE) 375
Box 5.8. Government information sharing online in the United Kingdom 378
Box 5.9. "311-Toronto" and other non-emergency service numbers 380
Box 5.10. The London DataStore to promote transparency, accountability and participation .. 384
Box 5.11. Building municipal accountability frameworks in Canada 385
Box 5.12. Balancing active consultation and consultation fatigue 388
Box 5.13. Our Córdoba Citizen Network and the *Plan de Metas* 389
Box 5.14. Community involvement in Chile's neighbourhood recovery programme: *Quiero mi Barrio* 392
Box 5.15. Centres of expertise on citizen engagement in Canada, Denmark, and the United Kingdom 394
Box 5.16. Learning from citizens to improve service delivery in Canada and Finland..... 399
Box 5.17. Building participatory capacity in among youth in the United Kingdom 401
Box 5.18. A sampler of methods for strengthening citizen engagement practices 405
Box 5.19. Key recommendations for strengthening participatory governance in Chile 415
Box 6.1. State representatives at regional and local levels in some OECD countries 440
Box 6.2. Regionalisation bills and regional pilot programmes 442
Box 6.3. Regional and municipal development plans..... 444
Box 6.4. Articulating planning and funding: The experience of EU funds 449
Box 6.5. Inter-ministerial Committee at the regional level..... 451
Box 6.6. Local government associations in Chile..... 452
Box 6.7. Co-ordination platforms in Italy..... 453
Box 6.8. Multi-stakeholder commission to discuss decentralisation reforms in Chile..... 454

Box 6.9. Formal steps regarding programming contracts (CPs) in Chile 457
Box 6.10. Enforcement mechanisms for more effective contracts across levels of government 459
Box 6.11. State-region planning contracts in France 460
Box 6.12. Different forms of "sharing and pooling" 461
Box 6.13. Association of Municipalities of the Province of Llanquihue for Sustainable Waste Management 463
Box 6.14. Financing inter-municipal associations: the case of France 465
Box 6.15. Incentives for cross-jurisdictional co-operation 467
Box 6.16. Contributions to public space in Chile 470
Box 6.17. Bill on regional responsibilities: A new regional governance for metropolitan areas 471
Box 6.18. Metropolitan governance pilot programme in Concepción 471
Box 6.19. Examples of good practices of metropolitan co-operation: Medellin and Bucaramanga 474
Box 6.20. The City Deals in the United Kingdom and Netherlands 475
Box 6.21. Contractual arrangements in urban areas in France 477
Box 6.22. Key recommendations for strengthening strategic co-ordination within and across levels of government 478

Acronyms and abbreviations

ACHM	*Asociación Chilena de Municipalidades* / Chilean Association of Municipalities
ADP	*Alta Dirección Pública* / senior public management
APP	*Asociaciones público-privado* / Public-Private Partnerships (PPP)
AMUCH	*Asociación de Municipalidades de Chile* / Association of Municipalities of Chile
ASEMUCH	*Confederación Nacional de Funcionarios Municipales de Chile* / National Confederation of Municipal Officials of Chile
BID	*Banco Interamericano de Desarrollo* / Inter-American Development Bank (IADB)
CEPAL	*Comisión Económica para América Latina y el Caribe* / Economic Commission for Latin America and the Caribbean (ECLAC)
CGR	*Contraloría General de la República* / Comptroller General's Office
COMICIVYT	*Comisión Interministerial Ciudad, Vivienda y Territorio* / Interministerial Commission for City, Housing and Territory
CORE	*Consejo regional* / Regional council
CORECIVYT	*Comisión regional Ciudad, Vivienda y Territorio* / Regional Commission for City, Housing and Territory
CORFO	*Corporación de Fomento de la Producción* / Chilean Economic Development Agency
COSOC	*Consejo Comunal de Organizaciones de la Sociedad Civil* / Municipal Council of Civil Society Organisations
CP	*Convenios de programación* / Programming Contracts
CSO	*Organizaciones de la sociedad civil (OSC) / Civil Society Organisations*
CTAM	*Comité Técnico Asesor para la Modernización Municipal* / Technical Advisory Committee for Municipal Modernisation
DAEM	*Departamento de Educación Municipal* / Municipal Education Administration Department
DIPRES	*Dirección de Presupuestos* / Budget office
ERD	*Estrategia Regional de Desarrollo* / Regional Development Strategy
FCM	*Fondo Común Municipal* / Municipal Common Fund
FIGEM	*Fondo de Incentivo al Mejoramiento de la Gestión Municipal* / Incentive Fund for the Improvement of Municipal Management
FNDR	*Fondo Nacional de Desarrollo Regional* / National Fund for Regional Development
FONASA	*Fondo Nacional de Salud* / National Health Fund
FOSIS	*Fondo de Solidaridad e Inversión Social* / Solidarity and Social Investment Fund
FRIL	*Fondo Regional de Iniciativa Local* / Regional Local Initiative Fund
FUA	*Areas urbanas funcionales* / Functional Urban Area
GORE	*Gobierno Regional* / Regional government

LOCGAR	*Ley Orgánica Constitucional en Materia de Gobierno y Administración Regional* / Organic Constitutional Law on Regional Government and Administration
HRM	*Recursos humanos (RRHH)* / Human Resources Management
LOCMUN	*Ley Orgánica Constitucional de las municipalidades* / Organic Constitutional Law on Municipalities
MDS	*Ministerio de Desarrollo Social* / Ministry of Social Development
MINEDUC	*Ministerio de Educación* / Ministry of Education
MINSAL	*Ministerio de Salud* / Ministry of Health
MINVU	*Ministerio de Vivienda y Urbanismo* / Ministry of Housing and Urbanism
MOP	*Ministerio de Obras Públicas* / Ministry of Public Works
MoU	Memorandum of Understanding
ODEPLAN	*Oficina de Planeamiento Nacional* / National planning office
OECD	*Organización para la Cooperación y el Desarrollo Económico (OCDE*) / Organisation for Economic Co-operation and Development
ONEMI	*Oficina Nacional de Emergencia del Ministerio del Interior y Seguridad Pública N* National Office of Emergency, Ministry of Interior and Public Order
PADEM	*Plan Anual de Desarrollo Educativo Municipal* / Development Plan of Municipal Education
PLADECO	*Plan de Desarrollo Comunal* / Municipal development plan
PNUD	*Programa de Naciones Unidas para el Desarrollo* / United Nations Development Programme (UNDP)
PRC	*Plano Regulador Communal* / Municipal Regulating Plan
PRI/PRM	*Plan Regulador Intercomunal/Metropolitano* / Inter-Municipal and Metropolitan Regulating Plans
PROT	*Plan Regional de Ordenamiento Territorial* / Regional Plan for Land-Use Planning
RS	*Recomendación favorable* / Favorable recommendation
SEMUG	*Servicios Municipales Garantizados* / Guaranteed municipal services
SEGPRES	*Secretaría General de la Presidencia* / General Secretariat of the Presidency
SEREMI	*Secretaría Regional Ministerial* / Regional ministerial secretariat
SERVIU	*Servicios de Vivienda y Urbanización* / Housing and Urban Development Agency
SII	*Servicio de Impuestos Internos* / Internal Revenue Service
SINIM	*Sistema Nacional de Información Municipal* / National system of municipal information
SMEs	*Pequeña y mediana empresas (PYMES)* / Small and Medium Sized enterprises
SNSS	*Sistema Nacional de Servicios de Salud* / National System of Health Services
SUBDERE	*Subsecretaría de Desarrollo Regional y Administrativo* / Secretariat for Regional Development and Administration
UFEMUCH	*Unión de Funcionarios Municipales de Chile* / Union of Municipal Civil Servants of Chile
UTM	*Unidad Tributaria Mensual* / Monthly unit fee

Executive summary

The Chilean government requested that the OECD conduct a comprehensive analysis of the country's municipal system, identifying the main challenges and recommending policy options for reform in the framework of the current governmental decentralisation agenda.

Chile is one of the most centralised countries in the OECD. As of today, regional governments are "mixed entities" (deconcentrated and decentralised) and municipalities are the only self-government entities. However, because of the nature of their tasks, their funding arrangements and the strong dependence on the central government, they are more "public services providers" than genuine local governments.

Chilean local government expenditure represents 3% of GDP and 13% of total public expenditure, compared to the OECD average of 17% and 40%, respectively. Local investment accounts for 12% of public investment – the lowest rate among OECD countries. Dependent on central government transfers, mainly earmarked to fund specific sectors, municipalities have limited own-source revenues. Chile is the only OECD country where local borrowing is prohibited. Municipalities are constrained in terms of staff resources and public services management. Policy design and implementation are still largely defined by the centre in a top-down process.

Chile also has among the highest levels of territorial disparities in the OECD. In 2013, Chile recorded the second highest level of GDP concentration among OECD countries, after Greece (index of 55 vs. 39 in the OECD on average).

Increasingly, a new model of economic and social development, based on place-based policies, is needed in order to maximise growth and productivity across the entire territory. Moving towards such an approach in Chile requires reforming the multi-level governance system so that the role of regions and municipalities may be reinforced. Chile needs to strengthen subnational contributions to national productivity in order to achieve more balanced territorial development.

Aware of these challenges, the Chilean government has made decentralisation a priority since the late 2000s. Important steps were taken in 2009 to further advance the agenda but a decisive impetus came with the 2014-2018 presidential programme, which set up a Presidential Advisory Commission for Decentralisation and Regional Development and defined a Decentralisation Agenda.

At municipal level, the Agenda's objectives are to empower municipalities by providing them with the tools, capacities, financial resources and legitimacy to effectively carry out their responsibilities and deliver local public services in a more efficient, transparent, accountable and equitable manner.

However, the implementation of this agenda has remained partial. In May 2016 a law was adopted allowing mayors to increase and reorganise the municipal workforce, but much more remains to be done. It is thus necessary to ensure that municipal reform:

- Is fully embedded in the overall multi-level governance reform.
- Is well-coordinated with on-going sector reforms and the regional reform (cf. law enacted in 2017 which allows direct election of the regional governors and laws under preparation related to future regional responsibilities and finances);
- Is conceived and implemented in a comprehensive, gradual and well-sequenced manner. Both a detailed action plan and an implementation plan are necessary, identifying the necessary steps for a reform's successful execution and including tools and indicators to permanently monitor and assess progress.

Key recommendations developed in this report include:

- Setting up a permanent "decentralisation committee" that involves public and private stakeholders as well as establishing an inter-ministerial committee on regional and municipal decentralisation at the central government level.
- Clearly redefining the assignment of responsibilities as a first step, determining the entire decentralisation process. A first line of work could consist of reducing shared tasks and increasing "territorial-based" exclusive responsibilities. The current uniformity principle should be reconsidered to favour more flexible and asymmetrical approaches adapted to municipal heterogeneity.
- Improving the municipal financing system to provide municipalities with the financial capacity to exercise their responsibilities. This issue is all the more crucial in the perspective of further devolution (or reorganisation) of tasks. It is recommended to increase and optimise existing funding sources (grants and subsidies, taxes), to diversify resources (property income, user charges, municipal concessions) and to expand borrowing capacities in a prudent and controlled manner.
- Establishing a stronger and more transparent fiscal responsibility framework is a necessary corollary of fiscal decentralisation. Presenting a consolidated account at the municipal level, including all three sectors (education, health and municipal activities) and corporations is urgently needed as well as reinforcing internal and external control mechanisms.
- Reforming the existing horizontal compensation system. While the Municipal Common Fund has proven its efficiency in terms of "solidarity", it also has some counter-productive effects on local and regional development. The system should be reviewed and complemented by other equalisation arrangements to combine solidarity and equity principles and improve economic efficiency (e.g., modification of allocation rules, vertical equalisation and regionalised approach).
- Improving human resources management practices, which is a prerequisite for efficient and effective decentralisation. Although the 2016 law represents a significant progress, it is still necessary to increase staff workforce and professionalisation levels, provide more recognition (attractive work conditions and remuneration) and improve managerial skills. Greater workforce planning and management, performance assessment, training strategies and strengthened HRM functions are needed.
- Streamlining and better coordinating the different performance management models of municipal services. The SEMUG system, which aims to define

minimum quality standards for basic municipal services, is a step in the right direction but it will be necessary to move towards a more comprehensive, coordinated and flexible management and performance system, complemented by "municipal service charters".

- Reinforcing transparency, accountability and citizen participation practices. Transparency techniques are strong but could be adjusted to better support accountability. Participatory practices, too often focused on the "inform" and "consult" forms of interaction, should encourage proactive forms of engagement with citizens. The capacity to contribute to municipal development and exercise oversight functions, particularly by municipal councils, Community Councils of Civil Society Organisations, and civil society organisations should be reinforced.
- Further reinforcing multi-level co-ordination and dialogue across and among levels of government through specific instruments and platforms (e.g. planning instruments, territorial contracts) and through stronger co-operation between municipalities (municipal associations, metropolitan governance).

Assessment and recommendations

Chile's complex geography, history and economic development model are all factors which account for why it is particularly challenging to implement a decisive decentralisation process. Chile has a long tradition of being a heavily centralised unitary country despite a history marked by several decentralisation pushes, and even an attempt at federalism. During the dictatorship, the governance reform in the 1980s, which transferred several central government tasks (education and health, for instance) and associated resources, was more a policy of deconcentration of state responsibilities to local entities than a real decentralisation policy. Since the return of democracy, progress has been made towards decentralisation and regionalisation which are seen as a means of re-democratising the country and reforming the state. Progress, however, has been slow. The centralist heritage remains strong and deeply-rooted in Chile's political-administrative culture and behaviour, thus slowing and scaling back the decentralisation initiatives.

Chile ranks among one of the most centralised countries in the OECD, alongside Greece and Ireland. In 2014, subnational government expenditure accounted for 3.0% of GDP and 13.1% of public expenditure (vs OECD averages of 16.6% and 40.2%, respectively). The same applies to public investment in which municipalities play a minor role (12.0% of public investment and 0.3% of GDP), with Chile ranking last among OECD countries. Chilean municipalities have limited own-source revenues and they largely depend on central government transfers earmarked to fund specific sectors or activities. Chile is the only OECD country where local borrowing is prohibited. Policy design and implementation are still largely defined from the centre by national ministries and public agencies in a top-down process. Locally, policy is carried out by deconcentrated state territorial entities and partially implemented by municipalities, often according to national uniform norms, that do not take into account local specificities and needs.

Chile has opted for the mix of two models: on the one hand, an economic model that trusts the market's ability to distribute resources and tends to limit public intervention; on the other hand, a "centralist model" of political-administrative structure. In several respects, this model has been successful, managing to ensure internal political and macroeconomic stability, national unity as well as economic efficiency and growth. However, this model has started to show its limitations. It has favoured social and economic concentration in Santiago and mining regions, reinforcing inter-regional and local disparities across the national territory. According to the Gini index, Chile displayed the greatest disparity in GDP per capita across TL3 regions in the OECD in 2013. The country also recorded the second highest level of GDP concentration among OECD countries, after Greece (index of 55 vs. 39 in the OECD on average). While Chile still has high productivity gaps compared to other OECD countries and that productivity growth has trended at below zero for much of the past two decades, growth and productivity remained territorially concentrated. Between 2000 and 2013, 69% of the GDP growth and most labour productivity growth were generated in Santiago.

A new model is needed to maximise growth and productivity across the territory while making them more balanced and inclusive. It is necessary to develop a more integrated territorial approach capable of mobilising regional productivity catch-up potential. Moving towards such an approach in Chile requires establishing a governance structure capable of context-sensitive interventions. Thus, it is now necessary to reform the multi-level governance system so that the role of subnational governments may be reinforced.

1. Towards a renewed, ambitious and sustainable municipal decentralisation agenda

Decentralisation has become a governmental priority, aiming at creating self-governing regions and modernising the municipal system

Recognising the interdependencies between decentralisation, regional and local development, and increased productivity and growth, the Chilean government has made decentralisation a priority on its policy agenda. Important steps were taken in 2009 to further advance the agenda. Following this, a decisive impetus was given in 2014 when the president, Michelle Bachelet, once again put decentralisation at the core of the 2014-2018 presidential programme, defining a Decentralisation Agenda and setting up a Presidential Advisory Commission for Decentralisation and Regional Development, which presented a detailed action plan in October 2014. The government also started to engage in the preparation of bills. Progress has again recently accelerated, marking a fundamental shift towards decentralisation.

The territorial agenda has two main pillars, regional and municipal. The regional pillar aims at transforming the current regional government system into self-governing regions. Today, the system is mixed, i.e. both “deconcentrated” and “decentralised”, being formed by a regional executive (the intendant) appointed by the President of the Republic and an elected regional council in power since the 2014 regional elections. A new crucial and decisive milestone was reached in January 2017 with the publication of a law that provides for the direct election of the regional executive (future “regional governors"). This regionalisation process should also lead to the transfer of new responsibilities and resources to the 15 regional governments but bills are still under discussion or under preparation. Meanwhile, the municipal pillar is a process of modernisation and empowerment of the country's 345 municipalities. The reform aims at providing the municipalities with the tools, capacities, financial resources and legitimacy to improve their autonomy and performance while reducing municipal disparities. Such reform is crucially important as today, municipalities, defined by the Constitutional Organic Law on Municipalities, as “public law corporations” act more as “service delivery agents” than genuine “local governments”.

The implementation of the municipal decentralisation agenda remains timid and needs to be re-launched with stronger ambition and sustainability

One result of the municipal decentralisation process launched in 2014 has been a major reform (adopted in May 2016) through a law, known as *planta* law, which allows mayors to manage municipal staff with more freedom and flexibility and to improve professionalisation and remuneration. However, despite this fundamental advance, much more remains to be done to turn the municipal decentralisation objective into a reality. The municipal agenda has progressively evolved towards a more timid process,

increasingly disconnected from the global decentralisation agenda and more focused on "modernisation" aspects.

Municipalities have a wide range of responsibilities but most are shared with the central government, particularly with regard to primary and secondary education and basic public health. However, additional tasks are regularly given to municipalities by line ministries, for example in the social sector. This tends to increase the burden on municipalities as they often do not have adequate staff, technical and/or financial resources to properly carry out such tasks.

In addition, one particularity of Chile compared to other OECD countries, is that each municipality manages three separate budgets, one for education, one for health and one for the "municipal sector". These budgets are not consolidated at municipal level, making the overall understanding and assessment of municipal finance particularly difficult. In addition to this budget complexity, the whole of the municipal governance system suffers from fragmentation due to this sector-based approach: administrative practices, staff management, municipal services evaluation, etc., are governed by different rules. As a result, it is almost as if Chile has 1 000 municipalities rather than 345. The situation is further complicated by the existence of "municipal corporations" as well as by a reliance on the private sector to provide municipal infrastructure and public services through a system of national concessions.

There remain serious challenges to address in order to advance further in the process. It is necessary for the government to:

- Give a new boost to the municipal decentralisation reform and reaffirm the need for a gradual but determined municipal decentralisation agenda.
- Reaffirm the need for a comprehensive reform which addresses the different challenges (responsibilities, finance, capacities, local democracy and participation, etc.) in an integrated manner. Municipal reform is not only about modernisation, it is also about transforming municipalities into real decentralised local governments. It also means that Chile should work at reducing sector fragmentation in all areas (e.g. finance, staff, evaluation), which currently prevents municipal reform from being dealt with in a comprehensive way.
- Fully embed the municipal decentralisation reform in the overall multi-level governance reform to avoid building an imbalanced political structure. Regional and municipal pillars interact with each other: they should be interconnected and their activities carried out in closer co-ordination.

Based on these assumptions, several recommendations regarding the overall design and implementation of the reform can be made:

- A well-designed, well-sequenced decentralisation process is key. The first step is to start by clearly redefining the assignment of responsibilities as it is the entry point that should determine the entire decentralisation process. A first avenue of work to explore could consist of reducing the number and scope of shared competences and increasing "territorial-based" exclusive responsibilities. This reflection should take into account current regional and sectoral reforms in particular in the education sector. In fact, the "New Public Education" reform intends to remove the administration and management of public schools from municipalities and create a system of education based on new providers (Local

Education Services"). This "de-municipalisation" of education would have significant impacts on municipalities.

- Prepare a detailed action plan, which would ensure the requisite overall consistency between the different lines of the reform. It should be prepared, discussed and monitored by a permanent "decentralisation committee" that involves public and private key stakeholders co-ordinated by SUBDERE. This could help to build stronger legitimacy, better anchor the decentralisation agenda within the national reform programme and foster its sustainability. At the central government level, an inter-ministerial committee on regional and municipal decentralisation could also be established to ensure horizontal sectoral co-ordination, in particular in the education sector.
- An implementation plan should identify the necessary steps for a reform's successful execution. It should include tools and indicators to permanently monitor and assess progress.

The municipal decentralisation agenda should reconsider the principle of uniformity and instead envision more flexible and differentiated approaches

As a general principle guiding the municipal decentralisation reform, it is suggested to reconsider the principle of uniformity which has been one of the key foundations upon which Chile is built. Recently, some progress has been made in this regard but Chile could be more proactive in this field by recognising the extreme diversity and heterogeneity of the 345 Chilean municipalities in order to design and implement more place-based and differentiated policies, programmes and tools. Further development of SUBDERE's tools could support the differentiation process (typology of municipalities (FIGEM) and National System of Municipal information (SINIM). Chile could also experiment with flexibility and asymmetric decentralisation, in particular by assigning responsibilities to municipalities according to their characteristics, needs and capacity, based on "municipal categorisation" through pilot projects. A flexible approach could be implemented in the framework of the education reform. Asymmetric decentralisation could also be an effective way of supporting the development and integration of indigenous communities.

2. Reforming the municipal finance system to meet current and future municipal needs

While public intervention is limited and has remained highly centralised over the last 25 years, municipalities have a very restrictive expenditure framework which needs reform

The Chilean subnational sector plays a limited role and lacks resources and a real ability to act. This situation has not changed much over the past 25 years. While there has been a slight increase in municipal expenditure in this same period, seen against the sustained economic expansion of GDP and the significant social needs, the increase is modest and unsteady.

Municipal expenditures are dominated by education and health spending (32% and 17% of total municipal expenditure, respectively). As a result, staff expenditure is most significant, municipalities being in charge of teachers and medical staff salaries (staff expenditure accounts for more than 75% of expenditure in these two sectors). One third

of municipal sector spending is made of local subsidies transferred to the education and health sectors to cover structural deficits as well as of transfers to the Municipal Common Fund (FCM), the horizontal equalisation mechanism. Municipal investment is low and declining, accounting for 9.9% of expenditure in the municipal sector, 3.2% in education and 1.6% in health in 2015.

Reforming this very confined spending framework is closely linked to the issue of municipal responsibilities, in particular with respect to the weight of shared responsibilities, such as education and health.

The current municipal financing system does not meet current needs and requires profound changes to cope with decentralisation challenges

The structure of revenues varies substantially from one sector to the next. Education and health are very heavily funded by current transfers from the responsible line ministries. In the municipal sector, there is a larger diversity of revenue sources comprising permanent own-source taxes (around 40% of municipal sector revenue including the territorial tax, vehicle registration tax, business licenses, waste management fee, etc.), the FCM (30%), transfers (17%) and other revenues. The analysis of municipal revenue focuses on three diagnoses:

- All three sectors increasingly depend on central government grants which are all earmarked and part of a rigid and fragmented grant system. Apart from education and health, sectoral subsidies are distributed in a piecemeal fashion through competitive procedures by numerous ministries without any co-ordination, thereby leading to dysfunctions and inconsistencies. Capital transfers, including the National Fund of Regional Development (FNDR), are scarce and lack flexibility.
- The tax system appears to be lacking local margin of manoeuvre and is out of step with the concept of decentralisation. Municipal taxation power is weak: municipal prerogatives to set tax rates are non-existent or seriously restricted; their capacity to influence tax bases is limited while significant exonerations are decided at central level. In addition, a significant share of tax revenue is transferred to the FCM for redistribution purposes.
- Municipalities have very limited capacity to exploit other sources of revenue.

These deficiencies in municipal resources call for profound reform, in terms of decentralisation but also acceleration of public investment in infrastructure, especially in urban areas. Different methods can be explored for improving municipal financing, based on the optimisation of existing funding sources but also on the need to diversify them. In this regard, a gradual and asymmetric approach of fiscal decentralisation could be followed. The main recommendations include:

- Improving the system of intergovernmental grants by: 1) assessing the relevance and efficiency of the grant system in a comprehensive manner; 2) improving central government transfers co-ordination at the national and regional levels; 3) reviewing the functioning of the FNDR; and 4) and reducing the share of specific earmarked grants in favour of general purpose grants. The current reform giving rise to the creation of the National System of Public Education will most likely have a major impact on municipal grant financing as it intends to remove the duties of administration and management of public schools from municipalities'

remit and to confer them instead to new providers of public education (local education services).

- Enhancing own-source tax revenue raising capacity by: 1) consolidating tax base of several municipal taxes, e.g. reducing the number and level of exemptions of territorial tax; and 2) extending decision-making authority on taxation through tax breaks and ability to set tax rates.
- Diversifying resources by: 1) developing users' charges for municipal services; 2) increasing property income (land-based financing instruments and "municipal companies"; and 3) better exploiting municipal concessions and PPP schemes for large municipalities.

Fiscal decentralisation also requires improving municipal financial skills and concluding a "fiscal pact" with citizens, in particular to develop taxpayer willingness to pay taxes.

3. Establishing a stronger and more transparent fiscal responsibility framework: the necessary corollary of fiscal decentralisation reform

Fiscal decentralisation reform should be accompanied by a clearer and stronger fiscal framework

Chile has developed a strict fiscal framework for municipalities, which has several shortcomings. First, the municipal budgeting and accounting framework is particularly complex and opaque, as it comprises three different sectoral budgets, as mentioned earlier, as well as municipal corporation budgets. Second, there is a structural mismatch between local spending obligations and allocation of revenues. Third, internal control is carried out by municipal control units but this has proven insufficient at times, while the municipal council's effective role in such control exercises is very limited. External audit, carried out by the regional branches of the Comptroller General's Office, is unable to deal with the large number of entities involved and thus often consists only of the formal examination of reported accounts. Fiscal decentralisation reform should also provide for the definition and implementation of sound budgetary, accounting and reporting frameworks, based on common standards for all levels of government. This would facilitate the monitoring, control and transparency of financial operations. To that end, recommendations include:

- Presenting a consolidated account at the municipal level, including all sectors and corporations.
- Ensuring that decentralised responsibilities are financed with sufficient resources and introduce specific measures to avoid unfunded or under-funded mandates.
- More precisely and transparently estimating the revenues expected to be collected during the year and reinforce the role of the Comptroller General's Office in this process (consolidated national assessment and guidelines).
- Enhancing the current budget balance rule.
- Reinforcing internal and external control mechanisms and accountability.

Expanding borrowing capacities in a prudent manner for the most capable municipalities should be put on the decentralisation agenda

Municipal borrowing is a particularly challenging issue for Chile in the context of increased decentralisation. Currently, Chile's cardinal rule is to prohibit any kind of borrowing for municipalities. However, faced with structural deficits, municipalities have developed certain practices and used more unorthodox methods of raising finance (leasing and leaseback operations, arrears, temporary pension debt). Municipalities are *de facto* indebted, a situation which has raised red flags even if the amounts of money involved do not represent a significant issue at the aggregate level.

Independent of the need to closely monitor, clean up and tackle the causes of the current debt situation, expanding long-term borrowing capacities in a prudent manner for the most capable municipalities is an inevitable debate. Without calling into question the principles of healthy public financial management in Chile, it is legitimate to ask if the ban on municipal borrowing for investing in local infrastructure is economically, socially and territorially justified. It is a proven fact that using long-term borrowing to finance investment permits a better allocation of resources over time and intergenerational justice. It is also currently a financial necessity resulting from the lack of local savings and capital transfers. In anticipation of future changes resulting from stronger fiscal decentralisation, which would enhance municipalities' creditworthiness, Chile needs to examine less restrictive ways of accessing credit for the most capable cities, which could be authorised to borrow in a controlled manner to ensure economic stability and sound fiscal management. There are different avenues to explore combining:

- The implementation of appropriately prudential rules (e.g. debt stock and services' restrictions).
- The control of the borrowing market (e.g. contracting loans with the Treasury or public bank).
- The adaptation of borrowing mechanisms to the diversity of municipal needs and capacities instead of applying a blanket legally-based solution.
- The development of internal or external rating mechanisms to assess municipalities' creditworthiness.
- The development of a clear set of fiscal rules for "responsible borrowing", including regular audits and controls and enforcement mechanisms and sanctions for non-compliance.

4. Designing more appropriate equalisation mechanisms for better territorial equity and performance

Chile is characterised by strong inter-regional and inter-municipal disparities. A poorly designed decentralisation process may exacerbate this situation and lead to increased disparities across municipalities. While municipal expenditure budget amounts range from 1 to 325 between the smaller and larger municipalities, on a per capita basis there is an inverse relationship between the demographic size of the municipality and the main financial indicators – a prominent and fundamental characteristic of the Chilean municipal system. The relation is non-linear: the level of per capita expenditure decreases with the increase in population size to a threshold of around 90 000 to 110 000 inhabitants. The geographical representation of levels of per capita expenditure reveals

significant differences between extreme territories (north and south), sparsely populated and some mountain areas with high values, and the largest number of municipalities with lower levels of per capita expenditure. It means that local interventions face structural constraints because of low and dispersed population, which increases the costs of the provision of local public services and facilities.

A multi-dimensional analysis of expenditure and resources allows clusters of municipalities to be identified at the national level but also at the level of the metropolitan region of Santiago. The latter shows strong internal fiscal disparities, which are mainly determined by municipal revenues. The governance of the metropolitan region is one of main technical, financial and political challenges of the future. It will be crucial to find the adequate institutional arrangements to enable the sustainable development of the metropolis based on more solidarity and inclusiveness.

In 1979, Chile implemented an equalisation mechanism to reduce inter-municipal fiscal disparities by providing additional resources for the most vulnerable municipalities: the Municipal Common Fund (FCM) which is essentially a "compensation" system based on the horizontal redistribution of municipal resources across municipalities. The FCM's resources come from automatic contributions from municipalities via the transfer of a portion of their tax revenues. FCM has become a crucial part of municipal financing, accounting for 29% of total municipal sector revenue.

This horizontal equalisation mechanism is commendable in the light of the principle of solidarity and redistributive justice as the system benefits the most disadvantaged municipalities in terms of tax revenue and/or demographic, geographical and climatic constraints. Several studies confirm the redistributive character of the FCM and its effectiveness in achieving the goal of a reduction in inter-municipal inequalities. However, the FCM has also been the object of continuous political and economic criticism. One main criticism is that there are very few contributors and the beneficiaries (the majority of municipalities) are highly dependent on FCM contributions. Therefore, although the FCM has significant results in terms of territorial "solidarity", it does not favour territorial "equity" (fairness). Other FCM limitations concern the overall logic of the mechanism and its *modus operandi*: the complexity and lack of transparency of the allocation algorithm; its counterproductive and disincentive effects (fundamentally encouraging "fiscal laziness" and increasing dependency) and its lack of impact on reducing deeply-rooted inter-territorial inequalities.

FCM equalisation mechanisms have already been modified several times but have not served to fundamentally alter its basic approach. Overall, this instrument should be preserved, but it but it also requires strengthening and renewal in order to avoid or minimise the potential negative or adverse effects. It should be complemented by other equalisation arrangements to combine solidarity and equity principles as well as economic efficiency. Various avenues can be explored to help accomplish this, based on two approaches:

- In the short-term, modifying the allocation rules of the FCM to mobilise more potential contributors according to their level of wealth per inhabitant. It implies reviewing the way inequalities – in terms of charges and resources – are measured for both aspects (needs and revenues) and revising the distribution algorithm of the FCM.
- In the medium and long-term, adopting a more ambitious reform process: 1) developing a vertical equalisation mechanism through state grants; 2) shifting

from a uniform approach to a regionalised approach. The new equalisation system could combine nationally-collected resources and regionally and locally differentiated distribution of FCM funds.

5. Modernising human resources management in Chilean municipalities

Through recent reforms, Chilean municipalities now have the same arrangements of public employment as the central government. However, they do not necessarily have the same employment conditions. Consequently, municipalities remain weak in their capacity to perform their duties owing to difficulties in attracting and retaining a highly-skilled workforce. Low salaries, limited career opportunities, low qualifications, centralisation and weak HRM functions are just some of the factors that damage the attractiveness of municipal public administrations as employers. In addition, management of municipal employment is particularly challenging as it reflects the same complexity as budgetary issues. There are three categories of "municipal employees" (education, health, and municipal sector) which are all governed by specific regulations while they are under the municipal government purview.

Until recently, the regulatory framework has provided little flexibility in municipal workforce management. Adding to recent improvements in recognising and strengthening the municipal sector's civil service, Law No. 20.922, published in May 2016 and effective in 2018, represents a major step towards decentralisation of the management of municipal staff. However, there are still significant challenges.

There is a lack of staff and properly qualified staff in Chile's municipalities calling for greater workforce planning and management

While Chile has one of the smallest public workforces among OECD countries and is highly centralised, the share of municipal workers in the total public workforce is significant, representing more than half. Staff spending accounts for 52% of municipal spending, the largest share in the OECD. However, most of this municipal workforce is made up of education and health staff (43% and 25%, respectively), showing once again the weight of these two sectors. On its side, the municipal sector is characterised by a lack of staff, a high level of heterogeneity across municipalities and a significant proportion of temporary employees (56% compared with 17% in the central government). Civil servants (the *planta* system) and contractual workers currently account for 30% and 14% of staff, respectively. This is due to tight controls on recruitment, which has limited municipal ability to restructure and re-skill staff, and generates job insecurity and high turnover. With the *planta* law, mayors will be able to adjust their public workforce levels to better meet their needs by increasing the number of civil servants and contractual staff. This is a change in the right direction and provides a good opportunity to reinforce workforce planning and management in municipalities. It is thus recommended to: 1) engage municipalities in strategic workforce planning as a tool to plan the composition of the municipal workforce in terms of numbers, competencies and skills; 2) encourage the National Directorate for the Civil Service to develop a framework for workforce planning at municipal level; and 3) use SINIM in a more strategic perspective as an observatory of municipal staff.

Employment conditions in the municipal sector remain critical and municipal capacity needs strengthening

Municipalities fail to attract and retain talent. This is due, in part, to low salaries, particularly at professional and management levels, combined with some opacity concerning recruitment and promotion, and limited opportunities for mobility across levels of government, career development and training. The salary gap has widened with the development of the "senior civil service programme" in central government which does not cover municipal managers.

The level of professionalisation has grown in recent years but there are wide disparities across municipalities and there are significant gaps in competencies and skills. Despite significant progress in terms of training options for municipal employees, including the Municipal and Regional Training Academy developed by SUBDERE, training remains a great challenge and is not implemented as it should be.

Finally, performance assessment and management in the municipal sector are weak, unlike in the central government and in education and health sectors. The *Sistema de Alta Dirección Pública* (ADP), a senior manager system, implemented at the central level, has not been extended to reach municipalities. There is also a lack of managerial skills in municipalities despite the fact that these managers have a key role to play in the process of municipal modernisation. To tackle these different issues, the following is proposed:

- Make municipal salaries of non-professional and *contrata* staff (not concerned by the 2016 law) more attractive and competitive through a more comprehensive reform of the salary system.
- Enhance transparency in recruitment and promotion processes through the use of selection committees, interviewing panels and discontinue the practice of recruitment based exclusively on academic degrees.
- Develop "training strategies" focused on learning and personal development provided at different stages of the public servant's career and shifting from a system based on diplomas/degrees and formal qualifications towards "competency management" and job profiling.
- Shift from traditional human resources management to a performance-driven culture and promote the development of a coherent performance management strategy; investing in the management capability of municipalities at senior and middle management levels and extend the coverage of the ADP system at the municipal level.

The HRM function does not really exist and should be strengthened through more decentralisation and professionalisation

Now that municipalities will have more legal capacity to manage their workforce, they need to develop an HRM strategy. This could be done in two ways: first by professionalising the HRM function in municipalities and establishing an HRM unit, based on HR professional standards; and second by decentralising or delegating some HRM functions to municipalities, particularly in relation to the composition and restructuration of the workforce and certain elements of compensation. This would imply three complementary actions: 1) proceeding in a gradual and differentiated way according to municipal capacities and the learning process; 2) strengthening accountability mechanisms based on a reinforced leading role for the National Directorate for the Civil

Service; 3) and encouraging innovation and building capacity, e.g. developing HRM shared functions through municipal associations.

6. Enhancing the quality and efficiency of municipal services to guarantee effective decentralisation

The management framework of municipal services in Chile is complex and opaque

Today, the quality and efficiency of management and service provision vary substantially among Chilean municipalities because of significant disparities in terms of financial and human capacities but also because of fragmented responsibilities. The decentralising process could result in a widening of these disparities in terms of service access and quality. Therefore, it is crucial to address this challenge with appropriate instruments.

Today, municipalities are required to comply with several performance management models, depending on the services they provide. Municipal education and health services follow national guidelines defined by line ministries, while SUBDERE has developed different successive management and certification models aimed at diagnosing and improving the quality of municipal services. In 2015, as part of the decentralisation agenda, SUBDERE moved towards a new paradigm based on the new "System for Strengthening and Measuring the Quality of Municipal Services" (SEMUG) which aims to define minimum quality standards for basic municipal services. This is a step in the right direction that should be pursued by Chile. Continuing this approach implies taking the following steps:

- Establishing a more comprehensive management and performance system of municipal services ("System of Municipal Services'), covering all municipal sectors. It does not mean that just one institution should be responsible for assessing all municipal services but that co-ordination should be reinforced, at national and subnational levels.
- The system should be flexible and adapted to the different capacities of municipalities.
- The SEMUG approach could be complemented by "municipal service charters", which can favour flexibility and autonomy for municipalities to tailor their policies to local preferences.
- SEMUG should evolve towards a more integrated management and assessment model integrating additional components such as governance, citizen participation, resource management, planning, etc. based on clear and measurable performance indicators. SINIM could provide a starting point. In the long run, a new independent platform dedicated to this effort could be created.

Improving the municipal services management system requires strengthening local capacities

An efficient municipal services management system requires efforts from the central government to provide municipalities with the financial, human and technical means to effectively implement and use the system, this includes: 1) creating financial incentives through re-allocation of resources tied to results and improvements; 2) encouraging

municipalities to take advantage of the *planta* law to hire specialised professional staff; 3) organising specific capacity-building activities, in particular through SUBDERE's Regional and Municipal Academy; and 4) complementing by other activities such as digital governance (developing e-municipal services), innovation or administrative simplification.

Public service management needs reinforced co-ordination and "institutionalisation"

Decentralising implies a gradual adjustment of the institutional framework to improve co-ordination mechanisms across sectors and across levels of government as well as to ensure more sustainability and entrenchment in public management practices, limiting political vagaries. Appropriately "institutionalising" public service management can meet these expectations. In the short term, SUBDERE's role could be strengthened to oversee municipal management performance and co-ordinate with central and regional governments. In the longer run, an independent body could be created, in the form of a Superintendence of Guaranteed Municipal Services or a National Commission for the Certification of Subnational Governments.

7. Reinforcing transparency, accountability and citizen participation practices at the municipal level

Chile's government has a clear objective: to use participatory governance as a means to build a more inclusive and more democratic society. It is actively doing so. However, there are several limitations which explain the deficit in participatory governance.

Institutions, frameworks and actors to support greater participation are in place, but there is a lack of incentive and clarity for further strengthening

Chile has established institutions, frameworks and actors to support citizen engagement and promote participatory practices, specifically through the Law No. 20.500 and the Presidential Instruction 007/2014, which established a National Council for Citizen Participation and Strengthening Civil Society. However, the current system has several shortcomings.

The first limitation is the heavily top-down approach that has been adopted which does not give much motivation for municipalities, in a context of poor awareness, limited municipal resources and political will and absence of sanctioning mechanism nor financial incentives. It is thus proposed to introduce incentive mechanisms for greater compliance with legal frameworks, particularly Law No. 20.500 according to two lines: 1) providing the National Council for Citizen Participation and Strengthening Civil Society with stronger oversight functions, including sanctioning power; and 2) considering a financial incentive that rewards successful implementation of participatory mechanisms in a strategic fashion.

The second limitation may be the government's institutional approach based on a large bureaucratic and administrative structure. It is thus suggested to streamline the number of institutional oversight bodies and make their purpose clearer at both national and local levels.

The third limitation is at local level. Local level actors – citizens, elected and representative officials, and civil society organisations (CSOs) – are pivotal to successful

participatory governance but in Chile the degree of citizen engagement will depend considerably on the mayor. Thus, ensuring that engagement practices are properly institutionalised through elected officials and representative organisations is important and should be reinforced:

- Support the capacity of municipal councils to contribute to the overall development and management of their municipalities, shifting them from serving as advisory or auditing boards to being partners in municipal governance.
- Strengthen the role of COSOC in the municipality.
- Reduce the fragmentation of civil society organisation (CSO) networks and activity.

Transparency techniques are strong but could be adjusted and better support accountability

Chile's approach to promoting transparency is relatively streamlined and flexible, being based on a Transparency Law and a National Transparency Council, the latter having oversight and sanctioning capacities, on government bodies and municipalities clearly tasked to increase transparency and on significant investment in this field. At the local level, compliance with access to information laws has improved significantly. Transparency itself, however, is not sufficient. The Chilean approach may need to shift from strengthening transparency mechanisms to actively building accountability. In this regard, there are several concerns which can be addressed:

- Make accessing information easier and ensure that the information is relevant to all citizens by combining it with accountability and citizen engagement.
- Better align transparency mechanisms with citizen preferences and behaviour, ensuring that the information provided is the information sought.
- Enhance Open Government Data practices.
- Build greater accountability of local authorities to citizens by supporting municipal authorities in the design and implementation of performance measurement/indicator systems and by bringing citizens into the local level planning process early on.

Participatory capacity needs to be strengthened among all actors, especially at the local level

Chile has done a good job identifying and promoting the development of key participatory tools such as transparency websites, improved access to information, participatory budgets, citizen councils, etc. However, Chile's participatory practices tend to focus more on the "inform" and "consult" forms of interaction than on deeper forms of engagement with citizens. Therefore, there appears to be little room for citizen "voice" in policy or programme design and implementation. Participatory practices also need to be supported by multi-level governance practices. To move forward, Chile may need to reconsider how it wants to proceed in strengthening participatory governance. It is suggested to:

- Give government officials (at all levels) and civil servants a stronger understanding of engagement frameworks and the aims and implications of diverse engagement mechanisms.

- Promote "proactive" rather than "reactive" participation.
- Strengthening the voice of the next generation through municipal youth councils, candidate youth fora, etc.
- Make sure that municipal capacity in staff, resources and knowledge match the government's participation objectives.

8. Strengthening strategic co-ordination within and across levels of government in a context of enhanced decentralisation

Institutional fragmentation at the national and subnational levels requires building a more coherent multi-level institutional framework

In Chile, territorial strategies, policies, and investments tend to be centrally defined and fragmented across sectoral ministries. The impact of institutional fragmentation at the central level is often played out at the subnational level, bringing with it responsibility overlap and complex accountability lines. All actors tend to work separately with no incentives to co-operate. Some progress has been made recently through the creation in 2015 of the "Inter-ministerial Commission of City, Housing and Territory" or COMICIVYT (including CORECIVYT, its regional expressions).

The decentralisation reform might be a good opportunity to re-think and map the distribution of responsibilities centrally across ministries as well as vertically, across different levels of government in line with the OECD Recommendation of effective public investment across levels of government (OECD 2014b). It also provides the opportunity to build a more coherent multi-level institutional framework by reducing fragmentation at the central level though reinforced interministerial co-ordination. COMICIVYT could become the main co-ordination platform for regional and local issues while SUBDERE would be reinforced in its co-ordination role in regional, urban and territorial policies. Fragmentation at the subnational level could be addressed by strengthening the role of the elected regional governor as co-ordinator of regional policies; and institutionalising co-ordination instances at regional level involving municipalities.

Decentralising further requires reinforcing multi-level co-ordination and dialogue through specific instruments and platforms

Co-ordination mechanisms involving municipalities in a concrete and permanent way are lacking. Three main challenges have been identified: 1) poor co-ordination and coherence of spatial planning between the national, regional and municipal levels, often discouraged by a budgeting process and funding mechanisms; 2) under-representation of municipalities in national fora and inter-sectoral dialogues at the national and regional level; and 3) marginal involvement of municipalities in programming contracts (*Convenios de programación*, CP). Several recommendations can be made to address these challenges, including:

- Ensuring co-ordination through more coherent planning instruments at regional and local levels and improve linkages between planning and budgeting.
- Integrating municipalities into co-ordination platforms as permanent members at national and regional levels (COMICIVYT and CORECIVYT) and fostering

dialogue between municipalities and private key stakeholders, citizens and universities.

- Enhancing the role of municipalities in CPs which could move towards "territorial contracts" with stronger bottom-up components.

Decentralising further involves supporting more co-operation between municipalities, both in rural and metropolitan areas

Chile has made substantial progress in fostering inter-municipal co-ordination on a voluntary basis. Since 2009, municipal associations have a legal status, that of not-for-profit organisations and in 2011, the law was revised to provide a new impetus. However, the legal framework remains restrictive in terms of status (only private), resources (very limited) and scope of co-operation. Therefore, inter-municipal co-operation in Chile is in its early stages (53 associations registered in 2016) and integrated projects remain limited so far. The development of municipal associations poses substantial challenges for the modernisation of the municipal system, calling for increased support and incentives:

- Envision giving public status to municipal associations thus ensuring their financial stability and sustainability at least for some critical services and lagging areas.
- Developing financial and non-financial incentives for municipal associations.
- Defining specific budget lines, through FNDR or other funding, geared towards financing municipal association projects or joint investments exclusively.

At the level of functional urban areas, horizontal co-ordination is still very limited. Chile still has significant metropolitan governance gaps. The situation is currently evolving thanks to the recently approved Law on Contributions to Public Space and the regional reform on the transfer of competences currently discussed in the Congress. It plans to give the regions the responsibility of managing metropolitan areas, becoming the "metropolitan regional government". Several pilot projects are already ongoing allowing regional governments to manage metropolitan areas. Improving the metropolitan governance framework should be further encouraged and reinforced by: 1) pursuing and further supporting pilot projects; 2) developing a flexible (and not "one-size-fits-all") metropolitan governance model and ensuring a consultative bottom-up approach that includes relevant public and private actors; and 3) providing the adequate funding to finance metropolitan infrastructure and services (metropolitan tax), fostering equalisation mechanisms within metropolitan areas and promoting contractual arrangements specifically targeted at metropolitan areas.

Chapter 1

The Chilean municipalities in the evolving national multi-governance system

This chapter provides an overview of Chile's multi-level governance system, including its organisation, and of the decentralisation process in a historical perspective. It ends with an analysis of the role of municipalities in a changing institutional system, underscoring the challenge to transform Chilean municipalities from being mainly "public service providers" to genuine "local governments". It is important to acknowledge the diversity of municipal realities and to reconsider the current uniformity principle by encouraging more asymmetrical approaches to local development.

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

Introduction

Chile's complex geography, history and economic development model are all factors which account for why it is particularly challenging to engage the country in a decisive decentralisation process.

A complex geography, history and economic development model

Geographically, Chile is part of the American continent, Oceania and Antarctica. Bordered by Argentina, Bolivia and Peru, it has a total area of 740 243 $km^{2,}$ on par with OECD countries such as France or Turkey. But Chile is one of the longest and narrowest countries in the world. It has the third longest length worldwide extending around 4 300 km long from latitude of 17° South to Cape Horn at 56°. Its average width is close to 180 km from the Pacific Ocean on the west to the Andes on the east, going from 90 km for the narrowest part to 440 km for the widest. Chile has also one of the world's longest coastlines (6 435 km) and counts around 5 900 islands including 8 islands with more than 2 000 km^2, which is particularly challenging for connecting areas and people.

The Chilean territory is characterised by its great variety of landscapes and climates. There are four main geographical regions: the coastline, the coastal range of the Cordillera de la Costa, the intermediate plains and valleys, and the Cordillera de Los Andes. Overall, the altitude is high, with mountains and volcanoes throughout the country (the highest being Nevado Ojos del Salado with an altitude of 6 891 m). Only 20% of Chile's surface is flat.

Chile is also a land of meteorological contrasts with at least seven major subtypes, ranging from extreme aridity in the north (Atacama is the driest desert in the world) to lakes, fjords and glaciers in the southernmost area in Patagonia, a humid subtropical on Easter Island, a temperate coastal region with rainforest, lakes and lagoons in the southern zone, Mediterranean climate in central Chile, etc.

By combining these morphological and climatic features, Chile is usually divided into five different natural regions each with their own characteristics in terms of vegetation, fauna, climate and topography: the far north (Norte Grande which comprises the regions of Arica and Parinacota, Tarapacá and Antofagasta), the near north (North Chico, Atacama and Coquimbo) central Chile (Valparaíso, Metropolitan Region of Santiago, Libertador Bernardo O'Higgins, Maule and Bío Bío), and the far south (Zona Sur, including La Araucanía, Los Ríos and Los Lagos regions) and the Southern area (Zona Austral, Aysen and Magallanes and Chilean Antarctica).

Located in the region of the "Pacific Ring of Fire", Chile is constantly affected by both natural and man-made hazards, including earthquakes, tsunamis, volcanic eruptions, droughts, storms, floods, fires and explosions. Chile is one of the most seismic countries in the world with around 90 earthquakes since 1570, including one in February 2010 (8.8 Mw), which was followed by a tsunami affecting eight regions and the coastline from Valparaíso to the Los Lagos region (ONEMI, 2014).

The geography of Chile, together with the location of mining resources, explains the distribution of the population. In total, the Chilean population is about 17.8 million inhabitants, a figure close to the Netherlands, or Ecuador and Guatemala. In the north of the country, the population is concentrated along the coast and in the mining enclaves, while in the central and south areas, it is distributed in a slightly more dispersed way. Population is however very concentrated. According to the geographic concentration

index, demographic concentration in Chile (61) is almost twice the OECD average (32). Almost half of the Chilean population lives in Santiago and almost 70% when adding Bio Bío and Valparaíso.

Despite this process of demographic concentration, external/internal migrations and population integration, Chile is a culturally diverse nation. The Chilean population is descended not only from indigenous people and Spanish colonisation but also migrants from Europe (Spain, Germany, France, Italy, Great Britain, etc.) and other countries of South America, such as Peru, Colombia and Argentina. Today, the population identified as indigenous peoples - with a high proportion of Mapuche - numbers almost 9% of the country's total population, one of the highest shares in the OECD after Mexico and New Zealand (see Chapter 1).

The concentration in settlement patterns and economic activity is high in Chile, contributing to very high levels of regional inequality. In 2013, Chile recorded the second highest level of concentration in GDP among OECD countries, after Greece (OECD regional database, see Chapter 3), i.e. 55 vs. 39 on average in the OECD. This situation largely reflects the importance of mining-intensive activities, which concentrate high-value economic activities in few regions (OECD, 2014a).

Historically, Chile has a long tradition as a highly centralised country. Centralisation dates from the Spanish colonisation during the 16th century when Pedro de Valdivia founded Santiago and established the city as the country's military, religious and economic centre. A colonial administrative structure was established under the form of *provinces* and *cabildos* whose initially significant powers were gradually reduced as the royal administration grew stronger.

The situation did not change with the country's independence in 1818, when a unitary form of government was established based on centralised institutions and an authoritarian presidential regime. Often inspired by European and US experiences, there have been, however, several attempts to push forward decentralisation, even going so far as experimenting a federal system during the Republic, when a set of federal laws (*leyes federales*) were adopted in 1826 creating eight self-governing provinces. Faced with strong resistance, the experience was short lived and the implementation of federal laws was suspended the following year, replaced in 1833 by a new Constitution which opted for a unitary form of government. The following attempt at decentralisation was the first municipal autonomy law adopted in 1891, a very advanced law for the time as it granted considerable autonomy to municipalities. However, it led to several excesses, and the law was abolished just before the adoption of the 1925 constitution, which significantly reinforced the control of the central government over municipalities.

During the Pinochet regime (1973-1990), there was a paradoxical phenomenon, on the surface consisting of a decentralisation and regionalisation process but which, in reality, was the establishment of strict military-style central control on municipalities. The "decentralisation" policy, consisting in transferring central government tasks (education, health) and associated resources to municipalities, was in reality a "deconcentration policy" as local democracy was interrupted. Municipal officials were no longer elected. Municipalities, managed by military officials, were subordinated to the system of state administration. In the same vein, the regionalisation process consisted in creating thirteen administrative regions to host the state territorial administration, and not in creating self-governing regions. This policy also aimed at reducing the size of the state through the privatisation of public services, at national and local levels. Therefore, municipalities

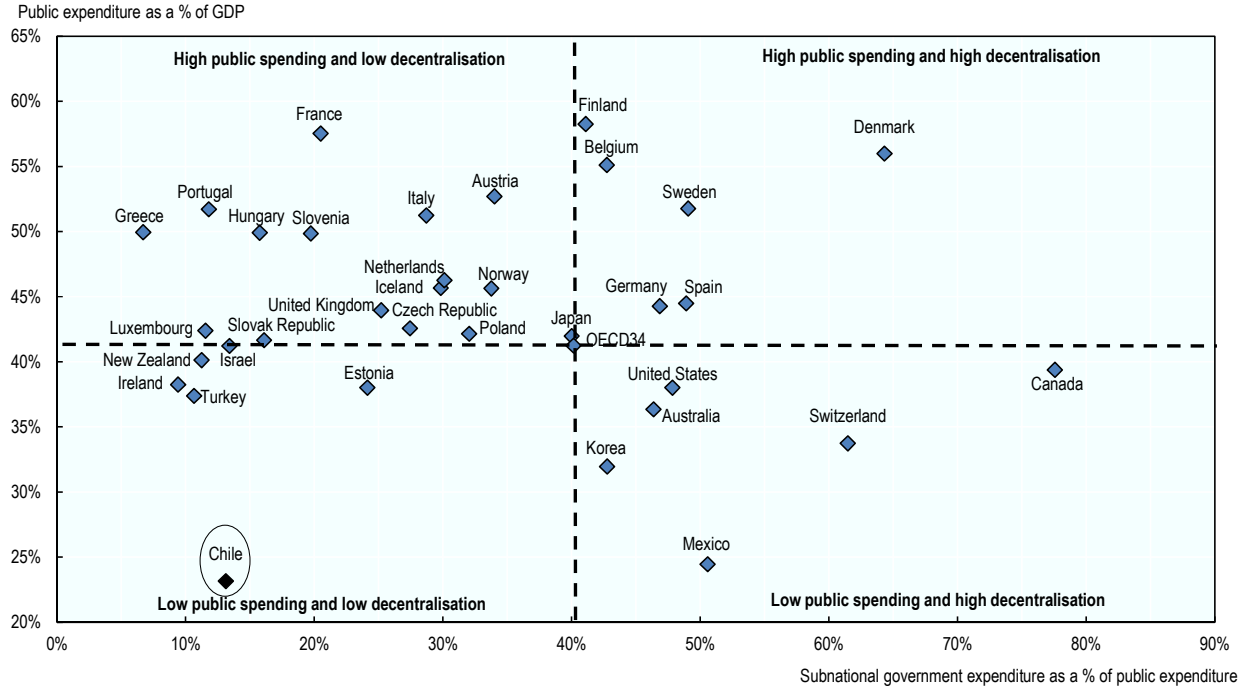
became more "service delivery agents" than "local government" (Stewart and Ranis, 1994).

With the restoration of democracy in 1990, some progress has been made towards decentralisation, seen as a means of re-democratising the country and reforming the state. To that end, the 1980 Constitution has been reformed several times since 1990 to incorporate democratic principles and push forward decentralisation and regionalisation. At the local level, a new organic constitutional law on municipalities, passed in 1991, paved the way for municipal elections, which took place in June 1992. At the regional level, the 1992 organic constitutional law created regional governments with their own legal status and assets.

However, progress has been very slow, with an incremental approach to reforms. Decentralisation initiatives have been often restricted to "administrative" decentralisation versus "political "decentralisation, and correlated "fiscal decentralisation". In fact, the centralist heritage remained strong and deeply rooted in the political-administrative culture and behaviour. There seems to be a "centralist model" driven by three motivations: political stability, protection of national unity and economic efficiency based on economic orientations that limit public intervention, favour market mechanisms and globalisation (OECD, 2009; Lorrain, 2014).

This model puts Chile in a unique situation compared to other OECD countries. It is reflected in the weakness of both public expenditure (as a % of GDP) and subnational government expenditure (as a percentage of public expenditure) (Figure 1.1).

Figure 1.1. **The singularity of Chile: A very limited and centralised public intervention (2014)**



Note: 2013 for Chile, Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. Data stated in local currency were converted in USD using purchasing power parity. OECD average is weighted.

Source: Created by the authors based on OECD data (2016a) and "Subnational Government Structure and Finance", OECD Regional Statistics (database), http://dx.doi.org/10.1787/05fb4b56-en.

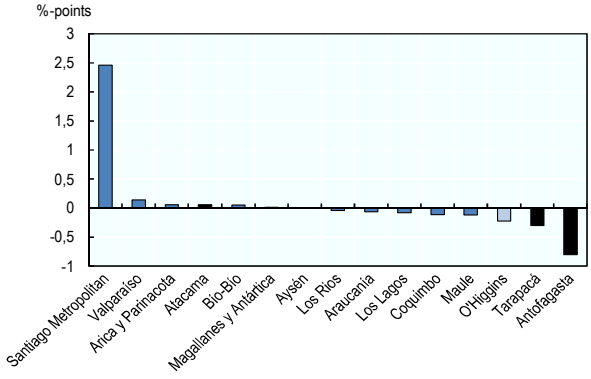
Chile ranks among OECD countries in which the share of subnational government expenditure in GDP and total public sector is the lowest, alongside Greece and Ireland; accounting for 3.0% of GDP and 13.1% of public expenditure in 2014 versus OECD averages of 16.6% and 40.2%, respectively (OECD, 2016a). The same applies for public investment where subnational governments play a minor role, representing 0.3% of GDP and 12.0% of public investment versus respectively 1.9% and 58.8% in the OECD. Subnational governments have limited own-source revenues and most transfers are earmarked by the central government to be spent on specific sectors or activities. Municipalities cannot generate debt for capital financing; Chile is the only OECD country where subnational borrowing is prohibited. Policy design and implementation are still largely defined from the centre by sectoral ministries and public agencies in a top-down process. Locally, the execution is mainly carried out by deconcentrated state territorial entities and partially by subnational governments. Execution of national public policies is done locally according to national, uniform norms established by the central government for the whole country, without taking into account local specificities and needs.

The Chilean development model has been successful but has also started to show its limitations

In several respects, this development model has been successful as it managed to ensure internal political and macroeconomic stability, national unity as well as economic efficiency and growth. Chile has gone through an extensive modernisation process, bringing with it greater economic prosperity, increased living standards and lower poverty.

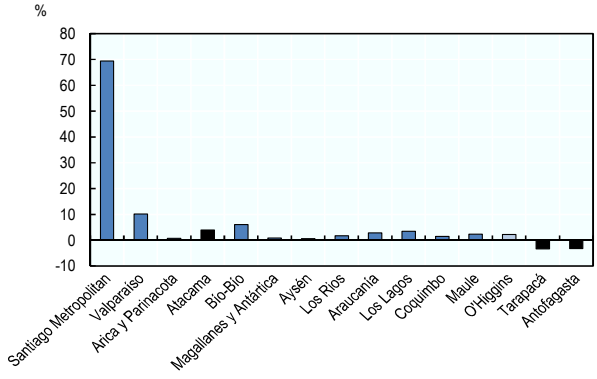
However, this model has started to show its limitations. This "hyper-centralisation" has gone hand in hand with a "hyper-concentration" of population, resources and powers in the metropolitan region of Santiago. Centralisation has reinforced inter-regional and municipal disparities across the national territory. While metropolitan region of Santiago covers 2.1% of Chile's land area, it represents 41% of population, 49% of GDP and 41% of employment. According to the Gini index, Chile displayed the greatest disparity in GDP per capita across TL3 regions in the OECD in 2013 (OECD 2016b). The country also recorded the second highest level of GDP concentration among OECD countries, after Greece (index of 55 vs. 39 in the OECD on average). While Chile still has high productivity gaps compared to other OECD countries and that productivity growth has trended at below zero for much of the past two decades, growth and productivity remained territorially concentrated. Between 2000 and 2013, 69% of the GDP growth and most labour productivity growth were generated in Santiago (Figures 1.2 and 1.3).

Figure 1.2. **Contribution to national labour productivity growth 2010-2013**



Note: Difference between national labour productivity growth as calculated with and without the indicated region.

Figure 1.3. **Percentage contribution to national GDP growth 2010-13**



Note: The contribution is the product of a region's GDP growth rate by its initial share of GDP.

Source: OECD (2016j), *OECD Regional Outlook 2016: Productive Regions for Inclusive Societies*.

Finally, the spatial inequalities are even more striking when the non-pecuniary dimensions of well-being are taken into account. Chile exhibits the highest levels of regional disparities among OECD countries when it comes to life satisfaction, environment, safety, and jobs as well as very wide disparities in education (OECD, 2016b, 2016k).

Such persistent inequalities partly reflect Chile's singular geography described above, including the very unequal distribution of mineral resources, which pre-conditions to some extent both settlement patterns and economic activity. However, even allowing for this challenging geography, it is difficult to avoid the conclusion that they also result from centralised, top-down and sectoral approaches which face difficulties in adapting to the different needs of Chilean regions (OECD, 2015a). In addition, centralisation has undermined the ability of local governments to efficiently fulfil some of their responsibilities, thereby resulting in a failure to take advantage of specific territorial opportunities and local assets.

The need to establish a multi-level governance system capable of place-based policies: towards stronger regions and municipalities

To mobilise the regional productivity catch-up potential, it seems that an efficient multi-level governance system is required, based an enhanced role for subnational governments (Box 1.1). Place-based components of productivity have been somewhat neglected so far, while most of the evidence suggests that they play an important role in determining the productivity potential of economies dominated by service sectors, which are mostly located in cities. In parallel, the development of tradable sectors, manufacturing and global value chains will probably be located in non-metropolitan areas close to cities. As a consequence, analysing the connectivity between those areas and the cities is necessary. Place-based policies and decentralisation should complement and enhance the impact of traditional structural reforms aimed at enhancing productivity

(International Conference on "Boosting Productivity and Inclusive Growth in Latin America", December 2016).

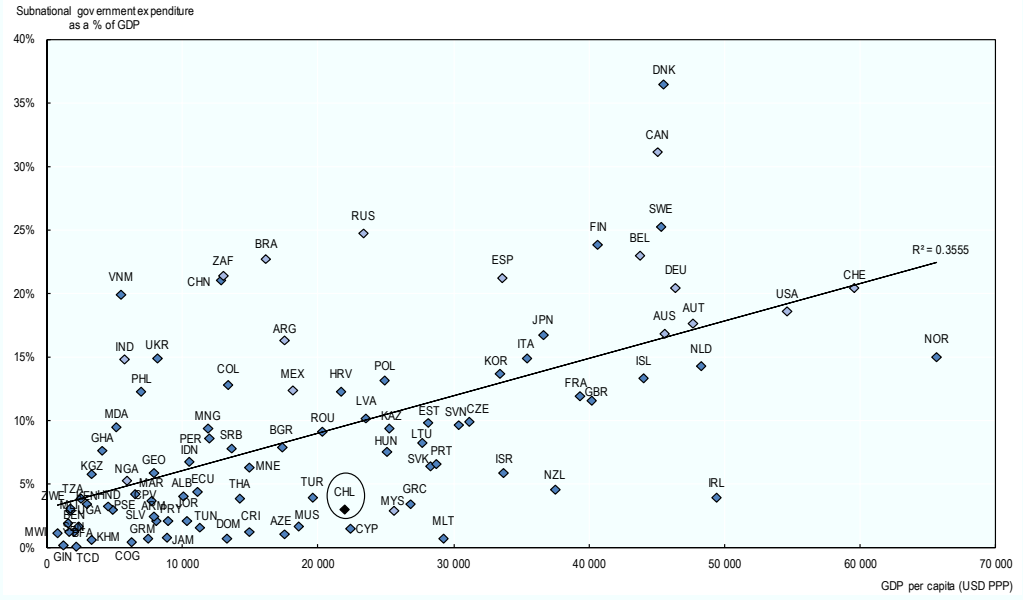
Box 1.1. **Decentralisation, wealth and growth**

Some evidence suggests that decentralisation and growth are positively correlated. While decentralisation of expenditure is not necessarily associated with increased growth, recent research shows that decentralisation of tax revenue is good for growth. A 10 percentage point increase in the sub-central tax revenue share is associated with an approximately 2% jump in GDP per capita in the long run. Tax decentralisation seems to encourage the development of the subnational economic and fiscal base. It also shows that balanced decentralisation is conducive to growth: when the various policy functions are decentralised to a similar extent, subnational governments are better able to co-ordinate policy and to reap economies of scale and scope across functions (OECD, 2016l).

Another study shows that the wealthiest countries tend to be more decentralised. If we compare the level of spending decentralisation, measured by the share in GDP or in public spending with the GDP per capita, there seems to be a positive correlation (Figure 1.4). It means that most decentralised countries seem to have the highest per capita GDP while the most centralised have the lowest (OECD/UCLG, 2016). Of course, this is not a general rule and there are several counter-examples. Some high-income countries are centralised while several low or middle income countries are decentralised. In addition, the cause-effect link between decentralisation and the level of development may not always be clear, in particular which way the causation works.

Many other socio-economic factors can play a significant role. Historical and institutional factors are also important, not least the federal/unitary structure of a country. Finally, decentralisation outcomes much depend on the way the process is designed and implemented, on the degree of maturity of institutions, on adequate subnational capacities and on the quality of multi-level governance, including efficient coordination mechanisms across levels of government.

Figure 1.4. Decentralisation and wealth: comparing the level of subnational expenditure in GDP with the level of GDP per capita



Note: Luxembourg is not represented on the graph as it is an extreme case due to its high GDP per capita.
Source: OECD/UCLG (2016), Subnational governments around the world: Structure and finance; OECD (2016l), Decentralisation and public finance: intermediate report (internal document).

In Chile, the growing recognition of the interdependencies between decentralisation, regional and local development, and national growth reinvigorated the debate on the urgent need to push for a decentralisation reform. It resulted in the acceleration of new proposals for in the late 2000's with the 2009 constitutional reform (Law No. 20.390), followed by intense legislative activity concerning both the municipal and regional levels, which allowed the process to advance step by step on the path towards decentralisation.

A decisive impetus came in 2014 when the president Michelle Bachelet put decentralisation to the core of her 2014-2018 programme. In the framework of the Presidential Decentralisation Agenda, the government established a Presidential Advisory Commission for Decentralisation and Regional Development (*Comisión Asesora Presidencial en Descentralización y Desarollo Regional*) in April 2014 to prepare a set of proposals. The Presidential Commission presented its report on October 2014. On this basis, the government started to engage in the preparation of bills to reinforce both regional and municipal decentralisation.

At local level, municipalities have always existed in Chile, albeit with varying degrees of democratic representativeness and autonomy. However, the 345 municipalities are more "public services providers" than genuine local governments. The Chilean government aims at providing municipalities with the tools, capacities, financial resources and legitimacy to improve their autonomy and performance while reducing municipal disparities in terms of capacity and finance. The objective is to strengthen their ability to effectively carry out their responsibilities and deliver local public services in a more efficient, transparent, accountable and equitable manner.

In that perspective, the OECD has been requested to accompany the Chilean government to reflect on and provide recommendations that can assist SUBDERE in designing and implementing the municipal decentralisation programme.

The objectives are to make a diagnostic of the situation of Chilean municipalities comprehensively addressing several dimensions: municipal powers and responsibilities, fiscal resources, institutional and human capacities, management of local public services, democratic oversight and citizens' participation at the local level and improvement of co-ordination and consultation mechanisms across and among levels of government. The following report comprises six chapters, corresponding to the main identified challenges.

The first chapter has three sections. The section 1 provides an overview of the organisation of the multi-level governance system. Section 2 presents the decentralisation process in a historical perspective. This historical side note is important to better understand how much centralisation is rooted in the Chilean society, making the path towards decentralisation long and difficult. It is fundamental to better understand the challenges that the decentralisation agenda is currently encountering. Section 3 analyses the role of municipalities in a changing institutional system. It seeks to underline the contrast between, on the one hand, the diversity and heterogeneity of the municipal landscape in Chile and, on the other, the uniformity of municipal organisation, responsibilities and financing as well as of national policies and norms applied at the local level. This situation suggests a progressive shift towards more asymmetric approaches. It also describes how municipalities co-operate today and considers the different ways to deliver municipal services, either directly or through indirect and private management models. Finally, the section ends by identifying the main challenges at stake

for the Chilean municipalities in the context of the regionalisation and decentralisation agenda.

How is governance organised in Chile?

The Constitution, approved in 1980 and fully effective since 1990, has been amended several times. It defines the Republic of Chile as a unitary, democratic and presidential state whose administration is functionally and territorially decentralised and deconcentrated (article 3 of the Constitution).

The Chilean institutional system

At the national level, the Chilean institutional system comprises three branches (executive, legislative, and judiciary) as well as the Constitutional Court.

The executive power is exercised by the government and the public administration, which are headed by the President of the Republic. The president remains in office for a term of four years and cannot be re-elected for the following period. The president appoints and removes freely the ministers of state, who are the direct and immediate collaborators in the government and administration of the state and who report directly to the president. There are currently 23 ministries (*ministerios*) and 32 under-secretaries.

Several ministers deal with subnational governments (see also Chapter 6). The Sub-secretariat for Regional and Administrative Development (SUBDERE) of the Ministry of Interior and Public Security has a special role. Its main missions are to design, implement and co-ordinate policies and programmes in the areas of regional and local development, decentralisation and citizen participation (www.subdere.gov.cl/programas). SUBDERE has three main operational divisions in charge of policy and studies, regional development and the municipalities. SUBDERE plays an important role in the administration of regionally defined investment. Broadly, SUBDERE is the national body responsible for promoting regional and local development, including the administration of funds such as the FNDR (*Fondo Nacional de Desarrollo Regional* - National Fund for Regional Development) and FCM (*Fondo Comun Municipal* - Municipal Common Fund) and strengthening the regional and local public administration capacity (OECD, 2009).

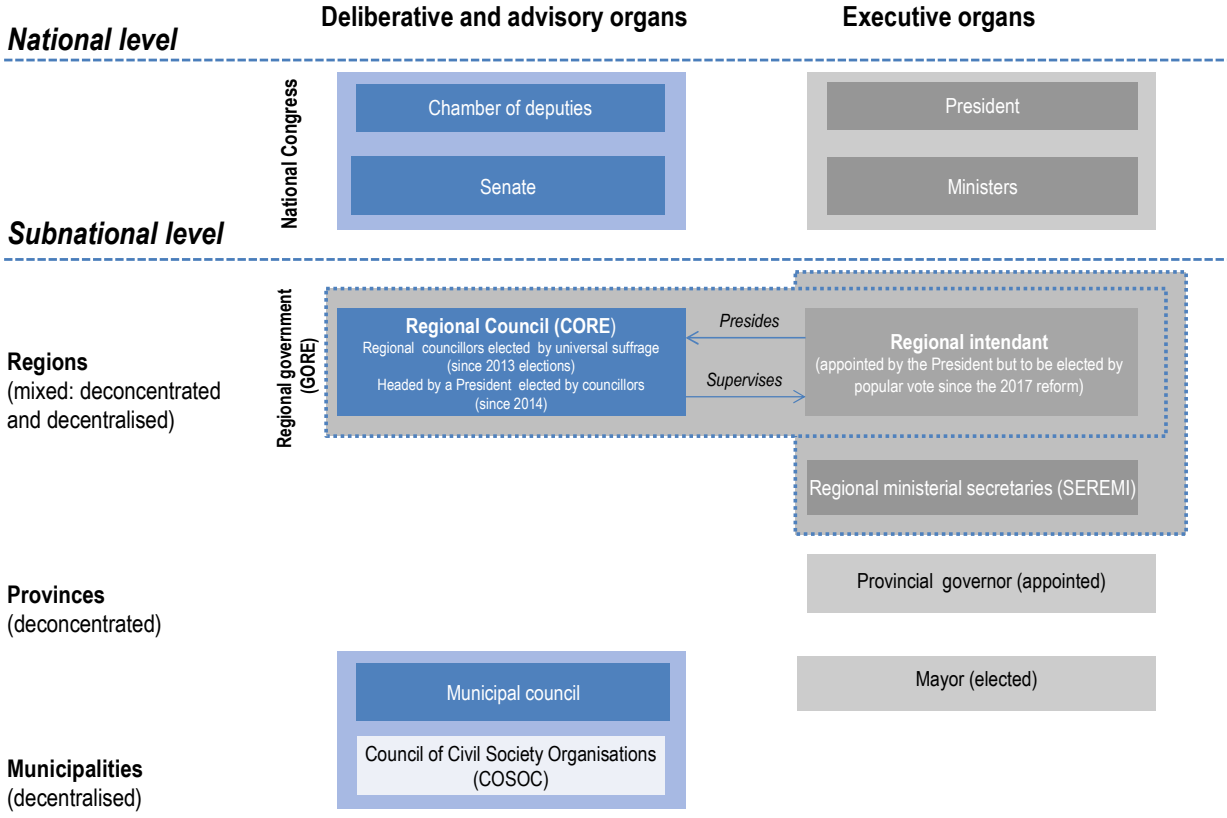
Other ministries also play an important role with regard to subnational governments. Almost all are deconcentrated at the regional level (see below). Among them are the Ministry of Education (municipal schools), the Ministry of Health (funds for municipal health centres), the Ministry of Social Development (solidarity and social funds, social programmes, indigenous communities), the Ministry of Housing and Urbanism (economic and social infrastructure with a national purview for urban and metropolitan policy, housing as well as overseeing the development of municipal land-use plans), the Ministry of Public Works (public infrastructure assets and services in the sectors of water, roads, port works, airports, public buildings, and projects developed through public private partnerships), the Ministry of Transport and Telecommunications (transport policies, public transport and urban connectivity), Ministry of Agriculture (rural development), Ministry of Environment (environmental impact evaluation), the Ministry of Labour and Social Welfare (municipal employment offices), and the Ministry of Finance (Budget Department/DIPRES, debt office, public procurement, tax office, etc.).

National public agencies responsible for delivering key public services have also developed links with subnational government, such as the Chilean Economic Development Agency (Corporación de Fomento de la Producción - CORFO), the Chilean Agency for the Promotion of Small and Medium-Sized Enterprises (SMEs) (SERCOTEC), the National

Training and Employment Office (SENCE) or regional offices of ministries such as: the Housing and Urban Development Agency (SERVIU) that deals with the construction and maintenance of urban roads; the National Institute for Agricultural Development (INDAP) which has developed a territorial network of 122 offices around Chile; the Solidarity and Social Investment Fund (*Fondo de Solidaridad e Inversión Social* - FOSIS) of the Ministry of Social Development which has developed a network of regional and provincial offices whose work focuses on attaining greater social protection and economic inclusion of the most vulnerable people in Chile.

Territorial policies appear to be fragmented across the different ministries, lacking an integrated and co-ordinated approach (see Chapter 6).

Figure 1.5. **Organisational chart of the Chilean multi-level governance system**



Legislative power resides in the President of the Republic – as co-legislator – and in the National Congress (*Congreso Nacional*) which is bicameral, consisting of a Senate (*Senado*) and a Chamber of Deputies (*Cámara de Diputados*) whose members are directly elected by universal popular vote. The Senate is formed by 38 Senators elected in 19 senatorial circumscriptions for eight-year terms, with half of them being replaced every fourth year. The Chamber of Deputies is formed by 120 members called honourable deputies (*Honorable Diputado* - HD) elected from 60 two-member electoral districts. They remain in office for a four-year term and can also be re-elected in their respective districts on the same quadrennial cycle. In April 2015, Law No. 20.840 was adopted replacing the binomial system with a more proportional electoral formula. The new electoral system will be effective with the 2017 general elections. The number of electoral districts and senatorial constituencies will be reduced to respectively 28 and 15 (corresponding to the 15 regions). Each electoral

district will elect between three and eight deputies, while each region will elect between two and five senators. Overall, the Chamber of Deputies will comprise 155 HD, and the Senate 50 senators.

The judiciary branch is made up of independent and autonomous courts that exercise the judicial function. It comprises the Supreme Court, 16 courts of appeals in each region and other tribunals and lower and specialised courts.

The Constitutional Court is not part of the judiciary, since it was set up as a body independent of any other branch of power. Composed of ten members, it is the court of last resort on constitutional matters preventing the adoption of unconstitutional laws or decrees.

Another constitutionally autonomous entity in Chile is the Comptroller General's Office (*Contraloría General de la República*), which exerts control over the legality of public administrative acts and monitors public accounts. There are also *Regional Contralorías* in each region, which are responsible for auditing local governments.

The Central Bank of Chile is an autonomous entity of technical nature having a constitutional rank. Its missions are to safeguard the stability of the currency and the normal functioning of internal and external payment systems. In this framework, the Central Bank promotes the stability and efficiency of the financial system in order to create a predictable and stable environment for economic agents.

An independent Election Examining Tribunal (*Tribunal Calificador de Elecciones*) and sixteen regional electoral courts are responsible for ensuring the electoral process is free and fair.

The subnational level

The subnational organisation is defined in Chapter XIV of the 1980 Constitution entitled "Government and Interior State Administration". Article 110 provides that for the purposes of the government and internal administration of the state, the territory of the Republic shall be divided into regions and provinces, while for the purposes of local administration the provinces shall be divided into *comunas* (managed by municipalities). As a result, Chile's administrative system at subnational level is particularly complex, comprising three main categories of entities:

- One which is both deconcentrated and decentralised (regions/*regiones*) at the upper level (Box 1.2).
- One which is deconcentrated (provinces/*provincias*) at the intermediate level.
- One which is decentralised at the lower level (municipalities/*municipalidades*).

Box 1.2. **Deconcentration and decentralisation**

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

Deconcentration refers to the delegation of central government tasks to non-elected central government units based in regions. Deconcentrated state services represent the central government at the territorial level, are responsible for implementing national policies at the regional and local levels, ensuring that they are in line with subnational government policies. Deconcentrated state services may also provide national public services at the territorial level.

This territorial organisation can be put in perspective with other OECD countries. If we lump the current Chilean "mixed regions" into "subnational governments" (i.e. self-governing regions), Chile belongs to the group of OECD countries with two layers of subnational governments, together with 18 other OECD countries. In the OECD, nine countries have only one level (municipal) and eight countries have three levels (regional, intermediary and municipal). Chile counts overall 360 subnational governments (15 regions and 345 municipalities). In total, the OECD comprised around 138 000 subnational governments including around 133 000 municipalities, 4 108 intermediate governments and 518 regions or state governments in 2015-2016 (Table 1).

Table 1.1. **Type and numbers of subnational governments in the OECD: Country by country, 2014-2015**

2015-16	Municipal level	Intermediary level	Regional or federated state level
Federations & quasi-federations			
Australia	571 (local government areas)		8 (6 states + 2 territories)
Austria	2 100 (municipalities)		9 (Bundesländer)
Belgium	589 (municipalities)	10 (provinces)	6 (3 regions + 3 communities)
Canada	3 805 (census subdivisions)		13 (provinces and territories)
Germany	11 092 (municipalities)	402 (295 rural districts and 107 district-free cities)	16 (länder)
Mexico	2 457 (municipalities)		32 (31 states + federal district)
Spain	8 119 (municipalities)	50 (provinces)	17 (autonomous communities)
Switzerland	2 294 (municipalities)		26 (cantons)
United States	35 879 (municipalities, towns and townships)	3 031 (counties)	50 (states)
Unitary countries			
Chile	345 (municipalities)		15 (regions)*
Czech Republic	6 258 (municipalities)		14 (regions)
Denmark	98 (municipalities)		5 (regions)
Estonia	213 (municipalities)		
Finland	313 (municipalities)		1 (autonomous region of Aland)
France	35 885 (municipalities)	101 (départements)	18 (regions)
Greece	325 (municipalities)		13 (regions)
Hungary	3 178 (municipalities)		19 (counties)
Iceland	74 (municipalities)		
Ireland	31 (county and city councils)		
Israel	255 (local governments)		
Italy	8 047 (municipalities)	107 (provinces and metropolitan cities)	20 (regions)
Japan	1 741 (municipalities)		47 (prefectures)
Korea	228 (cities, counties and autonomous districts)		17 (regional-level entities)
Latvia	119 (municipalities)		
Luxembourg	105 (municipalities)		

Table 1.1. **Type and numbers of subnational governments in the OECD: Country by country, 2014-2015** *(continued)*

2015-16	Municipal level	Intermediary level	Regional or federated state level
Unitary countries *(continued)*			
Netherlands	390 (municipalities)		12 (provinces)
New Zealand	67 (territorial authorities)		11 (regional councils)
Norway	428 (municipalities)		18 (counties)
Poland	2 478 (municipalities)	380 (314 counties and 66 cities having the status of county)	16 (regions)
Portugal	308 (municipalities)		2 (Azores and Madeira)
Slovak Republic	2 927 (municipalities)		8 (higher territorial units)
Slovenia	212 (municipalities)		
Sweden	290 (municipalities)		21 (county councils)
Turkey	1 397 (municipalities)		81 (provinces and metropolitan municipalities)
United Kingdom	389 (local councils)	27 (county counties, only in England)	3 (Northern Ireland, Scotland and Wales)
OECD35	133 007	4 108	518
EU28	87 754	1 077	261

Source: Adapted from OECD (2016a), *Subnational governments in OECD countries: Key data (2016 edition);* http://www.oecd.org/cfe/regional-policy/Subnational-governments-in-OECD-Countries-Key-Data-2016.pdf, OECD (2017a), *Multi-level Governance Reforms: Overview of OECD Country Experiences*.

The regional level

In Chile, twelve administrative regions were created in 1974 during the regionalisation process of the mid-1970s that grouped the former 25 provinces. The metropolitan region of Santiago was created in 1976 and two more regions were set up in 2007 following the subdivision of existing regions, resulting in the current number of 15 regions.

Since the 1990s, regions have gradually been transformed into self-governing entities. At present however, regional governments are still both deconcentrated and decentralised entities. The process of transformation started in 1992 when an organic constitutional regional law established a mixed regional government system (called "GORE"). Initial GOREs were formed by a regional executive (the intendant - *intendente*) appointed by the President of the Republic and a regional council (*consejo regional* - CORE) elected indirectly by the municipal councillors. In 2009, a new constitutional reform (Law No. 20.390) provided for the direct election of the CORE by popular vote for a four-year term, which was effective when the newly-elected regional councillors took office in March 2014 (Law No. 20.678). Finally, a new regional reform was enacted in 2017 to allow direct election of the regional governors, which will be effective in the coming years, creating fully self-governing regions. Elected regional governors will coexist with regional and provincial "presidential delegates" who will represent the central government in the different regions and provinces (Law No. 20.990).

The existence of a "mixed" regional level, both deconcentrated and decentralised, is not common in the OECD. In most OECD countries with a state territorial administration, decentralised and deconcentrated administrations are separated. The current decentralisation reform will clarify the subnational system, regions becoming fully self-governing entities.

The intendant represents the central government in the region and is the executive head in the region. The intendant oversees development initiatives and the co-ordination of sectoral policies. Currently, the average length of service for an intendant is slightly over one year. This is disruptive to stability and continuity, and is an obstacle to effective oversight as well as to the credibility of the office (OECD, 2013a).

Since the Law No. 20.757 of 2014, CORE has been headed by a chair elected by the regional councillors (previously it was headed by the intendant). With the new Law No. 20.990 of 2017, the CORE will be chaired by the regional governor. The number of regional councillors varies from one region to another depending on the number of inhabitants, ranging from 14 councillors to 34 for the most densely-populated region. Their main responsibilities, defined in 1994, have been increased by the 2009 constitutional reform No. 20.390 (Box 1.3).

Box 1.3. **CORE responsibilities**

Article 113 of the Constitution defines the CORE's functions as follows (prior to Law No. 20.990 of 2017): the regional council shall be an organ of a normative, arbitration and supervisory nature, within the own sphere of competence of the regional government, responsible for enabling effective regional citizen participation and for exercising the powers that the constitutional organic law entrusts it with.

The main CORE responsibilities, defined by the organic constitutional regional Law No. 19.175 adopted in late 1992, have been increased by the constitutional reform no. 20.390 adopted in 2009. They include the following:

- To approve the regional budget.
- To design programmes and policies for regional development.
- To approve a regional development plan.
- To take decisions regarding regionally-defined public investments in particular through the distribution of the major source of regional investment - the National Regional Development Fund (*Fondo Nacional para el Desarrollo Regiona*l/FNDR).
- To administer the paving of rural sidewalks and roads.
- To carry out tasks related to land management, human settlements and infrastructure equipment.

CORE is also in charge of approving municipal regulation plans, regional urban development plans and Programming Contracts (*Convenios de Programación*/CP).

Regional administration is today composed of three administrative units, called "divisions", that implement the various dimensions of the regional government work: Administration and Finance (*Administración y Finanzas*); Planning (*Planificación*); and Analysis and Oversight (*Análisis y Control de Gestión*) (OECD, 2013a). This organisation is changing as a result of the current regional reform. Three new regional divisions will be established within the GORE, in addition to existing ones, and new management functions will be created, such as regional manager or chief of control (see below).

Co-ordination of sectoral policies and programmes in each region is the responsibility of national ministries' representatives in the region (SEREMI). They report to line

ministers but they must also serve and co-ordinate with the current intendant (but with the regional governor in the future). Therefore, regional delegations make up the so-called "regional cabinet" of technical advisors to work with the intendant. Almost all ministries are deconcentrated except the Ministry of the Interior, National Defence, Foreign Affairs and General Secretary of the Presidency). Also present are regional representatives of the national public agencies that deliver key public services (OECD, 2009; 2011). SEREMI and regional agencies are in direct contact with the municipalities in their area of work.

The provincial level

Regions are divided into 54 provinces, which are deconcentrated administrative entities. A new province, Marga Marga, was created in 2010 in the central Chilean region of Valparaíso.

Each province is headed by a governor (*gobernador*) appointed by the President of the Republic. Provincial governors and the provincial administration support the region's intendant to oversee internal management in the province. Their role is now narrow and they have limited financial and human resources. They appear to depend on the region and the particular intendant in office (OECD, 2013a). With the Law No. 20.990 of January 2017, provinces will be headed by a provincial presidential delegate.

The municipal level

Municipalities manage the "communes"[1] (*comunas*) which form the basic unit of the political and administrative structure in Chile. They are recognised as self-governing entities in the 1833 Constitution, which provided for the election of local municipal councils through direct popular vote, a principle that has been maintained in the 1925 Constitution. During the Pinochet regime (1973-1990), the election of mayors and councillors by universal suffrage was abolished. However, during the same period, there has been a somewhat paradoxical process as some important state functions were decentralised to municipalities that received increased resources and some autonomy to perform these new tasks. But in reality, it was a deconcentration process of state functions and not a decentralisation one, as municipalities were no longer democratic or autonomous institutions. After the Pinochet dictatorship, restoration of local democracy was a matter of high priority. However, considerable debate took place on the nature of decentralisation. A consensus on a constitutional reform law was finally reached in November 1991, which modified Chapter 13 of the 1980 Constitution, dealing with local administration. It was followed by the adoption of a new Organic Constitutional Law on Municipalities in 1992, which paved the way for municipal elections in June 1992 and restored their autonomy.

Municipalities are now defined by the 1980 Constitution as a public law corporation, endowed with autonomy, legal personality and its own patrimony, whose purpose is to promote the economic, social and cultural development of the territory, with the participation of the local community. Municipalities are regulated by the Constitutional Organic Law No. 18.695 on Municipalities (LOCMUN) of 1988, amended several times. The mayor, as the head of the municipality and the Municipal Council, is the most important public figure of a municipality. In addition, the municipality has a consultative body, the Economic and Social Council, which aims at allowing the participation of the community. As autonomous entities, they do not have in theory a hierarchical relationship with the central or regional governments.

The decentralisation process: Historical overview, recent changes and prospects

A historical overview

Chilean municipalities and regions – when they were provinces – have a long history. This history merits some attention as it facilitates a better understanding of the long and difficult path towards decentralisation. The centralised nature of Chile is strongly rooted in the history, culture and behaviour of the country. Progressively, municipalities and regions have strengthened their organisation and capacities. But there is much to be done, and that is precisely what the new decentralisation agenda of the Chilean government intends to do. In that perspective, the two main pillars – regional and municipal – should be well connected and conducted jointly to avoid building an unbalanced multi-level governance system.

The colonial period: The birth of the municipal system

Chiles's centralist heritage dates from the Spanish colonisation during the 16th century when Pedro de Valdivia founded Santiago in 1541. The city was established as the country's military, religious and economic centre. At local level, a colonial administrative structure was established under the form of *cabildos* (Box 1.4). The territory was also divided into provinces managed by *corregidores*, which totalled 18 at the beginning of the 18th century.

Box 1.4. ***Cabildos*, the origins of Chilean municipalities**

Chilean municipalities emerged at the same time the colony was founded. *Cabildos* or "municipal councils" were initially created and formed of soldiers who participated in the process of conquest. They formed the basic local government authority in Spain's Latin American colonies. They assumed broad powers, including judicial, legislative and administrative duties at the local level (*Consejo, Justicia y Regimiento*), reporting to the president of the audiencia, who in turn reported to the viceroy.

According to the Spanish conception of a municipality, *Cabildos'* geographic area included both the city and the surrounding rural areas. Municipal councils comprised a board of councillors (*regidores*) and one or two magistrates (*alcaldes*) elected every year by the councillors. Initially, *regidores* were elected by qualified citizens but a system of royal appointment was implemented progressively for part or all councillors in several cities. *Alcaldes* served as judges of first instance in all criminal and civil cases and acted as president of the *Cabildo*, unless there was a *Corregidor*. In fact, the King of Spain also introduced *corregidores* to represent him directly and preside over the *cabildos*. These *corregidores* were replaced by intendants (*intendentes*) in 1786 with the Bourbon reforms.

Other important municipal functions were the *alférez real* (royal standard-bearer) the chief of police and law enforcement (*alguacil*), the "*mayordomo*" (public accountant), the *procurator* (city attorney), the *fiel ejecutor* (inspector of weights, measures and markets) and the *escribano público* in charge of secretarial duties (*Actas*) during municipal sessions. There were two types of municipal council meetings: ordinary (restricted to councils members) and open to qualified citizens (*abierto*). These latter disappeared progressively. *Calbidos* performed functions such as the construction, maintenance and improvement of public facilities, health and sanitation (hospitals), primary education, control of the union of artisans union, the administration of justice (until 1609), the regulation of prices and wages, the collection of royal taxes, the enforcement of law and the local militia.

Box 1.4. ***Cabildos*, the origins of Chilean municipalities** *(continued)*

Progressively, these municipal bodies lost some power as the result of the establishment of the royal administration. In the 17th century, the councils continued to lose much of their prerogatives with the creation of the Real Audiencia de Santiago in 1609 (Royal Court of Santiago) and the decision by the King of Spain to sell public offices for perpetuity, including for those of *regidores*. These *regidor perpetuo* were in return obliged to reside in the city. Some cabildos remained however powerful such as Santiago, Concepción and La Serena.

Source: Salvatore Bizzarro (2005), Historical Dictionary of Chile, Letelier, Memoria Chilena, Biblioteca Nacional de Chile (DIBAM); Núñez Muñoz (2006), *Realidad y desafíos del municipio chileno*.

Municipalities and provinces during the 19th century: Recognised but under strict control

After a federalist attempt in 1826, the 1833 Constitution recognised elected municipalities which were, however, under strict central control. From 1812 to 1818, in the period when the new Republic was created until just before the Declaration of Independence, various rules were established to recognise the municipality as a fundamental institution of the future legal and administrative governance system, to be based on elections. The Constitution of 1818 stated that that the cabildos "should promote the advancement of the population, industry, education of youth, hospices, hospitals and whatever is interesting to the public benefit", including urban police (Núñez Muñoz, 2006).

It is the 1833 Constitution which finally provided for the election of municipal councils for a three-year term by direct popular vote. This principle was however established by a law adopted only in 1887. In fact, the 1833 Constitution established the rules for the first administrative division of the country, into 26 provinces managed by intendants appointed by the President to execute the orders of the central government as the "natural and direct agents" of the President. It was also called the Portalian era (*Portaliana era*). The reality was that municipalities had little power and were under the direct control of the central government. Specific functions and only minor administrative tasks were assigned to them while they were subject to the intendant's authority (Walter, 2005).

This period was also marked by significant tensions between the "regions" and the "centre", as by the rebellion of 1851 and Civil War of 1859, which reflected, among other claims, the fight against the central power (Couso et al., 2011). In fact, regionalism movements emerged starting in the 1820s where there have even been some attempts to create a federal system. In particular, the *Leyes Federales* of 1826, sometimes referred as the 1826 Constitution aimed at creating, under the direction of José Miguel Infante inspired by the US experience and founder of the newspaper *Federal Valdiviano*, a federal system, dividing Chile in eight provinces enjoying large powers. Each province had a Provincial Assembly and an intendant elected by popular vote, as well as elected parish councils. Finally, running against a long tradition of centralisation and the will from most of the aristocracy to protect and consolidate the unity of Chile, the implementation of the laws faced strong resistance. It was suspended in 1827. Later, the consultation of the provinces, organised by the President Francisco Antonio Pinto (asking them which form of the government they would prefer) finally resulted in the choice of a unitary state.[2] The federalism process was definitively abandoned when the Constitution initiated by Diego Portales was adopted in 1833 opting for a unitary form of government

and an authoritarian presidential regime (see above). However, the territorial division into administrative provinces survived this federal attempt.

The first municipal autonomy law was adopted in 1891 but led to excesses

The year 1891, marked by the civil war, represented an important step at the local level. One of the consequences of the revolt against the president Balmaceda was the establishment of municipal autonomy through a law promoted by Manuel José Irarrázaval who was inspired by the European models, particularly the Swiss (Walter, 2005) and which was very advanced for the time. The law on the organisation and responsibilities of municipalities commonly known as the "municipal autonomy law" (*Ley de Comuna Autónoma*) was published on 24 December 1891 during the presidency of Jorg Montt. It granted considerable autonomy to the municipalities, giving them the control of the election process (registration of voters, organisation, oversight, etc.) and independence towards the government, in particular the intendant. The law also established the number of municipalities (267) and enlarged their functions, which included, among others, education, economic development, health and sanitation, public order and public works. It also defined the number of *alcaldes* and *regidores* according to the size of the municipality.

The law however provided some "checks and balances" to limit the power of the municipal council (Walter, 2005), in particular through the setting up of an "assembly of electors" (*Asambleas of Electores)* representing all eligible voters within the municipality, in parallel to the municipal councillors. Therefore, *regidores* had to share their powers with these electoral assemblies responsible for electing the municipal officials but also for approving the municipal budget and investment, establishing taxes and approving loans.

This control of the electoral assemblies on municipal councillors was not efficient, however, because of a lack of political culture and funds allowing the assemblies to perform their oversight role and limit the power of local *caciques*. Far from guaranteeing free and democratic elections and democratic oversight, the system led to drifts and electoral manipulation, including an increase in corruption. Therefore, the electoral law was modified in 1914 and 1915 in order to remedy the shortcomings of the previous system, abolishing the municipal responsibility in managing local elections. The assembly of electors was thus replaced by taxpayers.

Reinforced control on municipalities but first recognition of the regions

The 1925 Constitution was preceded by a *coup d'état* which resulted in the establishment of a Military Junta which abolished the Municipal Autonomy Law and reinstated appointed intendants. In the same vein, the new constitution, in force until 1973, reinforced the control of the government on municipalities, establishing that municipalities would be subject to the surveillance of the provincial assemblies (initially, these assemblies were to be elected but the enabling legislation was never adopted and they remained a central government agent).

The 1925 Constitution devoted an article to the topic of decentralisation of the state. It maintained the principle of elected municipalities, however reserving the right of the President to appoint mayors of large cities (Letelier S. L. 2006).[3] Finally, the Constitution recognised that "the laws will gradually entrust the provincial or municipal bodies with administrative powers currently exercised by other authorities in order to proceed with the decentralisation of the internal administrative regime". The fundamental law then ushered in a decentralisation process conceived "from above" as institutional arrangements. In short, it consisted in an administrative decentralisation based on

territorial consolidation with the clear objective of promoting and strengthening the country's economic growth through regional development (Boisier, 2000).

The first efforts towards regionalisation in the 1950s

The debate on decentralisation seems to have progressively faded with regionalisation taking its place. This time around, regionalisation was less violent than similar movements from the previous century, even if there were conflicting periods in the 1930s. In fact, centralisation has resulted in a gradual concentration of much of the political and economic powers to the detriment of the regions, especially in some areas where the coal and nitrates mining industries are developing such as Bío Bío and the far north.

Subsequently, in the 1950s, CORFO (the Chilean Economic Development Agency created in 1939) and the National planning office (ODEPLAN) started to promote decentralisation and regionalisation as a way to promote economic growth based on the theory of centre-periphery interrelations (Boisier, 2001). This approach did not have a political dimension, which would have consisted in converting these regional spaces into institutional actors, elected through democratic processes and able to design and conduct regional policies. It was fundamentally an economic approach aimed at promoting regional economic growth based on regional growth nodes and industrialisation as a substitute to imports (Box 1.5). During this period, national politicians consistently vetoed the creation of regional governments: between 1938 and 1966, there were seven unsuccessful proposals to introduce a regional level of government between the provincial and national levels.

Box 1.5. **The first regionalisation process (*primera regionalización*)**

In 1950, the Chilean Economic Development Agency (CORFO - Corporación de Fomento de la Producción) proposed a new political-administrative division consisting of six major regions: Norte Grande, Norte Chico, Núcleo Central, Concepción and La Frontera, Los Lagos Region and Los Canales Region. This division of the territory was based mainly on geographic and economic considerations. The objective of this regionalisation was to boost the regional economic development based on geographical, human and economic characteristics of each region (Boisier, 2001).

For its part, the National Planning Office (ODEPLAN - Oficina de Planeamiento Nacional) made progress in regionalisation in 1965 by establishing new regions based on a system of economic development centres. The territory was divided into eleven regions and one metropolitan area. This system was characterised by the creation of spatial units determined by a city or pole of economic development that expanded to the rest of the region. The city of Santiago and the metropolitan area were established as the main centre of national development and the three areas of multiregional development were Antofagasta, Valparaíso, and Concepción. There was a third level of hierarchy comprising another series of regional development areas (Boisier, 2001).

Under the Frei and Allende governments, there was no decentralisation reform per se but both governments promoted the democratisation of society and popular participation through local groups and neighbourhood associations to advance their social programmes (Stewart and Ranis, 1994).

Eduardo Frei Montalva, a member of the conservative party, won the presidential election in 1964, engaging the country in important economic and social reforms as well

as creating the neighbourhood associations (*Juntas de Vecinos*). In 1970, he was succeeded by Salvador Allende who undertook, based on his programme "The Chilean Path to Socialism" *(La vía chilena al socialismo*), the nationalisation of industries and mining while implementing welfare state reforms (education, health, land, neighbourhood food distribution programme).

The Pinochet regime (1973-1990)

With the advent of the military dictatorship led by Pinochet, which deposed Allende, there was what could be considered a paradoxical phenomenon. An authoritarian and neo-liberal model was established together with a process of "decentralisation" (deconcentration) and regionalisation.

With the *coup d'état* of 1973, local democratic life was interrupted, and Pinochet ruled Chile under a highly repressive military regime. Shortly after taking control, Pinochet replaced democratically-elected mayors with military officials and dismissed municipal councillors (Valenzuela A., 1977; Eaton, 2004), which was confirmed by the legislative decrees of 1975 and 1976. Appointment and removal of mayors were now a presidential power. Mayors were the direct agents of the central power and municipalities were subordinated to the general system of state administration. Municipal councillors were substituted with a new consultative body staffed with regime supporters (Eaton, 2004). This new local system was confirmed by the new constitution adopted in 1980 through its chapter XIII dedicated to regional and local administration.

At the same time, the regime gave a strong impetus to the process of "decentralisation" – in fact deconcentration – and regionalisation as a way to modernise the country, in parallel to monetarist, pro-market and open-economy policies favoured by the "Chicago boys" that led to the privatisation of many public assets and services (Stewart and Ranis, 1994). The 1980 Constitution – that survives to this day, though heavily reworked – and the different laws adopted during this period clearly confirmed that this process was not a genuine decentralisation policy but a policy of deconcentration of state functions at regional and local levels.

The creation of administrative regions

As far as regionalisation is concerned, a decree was promulgated in December 1973, creating the National Commission for Administrative Reform (CONARA) with the mandate to make proposals on the transfer and distribution of administrative responsibilities to subnational entities and to establish a new territorial division of the country. The new territorial and administrative system was implemented by the two Decree Laws 573 and 575 of 1974. Due to the peculiar geographical conditions, the basic principles of this new territorial organisation were to ensure cohesion, unity and equity, national security, socio-economic development and an effective national administration across the entire territory. Thus, the actual goal of this policy was to strengthen national integration, economically, socially and politically (Boisier, 2001).

Thirteen administrative regions were created in 1974, including the metropolitan region of Santiago (established in 1976). Their borders were defined according to several criteria such as the existence of natural resources and economic assets, rural-urban structure and the previous 25 provinces. Criteria were defined by ODEPLAN and the work of Walter Stöhr (Boisier, 2005). These new regions were only administrative entities as it was considered too early to provide them with democratic foundations. A regional administration was put in place, representing the central government at the

regional level, with regional intendants (*intendentes*) appointed by the President of the Republic and a regional planning office attached to ODEPLAN. Provinces remained as sub-regional administrations but with reduced prerogatives and responsibilities. Investment resources were also transferred from the government to the new regional administrations through the Regional Development Fund (*Fondo Nacional de Desarrollo Regional* - FNDR), created in 1974 to finance regional development and infrastructure projects. In 1987, Regional Councils for Development (*Consejos Regionales de Desarrollo* - COREDES) were established comprised of regional councillors (*consejeros*) whose selection was controlled by the central power. In fact, chaired by the regional intendant, COREDES comprised the provincial governors, a representative of the Army, and members appointed by public and private organisations of the region (Núñez Muñoz, 2006).

Decentralisation/deconcentration reforms at the municipal level

At the local level, important governance reforms were taken over the course of the late 1970s and 1980s. The Organisation and Powers of the Municipalities Act of 1981 (*Ley de Organización y atribuciones de las municipalidades*) implemented several provisions of the 1980 Constitution, introducing some major changes. The law transferred several central government tasks and critical expenditure responsibilities to the municipalities, in particular primary healthcare and primary and secondary education (Marcel, 1994; Yáñez and Letelier; 1995). Until then, municipal responsibilities were restricted to street cleaning and garbage collection. It also provided the municipal administration with greater resources to perform these new tasks through the decree-Law No. 3.063 on municipal revenues (*decreto-ley No 3.063 sobre las rentas municipales*), including education and health funds as well as the Municipal Common Fund, already created in 1979. The regime also used neighbourhood councils to directly channel social funds and use *juntas de vecinos* as a critical link between civil society and the regime (Eaton, 2004). However, although the 1981 Act was described as "law for autonomous municipalities" it reduced their level of freedom. Municipalities became subordinated structures of the state and are highly dependent on executive power.

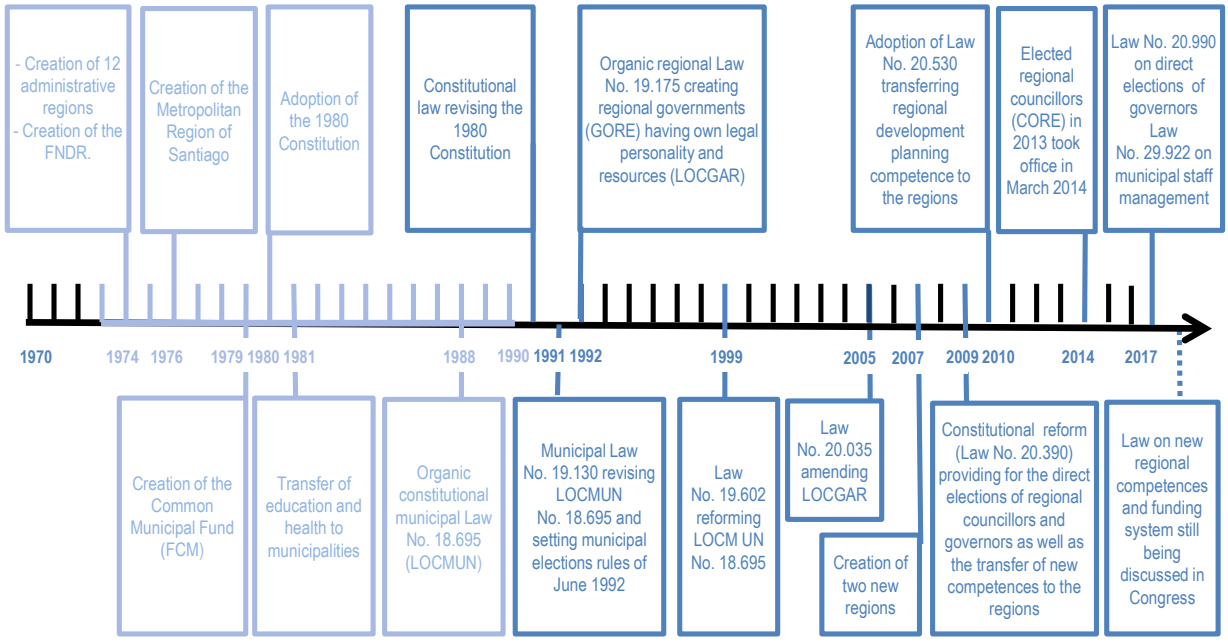
In 1988, the coercive system regulating the municipalities was loosened. The 1988 Organic Law of Municipalities (LOCMUN No. 18.695) revised several provisions of the 1980 Constitution. In particular, it confirmed the positive move of the constitution in the definition of the municipality as a corporation of public law with legal personality and own property. In addition, it created the CODECO (*Consejo de Desarrollo Comunal*), even if these councils were elected by the COREDES.

Overall, this policy was more a policy of deconcentration of state responsibilities to subnational entities than a genuine decentralisation reform. Provinces and municipalities were no longer elected: provincial governors and mayors were named directly by the president and were loyal to the national government first, their area second. Most of the mayors (and all the intendants and provincial governors) came out of the military, the objective being to transmit commands from above in the most efficient way possible (Stewart and Ranis, 1994). Therefore, all municipalities were under strict military-style national control while decision-making authority was at the central level.

While a major motive of decentralisation was to reduce the size of the state, it was conducted in conjunction with the privatisation of public services and companies. The provision of public services was then intended to operate like a private market, with strong central control. Municipal-level tasks were privatised wherever possible and the streamlining of all levels of government became a primary goal. Municipalities thus acted

like "service delivery agents" providing local public service on a cost-effective basis and not as "local government", having very limited local governing power (Stewart and Ranis, 1994).

Figure 1.6. **Historical timeline of decentralisation in Chile 1970-2017**



The return to democracy (1990 – 2008)

Democracy returned with the presidency of Aylwin, a Christian Democrat leading a coalition of centre and left parties, the *Concertación*. During this post-authoritarian period, progress towards decentralisation was made as decentralisation was seen as a means of re-democratising the country and reforming the state.

First, it was decided to keep most of the governance reforms implemented by the Pinochet regime. In fact, it would have been strange to restore democratic institutions at the subnational level and, at the same, recentralise the functions that had been devolved to the municipalities or abolish the new regions. Therefore, at the beginning of the 1990s, Chile was already a more decentralised country than before the dictatorship because some previously-deconcentrated tasks and resources were now in the hands of self-governing entities, municipalities.

Several reforms were adopted. The first was the adoption of the constitutional law, passed in November 1991, which modified chapter XIII of the 1980 Constitution related to municipal and regional administration.

Then, two reforms were adopted in 1992 concerning both the regional and municipal levels. Although limited in scope, they brought about significant advances:

- At the regional level, the organic constitutional regional Law No. 19.175 adopted in late 1992 (*Ley Orgánica Constitucional en Materia de Gobierno y Administración Regional* – Organic Constitutional Law on Regional Government and Administration - LOCGAR) created a mixed regional government organism (called "GORE") consisting of two distinct bodies: an executive function

represented by the intendant appointed by the President of the Republic and a "normative, arbitration and supervisory" function, represented by a regional council (*consejo regional* or CORE) that is indirectly elected by municipal councillors. The intendant plays a dual role as the head of the regional government but also as a central government official representing the President in the region. Under that role, he is responsible for overseeing the internal governance of the region and consults with other deconcentrated central representatives, the regional ministerial secretaries (SEREMIs). When these two roles come into conflict, it is the latter that tends to prevail (Martelli and Valenzuela, 1999; Eaton, 2004). The CORE has no political powers but only broad functions related to the social, cultural, and economic development of the region of normative, arbitration, supervisory and financial nature (LOCGAR, article 28). Specifically, the CORE supervises, has decision-making, regulatory and supervisory powers, and is responsible for approving the region's development plans and its budget, which must be in line with the country's national development policy and the national budget (OECD, 2011). Despite the reform, regional governments have no independent tax authority and are entirely funded by the central government.[4] Their budget is part of central government budget, determined in the annual budgeting process. They do have the right to assign and distribute to municipalities regional development funds for specific projects but these funds are centrally provided and allocation is made according to priority areas determined by the national government.

- At the municipal level, the Law No. 19.130, passed in 1992, revised several provisions of the law 18.695 adopted in 1988 during the Pinochet regime and set the terms for the first municipal elections held in June 1992. For the first time in Chilean constitutional history, the municipality was defined as a public law corporation, with a legal personality, its own patrimony and autonomy. Its functions are to promote the economic, social and cultural development of the *comuna*, with the participation of the local community. It is led by the mayor and the Municipal Council. In addition, the municipality has a consultative body, the Community Council of Civil Society Organizations (*Consejo Comunal de Organizaciones de la Sociedad Civil* - COSOC), which aims at allowing the participation of the community. This reform was followed in 1995 by the Law No. 19.388 which modified the Municipal Revenue Act, in particular the territorial tax and in turn the Municipal Common Fund.

An incremental decentralisation process in the 2000s, which remains limited

In the following years, decentralisation continued according to this gradual approach consisting in a permanent modernisation process to adjust the ways municipalities are organised, financed and managed. As far as regionalisation is concerned, SUBDERE has been an active promoter of decentralisation. It played a crucial role by advocating for the increased participation by regional governments in the investment decisions of the national government, as well as supporting a change in the election of regional councillors (Eaton, 2004). These policy options were summarised in a reform proposal, "The Decentralised Chile We Want" (*El Chile descentralizado que queremos*) (SUBDERE, 2001).

However, the centralist heritage remains strong and deeply rooted in the political-administrative culture and behaviour (SUBDERE, 2000) with tremendous political resistance to decentralisation initiatives. This is linked in particular to the highly-

centralised nature of Chilean political parties, the "powerful Santiago-based bureaucrats" and the resistance of legislators combined with the weakness of subnational actors in Chile's political system (Valenzuela A., 1978; Scully, 1995; Eaton, 2004). It is also based notably on the desire to protect Chile's identity as a unitary country and to favour unique and standardised solutions for diverse and complex problems (Raczynsky and Serrano, 2001; Eaton, 2004). In addition, centralisation is often viewed as a development model that has been able to ensure internal political and macroeconomic stability, national unity as well as economic efficiency and growth - thanks also to economic model based on market mechanisms and globalisation (OECD, 2009; Lorrain, 2014).

Linked to constitutional constraints, this has resulted in the slowing down and scaling back of the ambition of decentralisation initiatives, which are often "top-down" and restricted to administrative aspects (and even just deconcentration). This comes at the detriment of having more political approach associated with the democratic processes and the redistribution of powers among levels of government. In fact, a clear distinction between "powers" and "administrative functions" is made. According to this, only administrative functions could be decentralised to subnational governments while "powers" should remain deconcentrated, i.e. carried out by state deconcentrated administrations (SUBDERE, 2014). Therefore, the reforms adopted during this period deepened the processes of administrative decentralisation initiated previously but did not make major substantive contributions to political decentralisation.

At the regional level, after a little more than 10 years after the LOCGAR law created the regional governments, it was decided to improve the institutional framework. Law No. 20.035 of 2005 amended the LOCGAR to provide regions with greater legitimacy and representation, strengthen management and administrative capacities, and assigned them greater powers and resources, in particular for planning and regional public investment (Ropert, 2011). During this period, two new regions were created: Arica and Parinacota Region (by taking out the two northernmost provinces from the Tarapacá Region) and the Los Ríos Region (grouping the provinces of Valdivia, formerly part of the Los Lagos Region, and Ranco, formerly part of Valdivia).

At the municipal level, Law No. 19.602 was published in 1999 to formulate a new reform to the Constitutional Organic Law of Municipalities No. 18.695. This new law extended municipal powers, defining better both shared and exclusive functions. Municipalities acquired new responsibilities in the field of economic development, environment, planning, equal opportunities, etc. In addition, municipalities were given regulatory, policy and planning powers and tools as well as the capacity to implement programmes as long as they are consistent with national policies. The law also modified the existing provisions concerning citizen participation mechanisms, obliging municipalities to issue municipal ordinances detailing citizen involvement in municipal life, organise public hearings (for municipalities of more than 5 000 inhabitants), create complaint offices or giving the population the possibility to hold a local referendum or engage in participatory budgeting. Some improvements were also made towards the recognition and protection of municipal staff workers.

In addition, Law No. 19.602 empowered SUBDERE to collect, process and disseminate information related to municipal tasks, especially regarding their financial and budgetary management, personnel administration and service provision (article 2). This rapidly translated in the creation of a municipal information system which is considered a best practice, the *Sistema Nacional de Información Municipal* or SINIM (Box 1.6 and chapters 2, 3 and 4).

Box 1.6. **The National Municipal Information System (SINIM)**

The national system of municipal indicators, developed by SUBDERE, is a programme that collects, orders, processes and makes public information available concerning Chilean municipalities. It provides over 150 standardised indicators for each of Chile's municipalities, starting in 2001. It covers numerous areas: administration and finance, health, education, development and territorial management, social and community management, gender, human resources, information and communication technologies, and municipal characteristics. SINIM offers accessible information to the general public through its dedicated website (www.sinim.gov.cl).

The system offers a wealth of insightful information covering the fiscal activity of each and every municipality in Chile. In addition to detailed data on the indicators used in the attribution algorithm of the Common Municipal Fund (FCM), the tab "Información SINIM" provides access to different data under different formats, including the budgetary operations of the municipalities.

SINIM data make it possible to compare the performance of all Chilean municipalities and help different stakeholders make informed decisions. Beyond municipal fiscal data, SINIM is a veritable gold mine of information on the administration, health and education services, spatial planning, poverty, other social indicators, and the geographical characteristics of all of Chilean municipalities. SINIM provides insights into the progress being made by municipalities in the economic and social development of Chile. In addition, it allows a municipality to benchmark itself against other local administrations.

SINIM can be considered a best practice because it increases transparency, accountability and public scrutiny of municipal activities and finances.

Source: Based on www.subdere.gov.cl/programas/division-municipalidades/sistema-nacional-de-informacion-municipal-sinim and World Bank (Programa de Fortalecimiento Institucional Municipal - PROFIM project - http://www.worldbank.org/).

The Municipal Revenue Act was again modified in 2005 after several difficult rounds of negotiations, coupled with the continued pressure from ACHM including a national mobilisation of municipalities in May 2005 (Vial Cossani, 2014). The law 20.033, better known as the Municipal Revenue Act II (Mardones Z. R., 2006), introduced some fiscal measures concerning the property tax (automatic readjustment of real estate, reduction of municipal tax exemptions unilaterally granted by the central government to taxpayers without compensating the municipalities for lost tax revenue) and the Municipal Common Fund (direct contribution of the state to the FCM). However, this law was strongly contested as soon as it was promulgated, in particular by property owners to the point that a new law 20.280 was published in 2008 to amend the Law No. 17.235 on territorial tax and the decree-Law No. 3.063 of 1979 on municipal revenues. The law extends deductions concerning the municipal business licenses (*patentes municipales*).

Also noteworthy is the Law No. 19.737 enacted in 2001 which changed the electoral system concerning the mayor and councillors, establishing separate elections. In fact, until the previous electoral system set up in the Constitutional Law No. 18.695, the mayor was selected among the municipal councillors. The mayor was the councillor who had received the greatest number of votes and who also received at least 35% of the vote. When no councillor received the necessary quota to become mayor, the municipal council selected the mayor from among its members. This system was considered as detrimental to local democracy because it favoured electoral pacts and submission to party elites as

much as or more than to the constituents of local communities. With the new Law No. 19.737, there is a separation between the election of the mayor and the municipal councillors. The law also authorised the re-election of mayors, which was not the case under the previous electoral regime. The direct election of mayors helped to diminish the elitist nature of municipal electoral arrangements and increase democratic accountability of local elected officials. However, party elites still maintain a significant degree of control over local politicians (Posner, 2008). This new system has been in place since the municipal elections of 2004.

Recent changes and prospects since 2009

A new push towards a decentralisation agenda in 2009

The previous two decades can seem quite timid in terms of advances in decentralisation, especially when compared to the experiences of neighbouring countries (e.g. Argentina, Brazil, Colombia, Peru) and other OECD countries, where ambitious reforms were launched, particularly in Eastern and Central European countries. However, they have set the stage for more ambitious reforms, which now seem to be on track.

Decentralisation and regionalisation have become one of the most important items on the national political agenda. The continuing hyper-concentration of powers and wealth in the Santiago region correlated with a hyper-centralisation have reinvigorated the debate regarding the urgent need to reform the multi-level governance structure by modernising and transferring new powers and resources to subnational governments. This debate on decentralisation also takes place in a context of policy discussions about the productivity of Chile, pointing to the need to mobilise the regional productivity catch-up potential. For that, an efficient multi-level governance system is required, based an enhanced role for subnational governments i.e. more decentralisation (see also the introduction of Chapter 1). The debates take place in the economic and political arena but not only: several other groups of stakeholders have been engaged for some time in the promotion of decentralisation (Box 1.7). The debate resulted in the acceleration of new proposals for decentralisation and regionalisation from 2008-2009.

Box 1.7. **An increasing number of stakeholders are promoting decentralisation and regionalisation in Chile**

More and more organisations express their commitments to defending a model of decentralisation for Chile, based on self-governing regions and reinforced local governments. They obviously include national and regional associations of municipalities and regional councillors whose major role is to lobby in favour of decentralisation: *Asociación Nacional de Consejeros Regionales* (ANCORE), the two national associations of municipalities (the *Asociación Chilena de Municipalidades* – ACHM and the *Asociación de Municipalidades de Chile* - AMUCH), the National Commission of Councillors (Comisión Nacional de Concejales - ACHM) as well as regional and local associations such as the *Asociación Municipalidades Región del Bío Bío*, etc. Associations of subnational civil servants are also involved in the debate on decentralisation, such as the *Confederación Nacional de Funcionarios Municipales de Chile* (ASEMUCH) and the *Unión de Funcionarios Municipales de Chile* (UFEMUCH), including sectoral associations (e.g. health, education).

Box 1.7. **An increasing number of stakeholders are promoting decentralisation and regionalisation in Chile** *(continued)*

The academic sphere from national and regional universities and other research centres is also particularly involved in the defence of a regionalised and decentralised state. One can cite, among others, the *Universidad Autónoma de Chile* (e.g. *Instituto de Estudios Municipales* - ICHEM), the *Universidad de Chile* (e.g. *Instituto de Asuntos Públicos* - INAP), the Pontificia *Universidad Católica de Chile* (e.g. *Centro de Políticas Públicas* UC, *Instituto de Estudios Urbanos y Territoriale*s), *Universidad Alberto Hurtado*, the *Universidad de Los Lagos* (e.g. *Centro de Estudios del Desarrollo Regional y Políticas Públicas* – CEDER), the Universidad del Bío Bío (e.g. *Centro de Estudios Urbano Regionales* CEUR, *Centro de Políticas Públicas y Ciudadanía*), the *Centro de Investigación de Políticas Públicas de Tarapacá* (CIPTAR), the *Centro de Estudios Públicos* (CEP) or again the *Corporación de Estudios para Latinoamérica* (CIEPLAN).

Think tanks and business and citizen associations are also active. Several national and regional organisations are particularly strong supporters of regionalisation and decentralisation such as, the Chilean Chamber of Construction (*Cámara Chilena de la Construcción* – CChC, 2014), Grupo Res Pública Chile (Grupo Res Pública Chile, 2013), CorpAraucanía (*Corporación para el Desarrollo Productivo de La Araucanía)*, Corbiobio (*Corporación Privada de Desarrollo de la Región del Bío Bío*), Fundación Chile Descentralizado (ex CONAREDE - *Consejo Nacional para la Regionalización y Descentralización de Chile*), Fundación P!ensa.

Some groups have been involved in the work of the Presidential Advisory Commission on Decentralisation and Regional Development set up in April 2014.

Intense legislative activity concerning the municipal sector between 2009 and 2014 but no comprehensive decentralisation reform

At the municipal level, several amendments to the 18.695 Organic constitutional law have been enacted between 2009 and 2014 to improve municipal revenue and fiscal equalisation, enhance transparency and citizen participation, foster inter-municipal co-operation as well to enlarge some municipal competences.

The main municipal reforms were the following:

- Law No. 20.237, published on 24 December 2007 and implemented in 2008, introduced amendments to Decree Law No. 3,063 of 1979 on Municipal Revenues in order to improve the distribution formula of the Municipal Common Fund, the horizontal equalisation mechanism set up in 1979 to reduce fiscal inequalities between municipalities (see Chapter 3). Changes introduced by the new formula have benefited vulnerable municipalities the most, and extended the list of eligible municipalities to FCM transfers. The law also modified the LOCMUN, introducing rules that establish greater discipline in the administration of municipal resources.
- Law No. 20.285 Access to Public Information passed in 2008 and commonly referred to as the Transparency Law. It establishes citizen access to information at all levels of government, including regions and municipalities (see Chapter 5).
- Constitutional reform adopted in 2009 (Law No. 20.346), which aims at fostering municipal co-operation on a voluntary basis. It enables the formal association of municipalities in order to establish not-for-profit organisations for different

purposes. This law was revised in September 2011 through the Law No. 20.527, which regulates the municipal associations (see below and Chapter 6).

- Law No. 20.355 of June 2009 extended the application of Law No. 19.886 on public procurement to the municipal concession contracts in order to increase transparency about these contracts and provide greater protection in terms of labour and social security to employees working for concessionary companies.
- Law No. 20.417 passed in January 2010 extended municipal responsibilities in the field of environmental protection while it was setting up a Ministry of Environment. Before the law, municipal responsibility was limited to cleaning and embellishment of the municipality. With the new law, municipalities can propose and implement measures to materialise actions and programmes related to the environment. They also have to apply environmental standards in their area and prepare an environmental ordinance.
- Law No. 20.500 issued in February 2011 on the reinforcement of citizen participation. The law set up the consultative Community Council of Civil Society Organizations (*Consejo Comunal de Organizaciones de la Sociedad Civil* - COSOC), which replaced the old Community Councils (CESCO), which proved to be not effective enough. The objective of the new law is to ensure an institutional mechanism for citizen participation and control of municipal management and therefore to strengthen democracy at the municipal level (see Chapter 5).

Regionalisation agenda has made significant progress between 2009 and 2014

This step-by-step regionalisation process, started in 1992, has continued. A significant advance has been made with the constitutional reform No. 20.390 passed on 16 October 2009, which amended the LOCGAR No. 19.175. The constitutional reform substantially changed the structure and operation of the regional governments (OECD, 2013b):

- It included direct election by citizens of regional councillors, creating a democratically-elected body to manage regional development. The first direct elections took place in 2013 and regional councillors took office on March 2014.
- The law stated that the election of the CORE's president would be regulated by a subsequent law, which was achieved with the Law No. 20.757 enacted in 2014 establishing that the president of the regional council would no longer be the intendant but a councillor elected by his/her fellow councillors. All regions now have a president of the regional council elected in this manner.
- It enabled the president to transfer ministerial competences and public service delivery to the GORE, particularly with respect to public administration, territorial planning, economic development and social and cultural development (OECD, 2013b).
- It also included the transformation of the Programming Contracts (*convenios de programación*/CP) into compulsory and binding instruments. These annual or multi-year contracts can be concluded between one or more regions, ministries, municipalities or private institutions and represent a first step towards multi-annual budgeting and multi-level planning.

- This reform also established the regional annual budget and enables CORE to approve it. It is, comprised of central transfers, funds received from programming contracts and now revenue generated from the regions' mining, aquaculture and casino arrangements.
- It also recognised for the first time metropolitan areas as institutional entities, the precise definition of the characteristics and governance structure of these areas being defined in a subsequent law (still pending at the time of publication). Article 110 of the law enables the establishment of a metropolitan area co-ordinating council (*consejo coordinador regional de acción municipal*). The competences attributable to such a council include planning and co-ordinating inter-municipal initiatives dedicated to preventing and solving problems that arise from administrative fragmentation and which require a co-ordinated effort to resolve. The legislation also establishes a Metropolitan Investment Fund (*Fondo de Inversión Metropolitano*/FIM) to finance projects of metropolitan significance (OECD 2013a).

Another step was made in 2010, with the adoption of the Law No. 20.530, creating the Ministry of Social Development to replace the National Planning Ministry (MIDEPLAN). It established that the regional development planning function should be transferred to the regional governments by a law amending the LOCGAR, resulting in the creation of new regional planning divisions within regional governments (currently under discussion).

A decisive impetus was given in 2014 with the Presidential Decentralisation Agenda

A decisive step forward was taken by President Michelle Bachelet who announced an ambitious Decentralisation Agenda as part of her Government Programme (Government of Chile, 2014). It objective is to carry out profound decentralisation in the country, focused on coherence, gradualism and broad agreements, which would represent a marked contrast with the omnipresent centralism in place in Chile at present (SUBDERE, 2014).

To this end, the President started by setting up a Presidential Advisory Commission on Decentralisation and Regional Development (*Comisión Asesora Presidencial en Descentralización y Desarollo Regional*) in April 2014 to make proposals. The Commission had 33 members, representing numerous key stakeholders from the public and private sectors. The commission used a large participatory process that captured the views and aspirations of all territories. It was based on a web platform, hearings and meetings with various sectors. Fifteen regional dialogues were organised as well as a series of provincial or territorial workshops involving citizens, business, subnational governments, NGOs, corporations, universities, media, public workers, etc. (see Chapter 6). The commission presented its final report on 7 October 2014 (Box 1.8).

Box 1.8. **Report of the Presidential Advisory Commission on Decentralisation and Regional Development**

The report of the Presidential Advisory Commission on Decentralisation and Regional Development, presented in October 2014, contains 70 measures, grouped into five main topics: political decentralisation, administrative decentralisation, fiscal decentralisation, local and regional capacities and citizen participation.

The 10 essential measures proposed by the commission were:

1. Defining the Chilean state as a decentralised state: Adapt the constitution to empower regional governments with management autonomy, enabling them to carry out their tasks.
2. Democratic election of a regional authority: this authority should preside over the government and regional administration as well as the regional council.
3. Devolution of competences, services and programmes: gradual transfer of competencies, especially productive development; social development; infrastructure, transport and environment; education, science, culture and technology.
4. Creation of a system for the management of metropolitan areas.
5. Creation of a regional revenue law and strengthening of the municipal revenue law.
6. Creation of a Convergence fund for interregional equity, following international examples (European Union, Canada, Australia or Japan) and establishing common minimum guaranteed services in any part of the national territory.
7. Regional system for the management of human resources: set of specific measures aimed at development of "qualified human capital" (talent) for the development of municipalities and regions.
8. Strengthening regional public institutions and policies: enhancing the leadership of the regional government in the design, implementation and evaluation of regional public policies, thus supporting the political, administrative and fiscal structural reforms of Chile.
9. Reinforcing local and regional democracy e.g. encouraging the creation of regional political entity, limiting the re-election of regional and local elected representatives (not more than two or three consecutive mandates).
10. Strengthening citizen participation: a set of proposals that strongly stimulate the involvement and participation of citizens in matters of local and regional interest and increasing transparency (e.g. organisation of regional and local plebiscites; recall referendum).

Source: *Comisión Asesora Presidencial en Descentralización y Desarrollo Regional* (2014), *Propuesta de Política de Estado y Agenda para la Descentralización y el Desarrollo Territorial de Chile - Hacia un país desarrollado y justo*, https://prensa.presidencia.cl/lfi-content/otras/informes-comisiones/InformeDescentralizacion.pdf.

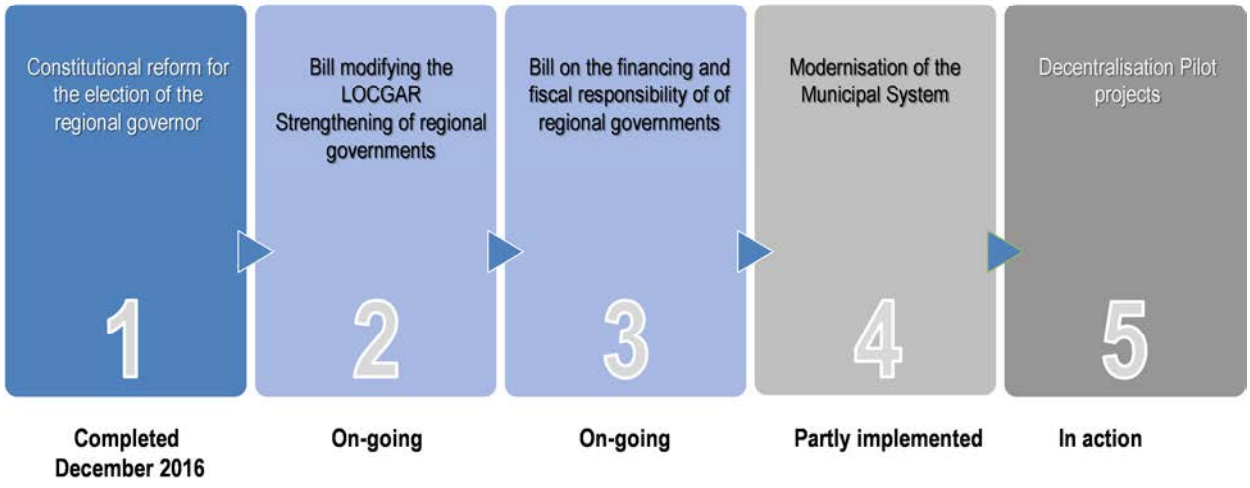
In the longer term, the president committed to writing a new constitution that would replace that of 1980, and that would foster greater citizen participation, equality and social justice, including the decentralisation principles.

The five pillars of the decentralisation agenda

The Decentralisation Agenda comprises five pillars (Figure 1.7):

- The first is the constitutional reform allowing the direct election of the executives of regional government who will become "regional governors". Regional governors will play both roles: executive of the regional government and president of the regional council.
- The second pillar is the transfer of competencies from the central government to regional governments. This project modifies the administrative structure of the GOREs creating new divisions (Productive Development and Industry; Social and Human Development; and Infrastructure and Transports), which will be in charge of the new competences. The project also creates a new regional manager and a chief of control. It also opens the possibility for the GORE to manage metropolitan areas, especially for urban infrastructure (mobility and public spaces) and waste management.
- The third pillar concerns a reform of the financing system of regional governments. It is still under preparation but it would include a regional financing mechanism mainly based on central government transfers in the form of grants but no regional own-source revenues at this stage. It would also include the design of fiscal responsibility rules for regional governments and allow access to borrowing under strict conditions. These plans are still subject to major change.
- The fourth pillar is dedicated to the “modernisation of the municipal sector”. In this perspective, the presidential message is clear: "That the municipalities go from fulfilling a function exclusively of administration, to the constitution of true Local Governments" (Government of Chile, 2014). This pillar comprises in particular a series of modifications to the current municipal officials' staff structure and management in order to strengthen human resource management practices and professionalisation (this resulted in the adoption of the Law No. 20.922, published in May 2016, known as *plantas* law). This municipal pillar also contemplates a complete reform of the financing system of municipal governments, including an increase of the Municipal Common Fund’s resources, as well as the definition of new rules of fiscal responsibility for municipalities.
- The fifth pillar, which is linked to pillars 1, 2 and 3, is the launching of pilot experiences to test the transfer of competences from the central government to the regions and to assess their impact on regional organisation and management. These pilot experiments are intended to be a “collaborative, gradual and inter-sectoral experience” whose purpose is to provide the region with appropriate skills, knowledge and methodologies (SUBDERE, 2016) in order to gradually strengthen regions and learn from experience. After two years of intense discussion, all five pillars have started to take shape in 2016 at regional and municipal levels.

Figure 1.7. **Decentralisation agenda: Regional and municipal levels**



Source: Updated from SUBDERE (2015).

The progress of the decentralisation agenda at the regional level

At the regional level, the law corresponding to the first pillar (No. 20.990) was published on 5 January 2017, stating that regional governors will be elected by popular vote every four years. The election date has not been determined but could take place close to the presidential, parliamentary and regional councillors' elections. The organic electoral law is still pending at the time of publication of this report.

The regional governor will be the executive of the regional government (instead of the intendant) and will chair the regional council. The regional governments, that already have legal personality under public law and their own assets, will be governed by an elected regional governor and a regional council. Regional councillors will have more oversight powers in order to ensure a balance of powers with the regional governor. It is important to note that the figure of the "intendant" will not totally disappear. In fact, he will be replaced by a "presidential delegate" at the regional level, appointed by the President of the Republic. This regional representative of the President will have functions of co-ordination, supervision and oversight of public services that depend on - or are related to - the central government. In addition, provincial delegations will be created, also appointed by the President of the Republic. The functions of these delegations will be defined by constitutional organic law.

The organic constitutional bill on the transfer of regional responsibilities (Pilar 2) is being discussed in a joint commission at the Congress (at the time of publication). The bill on regional financing and fiscal responsibility (Pilar 3) should be presented in 2017.

As far as pillar 5 is concerned, pilot experiments have been launched in order to test the incremental transfer of competences with selected regions in order to gradually strengthen regional capacities and learn from the experiences (see Chapter 6).

The development of the decentralisation agenda at the municipal level

At the municipal level, a Memorandum of Understanding (MoU) (*Protocolo de Acuerdo para la modernización del sistema municipal*) was signed on 14 November 2014 between SUBDERE and the Chilean Association of Municipalities (ACHM) as well as the National Confederation of Municipal Officials of Chile (ASEMUCH). Within the framework of the MoU, SUBDERE set up a Technical Advisory Committee for Municipal Modernisation (*Comité Técnico Asesor para la Modernización Municipal* - CTAM). Comprising experts in municipal issues including mayors, councillors and municipal workers (ACHM, AMUCH, ASEMUCH, UFEMUCH, National Committee of Councillors) as well as the Centre of Public Policies of Católica university (*Centro de Estudios Públicos*, CEP), the Inter-American Development Bank (IADB) and the International Labour Organisation, the CTAM first met in April 2015 with the mission to develop a set of proposals that would thoroughly reform the municipal system and that would be based on the following general objective: "Autonomous local governments, able to participate in managing their own resources in an effective and efficient way, aiming at economic, social and inclusive productive strategic development of its citizens in its territory". Four strategic objectives have been defined: modernisation, equity, autonomy and accountability. On this basis, five working commissions have been established to work on concrete proposals on the following topics: fiscal responsibility, competences and resources, human resources, management model of municipal innovation and community participation. To this end, an Inter-Ministerial Committee for Municipal Modernisation, encompassing the SUBDERE, the General Secretariat of the Presidency and the Ministry of Finance, has been created to analyse the CTAM's proposals.

Important advances have been made since 2014 in several areas for the modernisation of the municipal system. Several new laws have been adopted (Box 1.9 and related following chapters). In particular, significant progress has been made to further professionalise and improve municipal human resources, resulting in the publication of Law No. 20.922 in May 2016, on "strengthening management and professionalisation of municipal staff". This long overdue law allows the municipalities to make independent personnel decisions, which was not the case until now (Eaton, 2004).

Box 1.9. **Main laws adopted since 2014 concerning the municipal sector**

- Law No. 20.742 adopted in March 2014 covers a large range of subjects and represents an important step towards the modernisation and strengthening of the municipal system. It covers topics such as the strengthening of the oversight role of the municipal council (see Chapter 5) and of the Comptroller General of the Republic thanks to new tools and procedures; the setting up of new norms designed to increase transparency and probity of municipalities (see Chapter 3); and the promotion of a better municipal staff management (definition of staff functions and creation of a Competitive Training Fund for Municipal Officials managed by SUBDERE's Municipal and Regional Training Academy, see Chapter 4).
- Law No. 20.922 published in May 2016 modifies "provisions applicable to municipal officials and gives new powers to SUBDERE" in this field. It represents a major step towards decentralising municipal staff management. It gives the mayor more flexibility with which to manage municipal staff and thus meet needs in terms of workforce and qualifications. In fact, the mayors are now allowed, with the consent of two-thirds of municipal council members, to modify the size of the *planta* staff every eight years as well as to reorganise the public workforce in terms of skills. It also improves professionalisation and remuneration (see Chapter 4).

Box 1.9. **Main laws adopted since 2014 concerning the municipal sector** *(continued)*

- Law No. 20.958 on Contributions to Public Space, approved in October 2016 represents progress towards better administration and management of urban spaces as well as towards new land-based financing resources for municipalities. The law requires that when new urban projects are executed, they contribute to the construction of parks, public spaces, and transport infrastructure needed to host urban growth. The developers will have to pay a contribution to finance municipal or inter-municipal works (in case of metropolitan cities), 70% of which will be invested in mobility projects (see Chapters 2 and 6).
- Law No. 20.965, published in November 2016 allows the creation of Community Public Safety Councils and Plans in each municipality. Municipal public safety council, chaired by the mayor and composed of various key stakeholders (representative of the intendant, members of the municipal council and COSOC, police force, prosecutor office's representative, etc.) will have an advisory role, receiving, ordering and analysing all kind of data and information related to public safety to establish a diagnosis of the situation in the municipality. It will support the mayor in the preparation of the municipal safety plan. This plan will be the management instrument that establishes the guidelines and measures to be taken to reinforce public safety at the community level.

The role of municipalities in this evolving institutional system

The diversity of the municipal landscape

Chilean municipalities are large by international standards

In comparison to the OECD, Chile's 345 municipalities are quite large on average, both in terms of surface area and number of inhabitants. On average, Chilean municipalities host around five times more inhabitants than across the OECD (51 650 inhabitants vs. 9 570 in the OECD), surpassed only by Korea, the United Kingdom, Ireland, Japan, New Zealand, Denmark and Turkey. The median municipal size is lower (18 205 inhabitants) but Chile remains in the top of OECD countries (Figures 1.8 and 1.9).

Figure 1.8. **Average municipal population (number of inhabitants, 2015-2016)**

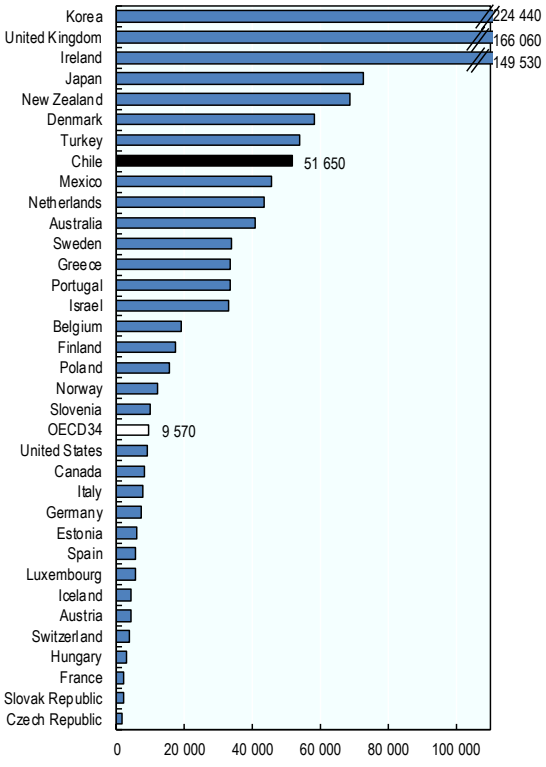
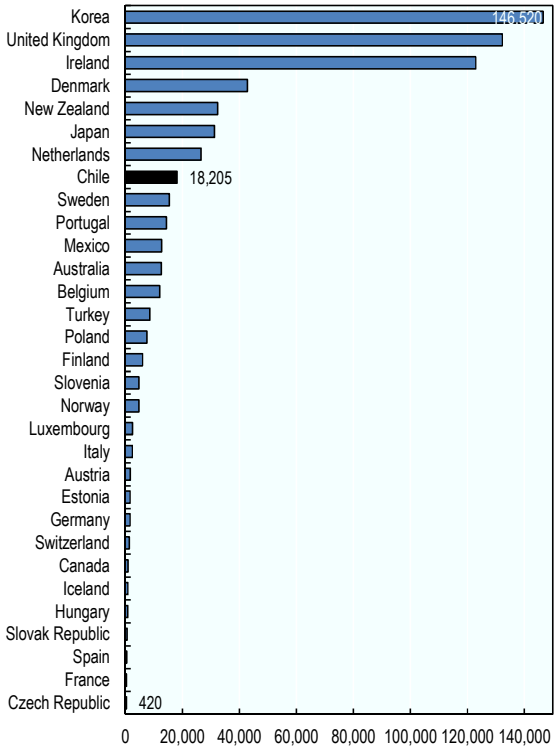


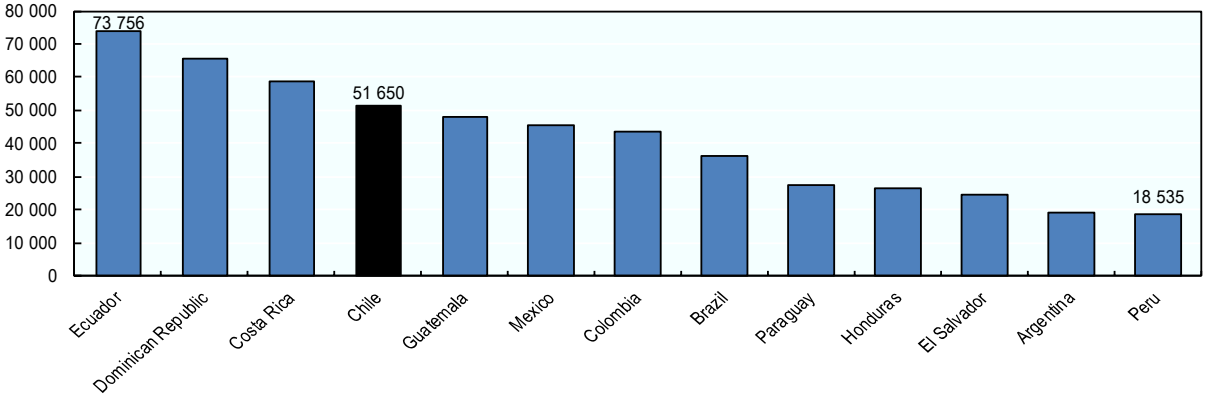
Figure 1.9. **Median municipal size (number of inhabitants, 2015-2016)**



Source: Elaborated from OECD (2016a), *Subnational governments in OECD countries: Key data (2016 edition).*

The situation of Chile regarding municipal average size is not uncommon in Latin America where municipalities are in general quite large ranging from 18 535 inhabitants in Peru to 73 756 inhabitants in Ecuador (Figure 1.10).

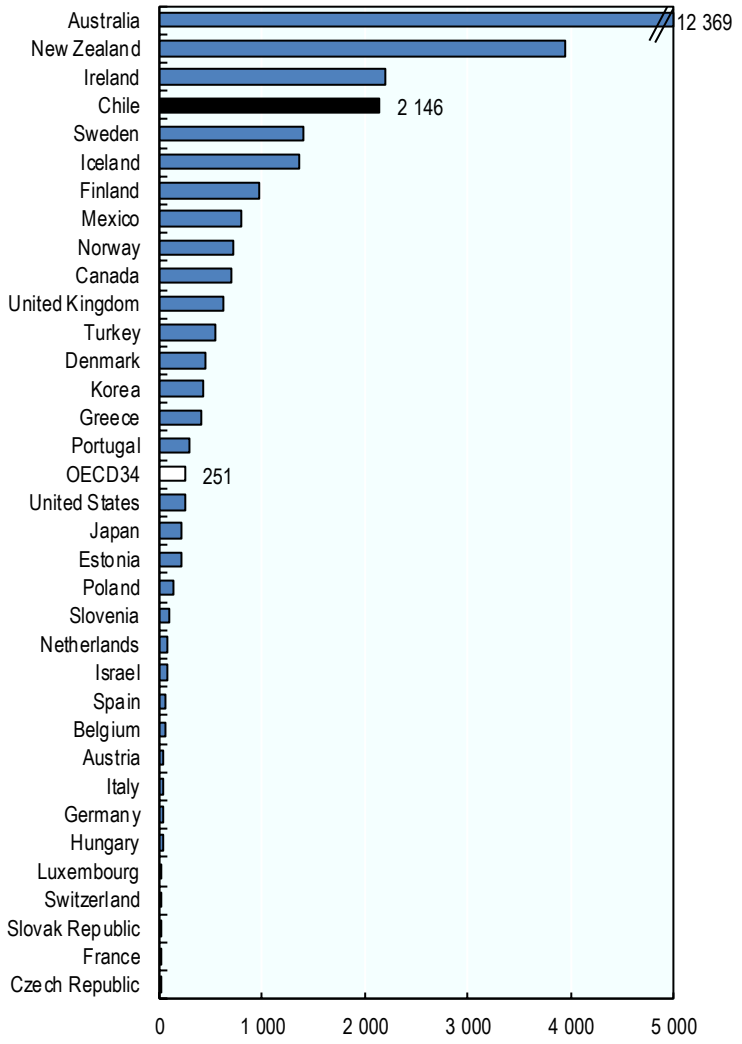
Figure 1.10. **Average Municipal size in selected Latin American countries (2015)**



Source: OECD/UCLG (2016), Subnational governments around the world: structure and finance.

In terms of surface area, only Australia, New Zealand and Ireland have municipalities with a larger average surface size (Figure 1.11).

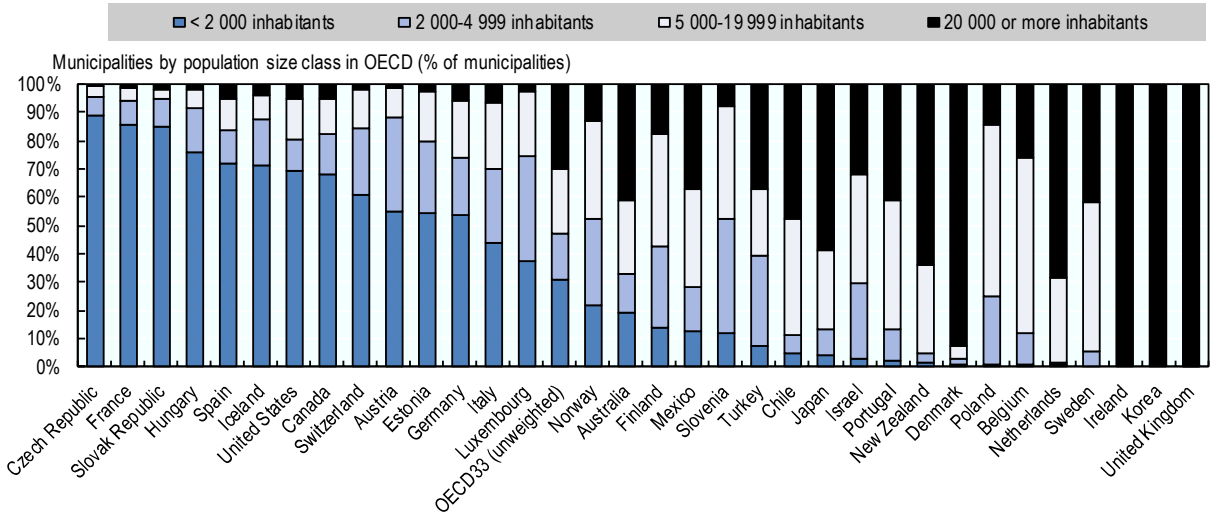
Figure 1.11. **Average municipal area in Chile is large compared to other OECD countries (2015-2016)**



Source: Elaborated from OECD (2016a*), Subnational governments in OECD countries: Key data* (2016 edition).

Looking at the number of municipalities by population size class, Chile also ranks high among OECD countries for having a very low number of small municipalities, i.e. fewer than 2 000 inhabitants (5% vs. 31% in the OECD on unweighted average). By contrast, 48% of Chilean municipalities have more than 20 000 inhabitants, which is significantly higher than the OECD average of 30% and on par with countries such as Portugal or Sweden. Finally, Chile has a great number of small to medium-sized municipalities (between 5 000 and 20 000 inhabitants): 41% vs. 23% in the OECD, which is also similar to Portugal, Finland and Slovenia (Figure 1.12).

Figure 1.12. **Municipalities by population size class in the OECD (% of municipalities, 2015-2016)**



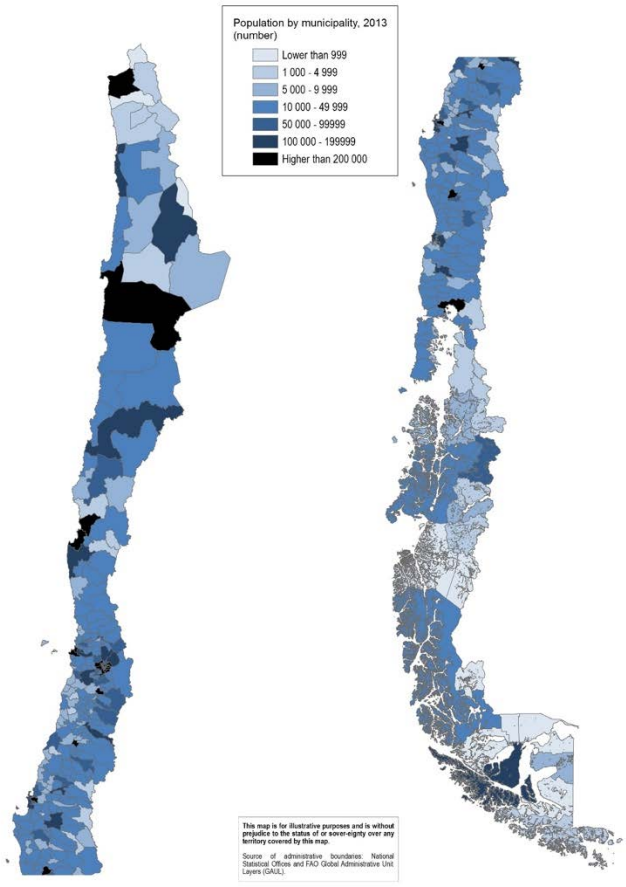
Source: Elaborated from OECD (2016a), *Subnational governments in OECD countries: Key data (2016 edition).*

Chilean municipalities in their national and regional contexts

The number of municipalities has been increasing throughout the history of Chile. In December 1891, a decree on the creation of municipalities (*Decreto de Creación de Municipalidades*) created 195 new municipalities, adding to a total of 253 municipalities. In 1917, this number reached 319, 335 in 1973 and 341 in 2004 as the result of the extension of the Chilean territory and the subdivision of existing municipalities into smaller ones. This was also accelerated by a presidential proposal and a parliamentary agreement allowing new municipalities to be established by splitting up existing ones. This has been the case of both the conurbations of Valparaíso and Concepcion where several new municipalities have been created since 1992 (Huntzinger and Prud'homme, 2004).

Today, the 345 municipalities cover the entire surface of Chile (Figure 1.13). By contrast to other countries with large uninhabited areas or with very low density (United States, Canada, Australia or Argentina for example), there are no unincorporated territories.

Figure 1.13. **Population by municipality**



Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal, Evolución presupuestaria (SINIM: www.sinim.gov.cl/).

The distribution of municipalities by region is very uneven. The region of Bío Bío and the Metropolitan Region of Santiago have the highest number of municipalities (54 and 52) while Arica y Parinacota and Antofagasta count respectively four and six municipalities (Table 1.2).

Table 1.2. **Chilean regions and municipalities (from most to least populated)**

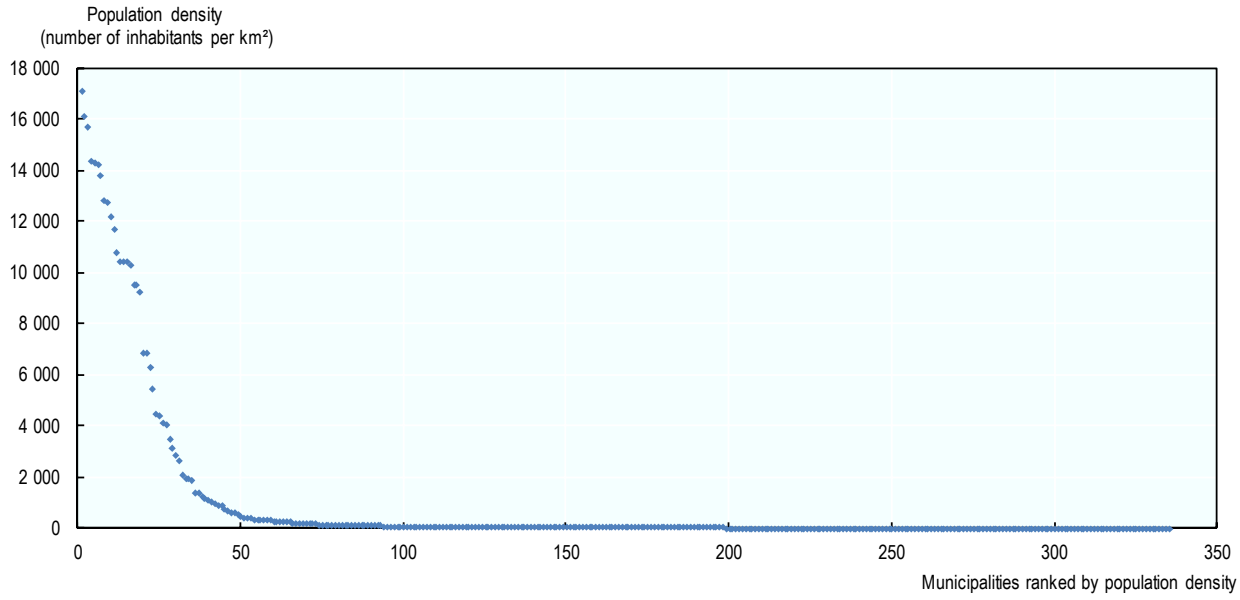
No.	Region	Area (km²)	Population (2014)	Population (% of national)	No. of Provinces	No. of municipalities*	Capital (main city)	City population
13	Metropolitan	15 403	7 228 581	40.57	6	52	Santiago (Puente Alto)	344 711 (602 203)
8	Bio Bío	37 065	2 100 944	11.79	4	54	Concepción	228 848
5	Valparaíso	16 402	1 808 300	10.15	8	38	Valparaíso (Viña del Mar)	295 075 (321 760)
7	Del Maule	30 299	1 035 593	5.81	4	30	Talca	231 860
9	Araucanía	31 845	983 499	5.52	2	32	Temuco	285 487
6	Lib. Gral B. O'Higgins	16 388	910 577	5.11	3	33	Rancagua	232 639
10	De los Lagos	48 585	834 714	4.68	4	30	Puerto Mont	239 534
4	Coquimbo	40 580	759 228	4.26	3	15	La Serena (Coquimbo)	212 621 (226 223)
2	Antofagasta	126 049	613 328	3.44	3	6	Antofagasta	372 325
14	De Los Ríos	18 431	401 458	2.25	2	12	Valdivia	166 048
1	Tarapaca	42 226	327 253	1.85	2	7	Iquique	196 437
3	Atacama	75 177	308 247	1.73	3	9	Copiapo	168 946
15	Arica y Parinacota	16 873	235 081	1.32	2	4	Arica	231 611
12	Magallanes y Antart. Chileno	150 775	163 748	0.92	4	11*	Punta Arenas	129 555
11	Aisén del Grl C. Ibañez del Campo	n.a.	107 334	0.60	4	10	Coihaique	59 862
	Total	**-**	**17 819 054**	**100.00**	**54**	**346**	**-**	**-**

* Including the municipality of Antártica which does not have municipality status.

Source: Instituto Nacional de Estadísticas (INE) 2014 (www.ine.cl) and OECD regional database (http://stats.oecd.org/Index.aspx?datasetcode=REG_DEMO_TL2).

The majority of municipalities in Chile have a low density. Among its 345 municipalities, 25% of them have a population density below 10 inhabitants per km², 62% have a population density below 50 inhabitants per km² and 75% of them have a population density below 150 inhabitants per km². This last threshold is the criteria used in the OECD definition to define rural municipalities (Figure 1.10). It means that according to the OECD definition of rural areas, 92% of the territory in Chile is rural and it hosted around 6.2 million inhabitants in 2014, representing 36% of the national population (Figure 1.14). In comparison to OECD countries, Chile has a higher share of population living in rural regions than the OECD average (25%), and a similar share as Greece, Iceland, Mexico and the United States. The percentage of the Chilean population living in predominantly rural regions has remained fairly stable since 1990 (OECD, 2014a).

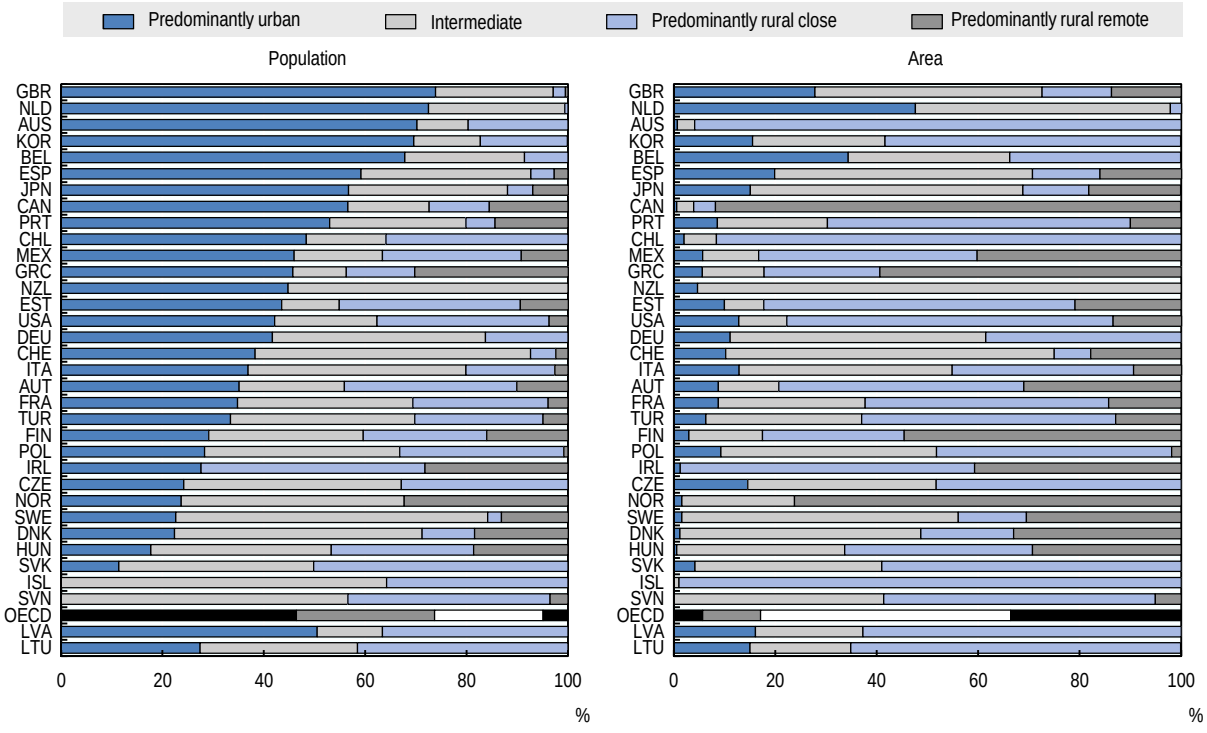
Figure 1.14. **Distribution of municipalities in Chile ranked by population density, 2014**



Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal, Evolución presupuestaria (SINIM: www.sinim.gov.cl/).

While the territory is mostly rural, the population is largely urban: 64.1% of inhabitants lived in predominantly urban or intermediate regions representing 8.4% of the Chilean territory.

Figure 1.15. **Distribution of population and area by type of region, 2014**



Source: OECD (2016b), *Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en.

Applying the OECD methodology to define functional urban areas (FUAs), which uses GIS techniques, census and commuting data at a municipal level, 26 FUAs have been identified in Chile. They were home to 77% of the population in 2012 and 101 municipalities (29% of the total) located either in the urban core area or in the hinterlands. Out of the 26 FUAs, 15 are classified as small urban areas (50 000 to 200 000 inhabitants) and contain 15% of the total FUA population. There are also eight medium-sized urban areas (200 000 to 500 000 inhabitants), where 19% of the total FUA population resides. Valparaíso and Concepción are considered metropolitan areas according to the FUA definition (more than 500 000 inhabitants) and have 15% of the total FUA population, while Santiago, which is the only "large metropolitan area" (more than 1.5 million inhabitants), has 51% of the FUA population (OECD, 2013b). By comparison, there are 1 179 FUAs in the OECD (based on 29 countries) including 275 metropolitan areas of which 82 are "large metropolitan areas".

Taking into account the municipal diversity

The 345 municipalities are very diverse in terms of size and density, population patterns, socio-economic characteristics and levels of resources. According to their location and level of development, they face challenges that need to be addressed individually.

In particular, there are large disparities between urban and rural municipalities, the latter have less technical capacity to administer, deliver services and manage their territory. This situation is even worse for remote and low-density municipalities located in mountainous or insular areas where connections are difficult and poor.

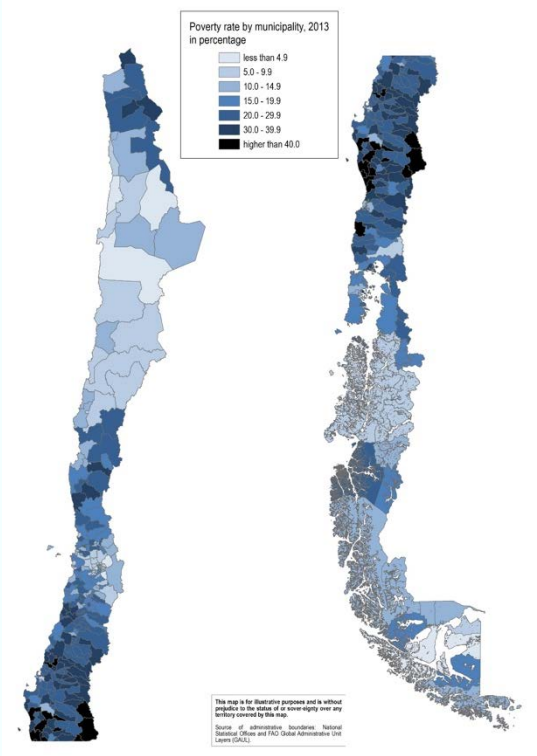
Urban municipalities also face specific problems. The 2013 OECD urban review of Chile revealed urban challenges with an economic dimension, including rising inequality, increasing poverty, the potential impact of housing policy on labour market mobility, and environmental concerns linked primarily to congestion (Box 1.10).

Box 1.10. **Municipal poverty in Chilean municipalities**

Poverty is another expression of inequality. While Chile has experienced an important process of modernisation, bringing greater economic prosperity and lower poverty since the late 1980s, poverty continues to grow. Three categories of people are affected by poverty and social exclusion: urban poor, rural poor and indigenous people. In particular, poverty is developing in municipalities located in urban areas. Poverty could be developing as an urban phenomenon in Chile as it is disconcerting that poverty is growing in 20 out of the 26 FUAs, and in some cases very rapidly and at high rates (OECD, 2013a). Overall, Chilean municipalities appear to have extremely uneven poverty rates, ranging from 0.3% in Vitacura to almost 60% in Alto Bío Bío. 73 municipalities (21% of Chilean municipalities) have a poverty rate over 30% and 17 over 40%.

Box 1.10. **Municipal poverty in Chilean municipalities** *(continued)*

Figure 1.16. **Level of poverty by municipality**



Source: OECD elaboration based on SUBDERE (2017a) the Sistema Nacional de Información Municipal, Evolución presupuestaria (SINIM: http://www.sinim.gov.cl/); OECD (2013a) Urban Policy Reviews, Chile 2013, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264191808-en.

In metropolitan areas, inequalities are very high among municipalities in the same agglomeration (see Chapter 3). The high degree of inequality in the agglomerations of Santiago, Valparaíso and Concepción is of particular concern, given the large social costs. The Santiago FUA displays the highest inequality across municipalities in estimated GDP per capita when compared to other OECD metropolitan regions (OECD, 2013a). Greater Santiago encompasses 35 municipalities, which are highly polarised in terms of poverty rates. This inequality is also present in household incomes and levels of education: Santiago's richest municipality has an average household income eight times that of the poorest, as well as higher levels of education. In addition, richer municipalities have better education coverage (especially in pre-primary and higher education) and better results on basic education performance tests (see also Chapter 3). High levels of inequality and spatial polarisation within the metropolitan areas are also a challenge to social cohesion and social stability (OECD, 2011). In some rural areas, poverty is also high, the average rate being 15%.

SUBDERE has developed a typology in order to better take into account the diversity of the municipal landscape and use this classification as a policy instrument to implement programmes: the FIGEM typology (Box 1.11).

Box 1.11. **The FIGEM typology**

In 2012, SUBDERE created a municipal typology for ranking municipalities in order to allocate funds aimed at improving municipal management (*Fondo de Incentivo* al *Mejoramiento de la Gestión Municipal* - FIGEM).

The idea behind this typology was to recognise the diversity of Chilean municipalities and their heterogeneous realities. Until recently, for historical and practical reasons, public policy has been evenly applied in Chile, which is reflected in uniform legal instruments and institutional design. Acknowledging this diversity through appropriate tools can help all levels and sectors of the public administration to design and implement programmes, projects, standards adapted to the different realities of territories. This new approach was seen as a fundamental factor for the achievement of the decentralisation and the strengthening and the modernisation of the municipal system. The typology has been conceived as a concrete and practical methodological tool for the recognition of the diversity of the municipal world. It should also help to reinforce collaboration, co-ordination and integration of public policies at the local level.

The classification is based on two main categories of criteria:

- Socio spatial-territorial: based on the range and quantity of services provided by the municipality. It is built on different sizes, dispersion of the political-administrative hierarchy, and type of locality. They are represented by a series of variables: population, number of housing units, level of rurality, density, disorder of population centres, administrative status.
- Socio-economic: based on dimensions of the municipality's assets, human capital and the socio-economic characteristics of the population. The relevant variables are property values, the average per capita income actually collected from the municipal business tax, the average education level, the illiteracy rate, poverty rates or the average household income.

On this basis, the typology of municipalities results from an analysis of clusters, the goal of which is to gather the elements and variables in groups that minimise internal variance and maximise variance between groups.

Source: SUBDERE (2005), Report "Tipología: Herramienta Base para el Reconocimiento de la Diversidad Comunal-Municipal".

The uniformity of municipal political organisation and responsibilities

Municipalities are regulated by the Constitutional Organic Law on Municipalities, Law No. 18.695 (LOCMUN) of 1988, which has been amended several times. According to article 1, the municipalities are "autonomous corporations of public law that have a legal personality and their own assets, whose purpose is to satisfy the needs of the local community and ensure their participation in the economic, social and cultural progress of the respective *comunas*".

Despite their diversity, all Chilean municipalities have the same political organisation, functions and funding arrangements, which can be, however, adapted to the size of municipalities.

Municipal political bodies

Articles related to municipal governments are now included in Chapter XIV of the 1980 Constitution, which has been amended several times (Government and Interior State Administration), from articles 118 to 122 as well as in the general provisions (article 123 to 126). Municipal organisation is detailed in the LOCMUN.

The mayor and municipal councillors are elected by direct universal suffrage

By law, municipalities are governed by a mayor who is the executive body (*alcalde*) and a municipal council, representing the deliberative body (*consejo municipal*), both directly elected for a renewable period of four years.

They are elected by universal suffrage. Candidates must be sponsored by registered political parties that obtained at least 5% of the vote in previous elections. The LOCMUN requires that the mayor and councillors be citizens in good standing, reside in the region where they are running for office, and be literate. Mayors are elected by a simple majority, while municipal councillors are elected according to a proportional representation system. Mayors and councillors are elected on a separate ballot as required by law since 2004. The law establishes that municipal elections take place every four years on the last Sunday of October. The newly-elected authorities take office on 6 December of that same year (the last elections took place in October 2016). It is forbidden to simultaneously hold national and local office and government officials and members of Congress cannot run for municipal office.

Mayor's functions

The mayor is the highest authority of the municipality, in charge of managing the municipality. The mayor convenes and chairs the municipal council meetings with the right to vote. The mayor's main responsibilities are to appoint and remove municipal employees, manage assets, goods and fiscal resources, manage municipal permits for different activities, enact general or specific resolutions and ordinances, co-ordinate with central government services, sign municipal contracts and call for municipal referendums (Couso et al., 2011). The obligation of probity and transparency has been recently reinforced through the publication of the Law No. 20.880 on January 2016 on "Probity in Public Service and Prevention of Conflicts of Interest". This law prevents conflicts of interest and forces mayors and councillors to send a declaration of interests and assets to the Comptroller General of the Republic who is responsible for overseeing the timeliness, integrity and veracity of the content of the declarations. It is also the mayor's responsibility to propose a municipal plan, a budget, investment programmes, and zoning plans to the municipal council for approval. The mayor also appoints delegates to remote areas of the community.

Municipal council's role

The number of councillors varies, from 6 to 10, depending on the number of registered voters in each municipality.[5] This number is among the smallest among OECD countries, where it ranges from 5 on average in Hungary to 60 in Germany (see Chapter 5).

According to the LOCMUN, the municipal council, chaired by the mayor, supports the mayor in municipal administration. It has decision-making, regulatory and supervisory functions. It is primarily responsible for establishing rules (regulating), resolving problems and controlling management. The council's responsibilities can be summarised as: approving ordinances and regulations; approving plans, budgets and

decisions for service provision; overseeing the mayor's management of the municipality, including compliance with investment decisions and budget execution. The municipal council approves local ordinances and regulations and oversees the work of the mayor, being authorised to call to the attention of the comptroller general any irregularities.

The council is also in charge of ensuring the effective participation of the local community and has an important role in local accountability.

Council of Civil Society Organisations (COSOC)

Law No. 20.500 stipulates that each municipality must have a Council of Civil Society Organisations (*Consejo Comunal de Organizaciones de la Sociedad Civil* – COSOC). They consist of representatives of civil society organisations (neighbourhood associations and functional organisations such as parent-teacher associations and mothers' groups) in order to ensure their participation in municipal activities. They are to consult with citizens on behalf of municipal authorities on matters selected by local officials, and keep civil society organisations (CSOs) and other relevant entities up to date on the operations of the municipality. Each municipality establishes the organisation, composition, competences and functioning, etc., of their COSOC (see Chapter 5).

Municipal delegations

The article 68 of the LOCMUN enables municipalities to create, in their territory, several municipal delegations (*delegaciones municipales*) to deliver certain basic services and ensure better communication in close proximity with populations, especially in sparsely-populated or remote areas (e.g. municipal archipelago). Some large municipalities have also created such delegations to establish closer contact and manage services at the level of their neighbourhoods.

Each municipal delegation comprises a municipal team headed by a delegate, which represents the municipal authority, co-ordinates municipal actions and may formulate development programmes for the community. Delegated tasks can be very diverse according to municipalities, including administrative functions (permits, licenses, civil register, etc.) but also social and legal assistance to the population, environmental protection, employment, sport and recreation, local roads and urbanisation, risk prevention and provision of emergency aid.

It is interesting to note that several OECD countries have similar sub-municipal administrative subdivisions, especially countries with predominately large municipalities (Box 1.12). Such status also appeared following municipal amalgamation policies, in order to mitigate the negative effects of consolidation. In fact, sub-municipal units are often the former municipalities which have been merged. This type of deconcentrated municipal units maintains a certain level of proximity in particular in remote and isolated areas, to better address local needs in terms of services and to overcome issues related to community identity, historical legacies, traditions and local democracy (OECD, 2017a).

Box 1.12. **Sub-municipal delegations: Some international experiences from the OECD**

Even if they depend on the municipalities, sub-municipal entities may have a legal status under public law with a deliberative assembly and a delegated executive body (mayor, council) sometimes elected by the population as well as its own budget and staff. These smaller sub-sectors are generally established at the initiative of the municipality (optional), but their existence can be also embedded in the law in the case of a municipal merger reform. They can have also different names, status and delegated responsibilities according to their "mother-municipality". This network of localities can exist all across the country, even if they do not systematically cover all the national territory (Slovenia, Portugal, United Kingdom, Korea, Ireland, New Zealand, Netherlands, Greece, etc.), or only in metropolitan areas, selected cities or the capital city.

- **In New Zealand,** the 110 community boards created by the 1989 local government reform still operate in both urban and rural areas to carry out functions and exercise powers delegated to them by their councils. The Auckland Council also has 21 local boards, which have elected representatives. They carry out functions and exercise those powers delegated to them by their councils.
- **In Greece,** the Kallikratis municipal amalgamation reform maintained historic communities as deconcentrated entities, providing "some intra-municipal decentralisation" (Council of Europe, 2015). Municipalities with more than 100 000 residents, as well as those of more than 2 000 which consist of former municipalities that have been amalgamated in the context of the 2011 reform, are subdivided into municipal communities (with a population of more than 2 000 inhabitants) or local communities (population up to 2 000 inhabitants). They have elected bodies also in municipal and local communities (a president and a council) which are the administrative bodies.
- **In Ireland,** the 2014 local government reform created a nationally representative system of sub-county governance, the municipal districts. The new district structures have no separate corporate identity but are rather part of the relevant county council, acting as constituencies for county councils, with councillors. Some municipal districts are titled "borough districts" or "metropolitan districts". They enjoy devolved local decision-making responsibilities to decide matters relevant to local communities. In the United Kingdom, there are 9 500 parish councils in England, some 730 community councils in Wales, and some 1 200 in Scotland. They have no statutory powers but receive small amounts of funding or a precept from the council tax collected by the district or county council.
- **In Korea,** municipalities are subdivided into 3 496 sub-municipal localities: 218 *eup* (urban division of the country), 1 195 *myeon* (rural division of the country), and 2 083 *dong* (within autonomous districts and lower-tier cities).
- **In the Netherlands,** there are around 2 200 villages and community councils that are legal entities organised according to public law (sections 83-84 of the Municipalities Act) or according to private law (as an association or foundation). In 2012, 53% of Dutch municipalities had at least one village council or one community council (OECD 2014c).

Box 1.12. **Sub-municipal delegations: Some international experiences from the OECD** *(continued)*

- **In France**, the 1971 Marcellin law created the status of "associated municipalities" which allows the abolished municipalities in a merger process to remain and retain some elements including a delegate mayor, a town hall, an advisory council. This arrangement was reactivated by the 2010 territorial law and the March 2015 law (new municipalities - *communes nouvelles*). This formula has had some success because it introduced greater flexibility for the composition of municipal councils therefore reducing opposition from local representatives. This success is also due to a large extent to financial incentives, allocated to small municipalities deciding to merge.
- **In Portugal,** municipalities are subdivided into civil parishes called *freguesias.* Their number was reduced from 4 259 to 3 091 after the 2012-13 reform. *Freguesias* have an executive body and a deliberative body (the *assembleia de freguesia*, "parish assembly"). The members of the *assembleia* de *freguesia* are publicly elected every four years. The presidents of the parish boards are also members of the municipal assembly.

Source: OECD (2017a), *Multi-level governance reforms: Overview of OECD country experiences*, http://dx.doi.org/10.1787/9789264272866-en, complemented by the authors from various sources.

Municipal responsibilities: Uniformity but complexity

Exclusive and shared responsibilities

According to article 3 of Law No. 18.695, municipalities have many statutory competences, which are uniform across municipalities, regardless of their size or specificities. Given fairly limited financial autonomy and the huge disparities across municipalities in terms of needs and capacity throughout the territory (see Chapters 2 and 3), delivering the same set of public services renders uniform service delivery unrealistic and often impossible (OECD, 2013a).

According to the law, municipal responsibilities are broken down into two categories (Box 1.13): 6 exclusive (*atribuciones esenciales*) and 12 non-exclusive functions which are shared and which can be implemented directly or in conjunction with the central government, the region or the provinces as well as with external public and private organisations (*funciones propias/compartidas*). To that end, municipalities have 11 key assignments (*atribuciones esenciales*).

Exclusive functions are mainly linked to the promotion of local development and planning through the Municipal Development Plan (*Plan Communal de Desarollo* - PLADECO) and the Municipal Regulating Plan for land-use (*Plano Regulador Communal* - PRC).

Non-exclusive (shared) functions with other levels of governments include two major responsibilities – primary and secondary education and public basic health – but they also include areas such as urban and rural road management, employment, environment, social housing, public transport, and social inclusion.

Box 1.13. **Municipal exclusive and non-exclusive functions and fundamental attributions**

Exclusive functions (*funciones privativas*), to be carried out in full compliance with operational laws, directives and technical norms (article 3 of the LOCMUN):

1. Preparing, approving and modifying the municipal development plan (*plan communal de desarollo* – PLADECO) according to legal and statutory standards set by the central government.
2. Preparing, approving and modifying the municipal land-use plan (*plano regulador communal* - PRC) according to legal and statutory standards.
3. Promoting community development (*desarollo comunitario*).
4. Enforcing transit and public transportation measures.
5. Ensuring that construction and urban development meet the standards of the relevant ministry.
6. Cleaning and enhancing public spaces.

Non-exclusive shared functions (*funciones propias/compartidas*), directly carried out or in connection with other bodies of the state administration (article 4 of the LOCMUN). This list of assignments is wider than the list of exclusive functions.

1. Education (primary and secondary) and culture.
2. Public health and environmental protection.
3. Legal and social assistance.
4. Training, promotion of employment and economic development.
5. Tourism, sport and recreation.
6. Urbanisation and urban and rural roads.
7. Construction of social housing and sanitary infrastructures.
8. Public transportation and traffic.
9. Risk prevention and emergency services.
10. Security of citizens (public order and safety) and social prevention actions.
11. Promotion of equity between men and women.
12. Development of activities of common interest at the local level.

The municipal management tools are (article 6):

- The municipal development plan and its programmes (*plan communal de desarollo* – PLADECO).
- The municipal land-use plan (*plano regulador communal* - PRC).
- The annual municipal budget.
- The human resources policy.
- The municipal plan for public security (*plan comunal de seguridad pública - PCSP*).

Box 1.13. **Municipal exclusive and non-exclusive functions and fundamental attributions** *(continued)*

Key assignments

- Implement the PLADECO.
- Execute the municipal budget.
- Manage national good of public use.
- Issue resolutions.
- Establish municipal rights.
- Acquire and dispose municipal assets.
- Grant subsidies.
- Apply local taxes.
- Create cultural corporations.
- Establish neighbourhood units.
- Approve the municipal land-use plan.

Resolutions adopted by municipalities can be of different types (OECD, 2016i):

- Municipal ordinances. These are general and compulsory norms applicable to the whole community. They can set fines for infractions, which are applied by the courts of the local police.
- Municipal regulations. These are general, compulsory, and permanent norms related to the internal order of the municipality.
- Municipal decrees. These are resolutions on specific matters.
- Instructions. These are directives to the subordinates, used for the internal organisation of the municipality.

Source: Organic constitutional municipal law No. 18.695 (Ley No. 18.695, Orgánica Constitucional de Municipalidades), https://www.leychile.cl/Navegar?idNorma=251693; OECD (2016i), *Regulatory Policy in Chile: Government Capacity to Ensure High-Quality Regulation, OECD Reviews of Regulatory Reform*.

Education, health and other "municipal activities"

Besides this legal classification of municipal responsibilities, there is another distinction based on budget accounting. In fact, it appears that education and health are clearly distinguished from the other municipal responsibilities as these two sectors are funded and managed almost independently from the municipal sector itself. For each municipality, there are three distinct budgets (municipal sector, education and health), and even four in several municipalities (cemeteries). Education and health activities are managed by specific administrative departments, directly connected with the line ministries. On top of this, education and health responsibilities can be delegated to municipal corporations adding to the complexity of the municipal system (see below 4.1).

Education and health account for around 49% of municipal expenditure, including 32% for education and 17% for health. While municipal internal management accounts

for around 29% of municipal expenditure, community services (waste collection, public lighting, water, upkeep of public spaces) amounted to around 17%, social programmes and benefits to 3% and recreational and cultural programmes to 1.3% (see Chapter 2).

It is as if there were “three municipalities in one”, although the mayor remains the highest authority. Finally, behind this “uniformity”, there is also great functional and financial heterogeneity of the municipal system, fragmented into almost 960 budget entities and 55 municipal corporations.

In addition, supplementary tasks are regularly given to municipalities by the different ministries in several areas (social inclusion programmes, environment, employment, risk prevention, etc.), which tend to increase their burden but without corresponding adequate human, technical and financial resources. These transfers are often not properly compensated, resulting in increasing structural deficits and “hidden debt” (see Chapter 2).

Today, municipalities are supposed to offer a wide range of services. They have sometimes been identified as a "service supermarket". Bernstein and Inostroza (2009) identified 75 services that municipalities should provide (Box 1.14). Obviously, depending on the characteristics of the municipality, all types of service are not available in all municipalities or are delivered at an unsatisfactory level (see Chapter 4).

Box 1.14. **Areas of intervention of municipalities in Chile: Approach by the organisation of services**

Bernstein and Inostroza identified 75 services that municipalities should provide related to community service, taxes, transport, security, urban development, social development, education and health, among others. This number could increase or change in the future. Direct services are those that the municipal level is exclusively responsible for. Delegated services are those for which a national or regional authority has allocated resources for the administration and provision of services. Obviously, depending on the characteristics of the municipality, all types of services are not available in all municipalities.

Direct services (61)	
Community (9) Driver’s License Waste collection Cemeteries Municipal companies Animal shelters Veterinary services Employment offices (OMIL) Neighbour care Transportation	**Urban (12)** BNUP Permits Building permits Land registry and Certificates Road concessions Lighting Publicity concessions Environmental Hygiene Parks and green areas Streets and sidewalks maintenance Recycling waste management Concessions: Parks and Squares
Taxes (5) Contributions Municipal business licenses Circulation permits Commercial licenses Various licenses	**Social and recreational (11)** Youth Senior Sports Recreational activities Concessions: Beaches and Rivers Casinos Families Tourism Women

Box 1.14. **Areas of intervention of municipalities in Chile: Approach by the organisation of services** *(continued)*

Direct services (61) *(continued)*	
Cultural & Events (6) Cultural activities Events and celebrations Libraries Training Administration of Theatres and Museums Heritage Maintenance	**Finances (4)** Inspection Sales and Leasing Assets Donations Subsidies
Inspection and Security (2) Legal Citizens security	**Various (2)** Courts Consumer
Transit (4) Traffic management Underground Parking Parking meters Traffic lights and signals	**Internet-Digital (2)** Information and Communications Web services
Delegated services (14)	
Delegated services (3) Education Health Minors	**Corporations (3)** Cultural Sport Roadworks
Social Programmes (5) Drugs and Alcohol Housing Social aid Public safety Micro-companies	**Urban-Social (3)** Urban Road Urban-Neighbourhood Improvement Citizens' participation

Source: Bernstein F. and Inostroza J. (2009), Modernización municipal y un sistema de evaluación de su gestión, Propuesta de una arquitectura, PUC.

In the field of social inclusion for example, municipalities are not in charge of paying social benefits from their own budgets but because they are close to beneficiaries, they play a fundamental role in identifying beneficiaries, administering central government funds and administering social welfare programmes on behalf of the central government (Box 1.15). These activities are financed by a myriad of specific subsidies and local development funds (Letelier S. L. 2006), for which it is necessary to apply resulting in agreements of transfers of resources between the participating municipalities and sectoral ministries (*convenios de transferencias de recursos*).

Box 1.15. **Strong involvement of municipalities in social programmes**

One good example of social programmes involving municipalities is Chile Solidario. Chile Solidario is a cash transfer programme targeted at families who live in extreme poverty. There is a special programme for the elderly, the homeless and children with a parent in prison. The purpose of the programme is to improve the quality of life of the most vulnerable families by improving their living conditions. Beneficiaries are granted preferential access to a range of social services, including housing, employment, healthcare, education and childcare. With the support of a social worker Chile Solidario recipients design an action plan, which is supposed to help them exit poverty (OECD, 2012). The programme is executed mainly by the municipalities, technical assistance to projects being funded by FOSIS. The programme was implemented in 325 municipalities, located in the 15 regions (*banco integrado de programas sociales*). The government recently made the decision to increase the cash transfers associated with Chile Solidario significantly with the new transfer system, the *Ingreso Ético Familiar* (the Ethical Family Income). This programme establishes different types of monetary transfers, both conditional and unconditional. The *Ingreso Ético Familiar* programme also transfers some resources to municipalities.

Another example is the "*Chile Crece Contigo*" (Chile Grows with You - ChCC). Launched in 2007, it is a system of protection for early childhood development. It provides a universal and multidimensional approach platform of programmes and services in the areas of education, health (universal health coverage), social and community services, to help children under the age of five and pregnant women who are the most vulnerable. The model is designed by the central government but implemented by municipalities, which have some flexibility to adapt to local conditions with technical and financial support from provincial and national networks. ChCC was initially rolled out in 159 municipalities in 2007, then expanded to all in 2008. Municipalities are strongly involved and are organised into a network. The system also offers technical assistance to municipalities. A programme dedicated to strengthening municipalities has been set up to support the ChCC municipal network co-ordinated by each municipality in its area. In 2015, the programme intersectorial works in 337 municipalities.

The programme *Mujeres Jefas de Hogar* (Women, head of household), in existence since 1992, is carried out by the Ministry of Women and Gender Equality and the Sernameg in co-ordination with 250 municipalities (as of 2016). The objective is to contribute to sustained integration of women, heads of household, into the labour market through regular and remunerated jobs. To do so, the programme seeks to develop capacities, skills and competences that improve conditions of employability, together with the promotion of labour intermediation processes at the local level that are relevant and participatory. The programme offers access to training workshops, where participants can acquire tools for their personal and work development, knowledge about labour rights and receive support to improve their employability. It also offers specific supports for jobs search e.g. help in preparing job profile, CVs, job interviews. It also supports women who wish to create or develop their companies e.g. preparing business or marketing plans, participating in entrepreneurship networks, applying to competitive funds, marketing channels, among others. The programme is implemented by the municipalities which receive applications from women and organise the activities in co-ordination with other networks and actors such as municipal employment offices, SENCE, FOSIS, DIBAM, JUNJI, INTEGRA, among others.

Sources: Chile Solidario/Ingreso Ético Familiar, www.ingresoetico.gob.cl/; Chile Crece Contigo (www.crececontigo.gob.cl/), Programme Mujeres Jefas de Hogar (www.minmujeryeg.gob.cl/prensa-sernameg-destacados/postulaciones-jefas-de-hogar-17); OECD (2012) OECD Economic Surveys: Chile 2012.

The provision of public employment services is also a shared responsibility between central government and municipalities. The main channels for service delivery are the municipal employment offices (*Oficinas Municipales de Información Laboral* - OMILs) and the online national jobs portal (*Bolsa Nacional de Empleo* - BNE). OMILs offer a range of employment services for both jobseekers and employers, including access to employability support programmes offering mainly job training. They are run by the municipal authorities, but are supervised by National Employment and Training Service (SENCE, part of the Ministry of Labour and Social Protection) which technically and financially support them. The number of OMILs increased from 167 in 2009 to 326 OMILs in 2015 covering 94% of the country (ILO, 2015). Despite the OMIL strengthening programme aimed at hiring staff or buying equipment (*Programa de Fortalecimiento OMIL, FOMIL*) and the substantial increase in earmarked funds targeted at municipalities, most of OMILs are under-developed and lack the administrative capacity to monitor job search efforts, deliver appropriate job search services, like basic job counselling and placement for the unemployed (OECD, 2015b). A study on the government's reinforcement programme for labour offices suggests that some small and rural offices lack basic equipment to the point that they used the placement incentive pay they received from the Ministry of Labour to acquire basic material (ClioDinamica, 2010). According to household survey data, only a negligible percentage of employees (slightly above 1%) feel that an OMIL has helped them find a job. It has been suggested to integrate the local employment offices into a nationwide network under the responsibility of the national employment agency (OECD, 2012; 2013c).

In some areas, there are growing concerns about the opportunity to continue this system of shared responsibility between the central government and the municipalities.

Today, intense debate has surrounded the future of primary and secondary education and basic health services. In the education sector, an important reform is currently on-going which would result in the de-municipalisation of the management and funding of schools (see below and Box 1.16).

Focus on primary and secondary education

One of the main competences devolved to municipalities in Chile since 1980 has been public primary and secondary education. This responsibility was transferred from the central government by the Law No. 1.3063 of 1980, consolidated by the Education Organic Constitutional Act of 1990 No. 18.962 and revised in 2009 by the General Education Law No. 20.370 (*Ley Orgánica Constitucional de Enseñanza*, LOCE).

The law transferred the management of public schools, teachers and administrative staff to the municipalities. The financing system was also modified: instead of transferring resources according to a historical criterion of expenditure, it was changed to a nationwide voucher system, implemented in 1982. In the private sector, there are two kinds of establishments: subsidised and non-subsidised. As of 2015, among 3.5 millions of pupils, about 55% were registered in private subsidised schools, 36% in the municipal schools and 8% in the private fee-based institutions. Almost 45% of teachers and 45% of schools (MINEDUC, 2016) were part of the municipal sector (municipalities and corporations).

In terms of organisation, the management of public schools is carried out either through Municipal Education Administration Departments (DAEM) or through corporations, which are municipally controlled non-profit organisations. About 80% of municipalities have established DAEMs (OECD, 2013b). Municipal education authorities

are responsible for the operation and financial management of public schools and the management of administrative personnel and teachers, including their appointment, dismissal and professional development of teachers. They also manage relations with the education community and the general public. Each municipality has to prepare an Annual Development Plan of Municipal Education (*Plan Anual de Desarrollo Educativo Municipal* - PADEM).

DAEM and corporations are supervised by the Ministry of education which is responsible for the design, implementation and co-ordination of education policies, standards and regulations. Regional and provincial education authorities (SEREMIs and DEPROVs) function as deconcentrated supervision structures for the central Ministry of Education.

Recurrent issues negotiated with the Ministry of Education concern the levels of public subsidies for municipal schools and teacher working conditions and salaries (with municipalities claiming, as their employers, a greater say in the definition of teacher working conditions and salaries).

A fierce debate has centred on the liberal nature of the education sector and the need to fundamentally reform education with a view to creating better opportunities for the less well-off families and making schools more inclusive, reshaping teachers' careers and increasing the quality of education. In fact, Chile still has considerable progress to make in improving educational outcomes and equity (Box 1.16).

In relation to these concerns, the discussion has also touched on how to reform the governance of education to reduce inequalities and increase the quality of education. It has even been suggested to strip municipalities of their management and administration duties for public schools. Municipalities are not equally well-equipped to run schools. Some of the wealthier municipalities have large and well-trained staff dedicated to the technical-pedagogical support of schools, while others can barely afford one employee (OECD, 2011). Education expenditure can be a real burden on municipalities, absorbing, with health expenditure, most of financial capacities (see Chapter 2). Several bills have been sent to Parliament since 2008 that have proposed alternatives to the municipal management of public schools.

In particular, under a reform of the administration of public education proposed as of late 2015, the 345 municipalities would no longer run public schools and a new system of public education would be created in a process called New Public Education. The draft law would create a National Directorate for Public Education within the Ministry of Education (*Dirección Nacional de Educación Pública*) to co-ordinate about 70 new local education services (*servicios locales de educación*), the new providers of public education. Each local education service would oversee a group of schools with powers transferred from the 345 municipalities. Prior to this reform, a number of different options for reforming the municipal school system were envisioned including de-municipalisation, creation of inter-municipal educational authorities and regionalisation of education. A central concern of the reform is to ensure adequate mechanisms to deliver quality education for all students throughout the country, while monitoring the effective, efficient and equitable use of resources at subnational levels (Santiago, et al., forthcoming).

The education reform is still under discussion while it brings some uncertainty, in particular at the municipal level. Some questions raised by the de-municipalisation of education remain e.g. the transfer of municipal assets (schools), liabilities (debt),

municipal staff in charge of education or the future of municipal corporations in charge of education services. It also raises further concerns regarding the size of national bureaucracy at the subnational level, if SEREMIs and DEPROVs are to continue operating side-by-side with the new local education services (Santiago et al., forthcoming; and OECD forthcoming). Another area of concern is linked to the future role of the regions which are fully self-governing with the introduction of the 2017 January law and which should be allocated new responsibilities in the coming months.

Box 1.16. **Principles of organisation and financing of the education sector through the voucher system**

The reform introduced in 1980 by the military government ushered in a radical, neo-liberal conception of the functioning and the management of the economy and the society (El Ladrillo, 1992; Reyes Cayul, 2013; Delooz, 2015). The military government introduced a radical change in education by promoting a dualist system based on the co-existence of public and private establishments and introducing competitive pressure between both sectors. Although this combination of private and public operators is widely practiced in many countries, the market-oriented reforms and the role of the private sector are particularly present in Chile.

Municipalisation, privatisation and voucher/free market

Municipalisation, privatisation and voucher/free market are the three key words of the change brought about during the 1980s to build a competitive education system meant to increase educative performances. The decentralisation of public school management responsibilities to municipalities was accompanied by the introduction of a nationwide voucher programme for both municipal and private schools, based on the principle of the parents' free choice of schools. The voucher mechanism finances the cost of a child's education by helping the user (parents) directly instead of subsidising the academic institution. The user can buy the service of the delivery institution that he prefers. The Chilean formula is a derivative version of the generic principle. Families do not receive the voucher, which is paid instead to the establishment where the pupil is enrolled. If the pupil moves to a new school, the voucher is paid to the new establishment. In the Chilean system, the voucher is equivalent to a subsidy called a scholar subvention (*subvención escolar*). Nevertheless, it is an unstable earmarked subsidy: users "threaten" the schools with the possibility they will "vote with their feet". The subsidised private establishments have developed a complementary funding method: the co-payment (*copago*) since the passing of law no. 19.247 of September 1993, which allowed the extra fees to be paid by the families.

Among OECD countries, Chile has the highest share of private financing for primary and secondary education. In other words, Chile is the only OECD country where the share of public funds in overall expenditure on schooling was below 80% in 2013.

Critical points and current reforms

This new system introduced local competition between the three different categories of establishments: public municipal schools (also divided into municipal and corporations), subsidised private establishments and private non-subsided establishments. The introduction of the voucher programme has led many private schools to enter the market, attracting a growing share of the student population. As a result, enrolment in municipal schools has declined substantially.

The voucher system has been a source of controversy, sharp criticism, and protests (for example "the penguins' revolution" in June 2006). Where students attend school depends largely on the income level of their family. Students from the most disadvantaged families attend municipal schools in droves. Private subsidised schools educate students from a wider range of backgrounds (OECD, 2013b).

Box 1.16. **Principles of organisation and financing of the education sector through the voucher system** *(continued)*

There is evidence that it has resulted in "cream skimming", with private subsidised schools selecting academically gifted students and those with middle and high economic status, while excluding pupils with learning difficulties or from disadvantaged socio-economic backgrounds (ODI, 2014; Bellei, 2009).

Chile continues to struggle with inequalities as the system did not lead to reduce social and territorial inequalities which remain huge, causing significant tensions and threatening social cohesion. Therefore, according to the 2015 results of the OECD Programme for International Student Assessment (PISA), which compares the academic performance of 15-year-olds across the globe, Chile's index of social inclusion was one of the lowest among PISA-participating countries and economies, Chile ranking 65 out of 68 (OECD, 2016c). There is also a territorial bias of this segregated school system, as 81% of schools in rural areas are run by municipalities. In areas where there are fewer than 100-150 pupils, there is no enrolment into private-subsidised schools. This concentrates the benefits of the voucher system in urban areas, with a negative impact on urban–rural equity (ODI, 2014). In addition, Chile ranks among the last concerning the quality of schools' educational resources (-0.32 PISA Index, rank 61/69). Teachers in Chile face comparatively low salaries and high workloads. Their statutory working time is around 30% more than the OECD average, and the student-teacher ratio in Chile is the second highest among OECD countries (OECD, 2016d). However, a new law regarding teachers' career was enacted in April 2016: it increases teachers' salaries (since July 2017 for the entire municipal sector) and gradually decreases the percentage of teaching hours (*Sistema Profesional Docente*, Law No. 20.903 or System for Teacher Professional Development). Its gradual application starts in 2016 and full application is expected by 2026.

Finally, despite significant improvements in the quality of basic education in Chile in recent decades (improved performance in reading and sciences according to PISA and Chilean education quality measurement system, SIMCE, better education access), Chile continues to lag behind the OECD average in terms of student performance in mathematics, reading and science. The 2015 PISA survey found that Chile ranked 42 out of 73 countries in reading, 50 out of 73 in mathematics and 45 out of 73 in overall sciences.

Faced with growing criticism, the system is on the cusp of being profoundly reformed. The Chilean government proposed a substantial change in the funding of the education system in 2014. A new law, adopted in 2015 (Law No. 20-845, *Ley de Inclusión Escolar* or Inclusion Law) aims to keep education free-of-charge and inclusive. According to this law, subsidised private establishments will not be able to receive public allocations and make profit. The copago should progressively disappear, the increase of the ministerial grants offsetting the revenue. Similarly, in schools receiving public funding, the reform aims to gradually end student selection, and forbids expelling students due to academic, political, ideological or other reasons. Some student selection will be allowed in special programmes (up to 30%), such as arts, sports or academic excellence. The reform has been effective since March 2016 and implementation is foreseen to continue until 2020. Its efficiency will depend, in particular, on the budgetary effort to maintain the increase of the scholar subsidy and the bonus for priority (socially-underprivileged) pupils.

Another important reform is currently on-going, which would result in the de-municipalisation of the management and funding of schools. This would have a major impact on municipal finance, both in terms of expenditure and revenue.

Sources: OECD (2016c), *PISA 2015, Results in focus*; OECD (2016d), *Education at a Glance 2016: OECD Indicators;* Santiago et al. (forthcoming), *OECD Reviews of School Resources: Chile*; Bellei (2009) "The Public–Private Controversy in Chile"; Delooz B. (2015), Le pouvoir territorial au Chili et en France. Eléments d'analyse critique de la décentralisation en droit comparé; El Ladrillo (1992), Bases de la política económica del Gobierno militar chileno; Reyes Cayul I.E. (2013), *La privatisation du système éducatif chilien depuis 1973 à nos jours*; ODI (2014), Improvements in the quality of basic education - Chile's experience, Overseas Development Institute; Santiago, P. et.al. (2013), Teacher Evaluation in Chile 2013, OECD Reviews of Evaluation and Assessment in Education.

Focus on primary healthcare

The health sector underwent its first reforms in the late 1970s with the Decree Law No. 2.763, adopted at the end of 1979 and revised several times in 2000 and 2004 (laws No. 18.933 and No. 18.469) as well as through the Law on Health Authority (*Ley de Autoridad Sanitaria* No. 19.937) and the Law on Explicit Heath Guarantees System Act (*Garantías Explícitas de Salud*, G.E.S n° 19.966). The reform separated the functions of planning, control and regulation with the tasks of provision of health services and set up a mix public-private system. New entities were created including the National System of Health Services (SNSS), the National Health Fund (FONASA), the Public Health Institute, the Procurement Centre, etc.

In 1981, the SNSS transferred all responsibility for primary healthcare to municipalities (urban and rural clinics and health centres), leaving only secondary and tertiary care in hospitals and specialised health centres (Raczynski and Serrano, 2001).

Today, Chile's healthcare system is a combination of private and public insurance coverage (Box 1.17). Public coverage accounted for 75.5% of Chileans in 2010. The National System of Health Services covers the entire country, composed of 29 autonomous Health Services, co-ordinated by the Ministry of Health's Undersecretary of Healthcare Networks. Each health service (*servicio de salud*) co-ordinates a territorial network of primary care centres, mainly administered by municipal governments and corporations, to deliver comprehensive family and community healthcare to FONASA affiliates residing in its area.

As in the education sector, municipalities can choose between direct administration of health through municipal departments of health or indirect administration through private corporations. In 2015, there were 271 municipal departments or municipal health directorates, and 50 health corporations. 65% of the municipal health directorates were located in the poorest municipalities. In 2015, the municipal health system comprised an infrastructure of 1 477 entities, including 113 health laboratories, 62 urban clinics (*Consultorios General Urbanos* (CGU), 65 rural clinics (*Consultorios General Rural* – CGR) and 1 075 rural health centres. In addition, there were 162 other types of municipal health facilities, such as Family Health Centres (*Centros de Salud Familiar* - CESFAM) or Primary Urgent Care Services (*Servicios de Atención Primaria de Urgencia* - SAPU), located throughout the country (AMUCH, 2015). Municipalities have to prepare an annual Municipal Health Plan (*Plan Anual de Salud Municipal o Plan de Salud Comunal*).

The new health system combines municipal and private healthcare centres with different payment methods, from free-of-charge to free-pricing. Municipalities receive every month a current transfer from the Ministry of Health aimed at financing municipal clinics and health centres.

According to international rankings, the Chilean health system has a respectable level. However, social and territorial inequalities put a damper on this performance. Among the main issues raised are the risk of anti-selection (linked with the limitative list of diseases of the AUGE) and the municipal differences of territorial capacities (resources, equipment, medical density).

Box 1.17. **Municipalities and the Chilean health system**

Two sub-systems, one public and the other private, coexist within the Chilean health system. The National Health Fund of Health (*Fondo Nacional de Salud* - FONASA), created in 1979, is in charge of ensuring healthcare coverage of the beneficiaries of the public system, i.e. about 75.2% of the Chilean population in 2014, including the rural and urban poor, the lower middle-class, the retired, and the self-employed and technicians. The delivery is ensured by the National Health Services System (*Sistema Nacional de Servicios de Salud* - SNSS) and the Municipal System for Primary Care. Part of the population is also covered by other public agencies (the Health Services for the Armed Forces). The private system is based on Health Provision Institutions (*Instituciones de Salud Previsionales* - ISAPREs) created in 1981. It covers approximately 18.5% of the population, mostly the upper-middle class and the high-income population. A small proportion of the population uses private health services and pays for them out-of-pocket. Overall, in nearly all OECD countries, the main source of health funding is the public sector, with the exception of Chile and the United States. In Chile, 49.2% of health spending is funded by public sources, which is far below the average of 72.3% in OECD countries (Ramírez-Valdivia et al., 2014).

The decentralisation in 1981 of primary health to the municipalities led to the creation of Health Consultation Centres (*Consultorios de Atención primaria* - EPS). The 2003 and 2004 reforms sought to improve equity and efficiency of the public system.

The system is based on two operational supports:

- The special plan for Universal Access to Explicit Guarantees or "AUGE" Plan (*Acceso Universal de Garantías Explícitas*) aimed to improve public service quality by selecting diseases for which several guarantees would be made to insured patients in the public system (56 health problems have been identified, including cancer in children, breast cancer, ischaemic heart disease, HIV/AIDS and diabetes).
- The beneficiaries must contribute to the financing of services. The financial participation follows a scale modulated according to the revenue (four classes with co-payment rates varying from 0 to a maximum of 20%).

Sources: OECD (2003), *OECD Economic Surveys: Chile 2003*; OECD (2007a), *OECD Economic Surveys: Chile 2007*; Becerril-Montekio V., J. de Dios Reyes and A. Manuel (2011), "Sistema de salud de Chile, Sistema de salud de Chile", [The health system of Chile]; Benavides S.P., L. Rubén Castro and J. Ingrid Jones (2013), *Sistema Público de Salud, Situación actual y proyecciones fiscales*, DIPRES; Ramírez-Valdivia et al. (2014), *Measuring the Efficiency of Chilean Primary Healthcare Centres*.

Towards asymmetric organisation and competences?

Restricting shared competences, increasing exclusive responsibilities

As underlined above, the breakdown of responsibilities across levels of government remains unclear. At the municipal level, the current system of responsibilities is quite complex with few exclusive competences and 13 shared competences whose dividing lines between central or municipal interventions are not well established and subject to change. Additional tasks are regularly attributed to municipalities without financial or technical compensation. Shared responsibilities, especially education and health, are a significant burden on municipal budgets (see Chapter 2). Until the recent law on municipal staff adopted in 2016, municipalities did not have the possibility to adapt their human resources, quantitatively or qualitatively, to these new functions (see Chapter 4). Today, the Chilean government has considered a number of different options for reforming the municipal school system and this is still under discussion (see above).

The regionalisation agenda aims to transfer new responsibilities from the central government to the regions, which would have a total of 111 responsibilities by 2022. Regional governments currently have 23 responsibilities defined by the LOCGAR. The bill under consideration plans to transfer 49 new competencies. The remaining 39 would be "competencies by occupation - *competencias por oficio* – see also Chapter 6. If adopted, this will have a profound impact on both central government and municipalities. Some regional competences could give them a co-ordination function over certain municipal activities. The current proposal concerning regional governance of metropolitan areas goes in that direction. The current regionalisation programme will clarify the complex distribution of responsibilities across levels of government and reshuffle municipal competences.

At this stage, two approaches could be considered:

- Examining the possibility of increasing the number of exclusive competences and reduce the number of shared ones. A work group could be set up grouping all ministries and SEREMIs involved in municipal affairs, regional governments and representatives of municipalities to examine more precisely the list of responsibilities that could be carried out exclusively by municipalities (these should involve local economic and social development). Another option would be to apply the general clause of competence or "subsidiarity principle" as it is the case in a majority of OECD countries as far as the municipal level is concerned.
- Keeping some shared responsibilities but reconsidering the scope, i.e. the functions carried out by municipalities within the area. This should take place in the framework of the current discussions underway in Chile with respect to the regionalisation process (i.e. new regional responsibilities) as well as to sectoral reforms.

In particular, it should take into consideration the current educational reform, which intends to remove from municipality remit the administration and management of public schools and to create a system of public education, based on new providers of public education (local education services) co-ordinated by the National Directorate for Public Education (see above and Santiago et al., forthcoming). In this area, there is a need for a more co-ordinated and integrated approach between both municipal and education reforms. In particular, it seems necessary to better assess the various impacts of the New Public Education Reform on the municipal sector (municipal finances, staff, assets and liabilities, etc.). A flexible approach of the de-municipalisation process of education could also be considered in order to allow those municipalities that are willing and capable to retain their status as school administrators (see below).

OECD countries have envisioned other avenues of work, in particular to reduce the cost of education services for subnational governments, which can be a real burden for municipalities when they include both current (in particular, the payment of teachers' salaries) and investment expenditure. Some current charges can re-transferred to higher levels of government while investment functions and associated costs (maintenance and repairs) as well as some operating expenditure (energy, extra-curricular activities, administrative services, canteens, pupils transport, non-teaching personnel, etc.) can be maintained at the municipal level. This is the case in France. In Austria, such a dividing line is seen between the central government and state governments at the regional level (Box 1.18).

Box 1.18. **How to assign education responsibilities across levels of government? The cases of France and Austria**

Education is the most common major public service to be shared substantively across multiple tiers of government. It is the single largest budget item for subnational governments in most countries. On average across OECD countries, education accounted for 25% of total subnational expenditure in 2014, amounting to almost 50% of total public education expenditure (OECD, 2016b).

It can be observed that in most OECD countries, lower levels of government are responsible for managing and funding lower levels of schooling (mainly pre-elementary, primary and sometimes lower-secondary education) whereas responsibility for secondary, and in particular upper-secondary, schooling is more often retained at provincial/regional or central levels. These functions are sometimes carried out on behalf of central government, with more or less discretion. This type of arrangement where sub-sectors of schooling operate under different political and administrative jurisdictions may raise significant challenges concerning efficient use of resources (risks of competition, duplication and overlaps) and co-ordination of policies and actors. It generally involves clearly defining the division of labour between different levels of government and putting in place appropriate co-ordination mechanisms and collaborative practices under the general umbrella of the Ministry of Education (OECD, 2016c).

There are different manners of sharing responsibilities, which are not exclusive, based on the level of education, on the functions or on the financing. The latter is, among others, the way chosen by France and it is envisioned in Austria.

In France, the educational system was historically very centralised. Decentralisation reforms in 1982-1983 and 2003-2004 resulted in a mixed system. The degree of direct management and control from the Ministry of Education has diminished considerably. However, the central government retains responsibility for the national curriculum and general educational goals, recruitment, training, management and remuneration of teachers (schools and university), while subnational governments are in charge of investment and maintenance responsibilities for the pre-elementary and primary schools (municipalities), the *collège*s (departments), and the high schools or *lycées* (regions). Since 2004, subnational governments are also responsible for recruitment, management and payment of technical and administrative staff. They are also responsible for school transport, meals and extra-curricular activities. Subnational governments nevertheless receive transfers from central government intended to cover the bulk of their education expenditures to cover operational expenses (other than teaching staff), equipment and building infrastructure (OECD, 2006; OECD, 2007). In 2014, subnational education expenditure accounted for around 14% of total subnational expenditure, representing 31% of total public education expenditure.

In Austria, the educational system was also strongly centralised for historical and political reasons. According to the general clause of article 15 (1) of the Constitution, education is one of the exclusive competencies that are assigned to the federal government with public security, taxes, civil and penal law, industrial affairs and heath care. However, the regional states (*Bundesländer*) have the constitutionally guaranteed right to execute some federal laws, especially in the area of education. This has led to a complex distribution of responsibilities between the federal government and the states. For example, lower-secondary schooling is currently offered by both the federal level (first stage of academic secondary schools) and the provincial level (within so-called New Secondary Schools). Education policy is a controversial topic with intense debates. A reform is currently under discussion in order to clarify the division of responsibilities between the federal government and the *Bundesländer* seeking ways to streamline the governance and funding of the Austrian school system.

Box 1.18. **How to assign education responsibilities across levels of government? The cases of France and Austria** *(continued)*

There are different options but one appears to be a feasible compromise which would consist in putting *Bundesländer* in charge of all investments and maintenance and leaving the federal government in charge of the funding and allocation of teachers through new education directorates based in each province (OECD, 2016c). In Austria, subnational education expenditure accounted for around 17% of total subnational expenditure i.e. 46% of total public education expenditure.

Sources: OECD (2016b), *OECD Regions at a Glance 2016*; OECD (2016c), *PISA 2015: Results in focus*, www.oecd.org/pisa/pisa-2015-results-in-focus.pdf; OECD (2016e); First Draft of the Thematic Comparative Report on the Funding of School Education Group of National Experts on School Resources OECD Review of Policies to Improve the Effectiveness of Resource Use in Schools; Nusche D et al. (2016), OECD Reviews of School Resources: Austria 2016; OECD (2007b), *OECD Economic Surveys: France 2007*; OECD (2006), *OECD Territorial Reviews: France 2006*.

Modifying governance arrangements and breakdown of responsibilities and functions could also be envisioned in other sectors, such as health or social policies.

In the OECD, subnational health expenditure is the second highest budget item, accounting for 17% of subnational expenditure on average, and even more than 23% in the United States, Spain, Austria, Denmark, Sweden, Finland, reaching 47% in Italy. Subnational expenditure represented 25% of total public health spending on unweighted average in the OECD in 2013. This share is less than 2% in several OECD countries where health remains a centralised responsibility, such as Greece, Ireland, Israel, Luxembourg, the Slovak Republic, France or the United Kingdom. In these countries, health competences fall more often under the responsibility of central government or social security bodies and subnational governments have no role, or a limited one. At the other end of the spectrum, this share exceeds 60% in Italy, Spain, Switzerland and the Nordic countries (Norway, Finland, Denmark and Sweden). In these countries, wide responsibilities for planning, organising, delivering and financing healthcare services and infrastructures are decentralised to the municipal level (primary care centres) but especially to the regional level (hospitals, specialised medical services). There is a trend of shifting responsibility from the local to the regional level in order to ensure more equitable access and efficiency to health services. It was the case in Denmark with the 2007 reform: while municipalities gained responsibilities for social welfare and education, making them responsible for most citizen-related tasks, the five new regions (resulting from the merger of previous 14 counties) were granted responsibilities for healthcare services, including hospital services. In Belgium, communities and regions gained additional competencies in the framework of the 6th State reform of October 2011. In particular, the reform transferred in 2014 further competencies in health, including hospital infrastructures, mental health services and preventive medicine. The case of Finland is interesting, as a new reform is currently discussed consisting in transferring municipal health responsibilities to future self-governing regions (Box 1.19).

Box 1.19. **Transferring health responsibilities from municipalities to self-governing regions: The current Finnish reform**

In 1993, a reform decentralised healthcare to the municipalities. Health expenditure became a significant item of local spending (29% in 2014), 61% of public health spending being carried out by municipalities and joint municipal boards. These inter-municipal co-operation entities can operate on a local basis – e.g. healthcare centres – or on a regional scale – e.g. specialised districts and university hospitals (OECD, 2014b). In recent years, there have been growing concerns concerning the capacity of municipalities to manage health services due to high waiting lists, diseconomies of scale, shortages of health personnel in certain areas and growing inequalities in terms of access and quality of services. In 2005 and 2007, a reform, called PARAS (Programme for Restructuring Local Government and Services) sought to improve health management by promoting voluntary municipal mergers and inter-municipal co-operation. It introduced quantitative population thresholds to be reached for a number of activities including primary healthcare (20 000 inhabitants). Progress was slow however. In addition, although municipal co-operation solved many scale and externality problems, it was insufficient to meet the challenges associated with population ageing, eroding tax bases in many municipalities (Moisio A. et al., 2010) and the difficulty to provide healthcare services according to national standards in certain areas due to increased fixed costs related to increasing specialisation and technological developments. Co-operation was also criticised for a lack of transparency and accountability in decision making (OECD, 2014b).

The PARAS reform was rapidly followed by other plans for municipal amalgamations in 2011 and 2013. Once again, this new reform also met strong resistance and finally, the new Finnish government, which took office in May 2015, decided to end the process and adopt an alternative strategy, based on regionalisation.

The new regional reform is to be based on the creation of elected self-governing regions, which would receive primary and specialised healthcare as well as social services transferred from municipalities. There should be 18 new regional governments, with 15 regions being responsible for their own social and healthcare services (the last three would organise services in co-operation with other regions). The aim is to reach similar objectives as those of municipal mergers, i.e. reaching greater efficiency for public services through up-sizing; reducing costs so as to bridge the EUR 3 billion sustainability gap; and reducing inequalities in service provision across the country. The financing system should also be revised and simplified (the aim is to introduce a single-channel funding system, in contrast to the multi-channel current system).

This reform is part of a larger package of reforms, built around five priority areas: employment and competitiveness; knowledge and education; well-being and health; bio-economy and "clean" solutions; and digitalisation, experiments and deregulation. Reforms include the pension reform, the social welfare and healthcare reform (aimed at cutting municipalities' costs by reducing duties and obligations), the 'Municipality of the future' project (aimed at increasing municipal authority in areas such as promoting vitality, entrepreneurship and employment, as well as encouraging municipal mergers), and regional and central government reforms (simplification of regional and central administration).

Source: OECD (2017a), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, OECD (2014b), *OECD Economic Surveys: Finland 2014*; Moisio A. et al. (2010), *Public services at the local level: The Finnish way.*

There is no one model for assigning responsibilities across levels of government. However, a general scheme for breaking down responsibilities across subnational governments, based on the observation of OECD country experiences could be enlightening for Chile (Box 1.20):

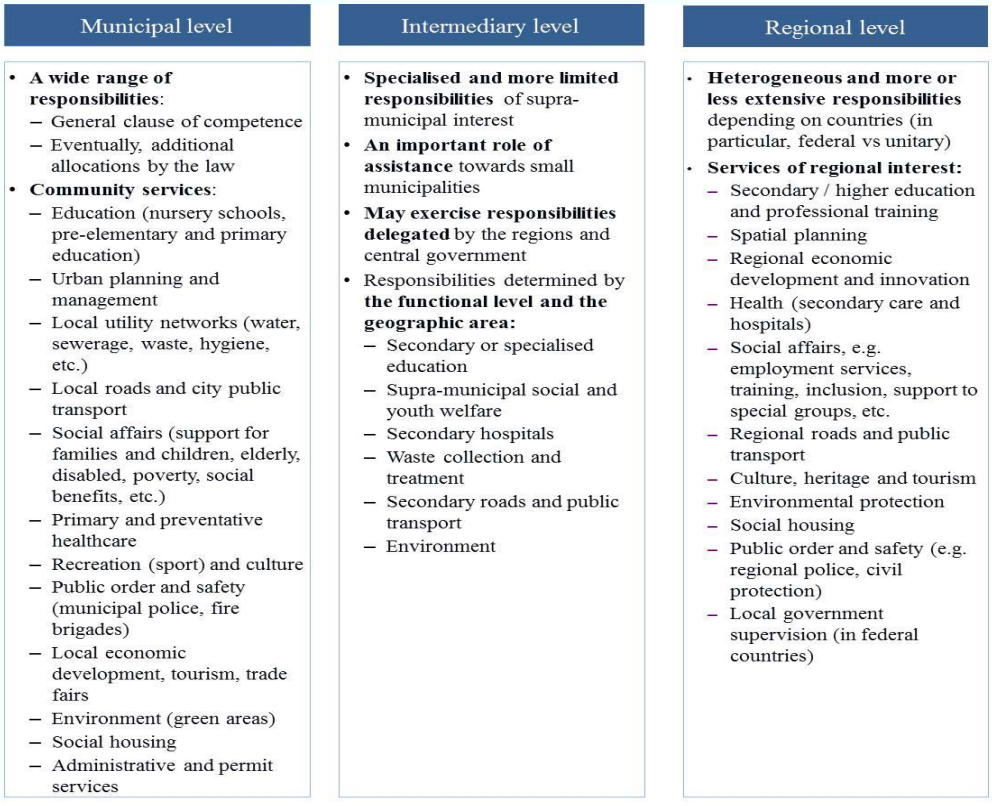
- In many OECD countries, the municipal level tends to manage community services. Municipal responsibilities are not always defined precisely as regulations often refer to the general clause of competence or "subsidiarity principle". This principle gives local authorities an explicit freedom to act in the best interests at the local level. In this case, laws rarely limit or specify local responsibilities but enumerate broad functions instead, except if a particular responsibility is devolved by law to another government level (OECD 2016b).
- In two-tier systems of subnational governments, the regional level between the municipalities and the central government, because it operates on a larger scale, usually provide services of regional interest which benefit from economies of scale, generate spillovers, involve redistribution and are required to meet the same standards across the jurisdiction (OECD, 2014a). The regional tier may also facilitate co-operation and strategic planning.
- In a three-tier systems, like in France, Spain, Italy or Poland, the breakdown can be complex, sometimes resulting in duplication, overlap and co-ordination challenges. However, over recent decades, the intermediate level has lost many of its powers and responsibilities in favour of regions, which gained more importance. In a majority of countries (except France for example), intermediary governments are now mainly responsible for administrative and delegated tasks, and have small budgets and in general no, or only limited, taxing powers.

Box 1.20. **Breakdown of responsibilities and functions across subnational government levels**

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

Box 1.20. **Breakdown of responsibilities and functions across subnational government levels** *(continued)*

Figure 1.17. **Breakdown of responsibilities across subnational government levels: A general scheme**



Source: OECD (2016b), *Regions at a Glance 2016*.

Towards more flexibility and differentiated responsibilities

Additional approaches might be explored to address in particular the diversity and heterogeneity of Chilean municipalities, in terms of unequal capacities but also in terms of needs, which may vary depending on their location or social and economic characteristics. They include:

- Creating incentives to promote the use of municipal associations for horizontal co-operation in service delivery and co-ordinated investment (see Chapter 6).
- Creating the possibility to delegate some tasks to a higher level of government through ad hoc agreements for a given period (regions). Such arrangements are developing in the OECD (e.g. in France since the law MAPTAM law of 2014 on the modernisation of territorial public action and affirmation of metropolitan areas).
- Improving the recognition and functioning of the municipal delegations that carry out municipal functions at the community level, especially in isolated areas. SUBDERE could launch a study to identify how many entities exist today in Chile, what types of tasks they perform, how they function in terms of human and financial resources as well

as to assess their efficiency in terms of proximity with the population and services delivery.

- Ascribing differentiated competences according to different categories of municipalities. Large, capable municipalities would have higher budget responsibilities compared to smaller ones.

This last topic of asymmetric decentralisation has received growing attention from several countries confronted with severe disparities in local capacities and/or various territorial, political or international cultural contexts. Asymmetric decentralisation can be an interesting way forward to improve and strengthen decentralisation, as it is currently experienced by Colombia and increasingly adopted for various reasons in France, Italy, Spain, Sweden and the United Kingdom (Box 1.21).

There are different ways to implement asymmetric decentralisation. It can be done by granting a special political status to only some regions or municipalities, assigning differentiated powers and responsibilities, defining dissimilar financing arrangements (in terms of taxing or borrowing power for example), allowing to enter into specific partnerships or agreements (e.g. public-private partnerships, concession agreements) or imposing different norms or requirements (e.g. accounting, reporting, audit, public procurement, etc.). In that perspective, it is necessary to clearly define, in a transparent and shared manner with interested stakeholders the criteria used to differentiate and categorise subnational governments.

However, asymmetric governance approaches contain risks, in terms of creating institutional complexity, such as in Czech Republic (Box 1.21) and preference treatments. This could lead to the creation of a "multi-speed municipal system", with favoured and less favoured municipalities, which would merely recreate significant "legal" inequalities. Therefore, an asymmetric approach should be accompanied by specific support for municipalities, which would remain under the common institutional framework and could feel marginalised.

Box 1.21. **Asymmetric decentralisation: Defining differentiated competences for different municipalities: the case of Colombia, Denmark and Czech Republic**

In Colombia, capacities vary greatly across jurisdictions. This represents an important obstacle for efficient decentralised governance and for when a government envisions decentralising new functions to the lower levels. To address this challenge, Colombia has set up a system of certification of municipalities, entailing differentiated competencies. To perform central government delegated functions in the areas of education, health, water and sanitation, municipalities must be certified. In the uncertified municipalities, the department is responsible for these competences.

Colombia is currently considering a new reform to differentiate competencies according to the degree of capacities. The new "Differentiated Competences National Programme" included in the 2014-2018 National Development Plan goes further to respond to the disparities among the capacities of subnational governments by providing the possibility of allocating more responsibilities to the more qualified ones. It also envisions alleviating some administrative requirements (e.g. reporting) as today, small municipalities have roughly the same obligations as the large ones, which can be a real burden for them.

The National Planning Department (DNP) has defined general and specific criteria linked to financial, technical and institutional capacities of Colombian municipalities. General criteria assess the institutional capacities of local actors independently of the competence to be delegated (including the provision of basic services, generation of own resources, accomplishing goals of development planning, appropriate use of financial resources, financial solvency and respect of fiscal procedures).

Box 1.21. **Asymmetric decentralisation: Defining differentiated competences for different municipalities: the case of Colombia, Denmark and Czech Republic** *(continued)*

A total of 492 municipalities out of 1 101 have recorded good results, while 215 scored in the lowest category. For a competence to be devolved, the municipality needs to comply at the same time with specific criteria defined by the national authority that will delegate the competence. Following these two steps of multi-criteria analysis, the DNP identified 131 municipalities that could assume functions currently delivered by the central level.

Sectors that could be more efficiently managed at the municipal level were identified. These include protection and reinsertion of victims, transport (tertiary roads), early childhood, and agricultural and rural development. The priorities will be to delegate competencies for victims' rights, land registries and transport (tertiary roads).

The municipality has to ask for the delegation of a specific competence. The transfer depends largely on the political will of the local government in taking on additional responsibilities, as devolution is not encouraged by any financial incentive beyond the transfer of the corresponding budget to the municipality. The request is then analysed by the sectoral ministry involved, which may be resistant to give up part of its prerogatives. The first delegation underway is the multi-purpose land registry in the municipality of Barranquilla.

In Denmark, between 2012 and 2015, nine local municipalities were granted exemptions from government rules and documentation requirements in order to test new ways of carrying out their tasks, in a policy experiment known as the "Free Municipality" initiative. The main focus has been on simplification, innovation, quality and a more inclusive approach to the individual citizen, with many of the experiments focusing on employment. The Free Municipality experiment is currently being evaluated, in order to form the basis for potential future legislation on de-bureaucratisation for all municipalities. The concept of Free Municipalities continues in an adjusted form until 2019, and is extended to more municipalities.

In the Czech Republic, in the process of decentralisation, the responsibilities of the 76 abolished state "districts" to the municipalities were largely passed on to 205 "municipalities with extended powers" (ORP) in 2003. These municipalities perform central government delegated functions on behalf of smaller surrounding municipalities such as child protection and issuing passports. These functions are associated with additional funding. Smaller municipalities can also delegate additional functions to the ORP that they do not want to provide, or cannot provide because of their lack of capacities (with 6 258 municipalities, the Czech Republic has the lowest average municipal size: 1 640 inhabitants vs. 9 570 in the OECD in 2016). To do that, they use contract agreements and in 2012 they concluded 5 784 contracts. Responsibilities transferred include administration as well as services such as healthcare and education. While this is very flexible and has increased efficiency, it also adds to complexity and has proved difficult to monitor. The Ministry of Interior in 2012 therefore proposed to move all delegated functions to the 205 ORP in order to streamline the system and increase efficiency.

Source: OECD (2016f), *Making the Most of Public Investment in Colombia: Working Effectively across Levels of Government*; OECD (2016g), *OECD Economic Surveys: Czech Republic 2016*; OECD (2017b), *OECD Territorial Reviews: Sweden 2017: Monitoring Progress in Multi-level Governance and Rural Policy*.

In Chile, until recently, regulations and policies were applied in a uniform way, with only some exceptions, e.g. in extreme regions and Chilean islands, which benefit from special treatment. In the 2000s, SUBDERE started to carry out several studies to better identify this territorial diversity at the regional and municipal level and design more

place-based and differentiated tools and programmes taking into account various geographical, economic, political or cultural situations. This new approach has made several changes to legislation, instructions or guidelines (e.g. in the allocation of education and health subsidies for rural municipalities) and to design specific programmes tailored to the characteristics and needs of territories. It has also resulted in the creation in 2012 of a concrete tool: a new typology of municipalities that classifies the 345 municipalities into five categories according to spatial and socio-economic criteria. This tool is used to allocate the funds of an incentive scheme (*Fondo de Incentivo al Mejoramiento de la Gestión Municipal* - FIGEM) aimed at encouraging good managerial practices.

To advance further in the process of decentralisation, this type of differentiated approach should be pursued and strengthened in Chile. Asymmetric decentralisation could be envisioned in several directions (see also the following chapters): devolving additional competences to the most capable municipalities; allocating additional fiscal powers to municipalities with greater financial and technical capacities (e.g. access to borrowing, tax power, ability to define user fees and tariffs, etc.); simplifying reporting mechanisms of weaker municipalities to alleviate the administrative burden. This flexible approach recognising differences in capacity and performance across municipalities could be incorporated in the framework of the New Public Education reform. Chile could draw inspiration from the model that serves as the basis for the Colombian certification system. This approach would avoid the risk of disruption and loss of existing capacities to certain performing municipalities resulting from the education reform (see above and Santiago et al., forthcoming).

In this scenario, the FIGEM classification could also be a useful tool. It would need to be updated, completed and used in a larger and systematic way to design and implement policies and programmes targeted at municipalities. To implement such an approach, Chile could also take advantage of pilot experiences in the devolution of competencies as a way to ensure a gradual institutional change and "learning-by-doing".

Finally, an asymmetric decentralisation approach could also be a way to support the development and integration of indigenous communities, as it is the case in several OECD countries (Box 1.22).

Box 1.22. **Decentralisation can offer space to design effective policies supporting the development and integration of indigenous communities: The experience of OECD and Chile**

Twelve OECD member countries - Australia, Canada, Chile, Denmark (Greenland), Finland, France (New Caledonia), Japan, Mexico, New Zealand, Norway, Sweden, and the United States - report having indigenous populations, which account for around 24.5 million people, 2,0% of OECD total population (OECD, 2016h).

Table 1.3. **Indigenous communities in OECD countries**

Country	Indigenous peoples	Population	% national population
OECD member countries			
Australia	Indigenous/Koori	670 000	2.8
Canada	First nation/Inuit/Metis	1 400 685	3.9
Chile	Various	1 565 915	8.8
Denmark (Greenland)*	Inuit	51 377	0.9 (91.6)
Finland	Sami	8 000	0.1
France (New Caledonia)*	Kanak	70 000	0.1 (25.9)
Japan	Anui	28 782	0.02
Mexico	Various	15 703 474	12.4
New Zealand	Māori	645 000	14.0
Norway	Sami	50 000 – 65 000	1.0 – 1.3
Sweden	Sami	20 000	0.2
United States	American Indian/Alaskan native	5 200 000	1.6
SUB-TOTAL		25 420 733	--

*Greenland is defined as an autonomous country within Denmark, whilst New Caledonia is a special territory of France. Masyarakat Adat is the official government title given to indigenous communities and do not represent a tribal group.

Source: OECD (2016h), *Linking indigenous communities with rural and regional development*, Discussion paper; Estimates from Food and Agricultural Organisation of the United Nations (www.fao.org/indigenous-peoples/en), International Working Group for Indigenous Affairs (www.iwgia.org); Country population totals from World Bank (http://data.worldbank.org/indicator/SP.POP.TOTL).

Indigenous communities are struggling, but opportunities can be addressed at the municipal level

While indigenous communities make an important contribution to culture, heritage and economic development, they are often confronted with strong social and economic difficulties. Often marginalised and discriminated, they generally experience poorer socio-economic outcomes (higher mortality rate, lower educational level, higher unemployment and poverty, etc.) and can have high levels of dependency on subsidies and transfers. While they are part of the dynamics of regional growth and development, they are often disconnected from it because of historical reasons and specific institutional arrangements related to self-determination and sovereignty which give them the right to govern their affairs, including traditional lands, and in some cases develop revenues and economic opportunities linked to their local assets.

Box 1.22. **Decentralisation can offer space to design effective policies supporting the development and integration of indigenous communities: The experience of OECD and Chile** *(continued)*

Regions and local municipalities are often an important way of addressing the challenges facing indigenous peoples. Indigenous communities tend to have a strong attachment to place (in rural and urban areas), and their socio-economic conditions and capacities can differ widely across national territories. The challenges facing indigenous communities (e.g. in regards to health, education, employment and land use) are linked, and addressing them effectively depends on working in partnership with them. This includes identifying ways to provide for continued cultural identity and values in an integrated market economy (OECD, 2014a). As such, decentralisation is important in delivering policies for indigenous people that are adapted to local specificities and needs.

Indigenous population in Chile

In Chile, the Chilean government currently recognises nine indigenous groups: the Atacameño, Aymara, Colla, Diaguita, Kawashkar, Mapuche, Quechua, Rapa Nui, and Yagán peoples. According to the Ministry of Social Developments' 2013 Survey, the population that identifies as belonging to or descended from one of the nine indigenous peoples, via parentage or surname, numbers 1 565 915 people, or 8.8% of the country's total population, one of the highest percentages in the OECD after Mexico and New Zealand.

The largest indigenous group is the Mapuche people (around 85% of all indigenous people in Chile), which is concentrated in the south and rural areas and which is in turn subdivided into various indigenous territorial groups (the Huilliche, Lafkenche, Pehuenche and Nagche). For example, they represent 25% of the population of the Los Lagos region and more than 32% in Araucanía. A sizeable contingent of Mapuche people also lives in the metropolitan area of Santiago, where they are called "urban Mapuche". Their characteristics and problems differ significantly from those of the Mapuche in the south. In total, 74% of indigenous population live in urban and 26% in rural areas.

In Chile, although poverty rates for the indigenous population have decreased over recent decades thanks to special initiatives targeted to them, they are still over-represented in the lowest deciles of the income distribution. They experience higher poverty rates (23.4%) than the non-indigenous population (13.5%). In rural areas, they have little land and tend to be concentrated in extremely fragile and rapidly deteriorating environments. In urban areas, such as Santiago, Concepción and Temuco, indigenous peoples are clustered in the poorest neighbourhoods, with limited access to social services, a high rate of unemployment or informality as well as racial discrimination, which reduces labour opportunities (OECD, 2015b).

The recognition of indigenous communities in Chile

After several failed attempts by the Spanish Crown to subjugate the Mapuche, their independence and territorial sovereignty were recognised in various agreements (*parlamentos*), delimitating it to the south of the Bío Bío river. This was maintained by the Chilean Republic until the end of the 19th century when Chile embarked upon the military conquest of Araucanía. At the same time, other indigenous communities (Aymara, Atacameño, Quechua and Colla) were integrated into Chile, in the North following the war of the Pacific (1879-1883) and Easter Island in Polynesia (Isla de Pascua inhabited by the Rapa Nui community). An accelerated process of assimilation was imposed by the government resulting in the gradual loss of territories, culture, language and resources, as well as sovereignty.

Chile's centralism led the country to ignore the existence of native peoples within the Chilean nation until the late 1980s. The various social and land reforms introduced by President Salvador Allende were reversed by the Pinochet regime.

Box 1.22. **Decentralisation can offer space to design effective policies supporting the development and integration of indigenous communities: The experience of OECD and Chile** *(continued)*

The return to democracy in 1989 sparked a new phase in the history of the relationship between indigenous peoples and the Chilean state. Patricio Aylwin's Concertación government established a *Comisión Especial de Pueblos Indígenas* (Special Commission of Indigenous People) to make recommendations which led to the adoption, in 1993, of the Indigenous Peoples Act (No. 19.253) on the "promotion, protection and development of indigenous peoples". It recognised the special status and rights attached to indigenous peoples and expressed its intention to establish a new relationship with them.

Among the most important rights recognised in the Act were the right to participation, the right to land, cultural rights and the right to development within the framework of the state's responsibility for establishing specific mechanisms to overcome the marginalisation of indigenous people.

In 2003, a special commission was set up consisting of various representatives of Chilean society and indigenous people. It made recommendations for a new state policy, which resulted in a report with proposals for reconciliation and a new deal between indigenous people and Chilean society.

In 2007, Chile adopted the United Nations Declaration on Indigenous Rights and in 2008, it ratified Convention 169 of the International Labor Organization in Indigenous and Tribal people (ILO 169), which guaranteed additional rights to the indigenous peoples living in Chile, such as the right to consultation, property, and self-determination. The same year Chile adopted an indigenous policy called "Re-cognition: Social Pact for Multiculturalism" (*Re-conocer: Pacto Social por la Multiculturalidad*), followed in 2012 by the policy called Towards a New Deal with our Indigenous Peoples.

In August 2016, the President of Chile set up a Presidential Advisory Commission of La Araucanía whose purpose is to prepare proposals in the areas of regional and territorial development and participation of indigenous population.

Despite this significant progress, there are still important problems such as unsettled claims over property rights and property titles, conflicts over water rights and natural resources and over traditional access to fishing and forestry activities. Different government efforts over the past four decades have not yielded the expected results, especially in terms of poverty, recognition and violence. In addition, Chile's constitution still does not recognise indigenous peoples and their rights and a constitutional reform has been before the national congress since 2007-2008.

Indigenous communities, asymmetric decentralisation and municipalities

One of the mechanisms set up by Chile to address these challenges is the National Indigenous Development Corporation (CONADI), a collegiate decision-making body acting as the main government body to form indigenous policy and consult with indigenous people. Chile's approach to dealing with its indigenous population parallels that of Canada and the United States, which have long relied on a separate agency to manage relations. This approach is unlike policies in countries such as Australia and New Zealand, which formally recognise the leading role that indigenous people played prior to the arrival of European settlers, or other OECD countries where responsibility is more fully devolved to individual groups or settlements along with resources to begin a bottom-up development process (OECD, 2014a).

Box 1.22. **Decentralisation can offer space to design effective policies supporting the development and integration of indigenous communities: The experience of OECD and Chile** *(continued)*

Decentralisation can offer space to design effective policies supporting the development and integration of indigenous communities while preserving their cultural identity. This can take place effectively at the level of municipalities. In areas where there is a high concentration of indigenous population, it could take place through decentralisation of certain competences, for example, giving to these areas more autonomy and control to design and deliver municipal, education and health services as well as special rights to be consulted and sometimes participate in national decisions. Such asymmetric decentralisation exists in countries such as Finland (the Åland Islands with the so-called Åland Settlement, 1921), France (New Caledonia or Polynesia), Denmark (Danish Home Rules on Greenland and the Faroe Islands). When indigenous population is less represented in a given municipality, this process can take the form of giving municipalities the possibility to design local policies to meet the needs of these populations, increase local participation and consultation and favour a local development policy able to mobilise endogenous assets to improved income and employment opportunities. Municipalities can represent a valuable "arena of indigenous policy" which can be particularly creative and efficient in this field (Richards, 2013).

Source: OECD (2016h), Linking indigenous communities with rural and regional development, discussion paper; OECD (2014a), *OECD Rural Policy Reviews: Chile 2014*; Richards (2013), Race and the Chilean Miracle: Neoliberalism, Democracy, and Indigenous Rights; Indigenousnews.org: Project for Indigenous Self-Determination network; Informe Comisión Asesor presidential de la Araucania (January 2016) https://prensa.presidencia.cl/lfi-content/otras/informes-comisiones/Informe_AP_Final.pdf.

Inter-municipal co-operation bodies

In Chile, municipalities can join forces and co-operate. However, this possibility is quite new thanks to the recent improvement of the legal framework for municipal co-operation.

Until 2009, associations of municipalities did not have a legal status. A project covering several municipalities could be presented but it had to be administered by a single municipality (for the group) (OECD, 2009). Despite these limitations, some convinced pioneers however started to co-operate to developed common projects, such as the *Asociación Municipalidades Región del Bío Bío* or the *Asociación de Municipalidades del Valle del Itata* created in 1998.

In 2009, a step was taken through Law No. 20.346 *Reforma constitucional en materia de asociacionismo municipal* to allow municipal associations to obtain legal personality under private law, and may form or integrate private non-profit corporations or foundations whose purpose is the promotion and dissemination of art, culture and sport, or the promotion of municipal public works and productive development.

This law was revised in September 2011 through Law No. 20.527, which regulates the municipal associations. It provided the impetus to create municipal associations, although the legal framework remains constraining in terms of status, resources and scope of co-operation. There are four categories of municipal associations:

- National, such as the Chilean Association of Municipalities (ACHM).
- Regional, made up of regional sections of ACHM or autonomous associations organised around interests related to regional development.

- Territorial, founded around a common territorial project based on cultural, agro-ecological or economic-productive goals (around 55% of municipal associations in 2011).
- Thematic, established by a group of municipalities wishing to co-operate around common projects in various areas (tourism, mining, rural development, economic development, etc.).

Chile has made important efforts to promote and strengthen municipal associations. There were 53 associations registered in the official registry maintained by SUBDERE under the provisions of the Law No. 20.527 (*Registro Único de Asociaciones Municipales con Personalidad Jurídica de Derecho Privado*). Despite the progress, integrated projects or investments conducted by municipalities associations remains limited so far, and the experiences vary greatly throughout the country. The development of municipal associations will pose substantial challenges for the modernisation of the municipal system (see Chapter 6).

Managing local public services

In the OECD, there are many options available to municipalities for managing the local public services under their responsibility, ranging from direct management via an internal municipal service or an autonomous municipal agency ("in house") to indirect management by an independent local public entity, which is organised under private law and delivers local public services. It can be 100% publicly funded or a combination of public and private capital (joint ventures). Another final option is the outsourcing of the public service to the private sector as well as the privatisation of the service. In the majority of OECD countries, municipalities enjoy freedom in this domain, except in some cases for "protected" sectors such as education or healthcare. However, this autonomy is generally heavily regulated.

In Chile, municipalities' freedom to choose management methods for local public services is restricted by the LOCMUN. They can use the formula of "corporations" in some defined areas but not that of "municipal public companies". In contrast, use of the private sector for service provision is widespread in the form of concessions (however mostly managed directly by the central government) and several local services are privatised. Overall, in many municipalities, responsibility for service provision is shared between the public and the private sector making the situation particularly complex at times.

Corporations

Municipal corporations are private non-profit entities with legal personality, bringing together a municipality and specialised local associations. Created by the decree Law No. 1-303.80 of 1980, they aim at administering and managing municipal services. Municipal corporations were originally focused on education, health, early childhood and elderly care. In 1988, while their scope was expanded by law, a ruling by the Constitutional Court strictly limited corporations to the promotion of the arts, culture, sport and leisure, in addition to traditional sectors (education and health).

Municipal corporations represent parallel or peripheral structures regarding the municipality. These "municipal satellites" are, however, part of the "municipal group". Relations with the "mother municipality" are institutional (the mayor is the president), functional (the municipality provides some means) and financial (part of the funding

comes from the municipality and is supplemented by state resources and fees coming from the corporation's activities).

Around 55 municipalities out of 345 have established municipal corporations, mainly in the fields of education and health, and more marginally for culture and leisure. They are most often large municipalities with more than 50 000 inhabitants. The formula is, however, used in less densely populated municipalities, ranging from 10 000 to 35000 inhabitants (e.g. Chonchi, Dalcahue, Tiltil, María Pinto, San José de Maipo) or, in a limited number of cases, in smaller municipalities (up to 4 000 inhabitants such as Curaco de Velez, Queillen, Quinchao).

Under the civil code, municipal corporations are associations under private law. This status has the advantage of providing, in addition to the plurality of its members, flexibility in the management of services. As a result, corporations are not subject to public law, especially public procurement rules (*Chile Compra*). They are subject to less formal requirements to purchase goods and services and can act more quickly. They also enjoy more room for manoeuvre in terms of staff remuneration.

Municipal corporations are sometimes large entities with an imposing organisational structure. They can manage a large number of health and education structures. For example, the municipal corporation of La Florida (COMUDEF) (388 000 inhabitants) is responsible for nine family health centres, three mental health facilities, one health laboratory, 25 schools and 16 kindergartens. The municipal corporation of La Prado (112 600 inhabitants) operates eight health facilities, six middle schools, two high schools, three schools and three educational facilities. The Chilean Council for Transparency (Consejo para la Transparencia) has noted their large size, which is sometimes much greater in terms of budget or staff than that of the municipalities from which they emanate.

There are several issues at stake concerning the role of municipal corporations. Like all "municipal satellites", municipal corporations' activity raises questions about, in some cases, their excessive autonomy in relation to the municipality and lack of transparency and accountability, in particularly important and sensitive areas for the (education and health). Corporations take full advantage of their mixed status: the lack of public constraints, thanks to their private status and the lack of private sector pressures, thanks to their public support. There are recurring issues such as the level of quality control exercised over their activities and transparency in management. Corporations are, however, subject to the supervision of ministries in the areas concerned. They also come under the legal control of the Comptroller General's Office. In addition, the mayor is the president and municipal internal control services should be in a position to ensure this inspection. However, the 2012-2013 activity report of the Transparency Council (*Consejo para la Transparencia, 2013*) paints a less reassuring picture. Municipal corporations obtained the lowest scores (14%) in transparency assessments, far behind central administrations (97%), universities (91%) and municipalities (47%). With one exception (Concepción), the 54 municipal corporations are viewed as less transparent than their mother municipalities.

Municipal public companies are few and far between

Another form of indirect management is when municipal services are provided by an independent local public entity, which is organised under private law to deliver local public services. It can be 100% publicly funded or a combination of public and private

capital (joint ventures, public authorities holding a minimum share of the capital of these limited companies).

In Chile, the use of municipal public companies or joint ventures (public-private) is very restricted. According to the article 11 of the LOCMUN, municipalities may develop or participate in business activities in the form of municipal public enterprises or joint ventures (public-private) only if there is a qualified quorum law authorising it, which implies an absolute majority.

There are, however, a handful of examples of municipal companies, established prior to the law prohibiting their creation, such as the drinking water company of Maipú (*Servicio Municipal de Agua Potable y Alcantarillado de Maipú* – SMAPA, which is owned by the municipalities of Maipú, Nogales and Puerto Octay. Created in 1950, it is one of the 24 main firms providing drinking water distribution and wastewater collection services in the urban zones of Chile and the Metropolitan Enterprise for the Management of Municipal Solid Waste in Santiago (*Empresa Metropolitana de Tratamiento de Residuos Sólidos Limitada* - EMERES). Created in 1986, EMERES is a municipal enterprise (*asociación empresarial*) formed by the association of 22 municipalities in the south of Santiago to manage waste collection as well as the area's largest landfill (Marello and Helwege, 2014).

Concessions

Faced with an infrastructure and service delivery deficit in the early 1990s, the government began promoting an active role for the private sector as a means of filling the gap. It launched an ambitious concession programme managed by the central government (e.g. the Ministry of Public Works - *Ministerio de Obras Públicas* - MOP), through Programming Contracts and by SERVIU regarding urban infrastructure concession projects (Box 1.23).

Therefore, Chile is quite unique among OECD countries. The private sector plays a critical role in the provision of numerous services, including transport infrastructure, ports, telecommunications, electricity, gas and water. Private operators, under concessions or programming contracts with the central government, provide and often finance most of the infrastructure supporting public service production, at national but also regional and local levels.

This partnership with the private sector led to quick and significant improvement in Chile's infrastructure and in access to basic public services, particularly for rural and remote areas (OECD, 2013b). However, municipal-level involvement is meagre in this process, although municipalities have the legal ability to enter into concession agreements with the private sector (in particular, articles 8, 36, 66 of the LOCMUN)[6] Numerous municipal services are managed by concessionaires but which have contracted with the central government (MOP or SERVIU), not the municipalities themselves, under terms and conditions dictated by national entities under national legislation. The centralised management of concessions also leads to homogeneous regulations that often are not well adapted to the heterogeneity of Chile's territories. Currently, the central government is in charge of most programmes and contracts, while the number of municipalities that have signed municipal concession contracts is low (OECD, 2009; 2012; 2013a).

Although municipalities have the legal ability to do so, they do not always have the technical capacity, especially in small and medium municipalities. Therefore, although municipalities benefit from privately-financed improvements in their area, they are often observers in the process (OECD, 2013a). This can be a significant handicap in many

ways. For instance, they cannot regulate the public service (e.g. timetables and frequency of ferry transport connecting several islands in a small rural municipality which are determined by Santiago) or adapt it to particular local or changing circumstances. Nor can they monitor the quality of service delivery or receive revenues from concessions. In a nutshell, they cannot fully manage the development of their territories, which remain operated by private concessionaires that negotiate directly with the central government.

For metropolitan cities, municipal concessions are also under-developed. Examples concerning municipal parking garages include facilities in Valparaíso and Santiago (World Bank, 2016). Most concession contracts are managed by the central government. In some cases, the explanation may be the lack of a metropolitan governing body able to co-ordinate several municipalities and/or with the legal, technical and financial capacity to enter into a contract. This was the case of the Transantiago integrated public transport system, which is managed by the central government. However, it should be underlined that both the "*Co-ordinación general del transporte de Santiago*" and the "*Directorio de transporte de Santiago*" are formed almost exclusively with central government institutions (different ministries and under-ministries), without any representation of local government on the institution's board (OECD, 2009).

Box 1.23. **Public private partnerships for infrastructure and urban development in Chile**

In 1993, Chile launched an innovative concession programme based on public-private partnerships focused on a number of highway-network development projects that were developed mainly through build-operate transfer (BOT) arrangements. Concession contracts are awarded through a national or international public bidding process. The winning concessionaire signs a contract with the national government under which a concessionaire finances, builds and operates the infrastructure facility. In exchange, tolls are collected for a fixed length of time, and the infrastructure facility reverts to the government when the concession contract expires – normally 20 to 30 years. Most contracts include minimum revenue assurance by the government, in the event that toll proceeds fall short of the agreed amount (OECD, 2009). The concessions co-ordination Unit of the Ministry of Public Works regulates and controls the system (www.concesiones.cl).

As of December 2013, Chile facilitated development of USD 14.8 billion in infrastructure through 76 concession contracts, leading to 237 889 m2 of public buildings; 146 409 m2 of airport terminals; 2 601 hospital beds; 18 km in public transit corridors; 179 km of urban roads; 3 506 km of intercity roads; and 12 435 interior plazas in penitentiaries. For the 2014-2020 period, the MOP has put together a pipeline of 29 projects with an estimated value of USD 7.946 billion. Investments are expected to contribute: 363 810 m2 of airport infrastructure; 99 324 m2 of public buildings; 930 km of intercity highways; 54 km of urban highways; 9 km sustainable public transportation; and 600 million m3 of water projects. Agenda 30 30 foresees a continued and central role for the private sector.

Focused on urban infrastructure, the Law No. 19.865 set up a "Shared Urban Financing System" facilitating urban concessions in 2003. The law empowered the Housing and Urban Development Agency (SERVIU) and the municipalities to enter into contracts with private companies to execute, operate or maintain works related to urban infrastructure, equipment, green areas, industrial parks, etc. These works must, in any case, be part of programmes of the Ministry of Housing and Urban Planning. Other ministries, public services - but also municipalities - may mandate SERVIUs to enter into participation contracts pertaining to property owned by them.

Box 1.23. **Public private partnerships for infrastructure and urban development in Chile** *(continued)*

The system proposed a simplified system compared to concessions under the Public Works Concessions Act and allow conducting both large-scale projects and smaller initiatives (plazas, community centres).

Sources: OECD (2009), *OECD Territorial Reviews: Chile 2009*; OECD (2013b), *OECD Territorial Reviews: Antofagasta, Chile 2013*; Ministry of Public Works (2014), Concessions Agenda: Infrastructure, development and inclusion, Chile 30 30, Co-ordination of Public Works Concessions, September 2014; National Congress: History of the law 18.865 www.bcn.cl/historiadelaley

Main challenges at stake for the Chilean municipalities in the context of the regionalisation and decentralisation agenda

Since the 1980s, most Latin American countries have begun decentralisation processes, albeit at different speeds and in different ways (Valencia Carmona, 2010; Brosio and Jimenez, 2012; Uhaldeborde 2016). Although the prospect of decentralisation has won over a number of political authorities and economic and social players in Chile, the definition of its nature, its intensity, where to begin and, especially, its practical implementation has sparked dissention and hesitation.

Designing a balanced, integrated, gradual and well sequenced decentralisation process

There are generally two major challenges to conduct a decentralisation reform: finding the right balance between the three interconnected dimensions of decentralisation: political, administrative and fiscal decentralisation; and finding the right sequencing for the implementation.

An "open-system" perspective should be adopted when designing, implementing and assessing multi-level governance reforms and decentralisation processes (Box 1.24 and Figure 1.18). Linkages between the three aforementioned dimensions should be considered to ensure effective decentralisation. These dimensions tend to be complementary and interdependent, and decentralisation reform outcomes depend on how the different elements of the reform are connected and interact.

Box 1.24. **Decentralisation reforms: Three closely interconnected dimensions to be considered in an "open-system" perspective**

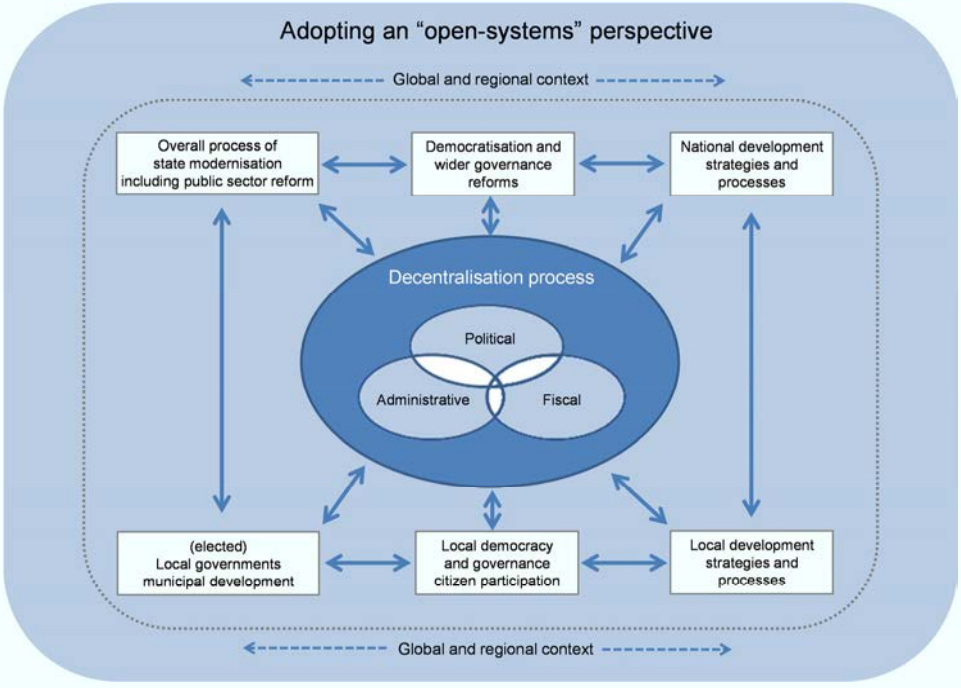
Decentralisation is a key component of public sector reform, as it consists in transferring a range of powers, competences and resources from central government to elected subnational governments. The term "decentralisation" generally encompasses three interconnected, political, administrative and fiscal aspects:

- **Political decentralisation** involves a new distribution of powers according to the subsidiarity principle, with the objective of strengthening democratic legitimacy.
- **Administrative decentralisation** involves a reorganisation and clear assignment of tasks and functions between territorial levels in order to improve the effectiveness, efficiency and transparency of national territorial administration.

Box 1.24. **Decentralisation reforms: Three closely interconnected dimensions to be considered in an "open-system" perspective** *(continued)*

- **Fiscal decentralisation** involves delegating taxing and spending responsibilities to subnational tiers of government. In this case, the degree of decentralisation depends on both the amount of resources delegated and the autonomy in managing such resources. For instance, autonomy is greater if local governments can decide on tax bases, tax rates and the allocation of spending.

Figure 1.18. **Adopting an open-systems perspective**



Source: European Commission, EuropeAid (2007), "Supporting decentralisation and local governance in third countries", *Tools and Methods Series*.

Decentralisation leads to a greater inter-dependency between the central and subnational governments: administrative (explicit or implicit sharing of policy-making authority), financial (co-financing, fiscal relations between levels of government) or socio-economic (issues and/or outcomes of public policy at one level have impact on other regions and the national level). In this context, decentralisation reform is a multi-level governance reform, which involves reshaping and improving these interactions between public authorities, i.e. between central and subnational governments and also within subnational governments. "Multi-level governance" approaches can also be more comprehensive and include interaction between public entities and private stakeholders (profit or non-profit ones), in particular citizens and businesses (Ostrom E., 2010).

Source: OECD (2017a), *Multi-level governance reforms: Overview of OECD country experiences*; Ostrom, E. 2010. "Beyond Markets and States: Polycentric Governance of Complex Economic System; European Commission, EuropeAid (2007), Supporting decentralisation, and local governance in third countries, *Tools and Methods Series*.

Should Chile start with the regions or municipalities in the current decentralisation process? So far, that dilemma seems to have been resolved in favour of the regions. At this juncture, it appears that it is now a priority to empower this critical intermediary level with a status that reflects the spirit of political decentralisation. The regions are, at present, simply conduits of central power in Chile, unlike the situation in most multi-level political-administrative structures, especially in the federal states neighbouring Chile. However, if the goal is to avoid building an imbalanced political structure, the regional reform cannot be designed or implemented by ignoring the regions' impact, within the overall system, on the central government and on municipalities. Focusing reforms on the regional level must not come at the expense of careful consideration of the modernisation that urgently needs to be undertaken at the municipal level. Can the status quo of the municipalities be maintained? Is there not some room for fast modernisation pending an eventual overhaul addressing the broader question?

Even if major progress was accomplished in 2016 with Law No. 20.922 on municipal staff, a lot remains to be done in other areas of municipal governance to transform the municipalities, which are today mainly administrative and service delivery agents, into real "local governments". First, the law on municipal staff is still in the implementation phase and it could need to be monitored and adjusted until it is effective in 2018. In addition, other reforms could be launched with respect to municipalities' human resource management (see Chapter 4). Second, municipal staff reform is only one component of what should constitute a comprehensive municipal modernisation reform.

It seems that municipal reform should be better integrated into the regionalisation and decentralisation agenda. There are still many important challenges ahead that should be addressed in a more ambitious and integrated manner. They concern, in particular, a better definition of municipal responsibilities and powers, increased municipal financial resources, greater equity and solidarity, more citizen participation and democratic oversight as well as improved co-ordination mechanisms across and within levels of government. This is all the more crucial because municipalities will now operate in a multi-level governance system undergoing profound changes (Figure 1.19).

The central, regional and municipal levels are interdependent components of a complex multi-level governance system. The on-going regionalisation will have an impact on the municipalities, which will have to redefine their role in relation to the new regional governments but also in relation to the central government, both at national (ministries and agencies) and territorial levels (future "presidential delegate", SEREMIs). In this attempt to rebalance the multi-level governance system by reinforcing the regions, there is also a risk of creating new imbalances if regions are strengthened but not the municipalities. Some interviewed people suggested that there would be a risk of transferring the centralised system at the regional level. Municipalities would remain the mere "executors" and "administrators" of central and, possibly regional, lines of credit, as well as service providers.

The need for more place-based policies and citizen participation and control are also two forces that plead in favour of taking municipalities into better account in the multi-level governance system. In fact, municipalities operate in the closest proximity with citizens and they are particularly well positioned to conduct local development policies.

Figure 1.19. **Chilean municipalities operate in a multi-level governance system undergoing profound changes**



The decentralisation process would also be an opportunity to concretely recognise the diversity of the Chilean municipal landscape. It could enable stakeholders to design and implement tools, programmes and policies adapted to the diversity of territories. Decentralisation would require stakeholders to question the principle of unity, which has always been the bedrock of the Chilean state. Chile could start to experiment with asymmetric decentralisation to meet the needs of more place-based policies.

It seems that the plan, at present, for the municipal system is limited to modernisation rather than genuine decentralisation and recognition of municipal specificities and differentiated needs. Nevertheless, it seems that there is a strong demand for decentralisation on the ground, as reflected by the interviews held in the regions of Bio Bío, Los Lagos and Valparaíso. It is therefore suggested to firmly embed the municipal modernisation plan into the decentralisation agenda in order to empower municipalities and create genuine "local governments" that would be more "accountable" and an essential link in the "social pact", which seems to be suffering, and not just mere managers of public services.

It is also necessary to design a gradual and well sequenced decentralisation process. As underlined above, a major challenge is to finding the right sequencing of reforms i.e. deciding when to deal with each dimension over a long-term decentralisation process.

Multi-level governance reforms, including decentralisation reforms, are often a learning process. They are particularly sensitive and difficult to conduct, as many countries, including Chile, can attest. As a result, the development of such reforms is typically very slow. Reforms do not produce instant results and need adaptation.

Permanent adjustments are necessary to correct for potential deviations. Introducing complementary reforms is often necessary (Box 1.25).

Box 1.25. **Multi-level governance reforms: Policy makers are faced with a variety of challenges**

Multi-level governance reforms are particularly sensitive and difficult to conduct. Policy makers face a variety of challenges (OECD, 2010). Governance reform processes are highly context-dependent. They are framed by political conjuncture and structural constraints including countries' specific features such as geography, population, economy, historical and cultural context, constitutional arrangements and organisational patterns. Moreover, they confront policy makers with the problem of "reforming the reformer" since the public administration must indeed design and implement its own reform, often imposing measures which may be contested both at central and local levels. These reforms are complex as they involve several layers of government and refer to reshaping vertical and horizontal interactions between central government and subnational governments, and also within subnational governments. They concern elected politicians and civil servants from central and subnational levels as well as various other stakeholders with sometimes conflicting interests. In addition, gaining public support is often a challenge. Either there is a lack of social demand of citizen and lack of interest or, when they express an interest, public resistance is still often observed. Reforms tend to be perceived as threats to an existing social order and as a risk of loss compared to previous situations, as witnessed by the failure of institutional and territorial reforms (e.g. municipal mergers, regional reforms, and decentralisation).

Therefore, multi-level governance reforms, including decentralisation, entail risks that should not be underestimated. Reform processes often stall, fail and may be cancelled, postponed or even reversed. They may not go according to plan, and may be only partly implemented, adjusted, or even circumvented during the implementation phase, without producing instant results or the expected outcomes. Therefore, reshaping the multi-level system of government takes a long time and may need adaptation. To generate expected benefits, additional and complementary reforms are often needed to correct for potential deviations and improve multi-level governance mechanisms. Moreover, this is a never-ending process: the challenge of multi-level reforms is not merely to adapt to a new, stable and definitive situation but to enable public administration at all levels of government to adapt continually to a permanently evolving environment.

OECD countries adopted diverse solutions and tools in response, some successful, others not. There are potential strategic levers for policy makers planning to introduce multi-level governance reforms, such as:

- Pilot programmes, experiments and place-based approaches can demonstrate the effectiveness of reforms and pave the way for change on a larger scale.
- Opposition from local governments can be overcome through the development of a multi-level co-operation culture and practice, wide-reaching consultations and negotiations at a preliminary stage and during the whole reform process, appropriate incentives to compensate potential "losers" and to build good relationship with associations of subnational governments.
- Mobilising and generating acceptance from central and local civil servants through good communication practices, incentives, compensations and training activities. As decentralisation reforms affect central government structures at ministerial and territorial levels, they can be perceived as a threat (loss of power and jobs) and can be resisted. Difficulties can also arise from local civil servants hence generating opposition to the reform. This dimension is key and should be addressed with appropriate responses.

Box 1.25. **Multi-level governance reforms: Policy makers are faced with a variety of challenges** *(continued)*

Gaining support from the civil society through information, public debates and consultations. Other consultation mechanisms may be mobilised (roadshows, consultation roundtables, conferences, e-voting, etc.) to listen to different stakeholder views as well as innovative sharing information tools including internet tools.

- Reaching greater political and gaining political adhesion across party boundaries through expert committees. This may be especially crucial to keep the momentum for reform going despite changes in governments. Parliaments may have an essential role to play in this respect, to reconcile different points of view and reach consensus between different stakeholders. Ad hoc parliamentary committees to consult, prepare and monitor reforms' progress can be key success factors. Such approaches can also include consultation through permanent multi-level co-ordination commission or forums or the reliance upon ad hoc expert advisory committees.
- Providing expertise, guidelines documents, technical support and prefiguring tools to local governments and stakeholders in the context of the reform can help to achieve its objectives. In contrast, lack of guidance from the central government has been identified as a problem in several countries.

Source: OECD (2017a), *Multi-level governance reforms: overview of OECD country experiences*; OECD (2010), *Making Reform Happen: Lessons from OECD countries*.

The next steps: Designing both an action plan and an implementation plan

The first step of the municipal decentralisation process is to start by reflecting on municipal powers and responsibilities. Clear assignment of responsibilities is the entry point that should determine the entire decentralisation process. It determines whether or not, or to what extent, it is necessary to reinforce fiscal decentralisation and how. Assignment of responsibilities guides the assignment of revenues i.e. what type of revenues for what type of responsibilities. Revenue sources (tax, fees, charges, grants, etc.) greatly depend on the nature (exclusive or shared) and area of responsibilities (transport, education, health, social inclusion, etc.). Likewise, changes in municipal financing can only really be carried out with success if they are closely linked to other reforms such as the reinforcement of human capacities both quantitatively and qualitatively (regional and local, political, technical and administrative staff), the improvement of initiatives favouring citizens' participation and inclusion, the necessary adaptation of politico-administrative structures (municipal associations, metropolitan governance, etc.), or else, the need to improve vertical co-ordination mechanisms across levels of government.

On this basis, an action plan, ensuring overall consistency between the different lines of the municipal reform, should be prepared and discussed within the framework of a multi-stakeholder dialogue in co-ordination with SUBDERE. An ad hoc permanent "decentralisation committee" could be established involving key ministers, subnational governments' associations, business and citizens' associations, universities, etc. to accompany the design and the implementation of the decentralisation reform. Setting up a decentralisation committee could help to build stronger legitimacy, better anchor the decentralisation agenda within the national reform programme and foster its

sustainability, a practice already employed in several countries for multi-level governance reforms.

In the OECD, such types of ad hoc and temporary commissions can be more or less independent, depending on their composition, administrative dependence and operational means (secretariat and staff, budget, communication). They may have more legitimacy and impact if they are directly connected to a high level of government (presidency, prime minister, parliament). These foras may involve experts and different stakeholders from the civil society and public and private sectors. It is a well-developed method in Nordic countries such as Denmark in Finland, as well as in Japan and New Zealand (Box 1.26 and Chapter 6).

Box 1.26. **Ad hoc commissions and committees facilitating the dialogue with stakeholders for designing and implementing multi-level governance reform**

Denmark: The Commission on Administrative Structure, appointed by the government in 2002 to perform a critical review of the Danish governance system, played a major role in reform processes. The Commission was established to provide a technical analysis of decision making regarding changes in public sector tasks. Its tasks were to assess the "advantages and disadvantages of alternative models for the organisation of the public sector". The Commission accomplished its work in 2003 and released recommendations in January 2004, proposing six different administrative models (OECD, 2009).

Finland: Working groups in charge of drafting the recent reform measures included members from the two coalition government parties and opposition parties as well as members from the Finnish Association of Local and Regional Governments. This led to a large political support base in favour of the reform despite a change in government during the reform process itself.

New Zealand: The independent Local Government Commission in charge of the 1989 local government reform was built with the aim of reaching across party boundaries (the chair of the Commission, Sir Brian Elwood, was a previous National party candidate, while the minister in charge was from the Labour Party) to protect the reform process from political interferences; all decisions were taken by the Commission and not by the government. The Commission consulted extensively with the civil society to build a stronger legitimacy. In particular, it worked in close co-operation with the association of local authorities (Local Government New Zealand) as well as with individual local authorities. The reform was implemented very quickly, especially regarding local government restructuring. The rapidity of the implementation and the delegation to an independent Commission were seen by many as positive for the success of the reform. Established by legislation, the Local Government Commission still exists. It has three members (appointed by the Minister of Local Government) and a small team of support staff. Its main role is to make decisions on the structure of local authorities and their electoral representation. The commission is a permanent Commission of Inquiry for local government reform.

Japan: Committees were in charge of drafting and monitoring the successive decentralisation reforms. The first committee, the "Decentralisation Promotion Committee" was appointed in 1995. Although it was not independent from central government (in contrast to New Zealand), committee members were typically from the private sector, local government, academia, etc., and not politicians, which helped to build legitimacy. The Committee was charged with drafting recommendations for the reform, to be submitted to the Prime Minister. The Committee was empowered with the ability to conduct investigations and deliberations, and could request information from both local and national authorities. The Committee published an interim report and Decentralisation Promotion Plans. These recommendations were discussed with the central government, undergoing some alterations, but were implemented within the Omnibus Decentralisation Law.

Box 1.26. **Ad hoc commissions and committees facilitating the dialogue with stakeholders for designing and implementing multi-level governance reform** *(continued)*

Thereafter, new committees were created to design and implement new reform steps in 2001 and 2007 (Trinity Reform and the 2nd Decentralisation Promotion Reform). In 2010, a Local Administration and Finance Examination Council was created in order to examine the review of the Local Autonomy Law. A bill creating a dialogue forum between the central government and local associations was also adopted in 2011.

Source: OECD (2017a), *Multi-level governance reforms: Overview of OECD country experiences*; OECD (2009), *OECD Territorial Reviews: Chile 2009*.

At the central government level, an inter-ministerial committee on regional and municipal decentralisation could be established to discuss and prioritise the recommendations of the OECD report, according to political choices and a more detailed analysis of the feasibility of measures proposed in policy reforms (technical, legal, financial, political, etc.) and possible implementation implications.

The implementation process that may follow the initial set of recommendations will be as crucial as the nature of the reform. The implementation plan will identify the necessary steps for a successful execution of the reform. It should include tools and indicators to permanently monitor the progress of the action plan and regularly assess the reform's outcomes. The lack of evaluation of governance reforms is often a striking common feature in the OECD. Despite some examples (e.g. Denmark or Iceland), they are not widespread, although evaluation is often considered a key issue.

Box 1.27. **Key recommendations for designing and implementing the municipal decentralisation agenda**

1. Promote a comprehensive decentralisation agenda for the municipalities

- Adopting an "open-system" perspective of decentralisation linking the three complementary and interdependent dimensions of decentralisation (political, administrative and fiscal). Decentralisation outcomes will depend on how the different elements of the reform are connected and interact. Finding the right balance between these three dimensions, including capacity building, is key in the process.
- Designing a comprehensive municipal decentralisation agenda as well as a gradual and well-sequenced process. A major challenge is to finding the right sequencing of reforms, while decentralisation reform is also a learning process. Permanent adjustments are necessary to correct for potential deviations.
- The process should start by reflecting on municipal powers and responsibilities. Clear assignment of responsibilities is the entry point that should determine the entire decentralisation process.
- Preparing an action plan to be discussed by a permanent "decentralisation committee" involving key ministers, subnational government associations and key stakeholders (business and citizen associations, universities, etc.) with a secretariat co-ordinated by SUBDERE, based on the recommendations of the OECD report.

Box 1.27. **Key recommendations for designing and implementing the municipal decentralisation agenda** *(continued)*

- Establishing an inter-ministerial committee on regional and municipal decentralisation at the central government level.
- Preparing an implementation plan, identifying the necessary steps for a successful execution of the reform and including tools to permanently monitor and assess the progress of the action plan. It would be monitored by the decentralisation committee.
- Linking closely the municipal decentralisation agenda with the regionalisation agenda. The municipal decentralisation agenda should be fully embedded in the overall multi-level governance reform, including central government reform. The municipal agenda should not limit to the objective of modernisation but should embrace a more ambitious perspective in order to empower municipalities and create genuine "local governments" instead of mere managers of public services that would be more "accountable" and an essential link in the "social pact".
- Promoting the involvement of associations of subnational governments at national and regional levels in the reform process though participation and consultation mechanisms in order to take benefits from their ground knowledge and expertise and overcome potential opposition to reform. They should become permanent partners of the reform.

2. Towards more flexibility and differentiated approaches

- Recognising the diversity and heterogeneity of the municipal world and designing and implementing policies, programmes and tools adapted to the diversity of territories. The FIGEM classification could be updated, enriched and discussed with stakeholders in that perspective. The National System of Municipal information (SINIM) could be further developed in this perspective.
- Reducing the number and scope of shared competences and increase exclusive responsibilities:
  - Setting up a working group to examine more precisely the list of responsibilities, which could be carried out exclusively by municipalities. They should be related to local economic and social development (territorial-based). This work should be carried out in the framework of the overall discussion about the assignment of responsibilities across levels of governments.
  - Reconsidering the functions carried out by municipalities within the area of some shared competences (e.g. by distinguishing financing functions). This reflection should be conducted in a co-ordinated manner with sector ministries to take into consideration current reforms, in particular the "New Public Education" reform.
- Creating incentives to promote the use of municipal associations for horizontal co-operation in service delivery and co-ordinated investment (see also chapter 6).
- Giving the possibility to delegate some tasks to a higher level of government through ad hoc agreements for a given period (provinces or regions).

Box 1.27. **Key recommendations for designing and implementing the municipal decentralisation agenda** *(continued)*

- Assigning different competences based on the different categories of municipalities. Large capable municipalities would have higher budget responsibilities than smaller ones. Less capable municipalities should be supported by specific schemes in order to avoid recreating inequalities. Chile could start by experimenting with asymmetric decentralisation through pilot projects to meet the needs of more place-based policies as a way to ensure a gradual institutional change and "learning-by-doing". Flexibility could be promoted in the framework of the education reform.
- Assessing the efficiency of municipal delegations in terms of a proximity tool with the population and public services delivery in order to determine the possibility of improving their recognition and functioning.
- Promoting asymmetric decentralisation as an interesting way forward to improve and strengthen decentralisation but also to support the development and integration of indigenous communities.

Notes

1. A single municipality may administer one or more communes. Currently, the only such case is the municipality of Cabo de Hornos, which administers the communes of Antártica and Cabo de Hornos. It explains that there are 346 communes but only 345 municipalities.
2. Capítulo X Art. 108,109,114 y 116 C. Política 1828.
3. The 1925 Constitution also established democratic elections for the provincial assemblies but Congress never adopted the enabling legislation. Provincial assemblies were never implemented.
4. Taxes, special regional rights and fees collected and distributed by central government agencies are however directed to the regions, including mining patents (50% of the income from mining patents is added to the share of the FNDR of the region to which the patent is assigned), tax on gambling casinos (50% of the revenue from this tax goes to the region in which the casino is located (to finance development of public works). In addition, 65% of revenue from the sale of public physical properties goes to the budget of the regional government in which the property is located (OECD, 2009).
5. Municipalities with up to 60 000 voters elect six municipal counselors; those with more than 60 000 and up to 150 000 voters elect eight counselors; municipalities with more than 150 000 voters elect ten counselors (Servicio Electoral de Chile, n.d.).
6. LOCMUN provisions concerning municipal concessions were amended in June 2009. Municipal concessions contracts are now also regulated by Law No. 19.886 on public procurement (which was not the case until this law).

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Chapter 2

The fiscal challenge: Developing Chilean municipalities' financial capacities and accountability

This chapter is dedicated to fiscal challenges in the current context and with respect to further devolution or reorganisation of tasks. While there is a general propensity to limit financial public intervention, the chapter shows the extent to which public finances are particularly centralised in Chile. The first part of the chapter provides a comparative overview of Chile with Latin America and OECD countries, based on macroeconomic public finance indicators at national and subnational levels. The second part focuses on the diagnostic through a retrospective analysis which provides greater insight into the trajectories of municipal budgets. The third part examines the weaknesses of the Chilean local government finance system. It suggests ways to improve it in order to provide municipalities with the financial capacity to better exercise their responsibilities, looking at the grant and tax systems as well as the ways to diversify municipal revenue sources. Finally, the chapter provides options for reform of the current budgetary and fiscal framework in order to ensure greater transparency of municipal functioning, reinforce the responsibility and accountability of local elected representatives, and guarantee fiscal sustainability of public policies. It also includes recommendations for expanding municipal borrowing abilities in a prudent and controlled manner.

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

Do the 345 Chilean municipalities have the fiscal capacity to fully and effectively carry out the missions that are entrusted to them? Must Chile first modernise the financial instruments available to its local authorities, and make human resource and organisational changes, before it can embark on a more ambitious programme of decentralisation? What strategy should be used to carry out the change and how to share it with elected officials and citizens? What could be the institutional conditions for the modernisation of municipal finances that empower local elected officials and guarantee the financial security of the system? Regardless of whether they are part of the diagnosis, arguments in favour of an overhaul or the foundation for a transformation, these are some of the fundamental questions that should be asked when considering the current state and future of the municipal sector in Chile.

The high degree of political centralisation that characterises Chile is reflected in rigid regulatory and budgetary arrangements and reduced financial room for manoeuvre for municipalities. They strongly constrain the free exercise of local powers and municipalities' accountability and ownership. In both of their components (spending and revenue), municipal budgets illustrate the magnitude of these constraints, including growth of local spending which is sometimes imposed.

In order to fully address the changes that need to be made regarding competences, sources of expenditure, and tax and financial resources to mobilise, it is helpful to first fully comprehend the extent to which Chilean public finances are centralised especially when seen against other countries. Therefore, the first part of the chapter provides a comparative overview of Chile with Latin America and OECD countries, based on macroeconomic public finance indicators at national and subnational levels using the methodology of national accounts harmonised according to international standards.

The second part focuses on the diagnostic through a retrospective analysis which provides greater insight into the trajectories of municipal budgets, both in terms of size and their composition. This analysis is done according to two time-perspectives: a long period of 25 years to identify long-term trends (1990-2015) based on data collected by the *Dirección del Presupuestos* (DIPRES); and a shorter period of 5 years (2011-2015), based on data from the *Sistema Nacional de Información Municipal* (SINIM), for a more granular look at the budget items and to identify instructive structural changes and trends. This last analysis shows how it is difficult to have a consolidated view of municipal budgets in Chile, municipalities having three (and even four) separate budgets corresponding to their main municipal functions: education, health, municipal activities (and cemeteries) and which are managed independently based on their own administration and management rules. As a result, is it as if Chile had almost 1 000 municipalities instead of 345, which reinforces the impression of a heavily fragmented municipal system.

The findings from both approaches of analysis developed in the first and second sections of the chapter (international comparison and changes over time) provide the strong basis to analyse municipal tools. The third section identifies the limitations of local finance mechanisms and makes proposals that aim to be instrumental in modernising and reinforcing the fiscal fundamentals of Chilean municipalities.

Finally, adjusting the current budgetary and fiscal framework to modernise and make municipalities more efficient and responsible is crucial. Reforms in this area should ensure greater transparency of municipal functioning, reinforce local elected representatives' responsibility and accountability and guarantee fiscal sustainability of public policies. Therefore, a specific and final section is entirely dedicated to the

definition of "prudential" policy rules that could apply to Chilean municipalities in the perspective of greater fiscal autonomy.

Financial weakness of public engagement and low decentralisation in Chile

Chile's choice of development model puts the country in a very unique situation compared to the other OECD countries. Chile has opted for the mix of two models: on the one hand, an economic model that trusts market mechanisms to distribute resources and that tends to limit public intervention; on the other hand, a political-administrative structure based on a strong centralisation viewed as a way to maintain stability and unity. The mix of these two characteristics shapes the possibilities and conditions under which local political responsibilities are carried out.

As a result, Chile's economic framework is conservative both in terms of fiscal public engagement and local government involvement. This is reflected in the weakness of public expenditure, investment, revenue and debt, both at national and subnational level, relative to the size of the population (per capita) and GDP.[1]

A low public sector financial commitment

Limited public expenditure and investment at the national level

Chile's total public expenditure is among the lowest of all OECD countries. In 2014, while OECD countries' public expenditure stood at an average of USD 16 080 per capita or 41% of GDP, Chile spent a mere USD 4 941 per capita, or 23% of GDP, on par with Mexico (Figures 2.1 and 2.2).

These figures stand in stark contrast with those in Northern and Western Europe, where a longstanding, social-oriented spending affects many aspects of inhabitants' lives. This is especially true in extreme cases such as Luxembourg and Norway (for very different reasons) where per capita GDP is unusually high. Most of Northern and Western European countries have per capita public expenditure figures of between USD 20 000 and USD 25 000. The United States, with USD 20 000 in public expenditure per capita, is at the low end of the range. Expressed as a percentage of GDP, the highest figures (between 44% and 58%) are well over double that of Chile (23%).

A comparison with other Latin American countries does little to alter the view that Chile's public expenditure is relatively low. The low ranking is, however, less marked due to the fundamental characteristics of countries in Latin America. Even when small countries (in terms of demographics and size) in Central America are excluded, Chile's modest public expenditure numbers are confirmed. More than in most countries, the use of the private sector to meet the needs of the population (education, healthcare, social protection) reduces the importance of the use of the public sector.

Figure 2.1. **Public expenditure in OECD countries (% of GDP, 2014)**

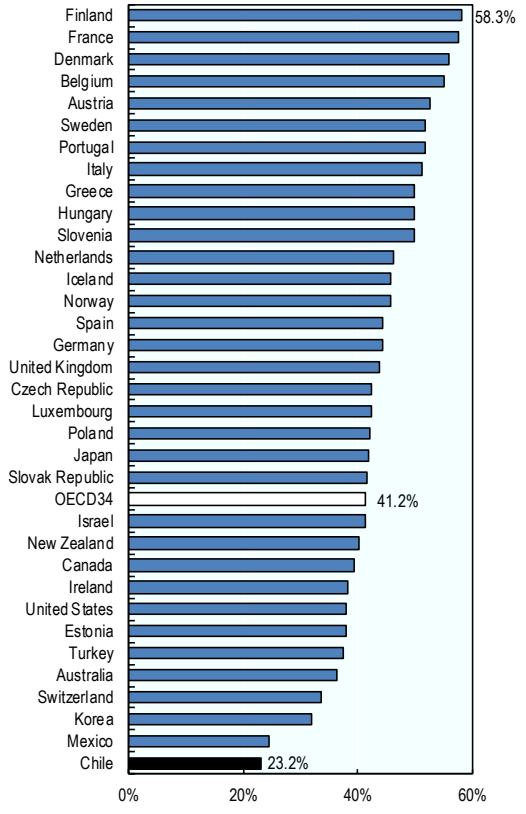
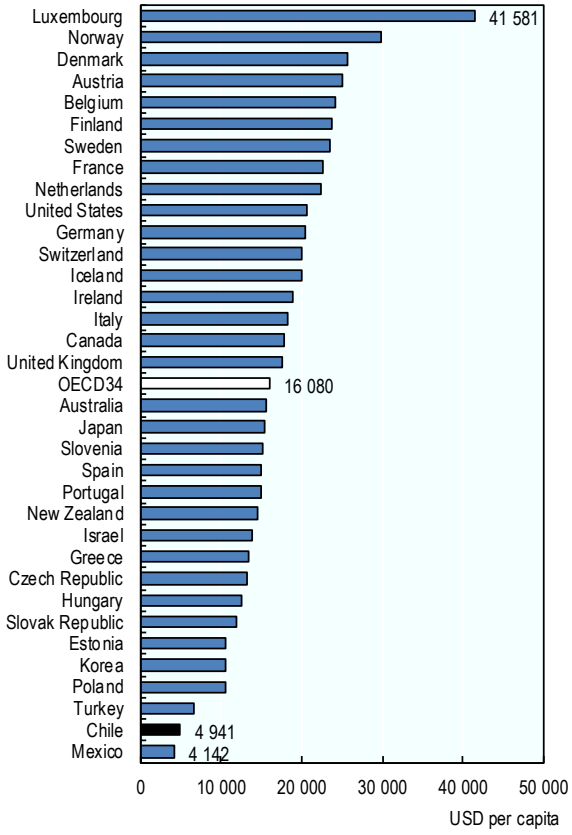


Figure 2.2. **Public expenditure in OECD countries (USD PPP per capita, 2014)**



Note: 2013 for Chile, Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. Data stated in local currency were converted in USD using purchasing power parity. OECD average is weighted.

Source: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

Weak public engagement in Chile is also reflected by trends in public investment. With a per capita public investment of USD 474 Chile ranks well behind the USD 1 240 average for OECD countries, again similar to the situation in Mexico (Figure 2.3). As a percentage of GDP, public investment in Chile is 2.2%, similar to that of Ireland, Portugal and Germany (versus a 3.2% average for OECD countries) (Figure 2.4).

Figure 2.3. **Public investment in OECD countries (USD PPP per capita, 2014)**

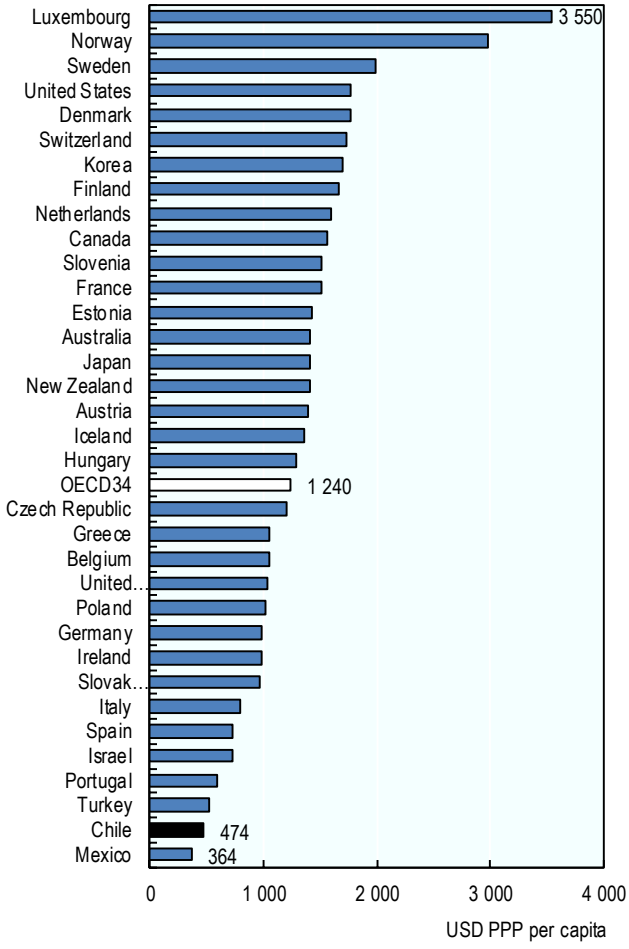
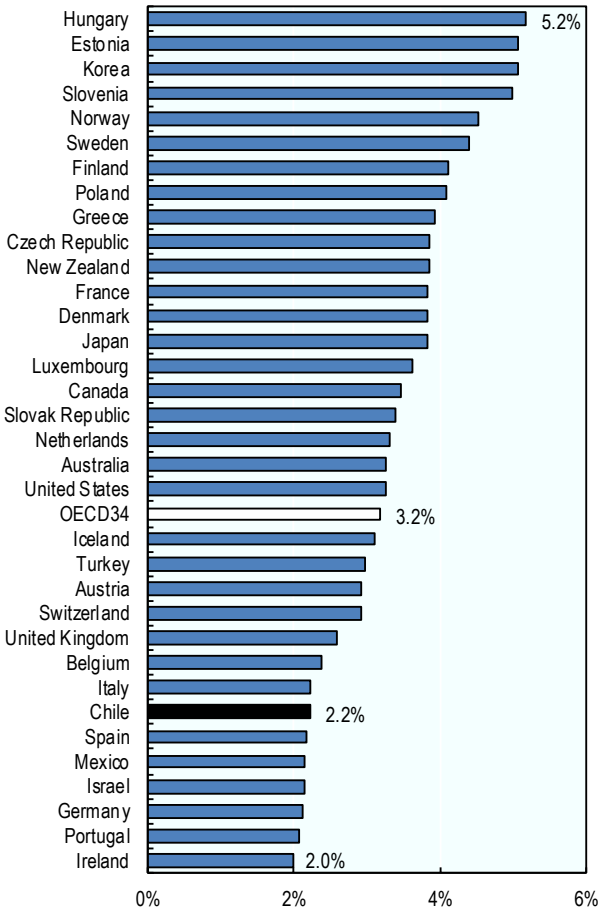


Figure 2.4. **Public investment in OECD countries (% of GDP, 2014)**



Note: 2013 for Chile, Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. Data stated in local currency were converted in USD using purchasing power parity. OECD average is weighted.

Source: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Editions) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

Weak public revenue

In 2014, Chile's public revenue was, with Mexico, the OECD Member State with the lowest public revenue. With 22.7% of GDP and USD 4 839, public revenue is well below the OECD average of USD 14 738 and 37.8% of GDP. What is different in Chile is public revenues' reliance on tax income, which is particularly high: 83% for an OECD average of 59% (Figure 2.5). Yet, tax revenues per capita and as a percentage of GDP were among the lowest in the OECD (except the extremely low level of Mexico) as shown in Figure 2.6.

Like expenditure, the weakness of Chile's ratio of public revenue compared with countries in Latin America seems less marked. At the end of the 1980s, a period of profound monetary, financial and fiscal disorder, most Latin American countries (albeit

not necessarily simultaneously) made the fight against inflation and a commitment to fiscal discipline a priority. The tax orientations that resulted from this period, the reinforcement of tax administrations and the improvement of macroeconomic conditions contributed to increasing the public revenue/GDP ratio. The gap between the average of all OECD countries and the average of Latin American countries shrunk between 1990 and 2000 by three points (from less than 18 to 15 percentage points). All countries' public revenue ratios increased significantly (with the notable exception of Venezuela where it has dropped precipitously): in Argentina the increase was 15 points, in Colombia 8 points. Against this backdrop, the 2-point rise in Chile (same for Mexico) seems paltry.

Figure 2.5. **Tax revenue as a % of public revenue in the OECD countries (2014)**

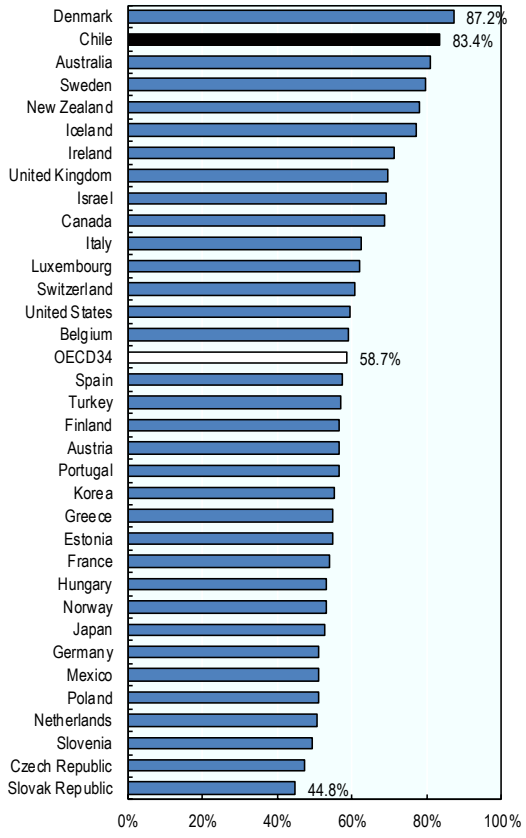
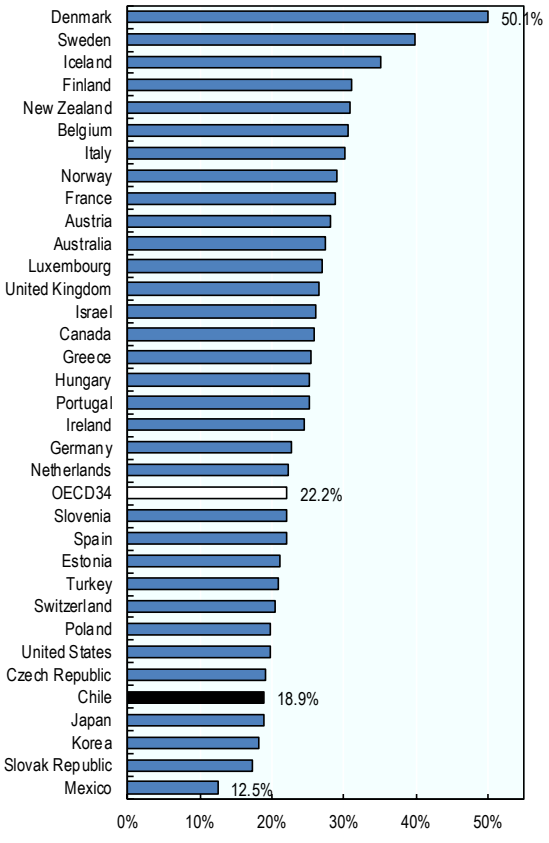


Figure 2.6. **Tax revenue as a % of GDP in the OECD countries (2014)**



Note: 2013 for Chile, Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. OECD average is weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

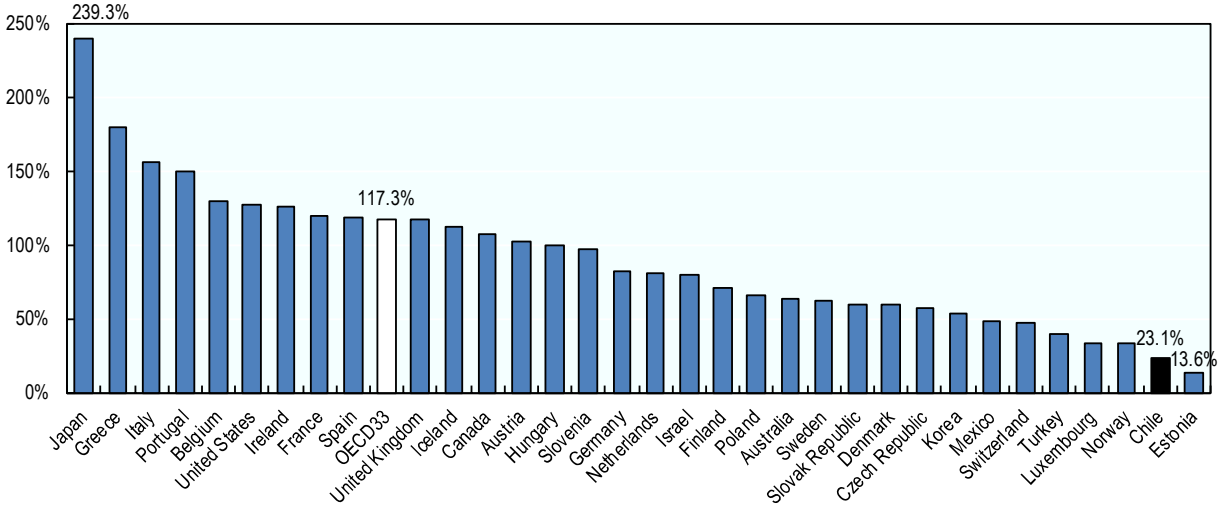
Minimal public debt

In Chile, public administrations' finance needs comply with the structural balance rules for public accounts, which reflects the country's strict management of its public finances. As a percentage of GDP, only seven countries managed to achieve a surplus in 2014 in the OECD, yet the average for OECD countries is negative, reaching 3.4% of

GDP. With a deficit of -0.5% in 2013, Chile has one of the healthiest fiscal balances among the OECD countries.

With regard to indebtedness,[2] Chile is extremely conservative when it comes to borrowing. Only Estonia, with a debt of 14% of GDP has a lower rate than Chile (23%). Chile's public debt rate is 10 points less than countries with strong public surpluses including Luxembourg and Norway and far from many European countries (especially the outliers such as Greece, Italy, Portugal or Belgium) or the United States or Japan (Figure 2.7). Not surprisingly, public debt in Chile is by far the lowest in Latin America. Chile's fiscal discipline[3] and commitment to balancing the budget make the country a case study in the effects and demands of such a strategy.

Figure 2.7. **Public debt as a % of GDP in the OECD countries (2014)**



Note: 2013 figures Switzerland, Mexico, Iceland and Israel; 2011 figures for Japan; SNA 1993 consolidated for Turkey and Canada; SNA 1993 non-consolidated for Chile and Japan; SNA 2008 non-consolidated for Korea, United States, Switzerland and Mexico. OECD average is weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

The financial confinement of local government in Chile

In Chile, subnational government expenditure and revenue are concentrated at the municipal level, unlike the situation in many other two or three layered subnational government countries of the OECD, federal or unitary, where the share of regions in subnational expenditure is significant. In Chile, the regions do not have yet a financial existence distinct from that of the central government. As far as municipalities are concerned, they have little room to embark on independent initiatives due to the centralised nature of the public financial system.

Modest local expenditure and investment

Low overall public expenditure is even lower at the local level. Municipal spending per capita stands at USD 648, which is nearly 10 times less than in the OECD countries on average and similar to levels in Turkey and Greece (Figure 2.8).

Figure 2.8. **Subnational government expenditure per capita in OECD countries (USD PPP, 2014)**

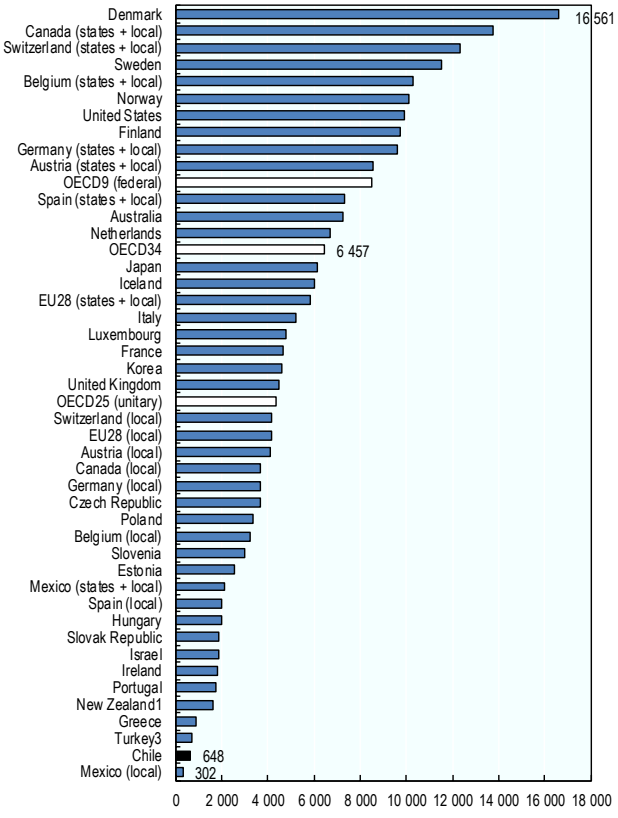
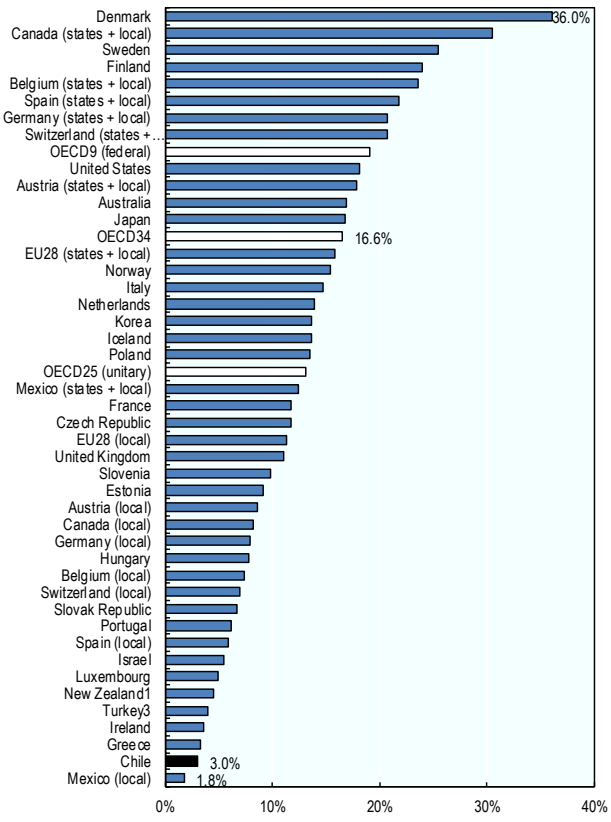


Figure 2.9. **Subnational government expenditure as a % of GDP in OECD countries (2014)**



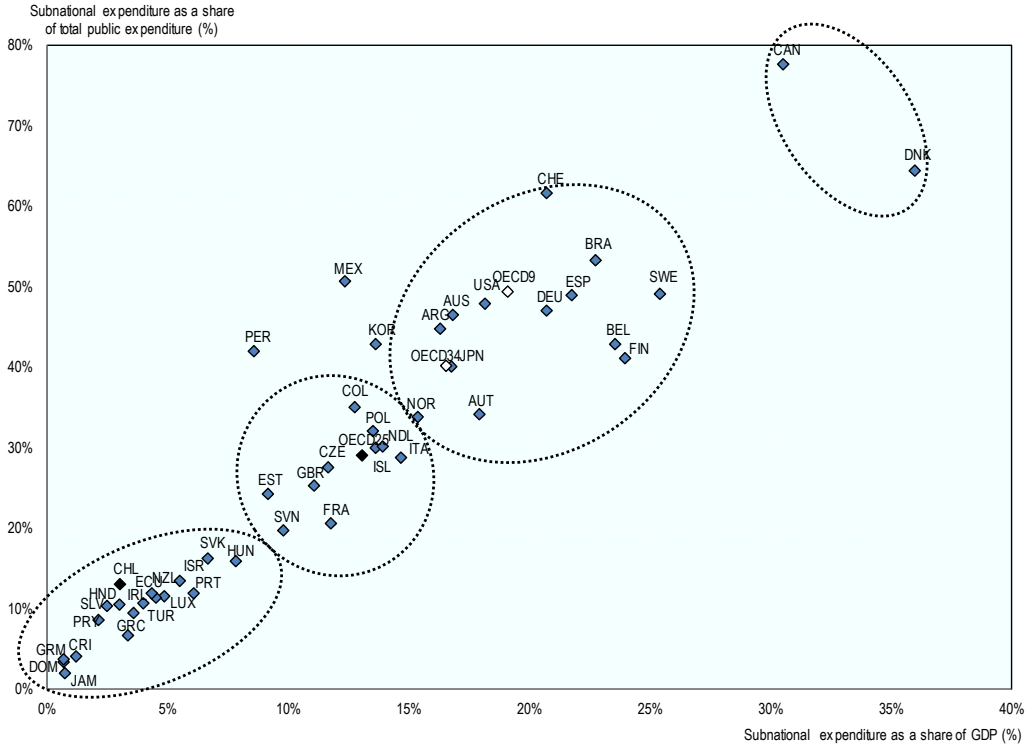
Note: 2013 for Chile, Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. Data stated in local currency were converted in USD using purchasing power parity. OECD average is weighted. OECD25 = unitary countries average: OECD9 = federal countries average.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

As a percentage of total public expenditure and GDP, municipal spending is also low in Chile, further underscoring the perception of Chile as a highly-centralised country. For the average of OECD countries, subnational expenditure accounts for 40.2% of total public expenditure and 16.6% of GDP in 2014, while it reached 13.1% of public expenditure and 3.0% of GDP in Chile, close to other centralised countries such as Greece, Slovenia, Turkey, Ireland or New Zealand where local governments have limited competencies and spending capacity (Figures 2.9 and 2.10). At the extreme opposite, we find most federal countries, with Canadian subnational expenditure reaching almost 31% of national GDP and 78% of public expenditure. In federal countries, subnational expenditure is the sum of the state and local governments, which explains the high ratios. However, we also find several unitary countries where local expenditure is an important share of public expenditure such as in Japan and several Nordic countries. In Denmark, for example, local expenditure amounted to 36% of GDP and 64% of public expenditure in 2014 due to the fact that municipalities administer a number of social security

transfers. Chile's ratios are also among the weakest in Latin America. However, the level of local expenditure in Chile is higher than in Mexico and Argentina when considering the local level only as in these federal countries, subnational expenditure is concentrated at the federated state level. In Mexico for example, purely municipal expenditure (i.e. without Mexican states expenditure) is twice as low versus Chile (USD 302 and 1.8% of GDP), which reflects the weakness of Mexican municipalities. It is not the case in Brazil where municipal expenditure represented 9% of GDP and 21.1% of public expenditure. But Chile lags far behind Peru and Colombia, two unitary countries (Figure 2.10). Chile is also among the most centralised countries in the world, despite a per capita GDP of around 22 000 USD PPP (Box I.1 in the General introduction).

Figure 2.10. **Subnational government expenditure as a % of total public expenditure and as a % of GDP in OECD and selected Latin American countries, 2014 (2013 for Latin American countries)**



Note: 2013 for Chile, Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. OECD averages are weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database); OECD/UCLG (2016), *Subnational governments around the world: Structure and finance.*

The low level of local public investment in Chile underlines the extent to which public action is centralised. At USD 57 per capita or 0.3% of GDP, Chile's local investment is last among all OECD countries (Figures 2.11 and 2.12). Local investment represents 8.7% of total local expenditure vs. an OECD average of 11.3%.

Figure 2.11. **Subnational government investment per capita in OECD countries (USD PPP, 2014)**

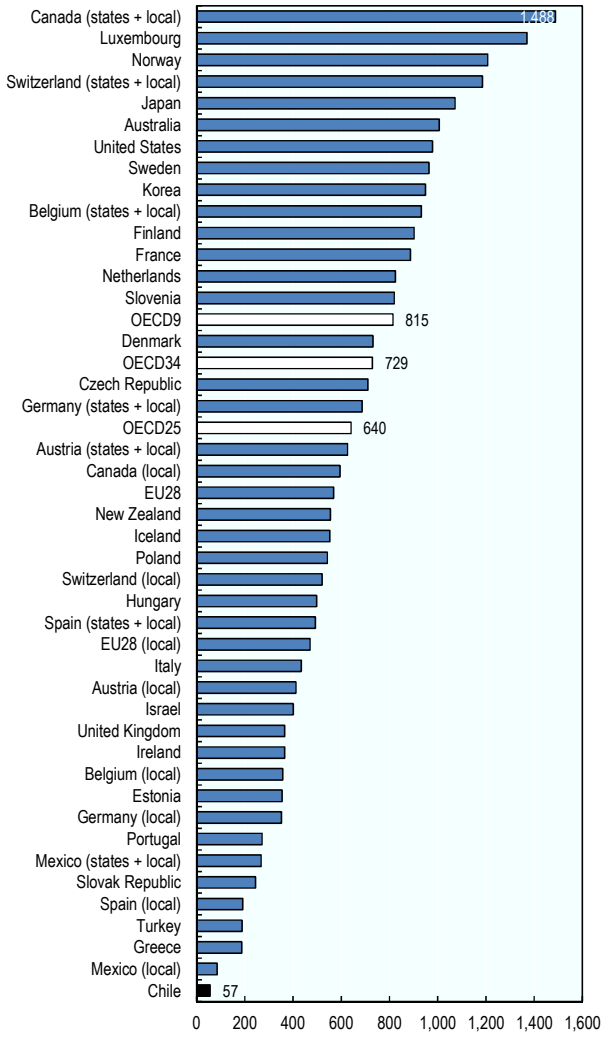
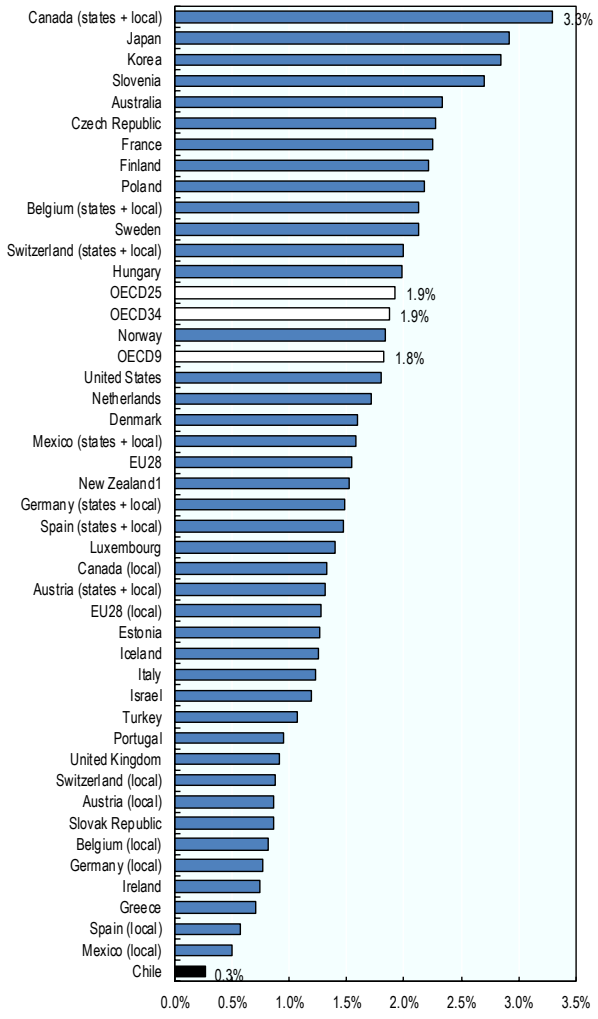


Figure 2.12. **Subnational government investment as a % of GDP (2014)**



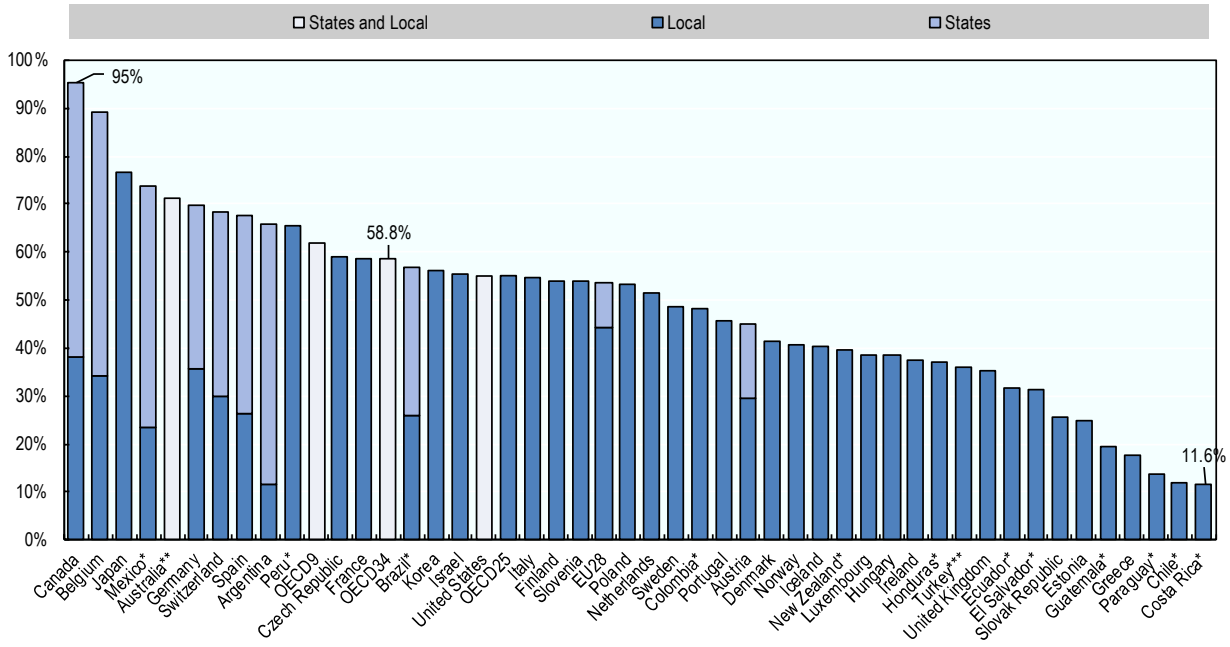
Note: 2013 for Chile and Mexico and New Zealand, 2012 for Australia and 2011 for Turkey. OECD averages are weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database); OECD/UCLG (2016), *Subnational governments around the world: Structure and finance.*

As a share of public investment, local investment is very low in Chile, representing 12% of total public investments. It stands in stark contrast with the average for OECD countries. Indeed, subnational governments play a key role in public investment in most OECD countries. In 2014, they carried out around 59% of public investment in the OECD area. This ratio tends to be higher in federal countries where it combines investments by the federated states and by local governments but it can be high in unitary countries such as Japan and France. Compared with other Latin American countries, Chile also ranks

among the last, just ahead of Costa Rica but on par with Argentinian municipalities (Figure 2.13).

Figure 2.13. **Subnational government investment as a % of public investment in OECD countries and selected Latin American countries (2014)**



Note: 2013 for Latin American countries and New Zealand, 2012 for Australia and 2011 for Turkey. OECD averages are weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database); OECD/UCLG (2016), *Subnational governments around the world: Structure and finance.*

The spectre of shrinking local revenue

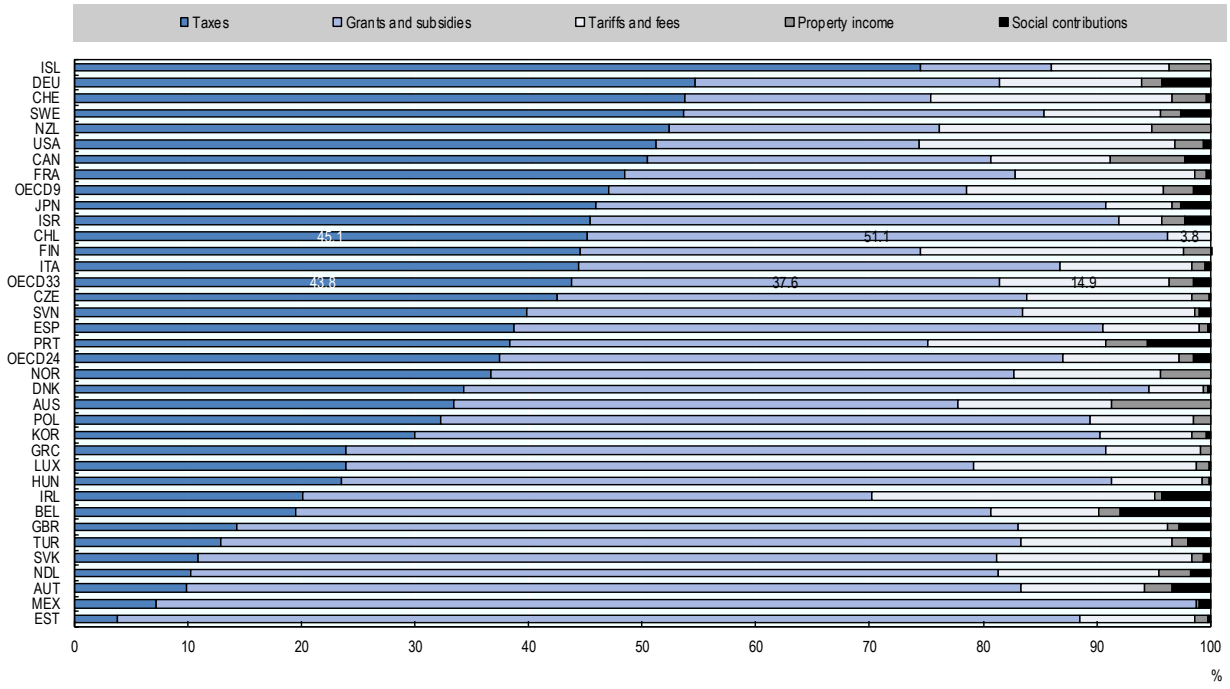
In correlation with total expenditure, subnational public revenue in Chile is among the weakest regardless of the indicator: USD 676 per capita or 3.2% of GDP, whereas the OECD averages are USD 6 241 or 16%. Likewise, Chile's subnational public revenue constituted 14% of public revenue, whereas the OECD average was three times as high (42.3%).

While tax revenue makes up a significant portion of public revenue for the central government in Chile, the subnational level's means of generating public revenue are different compared with other OECD countries (Figure 2.14):

- Greater reliance on grants and subsidies (51.1% of municipal revenue vs. 38% in the OECD) which reflects subnational governments' subordination to the central government.
- A marginal contribution from other revenue streams (tariffs and fees, property income and social contributions). They account for 3.8% of public revenue at the subnational level vs. nearly 19% for the average of OECD countries. In Chile, they are almost non-existent compared to other OECD countries.

- However, among subnational revenues, the percentage of tax revenues (45%) is similar to that of a number of other OECD countries, and slightly above the OECD average (44%).

Figure 2.14. **Structure of subnational government revenue (%, 2014)**



Note: 2013 for Latin American countries and New Zealand, 2012 for Australia and 2011 for Turkey. OECD averages are weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 Edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database); OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*.

What sets the Chilean local level apart is that it is one of the lowest in the OECD with regard to the extent to which tax revenues supply the local coffers and yet, at USD 305 per capita, it is higher than that of other countries (Estonia, Greece, Czech Republic and Turkey). In those countries, tax revenues, however, are bolstered by other sources of revenue including grants and fee-based revenue sources as well as other forms of tax, which – taken together – strengthen the firepower of their local budgets. The local sector in Chile does not have this leeway and finds itself squeezed by tax revenue that account for a mere 1.4% of GDP (OECD average: 7.0%) and 7.6% of public tax revenues (OECD average: 31.6%), as shown in Figures 2.15 and 2.16.

Figure 2.15. **Subnational tax revenue as a % of GDP in OECD and selected Latin American countries**

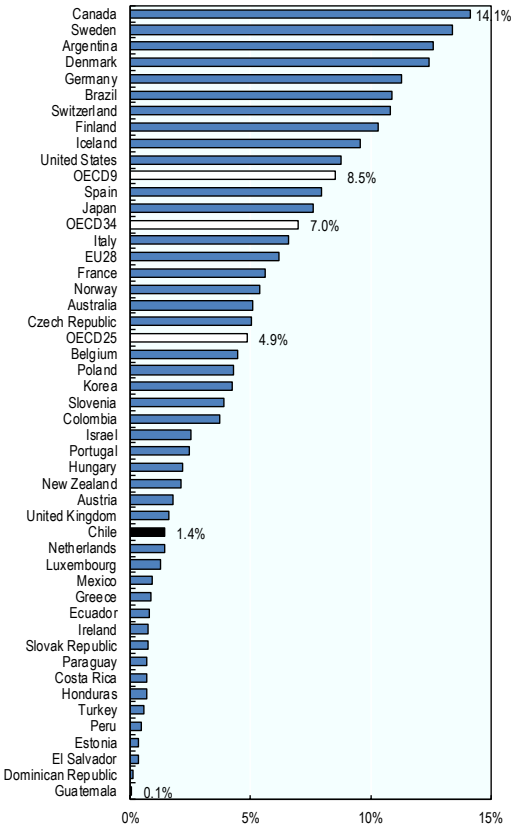
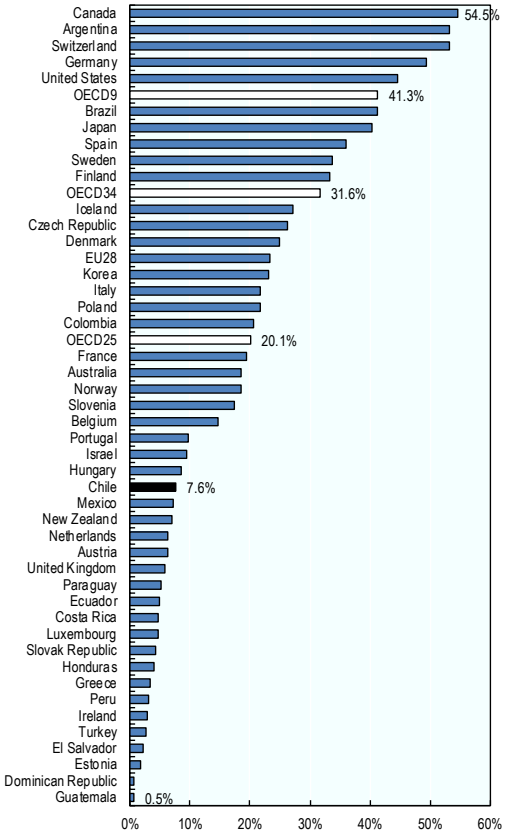


Figure 2.16. **Subnational tax revenue as a % of public tax revenue in OECD and selected Latin American countries**



Note: 2013 for Latin American countries and New Zealand, 2012 for Australia and 2011 for Turkey. OECD averages are weighted.

Sources: Created by the authors based on OECD (2016d), *Subnational governments in OECD countries: Key data* (2016 edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database); OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*.

A comparison with the situation of subnational public revenue in other Latin American countries underscores the impact of the lack of an intermediary level of governance in Chile with budgetary power. As a percentage of consolidated public revenues, the central government of Chile is in a dominant position (92.5%). Consequently, the amount of local taxes raised is relatively low, situating the country in the middle of the pack among the other countries of the southern cone (dominated by the major federal countries) and the countries in the Andean region.

Is local debt insignificant?

In 2013, local public administrations had a capital account surplus and were in a better position than public administrations at the central level. The balance of local budgets was in surplus by +0.1%, which contributed to the health of public administrations as a whole. It is highly likely, although it is impossible to determine from

the macroeconomic statistics, that the debt level of local authorities in Chile – unlike in other countries – is around zero. It is highly probable that local public debt is very low given that overall public indebtedness is very low to begin with. In addition, Chile has highly restrictive regulations regarding access to credit to finance local budgets. These restrictions are more severe than in many other countries. Municipalities are not allowed to borrow funds according to the Constitution and the LOCMUN, although use of short-term floating debt (commercial debt), leasing and leaseback operations and other forms of "hidden debt" are common. The same restrictions apply to municipal corporations.

In conclusion, in good financial stead with its fiscally strict framework, local Chilean authorities appear, compared to their counterparts in OECD countries, to be lacking resources and lacking a real ability to act. All public finance indicators (national or local) underscore the extent to which Chile is a centralised country. The local sector plays a limited role, especially compared to many other Latin American countries or OECD members.

Yet, Chile is in an enviable position in terms of the quality of life of its citizens and the social services that are offered to them thanks in part to its delivery of social services and its emphasis on trade and commerce. Chile has one of the lowest rates of dissatisfaction with social services (30%, i.e. one of the lowest in Latin America topped by only Costa Rica and Panama). Chile's score on the Human Development Index (HDI) is indicative of the progressive social situation in the country without masking the numerous inequalities (social, territorial, gender). In 2015, Chile was ranked 42nd out of 188 countries evaluated (data from 2014). It is part of the group of countries with 'very high human development' and is, alongside Argentina, the lone representative for Latin America in this category (UNDP, 2015).

Trends in municipal finances in Chile

Given the lack of access to relevant and uniform data, international comparisons are more often than not limited to macroeconomic observations. The comparisons are limited to robust yet basic observations that do not allow researchers to draw historical comparisons of the underlying trends that are sometimes slow in developing while broader ratios seem to not fluctuate at all.

The only way to decipher these trends is by conducting a longitudinal analysis of local revenue and expenditure over a relatively long period. By focusing on a shorter period it is possible to take a more granular look at the budget items and to identify instructive structural changes and trends.

This analysis is conducted by combining two sources of information. First, the past data collected by the *Dirección del Presupuestos* (DIPRES), which covers a quarter century (1990-2015). Second, in a different perspective and over a shorter time period covering the past five years (2011-2015), data from the *Sistema Nacional de Información Municipal* (SINIM),[4] which is part of the SUBDERE, shed light on the transformations in the composition of revenue streams and in the nature and areas of expenditure.

Unsteady but significant progression of municipal budgets over a long period (1990-2015)

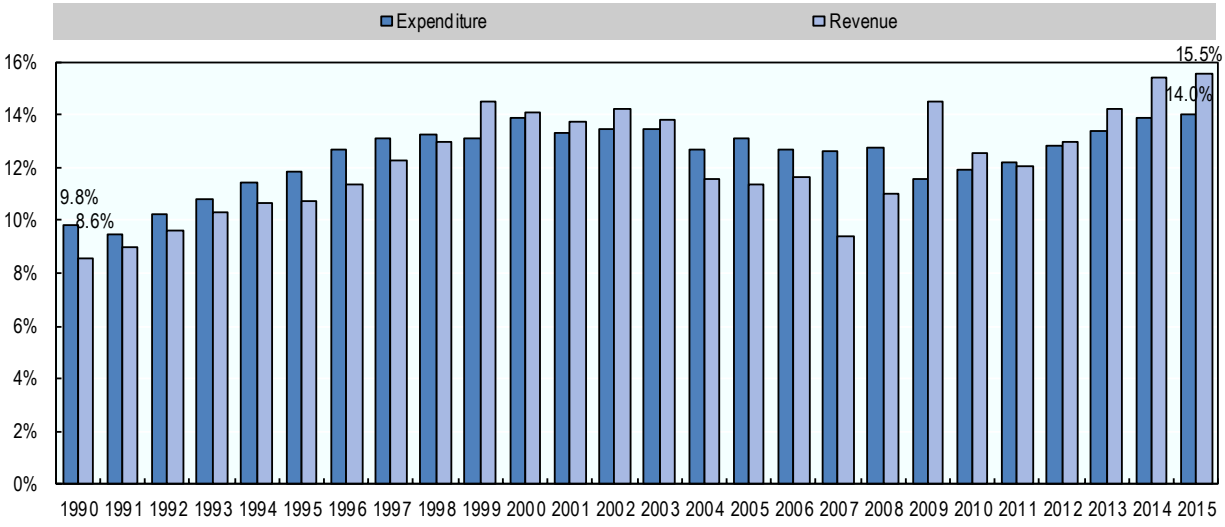
Over the lengthy period stretching from 1990 to 2015, municipal operations (revenue and expenditure) - as reflected in data gathered and compiled by DIPRES - are analysed both in volume terms and relative to financial data collected by the Consolidated General

Government (CGG), which aggregates financial data from the central government and municipalities. Over a quarter century, data expressed in local currency are magnified by high inflation over the first decade of the period. The expansion (in nominal terms) is driven by a monetary illusion whereby municipal expenditure in Chile expanded from CLP 209.3 billion in 1990 to CLP 5 563.6 billion in 2015, i.e. an increase of 27 times. The following observations will use figures that are deflated in 2015 CLP as a baseline. Through this technique, municipalities' fiscal expansion is brought into more reasonable proportions, i.e. less than seven times. With rising prices eliminated, per capita figures correct for the demographic expansion of the country. Between 1990 and 2015, the population of Chile increased 36.5%, swelling from 11.3 million inhabitants to around 18 million. In real terms, municipal expenditure per inhabitant in 2015 was 4.9 higher than in 1990.

This substantial expansion should be put in perspective regarding the fiscal sums that the operations of the general government (central government and municipalities) represent and especially the country's rising wealth, which can be seen by the increase in GDP. The increasing weight of the municipal sector over the quarter century is tangible.

As a share of general government expenditure, municipal expenditure increased from 9.8% to 14.0%[5] (Figure 2.17).

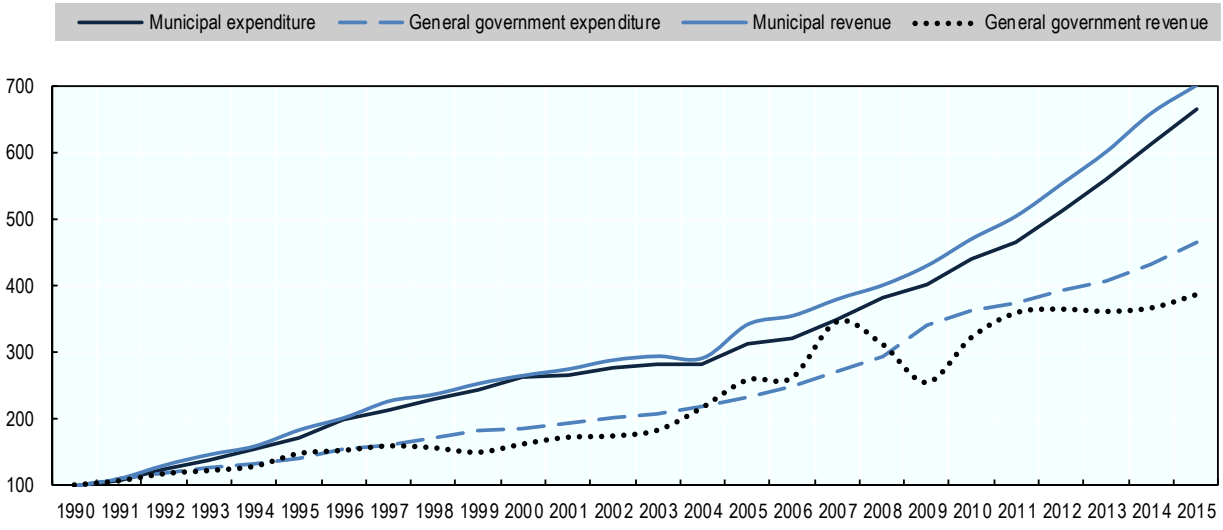
Figure 2.17. **Change in the share of municipal expenditure and revenue in total general government**



Source: Created by the OECD based on DIPRES (2015) - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto.*

In real terms, the increase of municipal expenditure is also significant compared to that of the general government as a whole, i.e. an annual increase of 7.9% in real terms for the local government over the 1990-2015 period compared to 6.4% for the general government (Figure 2.18).

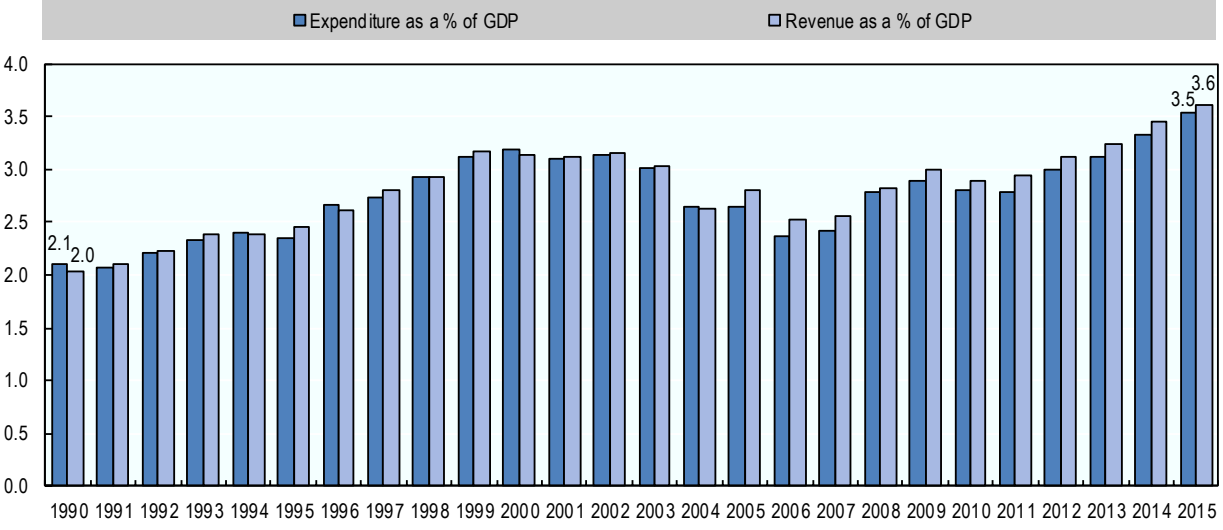
Figure 2.18. **Change in municipal and general government expenditure and revenue 1990 – 2015 (constant 2015 CLP, base 100 = 1990)**



Source: OECD based on DIPRES - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto.*

In terms of GDP, the increase is, however, more limited (1.4 point for expenditure and 1.6 point for revenue) and does not reflect a mass deployment of means by municipalities (Figure 2.19).

Figure 2.19. **Change in municipal expenditure and revenue as a % of GDP over 1990 – 2015**



Source: Created by the OECD based on DIPRES - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto.*

Limited municipality expenditure in terms of GDP reflects the political decision to keep a tight lid on the expansion of public expenditure in the economy and society. However, although municipal expenditure/general government expenditure expanded less

quickly, this gain is more significant. In an environment of restrained public intervention, the municipalities are gaining ground. The weight of central government expenditure remained, nevertheless, preponderant at the end of the period.

The changes that took place over this period were unsteady and, with varying intensities, they were mostly parallel for expenditure and revenue, due to budget balance rules across the various periods. However, structural trends in the composition of municipal budgets can be identified amid the fiscal expansion.

Municipal budget operations: An unsteady trend

The trend in municipal revenue and expenditure is far from linear. They have a similar profile over time, reflecting alternating phases of acceleration and slowdown. Their annual growth rates are up and down because their sensitivities to the national economic situation are different (variation of inflation rate and growth).

Some years were marked by expanding revenue while for others expenditure outpaced revenue.

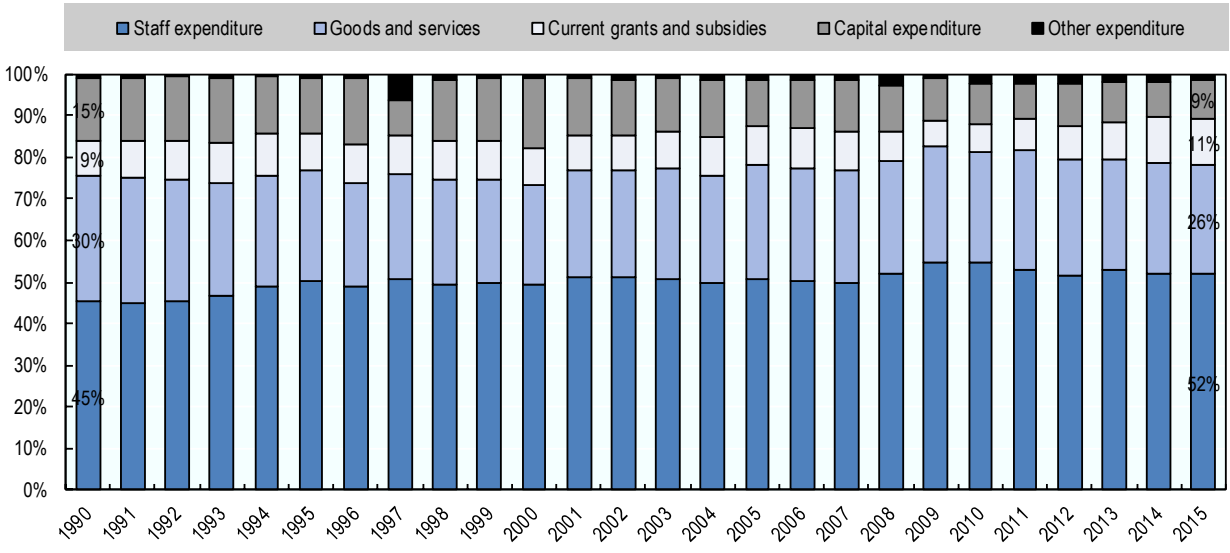
- Phase 1 covers the 1990s. Municipal revenue was strong in volume terms (always more than 10% per year) amid a context of high inflation. Although expenditure did not increase as quickly as revenue, the rise as a percentage of GDP was even more incremental. From 2.1% in 1990, spending topped 3.2% of GDP in 2000. At the same time, municipal revenue rose from 2% to 3.1%, resulting in a sharp increase in tax revenue (see below) from 1.1% to 1.5% of GDP.
- Phase 2 covers the 2000s, approximately, and includes two types of disruptions that marked the period 2003-2004 and the economic crisis that marked the end of the period (2009 primarily). The weight of municipal expenditure regressed significantly. Over the course of these ten years, the trend was thrown off balance,[6] which reflected greater GDP swings than before. This was seen after a marked drop in expenditure in 2006 and 2007 (2.4% of GDP) and a spectacular rebound in 2008 and 2009 as growth sagged during the global economic crisis.
- Phase 3. Since 2010, economic growth has slowed compared to the fast-growth 2000s, automatically leading to higher revenue and expenditure activity at the municipal level. From 2.8% of GDP in 2010, municipal expenditure rose to 3.5% in 2015. At the same time, the weight of revenue inched higher from 2.9% to 3.6% of GDP (1.3% to 1.6% for tax revenue).

During this period of fluctuation, municipal operations changed in ways that were different from the progression of central operations. At the start of the period (1990-1997), the pace of growth of central government operations was slower than local operations. This was most likely due to the use of the central government's budget to intervene in the economy. Central revenue and expenditure has tended to be subject to more marked fluctuation than its local counterparts. Consequently, compared to the state, the local authorities saw their share of revenue increase steadily until it came to a halt during the unstable period of 2004-2007. In 2015, municipal revenue was the equivalent of 15.5% of the general government, significantly higher from where it was 25 years earlier (8.6%). For expenditure, the same increase can be observed but at a less unsteady pace. The disturbance in the mid-2000s, which was marked for revenue, was hardly noticeable for expenditure.

Structural redistribution of municipal expenditure

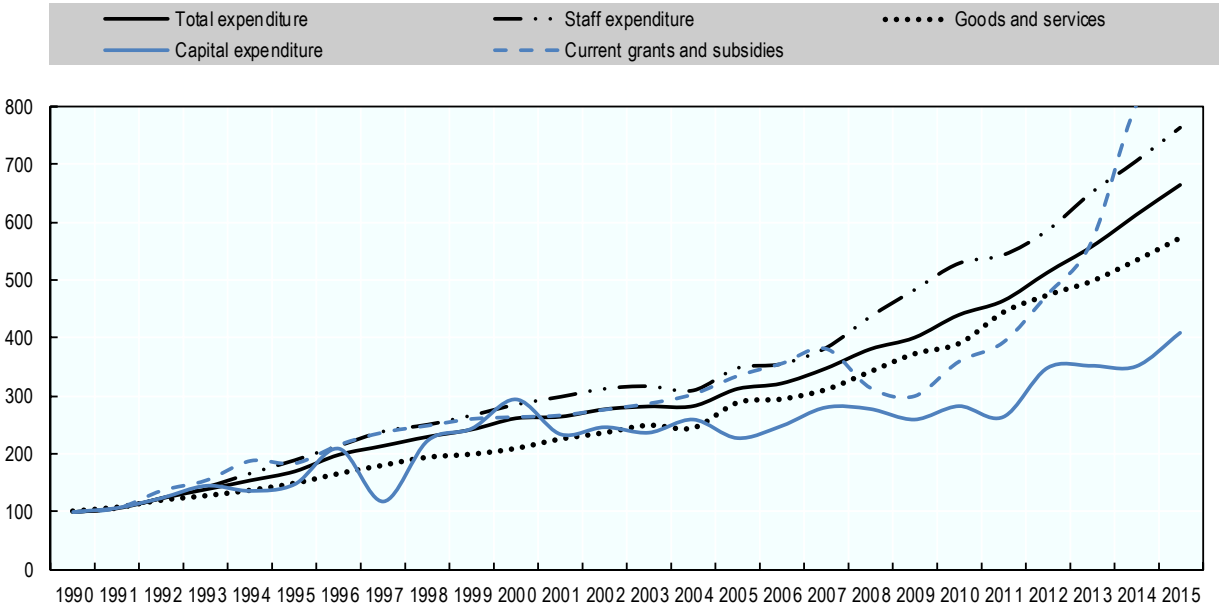
While staff-related costs is the biggest line item, their share, as a percentage of total municipal expenditure, increased regularly, with some ups and downs however over the period, from 45% in 1990 to 52% in 2015. This weight of staff expenditure results from the fact that municipalities are in charge of paying staff in the education and health sectors. In real terms, personnel expenses have had the strongest changes (+8.5% per year in real terms[7]), after that of current grants and subsidies (+9.1%). In fact, at the end of this period, (paid) current grants and subsidies, which had fallen sharply in 2008 and 2009 regained ground, to reach 11% of municipal expenditure in 2015 (vs. 9% in 1990). They seem to follow a more unsteady path with greater fluctuation than the other items. Unsurprisingly, capital expenditure has also had great variations over the period, with annual ups and downs, reflecting the high volatility of investment. Although capital expenditure grew by 5.8% per year in real terms, this progression was the lowest of all other expenditure items. As a result, capital expenditure as a percentage of total municipal expenditure fell from 15% in 1990 to 9% in 2015. As for (paid) current grants and subsidies, capital expenditure seems to play the role of an adjustment variable whenever economic headwinds create turbulence for municipal budgets. The share of intermediary consumption expenditure (goods and services) has also fallen steadily, from 30% of municipal expenditure in 1990 to 26% in 2015. In real terms however, it increased by 7.2% per year.

Figure 2.20. **Change in composition of municipal expenditure 1990-2015 (% of total municipal expenditure)**



Source: Created by the OECD based on DIPRES - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto.*

Figure 2.21. **Change in composition of municipal expenditure 1990-2015 (constant 2015 CLP, base 100 = 1990)**



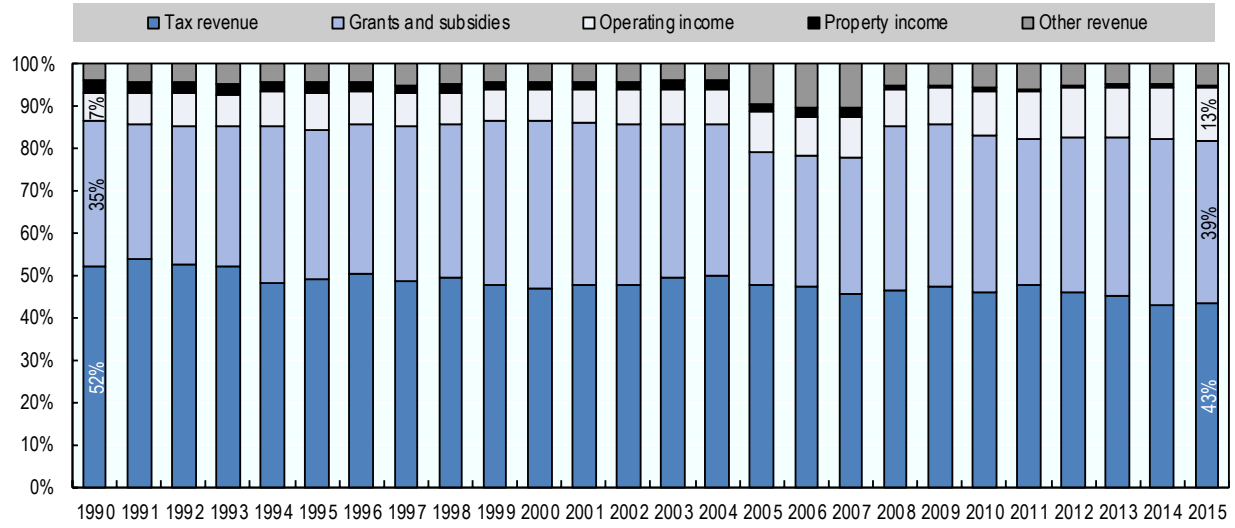
Source: OECD based on DIPRES - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto.*

Structural change in municipal revenue structure

Municipal revenue's rollercoaster ride was accompanied by a change in the composition of its resources, including three trends during this long period:

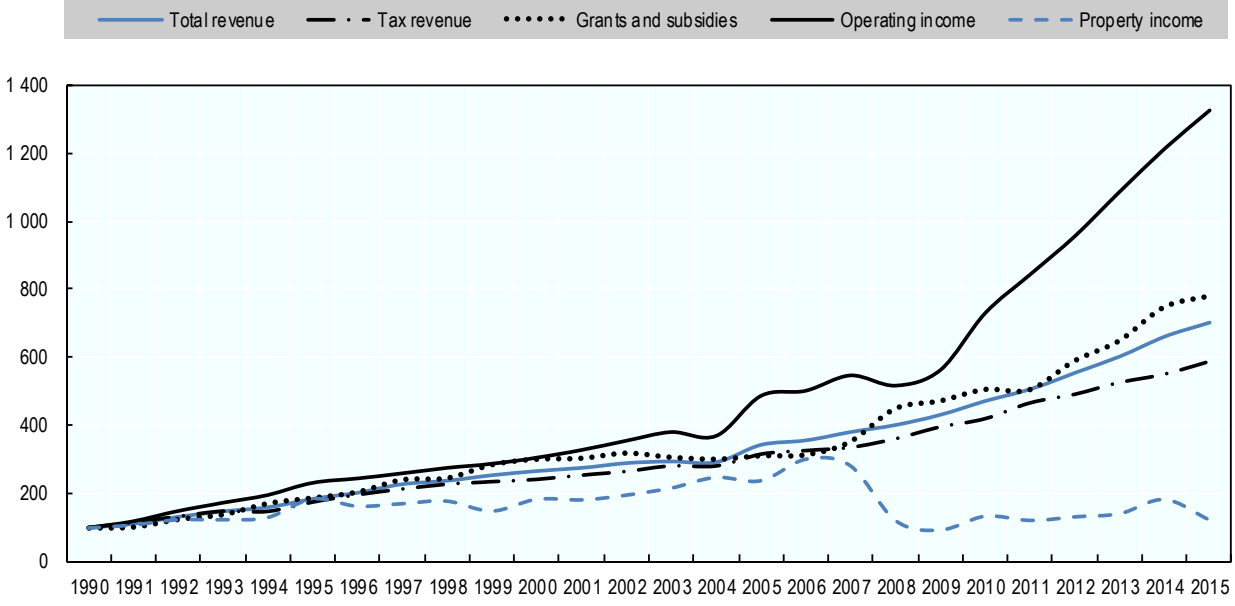
- Steady drop in tax revenue as part of total revenue. Accounting for more than half of municipal revenue in 1990 (52.5%), the relative weight fell over the period to 43.4% in 2015 (Figure 2.22). Tax revenue however grew by 7.3% per year in real terms from 1990 to 2015 (Figure 2.23).
- The growing importance of grants and subsidies. Except for 2005-2007, which were characterised by a substantial reduction in transfers (down to 32%), in 25 years their weights increased to climb from 35% of municipal revenue in 1990 to 39% in 2015. For years that break with this trend, the annual growth rates for grants and subsidies of 8.6% (on average annually) varied tremendously. This high instability was the consequence of variations in the budget of the central state that is responsible for these transfers.
- The growing importance of operating income. Minor in 1990 (7% of revenue), its weight increased steadily to almost 13% in 2015. This progression reflected a more active management by municipalities and an extension of the range of activities that could generate tariffs and user fees. The movement was not, however, linear. Robust over the 1990-1995 period, operating income slowed (as did other revenue) before picking back up again at a fast pace.
- However, property revenue (rents and the sale of assets) has inexorably moved to the sidelines of the municipal revenue structure. From less than 2.7% of revenue in 1990, it fell to less than 0.5% in 2015.

Figure 2.22. **Change in structure of municipal revenue 1990-2015 (% of total municipal revenue)**



Source: OECD based on DIPRES - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto*.

Figure 2.23. **Breakdown of municipal revenue 1990-2015 (constant 2015 CLP, base 100 = 1990)**



Source: OECD based on DIPRES (2015) - *Estadísticas fiscales, Estado de operaciones del gobierno general, municipalidades, 1990-2015, moneda nacional. Transacciones que afectan el patrimonio neto.*

Ongoing transformation of municipal budget structures over recent years (2011-2015)

Over recent years (2011-2015), Chilean local finance reflects the tensions resulting from the centralisation of territorial public policies. With limited resources and reduced political autonomy, overall, municipalities encounter difficulties to face their

responsibilities. This is expressed by the contrasting financial changes which are linked to a fragmented fiscal budgeting system at the local level.

A fragmented fiscal organisation at municipal level

The current assignments of spending responsibilities and revenues competences goes back to the Pinochet regime, in particular the municipal Act of 1981, modified by two other laws:

- The Organic constitutional municipal Law No. 18.695 of 1988 (Ley 18.695 Orgánica Constitucional de las municipalidades, LOCMUN).
- The decree-law on municipal revenues No. 3.063 of 1979 (decreto-ley No. 3.063 sobre las rentas municipales), revised in 1995 and 2005.

From the implementation of these acts, three main characteristics emerge.

In formal terms, the areas of municipal intervention are vast. According to article 1 of the LOCMUN No. 18.695, their purpose is "to meet the needs of the local community and ensure their participation in the economic, social and cultural progress of the respective *comunas*". The LOCMUN defines 6 exclusive and 13 non-exclusive/shared functions for municipal intervention (see Chapter 1).

Among the shared competences are two major responsibilities, transferred in the 1980s and which are particularly sensitive, politically, socially and economically: primary and secondary education and basic health services. Despite being "decentralisation laws", these regulations leave little autonomy to municipalities whose functions are to implement national policies. These functions are better defined as deconcentrated or delegated functions than truly decentralised functions. The financing of these two responsibilities comes from central administration transfers based on subsidies for benefits granted and coming from the ministries in charge.

In the education sector,[8] the per-student subsidy transferred directly to the municipality is not sufficient to cover the costs in many rural municipalities, despite improvements brought by the Inclusion Law and recent increase in education subsidies favouring preferably the municipal sector. In fact, municipalities do not receive specific funds to cover the administrative costs of managing their set of schools e.g. to cover the costs of municipal staff working in the municipal education department (Santiago, P. et al. forthcoming). Municipalities therefore have to supplement the national voucher with local resources. Larger and wealthier municipalities have the resources to have well-qualified staff, while smaller and poorer municipalities, with fewer pupils and vouchers, find it more difficult to finance public education and manage and meet the technical needs of the school system. Despite some improvements in 2006, this situation creates challenges to a number of rural communities given the presence of fewer students and fewer own-resources. In fact, rural regions faced with these challenges have high drop-out rates before secondary school. Clearly, there is a significant gap in the quality of education between rural and urban regions and the gap has not narrowed in recent years (OECD, 2014a).

In the health sector, the situation is similar. The per capita grants for these services do not cover the costs of delivering health services, which are often higher in rural and remote areas because of differences in density and distance. Municipalities have to complement the financing with other revenues. Since rural municipalities typically have lower incomes, they are less able to top up the national grant and, consequently, the

quality of healthcare is lower. Highly correlated with the level of municipal income, the result is a large variability in the quality of healthcare across the country.

In addition to these two main areas, the central government tends to regularly increase tasks assigned to municipalities, in sectors such as social assistance, civil protection or environmental protection (see Chapter 1), which are not compensated by sufficient spending, adding to the structural deficits and "hidden debt" (see below).

In the end, municipalities have a very broad spectrum of functions. However, in practice, municipalities are faced with numerous technical, managerial and financial constraints and limitations, especially in rural areas, that reduce the real level of municipal intervention and autonomy. In some areas, municipalities cannot intervene despite the huge needs and municipal legitimacy to do so. For example, the Word Bank has observed shortcoming in terms of utilities and their networks (water distribution, gas, sanitation, transport). Often, such services are carried out by private companies under concession agreements (World Bank, 2011).

The budgetary architecture is divided into three sectors

As a budgetary expression of legal (competences) and administrative (organisation of services) aspects, municipal accounts reveal the territorial dynamics underway and use an ad hoc nomenclature that simplifies but also quantifies the actual commitment. The SINIM's aggregation of local accounts identifies three main areas of local government activity:

- The municipal sector (*municipalidades)* covers the budgetary operations of normal municipal activities. The activities are reviewed concerning their nature (personal expenditure, goods and services, transfers, investment, etc.) and their scope of application. Municipal sector operations were the biggest line item in 2015 i.e. around 51% of total municipal expenditure and revenues. Areas identified in the SINIM include, by order of budgetary importance, municipal internal management (the most important area, accounting for around 29% of municipal expenditure), community services (waste collection, public lighting, water, upkeep of public spaces i.e. around 17%), social programmes and benefits (3%), recreational and cultural programmes (1.3%) and municipal activities (celebrations, inaugurations).
- The education sector involves operations linked to primary and secondary schools and school-related activities. The education sector represented around 32% of total municipal expenditure and revenues.
- The healthcare sector includes operations involving the provision of health-related services and basic care (operations by nature). It is the smallest one, representing around 17% of total municipal expenditure and revenues.

A fourth area of intervention exists: cemeteries (*cementerios)*, which is unique because it is only available in a small portion of the 345 municipalities in Chile. In fact, the vast majority does not provide cemetery-related services or do not distinguish the activity. For these reasons (concentration and small size of budget), cemeteries are not included in this analysis.

Municipal corporations add additional complexity to the municipal system (see also Chapter 1). Some municipalities (mainly the largest ones) use municipal corporations to administer and manage education and health services (rarely culture, sport and leisure

activities) substituting for municipal departments or services. Due to the lack of a consolidated approach at the municipal level, actual financial commitments remain unclear.[9] This situation is unsatisfactory in terms of financial and democratic transparency and also for budgetary data comparability.[10]

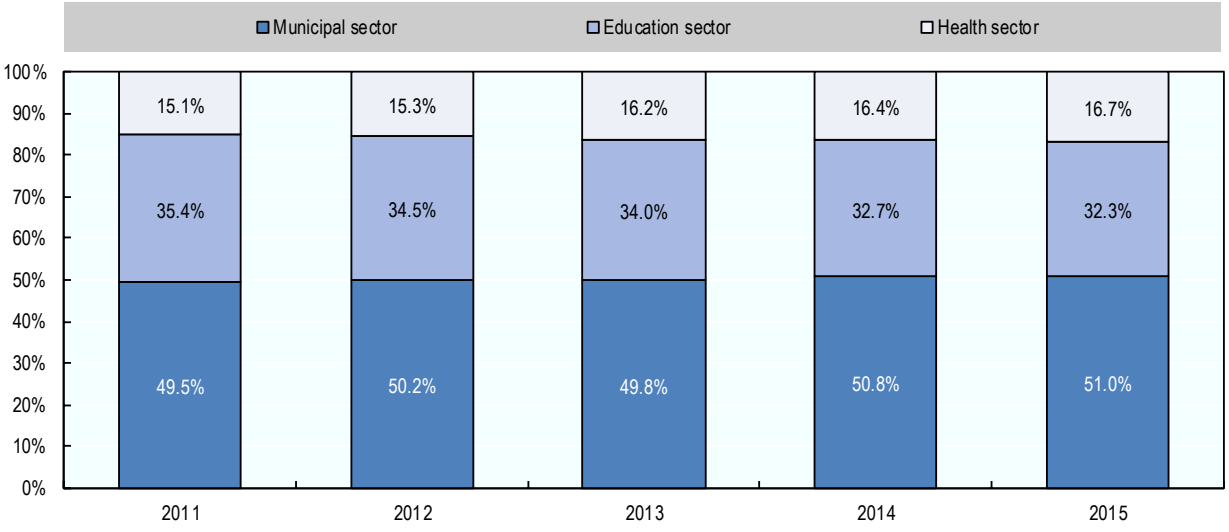
Contrasted fiscal trends

From 2011 to 2015, the sharing of financial commitments of local governments (all three budgets – education, health and municipal – being aggregated but not consolidated) has changed significantly for both expenditure and revenue.[11]

All expenditure areas increased on average, in real terms (+40%). The sharpest increases came in healthcare[12] (+53% in real terms), and the most modest increases were in education (+26%) while the municipal sector's expenditure increased by 43%.

This growth differential underscores the domination of municipal sector operations, which also increased as a share of total municipal expenditure from 49.5% in 2011 to 51% in 2015. Expenditure in education was down 3.1 points, decreasing from 35.4% of municipal expenditure in 2011 to 32.3% in 2015 (Box 2.1). By contrast, expenditure in healthcare gained 1.6 point (Figure 2.24). In relative terms however, it was on par with the municipal sector.

Figure 2.24. **Change in the weight of local expenditure by sector (2011-2015) (% of total expenditure)**



Note: Data are not consolidated.

Source: OECD elaboration based on SUBDERE (2017) *Sistema Nacional de Información Municipal, Evolución presupuestaria* (SINIM: http://www.sinim.gov.cl/).

For the municipal sector, the budgetary item that experienced the most significant increase in real terms between 2011 and 2015 was that of "transfers", which includes transfers to the Municipal Common Fund but also transfers to the education and health budgets (overall these transfers represent 32% of total municipal sector expenditure). As already mentioned, central government transfers to education and health do not cover all costs in many municipalities, which are increasingly obliged to compensate for the gap. In 2015, the municipal transfer to education covered 8.4% of the education sector

expenditure that to healthcare covered 15% of health sector expenditure. Municipal transfers to the health sector have increased sharply since 2013 in nominal terms while transfers to the education sector have tended to stabilise, or even slightly decrease (Figure 2.25). In 2015, municipal sector transfers to the health sector accounted for 31.8% of total municipal transfers, very close to transfers to the FCM (Figure 2.26). The second biggest item was investment (+53% in real terms between 2011 and 2015). Finally, staff expenditure, which represents around 25% of expenditure, increased by 45% in real terms.

Table 2.1. **Change in the structure of expenditure transfers in the municipal sector (2011-2015) (%)**

Item	2011	2012	2013	2014	2015
Education	23.9	23.6	22.7	18.7	16.7
Healthcare	18.0	18.5	21.5	31.2	31.8
Municipal Common Fund	39.1	38.5	37.4	32.7	32.3
Other transfers	19.0	19.5	18.5	17.4	19.2
Total	100	100	100	100	100

Source: OECD calculations based on SUBDERE (2017a) Sistema Nacional de Información Municipal, Evolución presupuestaria (SINIM: www.sinim.gov.cl/).

Figure 2.25. **Change in the breakdown of municipal sector expenditure transfers (2011-2015) (Millions of current CLP)**

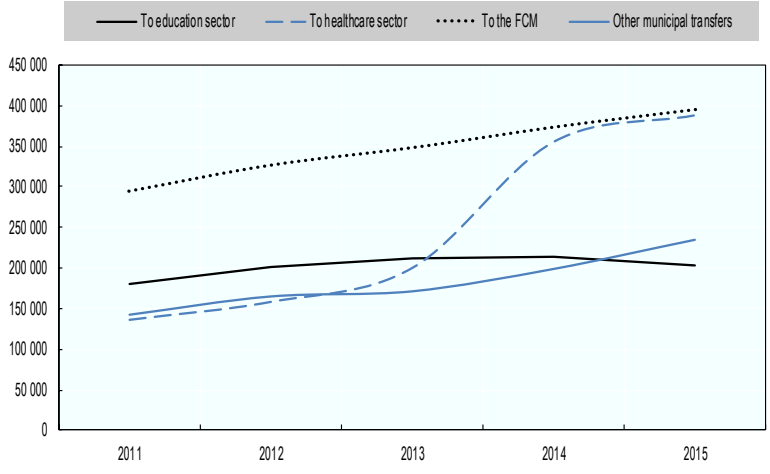
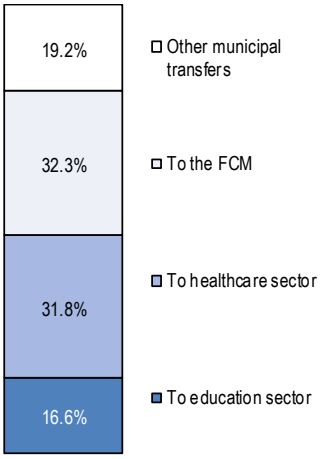


Figure 2.26. **Change in the structure of expenditure transfers in the municipal sector (2011-2015) (%)**



Source: OECD elaboration based on SUBDERE (2017a) *Sistema Nacional de Información Municipal, Evolución presupuestaria* (SINIM: www.sinim.gov.cl/).

In the health sector, the share of personnel expenditure was remarkably stable over the entire period at around 75% while staff expenses increased by 53% in real terms, resulting from the increased use of contractors and fee-based individuals, which are now used as often as salaried staff (*personal de planta*). Health investment is particularly low (1.6% of expenditure).

In the education sector, staff expenditure increased by 21% in real terms while this item accounted for 79% of the education budget in 2015 vs. 82.6% in 2011 (vs. 52% for consolidated local government). Within personnel costs, the trend is driven by contractual staff (*contrata system*) and those under the *honorarios* scheme (see Chapter 4). It appears that there is excess employment in the education sector among teachers, teaching assistants and administrative staff in many municipalities, even though there is no official estimate of the magnitude of the problem. Some informal estimates suggest up to 15% excess in employment levels (Santiago P. et al., forthcoming). Municipal investment in this sector is very limited (3% of education expenditure).

Box 2.1. **The relative decrease in municipal education activities**

Different exogenous factors have a significant impact on municipal finance. One of them is the relative decrease in the municipal education activities resulting from the increasing rivalry within the educational sector.

The decline of the share of the education expenditure in the total local expenditure does not seem to be temporary or cyclical. It seems to be more structural in relation with the disenchantment of families with regard to public education. Since 1990, the distribution of pupils between public and private sectors has been to the advantage of subsidised private institutions. This decline affects, to different degrees, all the indicators, including the number of schools and pupils. There has been a loss of pupils registered in municipal schools (-580 000 pupils, i.e. nearly a third between 2004 and 2015) as well as a decrease in the number of schools, however more limited (-816, i.e. -13%). The number of teachers employed in the public sector fell from 56.1% to 43.9% (Table 2.2).

Table 2.2. **Changes in the Chilean educational system**

Item	Schools		Pupils		Teachers	
	2004	**2015**	**2004**	**2015**	**2004**	**2015**
Number	11 289	12 001	3 740 575	3 548 736	140 642	224 236
Municipal sector	54,0%	44,0%	50,0%	36,4%	56,1%	43,9%
Municipal corporations	0,6%	0,6%	1,4%	1,3%	1,3%	1,0%
Subsidised private sector	37,8%	50,5%	41,0%	54,5%	29,7%	45,7%
Private fee-based schools	7,6%	4,9%	7,6%	7,8%	12,5%	9,4%

Source: Created by the OECD based on MINEDUC (2016), *Estadísticas de la educación 2015*, Centro de Estudios, División de Planifiación y Presupuesto.

This shift has multiple causes but the first effect is a decrease of education resources for the municipal schools. At the same time, expenditure has increased (see above "Recent changes in municipal education and health expenditure") and there is excess employment in many municipalities (Santiago P. et al., forthcoming), resulting in a scissor effect between expenditure and resource.

Box 2.1. **The relative decrease in municipal education activities** *(continued)*

Budgetary tension is jeopardizing the Chilean education system. If the international comparisons demonstrate some real progress, they also draw attention to two major issues: ongoing poor performance of students and the lack of public funding, despite recent substantial financial efforts (OECD 2010 and 2016e).

Considering municipalities' financial situation and their current inability to mobilise own taxes in a sustained manner, municipalities are unable to face these difficulties alone. Despite an increase in municipal transfers to the local education sector, there is a high risk that the situation will get worse. The planned reform of the education system, which intends to "de-municipalise" education will have major impacts in this respect.

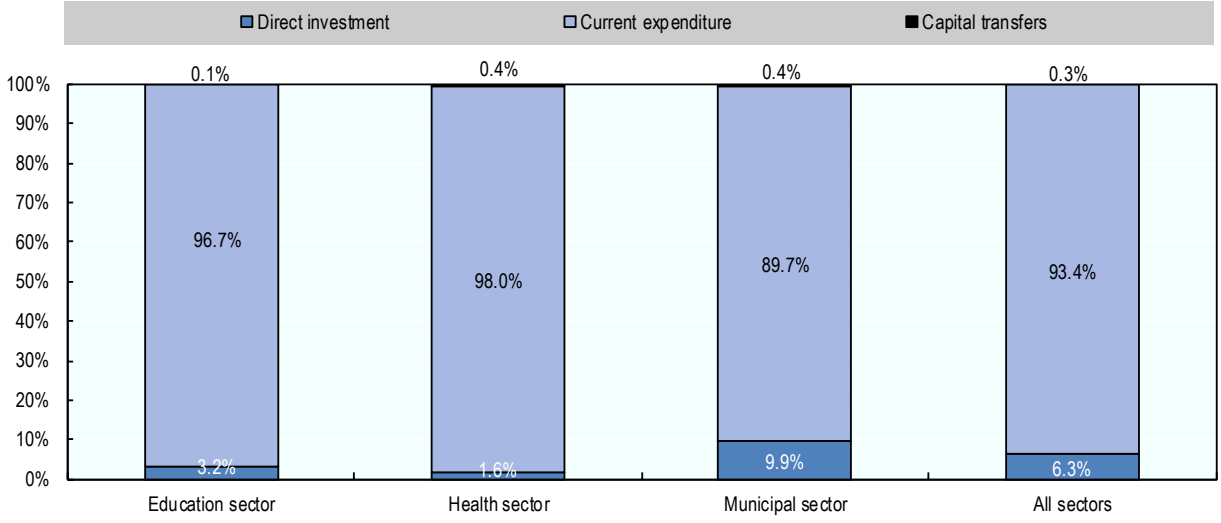
Beyond the financial aspects, the issue is also societal. The educational difficulties are negatively impacting the economic competitiveness and sharpening the social tensions. In this context, the change introduced by the recent reform (2015, *Ley de Inclusión Escolar*) opens new perspectives (see Chapter 1) even if it does not resolve all kinds of problems.

Sources: Santiago, P. et al. (forthcoming), *OECD Reviews of School Resources: Chile*, OECD Publishing, Paris; OECD (2010), *OECD Economic Surveys: Chile 2010*.

Municipal investment is low and overwhelmed by current expenditure

In the three areas, municipal investment is particularly weak, representing on average 6.3% of total municipal expenditure, but 9.9% for the municipal sector, 3.2% for education and 1.6% for health (Figure 2.27).

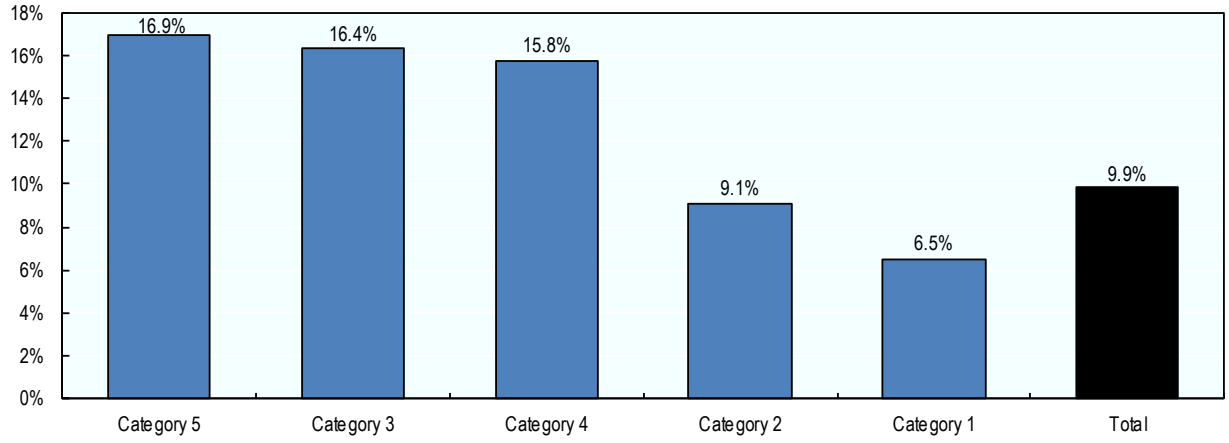
Figure 2.27. **Investment as a % of total expenditure in 2015 (%)**



Source: OECD calculations based on SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

In the municipal sector, it is interesting to note that there is a marked difference among municipalities in the level of propensity to invest, which has an inverse relationship with population size. While investment expenditure of all municipalities accounted for 9.9% of overall expenditure, this figure was just 6.5% for category 1 municipalities in the FIGEM typology, i.e. the biggest municipalities in 2015 (see Chapter 1). It reached 9% for category 2 and soared to 16% or more for other categories, i.e. the smallest municipalities (Figure 2.28).

Figure 2.28. **Investment by FIGEM category of municipalities (% of total expenditure, 2015)**



Source: OECD calculations based SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Over a long period (1990-2015), investment spending on non-financial assets as a percentage of overall spending, after peaking in 2001 (16.8%), has continued to fall, reaching 9.7% in 2015 versus 15.1% in 1990 (drop of more than 55%).

Relative to investment expenditure by the general government (central government and municipalities), the share of municipalities went from 14.6% in 1990 to 12% in 2015. In this rather bumpy slide, 2004 was a pivotal year in the decrease for municipalities. Since then, their weight has fluctuated in a range of 10-12% (Figure 2.29). In GDP terms, local government investment accounted for 0.33% of GDP in 2015, with significant variations over the 1990-2015 period but it has been on a downtrend since 2000 when it reached 0.54% of GDP (Figure 2.30).

Figure 2.29. **Change in local government investment as a % of general government 1990-2015**

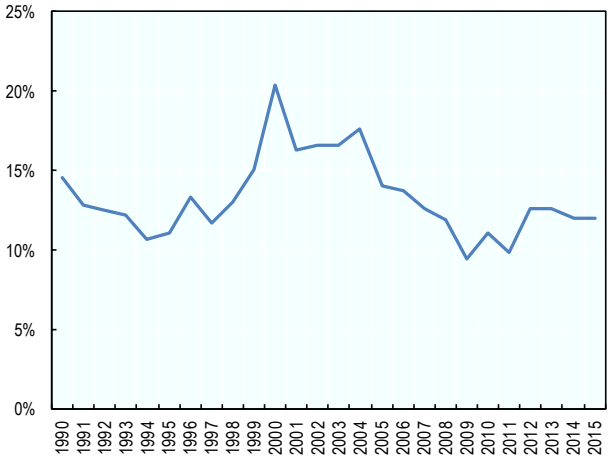
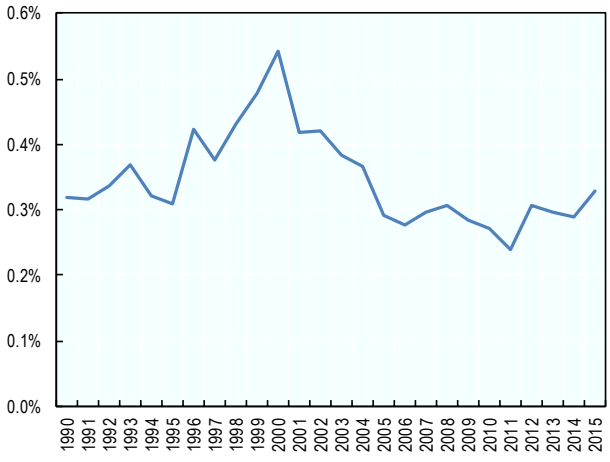


Figure 2.30. **Change in local government investment as a % of GDP 1990-2015**



Source: Created by the OECD based on from DIPRES data.

However, it is important to underline that an important share of public investment at the municipal level is directly financed by line ministries and implemented by SEREMIs on behalf of municipalities as far as sectoral investments are concerned. It means that, quite frequently, funds for municipal investment projects are not channelled through municipal budgets but by SEREMIs.

Municipalities have very little room for investment. The overwhelming weight of current expenditure and the insufficient level of own source revenues, resulting from a poor municipal taxation power, do not allow municipalities to generate self-financing revenue for investment. As a result, in a context where municipalities are prohibited from contracting long-term borrowing, municipalities have to rely almost entirely on capital transfers and subsidies for their investments, which are largely insufficient and lack co-ordination across sectors and actors (see part 3).

Recent changes in municipal, education, health sector revenues

The trends observed above for local expenditure in the municipal, education and healthcare sectors are identical for local revenue, as per Chile's fiscal balance rules. However, the variations observed between 2011 and 2015 are less marked for revenue than for expenditure, in particular for municipal and healthcare sectors while they are on par with general increases in education.

The source of revenue (local taxes, transfers or other revenues) varies substantially from one area of local intervention to the next.

For the education sector, the percentage of current transfers is extremely high, and has increased over the last years, from 91% in 2011 to nearly 95% in 2015 (Figure 2.32). Ministry of Education (MINEDUC) subsidies continue to occupy the lion's share of education-related funding (80%). MINEDUC transfers (Box 2.2) have increased by 28% in real terms over the period.

The profile of the healthcare sector's revenue structure is similar to that of education (Figure 2.33). Current transfers form the bulk of resources and are growing to reach 95%

of total revenues. The Ministry of Health (MINSAL) funds nearly 80% of transfers (and this figure is growing). The primary care (*atención primaria*), subsidy still accounts for over 75% of MINSAL's subsidy.

Figure 2.31. **Breakdown of revenues in the municipal sector (2015)**

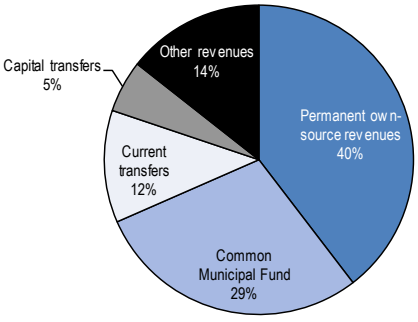


Figure 2.32. **Breakdown of revenues in the education sector (2015)**

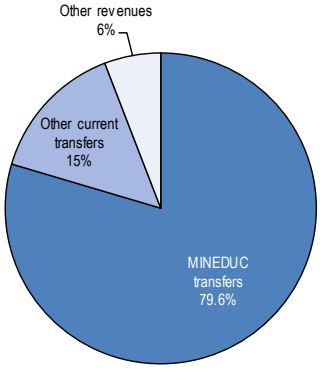
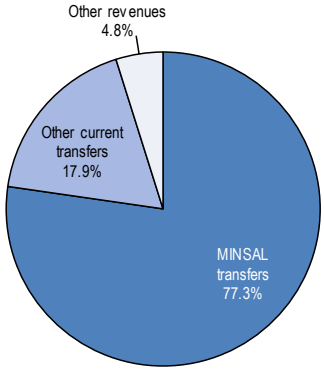


Figure 2.33. **Breakdown of revenues in the health sector (2015)**



Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal, Evolución presupuestaria (SINIM: www.sinim.gov.cl/).

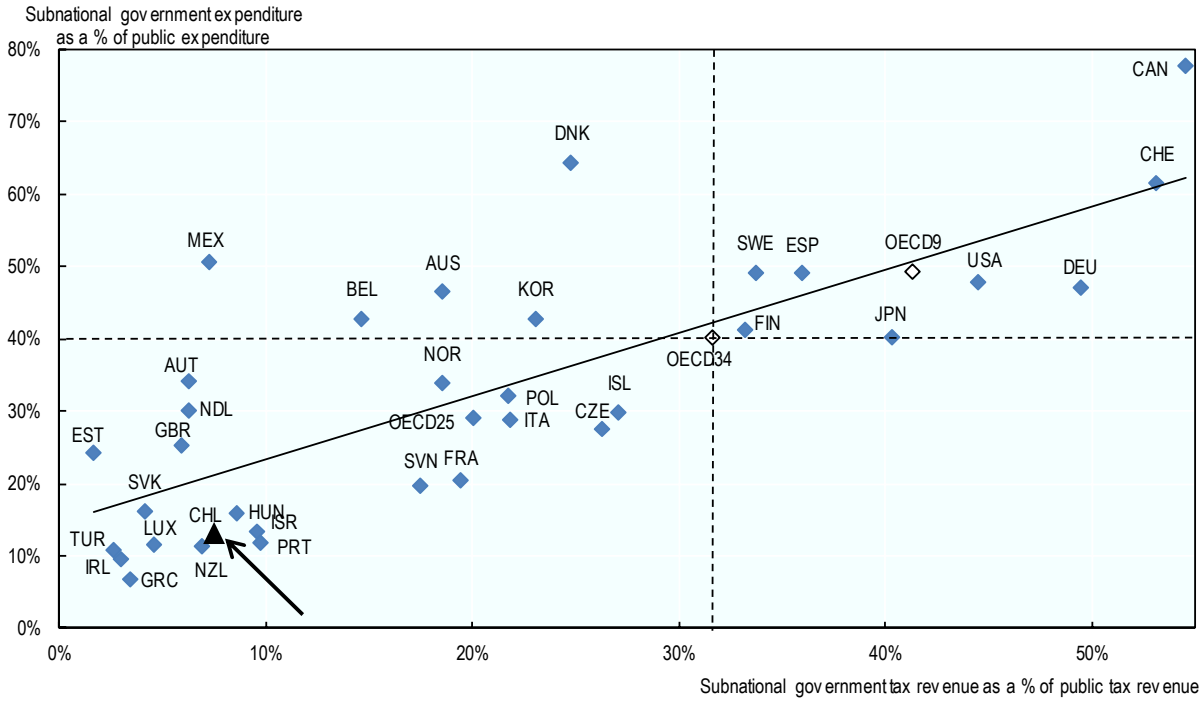
In the municipal sector (Figure 2.34), there is a larger diversity of revenue sources with, on the one hand, own source revenue based on taxes, tariffs and user fees, property income and on the other, grants and transfers from the central government (which sometimes pass through regional governments).

- Permanent own-source taxes (*impuestos propios permanentes*) accounted for 39.6% of municipal sector revenue in 2015, a share which has substantially decreased over the last five years (43.5% in 2011). Permanent own-source taxes increased however by 25% in real terms between 2011 and 2015. This category comprises revenues from the municipal business licenses (*patentes municipales)*, the territorial tax (*impuesto territorial)*, the vehicle registration tax (*permiso de circulación)*, other patents, the waste management fee, fines and other rights and concessions. Nearly all these components increased between 20% and 30% in real terms, except revenues from concessions, which decreased.
- As a share of total municipal sector revenues, the FCM is quite stable at around 30%. In real terms, resources increased by 30%. The FCM is analysed in Chapter 3.
- Current transfers were up sharply in real terms (+268%) and as a percentage of total revenue (from 4.4% to 11.7%) especially over the last two years.
- Capital transfers were stable in relative terms over the period at 5.5% of municipal sector revenues. They increased, however, by 36.6% in real terms.

In total, the structure of municipal revenues was more dependent on current transfers at the end of the period (2015) than at the start of the period (2011).

All three areas – municipal sector, education and health – strongly depend on current and capital grants while municipal taxation power is weak. This situation generates strong fiscal imbalances (Figure 2.34).

Figure 2.34. **Fiscal imbalances in the OECD countries in 2014**



Source: Created by the authors based on OECD (2016d), *Subnational governments in the OECD: Key data* and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database); OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*.

Conclusion

The retrospective analysis of financial trends over a lengthy period (1990-2015) reveals the slow progression, notwithstanding fluctuations over the decades, of the role of municipal authorities in the public realm. The increasing weight of the local public sector is less spectacular than the nominal and per capita trends would suggest. Seen against the sustained economic expansion of GDP, this uptick is both hesitant and modest.

A more in-depth look into the most recent period (2011-2015) underscores the reluctance with which the decentralisation process is moving in the direction of the local level. It also reveals that the direction of trends should consider the nature of the operations. Indeed, recent changes have affected the origin of revenue (slowing of relative value of own-source tax revenue in favour of received transfers) perpetuating a long-standing tradition. These findings do little to confirm the strengthening of the foundation of Chile's political decentralisation. The recent modifications to the structure of expenditure represent a more substantial break with prior trends. Until 2010, personnel expenditure as a percentage of total expenditure increased yet since then has decreased. As seen with the shifting status of employees, it appears that personnel expenditure is being affected by relatively strict prudential rules that were designed to keep such costs under control. Likewise, the share of transfers, which had been down since 1990, has increased in the past five years. Between the increasing dependence on external funding

and the rising use of outsourcing and service providers, any affirmation of municipal autonomy would be unfounded. Analysed across time and through its financial results, municipal autonomy appears limited amid a macroeconomic context that has been bogged down by uncertainty since 2008-2009.

The central government's recent willingness to use fiscal policy to stimulate economic activity (Rodriguez et al., 2016) creates a paradox for decentralisation. Used exclusively as an anti-cyclical mechanism, increasing expenditure by the central government has underpinned the trend of its increasing involvement since 2009. The gap with other OECD countries is narrowing and convergence is underway. However, the confirmation of this trend (on the condition of compliance with the cyclically-adjusted central budget) - without modifications to the institutional distribution of power and resources within the political and administrative structure - would accentuate the concentration of the central government's capacity to intervene. Without a political emancipation of the regions or a functional and financial strengthening of municipalities, the limitations on subnational finances in Chile, compared with other countries, would delay the development of a commitment to decentralise from the national political authorities and the central administration in Chile.

The limitations of the mechanisms financing local budgets and potential avenues for improvement

An international comparison of the structure of Chilean public finances highlights a clear trend: substantial centralisation in a system with a low level of public engagement. This is particularly the case for local authorities' capital expenditure. Compared with the encouragement proffered by many international organisations to promote decentralisation, based on the economic and social progress that are attributed to it, the process in Chile has considerable room for improvement.

Although change is on the horizon, effecting this change must take into account elements that go beyond mere macroeconomic considerations.

- An analysis of changes in Chilean municipalities' finances revealed structural modifications in expenditure and revenue reflecting the underlying transformations in this seemingly-stable system.
- An analysis of individual municipal situations underscores their heterogeneity and dispersion as well as the diversity of financial or expenditure practices at the local level, which has been masked by a uniform perception of the functioning of the municipal system.

The shifting and diverse realities in municipalities condition the mechanisms and implementation of the modernisation of Chile's municipal finance system.

As is the case in a number of countries, the centralised economic, social and cultural development model is showing its limits in societies that have developed rapidly and are now confronted with the urgent need to adapt to current technical and societal changes. Centralisation, promoted as being able to steward development with a firm and steady hand, is now being seen as a hindrance to channelling the energy and the vitality of local potential to develop a more open society – one that is better prepared and eager to embrace a less bureaucratic public management culture. There is pressure to accelerate responsiveness and respect the diversity of municipal situations. Indeed, there is a clash between public mindsets and mechanisms that continue to espouse a one-size-fits-all approach to solving problems and that perpetuate the procedures mired in their slowness, caution and rigidity.

These remonstrations, repeated endlessly, are becoming increasingly urgent. They are putting pressure on the decentralisation and modernisation process of the municipal system to speed up. The work of the Decentralisation Commission, set up in 2014, pleads in favour of this acceleration. However, municipalities do not seem to be priorities when it comes to designing and implementing irrevocable reform strategies. The electoral timetable (municipal elections in November 2016) and the speed bump that is the regional question have slowed the pace of an ambitious reform of the municipal system in Chile. The elections "buy" time to design a strategy for adapting the local level based on 1) a well thought-out diagnostic of its evolution; 2) the difficulties to resolve; and 3) the conditions needed to ensure successful modernisation. The strategy to develop, as is the case in many countries, will be three-pronged: clarification of competences; consolidation of resources; and revision of the territorial organisation by, particularly in the case of Chile, fostering structured inter-municipal co-operation.

The question of whether municipalities have sufficient resources cannot be addressed without tackling the question of competences, expenditure and investment. In the coming years, pressure will grow to give a modernised local level, in the name of economic efficiency or territorial equity, the resources it needs to support real territorial development. This will come in the form of more public infrastructure. Chile lags behind its OECD counterparts and many neighbours in terms of urban infrastructure and, more broadly, public investment. To catch up to its peers or simply upgrade its public capital stock, necessary to pursue the goals of sustainable development, environmental protection, economic growth and social equality, Chile needs to increase the gross fixed capital formation (GFCF) of its local public administrations. The direct financing of investments will be one of the first expressions of this financial effort and their implementation will lead to a sequence of recurring costs to operate them.

With this hypothesis in mind, municipal finance mechanisms will be addressed from two angles:

- The first involves diagnosing the situation. The grant system could be simplified to reduce fragmentation and increase municipal leeway.[13] The tax system and more broadly the basket of own resources (operating income, user contributions) appear, in their current form, to be lacking local leeway and out of step with the prospect of decentralisation.
- The second involves improving the system. The idea of consolidating and expanding municipal financial resources opens up a variety of directions to explore based on both optimising and diversifying existing funding sources. This exploration could include the use of borrowing, which is currently very limited.

The deficiencies of municipal resources

Total revenue received by the Chilean municipal sector includes a basket of resources whose volumes have evolved over the course of the last five years, as analysed above (2011-2015). Municipal sector total resources reached, in 2015, CLP 3 746.3 billion, with own resources (*ingresos propios)* accounting for 70%, 57.8% of which were permanent own resources (*impuestos propios permanentes* i.e. mainly taxes) and contributions from the FCM (42.2%). The extra 30% come from current transfers for the most part (12%) and other revenue (14%). Capital transfers (5.5%) and especially sales of non-financial assets (0.1%) only play a small role.

Supposing the FCM is analysed from an ad hoc perspective due to its redistributive role and the specific stakes it represents (see Chapter 3), the diagnosis of the resource situation focuses on other grants, tax revenue and revenues the municipalities can or could generate from user contributions, management of services and selling assets. The analysis focuses on resources to which all municipalities have access. Certain, highly specific resources are only mentioned briefly. However, it is important to bear in mind that, as the analysis of inter-municipal disparities showed, at times and in instances that are specific to local areas, they provide important or even essential support to the budget (*Casinos, patentes acuícolas, patentes mineras*). The analysis focuses on three diagnoses: the fragmentation and rigidity of the granting system, collection on existing taxes and the capacity to levy other resources.

A rigid and fragmented grant system

Education and health sector grants

As already underlined, central government transfers, in particular current grants, represent the bulk of education- and health-sector resources. Education-related revenues are derived primarily from MINEDUC but there are other sources, including the Regional Development National Fund (FNDR) and the Social Fund. MINEDUC grants are not sufficient to cover all the needs of municipalities, which have to contribute to the education budget with their own resources. Depending on the municipality, the municipal contribution either complements or substitutes for state funding. In the healthcare sector, resources from the Ministry of Health predominate but it also depends on financing from the FNDR and the Social Fund (Box 2.2). Municipalities also have to complement MINSAL financing with their own transfers. Municipal transfers compensate more than they complete the central funding. As in education, the municipal contribution is sometimes very high, absorbing a major share of own municipal sector resources. In these cases, the municipality is clearly stepping in and substituting for the lack of central support.

This funding model adds to the perception of an administrative decentralisation and sector deconcentration of the education competence. The nationalisation of resources, combined with national pedagogical standards, points to a simple territorial application of a national policy. Municipal initiative is limited. Similar to the situation in education, healthcare appears as if it were a deconcentrated service of the health ministry and almost completely dependent on the central authorities.

Box 2.2. **Central government transfers in the education and health sectors**

The central government is a major source of public funding for school education and health through sectoral ministerial grants (MINEDUC and MINSAL), the Regional Development National Fund (*Fondo Nacional de Desarrollo Regional,* FNDR) as well as the Social Fund.

The Ministry of Education allocates funds for municipal school services in a number of ways. Municipalities receive grants under the voucher programme. The determination of the School Basic Grant (*Subvención de Escolaridad*) uses a unit of account which is called the Unit of School Grant (*Unidad de Subvención Educativa*, USE). It is the central term of reference of the mechanism with a value that changes (for 2015, the USE has a value of CLP 22 321.769.). The amount transferred by the MINEDUC is obtained by multiplying the USE by two factors: 1) a coefficient that is a function of the level of education, the type of establishment (general, technical, specialised) and the intensity of the teaching activity (full or part-time); and 2) the average attendance during the previous quarter.

Box 2.2. **Central government transfers in the education and health sectors** *(continued)*

The School Basic Grant is complemented by a range of other more specific subsidies and grants to improve educational quality and equity and support the management and supervision of municipal schools: the Preferential Education Subsidy (*Subvención de Educación Preferencial*, SEP), the Grant for Concentration of Priority Students (*Subvención por Concentración de Alumnos Prioritarios*), the Grant for Education Strengthening (*Subvención de Reforzamiento Educativo*) targeted at disadvantaged students, the grant dedicated to boarding schools to cover the costs of boarding services, the grant provided to school providers for each disadvantaged student participating in the programme Chile Solidario, a specific support for special education as well as some supplementary subsidies by area (depending on how remote the school is), for rurality and for small rural schools.

The Grant for Maintenance Support (*Subvención de Apoyo al Mantenimiento*) is the main capital grant aimed at assisting schools in covering the costs of infrastructure maintenance, including equipment and furniture. It includes an annual allocation of funds calculated on the basis of the Basic Grant. Investment in the education sector is insufficient. According to an assessment of the state of infrastructure conducted between 2012 and 2014, there are significant gaps among municipal schools. Approximately 20% of the 5 509 registered schools were identified as having a precarious drinking water system and deficient construction standards. The Ministry of Education is currently implementing a Strategic Plan for School Infrastructure for the period 2014-2018, in order to upgrade infrastructure standards and to remedy the deficits and shortcomings of education schools. (Santiago P. et al., forthcoming).

In addition to the school grants, municipalities also receive public funds from special funds. It is the case of the Fund for Public Education (FAEP – *Fondo de Apoyo a la Educación Pública*) introduced mostly as a result of the education budget deficit faced by many municipalities. It aims at covering administrative costs incurred by municipalities in providing education services.

In 2015, about 71% of school grant funds were distributed through the school basic grant while the remaining 29% were distributed via other grants and allowances. The SEP amounted to about 16% of all grants provided to schools while the FAEP corresponded to 4.8% of the budget for education grants.

In addition, financial transfers also includes allowance programmes for teachers e.g. rewards for excellence, allowances for working in disadvantaged areas and a student financial aid and assistance through the National Board of School Assistance and Scholarships (*Junta Nacional de Auxilio Escolar y Becas*, JUNAEB). However, municipalities do not receive specific funds to cover the administrative costs of managing their set of schools e.g. to cover the costs of municipal staff working in the municipal education department (Santiago P. et al., forthcoming).

In the health sector, several sources of income come from the central government: a per capita government grant, which is adjusted to take into account municipal characteristics; a number of specific health government programmes; and capital transfers for investment programmes. The FNDR also contributes to municipal health financing.

The subsidy for basic care from the Ministry of Health (*Atención Primaria de Salud*, APS) consists of two components: a basic contribution calculated per capita and a variable part that is a function of structural characteristics of the municipality related to rural population, deprivation level and geographic zone. Additionally, a fixed amount is added depending on the percentage of the population over 65 years old and for difficult assignments due to geographic or sociocultural challenges, etc. In 48 municipalities characterised by low density and a high level of rurality with small populations (under 3 500) a "fixed cost" is used instead (*costo fijo*).

Sources: Santiago, P. et.al. (2013), Teacher Evaluation in Chile 2013, OECD Reviews of Evaluation and Assessment in Education; OECD (2014a), *OECD Rural Policy Reviews: Chile 2014*; Santiago, P. et al., (forthcoming), *OECD Reviews of School Resources: Chile*.

The municipal sector's current and capital grants

Not counting the Municipal Common Fund, which is a horizontal equalisation grant (see Chapter 3), the municipal sector is characterised by a low level of grants (current and capital) coupled with a high fragmentation and rigidity in their use.

Current transfers increased sharply over the last five years, from 4.4% of municipal revenues in 2011 to 12% in 2015. They come from numerous ministries, in particular SUBDERE, the Ministry of Social Development (social programmes), the Ministry of Housing and Urbanism, etc.

Capital transfers, stable at 5.5% of municipal revenue since 2011, are scarce (Box 2.3). The most important investment fund is the National Fund of Regional Development (FNDR). The FNDR is the largest capital expenditure fund. Municipalities can submit project proposals and most tend to be geared towards financing basic local infrastructure and services (most often in order to make up for revenue shortfalls). From a municipal perspective, requests for FNDR funds must pass through a complex set of filters and intermediaries (regional governments, Ministry of Social Development, Ministry of Finance, SUBDERE, SEREMIs) that can vary depending on the project's size. The process lacks the flexibility and speed necessary to meet certain municipal demands for investment in basic services. It favours fragmentation of municipal investment projects, without synergies (OECD, 2009).

Other regional funds, which may benefit municipalities, are the Regional Support Fund (*Fondo de Apoyo Regional, FAR*), the Convergence Fund (*Fondo de Convergencia*) and the Regional Funds of Local Initiative (*Fondo Regional de Iniciativa Local, FRIL)*. Small-sized projects financed through the FRIL are exempt from technical evaluation.

In addition to these regional funds, Chile's central government uses a wide range of instruments to interact with municipalities. In addition to SUBDERE programmes, numerous line ministries have developed specific programmes offering a variety of earmarked and specific grants: Ministry of Social Development, the Ministry of Housing and Urbanism (e.g. programmes devoted to improving neighbourhood infrastructure and equipment such as public spaces, paving services, green areas, lighting), the Ministry of Agriculture, the Ministry of Public Works, the Ministry of Transports, Ministry of Labour, etc. They are distributed directly to the municipalities, often through the SEREMIS, based on a specific agreement or through competitive processes.

Specific grants have been criticised for their proliferation, which makes co-ordination all but impossible (Letelier S. L., 2006). In the framework of the PROFIM programme, the World Bank also criticised the proliferation of ad-hoc programmes without any or limited co-ordination.

This sector-based (more than territorial) logic is not the best way to drive the municipalities to design strategic projects that involve a strong co-ordination of a variety of actors. In fact, there is often a lack of co-ordination between these different ministerial sources of capital funding, leading to dysfunctions and inconsistencies.

In addition, most grants are awarded to projects that meet national policy directions, standards and norms defined by central administrations without taking into account local characteristics and needs. These earmarked subsidies are allocated to specific tasks or projects and come with guidelines and stricter controls, reducing municipalities' decision-making powers.

Finally, this funding system, often based on open competition and complex procedures, often disadvantages small municipalities that do not have the technical or "relational" capacity to prepare the projects and compete in a bidding process. Sometimes, given the small population size, it becomes difficult to justify a rural or local development initiative under the ex-ante social profitability evaluation of the project, as it could appear as a "non-essential" initiative and/or relatively expensive given the small number of people it would benefit. In this context, bigger municipalities, or those with better technical capacities to develop projects, are in a better position to attract more investment resources. This system adversely affects rural municipalities, and might contribute to increasing rural-urban disparities (OECD, 2014a).

Financial subordination of this sort keeps municipalities heavily dependent, both politically and administratively. A decentralisation and modernisation process would demand an easing of this bureaucratic and vertical structure.

Box 2.3. **Capital transfers to Chilean regions, municipalities, associations of municipalities, and corporations**

Significant geographical differences and concentration of activities amplify the questions of regional and local disparities in Chile. To reduce regional inequalities and preserve territorial and social cohesion, the Chilean government has set up several funds aimed at supporting regional or municipal development projects. These funds are steadily growing.

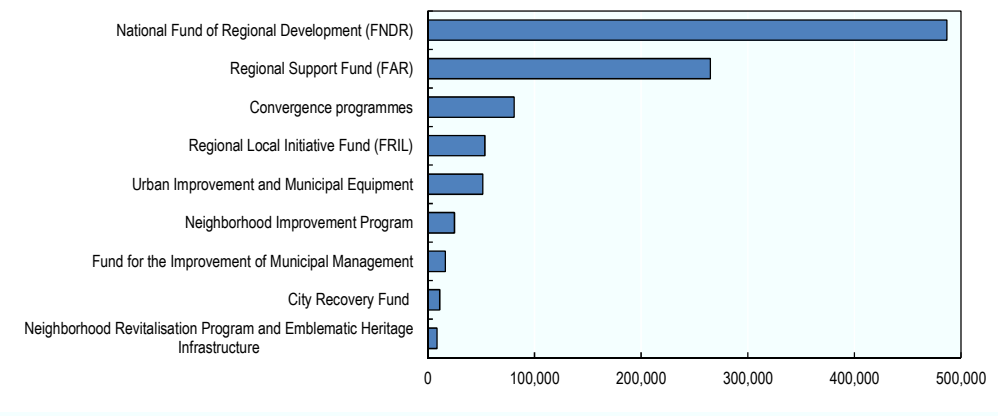
The National Fund of Regional Development (*Fondo Nacional de Desarollo Regional*, FNDR) created in 1974, is a part of the regional administration Act (Ley n° 19-175, *Orgánica Constitucional sobre Gobierno y Administración Regional*, LOCGAR). The FNDR is the most important lever of this policy. The resources transferred through the FNDR have increased from 2006 until now, except in 2007, 2010 and 2013. For 2017, the FNDR amounted to around CLP 486.7 billion (Figure 2.35), i.e. growth of 7.9% in nominal terms compared to 2015 (DIPRES, 2017). Under the responsibility of the SUBDERE, the FNDR is a programme of public investment whose main objective is to facilitate regional development and ensure territorial compensation. 90% of the fund's resources are distributed between the 15 regions according to two categories of criteria: socio-economic characteristics (poverty, rural poverty, family poverty where the woman is the head of household, etc.) for 55% of the funding; territorial characteristics (building cost, paving cost, regional base area, etc.) for the remaining 45%. Funds are also allocated to cope with emergency situations and to stimulate the efficiency of the use of the fund (in equal proportion). The regional governments allocate the fund between selected projects. Municipalities and corporations are allowed to compete.

Other important regional funds include the Regional Support Fund (*Fondo de Apoyo Regional,* FAR) and the Regional Fund for Local Initiative (*Fondo Regional de Iniciativa Local*, FRIL). Recently created by the Law No. 20.696 of 2013, the FAR is focused on connectivity, transport and regional development and it should contribute to the funding of general infrastructures and the modernisation of public transport. The FRIL is a regional government financing tool. Each region can define its priorities, the total amount, and rules benefiting specific grants served by the fund. Regional governments often combine the FRIL with other capital transfers targeting municipalities, mainly for the improvement of underprivileged districts. Projects financed through the FRIL of less than 2 000 UF (i.e. the majority of projects) do not go through technical evaluation.

Box 2.3. **Capital transfers to Chilean regions, municipalities, associations of municipalities, and corporations** *(continued)*

SUBDERE also manages specific programmes including Convergence Programmes (*Programas de Convergencia*) for lagging regions located in extreme areas, a Programme for Urban Improvement and municipal Equipment (*Programa de Mejoramiento Urbano y Equipamiento Comunal*), a Neighbourhood Improvement Programme (*Programa Mejoramiento de Barrios*), the Incentive Fund for the Improvement of Municipal Management (*Fondo de Incentivo al Mejoramiento de la Gestión Municipal*), the City Recovery Fund (*Fondo de Recuperación de Ciudades*), the Neighbourhood Revitalisation Programme and Emblematic Heritage Infrastructure (*Programa de revitalización de Barrios e Infrastructura Patrimonial Emblemática*).

Figure 2.35. **Regional and local programmes**



Source: DIPRES, Presupuesto 2017

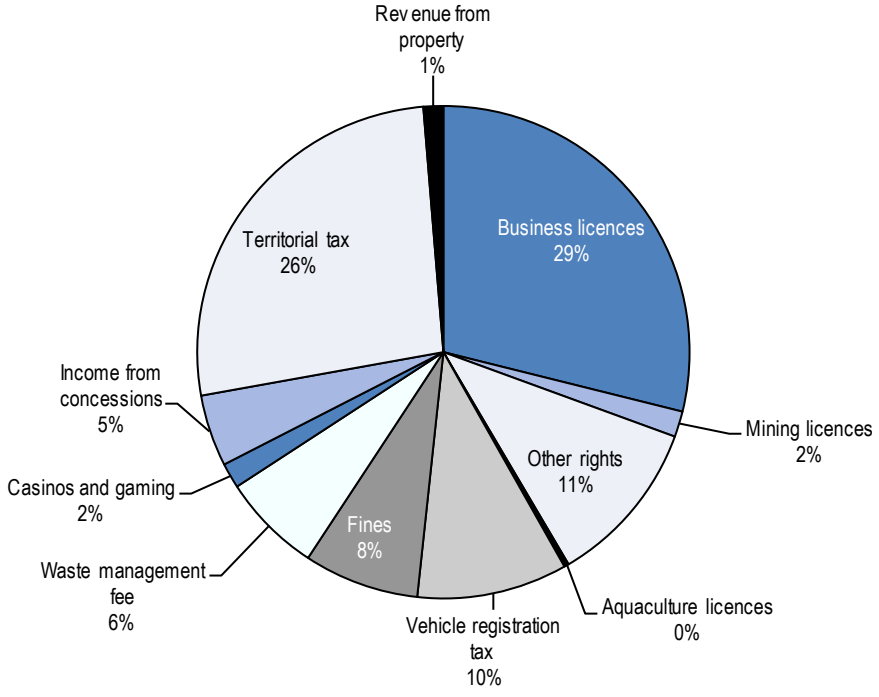
Finally, municipalities may also receive other capital transfers from regional governments amounting to around CLP 45 billion. Despite their differences, these funds present some important similarities. Municipalities and corporations are, for some of the resources, the end recipients of the funds, regional governments being decisive actors in the process. All the grants are earmarked and have to follow specific and strict conditions (with a few adjusted requirements for little projects under CLP 86 or 215 million). The beneficiary has to draw up a quarterly or half-yearly report. The *Fondo de Incentivo al Mejoramiento de la Gestión Municipal* is the only quasi-block grant mechanism funding municipal capital expenditure. Funds are not allocated by project but distributed across municipalities (categorised according to their socio-economic context), depending on a list of criteria related to management abilities. This incentive scheme aims at encouraging good managerial practices.

Others specific capital grants for municipalities and corporations stem from diverse ministries: MINEDUC (technical assistance, improvement of educative infrastructures), Ministry of Social development (territorial interventions), Ministry of Environment, Ministry of Public Works, Ministry of Transport, etc.

Limited return on tax revenue

In 2015, the permanent own revenues (*impuestos propios permanentes*) of Chilean municipalities amounted to CLP 1 482 billion. Nearly two-thirds came from three sources: the business license, the municipal share of the property tax called territorial tax (*impuesto territorial*)[14] and the vehicle registration tax (*permiso de circulación*) (Figure 2.36).

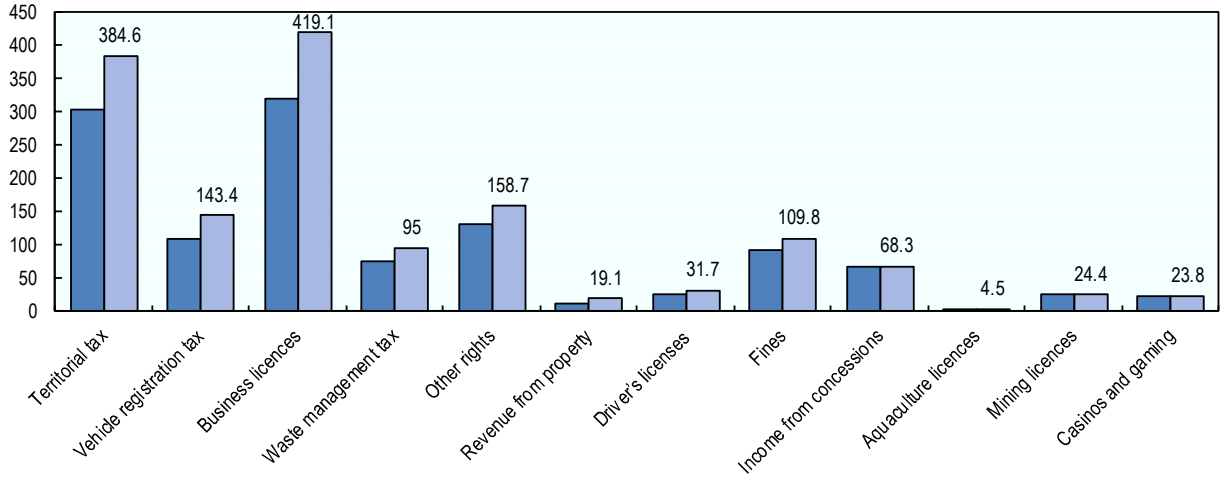
Figure 2.36. **Breakdown of permanent own revenue in 2015 (%)**



Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Compared to the return on these taxes, local authorities' power to take action on the two aspects of local tax autonomy is limited. Their capacity to influence the evaluation of tax bases is limited. Their prerogatives to set tax rates are seriously limited or non-existent.

Figure 2.37. **Change in the breakdown of permanent own revenue between 2011 and 2015 (constant billion CLP)**



Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

This breakdown is only one reflection of the weight of local revenue. It is a cracked mirror of the original distribution of the resources, by their detour, via the FCM. The FCM is funded, for redistributive reasons and in different proportions, by these municipal revenues (see Chapter 3). The territorial tax contributes to it for nearly 60%, vehicle registration tax for nearly 25%, municipal business licenses for 13%. The remainder (7%) is made up of less important resources. Neutralising the FCM smoke screen in evaluating the original weight of municipal resources corrects for the misrepresentation resulting from their contributions to the fund (Razmilic, 2014). The apparent percentages (net of contributions) are redistributed in favour of the municipal revenue source that provides the most resources to the fund, i.e. the territorial tax (Table 2.3).

Table 2.3. **From the apparent final distribution to the actual original distribution of municipal tax revenues (2013)**

Revenues net of FCM contributions	Volume (billion CLP)	%	Gross revenues without contributions to the FCM	Volume (billion CLP)	%
Municipal business licenses	336 927	16.77	Municipal flat taxes	448 093	22.35
Territorial tax	292 463	14.59	Territorial tax	761 702	38.00
Other taxes	125 320	6.25	Other rights	153 041	7.63
Vehicle registration tax	115 426	5.75	Vehicle registration tax	307 743	15.35
Fines and interest	86 278	4.30	Fines and interest	92 119	4.60
Waste management fee	71 896	3.59	Waste management fee	71 896	3.59
Concessions	56 512	2.82	Concessions	56 512	2.82
Other revenues	87 850	4.38	Other revenues	87 850	4.38
Contribution of the FCM	831 914	41.50	Components of the FCM that cannot be allocated	23 561	1.18
Total revenues	**2 004 588**	**100**	**Total revenues**	**2 004 588**	**100**

Source: Razmilic S. (2014), *Impuesto territorial y financiamiento municipal*, Centro de Estudios Públicos, Propuestas de Política Pública.

The territorial tax is more like a national tax allocated to municipalities than a real local own-source tax

The Chilean property tax regime

The municipal share of the territorial tax (Ley No. 17.235 from 16 December 1998, updated on 31 December 2012) is, by its fiscal importance, the number two tax resource for municipalities (26% of permanent own resources) and the number one before transfer to the FCM (38%).

The properties targeted include two categories, each having its own method for evaluating the tax base:

- Agricultural properties, including all properties, regardless of their location, whose land is mainly used for agriculture or forestry or whose primary economic purpose is to ensure such production.
- Non-agricultural properties cover all properties that are not included in the agricultural category. Mines and material and facilities (except if they are proper to an edifice, for example a lift) are not taken into account in this category. Public use buildings are not evaluated.

The territorial tax includes a long and extremely precise list of total or partial exonerations. These exemptions, which reduce the tax yield for municipalities, benefit private individual or legal persons and many public bodies.

The revaluation of properties has been carried out by the SII with reduced frequency since 2012 (every four years). Its goal is to account for changes that are liable to change the value of the property. Between reassessments, the consumer price index is applied to the base value every six months. The SII is based on the land registry (*cadastro*) and applies a separate evaluation index on each of the two categories of property. For agricultural properties, a difference is made for irrigated and non-irrigated land plus the value of the buildings if they are owned by the owner of the farm (*casa patronal*). For non-agricultural properties, the property value is based on the following two items:

- The valuation of the land (based on a rate per square meter depending on the municipal zone, on a location coefficient and a corrective coefficient for the specific aspects of the property versus a standard property).
- The value of the buildings (based on a formula integrating the unit value of the building according to type, a factor of special construction conditions, age (taking account of depreciation based on the nature and materials used and a location coefficient).

The sum of these two parts provides the tax value of the property. Derived from this administrative methodology (*tasación*), which is also found in other countries,[15] it tends to underestimate property values compared with various market prices. Besides setting the tax rate, the SII plays a role in transmitting tax-related information to taxpayers. Tax collection is the remit of the Public Treasury.

All territorial tax revenue is allocated to the municipalities. A portion (60% or even 65% in a few cases) funds the FCM. The income results from the application of a rate on the tax base, a rate over which municipalities do not have any control.

- A proportional rate of 1% is applied to non-residential property (regardless of the property value), which was lowered to 0.86% for agricultural property in February 2016[16] and increased to 1.204% for non-agricultural property.
- For non-agricultural residential property, a progressive rate, with two tranches, is applied to a property value threshold, below which it is 0.98%; above which it is 1.43%.

Certain exceptions to the rule make it possible to adjust it to specific activities or to unstable situations, or even to apply a surtax on vacant lots or abandoned properties in urban areas.

The positive economic effects of the property tax

Levying a territorial tax to finance municipalities is in line with both economic theory and tax practices in many other countries. The qualities of such a tax on property are regularly praised by economists (Bonnet et al., 2014; Fretes Cibilis and Ter-Minassian, 2016): visibility, lack of tax export, productivity thanks to the stability of tax bases and solid return on tax collection, lack of vertical tax competition by exclusive or priority allocation to the municipal level, implicit progressivity (property values rise alongside the revenue of their owners), horizontal equity (equal treatment of equals). Certain economists add the scientific nature of applying the tax and its contribution to transparency, although this assertion is less tenable.

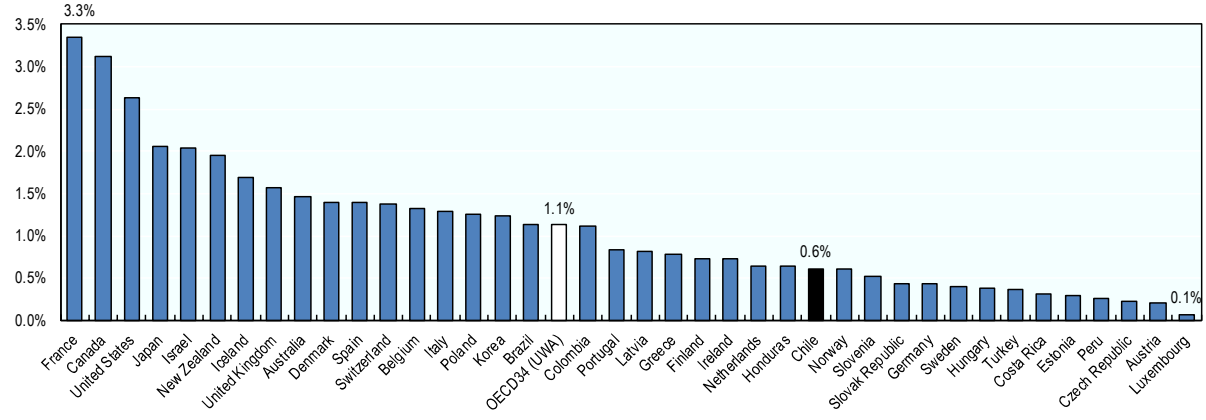
The property tax is a cornerstone of local taxation, according to a wide range of theories, and establishes a bridge between the enhancement of private capital and the improvement, by the provision of collective goods and services by the public authorities, of the environment in which that capital is located. This contribution is, in a certain way, capitalised by rising property and land values. It is, fundamentally, both economically efficient and socially just that the contribution of property owners be set in proportion to the benefits they receive (i.e. their property values increase) through the fact that public services enhance their assets. Seen from a different angle, in a more dynamic perspective and guided by concerns over sustainable development, the use of the property tax, can be a way to penalise owners who cling to property for speculative reasons (Fretes Cibilis and Muñoz, 2016) in tight urban property markets. It can also encourage property owners to put vacant housing on the rental market.

The theoretical merits of the territorial tax do not conceal the weaknesses and limits inherent in its practical application. Almost all countries encounter difficulty in keeping pace with the mass of wealth that property constitutes. If market values, which have their own faults, are not used then more oblique methods must be used to ensure the ongoing assessment of tax bases and, by extension, to maximise tax collection. The low elasticity to economic growth of these tax bases, relative to more modern taxes such as VAT and the income tax penalises the municipalities. The complexity of valuation methods seems to also cloud taxpayers' understanding of the situation thus arousing suspicion of a tax that is supposed to establish a degree of clarity in the relationship between the tax contribution and the services provided by collective service providers. The territorial tax is not without its critics from a taxation point of view, including distortions in valuations, implicit transfers, etc. (Yánez Henríquez, 2015). The territorial tax is not very popular with Chilean taxpayers.

Because of these debates and difficulties, but also due to cultural factors, the importance of recurrent taxes on property in subnational tax revenue varies considerably

across countries. It represents between 90% and 100% of local tax revenue in Australia, the United Kingdom, Ireland, Israel and New Zealand, which are mostly Anglo-Saxon countries. At the other end of the spectrum, it is a minor local tax revenue source in Nordic countries, Luxembourg and Switzerland. As a percentage of GDP, recurrent taxes on property range from 0.1% in Luxembourg to 3.3% in France. With 0.6% of GDP, Chile's rate is around half of the OECD unweighted average, but significantly less than in Colombia where the performance of the property tax has significantly improved in recent years (1.1% in 2014 vs. 0.8% in 2011) due to recent efforts to update and modernise land registries with a view to improving the performance of the municipal property tax.

Figure 2.38. **Recurrent taxes on property in the OECD and other Latin American countries (% of GDP, 2014)**



Note: Recurrent taxes on property include taxes on land, buildings or other structures (D29A) and current taxes on capital (D59A).

The performance limitations of the Chilean property tax

Collection of the territorial tax is eroded significantly by the proliferation of exemptions (Razmilic, 2014). In 2014, nearly two-thirds of all properties benefited from an exemption, 80% of which were agricultural properties (Table 2.4).

The way in which the value of properties is taken into account also adds to this observation:

- The value of exemptions divided by their property values (all properties taken together) is nearly two times less than (34% vs. 64%) their volume (the number of exempted properties divided by the number of total properties).
- The percentage of total tax revenue from non-agricultural properties (35%) is higher than that of agricultural properties (22%) even though the volume of agricultural properties is higher. This results from the high percentage of agricultural properties that are exempt from paying this tax.

The institutional and political logic is respected: the properties with the lowest valuations are the ones that benefit the most from the exemptions. This treatment results in the loss of over one-third of the potential tax collection on non-agricultural properties (35%) and one-fifth on agricultural properties (21.6%).

Table 2.4. **Territorial tax: Properties included in taxed properties (2014)**

Item	Agricultural properties	Non-agricultural properties	Total	% of non-agricultural properties
Number of properties	848 458	5 946 045	6 794 503	87.5
Number of exempted properties	671 622	3 688 290	4 359 912	84.6
Number of taxed properties	176 836	2 257 755	2 434 591	92.7
Percentage of exemptions (%)	79.2	62.0	64.2	-
Value of properties (million CLP)	9 817 553	149 605 618	159 423 171	93.8
Value of exempted properties (million CLP)	2 127 320	52 364 996	54 492 286	97.9
Value of taxed properties (million CLP)	7 690 233	97 240 622	104 930 855	92.7
Percentage of exemptions (%)	21.6	35.0	34.2	-
Unit value of properties (CLP)	11 571 054	25 160 526	23 463 551	2.17[a]
Unit value of exempted properties (CLP)	3 167 436	14 197 627	12 498 482	4.48[a]
Unit value of taxed properties (CLP)	43 487 938	43 069 608	43 099 993	0.99[a]

Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/) to evaluate transfers to the FCM.

Although the average value of non-agricultural properties is over twice that of agricultural properties, the gap is compensated by the unit amount (four times as high) for exempted non-agricultural properties as agricultural properties. The result is that the unit values of the two categories of property are nearly identical (CLP 43 million).

The high proportion of exemptions is a major and sensitive political question. The tax is not only a matter of financial tools; it is also a vital link between the citizens and the community. In this sense, the high proportion of exemptions simultaneously illustrates and solidifies the weakness of the "willingness to pay taxes" (as in many other Latin American countries). The disappearance of the fiscal link dilutes the "tax pact" which would be necessary to ensure the proper functioning of a modern and developed society. Beyond this fundamental issue, Chilean territorial tax exemptions face two pragmatic difficulties.

First, the plethora of exemptions enacted by the legislature raises the question of the full compensation of municipal budget shortfalls. The contribution of the national budget is far from covering the loss. For example, the 2017 budget allocated a credit of CLP 61.155 billion (*Compensación por predios exemptos)*.[17] Regardless of revenue loss, the exemption system presents two main deficiencies:

- A quarter of the amount is diverted to serve another goal (incentive to outsource the provision and transport of solid waste).
- The allocation of compensation to municipalities is a function of the number of exemptions and not of the value of exempted properties.

However, municipalities suffering from a high number of exemptions benefit from the FCM as the allocation of the FCM takes into account the number and the value of

exempted properties. Therefore, it is not an incentive to change the system of exemptions (see Chapter 3).

The second difficulty is that exemptions clearly reveal the dualism of the Chilean municipal structure. In fact, the average proportion of taxed properties is 36% (20% for agricultural properties and 38% for non-agricultural properties), but in practice, there are very few municipalities where effective taxation takes place. The proportion of taxed properties exceeds 50% in only 27 municipalities, i.e. 8% of Chilean municipalities. The top levels are concentrated in the Metropolitan Region of Santiago where the proportion of taxed properties is above 80%, and even near 100% for some municipalities.[18]

Unable to set the territorial tax rate, Chilean municipalities receive significantly less income from this tax, which is only "local" in appearance. It is analogous to a national tax allocated to the municipalities based on a distribution mechanism using the territorial distribution of the net value (after exemptions) of property wealth (Daher, 1995). A significant share of the resource is distributed, via the FCM, in the name of redistributive principles. The territorial tax set up by Chile thus is quite different from the one put forward by economic theory on property taxation.

Municipal business licenses: Little room for manoeuvre

The taxation regime of the municipal business licenses

Municipal business licenses come from the authorisation, granted by municipalities to establish and conduct a commercial activity in a set location.

There are two aspects to obtaining a license:

- The authorisation to conduct business. To be granted permission, the general rules (set by the municipalities) must be complied with (for specific activities subject to health, hygiene and safety rules, this is enforced by central entities). The license is granted for a period of one year except for independent activities, which are unlimited and not controlled by the municipality.
- The obligation to pay a tax that is annually set by each municipality. These taxes differ depending on the nature of the activity:
  - Commercial licenses linked to retail outlets buying and selling goods.
  - Professional licenses for independent activities (architectural firms, doctor's offices, law firms).
  - Industrial licenses linked to the production or transformation of goods (factories, bakeries, food products).
  - Alcohol licenses for bars, restaurants and liquor stores.

The rate set by the municipality can vary within a range of 2.5-5 ‰ and is applied to the value of the company's capital, which is recorded with the Internal Tax Service (SII) (*Servicio de los Impuestos Internos*). The minimum annual rate is set at 1 UTM (monthly unit fee - *unidad tributaria mensual*)[19] and the maximum is 8 UTM. Alcohol license rates are set by law. Their amount varies, depending on the nature of the building, between 0.6 UTM and 3.5 UTM. For independent activities, the amount of the license is set at 1 UTM. All non-profit activities are exempt from paying the municipal business license.

The economic weaknesses of the municipal business licenses

As with all local taxes linked to business activity, the licenses raise several questions. Some licenses apply the same conditions regardless of the business activity subject to taxation. Others treat different business sectors differently, depending on the economic or financial profitability linking the results of the establishment, i.e. local production unit (if they are easy to locate) or the company (sales, added value or profits) and the amount of capital. The ratios can be very different depending on the nature of the business activity and demands can be variable depending on initial capital expenditure. The lags between the inertia of equity and the fluctuations in revenue from the activity are also liable to make it difficult to pay the tax, especially for companies with declining revenues.

The other sticking points are directly linked to the local nature of the tax. They are related, on the one hand, to horizontal tax competition and, on the other, to wealth concentration.

Chile cannot be criticised for encouraging horizontal tax competition, which is a criticism that is often levelled against this type of economic tax. The narrow limits within which municipalities can set the license rate reduce this risk. While the rate is not necessarily a national rate, the range within which the rate can fluctuate is sufficiently narrow to limit the impact of the argument. However, to nuance the judgement, if the rates are low, they may double.

Nevertheless, companies with several branches have the possibility to practice tax optimisation. They use accounting techniques to "export" a part of the taxable revenues to a branch located in a low tax rate municipality.

Furthermore, in metropolitan areas, especially in the Metropolitan Region of Santiago, the topic is more sensitive. Municipalities that contribute to the FCM have to adopt the higher tax rate. Hence, the neighbouring municipalities can attempt to attract economic activity by choosing the lower tax rate.

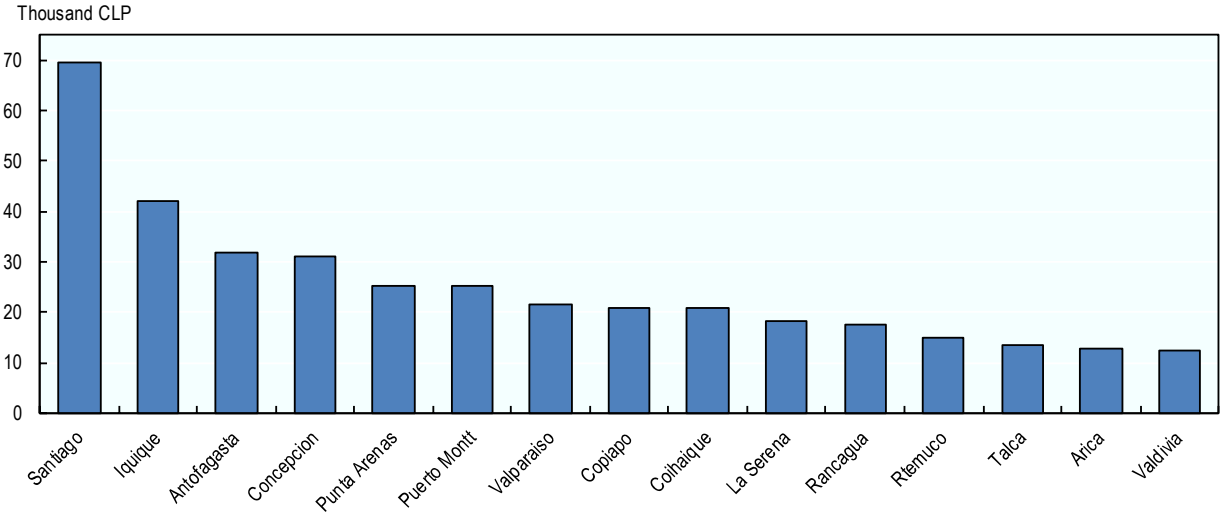
However, by its nature, the tax base gives the rate a weak elasticity. The revaluation of equity is an exercise that is often marked by strong inertia and sometimes tax biases work in favour of limiting their updating (increase in equity). The municipal budget is, of course, shielded from risks related to the variation in income that would result from more dynamic tax bases (particularly the results of the business or the value of production facilities). This assurance, while not eliminating the risks (particularly bankruptcy or the risk the company moves to another municipality), has a cost in terms of the effectiveness of the local tax. The municipalities could hope to expect a growing tax base that would give them greater fiscal leeway.

Marked by sectoral variation, licenses reflect the geographic concentration of economic activities and the relative economic specialisations of each territory (businesses, industries, services). These phenomena influence the effectiveness of the tax and are a source of disparities (see Chapter 3). Disparities between municipalities are substantial, although aquaculture and mining are outliers (Box 2.4). Small municipalities (less than 10 000 or even 5 000 inhabitants) receive a substantial windfall per capita (sometimes in excess of CLP 500 000) while others, with similar demographics, only receive a fraction (less than CLP 2 000).[20]

The Metropolitan Region of Santiago alone accounts for nearly two-thirds of licenses paid, which is out of proportion with its economic weight in the Chilean economy. Municipalities such as Las Condes, Providencia and Vitacura benefit tremendously both

in volume and per capita terms.[21] Disparities in income received from licenses result from possible gaps in the choice of tax rate but fail to fully explain the disparities in regional capitals. Excluding Santiago from the comparison, certain regional capitals receive per capita income from licenses of CLP 30 000 while others receive a mere CLP 15 000.

Figure 2.39. **Income from municipal licenses* per capita (2015)**



* Municipal license income net of FCM contribution. Santiago is the only regional capital that contributes to the FCM.

Source: OECD elaboration based on SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

The disparities in the tax windfall are present among municipalities that are sometimes neighbouring and confronted with different competences and attendant expenditure. This raises questions about the links between the location of the tax on business activity and the fragmentation of the administrative map. One illustration is the gap between the income from license revenue received by Antofagasta (CLP 32 000 per capita) and nearby Mejillones (CLP 202 000 per capita) or, slightly further away, Sierra Gorda (CLP 697 000).[22] This illustration represents a challenge for striking a balance between financial equalisation and municipal co-operation.

Box 2.4. **Aquaculture and mining licenses**

Resources from these two taxes are associated with the territorial tax (*impuesto territorial*). They are attached to two business activities, which are particularly prevalent in Chile, aquaculture and mining, but which are particularly concentrated in specific areas, especially aquaculture. Their overall impact seems small given total own resources yet their geographic concentration makes it an important revenue source for several municipalities.

In 2015, revenue from mining licenses (Law No. 19.143 on the distribution of resources from mining concession licenses) paid to municipalities reached CLP 24 440 million or 0.7% of total resources received by municipalities or less than 1.7% of permanent own resources. Most, though not all, municipalities benefiting from mining licenses are from the Antofagasta region and to a lesser extent Arica y Parinacota. For Antofagasta, the income received for mining licenses was CLP 2 245 million.

Box 2.4. **Aquaculture and mining licenses** *(continued)*

The municipalities of Sierra Gorda, Taltal, Calama, Copiapó, Tierra Amarilla and Diego de Almagro receive more than CLP 1 million; San Pedro de Atacama and María Elena, over CLP 0.8 million. The highest levels of per capita income include the smallest municipalities: Sierra Gorda, Rio Verde, Ollagüe, Camarones, Huara and several municipalities above CLP 100 000 (María Elena, Pica, Taltal, San Pedro de Atacama).

Revenue from aquaculture licenses (Law No. 20.033 art. 8) transferred to Chilean municipalities by the Public Treasury, form a contribution that is 5.5 times less than mining licenses. Aquaculture generates for municipalities a resource of CLP 4 477 million or 0.1% of total resources and 0.3% of permanent own resources. However, this tax only benefits 50 municipalities, mainly located in the regions of Puerto Montt and Cohaique such as Cisnes, Aisén, Chaitén, Quinchao and Quemchi. Per capita, the municipality of Cisnes receives over CLP 130 000 from aquaculture licenses which pales in comparison to Rio Verde (nearly five times more).

The distribution of per capita revenue from casinos/gaming and revenue from aquaculture are similar in that they both have the highest territorial concentration and greatest inter-municipal disparity (variation coefficients are greater than 10 while that of mining licenses is 4.9 and for other revenue it varies between 1.9 and 2.7).

Vehicle registration tax (permiso de circulación): A rate determined nationally

Vehicle registration tax (law-decree No. 3.063, from 1979) benefits municipalities every year. A significant proportion (67.5%) is redistributed by transfer through the FCM. This detour reduces the remaining amount paid to the municipality for around 10% of permanent own resources.

This tax applies to all owners of a motor vehicle. Its annual amount (although it can be paid in two instalments) is calculated using a scale established by the administration that takes into account the type of vehicle, the brand, model and age. The rate is national with no local variation. Given its territorial dimension, the vehicle registration tax, which is a kind of differential tax on motor vehicles, is a national resource that is allocated to the municipalities and redistributed (more than two-thirds of it). The owner of the vehicle can choose in which municipality he or she wishes to pay the tax whether he or she lives there or not. This option opens the door to inter-municipal competition, although they cannot compete via the rate scale, which remains a national prerogative. It does not appear, however, that municipalities use this leverage (i.e. enticing individuals to pay this tax in their jurisdiction) on a regular basis. However, vehicle owners are informed that the revenues will be integrated in the investment fund of the municipality where they pay the tax.

Although the fiscal stakes are not as high compared with the aforementioned resources, inter-municipal disparities, sometime significant, appear and for no particular reason beyond their residents' income level and the presence of activities requiring a fleet of vehicles.[23]

The waste management fee: Collection is flawed

The cleaning fee or waste management fee *(derechos de aseo) (*art. 7.8 and 9 of the Law No. 3.063 of 1979) is received by municipalities and compensates for trash collection and bins for solid waste disposal. The payment of this tax may be disassociated from or linked to the business license tax. The municipalities set an annual rate relative to

the actual cost of collecting household waste. The payment is a flat fee (total expenditure/number of users) and adjusted depending on the characteristics of the household or the housing unit. In some municipalities, housing units with a tax value of less than 25 UTM are exempt. In other municipalities, this threshold can be much higher (225 UTM). Municipalities also adjust the rate depending on social criteria (based on CAS points).

In 2015, the waste management fee generated CLP 95 billion for municipalities and the Metropolitan Region of Santiago accounted for nearly 60% of this sum. It is a resource concentrated in major urban municipalities and is one of the only revenue sources for which local officials have decision-making authority.[24] It appears that many citizens fail to pay this "trash tax", perhaps because they are not aware of it, thus provoking an accumulation of debts. In fact, an extension for paying fines and interest on this debt was granted because so many people had failed to pay on time.[25]

Weak mobilisation of the other local resources

Except the waste management fee, which is analogous to a fee for a service being provided,[26] Chilean municipalities do not tend to charge, directly or indirectly, for public services. Contributions from users to the finance of collective service is modest as illustrated by the low share of resources derived from "other fees" or service payments. This is also due to the fact that municipalities cannot charge for all services they want e.g. public lighting, construction of sidewalks, maintenance of green areas or cultural and sports buildings (SUBDERE).

Concessions and operating fees added CLP 68.3 billion to municipal coffers in Chile, or CLP 3 900 per capita, accounting for 4.6% of municipal permanent own revenues (Figure 2.36: Breakdown of permanent own revenue in 2015). However, it should be noted that Viña del Mar accounts for nearly 38% of this figure. If the six other major municipalities are included (including Estación Central, Santiago, Las Condes, Providencia, Vitacura with similar amounts which are concentrated in the Metropolitan Region of Santiago plus Arica), this figure rises to nearly two-thirds (63.5%) of all revenue of this category. These municipalities are the exception: the vast majority of municipalities recorded a value of zero for this line item since numerous concession holders frequently operate in their territory but are on contracts with the central government (e.g. ports, roads, mining).

Revenue from operations (*ingresos de operación*) from the sale of goods and services, while more widespread, are less productive - generating only half as much income as operating fees (CLP 37 billion and CLP 2 100 per capita). They are also more concentrated geographically than operating fees. Maipú alone accounts for over 68% of all income from this category and the 10 most active municipalities account for 91% of all revenue.

Revenue from property provides a contribution that is even more meagre: CLP 19.1 billion or 1 100 per capita and is another resource that would also stand to benefit from promotion by the municipality as it seeks to diversify its fiscal resources. This resource is present in many local budgets and points to the fact that municipalities have property at their disposal. However, the revenue generated is marginal (1.3% of municipal permanent own revenues), except for a few municipalities. The top ten municipalities[27] account for more than half (51%) of revenue generated from their properties.

Due to their low propensity to invest, Chilean municipalities do not make use of legal or financial structures such as next-generation public-private partnerships, which have been increasingly popular in other OECD countries over the past 15 years.

Between the low level of non-tax resources as well as their fragility and reduced room for manœuvre, municipalities in Chile find themselves heavily dependent on external sources of revenue mainly from the central government (except for the FCM). There is, as a result, significant room for improvement in setting up a system that is more in step with the perspectives of decentralisation.

Municipal debt: Forbidden yet commonplace

Chile's cardinal rule is to prohibit any use of borrowing for municipalities, except when explicitly authorised by the Ministry of Finance and only after a specific law is passed, (article 63 of the Constitution). This prohibition is detailed in the law 18.695 (articles 50 and 63) and in the Decree-Law No. 1.263 (article 1, 2 and 39) and also applies to municipal corporations (Law 18.695, articles 140 and opinion of Comptroller's Office No. 58.907, of 2009).

This prohibition for subnational governments to acquire public debt is unique in the OECD and Latin America. Chile has the simplest and most restrictive rule, which explains the country's extremely low debt rate.

Illustrating this strict policy, this rule provides a dual guarantee. First, the municipalities are not tempted to finance their activity without consideration of future consequences in an uncontrolled debt strategy that would be highly risky for municipal finances. Second and more importantly, the central state shields itself from the possibility that insolvency or liquidity risk could be transferred to their balance sheet, which could arise as municipal resources struggle to stay afloat and local leeway prevents them from using taxes to dig out of debt. In these conditions, the central government is the only entity to respond to a default by an insolvent municipality. It is potentially the lender of last resort. By setting a general ban and authorising case-by-case access, under its control, the central state neutralises the moral hazard of lending and buttresses itself against unpleasant surprises resulting from lax municipal conduct.

However, faced with structural deficits linked in particular to the weight of educational and health expenditure in municipal budgets (end of 2015, 74% of municipalities presented a negative budget balance), municipalities have developed certain practices and used more circuitous and unorthodox routes, which, *de facto,* lead them to take on short-, medium- and long-term debt.

Municipalities are tempted to get around the ban on credit in three ways (Letelier L. Letemier S., 2010):

- **Leasing and leaseback operations:** municipalities may engage in these operations under certain conditions and with the approval from the municipal council and the Ministry of Finance. Leaseback contracts are used to increase liquidity by selling a real estate property to a financial institution, and reacquiring the property over a given period (*Ministerio de Hacienda de Chile*, 2005). They are used to handle new situations affecting municipalities' finances and to finance investment projects and equipment purchases and material amortised over a short or medium time period, but with a higher interest rate than normal loans.

- **Commercial debt and arrears:** some municipalities have used delaying ongoing payments of short-term liabilities to service providers and suppliers (such as providers of electricity services and garbage collection) as a way to manage annual cash disbursements. This is referred to as floating debt (*deuda flotante*). Current short-term debt refers to obligations that were expected to be settled during the normal operating cycle of the municipality, but were not met. According to Chilean regulation, obligations must be settled within a period not exceeding twelve months from the balance sheet date. However, this is not always the case. Overdue balances are carried over from one financial year to the next, building up deficits.

  Even if floating debt is widespread in the management of Chilean municipalities, it does not represent a major issue at the aggregate level. According to SUBDERE, floating debt represented around CLP 74 billion as of 31 December 2015, i.e. around 1% of municipal revenues. This total amount was slightly reduced compared to 2014 (-0.86%) but significantly higher than in 2010 (an increase of 36.7% compared to 2010). It is very concentrated, some municipalities having particularly high levels of floating debt (Maipú, La Serena, Central Station, Quilicura, Valparaíso, Independencia, Buin, Copiapó, Recoleta and Concepción). Almost 40% of total floating debt is concentrated in 10 municipalities. For example, the floating debt of Independencia has increased from 9.3% of total revenues in 2011 to 18.8% in 2015. In addition, La Serena's floating debt increased from 6.8% of total revenues in 2011 to 8.5% in 2015.

- **Temporary pension debt:** outstanding balances for social security contributions on behalf of municipal employees (*deudas previsionales*) used to be another important source of debt at the subnational level. This was particularly relevant in the education and health sector, where municipalities are in charge of administrating staff and local facilities. In most cases, direct transfers from the central government are insufficient to cover all expenditures, resulting in postponing regular social security payments of teachers and primary health centre officers (Letelier E, Letelier S., 2010). Reforms introduced have helped to reduce the amount of outstanding balances for social security contributions. Indeed, since 2014, SUBDERE can block advances from the FCM to municipalities that have not fulfilled these payments. The Ministry of Education has also reduced its transfers to those municipalities that were not paying into the system. In addition, a reform introduced in the same year (Law No. 20742 from 2014), includes failure to pay social security contributions as grounds for convicting a mayor for gross negligence. As of 31 December 2015, the total adjusted amount of temporary pension debt (*deudas previsionales*) amounted to CLP 35.5 billion (CLP 5.5 billion in nominal terms) representing 57 municipalities and 23 municipal corporations, i.e. 23% of all "municipal entities". Among the 80 municipal entities, six held 50% of all total adjusted temporary pension debt at the municipal level. Municipal corporations represented 83% of total adjusted debt and municipalities, 17% (*Superintendencia de pensiones*, February 2016).

In addition to these practices, SUBDERE has developed a mechanism to introduce some flexibility into the system. This mechanism is analogous to a zero-interest loan (reimbursable subsidies) by offering municipalities subsidies that can be paid back over time, can be depreciated and are interest-free. This programme called Investment Programme City Development (*Programa de Inversión Desarrollo de Ciudades)* aims to promote the design and implementation of municipal investment projects in municipal

infrastructure that contribute to improving the quality of life of citizens. This programme has not been a big success to this point. In March 2016, it was revised in order to enable it to become more widely used.

These strict regulatory conditions explain why the debt level of municipalities was low in Chile in 2015, although it is difficult to have a global, consolidated statistical view.

As far as debt service is concerned, amortisation charges on loans appear in the accounts of only 32 municipalities (less than 10%). For nine of them, interest charges were zero. The municipalities that do borrow have an average debt service (amortisation of the principal and interest) of CLP 2 300 per capita. Except for one municipality with 4 000 inhabitants, this group includes the municipalities with a sizeable population (greater than 80 000 inhabitants).

Floating debt accounts for the bulk of municipal debt service (CLP 44.9 billion out of CLP 54.3 billion total). This is a common practice among most municipalities, only 67 municipalities (20%) forego the use of debt including this "supplier credit". The per capita amount is most often very low (less than CLP 1 000), reflecting how this practice acts as cash flow credit or as a way to get around recording a deficit at the end of the financial year. Unlike the more conventional part of the debt service, the per capita portion represented by floating debt is substantial and, in most cases, a cause for serious concern for municipalities, particularly those with small populations.

To date, municipalities have managed to deal with regulations restricting access to credit. The low propensity to invest in the Chilean local public sector has not provided enough pressure for this constraint to have a big impact. However, the question of cause and effect can be asked. The low propensity to invest may derive from the fact that finding finance to fund capital expenditure is difficult (excluding the acquisition of materials).

Improving municipal financing

Modernising its municipal finances is, for Chile, a prerequisite for ultimately enacting political decentralisation. The bare minimum to achieve this goal would be to improve the existing system technically, whereas a more ambitious and demanding overhaul would be to rethink the ways and means of political action. Empowering local officials, which is inherent in decentralisation, would require making them more accountable and would require a departure from the current hierarchical and subordinated structure. Briefly stated, top-down submission to the norms of the central administration must gradually shift to a horizontal regulation involving citizen oversight.

This broad design triggers ideas that should be tested for their legal feasibility, their political suitability and their social acceptability. Several initial directions should be investigated in terms of the modernisation of the system of financing Chile's municipalities. The transfer of competences and their related expenditure from the central government to the municipalities is an essential ingredient, regardless of how decentralisation is brought about. The question that would arise if and when municipalities' scope of competences was to be enlarged would involve the volume of resources to be transferred. In addition, the potential courses of action are located in different areas but they complement one another and some can take longer than others.

Increasing the depth of municipal resources is a prerequisite for enforcing the accountability of municipalities. One of the objectives is to correct the asymmetry between municipal expenditure and own resources (i.e. the fiscal mismatch). In doing so,

local budgets will be made solvent, thus ensuring that as municipalities take on more competences they will have the financial resources, the capital or the savings capacity to handle the additional operating costs and to make the necessary investments for their development. Today, the fiscal framework conditions for effective public investment at the local level are not met, not to mention weaknesses and gaps related to municipal capacities to design and implement investment strategies and a lack of co-ordination across sectors and jurisdictions.

Expanding borrowing capacities is an inevitable question. The highly restrictive mechanism for borrowing funds seems out of step with the notion of what constitutes economically-effective or socially-equitable public policy. The current system fails to provide the conditions that would enable infrastructure – and the amenities it entails – to be improved and economic development to accelerate.

Improving the system of intergovernmental grants

Chilean municipalities find themselves in a unique situation, i.e. two sectors (education and health) are financed almost exclusively through major current grants and a municipal sector with a more balanced funding model, based on taxes, horizontal equalisation grant (FCM) and central government transfers.

Developing a comprehensive and co-ordinated approach to the grant system

The relevance and efficiency of Chile's complex system of intergovernmental grants should be comprehensively assessed, i.e. by taking into account the three sectors. The budgetary separation between education, health and the municipal sector make it difficult to have an integrated and transparent view of central government financing at the municipal level. In addition, a close monitoring of transfers from the municipal sector to the other two sectors should be undertaken.

Without calling into question the financing modalities of education and health funds,[28] consolidated accounts for each municipality should be presented instead of three different budgets.

Central government transfers at the national level should be better co-ordinated, at least among the largest contributing ministries (education, health, interior/regional development, social development, housing and urban development, etc.), as well as at the regional level, particularly by the future presidential delegate who should be responsible for co-ordinating the activities of the deconcentrated state territorial administrations, including the SEREMIS.

In the same vein, the formula of co-financing instruments through contractual agreements such as programming contracts in Chile (*convenios de programación,* CP) could improve the co-ordination of funds from various sources for municipal projects. However, the role of municipalities in CPs has been limited so far and Chile should promote the use of this instrument by municipalities through different incentives (see Chapter 6).

Reviewing the National Fund for Regional Development (FNDR)

As underlined above, the role and purpose of the FNDR has been altered. While conceived originally as a tool for regional development and territorial compensation, projects submitted to the FNDR come largely from municipalities seeking to finance basic local infrastructure and services that they cannot finance with their tight budgets. The FNDR portfolio thus becomes largely the sum of local demands rather than the

integration of different regional initiatives attached to a regional development strategy. In addition, because requests for funding from the FNDR go through an ex ante cost-benefit analysis on a project-by-project basis at the national level, it is very difficult to achieve synergies between investment projects (OECD, 2009a, 2013e and 2014a). In addition, smaller rural municipalities are at a disadvantage in the open competition required to access FNDR funds. Their projects are often not sufficiently competitive according to the ex-ante social profitability evaluation of the project. They also lack the technical capacity to apply.

Several improvements could be made to the FNDR to better achieve its initial goal while ensuring a more equal access to the funds. The FNDR could be split into two segments, with one fund strictly dedicated to meeting regional development objectives and the other aimed at supporting municipalities in order to support productive or local economic development. This segment could also be used to support inter-municipal projects (see Chapter 6). The territorial dimension could be also integrated in the ex-ante project evaluation. This evaluation could incorporate additional variables that consider the cost of providing public services in scarcely populated areas in order to reduce the disadvantages of rural municipalities when competing for FNDR resources (OECD, 2014a). The FNDR should not be used to finance basic needs that should be covered by other grants or own-source revenues.

Shifting from earmarked to general purpose grants, the number of earmarked current and capital grants could be reduced.[29] This system encourages municipalities to operate in silos, without co-ordination across sectors (e.g. education, transport, housing, health, etc.) or across levels of government. These practices are major obstacles to effective public investment (Box 2.5).

Box 2.5. **Recommendation of the OECD Council on Effective Public Investment across Levels of Government**

When done well, public investment can be a powerful tool to boost growth and provide a solid infrastructure for economic and social development as well as to leverage private investment. In contrast, poor investment choices or poor management of investments is a waste of resources. It erodes public trust and may hamper growth opportunities.

OECD member countries have acknowledged the importance of better governance for public investment by adopting the Recommendation of Effective Public Investment Across Levels of Government in March 2014. The Recommendation groups 12 Principles into three pillars which represent three systematic challenges for efficiently managing public investment: co-ordination challenges, subnational capacity challenges and challenges in framework conditions.

Box 2.5. **Recommendation of the OECD Council on Effective Public Investment across Levels of Government** *(continued)*



An implementation toolkit has been developed to provide basic guidance and help policy makers at all levels of government implement this principle in practice, providing concrete examples and best practices for countries at any stage of decentralisation.

Source: OECD (2014b), *Recommendation of the Council on Effective Public Investment across Levels of Government*, http://acts.oecd.org/Instruments/ShowInstrumentView.aspx?InstrumentID=302&InstrumentPID=319&Lang=en&Book; OECD (2015a), *Implementation Toolkit of the Recommendation on Effective Public Investment Across Levels of Government*, www.oecd.org/effective-public-investment-toolkit/.

Excessive use of earmarked grants is generally associated with low flexibility and low efficiency, particularly when the grants do not require matched funding (Bergvall et al., 2006). The grant system substantially reduces municipal decision-making powers, especially since, within each ministry, the use of funds comes with guidelines, norms (defined nationally) and strict controls, further restricting municipal real spending autonomy and policy discretion to match local preferences and address local needs. It is particularly detrimental to the efficient use of public money as well for effective public investment. In addition, such a piecemeal approach prevents municipalities from financing integrated local development programmes and co-ordinating different sub-projects.

There is evidence that the Chilean system is too complex and rigid. In their process of decentralisation, a number of OECD countries have reduced the number of earmarked grants and increased municipal discretion in intergovernmental transfers by reducing the share of earmarked and conditional transfers and creating or extending general-purpose grants based on a formula (Box 2.6). Chile could develop the use of general-purpose grants, sometimes tied to more results-based regulation, rather than specific use (OECD, 2013c).

In this perspective, a gradual and asymmetric approach could be followed. In fact, it seems necessary to differentiate fiscal arrangements according to both the needs of municipalities and their capacity to meet management requirements that the change would imply. It is also essential to empower municipal actors to deal with the consequences of their decisions.

Experimenting with general capital grants for large municipalities

One recommendation would be to move away from the exclusive model of specific grants and subsidies and allow municipalities to finance integrated programmes that include different local development projects. It would consist in experimenting with general capital transfers based on a formula.

In addition, establishing a general capital grant would limit administration costs. It would also avoid compromising the overall investment programme coherence by suspending the risk of not obtaining the specific subsidy for a particular project which is part of the overall strategy. To set up such a general capital grant, it would be necessary to consolidate several different ministerial funding lines into one main transfer dedicated to investment. SUBDERE would be probably the ministry best suited for distributing to each municipality its share according to allocation criteria.

However, a system of general capital grants is more appropriate for large urban municipalities, which have important investment programmes. A system of specific subsidies should therefore be maintained for small and rural municipalities, according to existing but simplified procedures for project application and reporting. The FIGEM methodology and could be used to determine the eligible municipalities that could benefit from the system of general or block grants.

Following this same logic of differentiated treatment depending on municipal capacity, the recommendation on general capital grants could be accompanied by authorisation, granted to eligible municipalities, to access borrowing to complement the investment financial plan. This would also entail enlarging municipal taxation power in order to increase municipal creditworthiness (see below "Expanding municipalities' borrowing abilities").

Box 2.6. **Fiscal decentralisation reforms in selected OECD countries: From earmarked grants to general purpose grants**

United Kingdom (England): Recent measures have granted local authorities greater freedom and flexibility and more control over budgets. The number of earmarked grants decreased from more than 90 to less than 10. A new single general-purpose, formula-based grant ("Local Services Support Grant"), grouping all previous earmarked grants, was introduced in 2013. Only school funding and the new public health grant remain earmarked.

Netherlands: In the process of gradual fiscal decentralisation, earmarked grants have been substantially reduced from 500 in the 1980s to 136 in 2006 and 37 in 2011 (Dexia-collective work, 2008; Allers, 2011). In the 1990s, a greater share of transfers was offered in the form of general grants, giving the municipalities freedom to decide on the allocation of the resources. Municipal-specific earmarked grants dropped dramatically: their share decreased from 61% of municipal revenue in 1990 to 18% in 2011. The main block grant, the Municipalities Fund, become more significant to represent 36% of municipal revenue in 2011. Indexed to the trend rate of central government expenditure, this general fund is an equalising grant redistributed among municipalities according to about 60 criteria, an allocation system considered to be one of the most complicated in the world but reflecting the Dutch attachment to equity (Allers, 2013). The objective of the equalisation system is to enable municipalities to provide an equal level of services to the population everywhere on the Dutch territory while maintaining a reasonable tax burden and equivalent tax rates.

Box 2.6. **Fiscal decentralisation reforms in selected OECD countries: from earmarked grants to general purpose grants** *(continued)*

Poland: The 2004 Act on Local Government Revenue profoundly modified the financing of subnational governments, which gained more financial autonomy, with a decrease in the share of central government transfers, including that of earmarked grants offset by increased shared tax revenues (higher proceeds from the personal income tax and corporate tax). The general grant (non-earmarked) constitutes today the most important grant. It is made up of several shares, including the education share, the equalisation share, the balancing share and the regional share. The education share is by far the largest, accounting for over 20% of subnational revenues. It aims at covering educational expenses, including teacher salaries, but it is not earmarked. The equalisation share (5% of subnational revenue) is allocated to all subnational governments with below-average tax capacities. The balancing share (only for municipalities and counties) aims at financing social expenditure while the regional share is a general grant calculated for each region. Earmarked transfers include specific transfers for tasks delegated by the central government (e.g. social spending) and for capital expenditure.

Korea: The 1988 Local Finance Act, which determines subnational financing, was amended several times in 2005, 2009 and 2011, in order to increase fiscal decentralisation and reform the tax and grant systems. The share of earmarked grants, called "categorical grants", has decreased substantially thanks to reforms replacing several earmarked funds with a general-purpose grant. It comes from revenue sharing between levels of government. Revenue sharing is divided between Regular Revenue Sharing (RRS) and Revenue Sharing for Decentralisation (RSD). The RRS accounted for 18.3% of national tax revenue. A whopping 96% of receipts are non-earmarked and allocated to subnational governments according to an equalising formula based on the assessment of standard fiscal needs and revenues. The remaining 4% is earmarked (natural disaster recovery, construction of public facilities, national project, etc.). The RSD system, financed through a decentralisation tax, was introduced in 2006 to finance the decentralisation of administrative functions.

Japan: The 2004 Trinity reform aimed at increasing the share of own revenues in local governments' budgets while decreasing their reliance on inter-governmental transfers. It included three major components: the transfer of tax revenues from the central government to local governments (creation of a tax-sharing system); a reform of the equalisation tax; the abolishment and reduction of national earmarked grants. After the Trinity reform, another round of reforms affecting transfers to local government took place in 2011 and 2012. It involved the conversion of earmarked grants towards general-purpose grants, hence increasing the autonomy of local authorities over the use of funds. In particular, a Local Autonomous Strategy Subsidy was created for public works, leading to less authority from the central government over transfers to local governments.

Sources: OECD (2017a), *Multi-level Governance Reforms: Overview of OECD Country Experiences* OECD (2014), OECD (2014c), *OECD Territorial Reviews: Netherlands 2014*; OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*. Allers, M. A. (2013). *Decentralization with national standards. The case of the Netherlands.*

Improving the local taxation system to enhance own-source tax revenue raising capacity

The modernisation of the financial system at the municipal level is not just a technical tax question whereby raising existing or levying new taxes would correct for taxation problems. If this option is chosen, it must be based on other changes that would ensure that the corrective measures to the tax instruments would also contribute to the modernisation of the system.

Consolidating municipal tax bases

With respect to the current tax system, avoidance of an increase in the tax rate in order to increase taxation effectiveness must include the expansion of the tax base and fairer increases.

- Regarding the territorial tax, the justification of many exemptions must be challenged as they siphon funds away from this tax. At the least, this tax, which generates an erosion in the tax bases, requires adequate compensation for the shortfall. Less radically, the threshold for qualifying for an exemption is also one area to adjust, for both the territorial tax and the waste management fee.
- Meeting deadlines for the periodic reassessment of property values is an ongoing challenge that should be dealt with cautiously. It would be worthwhile to modify the index applied to tax bases, without disrupting the system or making a decisive change, to ensure property values increase between reassessments. It would be more appropriate to replace the consumer price index with the construction index given the nature of the properties that constitute the territorial tax.
- In its current configuration, the reliability of the local tax system is contingent on the quality of land registry maps. The quality of this instrument must be safeguarded and improved, particularly so precarious living areas can be identified better. This would require investing in technically-advanced tools that monitor territorial transformations as well as excellent collaboration between the services of the central state (the SII), and their technical skills, and local public players, who have extensive knowledge of their territory.
- Without shifting to methods of evaluating tax bases using economic values (market value for the territorial tax and income indicators for the municipal business license), an effort to educate taxpayers would be welcome. This would contribute to attenuating the hostility resulting from taxpayers' misunderstanding of the logic behind the taxation process.

Extending municipal officials' decision-making authority on taxation

In the current configuration of municipal taxation, the authority of elected officials at the municipal level is quasi non-existent. They can set the rate of the municipal business license within a relatively narrow range and set the scale for the waste management fee. The decentralisation process should introduce the possibility of empowering them with taxation authority. This could take two forms:

- To make their territory a more attractive place to do business, local authorities could be given the power to offer tax breaks, whether total or partial, general or limited to certain sectors, or over limited or unlimited periods of time. Being able to decide on deductions would promote social or family-oriented policies while contributing to local economic development (but would require co-ordination with other public or private players). The local level would assume responsibility for the fiscal consequences (shortfalls) resulting from decisions related to municipal tax autonomy.
- Symbolically, empowering local authorities with the ability to set tax rates on "local" taxes is an avenue to explore along several different lines. The most cautious would be to widen the rate range within which the municipal business license tax can be set. More radical would be the freedom to cap the territorial tax.

The possibility of provoking a substitution risk between taxes (e.g. between the territorial tax and licenses), motivated by opportunistic or electoral reasons, would be eliminated by tying the two rates to one another.

The current system of both the SII (tax basis and assigning roles) and the Public Treasury (collection) is fundamentally solid, in light of the savings it generates related to tax management, the technical competences mobilised for its administration and the security ensured in its collection. Administratively sound, it is compatible with the decentralisation process.

Diversifying municipal resources

Given the limited practice of the municipalities in Chile concerning own revenues other than taxation, the room for improvement is substantial. It is worthwhile to begin considering a loosening of the regulatory limitations and fiscal constraints concerning these categories of own source revenues such as user tariffs and fees, property income, concession revenues, etc. and to make up for their insufficient yield.

Making the most of tariffs and user fees within an inclusive perspective

Municipalities should be supported to further charge for services they provide in a range of areas, such as recreational, cultural or sporting, social activities, management of networks, public transports, etc. Raising tariffs and user fees would allow municipalities to substantially increase investment in infrastructure.

In particular, tariffs and user fees are widely seen as the most appropriate source of revenues for metropolitan areas to finance the operation and maintenance expenses of infrastructure (e.g. parking fees, transport fees, fees on other public services including waste, water, energy). Large urban areas could also charge for harmful effects, through "smart taxes" and fees, related to congestion, pollution, road safety, waste of time, quality of life, health and environmental destruction resulting from excessive car use in urban areas. For example, the revenues arising from congestion charges adopted in London, Seoul, Singapore, Oslo, Milan, Berlin or Stockholm have been used to finance urban public transport and other urban facilities (OECD 2015c, OECD 2013d). In Chile, such new approaches of "green taxation" could be explored in large Chilean urban areas given the high pollution rate in cities.

An appropriate legal framework and pricing scheme would need to be established, allowing users to be charged according to their financial capacity. There are several methods to leverage user fees. When designed well, they can reconcile economic effectiveness and social justice concerns thanks to an adjustable rate scale.

Increasing property income and exploring "municipal companies"

Property income from financial and non-financial assets (interest, dividends, rents and sales of land and buildings) is a potential source of revenue for municipalities, which is under-exploited in Chile. It could provide non-negligible additional revenue for investment. It would require an improvement in the methods used to manage municipal assets.

This limitation also results from the constraints imposed on the use of municipal companies according to article 11 of the LOCMUN (see Chapter 1). Chile could envision loosening its legal framework and allowing for the creation of municipal public enterprises or joint ventures (public-private). Chile could look at international experiences to develop its own model of municipal companies. In the OECD, and Colombia as well,

local public companies are widespread and provide substantial resources to their "mother municipalities" (Box 2.7). Of course, these companies must be managed efficiently and levels of economic profitability and quality of service must be adequate.

Box 2.7. **Local public companies in the OECD and Colombia**

Standing at the crossroads of the private and public sectors, local public companies (LPC) are independent local public entities organised under private law and delivering local public services. They can be 100% publicly funded or a combination of public and private capital (joint ventures, public authorities holding a minimum share of the capital of these limited companies). They aimed to be flexible and responsive businesses, while upholding the general interest and community values (French Federation of Local Public Companies).

In Europe, LPCs are particularly common and typically used to manage municipal services in sectors such as water and sewerage, energy, waste collection and treatment, local public transport, social services, healthcare, but also urban planning and development, etc. LPCs are active in a wide range of services, very often in basic infrastructure services where market failures or high transaction costs are present.

According to the French Federation of Local Public Companies, local public companies form a network of around 25 000 enterprises in Europe, including Austria (1 800), France (1 220), Germany (around 8 500), Italy (3 500), Poland (2 500), Sweden (1 800), Finland (950) and Spain (1 150). In some European countries, the emergence of LPCs goes back to the end of the 19th century, in particular in Nordic countries such as Finland or Sweden where the first *Kommunala företag* (municipal companies) were created in the 1870s, but also in Belgium with the *intercommunales* created in 1897, in Germany (Stadtwerke) and in France with the creation of local mixed-economy companies in 1926. In Southern, Central and Eastern Europe, LPCs are more recent, but their numbers are growing rapidly. In Spain, LPCs are widespread and cover activities such as municipal planning, land development and housing companies, funeral services, public transport and urban maintenance and environmental services. In other OECD countries, LPCs are also active in public service delivery such as in Korea (around 300) and Japan (around 8 700, particularly active in the sewerage businesses (42% of all LPCs), water supply (24%) and hospitals (7%).

In **France,** LPCs cover 40 areas such as urban planning, housing, tourism, transports, energy, waste management and water, have near 60 000 employees and generate turnover of more than EUR 12 billion (2014) for a share capital of EUR 3.89 billion. French local public enterprises have one of three different legal statuses:

- Mixed-economy companies (*Sociétés d'économie mixte* - SEM), which are the most traditional and significant type of LPC in France, but have to comply with competition rules. A SEM requires at least two shareholders, both public and private. Between 50% and 85% of their capital is held by public authorities. Their activities are not limited to the territory of their respective local authorities. They can operate in all areas and for all stakeholders.
- Local public companies (*sociétés publiques locales* - SPL): existing since 2010 in France, SPL are tools for co-operation among local public partners, requiring a minimum of two local authorities. They cannot include private shareholders. As they are considered in-house tools, they do not have to comply with competition rules. As a result, they can operate only in the local authority's individual territory.
- Mixed-economy companies having a single corporate purpose (*Sociétés d'économie mixte à opération unique* - SEMOP). Passed into law in 2014, the SEMOP are "institutionalised public-private partnerships" giving the municipality the opportunity to choose at least one private partner, which can hold between 15% and 66% of its capital. They are created for one single purpose and therefore have a limited duration.

Box 2.7. **Local public companies in the OECD and Colombia** *(continued)*

In **Colombia**, some large cities benefit from dividends from local industrial and commercial companies. *Empresas Públicas de Medellín* (EPM), the city's profit-making publically-owned utility, contributes 30% of financial surplus to the city's administrative budget according to the Governance Framework Agreement signed between the city and the company. In addition to this regular annual contribution, the EPM also provides discretionary grants to the municipality for carrying out its social development programmes, especially in the sectors of education, employment, recreation programmes, environmental improvement, mobility and urban infrastructure. In 2011, ordinary transfers accounted for 55% of total contributions while 45% were provided by extraordinary transfers for joint programmes and investment projects between the EPM and the city of Medellín. Roughly 40% of own-source revenues (or 24% of total revenues) of the city of Medellín come from dividends from the EPM. However, the EPM remains a unique case. There are however other interesting examples such as the Water and Sewerage Company of Bogota (*Empresa de Acueducto y Alcantarillado de Bogotá*), whose income is equivalent to 24.5% of the revenues of the municipality, reaching a surplus of COP 338 billion in 2014, or the Mass Transport Company of Cali S.A. (*Empresa de Transporte Masivo de Cali* S.A.), whose income represents 14% of the revenue of the municipality, with a surplus of COP 100 billion in 2014.

Sources: French Federation of Local Public Companies (2017), Overview of LPEs in Europe, Fédération des Entreprises Publiques locales, http://www.lesepl.fr/pdf/panorama_epl_europe.pdf; Dexia (2008), Subnational governments in the European Union: organisation, responsibilities and finance; Saussier, S. and M. Klien (2014), *Local Public Enterprises: A Taxonomy*; OECD (2016a), *Making the Most of Public Investment in Colombia: Working Effectively across Levels of Government*; OECD (2016b), *OECD Territorial Reviews: Japan 2016*.

Profiting from the use of the public domain

The use of the public domain could also generate more revenue for municipalities. Chile recently adopted a law with this in mind. Law No. 20.958 of 15 October 2016 establishes a system of contributions to the public space. Although the contribution does not really consist of direct income, it is a public expense that is avoided. This is of real social and economic interest even if the financial impact remains limited.

To go further in this direction, Chile could draw inspiration from international practices in land-based financing instruments. Colombian cities are leaders in Latin America in this domain, but there are other interesting arrangements in North America, Europe and New Zealand (Box 2.8).

Box 2.8. **Land-based financing instruments: Focus on several international practices**

Several Colombian cities are leaders in land-based financing instruments in Latin America, with a long-standing experience in this field. Inspired by the constitution which stipulates that one of the state's duties is to capture the added value generated by public actions, Colombia created, quite some time ago, two interesting revenue-raising mechanisms aimed at financing urban developments by capturing the capital gains from property and land generated by public infrastructure projects: the *Contribución de valorización* (created in 1921) and the *Participación en Plusvalías* (1997). The first one is a betterment levy (also called a special assessment), i.e. a "compulsory charge imposed by a government on the owners of a selected group of properties to defray, in whole or in part, the cost of a specific improvement or services that are presumed to be of general benefit to the public and of special benefit to the owners of such properties".

Box 2.8. **Land-based financing instruments: Focus on several international practices** *(continued)*

The second mechanism aims at recovering part of the increased land values resulting from the change in land-use regulations (changing zones, change in the designation of the type of land, change in density regulations). These instruments are used mainly by large cities and have limited penetration beyond them (World Bank, 2012). For example, from 1950 to 1990, this tool allowed the city of Bogota to finance more than 30 public works (roads, bridges and public spaces). In 2014, Bogota collected COP 231 billion via the *Contribution de valorization* and COP 11 billion via the *Participación en Plusvalías*. Other cities that stand out for their collection of the *Contribución de valorización* are Cali, Bucaramanga and Barranquilla.

There are other schemes in the OECD of land value capture such as "development charges" in Canada and in the United States or tax increment financing districts in the United Kingdom. In New Zealand, councils require development rights or development contributions from developers as part of granting consent for development so that developers bear the costs of new infrastructure (roads, water and wastewater infrastructure, and community facilities). They account for around 2% of their revenues. In Denmark, the extension of the metro line in Copenhagen was financed through fees from the development of the Ørestad area of Copenhagen (OECD, 2009b). New York City is financing the Hudson Yards subway line extension and station through the issuance of bonds by a special purpose vehicle, the "Hudson Yards Infrastructure Corporation", with debt service guaranteed by innovative sources of revenues, including: 1) tax equivalency payments, provided by the city in anticipation of future tax revenues from land value increases; 2) payments in lieu of taxes, which offer land tax exemptions to project developers in a specific area; and 3) transferable development rights from the transfer of public property land and building rights (OECD, 2013f).

Source: OECD (2016a), *Making the Most of Public Investment in Colombia: Working Effectively across Levels of Government*; World Bank (2012), *Amplifying the Gains from the Urban Transition, Colombia Urbanization Review*. OECD (2009b), *OECD Territorial Reviews: Copenhagen, Denmark 2009*. OECD (2013f), Mobilising private investment in sustainable transport.

Better exploiting municipal concessions

Only a few municipalities have developed municipal concessions and receive revenues from them, despite some progress introduced by Law No. 19.865. Most of the time, concessions at the local level are managed by the central government, without co-ordination with municipalities or their participation in the contract. Chile could consider to "municipalise" several existing concession contracts or, in case of legal impossibility, to give municipalities the right to look into the conditions of the contract and to intervene in their practical implementation (regulation of the public service and adaptation to local needs or changing circumstances), as well as to monitor the quality of services. The municipalities concerned should also be able to receive part of the concession revenues. For future concessions, Chile should identify the main legal, financial and technical obstacles to building genuine municipal concessions and explore ways to facilitate their development so that they become a strategic municipal tool for local development. Developing municipal concessions will however involve increasing own-source revenues and providing access to external funding sources (i.e. credit).

Supporting the development of PPPs for large municipalities

Although municipalities are engaged in the development of public infrastructure, it would be appropriate to examine the possibility of large municipalities to engage in public-private partnerships (PPPs). PPPs can be powerful tools to accelerate the realisation of investments but the calibration of financial commitments must be studied

closely to ensure that the sequence of subsequent payments is compatible with the financial situation of the municipality. To do so, elected officials need to be able to rely on highly competent and experienced teams, given the complexity of the financial and legal structures and the level of technicality of PPP projects. This high-level of expertise to design, implement, administer and monitor PPP projects is generally not available outside the bigger cities.

In that perspective, the Chilean government could launch a programme to build and reinforce municipal sector capacity to effectively engage with the private sector in PPPs. It could establish a public-private partnership unit dedicated to the municipal sector to transfer its know-how as well as provide financial resources to municipalities to access technical support. Chile could look at the UK model of the Private Finance Initiative (PFI) programme or French "public-private partnership contracts". Other best practices are Colombia and Mexico, which have developed highly decentralised models (Box 2.9). Nevertheless, PPP contracts at the subnational level remain limited in Colombia because of weak capacities to design and structure projects.

Box 2.9. **Subnational PPPs in Colombia**

PPPs initiated by subnational governments are still limited compared to PPP projects executed at the national level. However, there are several examples, particularly in large cities, of PPP projects that have been implemented successfully. Since the 1994 Law on Residential Public Services (*Ley de Servicios Públicos Domiciliarios*), which promotes a system of private participation in the provision and financing of public utility services, several important cities provided their urban services through concessions. For example, in Barranquilla, "Triple A" will provide water, wastewater and solid waste services for the metropolitan area under a concession contract until 2033. In the transport sector, one can cite the Transmilenio in Bogota, developed in 2000, to upgrade and operate a bus rapid transit system through a concession contract involving the Colombian government, the city and a number of private companies. Needless to say that Transmilenio has been adopted as a role model for the public transport system in over 100 cities covering every continent. Medellín has also been very active in this field, and several urban projects have been implemented through public-private partnerships with business or non-governmental organisations: Parque Explora, Botánico, Convention Bureau, Plaza Mayor convention centre, Salvia Salud, amongst others. Proantioquia, one of several business coalitions in the city, and the Chamber of Commerce of Medellín support many municipal initiatives, such as the well-being survey "*Medellín, ¿Cómo Vamos?*" as a clear example regarding the involvement of civic associations in the matter. Following the 2012 PPP law creating a clearer and more stable regulatory framework for PPPs, called "*Asociaciones Público Privadas*", Medellín decided to create a legal, administratively and financially autonomous entity entirely dedicated to PPP development, which is the first in Colombia at the subnational level, the Public Partnership Agency (Agencia para las Alianzas Público Privadas). The agency's mission is to promote, manage, evaluate and structure investment projects with high socio-economic impact involving public and private actors. It has been operational since June 2013 and several projects are already in the pipeline at different stages of development (Lleras Park urban renewal project, the football stadium, Nuevo Occidente, the urban highway Parques del Río, etc.). This agency will be a major step to upgrade the level of knowledge on this matter for the municipality.

At the national level, the DNP is trying to support subnational governments in this field and has set up and manages a database to register PPP projects. An important step forward is the standardisation of projects through the CONPES 3856, which will reinforce expertise in the preparation of projects in subnational governments.

Source: OECD (2016a), *Making the Most of Public Investment in Colombia: Working Effectively across Levels of Government*, http://dx.doi.org/10.1787/9789264265288-en.

Expanding municipalities' borrowing abilities

In compliance with the strict budget rules and the rigorous management of public coffers, political and administrative leaders of Chilean economic policy are reluctant to accept the idea of bestowing municipalities with the power to borrow. These restrictive practices are fundamentally questionable from an economic point of view. In anticipation of future changes, Chile needs to consider the conditions under which borrowing would constitute an advantageous financing method for Chilean municipalities. In recent years, several attempts to change the regulatory framework and authorise municipal borrowing under certain conditions have been made under the initiative of SUBDERE but so far they have not come to fruition.

Why loosen access to credit for municipalities?

Without challenging the principles of healthy management of public finances in Chile, it is legitimate to ask if they are economically justified. It is also appropriate to examine less restrictive ways of accessing credit, while respecting prudential rules on borrowing.

From an economic perspective, using credit to finance capital stock (private or public) is doubly legitimate. First, it is justified on grounds of economic efficiency. Credit enables resources to be better allocated over time. Second, its legitimacy is based on observations related to fairness. Borrowing allows for better intergenerational justice because the distribution of a capital investment's advantages and costs are spread more evenly over time. It is fairer, from a social perspective, to require the future generations who will also enjoy the services provided by the investment to participate in the payment of that initial investment.

Borrowing is justified not only for economic reasons but fiscal necessity as well. Due to the nature and the level of their current revenue and expenditure, municipalities are not able to generate savings that would be enough, on their own, to invest in capital goods. Because capital transfers are insufficient, only credit can make such expenditure a reality. Without it, all such investments would be put off until savings accumulated to the point where the municipality could purchase the capital good outright. Once a particular stage of economic and societal development is reached in Chile, the question will arise – if it is not already relevant today – of whether it is suitable to limit, and thus defer, the increase in capital formation. In modern economies, credit is one of the keys to economic growth and social progress via the amenities it provides to companies and households. Restricting the development of capital can be a drag on productivity and competitiveness gains and keep the economy from achieving its potential growth rate. A lack of credit is also liable to alter the living conditions and the standard of living of households and thus could jeopardise social stability, which is another prerequisite for economic growth. Therefore, the issue is to understand the compatibility and the compromises that need to be made between financial considerations and economic implications. It is important to avoid a situation whereby compliance with fiscal discipline, particularly principles on balancing budget, is accompanied by an infrastructure deficit as the economy seeks to expand.

The search for a compromise between a financially healthy management strategy and one that drives economic growth sparks a reflection on what would constitute less-rigid access to financial markets for municipalities. The avenues should be explored by combining the implementation of appropriate prudential rules and the adaptation of institutional borrowing mechanisms to the wide diversity of municipal capacities.

The justification of credit-fuelled financing becomes more tenuous when debt sustainability issues arise. To prevent the solution from becoming a problem, several general principles should guide the implementation of prudential rules codifying the use of credit (see section on fiscal responsibility framework).

For which types of municipalities should access to credit be loosened?

Under the shared rules aiming to secure the finance system, the methods and use of borrowing instruments must be adapted to the needs of local public players and their administration and management capacities. Although it is impossible to meet the needs of all situations and spending behaviour, there are a few ways to adapt the system to case-by-case situations, which should be founded on the reality of fiscal practices.

Many Chilean municipalities may lack creditworthiness, i.e. they lack the financial ability to repay loans over time and the technical capacity to manage the debt and therefore are unable to issue bonds or borrow from financial institutions.

A first consideration could be given to the demographic size of the municipality or, more imprecisely, the volume of the municipal budget (i.e. there is a strong correlation between population size and budget volume, but there are exceptions), including the capacity to raise own source revenues and stability, predictability and "unconditionality" of (at least some) intergovernmental grants (Martinez-Vasquez, 2015). In fact, to make municipalities feel responsible for their financing decisions and to avoid "moral hazard" (the transfer of solvency risk to the state), municipal borrowers should be able to meet their loan repayments. Given the downward rigidity of current expenditure, this requires municipalities to be able to ask local taxpayers to contribute, i.e. be able to change their tax rates in order to raise additional resources.

Second, consideration should also be given to whether the municipality's administration has employees with the relevant financial and management skills. Different municipal borrowers require different solutions. Borrowing mechanisms should be adjusted according to municipalities' administrative needs and resources instead of applying a blanket legally-based solution. The FIGEM typology could be used in both cases.

Finally, to assess creditworthiness, it could be envisioned to establish a rating mechanism for municipalities, either internal (through an ad hoc system based on financial ratios and prior authorisation developed by SUBDERE and/or the CGR) or external, through international rating agencies, such as the system introduced in Colombia in 2003 by the Fiscal Transparency and Responsibility law, which law tightened regulations on credit supply (banking sector) and required that departments and large municipalities obtain satisfactory credit ratings from international rating agencies before they could borrow on the market.

Accessing credit in the form of loans or bonds

While the credit market is highly liberalised in the OECD, each country has its particularities when it comes to municipal external financing. However, while debt securities are the most widespread form of external funding for subnational governments (federated states and local governments) compared to loans, at local level only, i.e. without federated states, the situation is reversed: debt securities are less significant while loans are predominant (Box 2.10).

Tapping into capital markets

Tapping directly into the market via the issuance of bonds is a preferred solution in countries such as the United States, Canada or Japan. In the United States, state and local governments borrow money from investors to fund specific projects by issuing municipal bonds, which are tax-exempt. Municipal bonds are used for economic and social infrastructure projects across the United States. In Canada, municipal bonds are not tax-exempt but they are used widely to finance provinces and municipalities. In several provinces, municipalities can borrow through municipal financing authorities or corporations (MFAs or MFCs) that are centralised provincial lending agencies with high credit ratings at low interest rates and low transactions cost. In Japan, local government bonds (*chihousai)* are also widespread as article 230 of the Local Autonomy Law authorises Japanese Local Governments - prefectures, municipalities (cities, towns and villages) – Tokyo's special wards and local government co-operatives - to borrow money. In principle, local government bonds can be issued to finance specific purposes, which are stipulated in article 5 of the Local Finance Law. Local government's draft budget must include its detailed bond issuance plan, which must be approved by the local assembly in accordance with the Local Autonomy Law. The Comprehensive Decentralisation Law to increase local governments' autonomy and ensure smooth issuance of bonds, changed, in 2006, the bond issuance system from a prior approval system from the central government to a consultative system.

Box 2.10. **Accessing credit in the form of loans or bonds : OECD practices at the subnational level**

Amounting to 71% of total debt on average in the OECD, "financial debt" (loans and debt securities) represents the largest share of subnational government debt.

Debt securities represent a large share of subnational government debt, accounting for 45% on weighted average of total subnational outstanding debt in the OECD (31 countries). This is explained by the importance of bond financing for federated states in federal countries such as the United States, Canada and Germany.

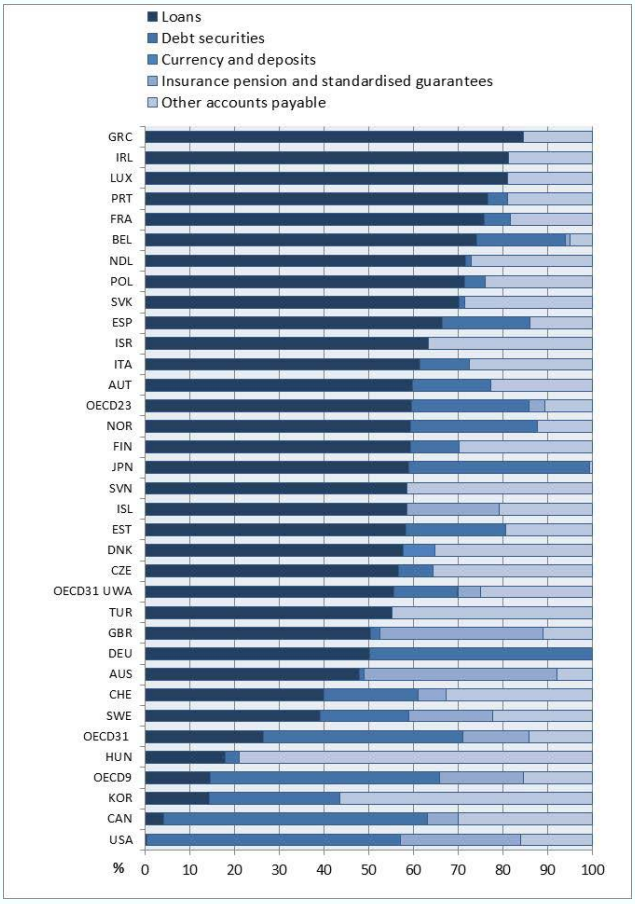
Although debt securities are also widespread at the local level in some unitary countries, such as Japan, Norway, Korea, Estonia and Sweden, bond financing is still low or non-existent in numerous unitary countries where it is often forbidden for local governments, restricted or rarely used.

Overall, loans accounted for 26% of total subnational government outstanding debt on weighted average in the OECD in 2014 but loans remained the most widespread form of external funding in numerous unitary countries, such as Greece, Ireland, Luxembourg, Portugal or France.

The share of "non-financial debt" varies greatly from one country to another. Other accounts payable (i.e. commercial debt with suppliers) amounted to 14% on weighted average at the end of 2014. Insurance pensions (i.e. liabilities related to funded or partially-funded civil servant pension schemes) represent 15% of subnational government debt on weighted average. Insurance pensions are non-existent (or not recorded) in 23 OECD countries.

Box 2.10. **Accessing credit in the form of loans or bonds: OECD practices at the subnational level** *(continued)*

Figure 2.40. **Breakdown of subnational debt by type of liabilities (%, 2014)**



Source: OECD (2016c), *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en.

Bonds are a potential solution for the largest municipalities and regions, which have a sizeable financial foundation. They are the only entities capable of floating bond issues that are, due to their size and regularity, financially viable and could do so through group issues backed by a banking pool as is the case in some countries. Size and frequency are the two conditions under which the municipalities will be able to take advantage of the favourable interest rate difference compared with bank-intermediated loans. It is expensive to tap into the capital markets (information disclosure/marketing, legal counsel, rating agency fees, intermediaries) and only amortised when issuance amounts are substantial and drawn out over time. Yet, size is not sufficient. Municipalities and regions can borrow on capital markets if they demonstrate to investors that they are creditworthy and have sufficient own revenues and stable grants to repay the debt.

Contracting loans with different types of lenders

For smaller municipalities (although the biggest municipalities can also make use of conventional loans), the use of the market is more hypothetical (except in the case of long-term group issues). In many countries, it is forbidden, restricted or rarely used by local governments. Therefore, local borrowing will have to make use of conventional bank loans. These factors explain why loans make up the bulk of local government borrowing in most unitary countries.

For smaller municipalities, specific loans come in the form of credit, which is in line with their infrequent borrowing needs and the nature of what the loans typically fund. For the more populated municipalities that can regularly invest in a range of capital goods, an overall loan financing the entire programme is an option that would reduce the administration costs of finance. Ingenuity in the banking field has led to the creation of a wide range of choices in terms of rates (floating or fixed, indexed, a variety of durations, amortisation methods). The shock wave of the financial crisis from 2007-2008 showed that local public entities must be cautious and must seek out good advice or risk falling prey to tempting loan offers that, after several years, turn into financial pitfalls ("toxic" loans and their soaring interest rates).

There are, however, several degrees of access to credit markets. In some countries, access is restricted to public lenders while in others, municipalities have free access to the public and private sectors, including commercial banks, savings banks, co-operative banks, or municipal funding agencies.

In only a few countries, municipalities do not have free access to the banking system and can only borrow from the ministry of finance or national debt office. This is the case in Latvia where municipal loans must be contracted with the national treasury or within specific funding programmes. Borrowing from another institution must be justified and authorised by the Ministry of Finance if it can be proved to the Board that the other institution offers better borrowing conditions than the state (OECD/UCLG 2016).

In other countries, local governments can access the banking sector but the Treasury remains the main credit provider. In the United Kingdom for example, the Public Works Loan Board (PWLB) is a statutory body operating within the UK Debt Management Office, an Executive Agency of HM Treasury (Box 2.11). PWLB's function is to lend money from the National Loans Fund to local authorities, at interest rates that are set by the Treasury. PWLB is also in charge of collecting the repayments. Since the liberalisation of local government borrowing in 2004 (new prudential borrowing regime abolishing prior government approval to borrow), PWLB's functioning has evolved. A reform is currently under preparation to transform PWLB into a fully integrated public body within the Treasury. PWLB has around 75% market share in the local government sector.

Box 2.11. **The transformation of the UK Public Works Loan Board**

The Public Works Loan Board (PWLB) is a statutory body which originated in 1793 and became established on a permanent basis in 1817. It is responsible for issuing central government loans to local authorities and other authorised borrowers. Since 1946, the PWLB has comprised twelve independent commissioners appointed by the Crown to hold office for four years. The Board's accounts are audited by the comptroller and auditor general whose subsequent reports are brought before Parliament.

The day-to-day operations of the PWLB have been delegated to the UK Debt Management Office (DMO), since July 2002. Since 2004, local authorities have been responsible for making their own borrowing decisions without government consent under the prudential regime in which any borrowing is automatically secured against authorities' revenues.

Because of these transformations, the UK government has proposed to change the governance arrangements relating to the function of the PWLB. It has launched a consultation in May 2016 proposing the abolition of the PWLB and the transfer of its functions to another body with a suggestion that the body to which the functions are transferred should be the Commissioners of the Treasury. The rationale is that whilst the role of PWLB is no longer required, the lending functions are still needed and transferring them to the Treasury broadly aligns policy and operational responsibilities with current practice.

Source: PWLB (2016) Transfer of functions from the Public Works Loan Board: response to the consultation Paper.

Several European countries use their national public banks to act as a lender to local governments, considering that a government vehicle can limit the cost of debt for local governments. They generally offer advantageous funding costs compared to commercial banks, thanks to the guarantee offered by the state and its excellent rating on capital markets (depending on sovereign rating). National public banks sometimes have a large market share in the local government sector, especially in times of crisis when commercial banks are more reluctant to lend (cf. credit crunch in Europe during the 2008 global crisis). Several public banks play an important role on the local government borrowing market such as in France (Caisse des dépôts et Consignations), Germany (KFW Kommunalbank), the Netherlands (N.V. Bank Nederlandse Gemeenten – BNG), Italy (Cassa Depositi e Prestiti S.p.A. - CDP), Poland (BGK), Norway Kommunalbanken Norway (KBN) or FINDETER in Colombia (Box 2.12).

Box 2.12. **The role of national public development banks in the financing of subnational governments: Takeaways from experiences in OECD and Latin American countries**

Norway: Kommunalbanken Norway (KBN), a 100% owned state government funding agency created in 1926, provides loans to the subnational government sector under attractive conditions, performing an important public policy function in providing such low-cost funding. KBN enjoys a very strong market position with a market share around 45% in 2016.

Netherlands: N.V. Bank Nederlandse Gemeenten (BNG Bank), established in 1914, is the largest lender to the Dutch public sector and is wholly owned by Dutch public entities (50% by the state and 50% by municipalities, provinces and a district water board). This ownership structure has been stable since 1925. BNG has the explicit public policy mandate to act as the lender to the local government sector. BNG Bank's market share of lending to local governments is 66% (in terms of outstanding loans) in 2016 and 70% when new loans are considered.

Box 2.12. **The role of national public development banks in the financing of subnational governments: Takeaways from experiences in OECD and Latin American countries** *(continued)*

Italy: Cassa Depositi e Prestiti S.p.A. (CDP) is a joint-stock financial company under public control. It is owned by the Ministry of Economy and Finance (82.77%) and banking foundations. Most of its funding comes from post office savings accounts. Since CDP's founding in 1850, the institution, considered a "service of general economic interest" has provided financial support for public entities in the form of loans and project finance (economic support for long-term projects). CDP also participates in infrastructure equity funds that invest in innovative and responsible service sectors. CDP's market share on the subnational public sector is around 48%, the core segment being the debt stock of local authorities, followed by that of regional governments.

France: Caisse des Dépots et Consignations (CDC) is the French cousin of the Italian CDP and the German KfW and also enjoys good funding conditions, which allow to finance the public sector. For example, CDC manages the funds from the tax-exempt savings deposits by the French banks, the main product being the "*Livret A*". Most of these funds are used by the CDC to finance French public sector social housing companies and local and regional governments (LRGs) through a total package of EUR 20 billion that the CDC has made available for local authority lending. The CDC also finances a number of local government projects by providing equity financing for housing, urban renovation, public facilities, digital infrastructure and renewable energy programmes.

Colombia: FINDETER (*Sociedad Financiera de Desarrollo Territorial S.A.*) is a public development finance agency created in 1989 and owned by the Colombian government (92.55%) and departments to fund significant local and regional infrastructure projects. FINDETER acts as a second-tier lender, encouraging first-tier lenders (commercial banks) to enter into direct relationships with local governments by rediscounting loans that commercial banks make to local borrowers. Therefore, it makes it more financially attractive for commercial banks to lend to local entities and it allows longer maturities at attractive rates to be offered. For its funding, FINDETER relies on international financing (Inter-American Development Bank, World Bank, Agence Française de Développement) and financial markets, receiving very high credit ratings. According to the most recent data from July 2014, FINDETER has 1 838 projects underway in 320 municipalities and 29 departments.

Sources: Moodys - Bank Nederlandse Gemeenten N.V. Semi-annual update – June 2016, Standard and Poors - KBN Kommunalbanken Norway – July 2016, Cassa Depositi e Prestiti S.p.A Annual report 2015, Fitch Ratings - Caisse des Dépôts et Consignations (CDC) Full Rating Report – May 2016; OECD (2016a), *Making the Most of Public Investment in Colombia: Working Effectively across Levels of Government*.

The development of local government funding agencies

Finally, inspired by the Nordic model of local government funding agencies, which is long established in Sweden, Finland and Denmark, several new agencies have emerged recently in the OECD, under the aegis of local authority associations in particular in France, New Zealand and the United Kingdom (Box 2.13). The goal of these pooling mechanisms is to provide participating municipalities the possibility of tapping into the bond markets through the agency in exchange for an initial capital contribution. Pooling demand for capital has a number of advantages, in particular economies of scale, higher volumes and liquidity, and diversified products, which can lead to significant cost benefits for local governments (Andersson, 2014).

Box 2.13. **The development of local government funding agencies in the OECD**

Local government funding agencies now exist both in decentralised and centralised institutional contexts. The first municipal funding vehicles were created in the Nordic countries: KommuneKredit in Denmark set up at the end of the 19th century (1898), Kommuninvest i Sverige AB in Sweden (1986) and Municipality Finance PLC in Finland (1989). In Belgium, the Crédit communal de Belgique, now a national public bank (Belfius) was also a municipal co-operative bank dedicated to the financing of member municipalities when it was created in 1860. These institutions have different organisational structures, but they have many similarities:

- They are owned by subnational governments, and they benefit from various forms of "last resort" support mechanisms from their owners. In Denmark, all Danish local authorities have voluntarily joined while in Finland and Sweden, the participation is 80-90% of subnational governments.
- They are not-for-profit entities with the sole purpose of providing competitive funding to subnational governments. In the case of Sweden for example, before the creation of Kommuninvest, local authorities were heavily reliant on bank loans for their investments and competition among the banks was not optimal, showing signs of becoming an oligopoly, imposed high interest rates on local governments that did not reflect their creditworthiness (Andersson L. M). Given the unfavourable situation, a group of local authorities in a region in central Sweden took the initiative to create Kommuninvest.
- They provide funding exclusively via the international and domestic capital markets, rather than via deposits, benefiting from a joint and several guarantee from its members.
- They hold big market shares in subnational government lending in their respective countries: more than 90% for KommuneKredit in Denmark and around 50% for Municipality Finance PLC in Finland and Kommuninvest i Sverige AB in Sweden.
- They have low-risk credit portfolios. Their 100% exposure to individual local governments is mitigated by the strength of subnational sectors in the different countries. These three local government funding agencies are all AAA-rated.

Amid the backdrop of the global crisis, new local government funding agencies have emerged in the OECD. In New Zealand, the NZ Local Government Funding Agency Ltd (LGFA) was created in 2011 to provide efficient funding costs and diversified funding sources for the country's local authorities. It was incorporated as a limited liability company under the 1993 Companies Act on 1 December 2011, following the enactment of the Local Government Borrowing Act 2011. As LGFA is majority owned by councils, it constitutes a "council-controlled organisation". As of November 2016, LGFA had 31 shareholders (New Zealand Government for 20%; and 30 councils (out of 78 in the country) for 80%). The agency had 51 Participating Local Authorities in November 2016, covering 97% of New Zealand's local government debt.

In France, *Agence France Locale*, was created by 11 subnational governments (one region, three departments, four inter-municipal co-operation bodies and three municipalities) in December 2013 as a result of new banking legislation dated 26 July 2013. It was granted a banking license on January 2015. Agence France Locale is 100% owned by French local authorities. Its mandate is to raise cost-efficient resources in capital markets by pooling together the funding needs of all member local authorities. It aims to provide French local authorities with alternative funding sources: its target market share is 25% (to be compared to 3% in 2015). It will lend a maximum of half its members' annual borrowing needs (or 100% if the amount requested is below €1 million). There were 147 local government members as of May 2016, from 98 inhabitants to 3.7 million and representing 11% of the French subnational debt.

Box 2.13. **The development of local government funding agencies in the OECD** *(continued)*

In the United Kingdom, the English Local Government Association (LGA), together with the Welsh Local Government Association (WLGA), started to explore the possibilities of creating a Municipal Bond Agency in 2011. This project was carried out in co-operation with Local Partnerships, an entity jointly owned by the LGA and the Treasury (50/50). The UK Municipal Bonds Agency Plc was created in June 2014 as a public limited company, owned by local councils and the Local Government Association. Its objective is to help local councils to finance their investment in projects including infrastructure and housing in an efficient and cost effective manner.

There are other examples of local government funding agencies worldwide such as Emissionszentrale der Schweizer Gemeinden of Switzerland, Municipal Finance Authority of British Columbia and The Alberta Capital Finance Authority Canada in Canada, Municipal Bondbanks of the US (such as Maine Municipal Bond Bank, Vermont Municipal Bond Bank, Sunshine State Governmental Financing Commission, etc.) or Japan Finance Organisation for Municipalities (JFM).

Sources: Andersson L.M. (2014), *Local Government Finance in Europe - Trends to Create Local Government Funding Agencies*; AFL (2016) L'Agence France Locale: un nouveau modèle de financement pour les collectivités (Local Government Funding Agency Overview 2016); Vammalle et al. (2012), *A sub-central government perspective on fiscal policy in a tight fiscal environment*"; T Storkey & Co Limited (2015), Local Government Funding Agency.

Reinforcing training of municipal financial managers and officials

The empowerment of municipal teams and the increase in municipal competences require excellent administrative, legal and technical support. The modernisation of the municipal system requires investing in human capital, involving both elected officials and the employees on which they must count. With greater responsibilities, a more complex organisational structure and a wider range of intervention comes greater legal and financial risk for the municipality. Training programmes on management techniques and tools (including in the area of taxation and debt management) must be set up to support the increase in competences. Training is a gage of the continued commitment to the modernisation of the organisation and institution.

Technical support for assisting low-capacity municipalities on budgetary issues should been reinforced to enable them to gradually enhance their administrative and financial capacities (see Chapter 4). This support should also be provided to staff in charge of municipal public procurement. Many irregularities do not result from fraud but from errors and a lack of capabilities (Box 2.14). The Municipal and Regional Training Academy (*Academia de Capacitación Municipal y Regional*) developed by SUBDERE, which has proven to be useful and effective, could be further strengthened (see Chapter 4). Developing agreements with universities to provide technical assistance to municipalities could also be envisioned.

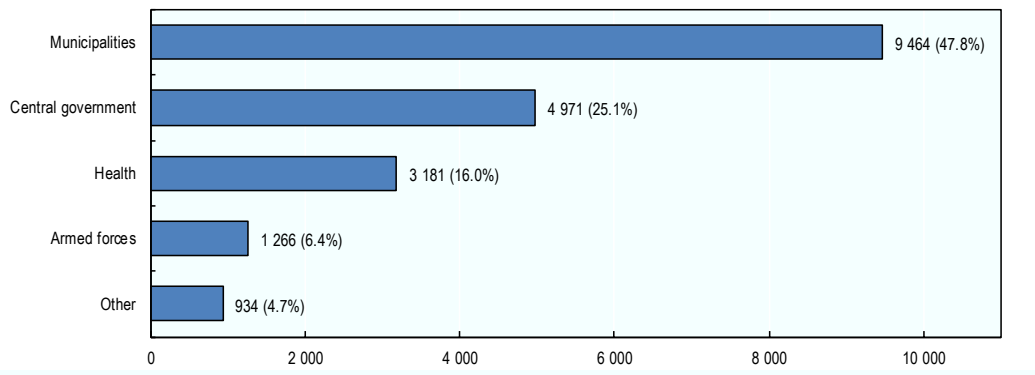
Aside from professional or managerial skills, this training must continue to safeguard the ethics of the public service. On a continent where the probity of the elite is not always guaranteed, Chile has an undeniable comparative advantage. According to corruption indices, only Chile and Uruguay, and to a lesser extent Costa Rica, have escaped the corruption trap that has sapped the spirit of the general public and created widespread mistrust (Chuaire and Scartascini, 2014).

Box 2.14. **Municipal public procurement: A high level of irregularities resulting from a lack of municipal capacities**

In 2015, municipalities accounted for 26% of all purchases through the public procurement system, Chile Compra. Despite this relatively small share, they accounted for 48% of claims for "irregularities in the purchase process". This rate reached more than 69% in the region of Maule but drops to around 35% in the Metropolitan Region of Santiago and Antofagasta.

There are several motivations of complaints including the fact that evaluation criteria are poorly defined (15% of claims), that the award does not comply with the evaluation criteria indicated in the tender (15%), that justification is insufficient or unclear to support an award or to declare it deserted (14%) or that the offer is discarded without justification (13%). The rash of irregularities are errors, not fraud, resulting from a lack of know-how and specialised personnel to conduct procurement within municipalities, in particular smaller ones where there is no dedicated staff while they still have to comply with complex procedures.

Figure 2.41. **Breakdown of claims for irregularities in the purchase process by public actors**



Source: Observatorio Chile Compra (2016) Annual report 2015.

Chile Compra was established in 2003 by the Law on public procurement No. 19.886 to standardise administrative procedures for contracting supply of goods and services necessary for the operation of public administration, at national and municipal levels. Public procurement amounts to around 3.5% of GDP. Through the law, municipalities have to ensure transparency, efficiency and equal competition concerning public purchasing. The objective is also to fight against corruption. Chile Compra has established an electronic system of public procurement and a bidding platform (www.chilecompra.cl and www.mercadopublico.cl) where all necessary transactions can be made. The Chile Compra Observatory was created to promote greater levels of probity and best practices in monitoring and detecting potential irregularities in the processes carried out by public agencies.

Source: Chile Compra, http://www.chilecompra.cl.

Greater citizen involvement in the fiscal decentralisation process: Towards a "fiscal pact" with citizens

Providing the appropriate responses to technical, administrative and legal questions is no guarantee of the success of modernisation or the changes and reforms it entails. In very few countries has tax reform not been a perilous endeavour. It creates a backlash from those who believe they stand to lose while those complaints are met with a meek

sceptical silence from those who stand to benefit. In European countries that are long accustomed to the massive presence of public power in the economic and social fabric (with high levels of public expenditure and taxes) consent remains a solid foundation, even though in the past two years this trust has tended to erode. Observers agree that one of the weaknesses of public power in Latin America is the lack of a strong "tax pact" within society. Because of its traditions, culture, political/administrative organisation, Chile is one of the countries in Latin America that is most capable of dealing with reform-related turbulence. Not only fiscal reforms must be communicated and explained, their social acceptance must be underpinned by awareness, and citizens must buy into and participate in the creation of reforms well before they are implemented. There are many possible channels and methods of such reform depending on the conditions and the environment in which citizens are living. While there is no guarantee of success, involving citizens is needed to ensure they understand the issues and how the changes will take place while dissipating or offsetting erroneous or ill-intentioned interpretations.

This inclusive and participative approach not only increases the chances the reform will be effective but is also one of the goals, in addition to its economic, tax and financial objectives, of decentralisation itself (see proposals of the Presidential Advisory Commission for Decentralisation and Regional Development and Chapter 5).

Conclusion

The modernisation of Chile's municipal financing system – economically and fiscally advisable – requires that the various players embark on a range of initiatives with timeframes that are sequenced over time. Without anticipating, at this point, the changes that will be made to the FCM which, in any case, are not independent from the political choices affecting the scope of competences or the nature of taxation, the following areas deserve consideration:

1. Improving the intergovernmental grant system, in particular for capital grants.
2. Strengthening the local tax foundation and the municipal tax autonomy.
3. Diversifying resources through the exploration of a more extensive use of user contributions, property income, concessions and other PPP schemes.
4. The political and cultural conversion to the belief that it is in the country's best interest to ease, in a controlled manner, dynamic municipalities' access to credit as the nation's infrastructure expands.
5. Acknowledging the reality that different financial models (particularly for credit) will fit the budget characteristics and conduct of some municipalities but not others (asymmetric fiscal decentralisation).

These recommendations would imply significant reforms of the Chilean fiscal framework, and indeed of the Constitution, which currently makes it difficult to establish differentiations with respect to specific productive sectors or subgroups. It is also necessary to take into consideration the impact of the current reform of the national system of public education, which will bring profound changes to municipal finance.

However, these are the priorities that could be explored in greater depth in order to advance the modernisation of the municipal system and extricate it from an antiquated and unsuitable framework so the country can reap the economic benefits of decentralisation and promote a fiscal framework that is conducive to municipal development and public investment.

In order to make public policies more effective, strengthening municipal fiscal autonomy requires developing appropriate arrangements that ensure more accountability and transparency and preserve fiscal sustainability. Both are closely interrelated and must be addressed jointly to ensure the success of the decentralisation reform.

Box 2.15. **Key recommendations for improving municipal finance**

1. Improve the system of intergovernmental grants, by:

- Developing a comprehensive and co-ordinated approach of the grant system:
  - Ensure a better co-ordination of central government transfers.
  - Central government transfers should be presented in a consolidated manner.
  - Develop the co-financing instruments such as Programming contracts.
- Reviewing the National Fund for Regional Development (FNDR):
  - The FNDR could be split into two segments, with one fund strictly dedicated to meeting regional development objectives and the other aimed at supporting municipal in order to support productive or local economic development.
  - The FNDR could be used to support inter-municipal projects.
  - The territorial dimension could also be integrated in the ex-ante evaluation of projects. It should consider the cost of providing public services in scarcely populated areas.
  - The FNDR should not be used to finance basic needs which should be covered by other grants or own-source revenues.
- Reducing the share of specific earmarked grants and developing the use of general purpose grants. In this perspective, a gradual and asymmetric approach could be followed
- Experimenting with general capital grants for large municipalities based on a formula.

2. Improve the local taxation system to enhance own-source tax revenue raising capacity, by:

- Consolidating municipal tax bases:
  - Examine the way to reduce the number and level of exemptions of territorial tax must be challenged. Exemptions call for an adequate compensation of the shortfall by the central government budget. The threshold for qualifying for an exemption should be adjusted (territorial tax and waste management fee).
  - Review the reassessment of property values. Review the indexation procedures of the property values between two measurement periods. Improve collaboration between the municipalities and the Internal Tax Service (*Servicio de Impuestos Internos*) to better evaluate the changes in property values.
  - Improve the quality of land registry maps. Invest in technically-advanced tools that monitor territorial transformations and develop collaboration between the state services and local public players who have extensive knowledge of their territory.
  - Business licenses: improve the adequacy of rules and procedures of territorial payment of the business licenses from the multi-located firms; review the minimum and maximum levels of the business licenses individual contribution.

Box 2.15. **Key recommendations for improving municipal finance** *(continued)*

  - Improve the recovery (*cobro directo*) of the waste management fee and encourage municipal efforts.
  - Develop tax service agreements between municipalities and the central administration (*Tesorería General de la República*) on recovering municipal taxes (especially, territorial tax, business licenses, waste management fee).
  - Educate taxpayers to develop their willingness to pay taxes.
- Extending municipal officials' decision-making authority on taxation:
  - Local authorities could be given the power to offer tax breaks, whether total or partial, general or limited to certain sectors, or over limited or unlimited periods of time.
  - Empowering local authorities with the ability to set tax rates on "local" taxes is an avenue to explore along several different lines: widen the rate range of the municipal business license tax; freedom to cap the territorial tax. To avoid substitution risk between the two taxes, the two rates could be tied to one another.

3. Diversify municipal resources by:

- Making the most of tariffs and user charges keeping in mind the importance of inclusiveness.
- Increasing property income and exploring the formula of "municipal companies".
- Profiting from the use of the public domain and developing land-based financing mechanisms.
- Better exploiting existing municipal concessions and developing new municipal concessions. Give technical and legal support to the municipalities during contract negotiations.
- Supporting the development of PPPs for large municipalities; launching a programme to build and reinforce municipal sector capacity to effectively engage with the private sector in PPPs. Establishing a PPP unit dedicated to the municipal sector to transfer its know-how as well as to provide financial resources to municipalities to access technical support.

4. Expand municipal borrowing abilities for the most capable local authorities under strict control, by:

- Implementing strict prudential rules, including the "golden rule" (see also section on fiscal responsibility framework at the municipal level).
- Developing of a rating system to identify "capable" municipalities based on FIGEM and other national or international systems of credit and risk analysis.
- Adjusting borrowing mechanisms according to municipal administrative needs and resources instead of applying a blanket legally-based solution.
- Controlling borrowing markets.

Box 2.15. **Key recommendations for improving municipal finance** *(continued)*

- This however implies increasing municipal creditworthiness (i.e. their financial ability to repay loans over time), which depends on municipal capacity to raise own source revenues and the stability, predictability and to some degree 'unconditionality' of intergovernmental grants, as well as the technical capacity to manage their debt.

5. Reinforce training of municipal financial managers and officials:

- In particular through the Municipal and Regional Training Academy.

6. Involve citizens more fully in the fiscal decentralisation process:

- Move towards a "fiscal pact" with citizens to develop their willingness to pay taxes. To this end, efforts to educate taxpayers would be welcome with a view to attenuating the hostility resulting from taxpayer misunderstanding of the logic behind the taxation process.

Fiscal responsibility framework at the municipal level

Chile has a strict fiscal framework for municipalities, requiring a balanced budget for both current and capital accounts. However, the municipal budgeting and accounting framework is particularly complex, thus lacking transparency, as it comprises three different budgets (the municipal sector, education, health) not to mention municipal corporations.

Chile could benefit from having a more comprehensive fiscal framework, presenting a consolidated view of municipal budgets, ensuring that decentralised responsibilities are financed with sufficient resources, ensuring a precise and transparent estimation of revenues in the budget and enhancing current budget balance rules. It could also implement a more transparent treatment of current municipal borrowing and consider relaxing the regulatory framework governing municipal borrowing. In that perspective, if Chile decides to allow municipalities (at least creditworthy ones) to issue debt, the government should develop a clear set of debt rules for "responsible borrowing" and debt monitoring instruments, allowing it to capitalise on potential efficiency gains from local autonomy, while meeting the objectives of sustainable longer term finances. Control and accountability should be reinforced through regular audits and controls ensuring the quality of fiscal data and including enforcement mechanisms and sanctions in case of non-compliance.

Municipal budgeting

The municipal budget documents

Municipalities in Chile have a general municipal budget and an additional separate budget document for each service that has been transferred from the national government (D.F.L. No. 1-3.063 from 1980). As a consequence, most municipalities in Chile have at least three different budget documents: the municipal, the education, and the health budget. Each one has different streams of revenues and corresponding expenditures. In addition, some municipalities have a budget document for cemeteries. Overall, there are 956 budgets related to municipal activities (Table 2.5). This budgetary system is a source

of complexity, which makes it impossible to have a consolidated view of all expenditure, revenues and liabilities at the municipal level (see Chapter 2).

Table 2.5. **Municipal, education, health and cemeteries budgets**

	Incorporated services				Total
Regions	**Municipalities (management)**	**Education**	**Health**	**Cemeteries**	
I	7	5	5	-	17
II	9	7	5	4	25
III	9	9	9	3	30
IV	15	14	13	2	44
V	38	34	32	3	107
VI	33	30	29	-	92
VII	30	30	30	3	93
VIII	54	54	54	17	179
IX	32	32	32	6	102
X	30	21	20	1	72
XI	10	10	-	-	20
XII	10	8	6	2	26
XIII	52	24	22	3	101
XIX	12	11	11	1	35
XV	4	4	4	1	13
Total	**345**	**293**	**272**	**46**	**956**

Source: Comptroller General's Office (2016), Informe Gestión Financiera del Estado 2015, Contraloría general de la Republica.

Each budget document follows the full budget cycle simultaneously. Most rules for the general municipal budget also apply to the other budget documents (e.g. transparency and reporting). However, each budget document has a separate planning or policy document, requiring consultation with different stakeholders and a separate budget approval by the municipal council. In addition, there is less flexibility in the health and education budget, where all modifications to revenues and expenditures require approval from the municipal council.

Having separate budget documents is not a common practice in OECD countries and can hinder efficiency in the budget formulation process. In the case of Chile, this is a reflection of the national government's control on services transferred to municipalities. The health and education budget are mainly financed with transfers from the national government, giving little autonomy to municipalities in the definition of their budget. The municipal modernisation agenda in Chile could consider breaking this silo in the budgetary process and increasing municipalities' autonomy in the definition of resources and prioritisation of expenditure. It should also consider introducing (or developing) multi-annual budgeting practices to help balance the present project-based approach towards integrated local development programmes co-ordinating different sub-projects.

The municipal budget process

In Chile, the municipal budget process follows the same calendar and structure as the national budget. It starts with a process encompassing revenue forecasting, planning and drafting that lasts from June to September, followed by discussion and approval from October to December, and the execution phase during the calendar year (Table 2.6).

Table 2.6. **Budget Timeline**

June/September	Planning and formulation process
First week of October	The mayor presents the budget proposal to the municipal council for approval
Second week of October	Negotiation of the budget proposal in the municipal council
December 15	Last day for approval
December 17 to 31st	The approved budget is communicated to all units along with instructions for the budget execution
1st January	Budget execution begins
30 April	Last day to submit the end-year report

Note: Fiscal year = calendar year (article 12 DL NO. 1.263 from 1975).

Municipalities have full autonomy to estimate their own revenues in the budget process. The finance unit is in charge of studying, estimating and proposing new revenues at the municipal level. Likewise, the municipal council is responsible for ensuring that estimated revenues are aligned with estimated expenditures. However there are no oversight mechanisms for ensuring a correct and unbiased estimate of own revenues.

During the budget drafting phase, the planning unit, the finance unit, the technical committee, and the units in charge of health, education and cemeteries inform spending units about the policies and annual targets defined according to the municipal development plan, the annual development plan for education and the plan for health and cemeteries. Based on this information, and taking into account past expenditure trends, spending units prepare their budget proposals. With the support of the planning and the finance unit, the mayor prepares the municipal budget document and sends them to the municipal council for approval (CGR, 2014). The education, health, and cemeteries budget are drafted with the support of the corresponding sectoral unit and sent to the municipal council for approval.

The municipal council is allowed to ask questions and propose changes to the mayor's proposal. However, the municipal council cannot increase total expenditure, which can only be redistributed or reduced, while expenditure established by law or agreements signed by the municipality are binding. If the budget is not approved before 15 December, the initial proposal from the mayor enters into effect.

Before the budget execution starts on the 1 January, the finance unit communicates the approved budget, the instructions for the budget execution, and the cash flows programme to all spending units. Budget expenditure should be registered in the municipal accounts, following the guidance and instructions of the Comptroller General's Office. Funds must be spent by 31 December and carry-overs are not allowed.

Before the end of April of the following budget year, the mayor must present an end-of-year report (*Cuenta Pública*) providing information on the budget execution balance and the statement of financial position, and a detailed description of municipal liabilities. The end-of-year report is available for public consultation and a summary of the report

should be distributed to the community. In the last year of the administration, the mayor is obliged to present a handing-over report including financial information from the four-year period (since the Law No. 20.742), which improved, among other things, transparency and probity in municipalities.

Current fiscal and accounting framework in Chile

Chile has a strict fiscal framework for municipalities including ceilings for certain types of expenditure. There are in particular regulatory constraints regarding staff expenditure whose goal is to keep a tight lid of the number municipal employees with permanent job contracts. Municipal personnel expenditure (*personal de planta*) is capped at 35% of the estimated own revenues (Law No. 18-204, article 1). Overall expenses on contractors cannot exceed 20% of expenditure related to the remuneration of municipal personnel (Law No. 1883 article 2). The payment of fees cannot exceed 10% of forecast expenditure for remuneration of municipal personnel (Law No. 19.280. art. 13). Other spending limits affect municipal subsidies. Subsidies to non-profit organisations cannot exceed 7% of municipalities' total budget. This grant limit does not apply to transfers allocated to education, health or youth protection.

The finance unit is responsible for accounting at the municipal level. It must follow national accounting regulations and guidelines issued by the Comptroller General's Office (*Contraloría General de la República* - CGR). Accounting information is reported monthly to the CGR to be integrated in the National General Accounting System (*Sistema de Contabilidad General de la Nación* - SICOGEN).

In 2012, the Comptroller General's Office launched the municipal scorecard report, which consists of a monthly compliance status regarding the obligation of municipalities to send their budget and accounting information to the CGR. This information is included in the CGR website. In the first publication, in April 2012, 23% of all reports that, at that time, had to be sent to the municipalities for the year 2012 were indeed sent and processed. In the fourth publication, in July, the percentage of all reports that, at that time, had to be sent by the municipalities for 2012 and that were indeed sent and processed had risen to 81.2% (OECD, 2014g).

Internal control and audit

According to article 29 of the Organic Constitutional Law, municipal internal control is carried out by the control unit. This office controls financial and budget execution, and informs the municipal council about illegal municipal acts. In addition, the control unit presents a budget execution report to the municipal council every three months. Internal control audits should perform internal audits. However, these are only operational audits and not financial audits of the municipal accounts.

Despite the critical role of the control unit, there are great disparities in the role and capacity of these units among the different municipalities. A report from the Comptroller General's Office carried out in 2010 concluded that 60% of municipal control units do not comply fully with the minimum requirements and do not have the needed technical capacity to perform their duties. In particular, the report highlighted the following deficiencies:

- 5% of municipalities do not have a control unit and the control function is not assigned to any unit in the municipal administration.
- 75% of municipalities do not have regulation chief auditor.

- In almost half of all municipalities the control unit is comprised of only one official.
- 65% of municipalities do not have internal operational audits.
- Overall, control unit staff have not been adequately trained in IT systems and in financial legal and budget control.

The municipal council is also responsible for overseeing budget execution. Since 2005, municipalities are obliged to inform the municipal council about accrued liabilities every three months. This information should be available to the public and published online. However, the role of the municipal council in holding municipal government accountable for public spending is still very limited. Since 1999, the municipal council has been able to contract an external auditor to revise the accounts every two years. However, this option is not often used by municipal assemblies (Valenzuela J.P., 2007).

External control

The Comptroller General's Office is the supreme audit institution in Chile. According to the Constitution (article 98) it is responsible for overseeing the legality of acts of the public administration, as well as revenue received and investment funded by the state treasury, municipalities and other statutory public entities; and examining and judging the accounts of individuals entrusted with resources of public entities under the supervision of the Comptroller (including municipalities).

Since 2010, the Comptroller General's Office has introduced changes to standardise ex post audit processes and guarantee standards of quality. These included sample methodology, standard tests per audit type and the incorporation of the Integrated System for Audit Control (*Sistema Integrado para el Control de Auditorías*, SICA) (OECD, 2014g).

The Comptroller General's Office has also created two new tools to improve capacity at the municipal level: a centre of studies of the state administration, and a support compliance programme to help municipalities to resolve issues that are pointed out during the audit process (SUBDERE, 2017b).

In 2014, the Comptroller General's Office audited around half of all municipal entities, including 70% of municipalities (Comptroller General's Office, 2015). Due to the amount of entities subject to audit, this process only includes a formal examination of reported accounts in order to ensure that they comply with the minimum standards and guidelines. In order to increase the reliability of the municipal accounts, this exercise could be complemented with in depth periodic financial audits commissioned by the municipal council.

Subnational fiscal rules in OECD countries

Fiscal discipline is the necessary corollary of fiscal decentralisation. Fiscal rules can help governments promote short-term economic stability, encourage aggregate efficiency, and help governments allocate public spending more efficiently. In particular, at the subnational level, there are useful tools to realise the potential efficiency gains from local autonomy, while meeting the objectives of sustainable longer term finances (Sutherland, Price and Joumard, 2005). However, the effectiveness of such rules depends on the ability of subnational governments to circumvent them, as well as on the monitoring requirements.

Fiscal rules for subnational governments have been in place in many OECD countries for a long time, and the recent global financial crisis has triggered several reforms tightening subnational fiscal rules (Vammalle and Hulbert, 2013). In particular, four types of rules have been used to support fiscal sustainability and short-term stability: balanced budget rules, subnational government debt and debt-service restrictions, tax and expenditure-growth ceilings and enforcement mechanisms of subnational government fiscal rules.

Balanced budget rules

Balanced budget requirements in OECD countries vary according to whether they are applied to the current budget and/or the capital account (the balanced budget requirement applies only to the current budget, thus allowing borrowing to finance net investments is usually referred to as the "golden rule" of public finance); whether they are set annually or multi-annually; and whether they are imposed from above or self-imposed. Most commonly, balanced budget requirements are applied to current and capital budgets, are set annually, and are set by entities further up the hierarchical chain (Vammalle and Charbit, 2010).

For some EU countries (e.g. Austria, Italy), budget balance rules have been modelled to a greater or lesser extent on the EU-wide economic governance rules, which curtail excessive deficits and require a "close to balance" fiscal position. It is notable that the oversight and co-ordination mechanisms across levels of government in some cases resemble those that apply under the EU Stability and Growth Pact (Box 2.16).

Box 2.16. **Recent reforms of subnational government balanced budget rules**

- In spring 2012, **Austria** adopted the new Internal Stability Pact, which came into force in December 2012. This pact sets new fiscal rules applying to all levels of government. Concerning deficits, all levels of government must reach a balanced budget in 2016. From 2017 onwards, a structural balance rule will be implemented, tying deficits to the output gap. The general government cycle will be used in order to calculate subnational government structural budget requirements (whose target will represent $2/9^{th}$ of the total cyclical effect, the other $7/9^{th}$ being allocated to the central government). In addition, the Austrian Fiscal Advisory Council (*Fiskalrat*) was created in 2013 as an independent fiscal institution to promote sustainable public finance and fiscal discipline, including at the subnational level.
- **Belgium:** The 2015-2018 Internal Stability Pact concerns for the first time all levels of government, including local authorities, which are formally integrated in accordance with the co-ordination mechanisms established by the Co-operation Agreement of 13 December 2013 to implement the Fiscal Compact. Individual targets in nominal and structural terms for central and local authorities are defined.
- **Denmark: T**he Budget Law, approved in 2012 introduced a balanced budget rule: structural deficits (on a yearly basis) should not exceed 0.5% of GDP.
- **Estonia:** The 2014 State Budget Act introduced a balanced budget rule for the general government, with a breakdown by level of government.
- **Finland:** Amendment of the Municipal Act in 2015 reinforced the macro-steering of the local finance system. An objective was set for local governments' deficits, and a spending limit was introduced on central government measures affecting local finances. Local budgets in Finland have to be balanced over a four-year period.

Box 2.16. **Recent reforms of subnational government balanced budget rules** *(continued)*

- **Greece:** The 2011 Kallikratis reform granted the Court of Audit additional powers in the monitoring of local governments. An Observatory for Financial Autonomy of the Local Government Organizations was launched by Law No. 4111/2013 and further implemented by Law No. 4270/2014. Tasks of this Committee are to ensure the preparation of realistic and balanced budgets by local authorities, in accordance with the applicable budgetary law as well as with monthly monitor budget execution by local authorities.
- **Germany:** In 2009, Germany introduced a "debt brake" in its constitution to ensure that subnational budgets are financed without any structural deficits from 2020 onwards, with only a small structural deficit allowed for the federal budget (0.35% of GDP). In addition, a new instrument, the Stability Council, was instituted to survey all public budgets on an annual basis using common benchmarks, to monitor public borrowing and to co-ordinate medium-term financial planning in a multi-level government context.
- **Iceland:** The Parliament passed a new act on local governments in September 2011, which includes two main fiscal rules on local government finance: a balancing rule for current operations, obliging them to balance revenues and expenditures over a three-year period and a debt rule that limits the total debt and liabilities to 150% of total revenue.
- **Italy:** The Domestic Stability Pact introduced a budget balance rule for municipalities and provinces. The Stability Law for 2014-2016 eased these budget constraints for local governments to exclude capital account payments of up to EUR 1 billion and another EUR 500 million to accelerate payment of past-due debts.
- **Japan:** The 2009 Act on Assurance of Sound Financial Status of Local Governments established new deficit and debt ratios to monitor the financial soundness of subnational governments. In addition, the 2010 Fiscal Management Strategy introduced numerical targets for the short, medium and long term to reduce the primary budget deficit of the central and local governments.
- **Mexico:** After the Fiscal Responsibility Law adopted in 2013, which established structural fiscal rules for the federal government, an equivalent law has been adopted for subnational government: the 2016 Federal Financial Discipline Law for States and Municipalities (*Ley de Disciplina Financiera de las Entidades Federativas y los Municipios*), which addresses the subnational deficit, debt limits and expenditure control and aims at reinforcing accountability and transparency.
- **Netherlands:** An agreement anticipating the entry into force of the Law on the Sustainability of Public Finances was reached in January 2013 with local authorities; a multi-annual budget balance path will be introduced for local governments. In 2013, a deficit limit of 0.5% of GDP was applied to local authorities as a whole.
- **Poland:** The Public Finance Act (2011) already stipulated that local current budgets must be balanced. In 2014, new rules came into force for local authorities: the debt servicing-to-revenues ratio had to remain smaller than the average ratio of current revenues (plus asset sales and operating expenditure)-to-total revenue over the last three years.

Box 2.16. **Recent reforms of subnational government balanced budget rules** *(continued)*

- **Portugal:** The 2013 Regional Finance Law and Regional Finance Law introduced new budgeting rules for subnational governments, including regarding arrears, off-balance sheet liabilities, expenditure ceilings and debt ceilings. Fiscal co-ordination mechanisms between central and subnational governments have been improved with the creation of the Public Finance Council whose mandate covers all levels of government.
- **Slovak Republic:** The Fiscal Responsibility Constitutional Act of 2011 and the Law on Budgetary Responsibility of March 2013 strengthened the fiscal rules applying to subnational governments, which came into effect in 2015. It also reinforced the role of the National Accounting Office (NAO) which controls local and regional accounting, budgeting and public expenditures.
- **Spain:** An amendment to the constitution was adopted in 2011 to underpin the fiscal consolidation targets for all Spanish administrations, following the EU framework. The main feature of the reform was that neither the central government nor the autonomous communities were allowed to have deficits exceeding the maximum set by the EU, and local governments were required to balance their budgets. The maximum structural deficit should be set according to law as a percentage of GDP. This limit will only be in force from 2020 onward. The Organic Law on Budgetary Stability and Financial Sustainability (2012) introduced a structural balanced budget rule for all levels of government from 2020 onwards. Debt reduction pathways will be revised in 2015 and 2018 to ensure that this objective is met. An independent authority for fiscal responsibility to monitor and report on compliance of all levels of government has been in effect since July 2014.

Sources: OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*; Vammalle, C., R. Ahrend and C. Hulbert (2014), *A sub-national perspective on financing investment for growth II - Creating fiscal space for public investment: The role of institutions*; OECD (2014d), *OECD Economic Surveys: Czech Republic 2014*; OECD (2014e), *OECD Economic Surveys: Denmark 2013*; OECD (2013b), OECD Economic Surveys: Japan 2013, Stability Programme 2014 (Belgium, Estonia, Italy, Netherlands); Convergence Programme Poland (2014); National Reform Programme Slovenia (2014).

Subnational government debt and debt-service restrictions

Borrowing constraints are widely used in OECD countries, but with a substantial variation in terms of restrictiveness. They range from strict limitations (Denmark and Korea) to no restriction at all. In most cases, subnational government borrowing requires prior approval by higher levels of government, and is often restricted to certain purposes such as investment.

Borrowing constraints can also come in different forms, such as numerical limits on the debt level, limits on new debt acquisition, or limits of debt service costs of subnational governments. The most common restrictions are the "Golden Rule", which allows subnational governments to borrow to finance capital expenditure only. This golden rule generally does not apply to federated states governments but it is almost universal in the OECD (and widespread worldwide) for the local government level. The golden rule is an efficient tool to contain the indebtedness of municipalities.

Other common prudential rules in OECD countries include limits on the total level of debt and on the issuance of new debt (OECD/KIPF, 2016). In most cases, limits are

expressed as a share of total or current subnational government revenues. They are sometimes set as a share of GDP, and in some rare cases, as a ceiling on total debt (Box 2.17).

Box 2.17. **Debt and debt service restrictions on subnational governments in selected OECD and Latin America countries**

- In **Austria**, The Internal Stability Pact that came into force in December 2012 introduced a debt brake for all levels of government in 2012. All levels of government must reduce their level of debt by 1/20 per year.
- **Brazil:** After several defaults by subnational governments in the 1990s, the federal government enacted in 1997 a deal for the restructuring of state government debt. It was followed in 2000 by the adoption of the Fiscal Responsibility Law (*Lei de Responsabilidade Fiscal e Finanças Publicas Municipais*) to prevent states and municipalities from running excessive budget deficits. It also introduced borrowing restrictions and spending constraints (including limits on staff expenditure). The law also imposed public reporting on key fiscal indicators for subnational governments. Significant changes to the law were introduced in 2008, which loosened borrowing constraints, putting the fiscal framework credibility to the test.
- **Colombia:** Fiscal responsibility rules were implemented in 1997 (Law No. 358 introducing a "traffic light" system based on liquidity and solvency indicators), in 1999 (Law No. 550 dealing with subnational government insolvency) in 2000 (Law No. 617) and in 2003 (Fiscal Transparency and Responsibility Law No. 819 introducing current expenditure caps) to introduce some restrictions to excessive subnational spending, deficit and indebtedness.
- **Czech Republic**: The new Constitutional Act (approved on October 2012) implemented new principles for budgetary discipline and accountability. In particular, at the local government level gross debt shall not exceed 60% of a four-year average of revenues. The debt service ratio of subnational governments should not exceed 30% of subnational government revenues.
- **Estonia**: Limits for local debt were introduced from 2009 to 2012. According to the Financial Management of Local Authorities Act, total subnational government debt must not exceed 60% of total subnational revenues from 2012 onwards.
- **Greece**: The 2011 Kallikratis law introduced additional fiscal rules limiting debt: interest payments for a given year cannot exceed 20% of ordinary annual revenues and total debt must remain under 60% of total annual revenues. A debt-brake was introduced for the few municipalities facing problems of over-indebtedness. The Kallikratis law provided that these municipalities would join a "Special Economic Recovery Programme".
- **Iceland**: The 2011 Local Government Act introduces a debt rule that limits the total debt and liabilities of local governments to 150% of total revenue. Local governments with debt and liabilities above 150% are required to bring the debt ratio under this limit within ten years. Local governments with total debt exceeding 250% of revenue are prohibited from raising new debt (except for refinancing).
- **Italy:** There is a debt service cap for municipalities. Interest payments must not exceed 12% of current revenues.

Box 2.17. **Debt and debt service restrictions on subnational governments in selected OECD and Latin America countries** *(continued)*

- **Peru:** Fiscal discipline is key part of the Peruvian decentralisation process. The revised Fiscal Responsibility and Transparency Law (Law No. 30099) enacted in 2013 reformed the previous Fiscal Responsibility and Transparency Law No. 27245 and the associated Decree No. 955 which were too complex (eight fiscal rules). In fact, most subnational governments did not comply with them. The new law streamlines the rules into two rules and aligns them with those for the national macro-fiscal framework: 1) the level of debt can be no higher than 100% of the average total current revenues of the last four years; and 2) the annual growth of non-financial expenditure can be no higher than the moving average growth of annual revenue over the past four years. Subnational governments can only borrow under the state guarantee and only for capital investment projects ("golden rule"). The new debt rule tackles the problem of other liabilities, by including them in its definition of total debt.
- **Poland:** The 2011 Public Finance Act stipulated that local current budgets must be balanced and it also strengthened debt limitations, requiring that the sum of loan instalments and interest payments must not exceed 15% of total debt. From 2014 onwards, the mode of calculation for debt ratios has been changed in order to reduce subnational government debt: the debt limit – outstanding and debt service – is no longer based on revenue but rather on gross savings calculated over a three-year period. Moreover, subnational government debt must not exceed 60% of GDP.
- **Portugal:** The two 2013 regional and local finance laws introduced new fiscal rules. At the regional level, the law stipulates that the two autonomous regions' liabilities should not exceed 1.5 times their three-year average net current revenue. At the municipal level, the law on Local Finances introduces similar requirements for each municipality individually (municipalities' liabilities should not exceed 1.5 times their three-year average net current revenue).
- **Slovak Republic:** According to the Fiscal Responsibility Constitutional Act of 2011 and the Law on Budgetary Responsibility of March 2013, total subnational government debt must not exceed 60% of total subnational current revenues. In addition, loan instalments and interest should not exceed 25% of the previous year's current revenues. Currently, subnational governments exceeding these debt limits must pay a fine to the Ministry of Finance amounting to 5% of the difference between the total debt and the 60% ratio.
- **Spain**: The Organic Law on Budgetary Stability and Financial Sustainability introduced overall debt ceilings for all levels of government. Debt should not exceed 13% and 3% of GDP for autonomous communities and local governments, respectively. Moreover, subnational governments should no longer be able to borrow in order to finance current expenditures after 2020.

Source: OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*; OECD (2011) Network on Fiscal Relations across Levels of Government Survey on Subnational Fiscal Rules and Macroeconomic Management, September 2011.

Tax and expenditure-growth ceilings

Overall limits on tax rates or reliefs are widely used in OECD countries, and usually take the form of an explicit limit on tax autonomy set by the central government. In contrast, only a relatively small number of OECD countries rely on expenditure limits for

subnational governments. Expenditure ceilings aim to restrain subnational governments' spending growth over the medium to long run, thereby indirectly limiting subnational deficits. Ceilings can be set annually (Denmark, Italy: state and local) or for a multi-year period (Austria: state and local, through calculations based on the EU mechanism). They may be set proportionally to income (Canadian provinces, Turkey) or linked to an objective needs criterion, such as population growth (Slovenia, Spanish local governments). In most countries, expenditure ceilings are set for current (operating) expenditure only (Denmark, Estonia, Italian local governments and Korea) (Box 2.18).

Box 2.18. **New expenditure ceilings for subnational governments in selected OECD countries**

- **Austria**: The new Internal Stability Pact signed in May 2012 introduced a limit on expenditure growth of subnational governments: aggregate expenditure growth of all levels of government should not be above the average potential GDP growth.
- **Denmark**: With the 2012 Budget Law, a new system of expenditure control was agreed. From 2014, four-year binding expenditure ceilings for all levels of government came into force. They cover most public spending with the exception of investments and unemployment outlays. Municipalities and regions have agreed to limit their expenditures; a breach in the ceiling for a given year will have to be compensated in the following year. Moreover, federal transfers may be reduced in case of non-compliance.
- In **Finland**, the Basic Public Services Programme approved in mid-2012 introduced a target for municipal expenditure (average municipal spending growth must be lower than 0.4% by 2020, assuming that local responsibilities remain constant). Moreover, from 2015 local responsibilities will have to match available funding; new responsibilities will have to be financed either through increased revenues or cuts in other expenditure.
- In **France,** after several years of discussions, subnational governments are now involved in the definition of an objective target to control annual public spending in the context of the new governance rules. The public finances planning law 2014-2019 (PSSA) included subnational governments in annual public spending objectives. In particular, it introduced an annual spending growth standard for local governments (ODEDEL, expressed in annual percentages) and improved budgetary decision-making.
- In the **Slovak Republic**, since 2014, individual municipal expenditures - for one given year - cannot be greater than expenditures for the previous year.
- **Slovenia**: The Fiscal Balance Act introduced several measures to reduce the general government's debt and deficit, which came into force in mid-2012. In particular, limits were set in order to limit labour-related costs for public employees (including at the local level).
- **Spain**: The Organic Law on Budgetary Stability and Financial Sustainability (2012) set new expenditure ceilings for subnational governments. Variations in expenditure must not exceed medium-term GDP growth (calculated over three years according to EU methodology).

Sources: OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*; OECD (2017) *Multi-level Governance Reforms: Overview of OECD Country Experiences*; Vammalle, C., R. Ahrend and C. Hulbert (2014), *A sub-national perspective on financing investment for growth II - Creating fiscal space for public investment: The role of institutions*; OECD (2013a), *Economic Surveys: Austria 2013*; OECD (2014e), *OECD Economic Surveys: Denmark 2013*; National Reform Programme Slovenia (2014); National Reform Programme 2014 (Finland).

Enforcing subnational government fiscal rules

Rules and controls are only effective if they are actually enforced, and subnational governments that break the rules are, in general, subject to a range of consequences. In the context of the recent fiscal consolidation plans, several countries have tightened their sanction mechanisms in case subnational governments exceed their fiscal targets (e.g. Spain, Italy). Sanctions and procedures for subnational governments breaking fiscal rules must not be confused with the procedures in place for subnational governments facing financial difficulties, even if they are sometimes similar.

In addition to establishing new or strengthening existing fiscal rules, some countries have also tightened their enforcement. This has been achieved either by increasing the transparency and reporting requirements, imposing financial sanctions or restructuring plans on subnational governments breaking the rules. Some countries have even established new sanctions for political officials responsible for breaking the rules (Box 2.19).

Box 2.19. **Procedures in case subnational governments fail to meet fiscal rules in selected OECD countries**

Procedures in cases where subnational governments fail to meet fiscal rules range from actions taken by the central government or subnational governments themselves. In many OECD countries, central governments may take action without making any changes to legislation:

The most common procedure consists of the central government imposing financial sanctions on subnational governments breaking the rules (either automatic or discretionary) and obliging subnational governments to offset the breach in future budget, or to take measures so that the rule is complied with in the future. These can take the form of a fixed fine, or cuts in transfers or shared taxes from the central government. In the Slovak Republic, the Ministry of Finance may impose a fine up to EUR 16 597 to subnational governments breaking fiscal rules. The new Austrian fiscal rules introduce possible deduction in shared taxes, proportional to the infraction. In the Czech Republic, if the debt target is not respected, the central authorities may cut transfers to a municipality or region by 5% of the difference between its amount of debt and the 60% target.

Administrative sanctions reducing the freedom of subnational governments are used in a few OECD countries. Such sanctions often take the form of greater control of central authorities over subnational finances, through the appointment of a public officer in charge of monitoring to some degree subnational government revenues, spending and borrowing.

Finally, in some countries, sanctions on subnational government officials are also possible. These range from their removal (in Poland, local governments' councils or executive bodies may be dissolved) to possible penal sanctions.

In Italy, there is a wide range of sanctions introduced by the 2011 Internal Stability Pact. Regions breaching fiscal rules may face a number of spending restrictions, such as hiring new personnel or borrowing. They may even experience a reduction or suspension of grants from the central government. Reporting rules have also been tightened, in particular for periods before elections. The audited financial statements of the regions must be published on their websites. If the results are not consistent with the Italian Internal Stability Pact, sanctions may be imposed on political officers, such as automatic disqualification from office for up to ten years.

Box 2.19. **Procedures in case subnational governments fail to meet fiscal rules in selected OECD countries** *(continued)*

In Spain, the Organic Law on Budgetary Stability and Financial Sustainability also introduced several types of sanctions for governments deviating from fiscal rules: they must submit a restructuring plan with fiscal recovery measures and prior permission to borrow and, in the case of repeated infractions, a temporary (partial or total) re-centralisation of budgetary powers can be imposed.

Source: OECD/KIPF (2016), *Fiscal Federalism 2016: Making Decentralisation Work*, http://dx.doi.org/10.1787/9789264254053-en.

Improving municipal fiscal discipline and accountability in Chile

Fiscal sustainability is the ability of a government to maintain public finances at a credible and serviceable position over the long term (OECD, 2013d). According to the OECD Principles for Budgetary Governance, budgets should be managed within clear, credible and predictable limits for fiscal policy. In order to do so, government should, at the very least, have a stated commitment to pursue a sound and sustainable fiscal policy; that means avoiding the build-up of large, unsustainable debts, and using favourable economic times to build up resilience and buffers against more difficult times. Overall budget targets for each year should ensure that all elements of revenue, expenditure and broader economic policy are consistent and are managed in line with the available resources (OECD, 2014f).

Fiscal discipline is a key component of fiscal decentralisation reform. Fiscal decentralisation reforms need to provide for the definition and implementation of sound budgetary, accounting and reporting frameworks, based on common standards for all levels of government, in order to facilitate the monitoring, control and transparency of financial operations. Strengthened fiscal decentralisation also requires rethinking the role of the state in the exercise of budgetary and financial controls on subnational governments. Finally, fiscal decentralisation needs to set up, or reinforce, co-ordination mechanisms in fiscal matters across levels of government.

Despite having a very strict fiscal framework, Chilean municipalities have developed short- and long-term borrowing practices that lack transparency, particularly with regard to their budget documents. Chile could benefit from having a more comprehensive fiscal framework. In particular, the following recommendations could be implemented towards having more modern and robust budget practices at the municipal level.

Present a consolidated account at the municipal level, including all sectors and corporations

As already stressed, the existence of one budgetary account for "municipal activities" with two or three appendixed sectoral accounts (education, health and cemeteries) and of municipal corporations in several areas (education, health services, culture, sport and leisure activities) is unsatisfactory in terms of financial and democratic transparency and for budgetary data comparability. There is no consolidated approach at the municipal level. Actual financial commitments remain fuzzy.

One recommendation would be to complement the sectoral budgetary submissions with a consolidated accounts of the "group Municipality of X" (sectors *municipalidades*,

education, health, cemeteries and with the integration of the corporations). The development of municipal associations will also require the development of budget reporting and control in relation to member municipalities.

Municipal budgeting

Ensure that decentralised responsibilities are financed with sufficient resources to avoid structural deficits

The first fundamental recommendation for fiscal health would be for the Chilean government to ensure that decentralised responsibilities are financed with sufficient resources to avoid structural deficits. In fact, structural mismatch between subnational spending obligations and the allocation of revenues is a common source of subnational government deficits and debts (OECD/KIPF, 2016) and any fiscal rule would remain ineffective if there is a structural problem of unfunded mandates (European Commission, 2012). The current high levels of floating and temporary pension debt in Chile are a red flag on this matter and need to be taken into account in order to ensure fiscal sustainability in the long term. In the Chilean case, this is particularly relevant in the health and education sector. Municipalities constantly raise their concerns on the impact of these services on municipal finances, resulting in structural deficits. Additional tasks are also regularly transferred to municipalities but not always accompanied by sufficient, permanent and stable compensation, leaving municipalities with the difficult choice about whether and how to continue services formerly financed by the national grants (Posner, 2010).

Some OECD countries have introduced reforms to mitigate or even reverse the use of unfunded or under-funded mandates and regulations in systems. In Denmark, two long-established basic principles guide decisions about how much the central government should contribute to the local government system when devolving new tasks to subnational authorities or when additional costs arise from a change in national legislation. These principles, adopted by agreements between the Danish central and local governments, intended to safeguard an equitable relationship between them and establish effective budget co-ordination. The first one, called Expanded Total Balance Principle *(Det Udvidede Totalbalanceprincip* - DUT principle*)*, requires the central government to compensate local authorities with extra grants whenever new national legislation has an impact on local expenditure. Conversely, resources must be refunded where new national legislation has the opposite effect. The second principle, called Budget Guarantee Scheme, compensates local authorities for additional expenditure resulting from external factors which are outside local government control. Some areas are particularly sensitive to changes in market or social conditions such as social security benefits, cash assistance for the unemployed, early retirement pensions, integration of refugees or immigrants, etc. (CoR, 2001). In the United States, three types of actions have been taken to mitigate the use of unfunded mandates and regulations in systems (Box 2.20).

Box 2.20. **Reforms to curb the use of unfunded mandates in the United States**

According to Posner (2010) there have been three types of actions proposed in the United States to mitigate the use of unfunded mandates and regulations in systems:

1. Legislative information requirements and other procedural requirements promoting greater deliberation on projected costs of proposed legislation.

According to the Unfunded Mandates Reform Act (1995), the Congressional Budget Office is required to estimate the costs of all major legislation reported by committees affecting both state and local governments and the private sector. In addition, to ensure compliance, the Unfunded Mandates Reform Act enabled any member of Congress to prevent the full legislative body from moving to vote on a bill if the required cost estimate was not produced. A separate "pre-emption note" has also been proposed to provide Congress with more information on the federalism impacts of proposals involving intergovernmental pre-emptions.

2. Agency requirements for cost-benefit analyses.

Federal agencies are required to review the costs and benefits of major proposed rules before they are issued. Several other tools have been added to ensure greater compliance and visibility for these requirements. For example, the President's budget office should review and approve all proposed regulations before they are issued, including a review of cost-benefit analyses. In addition, the public is given significant opportunity to review and comment on proposed regulations, including their costs and their benefits.

3. Mandate reimbursement approaches.

Under a national reimbursement provision, the national government is obligated to pay for all costs that are imposed on subnational governments due to national legislation or regulations. This approach was rejected at the national level in the United States but has been tested by several states in recent decades. The experience of the states shows that this approach raises a number of implementation issues, such as the possibility that legislatures and executives can skirt the requirement and the lack of definitive information on the costs of implementing programmes that is available when legislation is considered.

Source: Posner P.L. (2010), *Mandates: Fiscal Accountability Issues.*

Make a more precise and transparent estimation of the revenues expected to be collected during the year

Revenues should be estimated as precisely as possible from the outset of the annual process. This will ensure that budgets are not only balanced in the budget law approved by the municipal council but also in the budget executed during the year. The Comptroller General's Office could play a major role in improving the quality of these estimates by undertaking a consolidated national assessment and providing guidelines on how to improve these estimations.

Enhance the current budget balance rule

According to the Constitutional Organic Law for municipalities, the municipal council should not approve unbalanced budgets. However, the rule does not explicitly refer to the need to have a balanced budget at the end of the budget year (on an accrual basis) and it does not include specific cases where deficits are allowed and the procedure that should be applied to restore this balance. Therefore, existing budget balance requirements could be enhanced by requiring that revenues and expenditures are not only

balanced in the budget law approved by the municipal council but also in the budget executed during the year.

In addition, clear-cut escape clauses could be included to allow municipalities to temporarily deviate from the budget balance rules or expenditure/debt limitations in the case of exceptional circumstances such as economic downturns or natural disasters. This would provide subnational fiscal discipline with a greater degree of flexibility. Chile could also consider implementing mechanisms to compensate deviations in following years (Box 2.21).

Implementing an alert system to monitor unpaid balances and detect municipalities that are at high risk of non-compliance would be useful. This would make it possible to take action during the budget year, increase monitoring, and reduce the risk of a deficit forming. Chile could establish thresholds based on liquidity and solvency ratios, where increased monitoring would play an active role.

Box 2.21. **Escape clauses and follow-up mechanisms**

Escape clauses in the 2016 Federal Financial Discipline Law for States and Municipalities in Mexico

The objective of the new law of financial discipline of states and municipalities (*Ley de Disciplina Financiera de las Entidades Federativas y los Municipios*) is to promote sustainable public finances, a responsible use of public debt, and to reinforce the accountability and transparency of subnational governments. The law responds to a national trend of accelerated growth of debt in states and municipalities. It was enacted in April 2016.

According to this new legal framework, deficits are only allowed in three particular cases: reduction of tax share transfers due to GDP falls in real terms, natural disasters, and to implement measures that will have a significant positive impact in long-term fiscal balance (for example, paying compensation to reduce payroll). Strict process rules apply in order to trigger this clause (i.e. plan from the executive to finance and eliminate the deficit, and congressional approval and reporting requirements).

Control and correction tools under Germany's Debt Brake

In 2009, on the basis of groundwork laid by the Federal Ministry of Finance and a proposal by the Federal Commission (*Föderalismuskommission*), the German parliament approved the proposal to replace the golden rule with a debt brake. The stated objectives were to improve the sustainability of national finances, with strengthened fiscal co-ordination among federal and Länder levels, while providing flexibility to deal with cyclical and demographic challenges.

One of the core elements of the new system in place was the introduction of control and correction tools. Deviations, either positive or negative, from the permissible borrowing amount that arise during budget implementation are not simply forgotten: they are booked in a standing "control account" which must be balanced over time. (Deviations arising from unanticipated cyclical changes are not booked in such a way: it is assumed instead that these issues will be covered through re-calculated automatic stabilisers.) Redemption of the control account is required once it reaches 1% of GDP; however, to limit procyclical effects, redemption may be deferred during a downturn, and is - in any event - capped at 0.35% of GDP even during an upturn.

Source: Financial Discipline Law for States and Municipalities in Mexico (2016); OECD (2015b), *Budget Review: Germany*.

Improve transparency of current municipal borrowing

Hidden borrowing practices, such as arrears and leaseback contracts, hamper transparency of municipal financial management, hinder debt monitoring, and undermine governance mechanisms. Chile could benefit from recognising current borrowing practices, and clarifying the rules and limits for this practice. This approach is a prerequisite for the implementation of the recommendation regarding access of municipalities (at least in a selective manner i.e. for creditworthy municipalities) to medium- and long-term credit to finance their infrastructure development programme (see Chapter 2). This would increase transparency and accountability regarding the municipal council, the national government and citizens in general.

There have been improvements in the reporting and monitoring of municipal arrears in Chile; however, there is still room for improvement, both at the consolidated (national, regional) and individual levels. In particular, it could be recommended to publish - in the appendices of the municipal budget/accounts - all loan contracts, including the conditions of the use of borrowing and the terms of the loans obtained, to ensure transparency. Debt information could be published in the SINIM database (Box 2.22) and regularly reported in a clear and understandable manner.

Box 2.22. **SINIM budget databases**

The National System of Municipal Indicators (SINIM) provides over 150 standardised indicators for each of Chile's municipalities, including a wide range of fiscal indicators. The system offers a wealth of insightful information covering the fiscal activity of each and every municipality in Chile. In addition to detailed data on the indicators used in the attribution algorithm of the Common Municipal Fund (FCM), the tab "*Información SINIM*" provides access to different data under different formats, including the budgetary operations of the municipalities.

"*Datos municipal*", available in Excel format, provides budget data for different areas and sub-areas (municipal, education, healthcare, municipal personnel, etc.), and according to various criteria (for 2010 to 2015, by region and by municipality). It provides a wealth of indicators regarding the budget (revenue and expenditure), social data (education, schooling, healthcare and psychical and socio-demographic characteristics). Data, in current value terms, can be automatically transformed into actual values by applying a discounted monetary coefficient that is built into the database. "*Clasificador Presupuestario*" includes the most granular details possible regarding the overall budgetary operations in local authorities' areas of competence (municipal, healthcare, education, cemeteries). Each of these two entries is accompanied by a dictionary that describes in great detail, and using an accounting nomenclature, the expenditure revenue items that constitute these indicators.

"*Ficha Comunal*", provides a summary of these indicators by municipality and includes the partisan composition of local authorities, the organisation of the municipal structure, its location, etc.

"*Evolución Presupuestaria*", available only as a PDF, offers a complete presentation of the accounting nature of expenditure and revenue based on different scales (entire country, region or municipality) for each year from 2010 to 2015.

Source: SUBDERE (2017a) Sistema Nacional de Información Municipal (SINIM).

Allow capable municipalities to issue debt and establish a clear set of debt rules for "responsible borrowing"

Allowing municipal borrowing is a major component of fiscal decentralisation. It would provide more financial autonomy to municipalities, which is fully in line with the goal of modernising the municipal system in Chile. Beyond this political argument, it appears that current restrictions on municipal borrowing are fundamentally questionable from an economic point of view (see Chapter 2). In addition, allowing municipalities to acquire public debt can increase their financial capacity to invest in municipal infrastructure, which is an important prerequisite for creating an environment conducive to inclusive economic growth. However, more flexible debt management should go hand in hand with a good set of fiscal rules that contribute to ensure economic stability and sound fiscal management.

In this perspective, fiscal discipline is the necessary counterpart of fiscal decentralisation. All countries in the OECD have established a body of rules in order to secure the borrowing mechanisms available to their local authorities. Such debt rules should in turn allow sufficient autonomy to municipalities for delivering public services and financing public investment. They also should allow some flexibility enabling municipalities to cope with unforeseen events. New process rules should be clearly stated in the legislation, for example, requiring a qualified majority from the national assembly and/or approval from the national government.

In particular, the following recommendations could be taken into account when designing a "responsible borrowing" framework:

- Apply the golden rule to municipal borrowing in Chile. Restricting borrowing exclusively to investment projects is a common practice among OECD countries. This restriction should be complemented with a clear definition of investment projects in the legal framework and good planning and selection mechanisms to ensure positive impact on growth and development. This could help prevent "gaming behaviour", such as reclassification of expenditure. Redemptions on debt by subscribing to a new loan (revolving credit) should also be forbidden.
- Establish additional prudential rules to avoid over-indebtedness. In particular, the debt burden could be limited to a percentage of current revenue (actual or estimated).
- Short-term borrowing limits and special procedural requirements are also advisable. For example, requiring special approval above a certain threshold and/or requiring the cancellation of short-term debt at the end of a government period.
- Publish - in the appendices of the municipal budget/accounts - all loan contracts, including the conditions of the use of borrowing and the terms of the loans obtained, to ensure transparency (see above).
- Impose the mandatory coverage of all expenses related to servicing the debt by giving the expenses the status of "mandatory expenses", i.e. a legal obligation spelled out in the municipal budget. This recommendation aims to enhance the accountability of the local borrower and prevent risk transfer to the state budget and thus the national taxpayer. It entails consequences that follow the suggestions related to the reinforcement of municipalities' decision-making capacity. If they are not able to modify local tax rates, the suggestion is inapplicable. Imposing the

payment of an expense without being able to adapt the level of revenue is not viable, except if downward pressure can be put on other current expenditure.

Access to credit for municipalities (public or private depending on how the lenders would be used) would also require training into how such finance mechanisms function. A useful prerequisite to this access could come in the form of signing on to a code of conduct involving both the municipalities and banks. It would ensure that the path to modernising the municipal finance system, which is essential if public capital stock is to densify at the local level, is a safe and well-marked one.

Adopt a gradual and differentiated approach for municipal borrowing

In countries with great disparities across municipalities, such as Chile, implementing an asymmetric approach, which would allow municipalities to borrow (i.e. restricting the borrowing power to municipalities with high technical and financial capacities) can be an appropriate solution, at least as a first step, so long as other municipalities have not reinforced their capacities. A gradual process could be also tested consisting in implementing a system of prior approval.

Access to borrowing and debt limits could be adjusted depending on the characteristics of municipalities, including demographic size or financial capacity. Several countries, such as Colombia and South Africa, use such classifications for different purposes: assigning different responsibilities; allocating certain types of revenues (i.e. taxes, user fees); establishing differentiated expenditure ceilings; and providing access to certain types of borrowing (loans or bonds, for example) or for financial management and monitoring.

Municipal classification seems to be an interesting approach to recognise and take into account the diversity of municipalities, especially in countries as diverse as Chile. The FIGEM classification developed in Chile is a good tool but it would need to be completed and updated before being rolled out as a broader policy instrument, in particular for financial management purpose.

However, such approaches may have some shortcomings and may involve risks. As illustrated by the South African experience of municipal classification, the motive for differentiation is not always clear, and some classifications are not always useful for making decisions or allocating resources. Categorisation often depends on the policy purpose and often detracts from looking at the linkages between rural and urban municipalities, for example. Categorisation may also raise the issues of thresholds and of regular updates to take into account municipal changes. Municipal classification could be used more extensively and is certainly an interesting avenue for Chile to explore. But such an approach should define clear objective criteria and principles for differentiating municipalities (Box 2.23).

Box 2.23. **Examples of municipal classifications for financial management purposes: Colombia and South Africa**

In Colombia for example, Law No. 617/2000, modified by Law No. 1551 of 2012 established a classification of departments and municipalities to determine appropriate ceilings for current expenditure and for financial management and monitoring purposes. The different categories of municipalities are based on demographic size and the capacity of the subnational government to generate current own revenues, i.e. revenues generated by their real tax collection capacity. In particular, the law defined seven categories of municipalities. The smaller subnational governments and those with a more modest capacity to generate current income (due to a fragile tax base or a poor demographic profile) have a higher ceiling for current expenditures and conversely, the bigger and more financially autonomous subnational governments have a stricter ceiling, e.g. from 50% (special category) to 80% (categories 4, 5 and 6) for the municipalities and from 50% (special category) to 70% (categories 3 and 4) for the departments (Law No. 617/2000). At present, the Colombian government is working on a new classification of municipalities, which would also simplify the reporting mechanisms and grant exemptions to government requirements in order to alleviate the administrative burden.

In South Africa, the 278 municipalities have different underlying characteristics and face different socio-economic and political challenges. They also have different capacities for dealing with these challenges. This requires a differentiated approach, in particular to municipal funding. In this regard, different departments use many classifications to group municipalities. The 1996 Constitution provides for three categories: A (metropolitan municipalities), B (local municipalities) and C (district municipalities). Other classifications exist in other areas, such as the Municipal Infrastructure Investment Framework Investment that defines seven categories based on, among others, spatial characteristics, size of institution and budget, and population variables. The National Treasury also classifies municipalities into six "performance groups" using economic, demographic and performance variables such as access to basic services, poverty rate, municipal viability, staff vacancy, municipal debt, population density and size of the municipality's economy. As underlined by the Financial and Fiscal commission, the different classification methodologies highlighted above recognise that municipalities need differentiated approaches that take into considerations their different characteristics and needs. However, the Financial and Fiscal Commission also seems to consider that differentiation approach is not always clear, and some classifications are not always useful for making decisions or allocating resources as categorisation often depends on the policy purpose and often detracts from looking at the linkages between rural and urban municipalities, for example. In addition, the large volume of classification methodologies may undermine co-ordinated decision-making and intervention strategies.

Source: OECD (2016a), *Making the Most of Public Investment in Colombia: Working Effectively across Levels of Government*; South African Financial and Fiscal Commission (2012), *Report on the Local Government Fiscal Framework Public Hearings Sustaining Municipal Finance: Making Local Government Work*.

Monitor municipal debt to detect risk of insolvency

In the perspective of allowing municipal borrowing, transparency and reporting requirements are essential to monitor and control municipal debt levels. Implementing a central evaluation system for municipal public debt management is a best international practice. Creating a single public registry for public debt management could promote transparency, monitoring and evaluation mechanisms for debt, such as in Mexico, Portugal, Norway, Colombia or South Korea. Such tools would also make it possible to

detect the municipalities that are at risk so corrective measures can be implemented in a timely manner (Box 2.24).

Box 2.24. **Monitoring local government debt and municipalities in financial distress**

In Mexico, the Mexican Federal Financial Discipline Law for States and Municipalities (*Ley de Disciplina Financiera de las Entidades Federativas y los Municipios*) enacted in April 2016 aims to promote sustainable public finances, a responsible use of public debt, and to reinforce accountability and transparency. In order to facilitate transparency, monitoring and evaluation mechanisms for debt, the law created two mechanisms: 1) a single public registry (*registro público único*) dedicated to public debt management, containing the details of all financial obligations of every state and municipality; and 2) a warning system (*sistema de alertas*), through which the federal Ministry for Finance and Public Credit (SHCP) evaluates debt levels for each state and establishes borrowing limits depending on the classification received.

In Portugal, the 2013 Local Finance Law and Regional Finance Law set up an early-warning system for debt accumulation, different types of adjustment or restructuring plans for over-indebted municipalities, as well as a Municipal Resolution Fund (FAM) aimed at providing assistance to distressed municipalities.

In Norway, municipalities that do not meet balanced budget requirements must follow special approval processes by the county governor or the Ministry of Local Government and Modernisation in order to make lawful decisions about borrowing and long-term leases. These municipalities are listed in a specific registry (ROBEK, Register for Governmental Approval of Financial Obligations). In September 2014, 54 municipalities out of 428 were listed in this registry.

In Colombia, compliance with fiscal rules, including debt limits, is constantly monitored by the central government, which has implemented sound financial and administrative information systems allowing insolvency risks to be detected.

In South Korea, the government reformed its procedures in 2011 for dealing with serious financial difficulties at the subnational level and introduced an "advanced warning system" based on seven indicators (fiscal balance, debt service ratio, local public enterprise liabilities, etc.). In case of problems, a risk control committee deliberates. If a subnational government is identified as being in fiscal distress, an official announcement is made by the central government. The subnational government must then propose a budget deficit management plan, to be approved by the central government. During this process, local governments face constraints on issuing debt.

Source: OECD/UCLG (2016), *Subnational governments around the world: Structure and finance*; Financial Discipline Law for States and Municipalities in Mexico (2016); OECD/KIPF (2016), *Fiscal Federalism 2016: Making Decentralisation Work*.

Control and accountability

Regular audits and controls needed to ensure quality of financial data at the municipal level

Financial decisions must be based on reliable and accurate accounting information. Financial audits are necessary to assess the quality of financial reporting and the reliability of financial information. Audits can be carried out at the national level, or sub-central governments can directly be in charge of such controls. Even in such decentralised frameworks however, the central government still plays a major role: it should "set the

standards and monitor the effectiveness of the internal control systems at the local level" (Baltaci and Yilmaz, 2006). Most OECD countries have introduced some form of auditing of sub-central finances (OECD/KIPF, 2016) (Box 2.25).

Box 2.25. **Auditing local finances in Sweden and France**

For Swedish municipalities and county councils, an assembly is granted authority for decision-making, while elected representatives (grouped into committees) are responsible for administration and execution. Following the Local Government Auditing Inquiry (1998), the assembly elects auditors to monitor the financing and executing of policies. All the audits must be carried out independently, in accordance with standards published by the Swedish Association of Local Authorities and the Swedish Federation of County Councils.

In France, the Decentralisation Law of 1982 created the regional chambers of audit. These public bodies are responsible for an ex-post auditing of subnational governments accounts, and must also review the management of local governments and related entities. A report from the Cour des Comptes points out excessive spending and poor management in many French subnational governments, with particularly high personnel expenses, which are growing rapidly. Moreover, the court criticises the quality of financial data provided at the sub-central level.

Source: Baltaci, M. and S. Yilmaz (2006), *Keeping an eye on Subnational Governments: Internal control and audit at local levels*.

Since 2008, there have been efforts to implement information systems and reduce the technology gap at the municipal level. In particular, the Comptroller General's Office has played a major role in performing external audits of municipal accounts. However, due to the amount of entities subject to audit, this process only includes a formal examination of reported accounts. In addition, the internal control performed by municipal control units has shown to be faulty, reducing the reliability of the information reported by municipalities.

Chilean municipalities could benefit from improving the quality of their accounts by setting up an ongoing independent financial audit process.

Establish enforcement mechanisms and sanctions for non-compliance

Establishing enforcement mechanisms and sanctions for non-compliance are key elements to ensure that fiscal rules have a positive impact on economic stability and fiscal management. If subnational governments feel there are no consequences when infringing fiscal rules, they are like to be disregarded. In this framework, it would be necessary to have a clear definition of responsibilities regarding fiscal rules compliance and sanctions. Having an independent overseer to assess budget actions and to draw attention to actual or potential violations is helpful in ensuring compliance. Several countries have set up such independent councils.

Reinforce democratic oversight and accountability by strengthening the capacity of municipal assemblies on budgetary issues

Beyond municipal staff, the oversight role of municipal assemblies in the budget process is critical to promoting fiscal transparency and accountability. The current legal framework gives considerable responsibilities and powers to the assembly to request information and monitor financial performance; however, these tools are not often used due to weak capacity of municipal assemblies on budgetary issues.

Members of the municipal assemblies need to be equipped with the skills and capacities to understand how the budget process works, including the budgetary timetable, and the role and responsibilities of the municipal council. As a consequence, professional development for effective budget scrutiny could be incorporated into the initial training programme for new members at the start of the next municipal council session. In addition, Chile could consider introducing a permanent specialised team in charge of budgetary issues inside the municipal assemblies.

An additional key factor to improving municipal assemblies' capacity is to ensure that they have the proper support and can rely on the information and reports provided by the municipal control unit and the municipal finance unit. The Comptroller General's Office can play a major role in providing training and technical capacity to these units in order to ensure they can fully perform their duties.

Box 2.26. **Key recommendations for a more comprehensive fiscal framework and increased fiscal responsibility**

1. **Present a consolidated account at the municipal level**, including all sectors and corporations, and information on municipal associations as they develop.
2. **Ensure that decentralised responsibilities are financed with sufficient resources to avoid structural deficits**. Introduce measures to mitigate or even reverse the use of unfunded or under-funded mandates and regulations in systems (compensation principle).
3. **Make a more precise and transparent estimation of the revenues expected to be collected during the year.** Reinforce the role of the Comptroller General's Office in this process (consolidated national assessment, guidelines).
4. **Enhance current budget balance rules** by requiring that revenues and expenditures be not only balanced in the budget law approved by the municipal council but also in the budget executed during the year and including precise escape clauses to compensate deviations in following years.
5. **Improve municipal borrowing rules by,:**
   - Improving the transparency of current municipal borrowing through clearer rules, reporting and monitoring at consolidated and individual levels through SINIM.
   - Implementing an alert system to monitor unpaid balances and detect municipalities that are at high risk of non-compliance.
   - Allowing municipalities to issue debt and establish a clear set of debt rules for "responsible borrowing" including, at the very least, the "golden rule". Other additional prudential rules to avoid over-indebtedness can be explored (caps on debt stock and debt service, short-term borrowing limits, special procedural requirements, reporting requirements, etc.). New process rules should be clearly stated as part of a law.
   - Adopting a gradual and differentiated approach to municipal borrowing. The FIGEM typology could be reviewed to be used in this perspective. Other rating instruments could be developed.
   - Monitoring municipal debt level to detect risk of insolvency and implementing a central evaluation system for municipal public management, e.g. establish a single public registry of debt, an early-warning system for debt accumulation and a registry of municipalities in financial distress.

Box 2.26. **Key recommendations for a more comprehensive fiscal framework and increased fiscal responsibility** *(continued)*

6. Reinforce control and accountability:

- Audits and controls needed to ensure quality of financial data at the municipal level.
- Establish enforcement mechanisms and sanctions for non-compliance with fiscal rules: set up an independent overseer/council to assess budget actions and to draw attention to actual or potential violations is helpful to help ensure compliance.
- Reinforce democratic oversight and accountability by strengthening the capacity of municipal assemblies on budget issues.

Notes

1. The following data are derived from the IMF and OECD national accounts harmonised according to the standards of the System of National Accounts (SNA 2008) and refer to the "general government sector" (S.13). Regional financial data are not included in subnational government data (S.1313) but are still part of the central government sector (S.1311). As a result "regionalised investments" are not included in subnational government data.

2. The definition of gross debt follows the OECD definition, including the sum of the following liabilities: currency and deposits + debt securities + loans + insurance pension and standardised guarantees + other accounts payable. Most debt instruments are valued at market prices. It is consolidated and based on SNA 2008, except for some OECD countries including Chile (SNA 1993 non-consolidated).

3. Since 2001, fiscal policy in Chile has been based on the concept of a "cyclically-adjusted budget" (sometimes simplified to "structural budget") for the consolidated central government. Fiscal policy is based on the medium-term outlook and not the current situation. In theory, the approach consists of estimating public revenue while adjusting for the economic cycle and, consequently, authorising total expenditure as a function of these revenues. The goals is to eliminate pro-cyclical budgeting, i.e. during periods of economic expansion, a budget surplus will be set aside to be used during a slowdown. The approach's methodology has been improved since 2001 and is hailed by the IMF as the "cornerstone of Chile's impressive fiscal performance" (Larraín F. et al. 2011).

4. www.dipres.gob.cl, tab: estadísticas fiscales > gobierno general et Estadísticas de finanzas públicas. www.sinim.gov.cl, tab: Información sinim. Other sources were used for related and complementary aspects: Central Bank of Chile: www.bcentral.cl, tab: estadísticas; General Comptroller of the Republic of Chile: www.controlaria.cl, tab: informe presupuestario municipal; tab: Contabilidad pública > sector municipal > reportes presupuestarios.

5. This expansion does not mean that local governments have been given more freedom in the allocation of resources. Their increase often comes from national resources allocated to specific programmes by the central government.

6. Municipal operations, through the series proposed by the DIPRES, fluctuated wildly over 2003-2005 as if calendar effects or hesitations had an effect.

7. In addition to the increase in the number of staff resulting from municipal initiatives, local governments must bear the costs of personnel in the education and health sectors. On the other hand, the increase in remunerations, a national decision, is binding on municipalities.

8. A major reform of the national system of public education is being designed. It will have a significant impact on the funding of schools and thereby, on municipal financing. In fact, the reform intends to remove the administration and management of public schools from municipalities and create a system of public education, based on new providers of public education (Local Education Services). The reform was not taken into consideration in the present analysis as it was still being discussed at the time of the study.

9. An example of the importance of the municipal corporations and of the difficulty to evaluate the totality of the local financial operations is offered by the survey of the 'temporary pension debt' of the local institutions to the pension funds and others retirement provision institutions. At the end of 2015, 83% of the up-to-date temporary pension debt was concentrated in 23 corporations and 17% at 57 municipalities. Source: *Superintendencia de pensiones*.

10. For recommendations concerning the way of presenting municipal accounts that are in greater compliance with the principles of completeness, transparency and accountability, see Chapter 2.

11. Figures presented here are not consolidated, which explains the difference with the data published by DIPRES.

12. In 2015, the financial series that had been used ended. The future implications of the recent reform of inclusive education (2015) should be considered. The significant increases planned at the central level in the face of the education sector do not guarantee the advent of real local financial administration. Additional resources are allocated to essential state programmes.

13. However, the detailed analysis of the Common Municipal Fund, which is part of the grant system, and recommendations for reforming equalisation mechanisms are included in Chapter 3.

14. The territorial tax (*impuesto territorial*) is also called the real estate tax (*impuesto sobre los bienes raices*) or property tax (*predial*). It is part of the extended property tax family.

15. The valuation method used by the SII in Chile has a number of similarities (its precision leads to complex approximations) with the method used by the French tax authorities to evaluate the rental value of a property, which is a reference for taxes on built and non-built property. Like in France, Chilean citizens undoubtedly struggle to understand the system and the tax authorities and elected officials undoubtedly struggle to explain it.

16. Decree 1 on 12 February 2016, Ministerio de Hacienda.

17. Using the data of the table 2.4 (year 2014), with an average tax rate of 1% and with the value of the exempted properties (CLP 54 492.286 billion), the shortfalls for the municipalities is CLP 545 billion.

18. In 2014, the percentage of taxed properties was: Vitacura: 99.7%; Las Condes: 97.0%; Providencia: 97%; Lo Barnechea: 88.4%; Ñuñoa: 85.7%; La Reina: 81%; San Miguel: 80.7%; Santiago: 80%. A few municipalities have a high rate of taxed agricultural properties: Conchali: 100%; San Gregorio: 86%; San Bernardo: 84%, Maipu: 79%.

19. The Unidad Tributaria Mensual (UTM) is a unit of measure that exists only in Chile. It is used for tax purposes and for setting fines. Introduced on 1 January 1975, it equals a monetary amount expressed in CLP and is set by law and updated constantly by applying the fluctuation in the consumer price index. In October 2016, the rate of 1 UTM equaled 45 724 CLP (or 1 CLP = 0.000022 UTM). Applying a multiplication coefficient of 12 the UTA (Unidad Tributaria Anual) is obtained.

20. For example, San Gregorio (3 040 habitants), Zapallar (6 200 inhabitants), Santo Domingo (approx. 1 000 inhabitants), Ollagüe (315 inhabitants) and Rio Verde (134 inhabitants) generate more than CLP 350 000 per capita from municipal licences while, on the other end of the spectrum, Chiguayante (98 000 inhabitants) only receives CLP 1 700 per capita as well as many other big municipalities.

21. The highest overall revenue from licences in 2015 was found in the municipality of Las Condes: CLP 40 382 million, well ahead that of Santiago (CLP 23 920 million). Per capita, in Las Condes, municipal licences generate nearly CLP 400 000, in Providencia, nearly CLP 290 000 and in Vitacura, CLP 185 000. Santiago receives a mere CLP 154 000.

22. From the taxpayer's point of view, this does not mean that it is the business activities being conducted on the territory of the municipality that assume the entire tax charge voted by the municipality. They appear to be the ones paying the taxes but it possible, depending on the possibilities of passing on the local tax to prices, for example, it can lead to the translation of its charge to an end-taxpayer. This actual taxpayer's business might in fact be located in a different municipality; it is, in this instance, the vector of an export of the tax burden. The question of passing on the local tax is one of the most complex questions in public finance. It is only brought up here for informational purposes.

23. While revenue per capita from the vehicle registration tax averages CLP 21 500, a few municipalities, with varying sizes and environments, generate per capita amounts in excess of CLP 300 000. The small municipality of Rio Verde reached a lofty CLP 1.048 billion per capita.

24. Average per capita revenue from the waste management fee is, however, modest: CLP 5 300. Except for the big municipalities of Metropolitan Region of Santiago, only a few generate significant revenues (Algarrobo, Zapallar, Primavera, Santo Domingo, El Quisco, El Tabo, Papudo and to a lesser extent Vichquén, Viña del Mar, Isla de Pascua, Calama).

25. Added to the many exemptions, this contributes to the underfunding of the growing real costs of services.

26. On this point, it is interesting to note that the third chamber of the Supreme Court (Corte Suprema) ruled on 18 February 2016, in a case pitting a taxpayer against the municipality of Concepción, that the payment of the waste management fee should not be equated with paying a tax but rather paying for a service.

27. The wealthy municipalities of the Metropolitan Region of Santiago (Las Condes, Lo Barnechea, Maipu, Vitacura, Santiago) plus Osorno, Valparaíso, Coquimbo, Pudahuel and Chillán. Las Condes is clearly the biggest waste management earner (nearly CLP 3 billion), while the others range from CLP 0.5 to 1 billion.

28. These issues would need further analysis and are not within the scope of the present report. In addition, a reform of the administration of public education is currently being discussed ("New Public Education" reform, see Chapter 1). It intends to remove the administration and management of public schools from municipalities and create a system of public education, based on new providers of public education (Local Education Services) co-ordinated by the National Directorate for Public Education. The reform will imply a fiscal reform of the education system, thereby having strong implications for municipal finances and therefore should be implemented gradually (Santiago P. et al., forthcoming).

29. The number of earmarked capital grants should be reduced but not the total amount of capital grants. They remain low for the municipal sector and need to be increased, in particular to finance municipal investment.

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Chapter 3

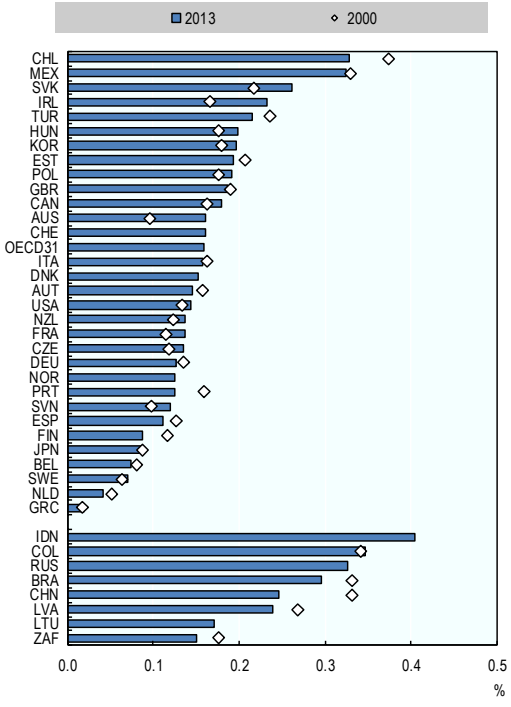
The equity challenge: Can existing horizontal equalisation mechanisms reduce municipal fiscal disparities?

This chapter focuses on the need to design more appropriate equalisation mechanisms, ones that go beyond the current system based on the Municipal Common Fund (FCM), a "compensation" system based on the horizontal redistribution of municipal resources across municipalities. This equalisation mechanism is commendable, however, it is not fully efficient and has some counter-productive effects on local and regional development. It should be complemented by other equalisation arrangements to combine solidarity and equity principles, as well as economic efficiency. Various avenues are proposed to help accomplish this, based on two approaches, in the short term through several adaptations of the current allocation rules and in a longer term approach through a more ambitious reform process, through more "verticalisation" and "regionalisation" of the mechanism.

Introduction: Chile is characterised by strong inter-regional and inter-municipal disparities

According to the Gini index, Chile, along with Mexico, the Slovak Republic and Ireland, displayed the greatest disparity in GDP per capita across TL3 regions in the OECD in 2013. During 2000-13, regional disparities increased in 18 out of the 32 countries while they decreased in Chile, in particular between 2008 and 2013 due to a better performance of the poorest regions (Figure 3.1). Despite this positive trend, regional differences in GDP per capita, measured by the range between the TL2 region with the highest and the lowest GDP per capita, remained markedly high in Chile in 2013. Together with Mexico and the United States, there are some regions in Chile that are at least three times wealthier than the national average, and other regions that have values that are less than half of the national average (Figure 3.2).

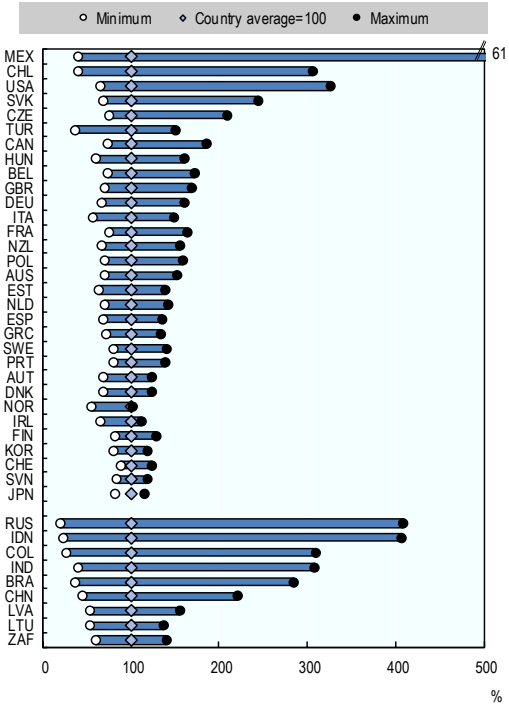
Figure 3.1. **Gini index of inequality of GDP per capita across TL3 regions, 2000 and 2013**



Note: in Chile, TL3 are the 54 provinces.

Source: OECD (2016a), *Regions at a Glance 2016*, http://dx.doi.org/10.1787/888933363221.

Figure 3.2. **Regional variation in GDP per capita (as a % of national average), 2013 (TL2)**



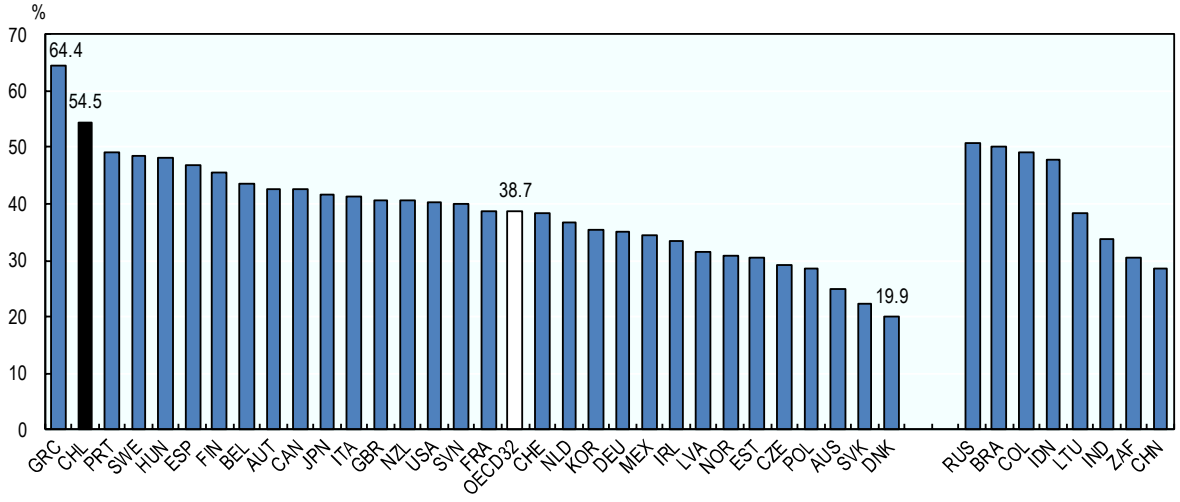
Note: in Chile, TL2 are the 15 regions.

Source: OECD (2016a), *Regions at a Glance 2016*, http://dx.doi.org/10.1787/888933363233.

In 2013, Chile had the second highest level of regional concentration in GDP among OECD countries, after Greece, i.e. a concentration index of 55 vs. 39 on average in the OECD. In the case of Chile, this largely reflects the importance of mining-intensive activities, which concentrate high-value economic activities in just a few regions (OECD, 2014).

Figure 3.3. **Regional concentration of GDP, TL3 regions**

National GDP concentration among the 10% population with highest regional GDP, 2013



Source: OECD elaboration based on OECD regional database (http://stats.oecd.org/Index.aspx?datasetcode=REG_DEMO_TL2).

Compared with other Latin American countries, Chile has one of the highest geographic concentration index (GCI of 0.6),[1] on par with that of Brazil, Uruguay, Peru and Colombia, and slightly higher than that of Argentina and Ecuador (ECLAC, 2015).

This reflects the Chile's population density and business activity in some small areas. The metropolitan region of Santiago (15,400 km^2 or 2.1% of national area) accounts for 41% of the Chilean population and also constitutes, in terms of economic activity, a powerful zone where a dense concentration of economic wealth is created. In 2014, the region generated 49% of the country's GDP and 41% of employment (Figures 3.4 and 3.5). It is equivalent to 2.7 times the GDP of Uruguay and nearly 3 times that of Costa Rica. By way of comparison, despite occupying 6.6 times less space, Santiago's per capita GDP is only slightly less than that of Sao Paulo (ECLAC, 2015).

Figure 3.4. **GDP breakdown by region (2013)**

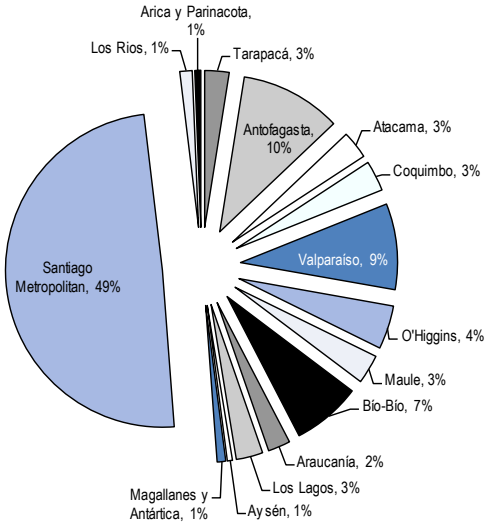
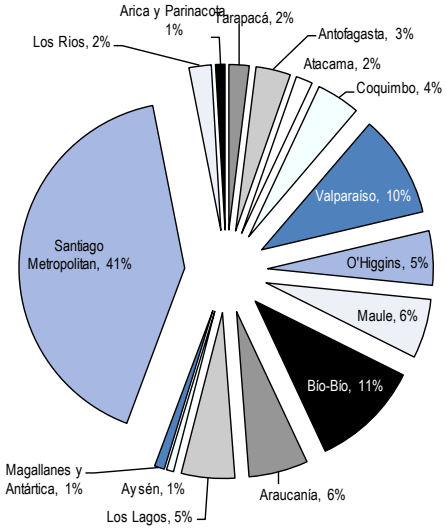


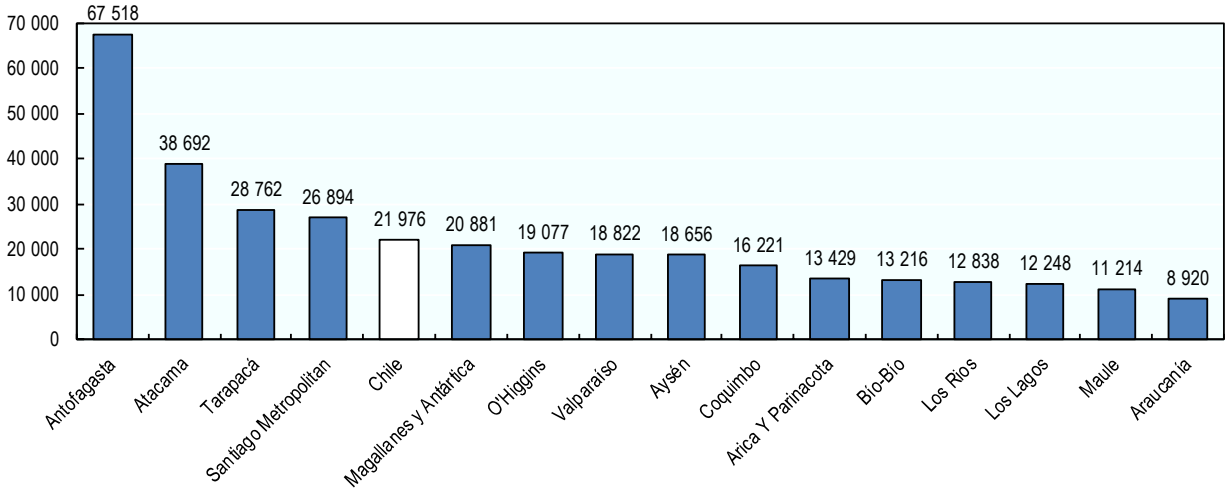
Figure 3.5. **Employment breakdown by region (2014)**



Source: OECD elaboration based on OECD Regional database (http://stats.oecd.org/Index.aspx?datasetcode=REG_DEMO_TL2). Data extracted on 10 February 2017.

In terms of per capita GDP, there are also wide discrepancies, reflecting the importance of mining regions in the production of wealth per capita. Antofagasta has a level of GDP per capita, 7.6 higher than in Araucanía. However, the high level of regional inequality is not only driven by Santiago and regions specialised in the mining activities. It also a result from the underperformance of a wide range of regions, including Aracania, Maule, Los Lagos, Los Rios and Bío Bío whose GDP per capita is significantly lower than the national average (Figure 3.6).

Figure 3.6. **Regional GDP per capita (2013, current USD, current PPP)**



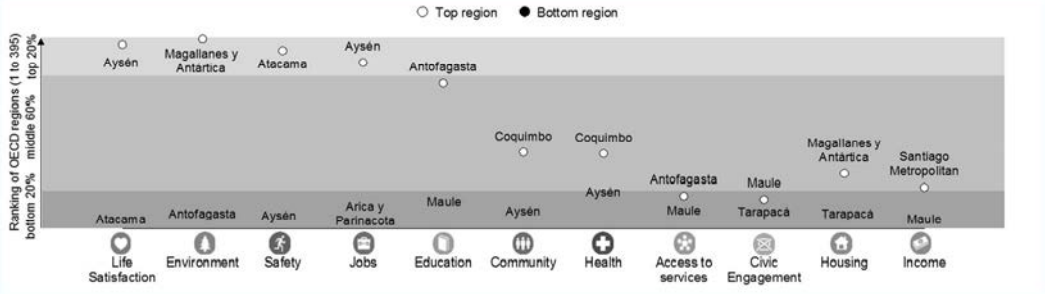
Source: OECD regional database, http://stats.oecd.org/Index.aspx?datasetcode=REG_DEMO_TL2.

Finally, the spatial inequalities are even more striking when non-pecuniary dimensions of well-being are taken into account (OECD, 2016a and 2016d). Chile has the largest regional disparities among OECD countries when it comes to life satisfaction, environment, safety, and jobs, as well as very wide disparities in education (Box 3.1).

Box 3.1. **Regional well-being in Chile and OECD countries**

Large regional disparities in Chile are found in life satisfaction, environment, safety, and jobs. In each of these dimensions at least one Chilean region ranks among the top 20% of the OECD regions and at least on region among the bottom 20% of the OECD regions. Small regional disparities are found in access to services, civic engagement, housing, and income, although in these dimensions all the thirteen Chilean regions rank among the bottom 30% of the OECD regions.

Figure 3.7. **Relative performance of Chilean regions by well-being dimension**

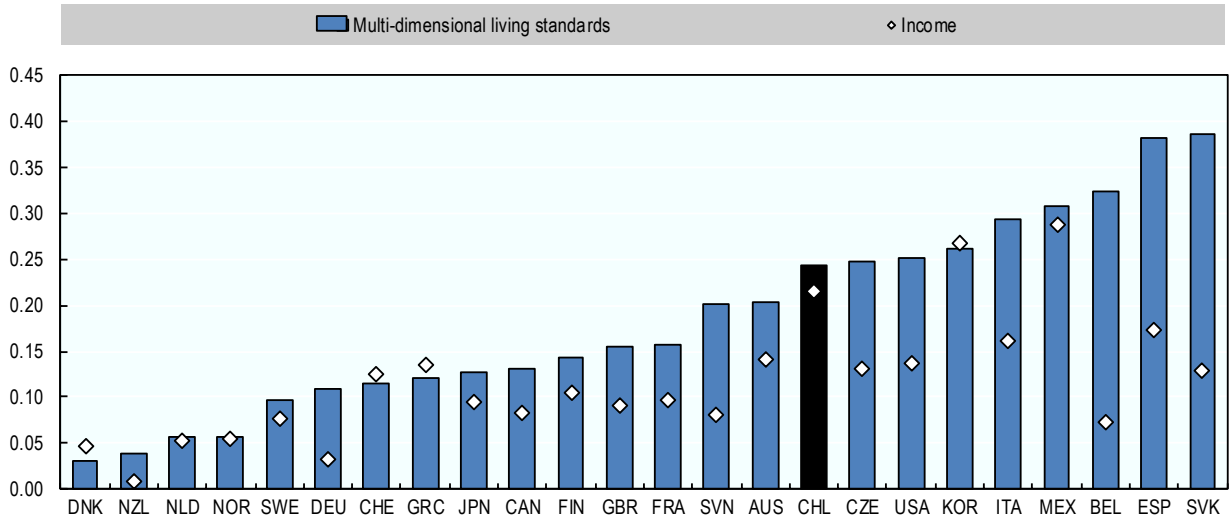


Note: Relative ranking of the regions with the best and worst outcomes in the 11 well-being dimensions, with respect to all 395 OECD regions. The eleven dimensions are ordered by decreasing regional disparities in the country.

Source: OECD (2016d) Regional Well-Being Database. Chile country fiche: www.oecd.org/gov/regional-policy/hows-life-country-facts-chile.pdf.

Another way to measure regional inequalities is to look at multi-dimensional living standards (OECD, 2016b). The OECD has recently produced a composite indicator that combines income, unemployment and health. This calculation at the regional level in a sample of 26 OECD countries finds that existing disparities in health and unemployment rates accentuate the gaps relative to household income only. This is the case in Chile, which ranks better among OECD countries than for the other indicators: 9 out of 26 (Figure 3.8).

Figure 3.8. **Regional disparities in multi-dimensional living standards are higher than for income alone**
Coefficient of variation (higher values mean larger disparities), 2012



Note: Income = disposable household income.

Source: Veneri, P. and F. Murtin (2016), "Where is inclusive growth happening? Mapping multi-dimensional living standards in OECD regions", *OECD Statistics Working Papers*, No. 2016/01; Calculations based on OECD (2016d), Regional Well-Being database and national income surveys. Statlink: http://dx.doi.org/10.1787/888933411860.

Such persistent inequalities partly reflect Chile's singular geography, including the very unequal distribution of mineral resources. They have pre-conditioned to some extent both settlement patterns and economic activity. However, this challenging geography is not the only explanation. It is difficult to avoid the conclusion that the approaches to regional policy hitherto employed have not delivered. They have been largely driven by centralised, top-down and sector-based approaches thus facing difficulties in adapting to the different needs of Chilean regions (OECD, 2015a).

In this context of sharp territorial disparities, regional disparities overlap with inter-municipal disparities. With 345 local political-administrative structures, there are as many unique situations as municipalities especially given the diversity of their population densities, geographic and climatic environment and their size (AMUCH, 2015). The 345 Chilean municipalities have characteristics that combine a relatively high demography and vast geographic area, excluding the most densely-populated zones (see Chapter 1). Although disparities between municipalities are determined in part by the region in which they are located, each case is different and ultimately depends on the level of their resources and expenditures, which can differ significantly depending on local circumstances. It is important to identify the situation clearly before the organisation and functioning of the political-administrative system can be modernised and improved. This diagnostic is important on two levels:

- To evaluate the gaps in the initial situation that would potentially be exacerbated by a poorly-designed decentralisation process.
- To evaluate the existing mechanisms (particularly the Municipal Common Fund) or the ones that should be promoted to ensure territorial equity.[2]

There is a certain amount of risk that only the most robust municipalities financially, technically and administratively will truly benefit from greater decentralisation. In this case, the gaps will widen versus the municipalities that are the least able to take on new competences, especially if the central state is incapable of enacting policies that ease territorial discrepancies.

In 1979, Chile implemented an original mechanism for the "cohesive redistribution of own resources between the municipalities": the Municipal Common Fund *(Fondo Común Municipal* - FCM*),* established by the article 38 of Law No. 3.033. It has become a crucial part of how municipal budgets are financed and plays a strategic role in the reduction of inter-municipal inequalities and political cohesion in the municipal system in Chile.

By identifying the magnitude of inter-municipal disparities and the diversity of their origins a clear picture of the challenges facing the FCM will emerge. To address them, a diagnostic, by deconstructing the mechanism, is essential to trying to understand the intrinsic characteristics of the mechanism and the justification of arguments according to which the FCM fails to contribute to the reduction of territorial inequalities. Based on this diagnostic, avenues to improve it will be explored by referring to the reconstruction of the mechanism founded on principles inspired by economic theories related to territorial equity.

Inter-municipal financial disparities

This section is based on the convergence of two approaches. First, an in-depth analysis is conducted on how expenditure and local finance mechanisms lead to inter-municipal disparities. In addition to identifying their intensity, it sheds light on the ways in which budget items are distributed geographically and whether they contribute to territorial disparities. Fundamental ways to improve the system are also discussed. Second, the local budget, more than just a series of revenues and expenditure distributed in a uniform or disparate manner across the territory, is a combination of these heterogeneous elements. An integrated approach towards these budget items reveals those that play an important role in creating various situations among municipalities. Typologies founded on the budgetary characteristics can leverage this synthesis.

A wide array of causes

Individualised statistical analyses, broken down by the type of operation (expenditure and revenue), are backed by municipal databases accessible on the SINIM website. They provide insight into the levels and dispersion for an entire series of budget indicators for each and every municipality. Unless mentioned otherwise, all evaluations use 2015 data, cover 341 of the 345 municipalities in Chile[3] and are evaluated on a per capita basis to limit effects related to size. Except where mentioned, the baseline population is the one estimated by INE for 2014, which does not include the "floating" population, which is accounted for in the resource attribution algorithm of the FCM.

An initial reference to the budget volumes in play set the parameters of the fiscal realities of municipalities in Chile. For both small and big municipalities, the difference between the budget amounts is substantial. Taking current expenditure in the municipal sector, the median budget in 2015 was CLP 2 170 million (CLP 2 714 million for total expenditure), ranging from a minimum of CLP 426 million (Coelemu) to nearly CLP 138 000 million (Las Condes), i.e. ranging from 1 to 325. For one quarter of the municipal budgets, current expenditure does not exceed CLP 1 476 million while for the highest quarter current expenditure is higher than CLP 4 622 million.

In logarithmic terms, there is an inverse relationship between the demographic size of the municipality and the main financial indicators measured on a per capita basis. This is a dominant and essential characteristic of the Chilean municipal system. With a few small variations, expenditure of the three sectors (municipal, education and health) falls in line with this trend. Looking at the per capita expenditure for the three sectors taken together, the relationship is non-linear (Figure 3.9, Table 3.1 – results are displayed on a logarithmic scale). The level of per capita expenditure decreases with the increase in population size to a threshold of around 90 000 to 110 000 inhabitants. Beyond this size, they are of a somewhat similar order of magnitude.

On this wide spectrum, the variation of per capita amounts is significant and indicates the diverse situations of municipalities concerning either the sectors of intervention (particularly healthcare and education) or the expenditure/revenue of strictly municipal budgets.

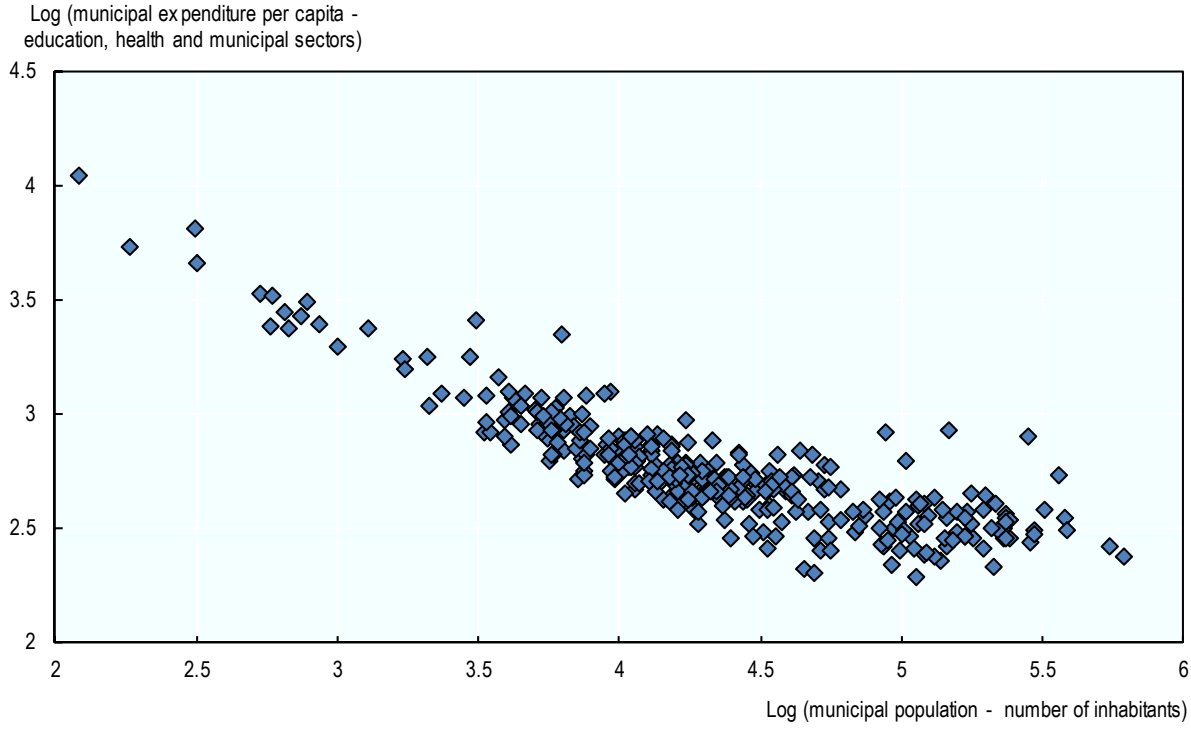
Table 3.1. **Correlation coefficients between expenditure indicator per capita (log value) and population (log value)* (2015)**

Expenditure per capita	All municipalities	Municipalities over 5 000 inhabitants	Municipalities of the Metropolitan Region of Santiago
All three sectors	- 0.850	- 0.734	- 0.479
Municipal sector	- 0.760	- 0.540	- 0.204
Education sector	- 0.830	- 0.765	- 0.765
Healthcare sector	- 0.227	- 0.103	- 0.162

* The correlation coefficient between education expenditure per capita (log) and healthcare expenditure per capita (+0.181 for all municipalities) indicates a statistical independence of both series.

Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

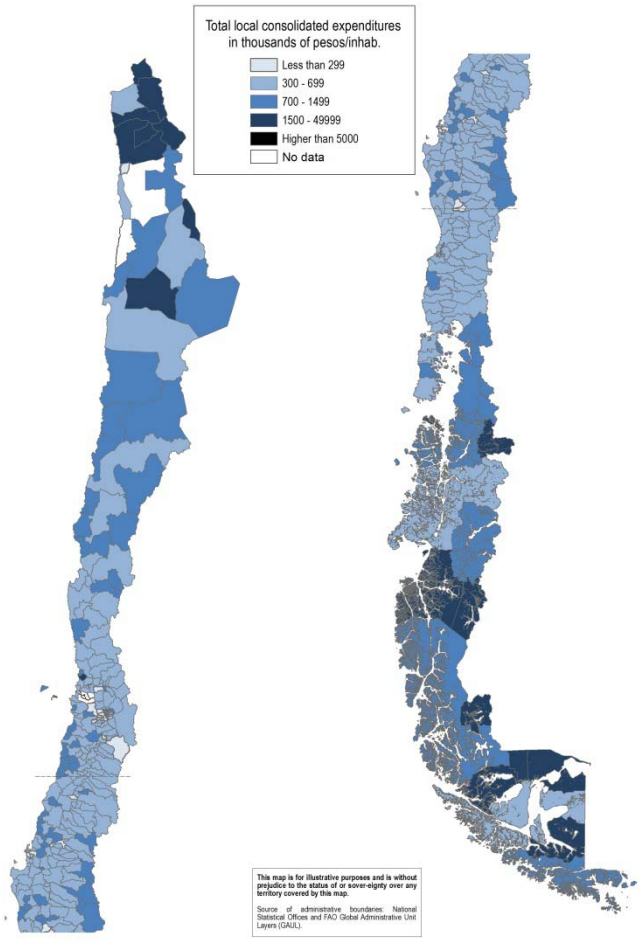
Figure 3.9. **Local expenditure of all three sectors per capita and population (log-log scale) (2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

The geographical representation of levels of per capita expenditure reveals significant differences between extreme territories (north and south) and some mountain areas with high values, and the largest number of municipalities with lower levels of per capita expenditure (Figure 3.10).

Figure 3.10. **Local expenditure of all three sectors per capita (2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

The variable heterogeneity of local expenditure commitments (education and healthcare)

The disparities between municipalities in the areas of education and healthcare (and cemeteries to a lesser extent) reflect the diversity of situations and choices local officials are facing in Chile. A side-by-side analysis of how budget line items (expenditure and revenue) are distributed reveals the similarities of the manifestations and causes of inter-municipal disparities that mark these two sectors.

The education sector: Spending disparities and variety of municipal behaviours

Generally speaking, the education sector is under the control of the central government and is financially dependent on central funding (see Chapters 1 and 2). Despite these uniformity factors, local education budgets vary a great deal from one municipality to the next.

The dispersion of expenditure per inhabitant provides a clear picture of this assessment. Although total average expenditure is CLP 135 000 per capita (i.e. weighted

average), the average of municipal expenditure per capita is CLP 257 000 (i.e. unweighted average), for a median value of CLP 230 000 per capita. This per capita expenditure ranges from a minimum of CLP 25 000 (Alto Hospicio) to a maximum of CLP 1.17 billion (San Gregorio), i.e. 9 times the average and 47 times higher than the lowest amount spent on education per person. In fact, nearly all municipalities whose expenditure per inhabitant exceeds CLP 700 000 have sparse populations and/or cover large geographic areas. The combination of these two elements means that local interventions face structural constraints because of low population density (e.g. Rio Verde, Timaukel, Primavera, Torres del Paine, O'Higgins, Ollagüe). The essential question regarding incidences of under population and how it affects local management (management, expenses) lies, however, in the concrete conditions of human presence on these immense spaces: concentration in one spot or dispersion across the territory. The question of isolation from major urban centres remains.

On the other end of the spectrum, the municipalities that spend the least on education per capita (less than CLP 100 000) include the vastest (Viña del Mar, Temuco, Concepción). This observation points to a relationship between small population size[4] and high level of expenditure, as underlined in the introductory remark.

However, in order to correctly interpret the reality of municipal education expenditure, it is necessary to take into account two factors:

- Only a few municipalities have corporations; but they are important municipalities.
- The distribution of pupils between municipal schools and private schools within the municipality.[5]

The analysis must also integrate the financing conditions of the education sector as level of expenditure and amount of resources for education are indeed linked. Subsidies from the MINEDUC (particularly the schooling subsidy) are high. On average, they account for 55% of spending but cover from 0 to 96% (La Serena) of expenditure depending on the municipality. The per capita amount of this subsidy also varies from 0 to CLP 774 000 (General Lagos). Although not all municipalities benefit to the same degree, all of the small municipalities' needs are met sufficiently. However, the lowest per capita education expenditures are found, to a large extent, in the municipalities in the metropolitan region of Santiago and in other major cities (Viña del Mar, Alto Hospicio). The contribution of the FNDR for education is more selective and concentrated.

The contribution of the municipal budget to education is obviously on a much smaller scale compared with MINEDUC funding. The share of the municipal contribution to the education sector varies, however, a great deal. In some cases, it is greater than 40% (Sierra Gorda, Torres del Paine, Las Condes, Lo Barnechea, Vitacura, Timaukel, etc.) and even reaches 70% in Rio Verde. The per capita amounts are, in some cases, very significant and although some municipalities do without municipal support (Huasco, Hualpen, Los Angeles) or limited support (Tolten, Victoria, etc.), other municipalities contribute heavily (e.g. Rio Verde, Torres del Paine, San Gregorio, Ollagüe). Evaluated in terms of municipal effort, the municipal contribution accounts for a significant part of overall municipal revenue (nearly 30% for Cabo de Hornos, Torres del Paine, San Pedro and El Monte).

Depending on the municipality, this fiscal contribution follows two distinct approaches:

- In small municipalities that are heavily supported by the ministry, municipal contribution tops up the central subsidy and increases the level of expenditure.
- In heavily-populated municipalities belonging to the Metropolitan Region of Santiago (Lo Barnechea, Las Condes, for example), municipal support substitutes for the central transfers.

Therefore, depending on the municipality, the municipal contribution either complements or substitutes state funding. Beyond these fiscal oppositions, two factors of cohesion stand out. First, in terms of share in total education expenditure, personnel expenditure is highly uniform, absorbing around 80% of total expenditure and the dispersion of municipal ratios is weak. The weight of personnel is the leading factor underpinning disparities in total expenditure. In addition, another element of cohesion adds to this preponderance and is denounced regularly by the municipalities: personnel costs exceed, by an average of 42.5%, the amount of the MINEDUC contribution (nearly 55% if the average of the municipal ratios is used). Excluding some outliers, very few municipalities are able to achieve a positive balance. Since 2011, this ratio has continued to deteriorate to the detriment of municipal finances. Second, investment expenditure in education is virtually non-existent.

The health sector: Spending disparities and variety of municipal behaviours

Despite some differences, the disparities between municipalities in the healthcare sector is a closely mirrors of the situation in education. However, the organisation is different, which modifies the scope of municipal approaches.[6]

Total expenditure per inhabitant (CLP 72 000 on weighted average and CLP 100 000 on unweighted average) are distributed in a similar manner to that of education. The top of the rankings include, once again, the small municipalities (Rio Verde, Timaukel, Torres del Paine, Juan Fernandez, Ollagüe) for which the level of expenditure is 3-6 times higher than the average. On the other end of the spectrum, the thriftiest municipalities (bottoming out at 1/5 the average excluding Quirihue) are in all population classes: Santiago and Maipu are close to municipalities ranging from 3 000 to 90 000 inhabitants. However, the correlation coefficient is weak (-0.227).

As in the case of education, the explanation for these high levels of total expenditure must reside in their small population size and higher subsidies, as well. As was true for education, healthcare is heavily dependent on transfers, primarily from the MINSAL, which accounts for approximately 60% of total revenue (topping out at 80%). Both in terms of contributions to resources or level per inhabitant, funding from the MINSAL does not vary much. However, funding from the FNDR for healthcare operates differently. More selective, it sometimes provides a very considerable contribution.

Given the central government transfers, contributions by the municipal budget to healthcare play a different role compared with the situation for education. The substitution effect plays a dominant role in municipalities with high expenditure. Municipal transfers compensate more than they complete the central funding. While average per capita funding is CLP 10-16 000, the most active municipalities allocate much higher amounts. Again, Rio Verde is an unusual example (CLP 526 000) but there are many other municipalities that provide substantial funding of around CLP 100 000. Another illustration of local engagement, the municipal contribution is sometimes very high: it is greater than 90% relative to the overall revenue of the healthcare sector in Valparaíso, Calera de Tango, San José de Maïpo, La Reina, Punta Arenas, Peñaloén, Limache, Queilllén, and Chonchí. In these cases, the municipality is clearly stepping in

and substituting for the lack of central support. Other indicator of the municipal effort, as in education, healthcare absorbs, in a few cases, a significant share of own municipal resources (36% in Chonchí, nearly 33 % in Punta Arenas or in Valparaíso, more than 30% in Pudahuel and Peñaloen).

Personnel expenditure is a cohesion factor that is identical to the education sector and accounts for an average of three-quarters of total healthcare expenditure. The average local personnel expenditure per inhabitant is CLP 77 000. Excluding Rio Verde (CLP 1.3 million), the indicator is weakly scattered across all municipalities. The effect is similar on operating expenditure (other than personnel costs). The comparison extends to the deficit in the MINSAL subsidy's coverage of personnel expenditure in healthcare. MINSAL subsidies only cover around 80% of personnel expenditure and although the deficit is not as great it remains unfavourable for municipalities and has tended to get worse over time (in another expression of this deficit, personnel expenditure exceeds the ministerial subsidy by around 24%). In another similarity with education, capital expenditure is very low and is only present in 59 municipalities (1/6 of all municipalities).

In all, for education and heath municipal budgets, there is a strong homogeneity in terms of structure of expenditure (and revenues), which is associated with strong disparities in levels of expenditure (and revenues).

The duality of municipal sector budget disparities

Municipal sector expenditure: Diversity and homogeneity

Municipal expenditure, per area and nature, has wider disparities than those of the education and healthcare sectors. Less standardised, municipal activities can respond to a wider variety of local preferences.

Per inhabitant, the dispersion indicators of total municipal expenditure, especially current expenditure, are two to three times higher than those of the two sectors of education and health. Once again, as was true for those two sectors, the smallest municipalities have a particularly high level of per capita expenditure: their expenditure per capita never falls below CLP 1 million and tops out at CLP 9.5 million in Rio Verde or CLP 5.5 million in Olliagüe while the average expenditure is CLP 215 000 (median: CLP 224 000). Excluding the big municipalities, expenditure ranges between CLP 80 000 and 160 000 per capita. This type of relationship tends to lend credence to the assertion that economies of scale are at work and that being underpopulated, for the smallest municipalities, comes at a cost.

At the other end of the spectrum from the big spenders, some 30 municipalities allocate less than CLP 150 000 to municipal sector expenditure. The regional capitals often have below average levels of municipal sector expenditure (Telmuco, Copiapo, Arica, Valdivia, Puerto Montt, Concepción, Talca) or close to the average (Antofagasta, Punta Arenas, La Serena). Iquique is above average as is Santiago which allocates over twice as many resources to municipal actions than other regional capital. For the others, in the populous municipalities of the metropolitan region, Las Condes, Providencia, Lo Barnechea, Vitacura spend the most. This propensity to spend contrasts with the stinginess of La Granga, Pintana, El Bosque, Lo Espejo, Aguirre Cerda and Peñaflor.

The breakdown of total or current expenditure based on area (i.e. municipal activities, internal management, cultural programmes, recreation, social programmes, community services, transfers to the FCM, etc.) adds to the notion that local municipal budgets vary tremendously. Regardless of the per capita differences in spending levels, the dispersion

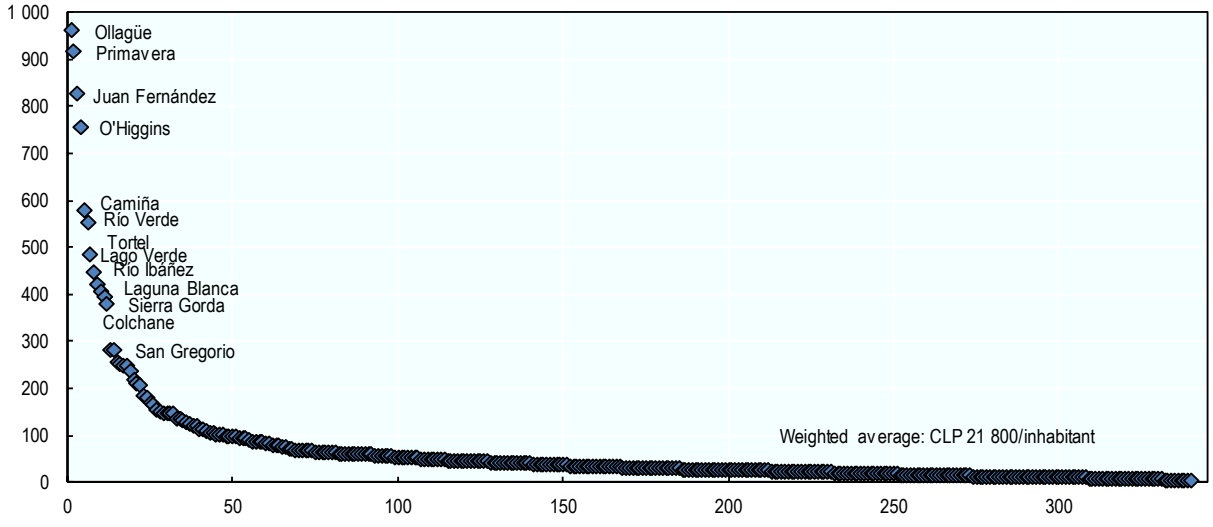
indicators are, excluding social programmes, higher than those of total expenditure. Each item contributes to widening the disparities although their aggregation attenuates the overall impact. To nuance this observation, it is important to observe that the dispersion is often the result of a handful of municipalities that spend amounts on certain line items that vary considerably from the average.

Expenditure, based on its nature**,** paints a fiscal picture that is even more varied. The biggest disparities concern some categories of expenditure that are very fragmented, for example municipal sector investment i.e. the acquisition of non-financial assets (buildings, land, machines, vehicles, furniture, computer hardware and software. Moreover, a few municipalities – which are sometimes among the least populated – can occasionally make sizeable investments, skewing the per capita ratio.

Municipal per capita investment (Figure 3.11) shows an inverse relationship with municipal population size. The smaller the municipality, the higher the per capita investment. Conversely, the larger the municipality, the lower the per capita investment. This nonlinear relation in traditional co-ordinates takes a linear form when the data (population, capital expenditure) are expressed as a logarithm The second figure shows that the correlation coefficient is strong (-0.77), while in the other, because of the exponential form of the relation, it is weak (-0.21). This increase in capital expenditure per capita in small municipalities illustrates their high propensity to invest (Figure 3.12).

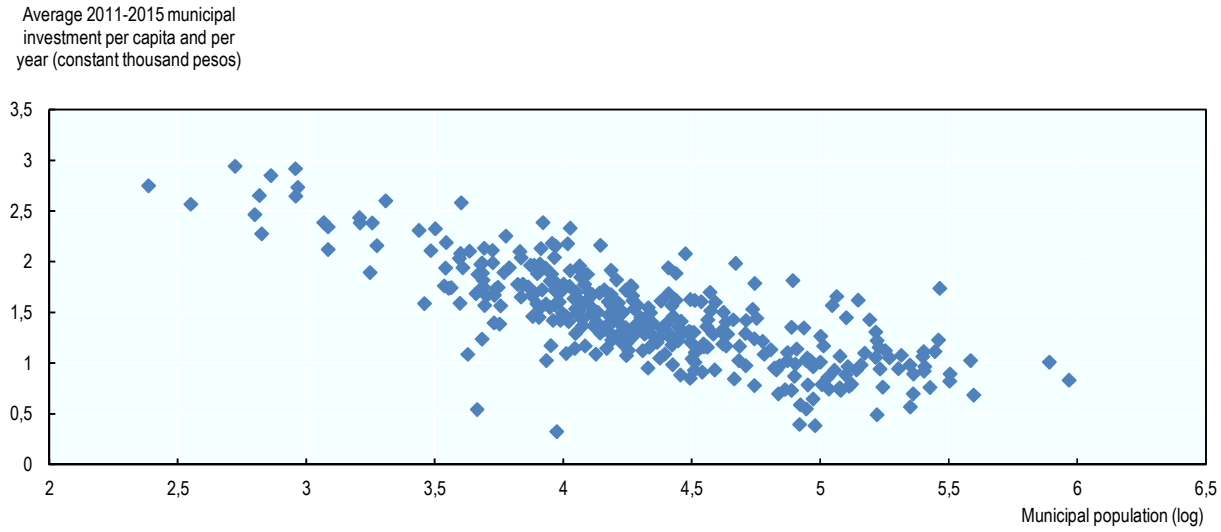
This inverse relationship between municipal demographic size and per capita expenditure (whether investment, current or total) is a prominent characteristic of the Chilean municipal system. It demonstrates the presence of sub-density costs in the provision of local public facilities and collective services. This is one of the challenges that must be faced in order to ensure that all citizens, in a large country and with scattered settlements (with the exception of metropolitan areas), have equal access to public services. The dispersion of the population makes it more difficult to capitalise on economies of scale, which would reduce unit costs or even per capita spending, which may be expected to increase alongside the size of the population to be served.

Figure 3.11. **Municipal investment per capita (annual average 2011-2015, constant CLP, value 2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Figure 3.12. **Average 2011-2015 municipal investment per capita and per year (constant thousand CLP) compared to municipal population (log)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

For more conventional and common items (personnel expenditure, goods and services, transfers), the disparities are much less marked. As seen previously, the smallest municipalities occupy the highest ranks of per capita expenditure. In terms of personnel expenditure, Rio Verde tops with CLP 3.4 million while Puente Alto dwells at the bottom of the list at CLP 11 500. The same observation holds true for the other items.

Municipal revenue: Divergences and convergence

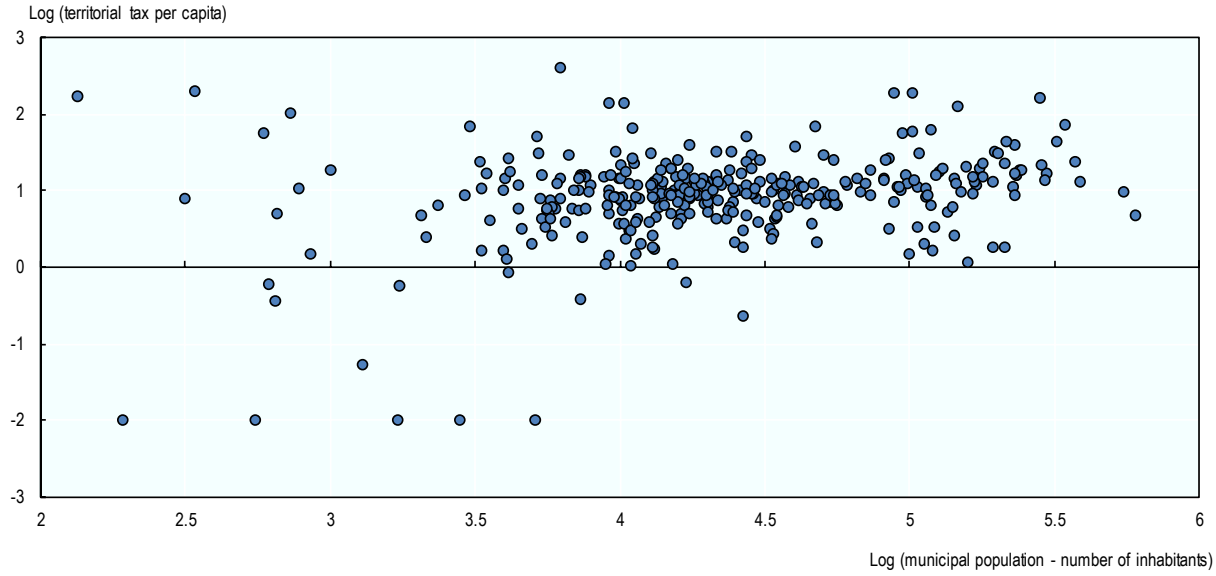
The analysis of municipal revenue will be here limited to an individualised approach. The evaluation of total revenue, under the constraints of budget balance rules, does not provide any additional insight compared with the total expenditure analysis. For all line items, the indicators measuring the dispersion of per capita amounts are higher. They are markedly higher than those identified for the municipal expenditure line items. The dispersion explains how revenue is distributed and spread unevenly amongst municipalities.

FCM contributions account for the lion's share of revenue distribution. The dispersion of FCM is intended to redistribute and correct the unequal contributions of tax revenues and the compliance of municipalities with specific constraints. Although conclusions cannot be drawn regarding the redistributive qualities of the equalisation mechanism, this dispersion implies that it is discriminatory by nature. The most significant contributions (CLP 5.374 million in Rio Verde, nearly CLP 4 million in Timaukel, over CLP 1 million in Torres del Paine, San Gregorio, Tortel, O'Higgins, Camiña, Laguna Blanca, Primavera) are concentrated in many of the municipalities in the region of Punta Arenas. Within each region, the capital city benefits the least per capita from the FCM. Illustrating how the mechanism functions, the municipalities of Santiago, Providencia, Las Condes, receive 200-300 times less revenue per capita from the FCM

than the best-off municipalities (excluding the outliers Rio Verde, Timaukel and Ollagüe). This basis of dependence on redistribution, averaging nearly 50% of the total, is accompanied by revenue that is contrasted with regard to the overall dispersion.

Revenues with the least dispersion include the territorial tax, SUBDERE subsidy and driver's license fees. This results in part from varying population densities and territorial wealth, and reflects the differing situations faced by local authorities due to tax legislation. The specificity of the territorial tax, received by almost all municipalities, is to confuse the budgetary points of reference that had previously been identified. Among the small municipalities, which receive a sufficient amount in transfers (particularly from the FCM), per capita contribution is sometimes zero (General Lagos, Timaukel, Colchane) or sometimes 10 times above the average (Rio Verde, San Gregorio, and to a lesser extent Torres del Paine). For the latter, it is on par with the amounts in the budgets of wealthy municipalities in the metropolitan region (Lo Barnechea, Las Condes, Vitacura). They receive per capita contributions from the territorial tax that are 2.5 times higher than Santiago.

Figure 3.13. **Territorial tax per capita and population (log-log scale) (2015)**



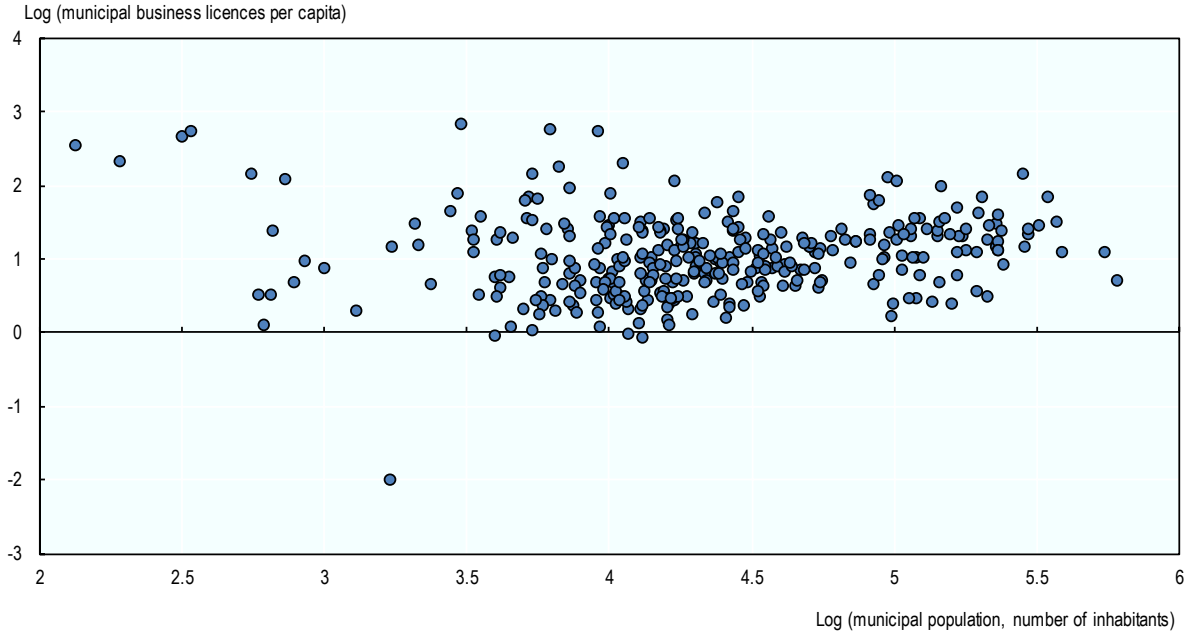
Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Operating income and user fees (*derechos de explotación, ingresos operativos*) are more dispersed than territorial tax revenue and are indicative of greater leeway for municipal management and for the financing of services. Overall, these resources are weak (CLP 1 000 per inhabitant) and contribute only marginally to total revenue (0.2-0.4%). This substantial dispersion suggests that local conduct varies considerably. Licences and the driver's license fees generate similar amounts of average revenue (CLP 28 000 per capita) and their dispersion is similar as well (variation coefficient of 2.65%).

The major, wealthy municipalities of the metropolitan region and the tiny municipalities in the extreme south both have high levels of municipal business licenses.[7]

This pattern (i.e. a mix of large and small municipalities) is also true for the lowest amounts of municipal business licenses. It suggests that there are differences in the fiscal choices at the municipal level that superimpose contribution inequalities regarding taxation.

Figure 3.14. **Business licenses per capita and population (log-log scale) (2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

The distribution of casino and gambling revenues to municipalities is unique in the resource mix and generally a minor – yet, in some instances, essential – contributor.[8]

In summary, the distribution of municipal revenue combines divergent forces and convergent factors. The identified dispersions are diverse and reflect this mix of influences where municipalities' capacity to take action is limited. The dependence of local budgets on the redistribution of resources (the weight of the FCM) provides financial security while limiting elected officials' ability to take action. By its intensity and heterogeneity, the dispersion of the inter-municipal distribution of variables, which reflect the level and composition of local budgets, suggests a differentiation among municipalities.

A typology of differentiated municipal situations

The focus on the dispersion of each line item comprising local budgets does not shed light on the role that they play and their place in the budgetary diversity of municipalities. This type of analysis presents two limitations: the perception is fragmented and does not provide a synthetic picture of the landscape; the perception is overloaded with the number of information to connect (financial variables, number of institutions). Therefore, it is interesting to complement it by a multidimensional analysis.

The goal of multidimensional analysis is to reveal the underlying elements of differentiation and resemblance which are overlooked among the large number of data. The goal of multidimensional analysis aims at restoring the big picture of the pockmarked environment resulting from an item-by-item analysis. Instead of the dispersion of each variable, this analysis focused on the contribution that they jointly make to the differentiation of municipalities. The correlations between variables organise, order and weigh the differentiation factors associating several variables. On the basis of these differentiation factors, clusters of municipalities are formed, according to the proximity or distance of their financial profiles, echoing the saying: "Birds of a feather flock together".

This exercise of identification of the underlying structure of the financial aspects of the municipal activities is done for the entire country in order to identify some common denominators but also for the Metropolitan Region of Santiago.

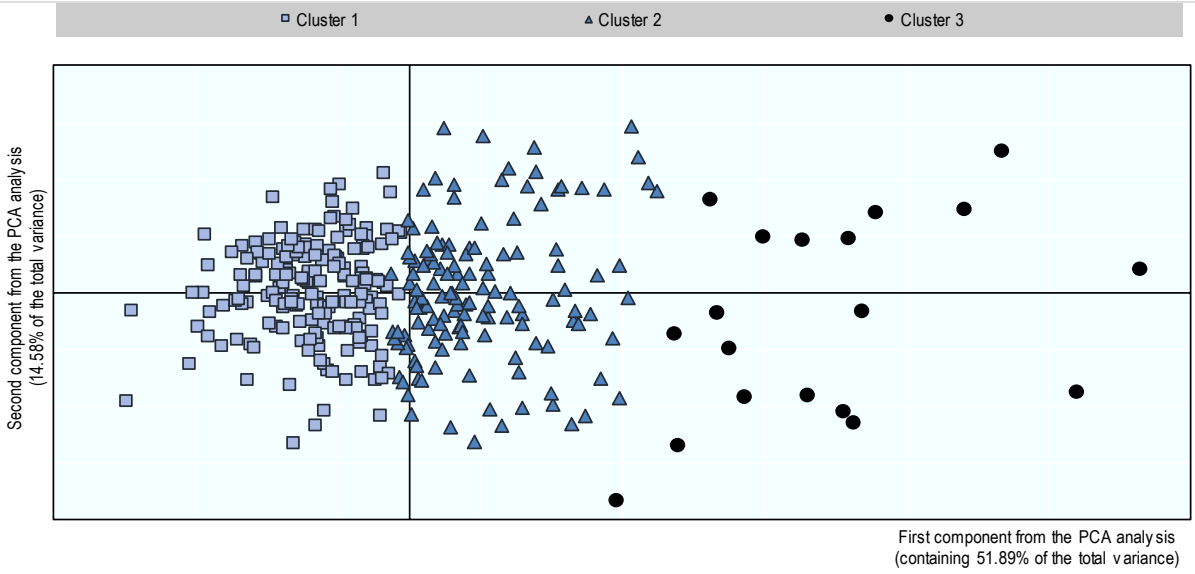
The fiscal differentiation factors of Chilean municipalities

The analyses are applied to the per capita expenditures of the "municipal sector"[9] for 2015. To better identify the phenomena and given the amplitude of the numbers that have already been identified, the data were transformed into a logarithm. This operation does not alter in any way the hierarchy or nature of the observations and merely reduces the amplitude of the graph.

Analysis of expenditure by nature

For expenditure by nature, over half of the overall variance (52%) is eliminated by the first factor, which resulted from the combination of personnel expenditure and intermediary consumption costs (goods and services) and reflects a dimension effect. The municipalities range from the smallest, penalised by their small geographic size and low density, to the biggest (all of the Metropolitan Region of Santiago municipalities) and the regional capitals. The second area of differentiation is determined by the municipalities contributing to the FCM. Santiago, Lo Barnechea, Las Condes and Providencia are virtually the only contributors to the construction of this second area of differentiation, which eliminates 16% of the overall variance. It can be interpreted as the expression of a wealth effect.

Figure 3.15. **Factorial axes of differentiation in per capita municipal expenditure by nature (logarithmic transformation) (population INE)**

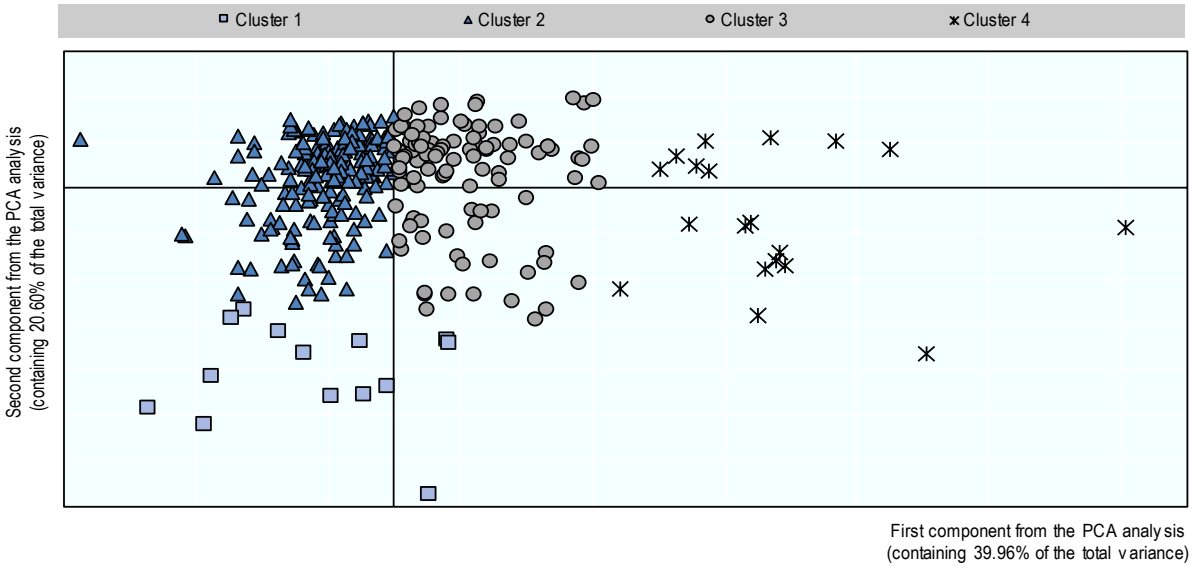


Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Analysis of expenditure by area

The analysis of expenditure by area in which the resources are allocated solidifies the results of the differentiation by their nature. The first factor, which eliminates 40% of the inertia of points forming the cloud, is one-directional. As was the case previously, it includes a dimension effect (under-population and economies of scale). It profoundly marks current expenditure and social welfare actions. The second factor (20%) expresses the hierarchy of municipal priorities between performing basic functions as well as cultural and recreational activities. Of the municipalities that contribute the most, none spend money on this second type of intervention. It represents a priority for quality of life. The third factor, responsible for 10% of overall variance, is exclusively determined by the means allocated to community services (green spaces, signs, public lighting, and collecting household waste).[10] They are intended to improve citizens' surroundings, in particular Chileans' living environment.

Figure 3.16. **Factorial axes of differentiation in per capita municipal expenditure by area (logarithmic transformation) (population INE)**

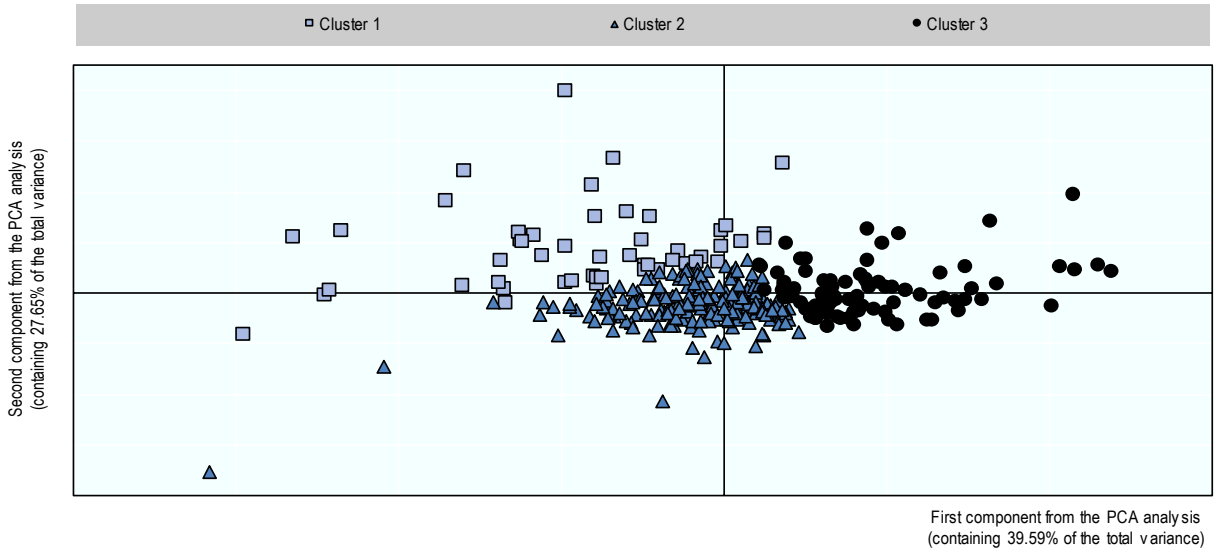


Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Analysis by municipal resources

The combined factors of municipal differentiation by their resources, confirms, under a different angle, the diagnostic made from the analysis of expenditure. The first differentiation factor (40% of the variance) combines revenues from the waste management fee (*derechos de aseo*), the territorial tax and contributions from the FCM. This combination, which may seem surprising, is found most often in municipalities with substantial per capita resources. This superior level comes from two sources: the territory (*aseos, impuesto territorial*) and inter-municipal solidarity (contributions from the FCM). Both wealthy municipalities and those that receive support are spread along a wealth axis. Resources provoke a size effect on the local budget depending on the two ways in which they are constituted: endogenous and exogenous. The second factor (28% of variance) is based on the combination of three sources of revenue: driver's license fees, licenses and transfers (other than the FCM). The municipalities that contribute to it are found in large quantities in the middle of the distribution of local budgets.[11] They are characterised by a two-pronged situation: less dependent on the FCM and a more diversified tax base, less founded on property values (*impuesto territorial*) than backed by economic activity.

Figure 3.17. **Factorial axes of differentiation in per capita municipal revenue (logarithmic transformation) (population INE)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Of these differentiation factors the most readily apparent is the size effect, which affects directly affects expenditure, and indirectly affects resources. Not surprisingly, size is the most important differentiation factor (from 40% to 50% depending on the theme) of local budgets. Secondary factors have less impact, though it is not negligible (from 16% to 28% of the variance) and create divisions that would not have spontaneously arisen (wealth, action priorities, relative economic specialisation).

Revenue differentiation of the municipalities of the Metropolitan Region of Santiago

By the composition and the per capita amount of their revenues, the 52 municipalities of the Metropolitan Region of Santiago draw a traditional landscape with an easily identifiable structuration.

The two first axes of differentiation of the financial profiles alone explain nearly 80% of the total variance of the scatter plots. The only original thing to note is the atypical source of revenue from casinos and gambling. This puts the municipality of Cerro Navia in a class of its own. The elimination of this specific revenue does not change the clusters of municipalities, except, obviously, for Cerro Navia.

Figure 3.18. **Factorial axes of the per capita revenues of the municipalities of the Metropolitan region of Santiago (logarithmic transformation)**

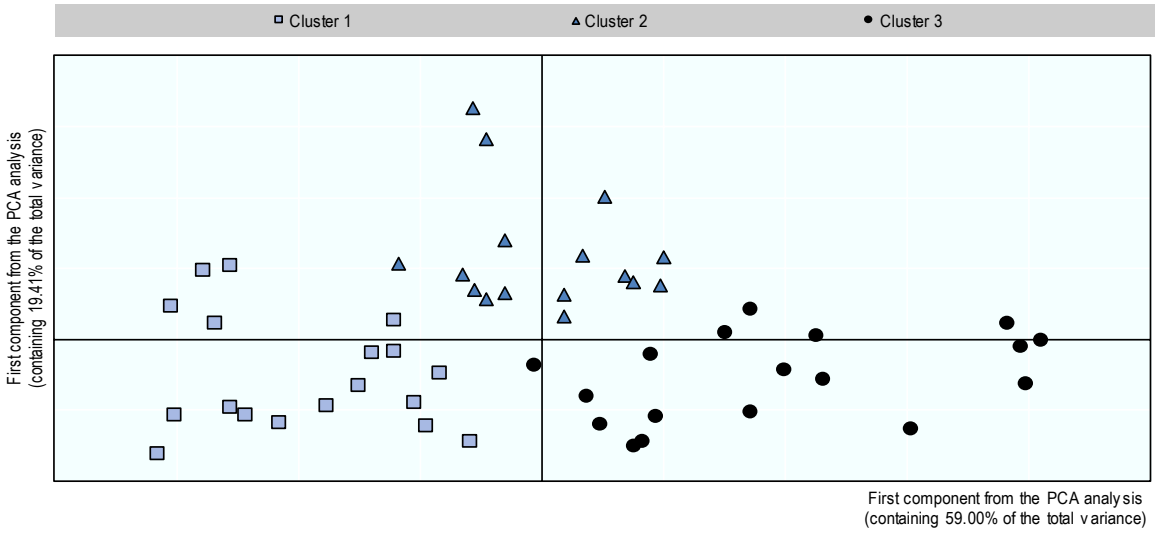
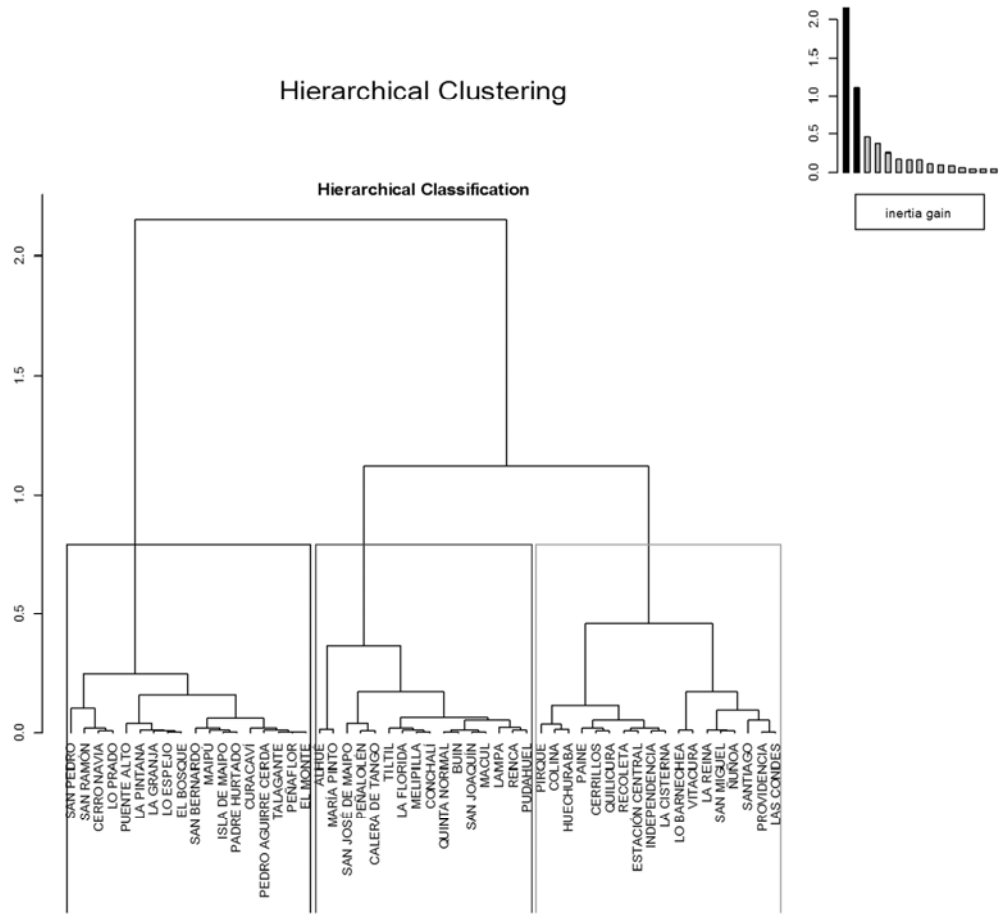


Figure 3.19. **Clusters of municipalities of the Metropolitan Region of Santiago based on municipal resources**



Source: OECD elaborations based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Affluence vs. dependence

The first line of differentiation explains around 60% of the variance. In a regional context where there are no tiny municipalities, contrary to what is observed at the national level, it is not a size effect which emerges. This axe is constructed by opposing on the one hand, revenue obtained from the FCM and, on the other, the conjunction of revenues linked to the social and economic wealth of the municipalities: high amounts per inhabitant of the territorial tax, business licenses, traffic permit, cleaning rights. Two distinct clusters of municipalities clearly emerge:

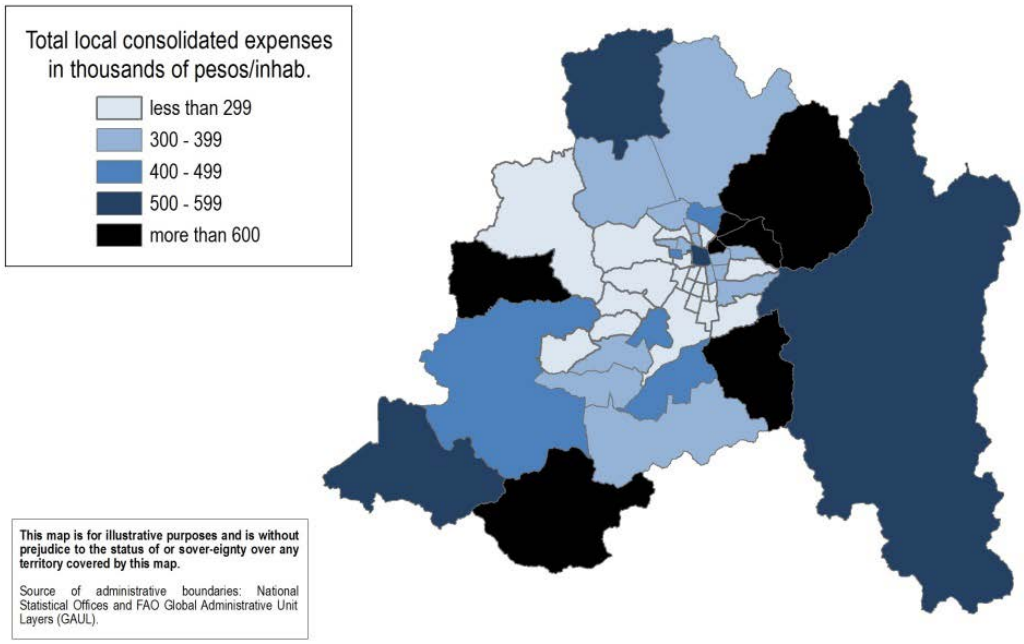
- A first cluster of municipalities with sufficient capacity to guarantee a certain level of financial autonomy. Represented in this group are the wealthy municipalities of the heart of the Metropolitan Region: obviously, the big four contributors to the FCM as well as Lo Barnechea. They enjoy a high amount of tax revenues (relative to Chilean standards) and a low poverty rate (below 5%). Inside this cluster, a secondary differentiation appears according to the level of the values of the variables and their respective weights. Comparatively to the other municipalities in the Metropolitan region, they appear relatively well funded (Cerillos, Ñuñoa, Independencia, Huechuraba, San Miguel, etc.).
- The second clearly identifiable group comprises municipalities, which are heavily dependent on external resources. As they receive very small amounts of taxes per capita, they are mainly funded by the FCM. The latter represents for many of them more than 50% of their total resources, and even more than 60% (La Granja, El Bosque, Espejo, Puente Alto, La Pintana). For most of them, poverty rates are high (15-20%). These disadvantaged municipalities are located in the outlying territories of the region (San José de Maipo, San Pedro, Melipilla, Maria Pinto, Curacavi, Tiltil) or in the heart of the Santiago agglomeration, in the south (Puente Alto, La Pintana, El Bosque), forming the poor and popular horn of the city in deep contrast with the wealthy municipalities located in the north.

Diversity and intermediary position

The second line of differentiation (19% of the variance) is built around revenues from current transfers. The municipalities that contribute heavily to this category have high levels of expenditure per capita, even higher than in Santiago. These municipalities have a diverse basket of revenues, primarily based on the territorial tax (Calera de Tango) or on the business license (Lampa) or both (Quilicura). The composition of this group is not as clear as the two others. It is the intermediary group, located in the inner periphery (Figure 3.20).

To conclude, the first line of differentiation, based on municipal revenues, is the decisive factor which explains the structure of the metropolitan region between dependent and disadvantaged municipalities and more favoured ones. The governance of the metropolitan region, which appears to be both fragmented and structured around these clusters, is one of the main technical, financial and political challenges of the future. It will be crucial to find the adequate institutional arrangements that will foster the sustainable development of the metropolis based on more solidarity and inclusiveness.

Figure 3.20. **Local expenditure of all three sectors per capita in the Metropolitan Region of Santiago (2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Conclusion

An analysis of the inter-municipal budgetary disparities sheds light on the original situations and raises different questions regarding the organisation and functioning of the Chilean municipal system.

The importance of ministerial grants to finance education and health budgets reveals the logic of deconcentration that is prevalent in Chile. The municipalities are, therefore, in a situation of dependence combined with financial insufficiency. Unlike true deconcentration, which should be neutral for municipalities' budgets, municipalities must participate in the funding of services. A simple indication of this contribution resides in the fact that personnel expenditure needs exceed the ministerial subsidy. This imbalance is present for nearly all municipalities and sometimes in considerable proportions. It is more marked for education and has continued to worsen over recent years. The deterioration of this ratio is an indicator of an alarming evolution for municipal finances and yet an opportunity to reconsider the system. Regardless of the method chosen, it implies the need to increase the financial contribution from the central government.

Despite the tremendous diversity of situations, the analysis of disparities helps identify a common dimension to all territories. In the case of Chile, this common dimension is singularly marked: the geographic concentration of economic activity and the population results in sharp budgetary contrasts. The Chilean financial system, legally uniform, is based in reality on the coexistence of differentiated financial regimes. This multiple reality cannot be ignored in the design, creation and implementation of measures aimed at modernising the system. To be useful and effective, they must be adapted to the economic realities and capacities of the local administration.

The diversity and the accumulation of budgetary disparities are the symptoms of a system that could potentially create serious inequalities. Sectoral transfers from the central government point to the existence of a mechanism correcting municipal handicaps.

The transition from the observation of inequalities to the judgment of the system's inequity requires a more in-depth analysis. Inequalities may in fact have several origins which, in a system of political decentralisation, are not all inequitable. They are often the result of situations that are imposed on the municipalities (geographical constraints, social characteristics, for example). They can sometimes derive from the management choices of local elected representatives (preference for collective services that increase expenditure, choices regarding taxation, etc.). The search for territorial equity aims to reduce the only inequalities that are really inequitable. This requires adequate assessments of inequalities among municipalities.

The FCM and the treatment of inter-municipal disparities

Introduction

The Municipal Common Fund (*Fondo Común Municipal* – FCM) is an equalisation tool aimed at reducing inter-municipal disparities. Created in 1979, it has been continuously criticised, in particular regarding the effectiveness of its redistributive functions as well as several potentially counter-productive effects. Its mechanisms have been modified several times however without fundamentally altering its basic approach. The FCM has three main characteristics:

1. The FCM is a mechanism founded on the idea of a horizontal redistribution of resources. Where numerous countries fund their inter-municipal financial equalisation mechanism by vertical transfer of resources allocated from the central government budget to subnational governments (Box 3.2), the FCM operates in what is nearly a closed circuit. Its resources come from automatic contributions from municipalities via the transfer of a portion of their tax receipts. The FCM's uses are comprised of contributions to municipalities calculated based on a mechanism that accounts for each municipality's specific situation. Explicitly, the mechanism takes into account the weakness of municipal resources but implicitly, it considers special needs (relative poverty intensity and lump sum allocation). The FCM thus subscribes to the notion of horizontal equalisation as opposed to vertical equalisation, which entails a grant from the central budget. All municipalities contribute to the fund in varying amounts and, simultaneously, all municipalities receive money from the fund. A municipality's "yield" on this redistributive mechanism is measured by the size of the positive/negative balance between contributions and allocations. Municipalities are net contributors when contributions are higher than the allocations they receive or are net receivers when allocations outweigh contributions.[12] This original mechanism is also the subject of questions about its effects on the broader system.

2. The FCM is the leading resource for municipalities as a whole. The FCM is a fiscally-important resource mobilising nearly CLP 1 100 billion in 2015. The FCM accounts for 29% of total municipal sector revenue and over 42% of their permanent own resources. Between 2010 and 2015, in nominal value, the volume of the FCM increased nearly 70%. Its share in total municipal sector revenue fell, however, from 30.4% to 29%, as non-tax revenues rose faster (particularly "Other

transfers"). However, as a percentage of permanent own resources it increased by 1 point. Therefore, the FCM redistributes revenue on a massive scale. Taking account of this redistributive dimension, this overall ratio does not accurately reflect the essential role played by the FCM in the budgets of its biggest receivers and contributors. The tensions related to the financial stakes of the FCM are focused on the perception of individual municipalities regarding the size of payments made into the system and the financial dependence on contributions for the beneficiaries of the redistribution.

3. The FCM is a politically and economically contested mechanism. The biggest net contributors point to the predatory nature of the tax, which targets a few municipalities that have been labelled "rich". However, above and beyond these opinions on the FCM's impact on individual budgets, the overall logic of the mechanism is being called into question. The critics have several complaints: the complexity and lack of transparency of the allocation algorithm; outdated and fundamentally incompatible with the precepts of territorial equity; the counterproductive effects (fundamentally disincentivising and encouraging "fiscal laziness"); the approximate measures of its actual redistributive "yield" and its contribution to reducing deep inter-territorial inequalities.

Box 3.2. **Overview of fiscal equalisation systems in OECD countries**

Equalisation mechanisms are extensively used in OECD countries, introducing either vertical transfers (from the central government to financially weak subnational governments) or horizontal transfers (from wealthy jurisdictions to the poorer ones). Not only federal countries but also unitary countries have put in place equalisation procedures as a key part of their fiscal policy. Across the OECD, fiscal equalisation transfers average around 2.5% of gross domestic product (GDP), 5% of general government spending and 50% of intergovernmental grants.

The differences in per capita GDP across jurisdictions results in unequal tax-raising capacities and, thus, differences in public service provision. In addition, the cost of public services is another factor that leads to unequal public service provision: special groups such as children, the elderly, the disabled, etc. will raise the cost of public services and the geographical factors (mountains, islands, isolated or low density areas, etc.) will also have an impact on the cost per service unit.

Equalisation arrangements can hence be broken down into revenue versus cost/charges equalisation. While the former equalisation aims mainly to reduce differences in tax-raising capacity, the latter reduces the cost of providing public services. Most OECD countries apply various equalisation arrangements, although the combination of vertical and cost equalisation tends to be prevalent.

Across OECD countries, equalisation has a strong redistributive effect: on average it reduces pre-equalisation disparities by more than two-thirds and, in some countries – such as Australia, Germany and Sweden – revenue-raising disparities are virtually eliminated. Equalisation mechanisms should be tailor-made for each country. Fiscal equalisation depends on a set of institutional factors such as size and number of subnational governments, their geographical distribution, spending assignments and fiscal resources allocated to each jurisdiction, among others.

Although equalisation is now recognised as a necessity in a growing number of countries (and in certain countries such as Germany, Italy, Spain and France where it has constitutional force), it is often the subject of technical and political debate, and is often contested.

Box 3.2. **Overview of fiscal equalisation systems in OECD countries** *(continued)*

This is particularly true for horizontal equalisation, which limits local autonomy. Rules and criteria are constantly being adjusted. Debates have taken on greater importance with the crisis and as territorial inequalities deepen. Many reforms have been implemented recently or are on-going in the OECD including a component aimed at improving equalisation mechanisms.

In France, the main general purpose grant (*Dotation Globale de Fonctionnement* - DGF) for municipalities and inter-municipal co-operation bodies is being reformed. The goals of the DGF reform include greater simplicity, transparency and equity and to adapt the DGF to the territorial reform. In fact, the DGF's architecture comprises a great number of components and distribution criteria based on charges, resources or specific constraints, which make it particularly complex and opaque. Its redistributive function could also be improved given the marked disparities between municipalities in per capita DGF that are not justified by objective resources/charges criteria. Finally, the reform aims at encouraging pooling of services. This reform is also a chance to assess and revise other existing equalisation mechanisms, with the aim to make the whole system more coherent and to increase horizontal equalisation. In 2015, the vertical equalisation tools represented almost 80% of the amounts devoted to equalisation. Horizontal equalisation was introduced recently by the 2010 local finance reform, which established new fund mechanisms: the equalisation fund for inter-municipal and municipal resources (or FPIC), which is the most horizontal instrument (it aims at redistributing 2% of tax revenues in 2016), the departmental fund of equalisation of revenue from the transfer tax on property transactions (*droits de mutations*) and the Equalisation funds of the revenue from tax on businesses' added value (CVAE) for the departments and regions.

In Sweden, a new audit of the equalisation system – already revised in 2005 – has been entrusted to a parliamentary committee in 2008 to find out if there were any growth-deterring factors linked to the equalisation system. The review led to several measures adopted in 2012 and 2014 which finally benefited the subnational governments with the highest revenues (reform of the equalisation rate on tax resources and of the cost equalisation grant to simplify the evaluation of cost disparities and increase transparency). Since 2015, new measures are on-going to correct this situation.

Source: OECD (2017), *Multi-level Governance Reforms: Overview of OECD Country Experiences*; OECD (2016c), *Territorial Review of Peru*; OECD (2013), *Fiscal Federalism 2014: Making Decentralisation Work*.

The financial importance of the mechanism, its strategic role and the political and technical debates that it creates, place the FCM at the heart of issues related to the modernisation and cohesion of the Chilean municipal system. The FCM is a mechanism that strives to meet the challenges posed by the territorial inequalities inherent in the fragmentation of the political-administrative landscape. Its response to these challenges is rooted in a specific economic reasoning that restricts the technical mechanisms of the fund. In addition to this evaluation of the intrinsic characteristics of the mechanism, its qualities must be assessed in light of the goal pursued by the redistribution of resources, namely the reduction of their unequal distribution between municipalities.

FCM's redistribution approach

Different avenues could be explored to address the question of inter-territorial inequalities. Financial equalisation, combined with other institutional arrangements, is the preferred angle of attack in countries with a multi-level political-administrative organisation. On these economic foundations, Chile has built a unique technical

mechanism that seems to address several concerns about how public policies address the inequalities – in terms of both wealth and social needs – between municipalities.

The FCM's founding economic principles

The FCM is part of a family of resource transfers (in the economic sense, of horizontal redistribution, i.e. between municipalities, and not in the legal sense) that aims to respond to inequalities inherent in the incongruence between local revenue environments and the expenses incurred by meeting social needs. Other methods, disjointed from the transfer of resources or associated with it, are likely to ensure the compatibility between municipal decision-making autonomy and the reduction of inequalities that decentralisation can exacerbate.

Political decentralisation: Revealing inter-territorial financial inequalities

Fragmentation of the political-administrative fabric is indicative of the inequalities in the spatial distribution of economic activities and people. Economic activity, mirroring the country's geography, tends to be concentrated in particular areas with comparative advantages. This density facilitates exchange opportunities and these areas benefit from proximity, accessibility and economically-useful resources. There are many factors that render them attractive places to live and work; they benefit from agglomeration effects, and opportunities to improve one's lot in life, both socially and economically. This concentration of economic activities and population, in its continuity and discontinuity, is fragmented by administrative borders that underscore the extent of inequalities in the economic and social composition of political-administrative entities. In certain cases, a municipality with high tax revenue and wealthy inhabitants will be located just next door to a municipality with low tax revenue and relatively poor inhabitants. Between these two extremes, all combinations are possible and have various characteristics: urban/rural; mountain/plain; city in the centre of an agglomeration/suburban municipalities; industrial enclaves/bedroom communities; growing municipalities/municipalities in decline; wealthy residential municipalities/low-income municipalities.

Depending on the nature of the resources allocated to the municipalities and the range of competences they are empowered with, the imbalance between resources and needs will be more or less substantial. For instance, when the municipality's taxation is based on economic activities and its tax base is dynamic, the gap is wider due to the high spatial concentration of companies. When local policies are financed by resources that are distributed universally across the territory (e.g. land values), the imbalance will be less marked. Although the differences in tax wealth are real, they are not as strong as differences resulting from the contribution of economic activities.

Structurally, ramping up decentralisation is liable to exacerbate the differences and trigger a divergence spiral where the gaps widen. Decentralisation provides groups of people in a given area with the increased possibility of expressing – through their duly-elected officials – their preferences in terms of collective services and tax contributions. The variety of choices available translates into a wide range of situations whose comparison reveals inequalities in expenditure levels (often quickly equated with level of service) and/or tax contributions. It is impossible to conclude that these observed inequalities are unfair. To draw such a conclusion, it would be necessary to refer to a territorial equity criterion.

Resource equalisation: One way to reconcile decentralisation and absorb inter-municipal inequalities

Political decentralisation's inegalitarian tendency can disrupt the principles of equality and social cohesion on which developed societies are founded. The tensions that are liable to spill over from this disruption can threaten the advantages associated with decentralisation, namely an improved allocation of resources and efficiency. To reconcile the principles of decision-making autonomy and equality a range of institutional solutions should be considered. They are all facets of solidarity, which is the principle that reconciles freedom and equality. Three institutional arrangements can be distinguished:

- The transfer of responsibilities or even reallocation of a tax to an entity higher up in the hierarchy (then redistributing its receipts to the municipalities) that will homogenise the offer of local goods and its means of finance across a wider geographic scope. Paradoxically, "good" decentralisation in this case would take a centralising detour. The situation could arise whereby the public asset in question provides geographically-broader externalities due, for instance, to the spatial mobility of the beneficiaries of the collective service or the possibility of spatial translation of the budget charge of the tax.
- Inter-municipal co-operation which enlarges, locally, the scope of solidarity and municipal policies. For instance, competences could be bestowed on an ad hoc structure that would cover a geographic territory that is more relevant economically. This structure would be in charge of ensuring that the competences are funded in accordance with the principle of solidarity. Motivated just as much by allocation effectiveness and management efficiency as equity objectives, this type of co-operation could result in the fusion of the municipalities involved.
- Financial transfers that foster equalisation try to compensate for the negative effects of the territorial structures causing the inequalities in the first place, but leave them intact. The redistribution intends to correct the inequalities of the primary disbursement of resources and make a secondary disbursement less unequal. Unlike the grants mentioned in the preceding paragraph, its implementation is directly inspired by equity considerations. Its impact on equalisation is just as important in terms of allocation of resources and effectiveness.

These three institutional arrangements are not mutually exclusive and can be used together in a combined strategy. Although the FCM is clearly part of the third category, with regard to both effectiveness and equity, the formulation of co-operative strategies is an avenue that could be explored, in Chile as in a number of other countries, to address the question of the organisation of the metropolitan areas. The expansion of cities and their sprawl provide myriad opportunities for local public assets and local taxation to also spill over geographic borders. Urban areas continue to encompass more political-administrative units whose policy organisation must be horizontally co-ordinated to ensure optimal resource allocation. Resource mobilisation, while ensuring solidarity, is a vector of effectiveness. It is also, even though it may not be the primary objective, an opportunity to address locally and within a defined space, questions of territorial inequalities. This territorialised contribution to equality eases and completes the action of equalisation mechanisms with a national scope.

The FCM's mission is unequivocal: correct the inter-municipal inequalities and provide additional resources to municipalities with the lowest tax revenues so they can fulfil their basic competences. Although the FCM is the most important and biggest

instrument of this correction, other transfers from the central government also contribute, in other ways, to serving this priority. The specific grants allocated to the education and healthcare sectors are based on allocation criteria that address equality concerns. Specific subsidies can also benefit, in a more discretionary way, municipalities deemed to be disadvantaged or slower to develop. In conclusion, the overall equalisation effort is not limited simply to the FCM. The conclusions that could be drawn from analysing solely the FCM would fail to shed light on the impact of other transfers.

Technical aspects of the FCM

Since its creation in 1979, the FCM has continued to uphold the principles of solidarity as it executes its mission of redistributing income. The fund's resources emanate directly from tax receipts allocated to the municipalities, a portion of which is given back to them. The money in the fund, which comes from the municipal tax haul, is allocated to the municipalities after applying a formula that is set in advance, shared among all municipalities and long-standing. In addition, a small amount is provided by a fiscal grant from the central government: the mechanism works like a closed circuit. Because these block contributions to the fund can be allocated freely, the FCM is analogous to an overarching subsidy that is paid in full in one instalment. It fluctuates in lock step with the return on redistributed tax receipts.

Though this founding philosophy has not changed but in its expression, both in terms of resources going into the fund and payment mechanisms in favour of the municipalities, the operating rules have evolved.

Rules for funding the FCM: The concentration of a broader tax base

Since its latest reform (2007-2009), the FCM has been funded via a variable percentage of a series of taxes (Table 3.2) plus a fiscal contribution from the state (set annually at 218 000 UTM). Since 1979, the original mechanisms – based on the payment by each municipality of 50% of the participation in the territorial tax – have been modified incrementally in four ways:

- Broadening of the scope of taxes involved in the transfers to the FCM.
- Increase in the quotas of the tax revenues transferred.
- Municipal contributions have been differentiated, the wealthiest municipalities contribute more.
- Municipal tax contributions are now topped up by annual fiscal assistance from the state (permanent or temporary).

Table 3.2. **Revenue sources of the FCM**

Revenue source	Quota	Contributors
Territorial tax	65% 60%	Municipalities of Santiago, Providencia, Las Condes, Vitacura All other municipalities (341)
Municipal business licenses	65% 55%	Municipalities of Providencia, Las Condes, Vitacura Municipality of Santiago
Vehicle registration tax	62.5%	All 345 municipalities
Tax on vehicle transfer	50%	Taxpayers (who sell a vehicle)
Revenue from fines (infractions)	50%	Offenders to the Traffic Law
Fiscal contribution	218.000 UTM	State

Source: OECD elaboration based on information provided by SUBDERE.

FCM allocation rules: The redeployment of implicit missions

At present, the calculation of individual municipal allocations from the FCM is based on an algorithm that covers 100% of its resources. The Fund now integrates a stabilisation mechanism the purpose of which is to absorb the shocks suffered by municipalities when contribution criteria are changed. The criteria-based breakdown combines four different items that have different weights. Several proxy variables are used to evaluate the level of disparities within each item:

- 10% of the FCM fund is allocated depending on the relative poverty of the municipality measured by the poverty rate.
- 25% equal across all municipalities.
- 30% depending on the number of properties exempted from the territorial tax.
- 35% depending on the weakness per capita of revenue from permanent own tax.

Easter Island *(Isla de Pascua*) is handled differently.[13]

Redistribution effectiveness of the FCM

At first take, the redistributive performance of the FCM can be estimated by the changes in resources that are paid into it as well as the growth rate differential (especially for comparisons over a long period of time) in the FCM's favour compared with other resources. To evaluate whether the FCM is reaching its equalisation goal it is best not to take a volume perspective. What is the effectiveness of the FCM in terms of reducing inequalities between municipalities (Box 3.3)?

A dynamic approach is useful to identify convergent factors that would provide clarity regarding this complex question (especially to quantify the intensity of the phenomenon and its effects). Four characteristics emerge and are detailed below.

Box 3.3. **How to evaluate the effectiveness of an equalisation system?**

Identifying the reduction of inter-municipal inequalities and – by extension – the equalising power of the FCM requires the use of the right indicators. Their evaluation across time helps to evaluate the corrective trend underway. This methodological detour is inspired by contributions by A.B. Atkinson (1970) and D.G. Champernowne (1974) and builds on the empirical work in France of G. Gilbert and A. Guengant (2004) dedicated to the evaluation of the equalisation effects of state aid to local authorities.

The challenge of the evaluation

The evaluation of equalisation mechanisms' ability to correct inter-municipal inequalities is a difficult task from an institutional and methodological standpoint. The approach would estimate the corrective ability of transfers' buying power of local resources by measuring, before and after the transfer, the value of a synthetic equalisation index. The percentage of reduction in the value of the index expresses the corrective power of the transfer(s). When evaluating mechanisms' corrective capacities the choice of indicator is important. All transfers are involved, including those that do not have a clear equalisation function. The overall measure of the corrective power is broken down to assign to each component of the mechanism and its contribution to the fluctuation (up and/or down) of the value of the equality index.

Box 3.3. **How to evaluate the effectiveness of an equalisation system?** *(continued)*

Characteristics of a successful statistical indicator of inequalities

- Easy to obtain and calculate data
- Indifference regarding individuals
- Independence regarding the number of total individuals
- Independence regarding an equiproportional modification of each value
- All the values of the indices must be between 0 and 1
- Capacity for an index to illustrate, among other things, a specific aspect of inequality (proportion of very poor or very rich or average)

The variety of inequality indicators:

- Gini coefficient
- Relative divergence from mean
- Variation coefficient
- Relative divergence logarithms
- Champernowne 1 index (geometric vs. arithmetic mean)
- Champernowne 2 index (geometric vs. harmonic mean)
- Entropy index of Theil

Sources: Atkinson A.B. (1970), "On the Measurement of Inequality", *Journal of Economic Theory*, Vol. 2, pp. 244-263; Champernowne, D.G. (1974), "A Comparison of Measures of Inequality of Income Distribution", *The Economic Journal*, Vol. 336, pp. 787-816; Gilbert G. and A. Guengant (2004), *Evaluation des effets péréquateurs des concours de l'Etat aux collectivités locales*, Commissariat général du plan, Paris.

The sustained growth of the resources of the FCM

A long dynamic period increasing FCM resources

Over a long period (1990-2015), many indicators point to an increase in the FCM.

- In real terms, the FCM rose from CLP 173 billion in 1990 to nearly CLP 1 100 billion in 2015. With a multiplying factor of 6.3, the real progression rate is almost 530%. Growth was faster during the 1990-2000 period (2.4 as multiplying factor) than in the following 2000 decade (1.9). It has stabilised at a high level of progression between 2005 and 2015 (1.9).
- As a share of municipal own tax revenues, the FCM has grown regularly: 60% in 1990, 70% in 2010 and 73% in 2015.
- As a share of permanent own revenues (own taxes + FCM), FCM rose from 38% in 1990 to 42% in 2015.
- There was, however one exception: as a share of municipal sector total revenues, FCM has slightly decreased from 31% to 29%. This is explained by the sustained

increase in transfers (notably current transfers).The dynamic of the total resource to redistribute does not depend, like in many vertical equalisation mechanisms, on indexing the amount transferred to the fluctuation of a macroeconomic indicator (GDP growth, inflation) or the fluctuation in state receipts. The expansion of the resource to be shared is linked to the growth of the revenue municipalities are able to levy through taxes. The intensity of solidarity-based redistribution is conditioned on growth in municipal taxation.

The random progression of the FCM

Over this period of growth (1990-2015), the pace of inter-annual growth was anything but steady. For example, during the 2000s the inter-annual rates fluctuated between high and low levels: 10% growth in 2001 and 2002 was followed by a drop to 2% in 2004 and 2005, before robust expansion returned in 2009.

Hence, these variations, partially linked to the changes in economic activity, complicate the recurrent funding of the municipal budgets. In a restrictive context, the presence of a stabilisation mechanism (*mecanismo de estabilización),* created in 2007*,* aimed to cushion the local impact of the negative variation of the FCM contribution, thus reducing its redistributive capacity.

This way of funding an equalisation mechanism shields it from potential breaches in the "contract" that the central government would impose (by stiffening or suspending indexing conditions) on municipalities in the name of macroeconomic imperatives in tightening their budget. This assurance against political moral hazard shifts the risk of resource fluctuation by subjecting it to the resulting aggregate tax windfall of municipalities. The fund's resources will increase alongside the rising municipal tax haul that pumps money into them. This growth depends on two factors:

- The increase in the tax bases, which, itself, is subject to economic ups and downs and conditioned on, in a more structural way, the intrinsic quality of tax bases in terms of elasticity to revenue.
- The municipal prerogatives regarding the tax scale. Although leeway in setting the rate is minimal in Chile, in certain cases elected officials are in charge of setting the tax exemption threshold. They can also intervene in monitoring exemption thresholds and influence property revaluations (Bravo, 2014). A technical method for avoiding this influence of municipal decisions on the level of its tax wealth would be to take into account gross tax bases. If, in the future, local elected representatives had more fiscal power, this risk of strategic behaviour in the determination of tax receipts to be redistributed between municipalities should not be neglected.

The extension and the concentration of FCM contributions

From the initial, 1979 version to the current one, the step-by-step expansion of the basis of contributions to the FCM derives from two contrasting lines of growth: extensive and intensive.

An extension of the scope of shared taxes

The extensive line concerns the scope and the quota of shared revenues, from unicity to diversity. The first sharing formula was simple: all the municipalities had to contribute to the FCM half of the territorial taxed recovered on their territory. However, as the formula is determined for three years, it is possible to regularly review the FCM's

mechanisms. Therefore, throughout successive reforms, the FCM's basis has broadened to gradually integrate new resources:

- 1984: inclusion of the vehicle registration tax (*permiso de circulación*) with a proportion of 50% increased to 62.5% in 2000; increase of the transferred portion of the territorial tax; integration of the business licenses of municipalities with highest revenues.
- 1995: integration of the revenues from the tax on vehicle transfer.
- 2002: integration of some revenues from fines.

In parallel, in 1984, the central government started to contribute directly to the Fund (218 000 UTM). In 2005, the municipalities of Providencia, Las Condes and Vitacura had to pay an additional budgetary contribution (70 000 UTM).[14]

As a result, while the FCM was entirely composed of the territorial tax when it was established, it is now made up of a diversified basket of resources. However, three taxes provide more than 93% of total resources: the territorial tax (53%), the vehicle registration tax (23%) and the municipal business license (13%).

A concentration of the scope of contributing municipalities

Initially, the FCM mechanism was operating without any discriminatory formula regarding the way resources were collected: the participation rate applied to the territorial tax was unique and identical for all municipalities (50% of tax revenues). In fact, the discrimination was made only on the "redistribution side", i.e. the ways in which funds were reallocated between municipalities. Some municipalities were officially excluded from benefiting from the FCM (Las Condes, Providencia, Machali, Santiago and Viña del Mar). Later, it was decided to strengthen the solidarity system by imposing new contribution rules on the four municipalities of the Metropolitan region of Santiago that are considered to be the wealthiest: Las Condes, Santiago, Providencia and Vitacura:

- The quota of the territorial tax, which is transferred to the FCM, is greater than that of all other municipalities (65% instead of 60%).
- In addition, and above all, these four municipalities are the only ones contributing part of their municipal business license (55% for Santiago and 65% for the three others).

This funding model leads to two notable financial situations:

- Reflecting the concentration of the taxable basis within the Metropolitan region of Santiago, its municipalities contribute more than two thirds of FCM funds (67.2% in 2015 with a quasi-constant percentage since 2010). Alone, the four major contributors account for almost 45% of the FCM (20% for Las Condes, 9-10% for Santiago and Providencia, over 5% for Vitacura). With such a weight in the funding of the FCM, it is not surprising that these four municipalities are major "net contributors" to the FCM ("payment to" vs. "revenue from"). In 2015, they were at the top of the ranking. They were followed by 10 other net contributors from the Metropolitan region, having a contribution rate ranging from 3% to 35% (La Reina, Pirque y Zapallar).
- In terms of reduction of per capita tax revenue inequalities, the results are contrasted. Looking at all Chilean municipalities, it appears that there is no change in terms of dispersion or concentration indicators (variation coefficient or

Gini coefficient). This is due to the fact that, apart from "business licenses", the inter-municipal differences in FCM repayment rates are either too low (territorial tax) or non-existent. They do not significantly alter the dispersion of resources per capita within all municipalities. Thus, globally, the value of the dispersion indicators is almost identical.[15] Despite this apparent stability, some changes appear in the ranking of the revenue per inhabitant of the business licenses. The position of the four exclusive contributors is lower.[16]

On the scale of the Metropolitan Region of Santiago, the perception is quite different, especially for the distribution of the business licenses. The drop of dispersion of the per capita amount is 35%. The concentration of the contribution leads to major changes in the position of the four contributors within the group of 52 municipalities. For example, for some municipalities, revenues from their municipal business licenses noticeably exceed those of Santiago.

This specific situation illustrates the political and financial inspiration of the FCM funding model. The goal of the FCM is not so much to achieve territorial equity (fairness) – through raising resources from all potential contributors on the basis of per capita wealth, possibly by applying a progressive scale – as it is to work towards inter-municipal solidarity by raising resources from a "concentrated source" of contributors.

At present, the FCM combines two main characteristics:

- An extended basis of resources (but not all local taxes and with differentiated rates of contribution).
- A narrow basis of contributors, concentrated in a few rich municipalities that must contribute a large share of their own resources.

This dualist configuration has led observers to consider future reforms that would promote renewed equalisation mechanisms based on more solidarity, inclusiveness and territorial equity.

Strengthening support to vulnerable municipalities

The changes introduced by the last FCM reform implemented in 2008 (Law No. 20.237 published on 24 December 2007) have benefited vulnerable municipalities the most, and extended the list of eligible municipalities to FCM transfers.

The removal of the incentive component of the FCM

Before the 2008 reform, 90% of the FCM was distributed to the municipalities according to usual criteria of needs and resources. The remaining 10% was reserved, in equal parts, to emergency and an incentive subsidy related to municipal management performance. With the reform, this second component has been reintegrated into the general disbursement while a specific incentive mechanism has been established in the form of a grant managed by SUBDERE (*Fondo de Incentivo al Mejoramineto de la Gestión Municipal*, FIGEM).

The consolidation of the FCM's architecture

The architecture of the fund is implicitly based on the two main sources of municipal inequality, i.e. disparities in terms of charges (needs) and in terms of resources. The first category is based on the two variables of "poverty" and "equal distribution" (see above), thus accounting for 35% of FCM funds. Disparities in terms of resources are calculated based on the level of "compensation of exempted properties" and the "weakness of per

capita permanent own revenue", accounting for the other 65% of FCM allocations. This architecture implicitly means that in Chile, it is considered that 35% of inter-municipal inequalities derive from greater needs (e.g. because of higher costs for a given service) and 65% from limited resources (e.g. due to weaker per capita tax bases).

The orientation of the algorithm and criteria to vulnerable municipalities

Analysing the algorithm and the criteria of attribution of the drawing rights, it clearly appears that the first objective is to support the most vulnerable municipalities, especially the smallest. It explains the growing share from 10 to 30% of the "equal treatment" component. A lump-sum attribution by entity is substituted by a lump-sum resource by inhabitant. Each municipality obtains 0.289% (100/345) of the resource dedicated to "equal treatment". Ollague (313 inhabitants) and Puente Alto (610 188 inhabitants) receive the same amount.

Elsewhere, the component "territorial tax exemptions" uses the number of properties as an attribution criterion and not the value of the properties. The former indicator is more favourable to the small and rural municipalities than the second (see Chapter 2, the territorial tax).

More indirectly, the "weakness of revenues" component confirms this orientation, as the eligibility criterion for benefiting from a "floating population" bonus is a function of the share (greater than the national average level) of the exempted properties. It is another way of identifying vulnerable municipalities.

The ambiguous impact of an operating redistribution

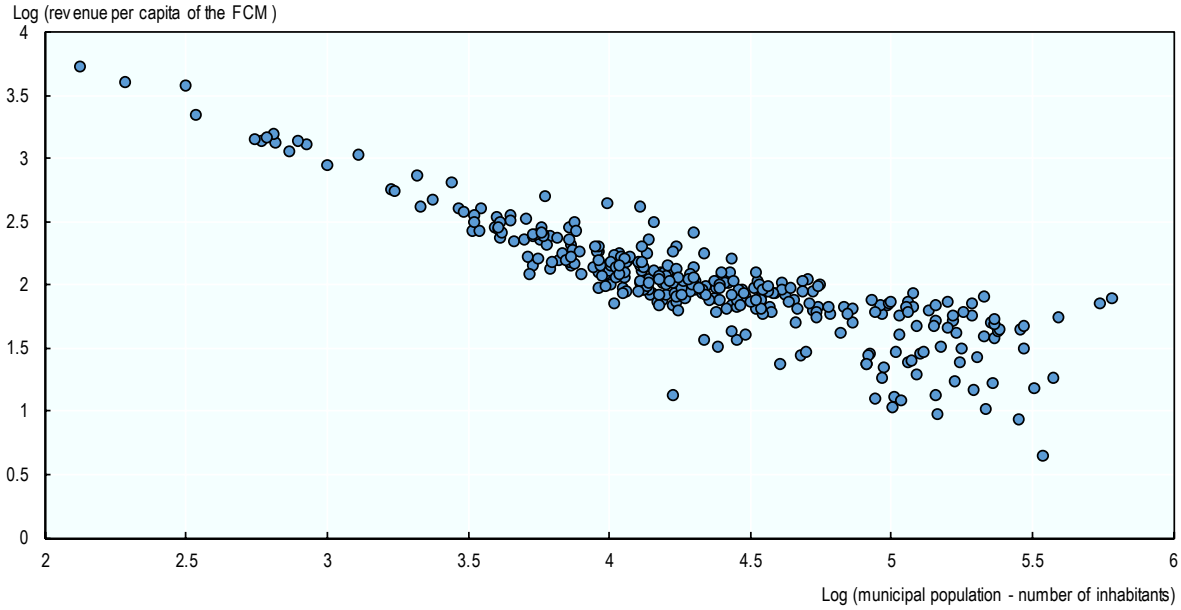
In light of the FCM's policy objectives, various studies agreed on the efficiency (or effectiveness) of equalisation provided by this horizontal redistribution. However, some question marks emerge from the evaluations.

The effectiveness of the contribution of the FCM

Various specific evaluations point to the FCM's effectiveness:

- The correlation coefficient between the FCM amount per inhabitant and the population (both log evaluated) is inverse and strong: -0.875. There is a slight but identical correlation when density is used (-0.732). It means that the amount of FCM per inhabitant is proportionally inverse to the size or density of the municipality. The smaller or less densely populated the municipality the higher the per capita amount it receives. Figure 3.21 illustrates the relation.

Figure 3.21 **Relation between revenue per capita of the FCM and population (2015) (log-log scale)**

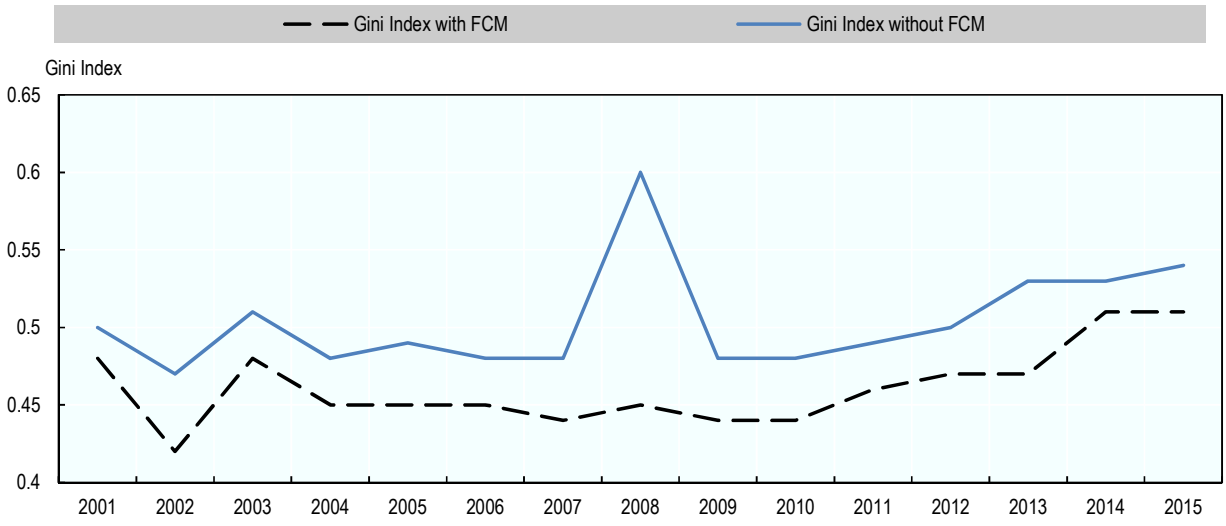


Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

Different estimates were given for the reduction of the inter-municipal inequalities attributable to the FCM. Indeed, J. Bravo (2014)[17] compared the distribution per decile of permanent own resources (excluding the FCM) then adding the impact of the FCM. He observed that the gap between 1 and 20 (between the 1st and the last decile) is reduced to 1 and 4 after FCM transfers (incoming)-allocations (outgoing). The evaluations of the way in which they work illustrate the amplitude of the resource shift caused by the FCM.

The study of Cortés Y. and Paredes D. (2016), coming from another perspective and using a different methodological approach, confirmed the redistributive character of the FCM. Throughout the period studied (2001-2015), the value of the Gini coefficient of the inter-municipal distribution of the resources is systematically lower when the FCM is integrated (Figure 3.22). From year to year, comparing the two values, the reduction of the value of the Gini coefficient is between 5 and 10%. Paradoxically, even with the FCM, since 2009, inter-municipal disparities have been growing. The FCM has limited - but failed to close - the gap (the value of the coefficient hasn't decreased).

Figure 3.22. **Change in municipal revenue inequalities (2001-2015)**



Source: Cortés Y., Paredes D. (2016), "El Fondo común municipal: ¿Cuál es su rol en ma convergencia de ingresos locales ?", *Latin American Research Review*, Vol. 51/3, pp. 161-180 - based on SINIM data (www.sinim.gov.cl/).

In 2015, the positive balances (transfers – allocation) were, for certain municipalities, extremely high multiples of the FCM contributions. For instance, the "FCM contributions/contributions to the FCM" ratio reached 437 for Easter Island, an outlier, 290 for Timaukel, 242 for Camiña, 201 for Cabo Hornos, etc. On the other end of the spectrum, of the 15 municipalities that are net contributors, the ratio transfers/allocations was a mere 0.04 for the four "over-taxed" municipalities, Lo Barnechea followed with a ratio of 0.16 then a group of municipalities around 0.35 (La Reina, Pirque, Zapallar), etc. In the sub-category of regional capitals, the positions are also contrasted between Coihaique and Arica whose ratios are around 8 to 10 and Antofagasta and Iquique whose ratios are slightly above 1.

The limits of the contribution of the FCM

Several limitations of the FCM concerning its underlying principles and *modus operandi* can be identified.

There are some methodological shortcuts. In fact, the lack of indicators pertaining to wealth inequality and cost of service provision is a major shortcoming. Without such indicators, it seems difficult to really confirm the FCM's role in promoting territorial equity. The selectivity of the operating rules governing contributions, FCM attribution rules are easy targets of criticism. Some technical choices concerning the indicators may appear methodologically contestable, even if politically endorsed. However, it should be recalled that the FCM's main goal is not equity but inter-municipal solidarity, i.e. to redistribute resources in such a way that each municipality (regardless of its size or wealth) is able to perform the basic functions that are required of it by the constitution. This political choice gives prominence to demographic criteria (or spatial-demographic). That is why there is an inverse relation between population and the different per capita indicators.

Institutional impediments. To protect municipalities that would see a drop in their allocation, there is a mechanism that smoothens the decrease (*mecanismo de*

estabilización). This safeguard clause constitutes a buffer for municipalities facing declining and inelastic expenditure. Nevertheless, as the FCM is a closed grant (i.e. a zero-sum game), the amount used by the stabilisation mechanism cuts the resource used for equalisation. This reduction is the cost or the "insurance contribution".

There are systemic effects. Regardless of the discussed hypothesis of "tax laziness", the FCM introduces a dependency effect. In 2015, for 29 municipalities, the FCM accounts for more than 90% of their own permanent tax, reaching 97.8%. For 38% of municipalities, the dependency ratio exceeds 75%. At the other end of the spectrum, a few municipalities present a ratio less than 10% (Table 3.3).

In recent years, this situation has led to a complex conclusion: the redistribution is effective, does not progress, and the dependency is increasing. Between 2010 and 2015, the average dependency ratio (municipalities ratio: FCM/total own revenue) was quasi identical (42%). However, the median value of this dependency ratio is higher (nearly 70%) and increases steadily.

Table 3.3. **Ranking of the municipalities according to the dependency ratio on FCM revenue (2015) (%)**

Ratio 1 FCM as a % of own taxes		Ratio 2 FCM as a % of total resource	
Lowest	**Highest**	**Lowest**	**Highest**
Santiago: 1.8	Juan Fernandez: 97.8	Santiago: 1.1	Isla de Pascua: 87.8
Las Condes: 2.1	Isla de Pascua: 97.6	Las Condes: 1.1	Navidad: 81.3
Providencia: 2.3	Saavedra: 96.2	Providencia: 1.3	Juan Fernandez: 78.1
Vitacura: 2.6	O'Higgins: 96.1	Vitacura: 1.6	San Rosendo: 78.1
Lo Barnechea: 2.8	Lago Verde: 95.2	Lo Barnechea: 2.3	Carahue: 78.1
La Reina: 6.9	San Rosendo: 95.2	La Reina: 4.6	Treguaco: 75.1
Viña del Mar: 7.2	Rio Ibanez: 94.3	Ñuñoa: 5.4	Quillon: 74.6
Zapallar: 8.6	Portezuello: 94	Viña del Mar: 5.7	El Tabo: 73.3
Ñuñoa: 8.6	Currarehue 93.7	Iquique: 5.8	Hualqui: 72.2
Huechuraba: 8.6	Treguaco: 93.7	Zapallar: 6.1	Emperado: 72.1

Note: Ratio 1: IADM75; Ratio 2: IADM03.

Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM: www.sinim.gov.cl/).

In this context, to avoid the adverse effect of "tax laziness" and to consolidate the redistributive performance of the FCM, the Commission of Decentralisation has proposed an important modification of the mechanism. It is not only a matter of changing the name of the FCM to Fund of Municipal Solidarity (*Fondo de Solidaridad Municipal*, FSM). The main goal of the proposal is to combine the incentive to eliminate the risk of "tax laziness" with an increase in the selectivity of FCM redistribution. The idea is to concentrate contributions and repayments while the fund would continue to be financed by the same basket of tax resources:

- Tax contributions would only concern municipalities belonging to the last three deciles (the highest) of the distribution of municipal resources per capita. The contribution rate would be digressive based on belonging to a decile of lower rank (it would decrease from the 10th to the 8th decile).
- FCM repayments would be reserved for municipalities belonging to the first three deciles (the lowest) of the distribution of municipal resources per capita. The

repayment rate would be regressive (the repayment rate would decrease) rising in a decile of higher rank of the 1st to the 3rd decile).

- All the other municipalities belonging to the deciles from the 4th to the 7th would not be affected by the system.

On the "incentive side" aimed at alleviating "tax laziness", the proposal suggests keeping the advantages of the FCM in terms of repayments for the municipalities raising their tax collection but which then would lose their eligibility to the Fund. Likewise, the proposal calls for a freeze on repayments for municipalities with passive tax behaviour (it would function like a "bonus-malus" system).

This is one avenue to explore in an effort to enhance Chile's innovative inter-municipal solidarity mechanism.

True to its mission, the FCM redistributes resources on a large scale between municipalities in Chile and makes an essential contribution to the budgets of many municipalities with tiny populations. Via its redistribution role, the FCM contributes significantly to reducing the inequalities and flattens the amplitude of the dispersion of initial revenue grants. Despite these important results, it is not possible to validate the assertion that the mechanism is effective with regard to the criterion of territorial equity. The qualities of this redistribution seem less assured and the methodological and technical choices on which the FCM is based raise question(s).

Change in FCM operating procedures

Despite the results obtained, the deficiencies in the underlying design of the FCM have led observers to suggest improvements in its approach and its allocation rules. The areas of caution and correction are found on different political horizons and ambitions. The proposals put forth do not intend to suggest "turnkey" reforms that are ready to apply. They aim to spark a dialogue in order to explore, in their political and legal feasibility and the methodological and technical implications, ways of improving the mechanism. The prospect of a significant increase in national resources (more than quadrupled from 218 000 to 1 052 000 UTM in 2018) should not serve as an excuse for policy makers to refrain from taking decisive action.

The structural questions underlying the fund remain unanswered. The revision of the FCM can be envisioned according in two ways:

- A methodological and pragmatic vision: positioned on a short-term timeframe, its changes reflect the FCM's current approach. However, the transitions that must be managed in order to put the FCM on a virtuous path with regard to territorial equity criteria are inevitably more long-term in nature.
- A prospective and political reflection: positioned on a medium and longer timeframe, it is part of a decentralisation and modernisation dynamic where inter-municipal inequalities are addressed as regional power is consolidated.

Modifying the allocation rules of the FCM (short-term approach)

Regardless of the path the FCM will take, it is currently based on methods and applies allocation algorithms that are not completely in step with the qualities that could theoretically be expected of an equalisation mechanism. In addition to the central question of wealth inequalities, there are questions on the methods and calculation of

allocation indicators. All equalisation tools must be taken in for a periodic "check-up" and its inner mechanisms must be repaired or fine-tuned.

A revision of the measure of inequalities

As they strive to fulfil their mission of territorial equity, all equalisation mechanisms are confronted with two essential challenges: identifying the socio-economic conditions on the ground and defining the reference indicators. The FCM displays shortcomings on these two key aspects for guiding the action of the equalisation mechanism correctly.

From unequal conditions on the ground toward greater territorial equity

It is intellectually relevant and analytically stimulating to separate inequalities into two different groups: those deriving from management decisions and those resulting from present conditions within the territory. The former (e.g. decisions related to the range and level of services provided, choice of finance, etc.) reflect the decision-making autonomy of local authorities and do not merit compensation. However, the latter result from the geographic, social, economic, demographic, taxation characteristics and structural conditions that are imposed on local authorities when they take office and over which they have no control. This is true at least in the short term, because in the medium term it can be assumed that the goal of public action would be to improve these conditions. The environment in which public policy is enacted and the policies themselves are inseparable and the separation between situational inequalities and management inequalities is fading. Limiting the analysis to a short-term approach, the existence of inequalities in conditions on the ground justifies the use of an equalisation therapy that remedies the handicaps relative to the healthier territories.

The analytical difficulty resides, however, in breaking down what can be a confusing picture on the ground, namely the difficult task of assigning to each source of situational inequality a degree of responsibility.

- Insufficient primary disbursement in terms of taxable base.
- Excessive charges: more difficult to estimate, they result from a host of different characteristics in the territory: the composition of the population (social, revenue level, age, active or not, etc.); the geography of the territory (density, land mass, altitude and weather conditions, etc.); the existence of uncovered (or "internalised" in the economic jargon) charges related to services, uncompensated charges, cost of amenities and services provided by municipalities with exceptional infrastructure to residents of other municipalities ("centrality charges"), seasonal use infrastructure, etc.

This method is an approach that strives to achieve territorial equity. It tries to even out the "advantage-effort" ratio, i.e. to make sure public services offered to users are on the same level as the tax effort being asked of taxpayers. This type of approach has the advantage of not dissociating expenditure decisions and financial decisions; rather, it considers them to be interdependent.

Stated differently, in order to comply with the basic principles of territorial equity, the target of equalisation should be to even out municipal tax wealth corrected for the charges that wealth helps pay for. The equalisation of purchasing power of local public services is the objective toward which equalisation mechanisms should work.

From nominal tax potential to real financial potential

The focus on remedying the inequalities suffered has immediate repercussions on the way in which inter-municipal resource inequalities are evaluated. The theoretical demands and the methodological difficulties are three-fold.

First requirement, the basic question always concerns the accurate definition of the scope of the resources covered by the tax and financial potential and remains unanswered. The indicator will be skewed as long as the resources are not defined in their entirety. The risk of this occurring is high for atypical revenues that only apply to a few municipalities. Its real level is underestimated because of the non-integration of these resources in the evaluation of the financial potential, which is advantageous for these municipalities because they would appear poorer than they really are. The FCM shields itself from criticism by integrating resources such as casinos or business licenses (mining, aquaculture) in the calculation of permanent own revenue (*impuestos propios permanentes*), which is the FCM's nominal wealth indicator.

The second condition involves stripping the measure of all impact of municipal tax decisions. The simple solution would be to use tax revenues; but this is not possible because the revenue, even if it takes account of the amount of the bases, is also a function of the rate whose level is under the municipality's political control. Of course, in Chile's case, rate-setting power is limited. It is non-existent for the territorial tax and for the vehicle registration tax. For the municipal business license the leeway is narrow. However, it can be doubled, albeit within a tight range. Municipalities are allowed to set the waste management fee and the size of fines and interest. The question of exemptions and elected officials' influence in this area also raises questions.

The way to put the measure of tax wealth out of the decision-making reach of the municipalities is to reason in terms of tax or financial potential (Uhaldeborde, 1979). The neutralisation of the municipal rate effect leads to the substitution of the revenue received by the municipality with the revenue it would receive if it applied a standard rate to its tax base. Most often, the average rate is used. The transformation of bases into revenue (even potential) is an arithmetic challenge. Municipal tax wealth is an aggregate and therefore the tax bases cannot be added to one another. Only the revenues can be added together. The means of expression of the municipal reference rate thus makes it possible to estimate the revenue that would be generated by the various bases by applying the respective reference rates to them. It is a way of comparing the municipal situations, while stripping them of the influence of the decisions that are the remit of elected officials.

The third challenge pertains to how wealth potential must try to account for the purchasing power of the tax base (Ahmad, Letelier and Ormeño, 2016). This approach, in line with the tenets of balancing the "advantages-effort" ratio, faces two hurdles:

The first difficulty resides in the coupling with a "charge index" in order to have not just a nominal wealth indicator but a real wealth indicator, i.e. one that takes into account the purchasing power of the financial potential. Reasoning in terms of "purchasing power parity" struggles to impose itself as the best solution. The problem can be circumvented in several, circuitous ways:

- Comparing the per capita tax wealth situations within the same demographic level with the implicit assumption that similar, big municipalities are confronted with the same charges.

- Weigh the financial potential with an implicit index of the cost of municipal services.
- Combine resource and charge indicators taken into account by the municipality's socio-economic or geographic variables.

The second challenge resides in the fact that the reliability of the calculation of tax wealth is dependent on the shortcomings of the evaluation of local tax bases – and algorithm designers have yet to model this correctly. The uncertainties emanating from the spatial homogeneity of their evaluation skews the comparability of the bases and projects onto the measurement of financial potential when, notably, the equalisation reference is national.

A revision of the distribution algorithm

As with many equalisation mechanisms, the FCM mechanism transfers funds to the municipalities like a group of budgets dedicated to specific areas to which resources are distributed in exchange for drawing rights. These rights are determined by the value of representative indicators (the relative poverty rate, size of exemptions). These two levels (i.e. the dedicated budgets and indicators) are the elements that make up the distribution algorithm. Technical in appearance, its configuration is in fact a political choice, which makes adapting them (simple to set up technically and simulate) difficult to implement because of their financial impact. The review of the algorithm can therefore be considered both from the coherence of its architecture (the respective importance of different budgets) and the relevance of the indicators.

The revision of the FCM architecture

Excluding the special treatment of Easter Island, Chilean municipalities are admitted to the four dedicated shares of FCM resources (poverty, equal distribution, exempted properties, permanent own revenue). The question, but which expresses a compromise or a political preference, involves their respective weighting. The architecture must match the political objectives that the fund serves but without neglecting the trend towards greater territorial equity.

For example, the mechanism favours small municipalities over the poorest by assigning a weight of 25% to all municipalities (each municipality will receive the same amount regardless of population size), and only 10% to the municipality's poverty rate, evaluated by transfer per capita. The inversion of the weightings would shift the centre of gravity of transfers and modify the reach of the equalisation mechanism. The question is not to challenge political decisions. The question is about identifying the cost in terms of redistributive effectiveness and convergence toward the goal of territorial equity. This question applies to all of the "dedicated budgets" architecture. Impact on territorial equity should be at the heart of policy makers' decision making.

The revision of the indicators used in the allocation of the FCM

The indicators used in the FCM should regularly be tested for their relevance, to verify if the decisions made at some point in the past and on the basis of data available and their collection methods at the time, are still topical, to compare the indicator with the objective that it is supposed to accomplish. Given this, an examination of the functioning of the FCM raises certain questions.

An initial illustration is seen in the reference to the weakness in revenue from permanent own resources. It is supposed to be a proxy for tax wealth, but it should be

replaced with an indicator of tax or financial potential per capita, if the question is to be handled appropriately. The way in which the indicator is used (municipalities with an above-average indicator are denied the allocation) would be worth discussing in terms of the threshold effects introduced by the rules and alternative, less-radical formulas in the calculation of this component of transfers (e.g. amount could change depending on the gap vs. the average tax revenue per capita).

A second illustration is provided by the facility dedicated to the property exempted from the territorial tax. The indicator used refers to the number of properties. Would it not be more relevant to use the value of the exempted properties? Depending on the kind of property (agricultural or non-agricultural), the situations are inversed if the volume is used or the value of the properties is used. Given this, depending on the percentage of each type of property in the municipality, the choice of one indicator or the other will not have the same impact. Using the number of exempted properties volumes instead of values of exempted properties over-represents agricultural properties.

The third illustration is the reference to the floating population that is used to evaluate the per capita amount of permanent own resources. In theory, the increase in the permanent population - by taking into account the seasonal population - is a sensible approach. The temporary rush of people into an area puts strain on resources, which must be calibrated to absorb the extra population yet only the permanent residents are required to pay for this extra capacity. This demographic bonus entails an increase in the allocation (if the amount of per capita taxes, calculated with this excess population included, does not exceed the average). It can be likened to a contribution to the internalisation of positive externalities issued by the touristic municipality. The same line of reasoning is valid for expenses incurred by centrally-located municipalities that are not commonly borne by more peripheral municipalities. However, the method of calculating the floating population, set in 1980, delivers some spectacular results. The floating population boosts the national population by 32%, but for five municipalities - deemed “touristic” by the National Tourism Service (SERNATUR) - the increase leads to a jump of over 1 000% of the population. For instance, El Quisco rockets from 12 800 inhabitants to more than 239 000; El Tabo, on the back of the floating population rises from nearly 10 000 inhabitants to 146 000; San Pedro de Atacama goes from 7 200 inhabitants to 96 000. Such increases linked to the vacation-related population raise the question of the relevance of the evaluation method of this extra population. But the rules of the FCM create other surprises. For example, an interesting situation occurs when comparing Valparaíso and Viña del Mar. Valparaíso obtains the status of a “touristic” municipality; Viña del Mar is not considered to be touristic, despite a floating population far exceeding that of Valparaíso. In fact, the attribution of the status of “touristic municipality” requires another condition: a relative importance of the properties exempted of the territorial tax exceeding the national average share of exemptions. In Viña del Mar, 36% of the non-agricultural properties are exempted from the tax; in Valparaíso the ratio is 66%. In Viña del Mar, the revenue of the territorial tax is nearly three times greater than in Valparaíso. The compensation of the over-expenditure linked to influx of tourists is weighted by the relative size of revenue shortfalls linked to territorial tax exemptions.

These different observations underline the importance of the technical revision clause of these mechanisms, which must be carried out on a periodic basis. Its method should be tested against the effects on the equalisation of resources, as all corrective measures should.

Revising the FCM's intervention approach (medium and longer term approach)

The prospective opening of FCM reform assumes that Chile will make a firm and long-term commitment to the decentralisation process. The modernisation of the municipal system will lead to a stabilised and well thought-out decentralisation process that builds on the regionalisation process begun in 2015. The timeframe is ten years.

The FCM is grounded in two founding principles: it ensures horizontal equalisation; it has a "one-size-fits-all" design (i.e. the same rule applies to all municipalities, regardless of size or environment). Against this backdrop, a hybridisation of the two mainstays of the FCM could be considered: 1) the horizontal approach of the mechanism, inflected by more verticality from the contribution of budget grants from the central government and 2) the uniform approach, which could shift to a more regional approach where its allocation mechanisms better reflect territorial and social realities resulting from the country's diverse geographic characteristics.

A hybridisation of FCM funding sources

In a majority of countries, equalisation mechanisms include both "vertical" and "horizontal" mechanisms but vertical equalisation arrangements are much more widespread and powerful. Equalisation often occurs through the transfer of national resources, which is the counterpart to the asymmetry between expenditure and resources that marks the municipal sector, in particular. Chile distances itself considerably from this model by organising equalisation in a horizontal manner. Decentralisation would provide an opportunity to review the current equalisation framework and its basic principles. The "horizontality" of its funding sources could be joined by a "verticalisation" of the contributions. Already underway, FCM "hybridisation", via the contribution of national resources, could be ramped up.

The difficulty in increasing municipal contributions

Financially, by extension of the contributor base or increase in quotas, additional resources can be generated from the wealthiest municipalities, which is what the FCM has always done. The revenues they have left over after payment to the fund maintains them in a comfortable financial situation compared with the dire straits other, less fortunate from a taxation point of view, municipalities find themselves in.

The difficulty in pursuing this avenue politically comes from the transparency that characterises the extraction of resources for redistribution, resulting in a "Robin Hood" effect. Indeed, taxpayers sometimes feel that the mechanism is stealing from the rich to feed the poor. Their reticence is exacerbated by a suspicion of the disincentivising effects of the transfers as compared with the mild taxation requirements of other municipalities. This could produce "revenue effects" (Bravo, 2015) leading to "tax laziness" (*pereza fiscal*), with the subsidised municipalities exempting their own taxpayers from making contributions. Following this logic, poor municipalities do not make a sufficient effort to generate - for themselves - the necessary resources to cover their needs. Rather, they wait passively for the "heavens" to come and rescue them.

On the flip side, vertical equalisation (via the state budget) of national resources is less transparent but less painful, as if an invisible hand were distributing a windfall from the heavens. Behind the veil of a tax illusion, vertical equalisation is often more politically and socially acceptable than equalisation backed by horizontal transfers, which is – however – the more transparent and civically virtuous of the two.

The negative perception of redistribution is tangible in many countries: the wealthiest regions are reluctant to finance transfers to poorer regions who may make dubious and economically-ineffective use of it in a vain attempt to dig out of poverty. Solidarity is sometimes hit with an egotistical backlash as rich municipalities dig in their heels in resistance. A substitution effect (reduction of the tax contribution) can outdistance a revenue effect (increase in the payment to offset the loss of resources transferred). Although the municipalities that are the biggest contributors limit the use of taxation that feed into their FCM contribution (through setting low rates, exemption thresholds) increasing the quota of payments is the only way to keep the fund's resources afloat, which would run the risk of worsening hostility and internal tensions in the municipal financial system. According to this inference, redistribution from municipal origins would stagnate. A form of tax abstention from rich municipalities would limit the advancement of solidarity-inspired redistribution. Fewer municipal contributions would mean greater national contributions.

Usefulness of additional national resources

The hybridisation of horizontal equalisation by injecting national resources is already well underway. The FCM contribution has been criticised as being too timorous. However, temporary contributions have bolstered it in order to prevent a decline in FCM resources.

The central government's extra firepower is justifiable from a "fair return" perspective according to the principles of justice and accountability: "he who decides, pays". Many municipalities rebuke the state for not totally compensating the shortfall resulting from sizeable exemptions, particularly in the territorial tax. The erosion of the tax bases, resulting from national decisions is a budget expenditure borne by municipal budgets when uncompensated. The contribution of the budget grant would settle tax-financial disputes with the municipalities.

These additional resources would facilitate the adoption of payment rules by easing tensions linked to competition, in a zero sum game, between resources allocated to manage a transition for municipalities penalised by the adjustments made to the mechanism and those dedicated to equalisation. The adjustment periods consume vast amounts of resources.

Lastly, the additional fiscal contribution ensures that FCM resources will continue to progress and could be motivated by more affirmative concerns or as a support provided to decentralisation and the equalisation that must accompany it. The budget support from the state could take the form of a pact or agreement that would set the original commitment level and the way in which it is indexed (beyond the reference to the UTMs, whose unit value fluctuates with price changes).

In any case, the increase in resources that an initial supplement from the state would entail would provide additional pressure to correct the bias that the FCM contains. Through the revision of the criteria and indicators of its distribution (see above), it is important to neutralise the system effects that could arise, particularly the revenue effects it is suspected of causing.

The increase of the state contribution linked to the reform of municipal human resources is a first step. The improvement of national resources in 2018 from 218 000 UTM to 1 052 000 UTM is significant. However, their weight will be limited to around 5% of the totality of the resources of the FCM. The process of hybridisation or mix of resources is underway, yet there is plenty of room for improvement.

A hybridisation of FCM allocation frameworks

The rules governing the transfer of collected funds make the FCM a uniform or "unitary" mechanism and reflect the public powers' vision of its organisation. The same distribution mechanism is applied to all municipalities, except in truly unique circumstances when marginal adjustments are made (e.g. Easter Island has constraints and specific charges related to its insularity).

Adjusting the rules on allocation is an area to explore in order to maximise – by adapting to local situations – the effectiveness of redistribution. The implications of setting different rules for different municipalities (i.e. "differentiation") are more politically and culturally loaded and liable to spark discontent than making adjustments – even major adjustments – to the current framework. This perspective calls for a change in the framework backed by an advanced regionalisation of public policy.

The modalities of differentiation of FCM allocations

Differentiation would translate into a decoupling of the FCM's resources and charges.

On the resources side of the ledger, the FCM would continue to operate within a national framework. The financing of the fund would continue to be ensured by a centralisation of transfers of the revenues assigned to the municipalities, plus the central budget grant. The differentiation would concern the way in which those resources are used or allocated. FCM transfers would be governed by rules that could differ in order to adapt better to the specific aspects of each region. In the beginning, this regionalisation would not mean that the operations would have to follow the current regional landscape. This regional distribution could be conducted via ad hoc zoning by grouping regions confronted with similar territorial problems (e.g. Metropolitan Region of Santiago, northern regions, southern regions, central regions excluding the Metropolitan Region).

Its *modus operandi* would be rooted in a two-phased allocation process. The first step would entail the distribution of resources among the "big" regions (FCM zones) using economic and social disparity indicators. In the second stage, this FCM grant would be distributed between the territory's municipalities using its own algorithm. The rule governing the distribution mechanism could be designed in several different ways:

- Politically, by mobilising all players in its design, ensuring political and administrative representation of all stakeholders (municipalities, region, state in the form of a territorial conference).
- Technically, by dosing - in proportions to be decided on - shared indicators (e.g. discrepancies in tax wealth, population, etc.) and their own indicators reflecting the specificities of the territory (e.g. the poverty density or index, water network coverage, the surface area of green spaces, etc.).

Regionalising FCM allocations

FCM hybridisation of this type, combining nationally-collected resources and uses that are territorially differentiated (i.e. distributed differently between territories) raises a host of questions as it breaks significantly with the unitary culture. The risks that would undoubtedly be debated (centrifugal force, principle of equal treatment of citizens, etc.) can be counterbalanced by the benefits that the country would stand to gain (e.g. more effective public policies from better territorial co-ordination of its objectives and resources). Territorial differentiation of the rules, via a well-designed mechanism and shared governance, can foster political cohesion (via the learning process of co-

management), economic soundness of territorial development strategies and effectiveness of the allocation of public funds (via the diffusion and sharing of all information on the public resources invested in the territory). These are the risks and challenges associated with a medium-term political and societal project founded on a well thought-out decentralisation strategy that energises local players.

Conclusion

With the FCM, Chile has an original and powerful mechanism to redistribute resources among the municipalities. This horizontal equalisation mechanism between municipalities is commendable in light of the principle of solidarity reinforcing the feeling of belonging to the same nation. It plays a strategic role in the redistribution of resources according to redistributive justice as the system benefits the most disadvantaged municipalities in terms of tax wealth and/or demographic constraints (small size) or geographical and climatic constraints (large area). It aims at supporting the most vulnerable municipalities, especially the smallest in such a way that each municipality (regardless of its size or wealth) is able to perform its basic constitutional functions. According to these conclusions, the FCM is indeed effective in achieving that goal. The smaller or less densely populated the municipality the more it receives per capita. Several studies confirm the redistributive character of the FCM. It thus reduces inter-municipal inequalities and ensures greater political cohesion in the municipal system in Chile.

Despite these shortcomings and limitations, the FCM should be preserved and strengthened but also renewed and supplemented to combine solidarity and equity principles as well as economic efficiency. In order to reorient the FCM towards territorial equity principles and methods, various avenues need to be explored. The overall objective of the reform would be to widen the base of municipal contributions, to make it less selective and to better assess municipal wealth in order to determine contribution and benefit levels. The horizontal mechanism should be complemented by a greater vertical equalisation mechanism through state grants.

A thorough review of the FCM's design and its allocation methods and rules should be conducted. Beyond the adjustments of a technical (albeit politicised) nature, the needed revision of the equalisation mechanism provides an opportunity to make it a lever of an institutional arrangement with a systemic reach. Steering the reflection and action in this direction brings to the fore topics regarding the opportunities and the feasibility, the advantages and the risks of a decentralisation process, that is under control politically and efficient economically.

Box 3.4. **Key recommendations for reforming equalisation mechanisms**

1. Modify the allocation rules of the FCM (short term approach):

- Review the measure of inequalities in terms of charges and resources and contribution criteria, by:
  - Better identifying socio-economic conditions on the ground, in particular excessive charges resulting from unequal conditions, and defining the reference indicators. Establishing a research programme aimed at increasing knowledge of the costs of provision of municipal services in various contexts (urban, rural, small municipalities).

Box 3.4. **Key recommendations for reforming equalisation mechanisms** *(continued)*

  - Changing from a methodological approach based on "nominal tax potential" to an approach based on "real financial potential".
  - Broadening the number of contributing municipalities by differentiating the rate of contribution according to tax revenue per inhabitant (territorial tax, business licenses).
  - Including all municipal taxes in the measurement of municipal wealth as a basis of the differentiated contribution to the FCM.
- Review the FCM's distribution algorithm, by:
  - Re-examining the FCM's current architecture: the weight of each of the four items assessing charges and resources disparities could be reviewed to match the political objectives that the fund serves but without neglecting the need to move towards greater territorial equity (e.g. increase the FCM's share allocated based on "poverty rate" and decrease the based on the criteria of "equal treatment").
  - Reviewing the ways indicators used in the allocation of the FCM are calculated (e.g. "weakness in revenue from permanent own resources" and "number of property exempted from the territorial tax') and some methodological aspects (e.g. method used to calculate the "floating population").
  - Reassessing the criteria and indicators used in the attribution of the FCM to avoid tax "laziness"; revision of measurements, in gross terms, of inequities, differentiation of the attribution according to the municipal per inhabitant level of wealth evaluated in real terms i.e. by taking into account differences in the cost of providing basic services imposed by inequalities (geographical, demographic or social).

2. Revise the FCM's intervention approach (medium and longer-term approach):

- Complement horizontal equalisation by more vertical equalisation via the state budget: increase the central government contribution to the FCM, to reach gradually a target of 10% (for example).
- Differentiate and tailor procedures of FCM allocation according to a regionalised approach:
  - "Regionalise" equalisation mechanisms, not in regard to resources but in regard to allocation criteria. Equalisation transfers would be governed by rules that could differ in order to adapt better to the specific aspects of each region (to be defined as it can also be a group of regions or specific zoning determined using economic and social disparity indicators). Distribute resources among "big" regions and then among municipalities within each region using its own algorithm.
  - Despite progress in "regionalising" Chile's equalisation mechanism, maintain national funding for the FCM.

Notes

1. The geographic concentration index (GCI) of GDP is equal to half the sum of the differences, in absolute value terms, between the proportion of the land mass and the percentage of GDP of the administrative area as a percentage of the entire country. A value of 0 means the production and land mass of all subnational entities have the same proportion throughout the country. A value of 1 means the differences between the proportion of GDP and the land mass of each subnational entity are enormous.

2. For a clear and detailed definition of the concept of territorial equity and how to measure it in operational terms, see III, 1.1.

3. For 2015, four municipalities, whose data were not used, are not included in the file or the analyses: Pozo Almonte, Tocopilla, Alto Bío Bío and Málfil. Their data was late and not included in the database. The cumulative population of these four municipalities accounts for 0.3% of Chile's total population. The municipality of Antártica (184 inhabitants), which does not have municipality status (considered part of Cabo de Hornos), is never included in datasets.

4. In the measure of expenditure per capita, the substitution of the pupils to the inhabitant does not change the relation. The individual amount lowered but the distribution of the municipalities is not modified. This situation is linked to the high level of correlation (0.9875) between the two populations.

5. For example, in the Metropolitan Region of Santiago, the municipal schools represent less than 25% of all schools. In contrast, the share of public education sector is very important in the regions III, IV and XI.

6. Unlike education, budget data on healthcare is less exhaustive and uniform. For a number of items, nearly 30 municipalities are lacking data ("*sin dato official*"). For around twenty municipalities (primarily in the region of Cohaique), no services are available ("*sin servicio*"). This does not involve tiny municipalities. Expenditure seems to take account of flat costs ("*costo fijo*"). This mechanism is reserved for municipalities with less than 3 500 habitants and aims to cover the cost of basic care.

7. With their high degree of correlation (0.708) business licenses and territorial tax cumulate their incidence to accentuate the inter-municipal gap of wealth.

8. Distributed revenues from tax on casinos and gambling are concentrated in 20 municipalities. The amounts per person are most often modest. Yet, it represents a windfall for two municipalities: Rinconada (CLP 309 000 per capita, i.e. three times greater than the contribution of the FCM) and Mostazal (CLP 249 000 per capita, i.e. four times greater than the FCM).

9. For operations in the education and healthcare sectors, the weight of personnel expenditure and that of transfers renders irrelevant the interest of an approach aiming to update the factors of differentiation.

10. The cost of household trash collection and cleaning expenses form the bulk of costs related to community service programmes, followed by electricity and park/green space maintenance. The weight of other areas was minor.

11. For the most part, they are part of categories 3 and 4 of the FIGEM typology.

12. This accounting mechanism is however badly identified because of the way FCM's payment operations are carried out in practice (e.g. sometimes they are delayed).

13. The FCM amount allocated to the Municipality of Easter Island is 1.4 times the sum of expenditure related to staff and purchase of goods and services from the previous year (section 3o of FCM regulation published on 2 January 2009). This approach transforms the FCM into an "on tap grant" for the benefit of the municipality as the amount allocated to the municipality depends on the level of expenditures that it, itself, has voted. The FCM allocation exceeds 40% of municipal operating expenses, which contributes to a high per capita FCM amount but also a strong municipal dependence on FCM resources.

14. This contribution is determined within the framework of a co-operation agreement for the financing of the theater of the municipality of Santiago.

15. For business licenses, before and after deductions, variation coefficients are respectively 2.64 and 2.67 and Gini coefficients are 0.715 and 0.699. For territorial tax, before and after deductions, variation coefficients are respectively 2.00 and 1.97 and Gini coefficients, 0.59 and 0.58 (based on all municipalities).

16. In 2015, without the contribution to the FCM, in the top 10 of the amount per capita of the revenue of the business licenses, Las Condes occupies the sixth rank and Providencia the ninth. With the contribution they are out of this ranking. At the top of the amount per capita: Siera Gorda, Zapallar, Santo Domingo, San Gregorio, Ollagüe, Rio Verde, etc.

17. Pérez Morales M. (2013) with an econometric methodology confirmed the effectiveness of the redistributive character of the FCM and relativizes the main conclusion of Javiera Bravo: the existence of a "tax laziness" effect. Mario Perez observed this behaviour in big municipalities of the metropolitan areas only.

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Chapter 4

The management challenge: Strengthening the human capacities and management tools of municipalities

This chapter focuses on improving municipal management and performance through adequate human resources and efficient tools for public service production, delivery and monitoring across the whole national territory. The first part is dedicated to the modernisation of human resource management (HRM) in Chilean municipalities, looking at the development of workforce planning and management, the strengthening of human resources capacity and the need to reinforce the HRM function at municipal level. The second part focuses on how to enhance the quality and efficiency of municipal services in Chile through the development of a municipal services management model, including the establishment of minimum standards for municipal services as a means to reduce territorial disparities, and the provision of appropriate incentives as well as a suitable institutional framework.

Modernising human resource management in Chilean municipalities

In Chile, like in countries with legally or constitutionally guaranteed subnational self-government, multi-level governance also means multi-level human resource management (HRM). Municipal governments in Chile now have the same public sector employment arrangements as the central government, but not necessarily the same employment conditions. Consequently, municipalities remain weak in their capacity to perform their duties as they find it challenging to attract and retain a highly-skilled workforce. Low salaries, limited career opportunities, and politics are just some of the factors that hinder the attractiveness of municipal public administrations as employers.

Governing municipal public employment

General public employment in Chile is regulated by the Political Constitution of the Republic, which establishes the general framework of the action of the state and the right to a career in the public sector. In addition, Act No. 18.575 establishes the Constitutional Organic Act for the Administration of the state, which regulates the organisation of the state; Law No. 18.834 contains the Administrative Statute, which is the general code for public employment in Chile; and Law No. 19.882, creates the Senior Public Management System.

Until recently, the regulatory framework had provided little flexibility in municipal workforce management…

The legal framework regulating municipal sector public employment in Chile includes several laws and policies. Different laws regulate municipal employment in the health and education sectors, which are also under the municipal government purview.

Municipal sector public employment is regulated by Law No. 18.883 on the Administrative Statute for Municipal Employees (Government of Chile, 1989).[1] It regulates employment conditions for *planta* and *contrata* staff who are considered as officials. This law does not regulate temporary employees (*honorarios*) as they are governed by their individual contracts and the Labour Code. Law No. 19.518 regulates the training of municipal employees. The legal framework, unchanged for over 20 years, has limited the possibility to adjust the workforce to the municipality's needs by local authorities and the adoption of incentives to attract and retain highly qualified personnel. Municipalities cannot modify the size and composition of the technical-professional *planta* of the municipal workforce or remuneration. The main issue has been that the size of the municipal public workforce is largely determined by law and not by local necessities.

The labour relationship between education and health workers with the municipality is regulated by different regulatory frameworks. Staff in the education sector are governed by the *Estatuto Docente* (Teachers Statute) of 1997 that regulates the requirements, duties and rights of teaching professionals working in the municipal sector, including their career structure and salary (Santiago, et al., 2013). It also includes mechanisms to define the size of the *planta* and the number of teaching hours (*dotación docente*). These mechanisms can be reviewed once a year. Non-teaching staff in the education sector are regulated by the Labour Code but their salary adjustments are set by the rules that apply to public functionaries.

Healthcare employees are governed by Law No. 19.378 on the Statue of Primary Care (*Estatuto de Salud Primaria*). This statute allows each municipality to create its own

planta for professional and non-professional workers in the health sector. This facilitated the creation of a career in the health sector that reflects the characteristics of each municipality and prevented the automatic increases in salaries based on seniority as it is the case in the education sector.

One of the main problems for municipalities in the management of these two sectors is that the salary conditions are negotiated at the ministerial level, between the central government and the national associations of professionals in both sectors, without taking into account the particularities of each municipality.

…but recent reforms aim to provide more flexibility and increase professionalisation levels.

In May 2016, a new law was published to strengthen municipal management and professionalisation of staff. Law No. 20.922 - also known as the *plantas* law - reformed parts of Law No. 18.833 and key changes include:

- Ability given to mayors to modify, in accordance with two-thirds of municipal council members, the size of the *planta* staff every eight years as well as reorganise the public workforce. 75% of all new *planta* positions will have to be in technical and professional roles.[2]
- Improved remuneration for technical, administrative and professional staff.
- Introduction of a graded pay scale for 8 700 professional municipal employees that rewards academic and professional development qualifications.
- Increase in the maximum share of expenditure in *contrata* staff from 20% of municipal expenditure to 40% in the *planta*.
- Improvement in job stability.

Since the law was approved in 2016, the fiscal contribution to funding started in 2016 rather than in 2015 (as initially budgeted). The contributions to the Municipal Common Fund only begin in 2018. In 2016 and 2017 are transfers to municipalities, according to the criterion indicated in the law.

To cover the costs of these changes, the central government increased its transfers to the municipalities in 2016 and 2017 (respectively CLP 32 and 26 billion). By 2018, the state's contribution will be done through the FCM which is expected to increase almost fivefold. Municipalities will be required to exercise fiscal responsibility and probity when setting staffing levels. This bill does not apply to the education and health sectors.

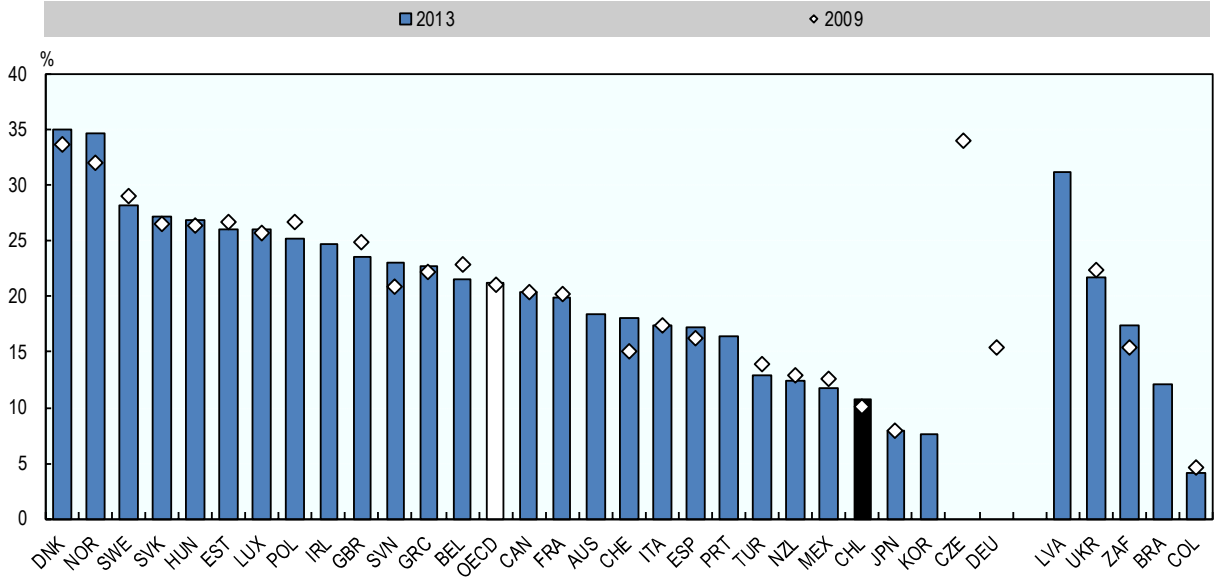
This law adds to recent previous improvements concerning municipal officials, especially the harmonisation of the remuneration of municipal staff with that of central government civil servants, both for base salaries' scale and bonuses[3] (Law No. 20.624 of 2012 on base salaries scale [4] and Law No. 20.723 of January 2014 on municipal bonuses). These improvements, especially the last Law No. 20.922, contributed to progressively creating a stronger municipal civil service.

Workforce planning and management

Chile has a relatively small public workforce compared to other OECD countries

Chile has one of the smallest public workforces among OECD countries. Public employment represented just over 10% of total employment in 2013. Only Japan and Korea have a smaller public workforce than Chile. There is no right size of the public sector workforce. As Figure 4.1 suggests, there are large differences in the share of government employment among OECD member countries, reflecting different choices with regard to the scope, level and delivery of public services. A critical point is, however, how the workforce is managed to enable government to produce goods and services in the quality and quantity required by the population.

Figure 4.1. **Public sector employment as a percentage of total employment, 2009 and 2013**

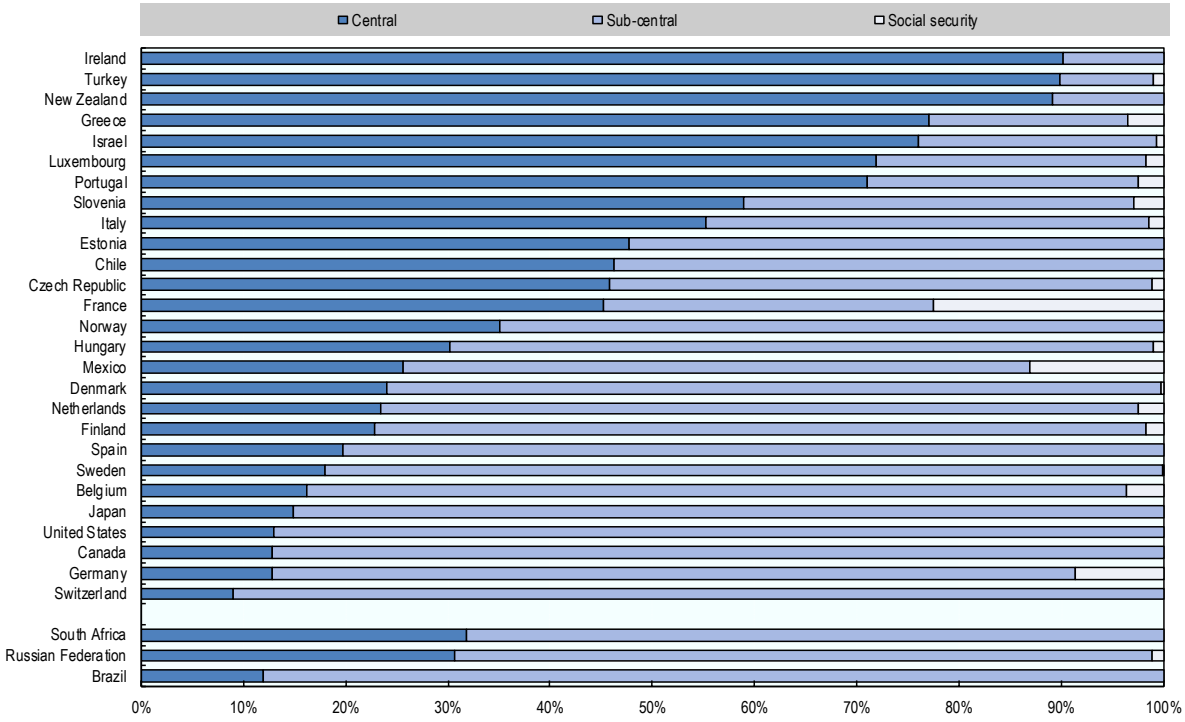


Source: OECD (2015), *Government at a Glance 2015*.

Municipalities are the main employers of the public sector

In 2015, the general government sector employed just over 500 000 public servants of which 46% were employed in the central administration whereas 54% worked in municipal administration (Figure 4.2). Generally, the proportion of staff employed at the subnational level of government is an indicator of the level of decentralisation of public administration. As Figure 4.2 shows, the variance in the proportion of government employees at the central level of government is much larger in unitary countries. Chile has a slightly larger public workforce in municipalities but this probably can be explained by the fact that municipal administrations are responsible for education and health, which are sectors that require large public workforces. Indeed, in 2015 only 32% of the municipal public workforce worked for the municipal administration, 25% in the health sector, and 43% worked in the education sector (Table 4.1). As far as the latter is concerned, there is a consensus among officials and experts that in many municipalities there is excess employment among teachers, teaching assistants and administrative staff (Santiago P. et al., forthcoming).

Figure 4.2. **Distribution of general government employment across levels of government, 2011**



Note: Data for Chile are for 2015.

Source: OECD (2013a), *Government at a Glance 2013*. For Chile, SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM) and DIPRES (2016), Estadísticas de Recursos Humanos del Sector Público 2006-2015, Dirección de Presupuestos.

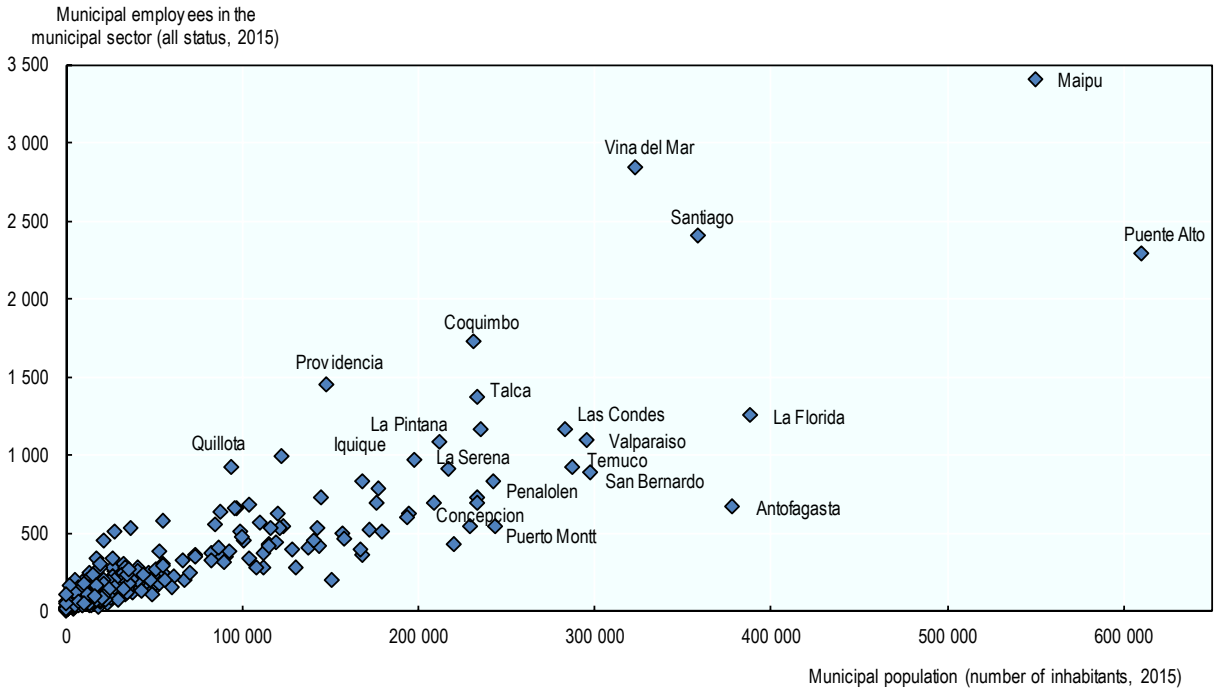
Table 4.1. **Distribution of public employees across levels of government in Chile, 2015**

Sector	Number of personnel	%
Central government	**236 736**	**46**
Municipalities	**274 177**	**54**
- Municipal administration	88 629	32
- Health	68 712	25
- Education	116 836	43

Source: OECD calculations based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM) www.sinim.gov.cl and DIPRES (2016), *Estadísticas de Recursos Humanos del Sector Público 2006-2015*, Dirección de Presupuestos.

In the municipal sector, municipalities count, on average, 257 workers (131 for the median). There is, however, great heterogeneity: 73% of municipalities are under this average, including 37% with fewer than 100 employees. At the other end of the spectrum, 13% have between 257 and 500 employees, 10% between 500 and 1 000, while 12 municipalities have more than 1 000 employees. Santiago, Puente Alto and Maipu, three municipalities of Santiago metropolitan area and Vina del Mar, have more than 2 000 employees (Figure 4.3).

Figure 4.3. **Comparing municipal employees and municipal population (2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM) (www.sinim.gov.cl/). Municipal employees include staff with all statuses (*planta, contrata, honorarios/programas*).

Temporary staff comprises the majority of municipalities' administrative …

To a large extent, Chile has the same structural employment arrangements covering both national and subnational levels of government. This is not surprising as in many other countries, such as France and Germany, it is a way to stress cohesion, internal mobility and whole-of-government perspectives among the staff engaged in the machinery of government (OECD, 2008a). In Chile, public employees are classified as *planta*, *contrata* and *honorarios*.

In the *planta* system civil servants are expected to stay in the service more or less throughout their working life and entry is generally at the lowest hierarchical level. This traditional system is highly inflexible and covers around 30% of municipal employees working for the administration who are hired for life.

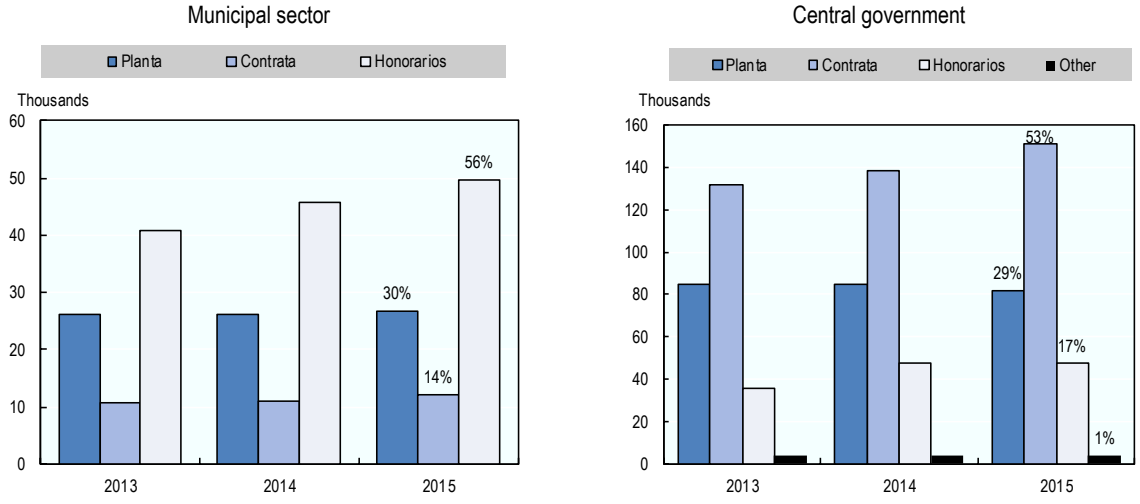
The *contrata* system is more flexible in terms of management as they can enter at different levels of the hierarchy. This system covers approximately 14% of administrative employees who are hired on one-year contracts that can be renewed an unlimited number of times. The share of *contrata* staff is expected to increase with the reforms of Law No. 18.833. Interviews for this review revealed that *planta* and *contrata* staff do not always have clear opportunities for career development and remunerations are low compared to the central government. This reduces the attractiveness of the municipal administration as an employer of choice limiting the possibility to attract highly qualified staff.

Other members of the staff are casual employees known as *honorarios* (consultants or staff on fixed-term contracts) whose contracts can be for up to one year and represent 56% of municipal administrative staff. Hiring staff under the *honorarios* scheme provides

some flexibility (ability to redeploy staff, reorganise work and increase mobility) and mobility, with a broader basis for recruitment in municipal employment; but this flexibility is limited by norms on temporary employees, and on the type of work that can be undertaken in the form of professional services. Moreover, *honorarios* staff is hired depending on budget availability and not on objectives and expected results.

Until recently, the rigid rules that govern the management of the *planta* and *contrata* staff have negatively affected municipal administrations' ability to restructure the municipal workforce to adapt it to their local needs. The problem is that in some municipalities the population increases but municipalities cannot increase the size of the *planta* staff. The large volumes of temporary staff in municipal administrations suggest that there are too few *planta* and *contrata* to perform the duties of the municipality (excluding health and education) so they need to hire temporary staff to acquire the necessary skilled workforce. The large share of temporary staff in the municipal administration (56%) contrasts with the lower share in the central administration (17%).[5] Figure 4.4 suggests that the central government has more flexibility to adjust its workforce through *contrata* (64% of its workforce). This offers them better working conditions than those of *honorarios*, thus making the central government more attractive to highly qualified candidates. The reason is that *honorarios* are not officials and thus they are not entitled to the benefits enjoyed by public servants.

Figure 4.4. **Breakdown of staff according to their status in the central government and in the municipal sector**



Note: In the municipal sector the "*honorarios*" group includes the category *Honorarios a Programa* which refers to programmes co-managed with external public entities. For the central government "other" refers to civil personnel classified as *honorarios asimilados a grado, jornales permenentes* and those hired under the Labour Code as reported by DIPRES in www.dipres.gob.cl/594/w3-propertyvalue-23222.html.

Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM) www.sinim.gov.cl and DIPRES (2016), *Estadísticas de Recursos Humanos del Sector Público 2006-2015*, Dirección de Presupuestos.

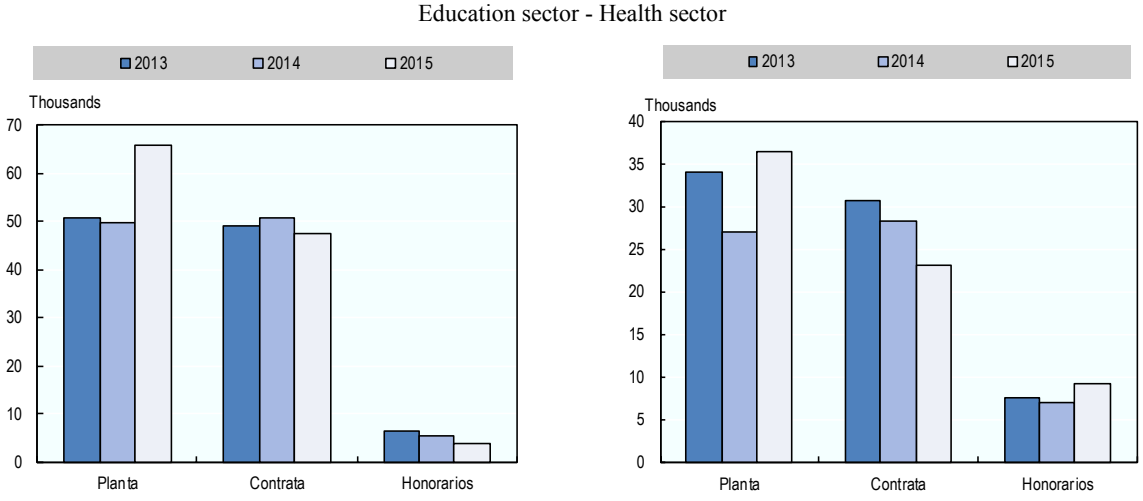
The tight lid on municipal public employment levels and salaries suggests that Chilean municipal public employees are seen as "costs" rather than as "assets". This has been highly problematic for municipal administrations, as this tight control on recruitment has limited their ability to restructure and reskill while also generating job

insecurity and high staff turnover. Improving productivity and capacity while maintaining costs level is a difficult balance for municipalities to strike. The challenge for municipalities is to implement workforce productivity improvements that recognise the balance between costs and quality and continuity of service. For municipal services, continuity of service is a core value related to citizens' trust in government and the public administration.

… whereas more than half of the education and health personnel belong to the planta system.

In sharp contrast to the municipal administrative employees, the education and health sectors have a larger share of *planta* and *contrata* staff. In both sectors, the number of *planta* personnel has been growing in recent years. In 2015, the share of *planta* staff in education and health accounted for 56% and 53% respectively of the total sectoral workforce. *Honorarios* or temporary staff represented 13% of the health sector workforce and only 3% in education. As education and health sectors account for 68% of municipal employment (see above), these sectors absorb most of the financial resources of the municipalities to pay for salaries.

Figure 4.5. **Breakdown of education and health sector personnel by status, 2015**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM) www.sinim.gov.cl accessed on 17 January 2017.

2.5 Restructuring the municipal public workforce through strategic workforce planning

The new caps on the municipal workforce established by Law No. 20.922 intend to give more room for manoeuvre to municipal governments to adjust their public workforce to their needs while at the same time preventing any long-term excessive growth in municipal public employment. To implement these new provisions and avoid seeing the workforce caps as a limitation, municipal governments may wish to engage in strategic workforce planning. This is particularly relevant to municipal governments where the workforce is in constant flux due to flows in and out of public employment. It is especially relevant as municipalities can now modify the structure of the *planta* staff and set a new number of posts and grades (*cargos* and *grados*). Workforce planning can be a

key tool for municipal authorities to plan the composition of the *planta* in numbers and competences and skills in a more strategic manner. It would assist governments in anticipating possible future developments and maintaining a well-structured workforce of an appropriate size, which is able to meet the changing needs of the public service in general in a cost-efficient manner. To define the structure of positions it is necessary to see the functions and tasks that need to be fulfilled as well as the profiles and the number of people required. Strategic planning should go hand-in-hand with workforce strategic planning. A distinction has to be made between the short-term or operational dimension of workforce planning, and the longer term or strategic dimension. In the short term, there is a direct link between workforce planning and operational decisions. In the longer term, workforce planning is instead linked to strategic decisions about where government entities will be a few years down the road.

Workforce planning is not necessarily the same as central or top-down planning. Adequate workforce planning can be developed in any organisation (centralised or decentralised) and by any level of government. At the very least, the municipalities should have the responsibility and be able to monitor employee numbers, costs and competencies. For workforce planning to be effective in Chilean municipalities, however, there is a very strong need to provide for flexibility in the management of the workforce and the strengthening of managerial and HRM capacities. Seeing workforce planning as a continuous process of shaping the workforce to ensure it is capable of delivering the objectives of the municipal development plans is key. Workforce planning should not be overly sophisticated. Its purpose is to avoid rough back-of-the-envelope calculations about future staff needs and encourage more professional linking of human resource management to the municipalities' strategic management.

The National Directorate for the Civil Service (NDCS) could develop a framework for workforce planning that allows for the establishment of government-wide analysis and targets of workforce size, competencies and allocation across sectors. This is especially important for staff in the *planta* system as employees are usually employed for their entire working life. Box 4.1 provides guidelines for workforce planning based on the experience of OECD countries, which could be a source of inspiration for Chile. The NDCS could assist municipalities in helping them take the first step towards strategic workforce planning, particularly in the larger municipalities as a way to pilot the process and create experience. It is important that, during the first stage, efforts focus on administrative staff (*planta, contrata* and *honorarios*), as it would be overly complicated to include education and health staff in such an initiative. The first steps should focus on critical data and emerging trends based on information provided by SINIM. Municipalities, with the assistance of the NDCS would need to consider three aspects:

1. Where is the municipality heading? This involves understanding the strategic context, identifying organisational and business skill requirements emerging from the most likely future scenarios.
2. Where is the municipality now? This involves examining the current state of the workforce and the work programme, the analysis could include an examination of critical workforce data.
3. How is the municipality going to meet its strategic development objectives? This refers to identifying gaps/deviation in current and future workforce capability.

Municipalities should end up with a clear picture of which jobs should be fulfilled by *planta* staff, which ones by *contrata* and which ones with *honorarios*. This includes the

competencies and skills that the municipality requires in-house permanently. Some specialised skills may have to be acquired through *honorarios* and the municipality should be prepared for that.

Box 4.1. **OECD guidelines for designing, implementing and assessing workforce planning**

There is no single approach to workforce planning that can succeed in all countries; rather each model needs to be adapted to the relevant political and institutional context and be seen as part of a learning process. The experience of OECD countries suggests that to introduce workforce planning countries need to consider the following:

Design a workforce planning strategy

- **Have a clear vision and objectives**. It is critical to know from the outset the main objectives and goals of government and how the public workforce is expected to contribute to achieving them. There should be clarity of purpose and of expectations.
- **Restructuring the public workforce requires a "scalpel approach"**. If the need is to contribute to fiscal consolidation then recruitment could be slowed down and be more focused on areas of need including at senior and entry levels.
- **Be pragmatic**. To be effective, workforce planning needs to be flexible, ongoing and sensitive to the different and evolving needs of units. The objective needs to be changed as needs change so that it is seen as building a context for decision making, not predicting the future.
- **Align workforce planning and the budget process**. Budget and HR people need to be in constant communication and co-ordination. Staffing levels tend to be defined according to budget availability and not according to objectives and expected results.
- **Involve key stakeholders** to create a deep understanding of government's needs and objectives and the way to achieve them.
- **Ensure a fair, transparent and evidence-based decision-making process**. This is essential to improve understanding of the workforce planning proposals, what is trying to be achieved, and how people will be affected.
- **Keep it simple**. Workforce planning should not be too ambitious in its objectives. This is particularly important if experience on workforce planning is limited.

Implementing workforce planning

- **Ensure management flexibility** to change the profile of the workforce according to changing needs - priorities.
- **Build incentives for managers to engage in workforce planning** by linking workforce planning to management accountability frameworks.
- **Ensure consistency in HRM implementation** to attract and retain qualified staff, ensure all public employees know the "rules of the game".

Box 4.1. **OECD guidelines for designing, implementing and assessing workforce planning** *(continued)*

- **Develop HRM skills to do workforce planning** by training and retraining HR staff in the relevant skills. Having HR and management capacity for workforce planning is key.
- **Address workforce issues and revise the HRM process** such as: retention of staff through more flexible work practices, investment in learning and development, improving the attraction and recruitment strategies.
- **Leadership is important** to push the implementation of workforce planning if it is to be successful.

Assessing workforce planning strategies

- Workforce planning needs to be adapted to changing circumstances.
- Monitor and evaluate the workforce planning strategy.
- Manage expectations.

Source: Huerta Melchor, O. (2013), "The Government Workforce of the Future: Innovation in Strategic Workforce Planning in OECD Countries", *OECD Working Papers on Public Governance*, No.21, http://dx.doi.org/10.1787/5k487727gwvb-en.

Workforce planning should be done by municipalities individually. There is a large diversity in the municipalities that needs to be taken into account. Urban municipalities may require more staff specialised in auditing, administration, and finances whereas smaller municipalities with high levels of poverty may need more specialists in social work.

Using SINIM as a strategic workforce planning tool

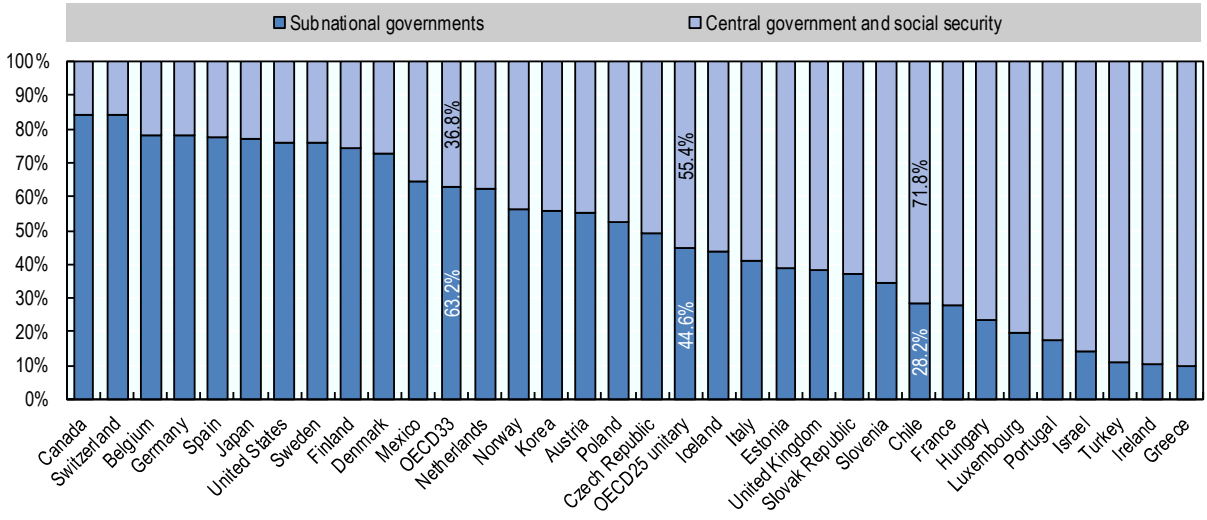
Municipal workforce planning in Chile could be based on the National System of Municipal Information (SINIM). This database shows a clear picture of staff numbers, compensation costs and some management indicators. Information is detailed by municipality and is available on the Internet (www.sinim.cl). This database has been key to control and prevent excessive growth in the municipal workforce in the long-term. The issue for Chile is to continue keeping a detailed account of municipal staff numbers and costs in the context of the implementation of Law No. 20.922. Moreover, Chile could use this database to put the accounting of public employees in a more strategic perspective. This is not only an issue of control and good book-keeping. These are data that have to be used by decision-makers when deciding how to deliver services through municipalities and how to manage their workforce accordingly. One possibility for Chile is to use the SINIM as a public service observatory like that of France. The observatory has a proactive publication policy with an annual publication on the state of the public service, which has become a reference for decision makers engaged in government reforms.[6]

Strengthening municipal governments' capacity

Public expenditure on municipal personnel is low compared to OECD countries

Spending on municipal personnel represents 28% of public staff spending in general government, which is low compared to the OECD average for all countries (63%) as well as to the OECD average for unitary countries only (45%) (Figure 4.6). This level is all the more surprising as municipalities employ a large share of education and health workers that usually weigh considerably on public spending. In fact, this apparent paradox comes from the fact that numerous education and health workers also belong to the private sector, due to the privatisation of education and health sectors that which took place in parallel to the decentralisation process (see Chapter 1). The other explanation is the low level of qualification of municipal staff combined with lower salaries than in the central government sector. It confirms that municipalities have very restrictive means to perform their duties, in particular insufficient resources to hire talented workers.

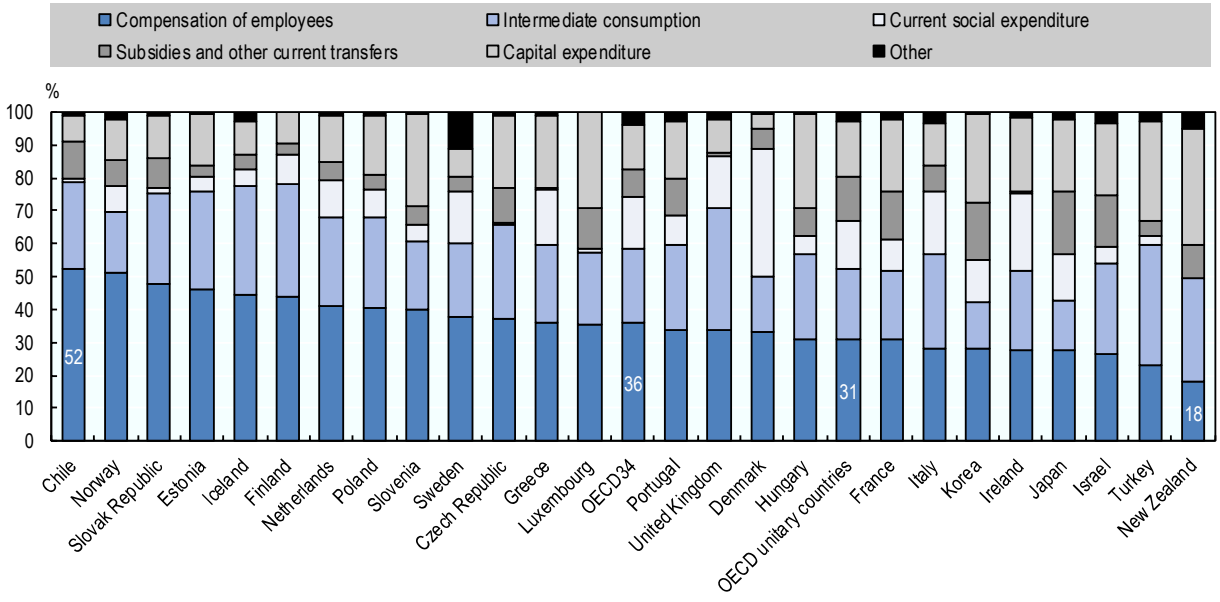
Figure 4.6. **Subnational staff expenditure as a share of total public staff expenditure**



Source: OECD (2016a), *Subnational governments in OECD countries: Key data* (2016 edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

However, municipalities spend, on average, over 50% of their budget on staff spending for the three sectors (Figure 4.7). This constitutes the largest share of the subnational governments' expenditure across the OECD countries; the OECD average is 36% and 31% for unitary counties only. Only Norway spends as much as Chile on compensation, but Norway has one of the largest public sector workforces in the OECD and most of the goods and services are provided by local government. Interestingly, in November 2016, for example, municipal staff expenditure (including health and education) was broken down as follows: 47% was for *planta*, 22% for *contrata* and 32% for other staff including *honorarios*.[7]

Figure 4.7. **Structure of public expenditure at the subnational level, 2014**
OECD unitary countries



Note: 1) 2013 figures; 2) 2011 figures. Other (*) refers to paid taxes, financial charges (including interest), adjustment for the change in net equity of the households in the pension funds.

Source: OECD (2016a), *Subnational governments in OECD countries: Key data* (2016 edition) and OECD Subnational Government Structure and Finance, OECD Regional Statistics (database).

Municipalities fail to attract and retain talent due, in part, to low pay

Interviews for this review showed that due to low salaries, limited opportunities for career development and training, and the complex political environment municipalities are experiencing problems to recruit and retain a talented and highly trained workforce. The perception is that salaries are much lower in municipalities than in the central government, particularly at professional and management levels. The salary gap widened with the development of the senior civil service programme (*Sistema de Alta Dirección Pública*) that does not cover municipal managers. Thus, low salaries only allow municipalities to recruit a less experienced workforce. In small municipalities, managerial positions are taken by young professionals who are just waiting for an opportunity to move to a bigger municipality, the central government or even the private sector. The OECD (2012) has found that freezing and/or cutting salaries and wages could affect the government's ability to attract and retain staff, with high performers leaving or forgoing the public sector to pursue higher paid opportunities in the private sector. Low salaries are limiting Chilean municipalities' ability to re-skill their workforce, and are having a negative impact on the morale of staff and managers. According to the information available to the OECD, the recent reforms to strengthen municipal workforce management have introduced provisions so that *planta* and *contrata* personnel in professional and managerial positions receive the same compensation as staff in central government. This may enhance the attractiveness of municipalities as employers and their ability to keep talent in positions with high levels of responsibility. It must be noted that municipalities will not set levels of remuneration, which will continue to be defined by the central government. The provision that nobody can earn more than the mayor remains

but not all mayors earn the same, their salary is defined based on the size of their municipality. Moreover, for the health and education sectors there are different salary scales as different statutes determine the salaries. This makes it more complicated to bring salaries up to the central government level

Wages of municipal public employees are based on a scale of pay and associated benefits. All new hires must fit into this scale as well as the system for promotion. When a person is hired either as staff or in another category, the functions that he/she will be expected to fulfil are stipulated in the corresponding job contract and there are, therefore, no major differences between the national and subnational systems, except the resources assigned to each level of the administrative hierarchy. The organisation of municipalities is determined by their staff structure, which, in turn, determines pay and working conditions, depending on the position within the administrative hierarchy. This also permits the existence of a system of promotion, which is defined as an integrated system for the regulation of employment at the municipal level that applies to all competitively-hired staff members. This is grounded in hierarchical, professional and technical principles that guarantee equality of entry opportunity, the dignity of municipal employees and their objective evaluation on the basis of merit and seniority. The pay scale is based on administrative hierarchy, divided into division directors, professionals, heads of department, technicians, office staff and support staff. On this basis, staff members have a right to receive a basic wage and remuneration. Other benefits such as expenses for work trips, transport, overtime, seniority and family benefit, etc. also exist.

Municipal public employment attractiveness could be improved through competitive salaries

To make salaries fairer and more competitive at the local level, the Law No. 20.922 included provisions to increase the salaries of professional and managers in municipalities in the *planta* system (28% of the *planta* staff in 2015) to levels that are on par with wages in the central government. Regarding the non-professional *planta* staff[8] (72% of the *planta* staff in 2015) the reform contemplates their promotion to a one pay grade higher (*grado immediate superior*). The upgrading of the *contrata* staff to the same terms as the *planta* will be determined by the mayor as long as the individual has been working for the municipality for at least five years. It is worth noting that for the vast majority of municipal staff, the reform only involves a one-step promotion. This begs the question of the extent to which this measure will make municipal salaries competitive, as only employees in professional and managerial positions will have a similar salary to the central level.

Municipalities have very little latitude to change the salaries of the non-professional *planta* staff and *contrata* staff. It is understandable that Chile wants to keep the cost of public service low by saving on salaries and wages. However, the experience of OECD countries suggests that it would be advantageous to assess the savings relative to the costs – the loss of institutional knowledge when key employees resign or retire, the time lost by managers and employees who have to deal with the issues related to vacancies and reorganisations, and lost productivity while people acquire new skills and learn new jobs. Possibly the largest cost is the falloff in the performance of the municipal public administration due to the low capacity, and the falloff in the performance of public employees who tend to become discouraged.

Once the measures included in Law No. 20.922 are implemented, Chile may wish to explore different ways to make the salaries of non-professional staff and *contrata* more

competitive. A more comprehensive reform of the salary system should be planned to support municipal human capital plans and their core functions and responsibilities. Furthermore, a new pay programme could be put in place to meet the municipalities' needs for years to come. That is particularly important in government, since there is often opposition to replacing a pay system. It will be essential for Chile to adopt plans that "fit" the municipalities' reality, their workforce plans, and the employer-employee relations climate. For example, in Antofagasta the issue of remunerations is particularly acute, the cost of living is high and public sector salaries cannot compete with those paid by the private sector, particularly in the mining sector (OECD, 2013b). The central and municipal government could also commit to a periodic assessment of the programme and take steps to improve it.

OECD countries' experience suggests that the best programmes are those that enable an employer to attract and retain qualified employees, to provide attractive career opportunities, and to encourage employees to meet or exceed performance expectations. The thinking behind a best practice programme now recognises that the way employees perceive the programme and its management is central to its success or failure. Perhaps one first action for Chile would be to work on having only one pay scale for both the central and subnational levels. That would facilitate mobility of staff across levels of government, as some municipal staff could be transferred to central government and vice versa as part of capacity building exercises. The second action for the central government would be to consider a reform of the compensation system that fosters flexibility and fairness in compensation and is attractive to highly talented people. The reform could follow the principles of the United Kingdom's compensation reform (Box 4.2) that seeks to promote better performance and reward good performers even though financial resources are limited.

Box 4.2. **United Kingdom: Government principles for compensation reform**

The reform of the compensation of civil servants in the United Kingdom is based on these principles:

- Top performers should receive better cash rewards than average performers.
- There should be financial incentives for meeting key business objectives.
- Best performers should take on the most demanding assignments.
- Assessments should be relative to ensure continuous improvement.
- Consolidated pay increases should align with the market.
- Team bonuses and gain sharing should be introduced.

Source: Livingston, D. (2011), "Pay Freeze in the UK Civil Service: An Overview of the Pay Freeze Policies in Place 2011/12-2012/13", Presentation given at the Experts Meeting on Compensation of Public Employees, OECD, Paris, 9 September 2011.

For some municipalities it will be hard to lure talented people from more prosperous areas, the key to getting around this may be to focus on the development of local, homegrown talent. Bringing remuneration in line with local living conditions is essential to retaining the most talented people in the municipality, particularly in those in remote and less favoured areas. But an improvement in salary would have to be accompanied by

other measures such as the provision of training in the locality and working conditions that favour a better life-work balance. For that, Chile's government may be advised to develop a more structured approach to "total reward". It means that all aspects of compensation would need to be analysed: pay, benefits, learning and development, and work environment (OECD, 2012). The last two aspects of compensation could be delegated to municipalities. The aim would be to develop a more versatile public sector salary system at the municipal level with greater scope for managers to adapt the intangible parts of compensation to the business needs of the municipality. This would maintain coherence in salary setting across the public sector and increase the scope for municipal managers to provide attractive working conditions. Municipalities, and in particular managers, need to develop the skills and competencies necessary to rethink the way pay is planned and managed. But that would assume that a certain latitude is delegated to municipal governments to determine pay levels.

Recruitment and promotion are perceived as responding to personal and political factors rather than merit…

Municipal, education and health *planta* staff is hired through a competitive public process in accordance with the norms established by the corresponding statute. In the case of short-term hires and professional services their hiring is at the discretion of the mayor. According to legislation, entry into the Chilean civil service is through a competitive examination for *planta* staff. To guarantee a merit-based selection all vacancies are published and specialised panels are in charge of conducting the recruitment process. There are specific criteria for admission to the civil service, for instance, having a university degree in the case of professionals. Obtaining a promotion is dependent on factors such as training, performance evaluation, qualified experience, suitability for the job and the existence of a vacancy in the case of the *planta* system. Regulations and procedures have been established in order to introduce internal competitive examinations as a mechanism for determining staff promotions among senior officials, professionals, supervisors, and technicians based on training factors, performance evaluation, qualified experience, and position-related skills. However, there seems to be a low level of trust in the HRM system as - most often - recruitment, promotions and position allocation depend on political and/or personal reasons rather than merit (Ormeño Campos, 2011). The problem seems to be that, until recently, the number of *planta* staff could not be modified by municipalities. This forced them to hire new staff with *contrata* or *honorarios* status. For these positions, there is no need to open a competition and appointment is mostly at the discretion of the employer. Thus, part of the challenge consists in incorporating the variable of merit into the municipal administrative culture instead of the current system based personal and political ties.

Vertical mobility is rather limited as the system is still very rigid. There is no movement between the national, regional and municipal employees. Movement across municipalities depends on individual efforts rather than a human resource management strategy. Exchanges of staff, however, might be possible in exceptional circumstances. Personnel in the *planta* system can only be removed from the job if the employee has had two consecutive negative performance evaluations but this rarely occurs. In the case of fixed-term contract staff, they can be dismissed at any time at the discretion of the respective authority or simply by not renewing the contract. A person can make a career in the administration based on the time of service but not because of his or her competencies. There is no upward mobility for municipal employees.

… thus transparency in recruitment and promotions needs improvement.

Although there is a clear and defined recruitment and selection process for *planta* staff through a public examination, the transparency of the process should be enhanced. The idea is to change the perception of political interference and the prevalence of personal links. There are at least three measures that could be considered. First, the integration of the selection committees should have a more representative and participative character. Municipal organs should have representation to give validity to the process, for example, by including the future manager of the person to be recruited. Recruiters and other parts of the administration should be part of the selection committee or, at the very least, part of the panel that interviews candidates shortlisted by the HR analyst. Second, the interviewing panel should make the final decision on the person to be recruited and not the mayor. This would certainly contribute to eliminate perceptions of subjectivity in the recruitment and selection process. The mayor could just ratify the decision made by the panel. As part of the selection process, unsuccessful interviewees should receive feedback on why they were not selected. Finally, as it will be discussed below, to make the recruitment process fairer, people who do not have academic titles should be given the opportunity to participate in the process through the certification of their competences acquired through experience. The use of job profiles rather than job descriptions could be crucial in this respect (see below).

Some municipalities may not have the capacity to conduct sophisticated HRM practices. In this case, assistance provided by regional governments or even external agents such as universities could be considered. This would ensure that the standards and procedures defined in the legal framework are followed. But this has the disadvantage that universities are not recruitment agencies and their involvement could jeopardise the recruitment process. Universities would have to be paid for this and that could be very costly (e.g. Colombia). One option to enhance sophistication, transparency and credibility in the recruitment and promotion processes would be to create special entities in charge of supporting the professionalisation of the municipal workforce. One example would be Mexico's *Institutos Estatales de Profesionalización* (state professionalisation institutes) which are in charge of supporting the professionalisation efforts in their respective states and provide assistance to municipalities.[9] They provide training, conduct research, provide advice on strategic HRM, assess the professionalisation efforts of the different state government bodies, and could act as the recruitment agency for certain positions in the state and municipal administrations. Chile could adapt this model to its political system. The important issue is to organise its financing, which could come in the form of a joint investment between the regional and municipal governments. Another possibility for Chile is to create a central body charged with developing guidelines for a sophisticated selection process and with monitoring and supporting their implementation. One example is the federal selection office in Belgium called SELOR. It advertises the job, receives applications, vets applicants for formal requirements, conducts tests and exams and draws up a ranked list of applicants who have passed the selection process and are eligible for tenured public service. This agency conducts recruitment processes not only for the federal government but also for regional and municipal governments.[10] France established the National Local Civil Service Centre (CNFPT) to recruit and train regional, departmental and regional employees and take on certain missions of a national management centre.[11]

Municipal public workforce: The skills gap

Although there is no shortage of training options for municipal employees, training does not always seem to meet the professional and technical needs of the local public administration. Municipalities still face a gap in competencies and skills in relation to their future tasks and development challenges. The OECD (2013b) found that in Antofagasta, for example, of the urban projects submitted to the regional SEREMI for approval only 28% meet the necessary technical standards. Although this could be due to a lack of professional staffing it also has to do with a lack of training as smaller municipalities such as San Pedro de Atacama have greater success.

To bridge the municipal capacity gap SUBDERE has developed the *Programa de Mejoramiento Progresivo de Calidad de la Gestión Municipal*, as well as a programme to build capacity in developing project proposals. In addition, the ACHM and AMUCh also provide capacity-building opportunities through a variety of seminars, courses, workshops and fora. There is even an online platform for education and training. Since 2015, the Municipal and Regional Training Academy developed by SUBDERE (Box 4.3) has implemented a system of training based on occupational profiles for the municipal sector that have been certified by the National Certification System of Labour Competencies *ChileValora*. However, according to AMUCH (2016), training activities rarely produce visible benefits to the municipal administration, and if they do the benefits are minimal. There seems to be a lack of monitoring and assessment of the impact of training in the municipal administration.

Box 4.3. **Chile's Municipal and Regional Training Academy**

The *Academia de Capacitación Municipal y Regional* is a programme of the Subsecretaría de Desarrollo Regional (SUBDERE) whose aim is to strengthen human capital in the municipalities and regional governments through free training. It provides training to municipal and regional employees in a wide range of areas under three forms: face-to-face (100% classroom training sessions), semi-attendance (programmes taught under b-learning mode i.e. combining classroom classes and non-classroom classes) and virtual spaces (100% e-learning, through a virtual platform and distance learning methodologies). The academy provides three categories of training: management training, skills training, contingent training i.e. one-time focused seminars and courses given by specialists. The academy also provides courses and seminars in partnership with other public institutions regarding specific and/or contingent matters.

Since Law No. 20.742 was published in April 2014, the academy has managed the *Fondo Concursable de Capacitación Municipal* which seeks to develop municipal officials' specific competences, skills and aptitudes, based on annual allocations from the Budget Law. It provides individual subsidies to finance training that leads to a technical or professional diploma. The official who benefits from a grant must perform in the municipality the same number of years spent studying.

The academy intends to take a proactive approach to training. It will do so by diagnosing and anticipating training needs and then build a curriculum focused on developing human capital in regional and municipal government. The academy has developed a number of alliances with academic centres to be able to provide training in any part of the country.

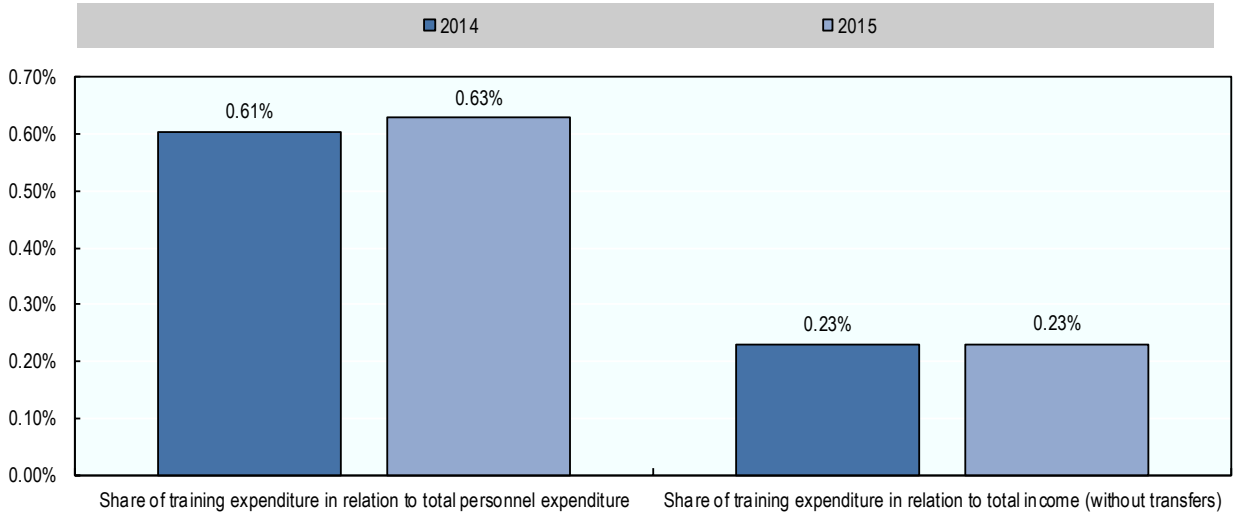
Source: Academia de Capacitación Municipal y Regional, www.academia.subdere.gov.cl/?page_id=2730.

To ensure the workforce has the right skills and competences, Law No. 18.833 requests municipalities to develop an Annual Training Plan establishing their training needs and the way to acquire them. The Plan must be linked to the strategic objectives of the municipality, but not all municipalities have the capacity to conduct such an analysis (either because they are short staffed or lack the technical complexity) and thus training is mostly defined based on perceived needs. Training is divided into three types: 1) training related to promotion and the needs of a new position; 2) training to improve performance in an existing job; and 3) voluntary training that reflects the interest of an employee and is not tied to a particular position.

However, training decisions are centralised within the municipality. Indeed, the mayor, the municipal administrator and their councillors select the staff who will receive training, based on the profile requirements outlined by SUBDERE and municipal needs. The problem is that training does not seem to be valued by senior- and middle managers as a tool to increase productivity but only as way to reward staff for good performance. Municipal employees only see training as way to obtain a certification or degree to improve their remuneration. It is rarely perceived as a way to effect organisational change or contribute to institutional objectives (AMUCH, 2016). Moreover, there seems to be a general reluctance to send staff for training because 1) the municipalities in general are understaffed and cannot afford to hurt productivity; and 2) well-trained staff leave for better and better-paid opportunities, often at the regional or central level given the low wages at the municipal level.

Another problem seems to be the lack of sufficient funding for training in most municipalities. Not all municipalities can afford to set aside financial resources to train their staff. The expenditure on training passed from 0.456% of personnel costs in 2010 to just 0.628% in 2015 (AMUCH, 2016). This means that, in general, municipalities spend less than one Chilean peso/100 on training. Because training is voluntary and unrelated to as specific position, the administration perceives training as providing very little added value. According to the Human Resources Management Handbook (*Manual de Gestión de Personas – municipalidades,* SUBDERE, 2015), training activities must be evaluated in relation to their contribution to municipal objectives. Nonetheless, municipalities lack the capacity - technical and financial - to conduct this kind of analysis and there is no follow-up to the training activities when they are actually provided. Another aspect is that the training method may not be entirely adequate for knowledge and skills transfer. Training is mostly provided through traditional teaching methods, other training techniques such as online and in-service training are not widely used.

Figure 4.8. **Share of expenditure in training in Chilean municipalities (2014 and 2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal (SINIM) www.sinim.gov.cl.

To bridge capacity gaps, municipal training strategy should focus on 'learning and development'…

Given scarce municipal financial resources and a huge need for highly qualified people, Chilean municipalities need to place training and learning at the core of their HRM strategy. Training should be provided at different stages of the public servant's career. Entry-level training would enable new hires to acquire the skills needed for the job; continuous training would enable employees to acquire new qualifications and allow the functional competencies of the workforce to be adapted to changes in the strategic missions of government organisations.

The effective professional updating and re-skilling of municipal public servants is essential to improve municipalities' performance. Training programmes need to be based on learner-centred methods. To this end, OECD countries tend to focus on developing employees' capabilities through continuous learning and development, much of which takes place in the workplace. This is not to say that Chile should abandon formal training completely. The increasing knowledge content of work makes ongoing skill development indispensable. However, as decentralisation progresses, and adaptability, problem solving and innovation become increasingly important for municipalities, training in the skills needed for a particular job should be complemented by other forms of learning to develop a range of technical and behavioural competencies. The notion of "training" should be replaced by the broader perspective of "learning and development". To contribute to the re-skilling of municipal public servants, Chile may consider the following specific actions:

- **Integrate learning and development with other areas of HRM**. Building a culture of learning and development will require changes in other areas of HRM that affect incentives for managers and staff to invest effort and resources. In particular, links need to be created with promotion, career opportunities and performance management. As regards promotion, building up the capacity of the municipal public service will mean giving more weight to recent staff

development (vs. seniority) as part of assessing how well prepared they are to undertake a higher-level role. As regards career opportunities, there is great disparity in the extent to which public servants have access to promotions and therefore in their incentives to engage in ongoing development. Overhauling the career structure to create more pathways for professional growth and career progression is a necessary part of a skills strategy for government. Training plans should consider medium-term programmes with clear goals that are in line with the needs of the municipality and the trainee.

The developmental aspect of performance management should be strengthened using the competencies approach. Municipal managers should be trained in how to assess and address the developmental needs of their staff in order to improve on-the-job performance. At the same time, the right balance must be struck between the "development focus" and the "results focus" of performance management.

- **Update training and development methods**. Given that the majority of the municipal workforce is hired at a very early stage in people's career (recent graduates), investing in initial training is essential. There could be a requirement for a minimum initial training appropriate for the different types of jobs, although some flexibility should be maintained to adjust the training to the needs of the different municipal areas. The Academy for Municipal and Regional Training should ensure that classroom-based training is based on the most modern adult-learning methodologies. Other forms of development – workplace-based activities such as on-the-job training and developmental assignments and secondments – should also be supported. Distance learning should continue to be developed as a means of expanding access to ongoing training. A modular approach to training should be developed, linked to a competency framework.

  Given the geographical dispersion of the municipalities in Chile, it is understandable that the Academy for Municipal and Regional Training provides courses in different regions. However, it is necessary to ensure that those courses are tailored to the needs of the municipalities in that region. Chile could establish a Regional Training Programme for Public Employees based on certification of competencies. In addition, municipalities could use certified private providers. But they should avoid duplication of efforts and focus investment in priority programmes and areas. Quality assurance methods should be applied to both government schools and private training consultants. Universities should be encouraged to set up courses in public management and to develop partnerships with municipalities to provide specialised ongoing development for particular professional and technical groups. Partnerships between universities and municipalities for research and training on municipal administration should be promoted.

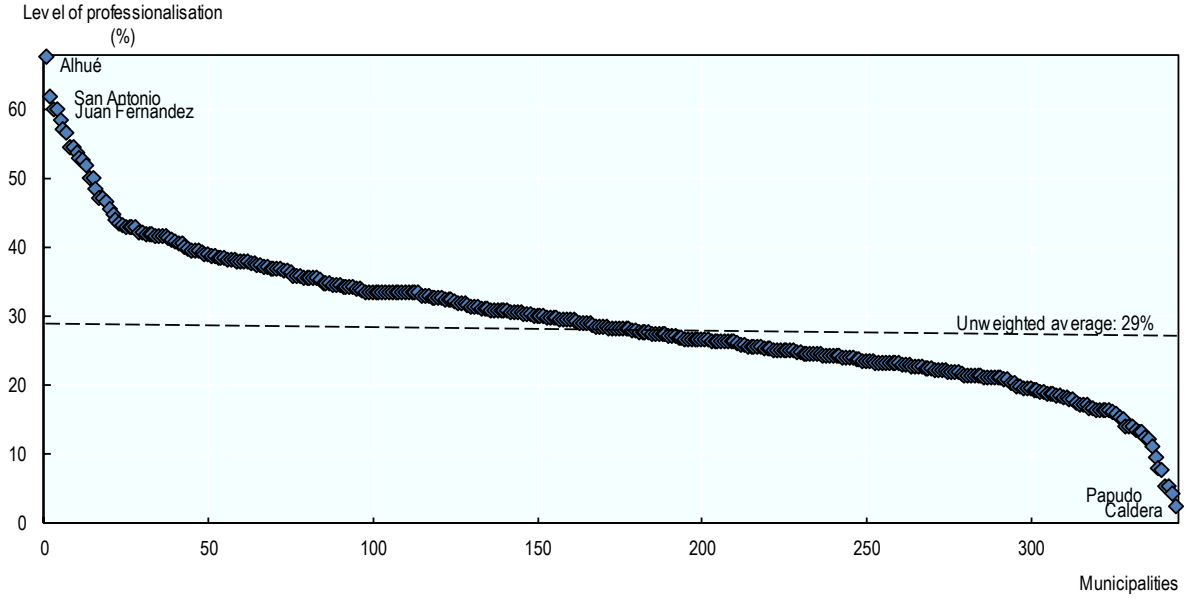
- **Evaluate the cost effectiveness of training**. Evaluation should focus on the extent to which training and development are meeting the needs of the municipality: for example, the percentage of staff deemed to be at acceptable competency levels and whether the skills and qualification profile of the municipality is satisfactory. The national government could develop cost effectiveness measures for training schools to evaluate their training activities: for example, management feedback data on how employees apply what they learn and improve their performance; feedback from municipalities and municipal managers; and cost-benefit data for specific training programmes.

- **Develop municipal leaders and managers**. The Academy for Municipal and Regional Training and the network of other public and private training schools should focus on developing municipal leaders and building managerial capacity. Initial and ongoing development should be linked to core competencies to ensure a common framework for development. A framework for ongoing development should incorporate not only formal training but also a range of other activities, such as networking and executive coaching. It is recommended to establish specific requirements regarding the training and development of municipal managers. This should include introductory as well as ongoing development based on core competencies. In addition, those coming from the private sector should be required to undergo an introductory programme addressing public service values, ethics and the code of conduct.
- **Training should be continuous**. Municipal officials could be required legally to undertake refresher courses at regular intervals to keep their skills up to date or even to certify their competencies. The idea is to institutionalise training and continuous learning in municipal public administrations. Continuous learning could be a requirement for promotions and career movements.

… and promote the development of competencies in the municipal administration.

Chile, like many countries in the region, emphasises college degrees and other formal qualifications to access public employment. The number of professionals (people with diplomas) in the municipal administration has grown slightly over the last five years passing from 25.76% in 2010 to 29.36% in 2015.[12] The Law No. 20.922 intends to increase the number of professionals in the municipal administration by requesting that 75% of new *planta* positions be in the professional and technical groups that require academic degrees or certificates. There are certainly different degrees of professionalisation across the municipalities ranging from over 60% in Alhué and San Antonio to less than 5% in Papudo and Caldera (Figure 4.9).

Figure 4.9. **Level of professionalisation of personal staff (as a %, municipal sector, 2015)**



Source: OECD elaboration based on SUBDERE (2017) Sistema Nacional de Información Municipal, Evolución presupuestaria (SINIM: www.sinim.gov.cl/).

However, focusing on academic degrees to measure the level of professionalisation may not be enough to assess the capacity levels of a municipality. The experience of OECD countries suggests that educational qualification requirements (diplomas) do not guarantee staff will have the right competences to improve performance. People can also be appointed to specific functions if they can demonstrate the necessary competencies (skills acquired off-the-job) even if they do not have the required diploma (OECD, 2011).

With the support of the central government, municipalities could also begin the shift towards 'competency management' and make the HRM process more flexible. There are at least three reasons for this: 1) it helps to define the abilities and behaviours needed for people to do their jobs well (sometimes it is not necessary to have an academic background to work in the public sector); 2) it is instrumental in linking a number of key HRM activities to ensure that an organisation is staffed by competent people who perform effectively; and, 3) it can serve as an integrating mechanism and a lever of change for other areas of HRM. Competencies are generally defined as the combination of knowledge, skills and behaviours that result in good performance in a job. These are usually identified and validated through observation and analysis of what it takes to perform well.

In order to use competencies as a strategic management tool, they need to be integrated into a framework and linked to other elements of human resource management. The links that most organisations tend to make are with recruitment and selection of staff, training and development, and succession planning or career planning, so that these activities are well aligned with the organisation's needs and well integrated with one another. Since municipalities have limited HRM expertise, the central government could provide technical assistance, at least initially. The key aspect of competency frameworks is not their structural design, but the fact that they enable the government to work more systematically and in a more goal-oriented way on workforce planning and on investments in human resources.

Chilean municipalities could use the accumulated experience of *ChileValora* in the certification of labour competencies to define and certify competencies for jobs at the municipal level. *ChileValora* is a way to value experience as competences are certified independently of the manner in which they were acquired. Linking competencies to recruitment, for example, would facilitate access to the public service for people who do not necessarily have academic credentials but who have plenty of experience in their field of. Moreover, it will also ensure that managers and leaders have people with the right skillsets at their disposal, which is critical for managing change in the municipal public administration.

One way to reinforce the work of *ChileValora* and help municipalities develop competency management is the use of job profiling. Job profiling is a valuable tool for applying competencies, particularly in recruitment, and for ensuring a clear link between competencies and outputs. A job profile is a way of combining a statement about what is expected from a job with the competencies that the person doing the job must have in order to deliver the expected results. Many OECD member countries now use job profiles rather than job descriptions in order to focus attention on the outputs or results to be attained rather than on the tasks to be carried out. This signals a move away from rigid, mechanistic definitions of jobs to a more flexible, performance-oriented approach. Job profiles differ from traditional job descriptions – like those used in Chile's *Catálogo de Perfiles Ocupacionales, Unidades de Competencia Laboral y Actividades del Sector Municipal*[13] – in two important respects: 1) they focus on the outputs or results expected

from the job rather than the tasks or functions to be carried out; and 2) they include a statement about the skills and personal attributes needed for the job. Whereas traditional job descriptions tend to be treated as stand-alone items, job profiles lend themselves to integration with other elements of human resource management and with broader organisational and management imperatives. The competencies required are determined by the job profile: for example, behavioural competencies may include aspects such as the ability to work in teams or build networks; if there are managerial responsibilities, competencies would typically include interpersonal skills and leadership abilities. Depending on the type of job, both generic competencies and job-specific competencies may be included in a job profile.

While the goal in Chilean municipalities should be to use competency management as an integrating mechanism for developing HRM, there is a real risk of it becoming unwieldy and overly bureaucratic. There are numerous examples of organisations in both the public and private sectors with large competency handbooks that are not particularly useful to managers or staff. Ways to avoid this situation include: involving managers and staff in defining competencies; reviewing competencies periodically to ensure they are still relevant; focusing competencies on things that affect outcomes for users of public services; keeping it simple – not too many competencies; investing a lot in training managers to work in a competence-based manner.

Performance management in municipalities is weak

Across Chilean municipalities, the culture of performance management is not as strong as in the national government. Law No. 18.833 establishes an evaluation system (*Sistema de calificación*) designed to assess an employee's performance and aptitudes from the perspective of the demands of his/her post and serves as the basis for promotions, incentives and firings. Evaluations are annual and are carried out by an employee's immediate boss and an evaluation commission (*Junta Calificadora*). However, interviews for this review revealed that performance management and performance assessment are mostly viewed as bureaucratic processes and requirements and they are not given the strategic role they could have in the productivity and better performance of the municipality as a whole. They are not used, for example, to diagnose the training needs of the staff and how they could contribute to municipal development objectives, and to improve the municipalities' effectiveness in accomplishing its goals. The management of people is not linked to the institutional goals and strategies of the municipalities. The problem seems to originate in the lack of managerial skills and awareness of the importance of performance management within the municipality's senior management. The *Sistema de Alta Dirección Pública*, a system for senior managers, has been implemented at the central level but has not been extended to municipalities. Municipal managers are not trained to be managers and they are not aware of the benefits of performance management and assessments. It is likely that managers are mostly recruited based on personal and political considerations rather than on their abilities as managers.

In the education sector, in 2003, Chile developed a national framework defining standards for the teaching profession, the Good Teaching Framework (*Marco para la Buena Enseñanza*), which is currently being revised. It also established the teacher performance evaluation system (also referred to as *Docentemás*) within the municipal school sector, following a tripartite agreement between the Ministry of Education, the Chilean Association of Municipalities (*Asociación Chilena de Municipalidades* - ACM) and the Teachers' Association (*Colegio de Profesores*). This system is complemented by

a range of reward programmes, which involve an evaluation, including the Programme for the Variable Individual Performance Allowance (municipal sector only) and the National System for Performance Evaluation (SNED). The latter provides group rewards for teaching bodies in publicly subsidised schools. The teacher evaluation was perceived as an instrument to hold teachers accountable and not as a formative instrument. Teachers received limited feedback from the evaluations, the results were not systematically used to inform a professional development plan including career steps, and the concept of feedback was not fully ingrained among school agents. The system was improved recently through the certification process associated with the transition of stages in the new career structure (cf. Law No. 20.903 on teachers' career): the System for the Recognition of Teacher Professional Development (*Sistema de Reconocimiento del Desarrollo Profesional Docente*). This system will be implemented as of 2017 and will lead to the discontinuation of the AVDI and the AEP (Santiago P. et al., forthcoming).

In 2002, primary healthcare workers across the country advocated for increases in their salaries. In order to drive improvements in primary healthcare performance, Chile decided to adopt a pay-for-performance scheme, which led to the creation of the "Health Goals". The Health Goals are a set of eight goals comprised of ten indicators, which serve as an economic incentive for frontline healthcare workers by providing a bonus in salary for achieving the set targets. Workers have the opportunity to receive bonus wages every three months, ultimately adding up to two months of potential extra payment over the course of a year. The same indicators and "minimum goal" are used throughout the country, but the targets are adapted to the context of each municipality. Development of these Health Goals was a politically complex process, which included working with the Ministry of Health (MoH), Ministry of Finance, the Association of Chilean Municipalities, and the National Union of Workers of Primary Care to come up with the agreed upon indicators and incentives. The goals were developed to target the main health problems in the country and areas with low-compliance.

Municipalities need to place more emphasis on the developmental function of performance evaluation…

It is evident that Chile is interested in bridging the capacity gaps in municipalities. The number of programmes and instruments to assess performance of public employees (including teachers and doctors) is proof of that. However, it is also evident that such efforts have been needlessly hampered by inadequate and inappropriate structures and training of managers. For example, the OECD (2013b) found that performance-based mechanisms are infrequent in Antofagasta. Thus, one of the first actions is to place a stronger emphasis on public employees' evaluation for performance improvement (i.e. developmental evaluation). All human resource management components should be designed to facilitate and promote enhanced performance. They should be part of an integrated, mutually supportive system that generates synergy effects. This will require co-ordinated changes in certain human resource management arrangements. As assessments become an important component of pay rises, promotions and assignments/transfers, it will be increasingly important for all municipal employees to be assessed according to a common model and measured against a common standard. It is not enough that Law No. 18.833 sets the process for performance assessment. It is recommended that the Chilean government continue to strengthen its framework for municipal employees' assessment (preferably by sector) and establish a mechanism for monitoring the implementation of such a framework. Support from the Municipal and Regional Training Academy could be useful in pursuit of this goal. Managers should be

able to manage their workforce in a way that better suits them in meeting their objectives. In this sense, municipal governments, with the support of the central government, should also invest in training managers/supervisors in skills and performance assessment, and support them in their roles as assessors by providing guidelines, handbooks and other forms of support.

Reorienting municipal human resource management towards enhancing performance requires parallel and synchronised efforts at different levels of government in several fields, including managerial competencies and mandates, performance assessments and performance incentives. It often also necessitates increased decentralisation of pay setting (currently decided at central level) and other elements of human resource management. These changes have to form part of a coherent performance management strategy that could be promoted by SUBDERE. Achieving this coherence across policy areas can be a substantial political challenge.

The Chilean government should not expect to get quick results. It will take time for the different stakeholders (managers, supervisors, employees, union representatives, municipal associations) to gain the necessary skills and experience with performance assessment in order to differentiate rewards regarding competence and performance. Instead of attempting a wholesale reform, the government should start small, invest in improved capacity and competency, and gradually expand the role of skills and performance in salaries and promotion.

… and enhance their management capability to improve performance.

As performance and efficiency issues become more urgent in municipal public governance and management, more attention needs to be paid to the role, tasks and capabilities of senior and middle municipal managers. They have a key role to play in improving the performance of the municipal administration and employees. In particular, high-quality middle management is critical to ensure motivation of staff, the acquisition of new skills at work, the well-being of staff, and ultimately their productivity. Middle managers and supervisors must understand the crucial link between the strategic objectives of the organisation, their department or team objectives, and their day-to-day people management, in areas such as communication and consultation; training and development; and conflict, stress and absence management. It is essential that line managers learn the key people management skills necessary for their role. In fact, managers should be promoted not only because of their particular skills or technical expertise, but also because of their ability to actually manage people.

Extending the coverage of the *Sistema de Alta Dirección Pública* (ADP) to the municipal level would be a way to enhance municipalities' management capability. The ADP, since its creation in 2003, has extended to cover more central government agencies. It sets the rules and procedures for recruiting senior officials for central government positions under a transparent and merit–based process. The ADP has served as an instrument to attract highly qualified people from the private sector to the public sector. Thus, municipalities together with the *Consejo de Alta Dirección Pública* would need to define which senior and even middle management positions would be feasible to integrate into the ADP system. In that way, municipal managers would be recruited following the same rules and procedures of those in the central administration. Moreover, information such as descriptions of the skills needed to fill vacant positions and why certain candidates were selected would be made public to increase transparency. Managers would be assessed based on their performance (to what extent they achieved their

objectives) and management skills. Moreover, to limit political influence it would be important to define clear rules for the dismissal of managers in ADP positions. Including municipalities in the ADP would be part of the modernisation process of the system itself. Not all municipalities would be in a position to join the ADP as it will depend on how well organised they are. In a first phase, the largest municipalities could join the ADP system, which eventually would be expanded to mid-sized municipalities.

Certainly, mayors and municipal councillors, since they have a more political role, cannot be part of the ADP system. However, it is important to ensure that all officials have baseline competences in these positions. Attending a training programme could be mandatory for new officials. It could focus on municipal public administration, leadership, communication, negotiation, conflict management, inclusion policies and ethics. The same requirement could be set for senior and middle managers.

Strengthening the HRM function at the municipal level

The enactment of Law No. 20.922 is a positive step towards a process of modernisation of the municipal public administration. However, changes will not be felt in the short term and this reform by itself will not be sufficient to boost municipalities' economic and social development potential. This reform needs to be accompanied by other transformations that can be conducted in parallel. The delegation of authority to municipalities to manage their human resources may be a critical complement to the recently approved reforms.

Delegate HRM responsibility to municipalities to promote flexibility in staff management…

As part of the current decentralisation efforts, Chile could delegate the authority to manage the workforce to subnational levels of government. Municipalities are expected to contribute to the economic development of their region and the well-being of their inhabitants, but most of the time they are unable to adapt their workforce to meet effectively their most pressing needs. The reforms to make the regulatory framework more flexible by allowing mayors to modify the *planta*, the internal organisation of the administrative structure and the hierarchical levels are steps in the right direction. But more could be done to make public workforce management at the municipal level more flexible.

The experience of OECD countries suggests that people work better and contribute more if they are motivated, rather than merely ordered, to do their work. In order to manage their people in an appropriate and constructive manner, municipalities need to develop a human resource management strategy and for that they need to be able to decide on four key dimensions: 1) values, norms and management style; 2) the structure of the organisation, job roles, reporting lines and accountability mechanisms; 3) staff skill levels, development potential and management capability; and 4) the people-focused mechanisms which deliver the strategy. The key human resource systems have to include workforce planning, employee selection and development, career management, employee rewards and motivation, among others. There is no single best way of designing these systems, they have to be adapted to the local context and in particular some small municipalities with little capability will find it particularly challenging. Thus, delegating HRM responsibility could be done in an incremental way, starting with municipalities that have greater managerial capacity.

The key motive for delegation is the need to enable municipalities to adapt their human resource system to their needs and objectives. Municipalities should be able to determine how many employees they need, and which skillsets these employees should have. They need to be able to decide when to use contractors and purchase services. This type of delegation might also entail a right to adjust headcount whenever there is a justified need (and not just every eight years). On recruitment, municipalities should be able to decide the required competences and selection criteria, which is important for manpower planning. As a rule, the design and operation of the pay system is decided at the central level with little latitude for municipalities to modify pay structures or pay levels. Chile may wish to consider granting some leeway to local governments to adjust pay to make their salaries more competitive and attractive. This would be subject, of course, to an appropriate financial framework. Box 4.4 shows how other OECD countries are approaching this issue.

Box 4.4. **OECD countries' experience on delegating pay-setting to subnational governments**

The OECD has found that there are several reasons why a national government may seek to influence or control remuneration and other employment conditions for staff in the subnational administrations: 1) differences in employment conditions might hamper a desired mobility across public administrations and government levels; 2) limit or cap the growth of public expenditure; or 3) ensure coherence in public employment conditions. Countries are using a number of instruments to oversee municipal payrolls while at the same time granting them flexibility to set their own wages.

- In **Spain**, the law that regulates the civil service also regulates the structure of the pay system for civil servants at both national and subnational levels. The annual increment of the wages is contained in the general state budget. Contracted employees are employed under normal labour market conditions.
- In **France**, each local government can determine remuneration and other employment conditions for its employees, but their actions are regulated by law and by the fairly complex regulations for the French corps (or career) systems.
- Subnational governments in **Denmark** set their own wages. However, the State Employers Authority has an informal, ongoing dialogue with municipal and regional associations that function as central employers for the subnational administration. The State Employers Authority is also represented on the municipal and regional Boards of Wages and Tariffs that function as employer representatives in negotiations with the unions in these sectors, and has veto power on the regional board.
- In **Belgium,** subnational governments set their own wages. The national government has no possibility or even legal capacity to introduce or strengthen a framework for controlling or capping overall compensation costs. There are mechanisms for co-operation and consultation but they are not very formalised.

Measures to control subnational government remuneration are largely interchangeable with measures to control or discipline subnational government spending due to the dominance of labour costs in subnational government expenditure. National controls on subnational remuneration seem however to be much more common than establishment controls. Trade unions also typically strive for coherent remuneration structures when negotiating pay contracts.

Source: OECD (2008b) *Challenges of human resource management for multi-level government*, Public Employment and Management Working Party.

It is important for municipalities to motivate their employees. This includes a need to be able to reward them for good performance and behaviour and be able to sanction misconduct and unsatisfactory performance. This can be done in different ways but some delegated control over monetary rewards is probably indispensable. If Chile wants to continue managing pay-setting centrally, it may consider delegating the handling of special performance-related pay elements or other variable pay elements to municipal authorities.

Delegating HRM authority will not be without its challenges for Chilean municipalities. This issue always comes with its dose of controversy and complications. Delegation will entail a major cultural change, but the national government and the municipalities need to be convinced that the public service ethos and the political system can be maintained even after the delegation. Chile would not be moving to a federal system with these changes. Another challenge is the need to develop and maintain sufficient managerial capacity and competence in the municipalities for handling their own public workforce. But managers' lack of training and experience in HRM and the absence of professional HRM units are critical drawbacks. A final challenge for Chile will be to avoid the creation of small *planta* systems that are inflexible and inefficient. Chile needs to avoid the creation of islands of un-modernised management due to the different capacities across municipalities. Unwarranted differences in employment conditions may also cause dissent and inefficiencies.

The positive outcome of delegation of human resource management is by no means a given. The lack of sufficient managerial capacity and competence in municipalities could prevent the expected benefits from materialising. Even the planned reforms are at risk due to these deficiencies. A delegation of HRM responsibility must be thus accompanied by adequate capacity-building in every municipality in the form of both managerial development and the setting up of professional human resource management units. This delegation can be also done in a gradual and differentiated way according to municipal capacities and learning process (asymmetric process).

… but accountability mechanisms are required.

The delegation of HRM responsibility is never total. Governments typically still want to maintain a set of shared values and common structures and processes, and this needs to be managed from the centre. The central government would still need to monitor the development, since unwarranted differences in conditions between different parts of the public administration are potential sources of dissatisfaction and inefficiency. Municipal authorities would have to be accountable to central government for the handling of human resources. It may be a paradox but delegating authority over HRM to municipalities and making it more flexible may need to be accompanied by a strengthening of certain central functions like the oversight of municipal public administrations. This is the role that the National Directorate for the Civil Service may want to assume.

If responsibility for the management of the municipal workforce is delegated to municipal governments, they need to be accountable for their new responsibilities. For this purpose, the central government needs to develop and implement reliable mechanisms for accountability and transparency for oversight and also for feedback. There should be a requirement by law to hold municipalities accountable for the management of the workforce, ensuring joint action, common standards, and shared systems. The National Directorate for the Civil Service could play a leading role on this issue. Certainly, these mechanisms should not limit the room for manoeuvre of

municipalities to adapt their workforce numbers and shape their staff profile to meet their own needs.

Municipalities need to innovate to build capacity and take on new responsibilities

Chile is in the process of decentralising functions to regional governments. This review argues that municipalities should also be part of this process. Chile has 346 municipalities, although this number is not huge compared to countries such as France, their size varies a great deal. Many are small, have limited resources, and can be assumed to be unable to take on any more responsibility. If Chile wishes to extend the decentralisation process to municipalities, one prerequisite for transferring responsibilities and competences to them is to ensure that the municipalities are capable of handling the new responsibilities and competences. Other countries have faced similar situations. One measure they have adopted is to merge several small subnational governments into economically viable units better able to provide adequate local services (i.e. Belgium and Denmark). It may be politically difficult to do this in Chile as municipalities are already quite large and their ability to resist mergers depends on their level of autonomy, yet resisting calls for decentralisation is becoming increasingly tenuous.

One way Chile could strengthen the capacity of its municipalities would be to establish associations of neighbouring municipalities. For example, in Iceland, two or more municipalities can join forces to provide with particular services, mostly in connection with joint projects that entail greater efficiency and lower costs. Examples of such co-operation include homes for the elderly, waste management and pollution prevention, co-operation in the field of culture, sports, public transport, fire services, environmental health, sewage, water and electricity works and central heating. Also, in Germany, it is common for municipalities to pool their resources to perform specific tasks jointly. They also, to an increasing extent, co-operate in management and administration duties. The latest trend is the joint provision of services in what is called back offices, which are organised jointly by several municipalities. German municipalities often form what is known as joint authorities (*Zweckverband*) to co-operate. Chile should note that inter-municipal co-operation of this nature is often voluntary, based on shared interests, arranged within a legal framework, and allows each municipality to retain its own identity (OECD, 2008a). This type of co-operation would imply sharing human resources across the municipalities for the specific services that are delivered jointly.

Municipalities lack HRM professionals

Not all municipalities have an HRM unit, and HRM-related work is done by intuition. In some municipalities, public servants have to conduct a wide array of functions and HRM work could be just one of the several duties they have. It is rare to find staff members who are specialised in defining competencies and job profiles, or even setting up an annual training plan. HRM mostly consists of daily paperwork and is therefore quite bureaucratic in nature. There is no evidence that people working in HRM received training to become HRM professionals. Attracting HRM professionals from the private sector is a complicated task. One of the problems is the centralisation of the bread-and-butter HR functions, as the central government sets most of the basic pay, benefits, leave, etc. for all government employees. This leaves very little room for innovation and flexibility in the management of the workforce according to local needs. Municipal government is therefore not seen as a career advancement option for HR professionals as it could be in the central government. It could also be argued that managers and political leaders in municipalities do not see HRM as a strategic function that could help them to

achieve the goals of the political agenda. Financial constraints are another reason so few municipalities have HRM units.

Municipalities need to professionalise the HRM function

There is a substantial capacity gap in Chilean municipalities, which government should close through co-ordinated efforts across different areas of human resource management, such as competencies, job profiling, workforce planning, recruitment, training, remuneration and performance management. For that, it is essential to professionalise the HRM function in municipalities. This means that HR professionals should be given the opportunity to develop a career in the public service at both the central and subnational levels. It is true that the HRM function is a support service to the core functions of government, but managing the public workforce effectively is essential in helping municipalities reach their goals. HR professionals should work closely with municipal authorities to achieve strong leadership, build capacity for core functions, and support managers to get the best out of their people. They would need to be responsible for co-ordinating the workforce planning efforts in close co-operation with the senior and middle managers within the municipality. HRM professionals should be in charge of co-ordinating the job profiles and skills and competencies of the new *planta* staff recruited based on the new law and the current municipal priorities. Municipalities need to install an HRM unit as part of their organisational structure and give the unit an integral role in enabling change and supporting improved public service delivery. The HRM function should be seen not as in charge of the paper work, but as a strategic function that facilitates the operation of the municipal administration.

If the HRM function in municipalities is going to be strategic, traditional HR expertise must be combined with an understanding of how it can help meet the strategic goals of the municipality. Thus, it would ideal if, at a later stage (i.e. once HR units are consolidated), HR experts could have access to a range of career paths, similar to those of other professionals. In other words, the HR career path must make it possible for HR professionals to stay in their positions, move sideways to gain broader experience, take on a bigger role, or (temporarily) move out of the municipal public service and go to the central government or even the private sector. This could be central to attract HR professionals to municipal employment in addition to offering an attractive remuneration package. The new law is expected to facilitate careers in the municipality and acknowledging the work of municipal employees and HR professionals could be part of these efforts. It is important for municipalities to develop a profile for the HR profession, which *ChileValora* could certify. In this sense, the experience of the Cabinet Office of the United Kingdom in setting professional HR standards as part of its Professional Skills for Government Agenda could be of inspiration to Chile. The important point is to define what is expected of HRM professionals and how to measure their performance. HR professional standards set out the requirements for HRM professionals in four key areas: 1) knowing the business; 2) demonstrating HRM expertise; 3) acting as a change agent; and 4) building personal credibility. Each of these areas is calibrated at three different levels of expertise, which are cumulative.

Box 4.5. **Key recommendations for modernising human resource management**

1. Develop workforce planning and management:

- Engage in strategic workforce planning as a tool to plan the composition of the municipal workforce in terms of numbers, competencies and skills, particularly in light of the new *planta* law.
- The National Directorate for the Civil Service (NDCS) could develop a framework for workforce planning.
- Continue keeping a detailed account of municipal staff numbers and costs in the context of the implementation of Law No. 20.922.
- Use SINIM to put the accounting of municipal public employees in a more strategic manner.

2. Strengthen municipal human resources capacity:

- Make municipal salaries of non-professional and *contrata* staff more attractive and competitive through a more comprehensive reform of the salary system. It could include a new pay programme to meet municipal needs for years to come.
- As part of the total compensation package include provisions of training at local level and working conditions that favour a better life-work balance.
- Enhance transparency in recruitment and promotion through: 1) selection committees that are more representative and participative; 2) the interviewing panel should make the final decision on recruitment, not the mayor; and 3) do not focus exclusively on academic degrees to assess the candidate profiles.
- To ensure a more sophisticated, credible and transparent recruitment process, special entities in charge of supporting the professionalisation process could be created.
- Municipalities could establish a training strategy focused on learning and development.
- Promote the development of competencies in municipal administration; the use of a competency management framework, and job profiling could be considered.
- Municipalities need to emphasise the developmental function of performance evaluation by shifting human resources management to a performance-driven culture.
- Invest in the management capability of municipalities at senior and middle management levels.

3. Strengthen the HRM function, by:

- Delegating HRM responsibility to municipalities to promote flexibility particularly in relation to the composition and restructuration of the workforce and certain elements of compensation.
- Establishing an accountability mechanism to monitor the management of human resources at the municipal level.
- Promoting innovation to build capacity at the municipal level through the establishment of municipal associations for greater efficiency and lower costs in service delivery through shared functions in HRM.
- Professionalising the HRM function at the municipal level by incentivising HR professionals to dedicate their career to municipal administration, based on HR professional standards.

Enhancing the quality and efficiency of municipal services in Chile

Improving municipal management and performance is a key piece of decentralisation reforms. Inefficient municipal administration often directly leads to poor service provision. Poor service typically reflects both insufficient capacity and resources to carry out subnational responsibilities. Decentralising involves reforming municipal financing but it also implies better service performance both as a pre-requisite for further delegation of competencies to subnational governments, but also as a learning-by-doing process. Municipalities will provide better services only if they have the opportunity to do so. This is also part of the process of transforming municipalities from being service providers to veritable local governments. Subnational capacity to handle actual or new responsibilities is one of the biggest roadblocks on the road to decentralisation reform in Chile. Improving municipal management can help pave the way.

Better quality public services can lead to more satisfied users, which, in turn, can increase trust in government. At the same time, more equitable access to effective public services, such as social programmes, infrastructure, healthcare or education, provides citizens with a means to connect to social and economic networks, and thus access opportunities. In addition, improving access to services for citizens across areas may also reduce territorial disparities. Governments across most OECD countries and beyond are constantly working to improve public service production and delivery in order to meet the increasing expectations of the population, while addressing the need to expand access for all citizens, regardless of income levels, location or other social and economic determinants (OECD, 2016b).

Strengthening municipal services management in Chile

Chilean municipalities are responsible for a wide range of services at the local level. The Organic Law on Municipalities identifies a number of exclusive and shared responsibilities to be carried out by all municipalities regardless of their size and specificities. Overall, Bernstein and Inostroza (2009) have identified 75 services that municipalities should provide related to community services, taxes, transport, security, urban development, social development, education and health, among others (see Chapter 1). This broad landscape of municipal responsibilities entails important challenges: on the one hand, the provision of municipal services strongly depends on different and specific management strategies, especially for shared responsibilities; on the other hand, the heterogeneity of local capacities across the country, rendering uniform service delivery defined by law unrealistic and often impossible (see Chapter 1) (OECD, 2013c).

Assessing municipal service provision and management

Chile has made significant progress to improve municipal services through management models implementing a framework for Quality Management Programme for Municipal Services (*Programa Gestión de Calidad de los Servicios Municipales*). These efforts started in 2006 with the Certification System of the Quality of Municipal Services (*Sistema de Acreditación de la Calidad de Servicios Municipales*). Adopted by almost 100 municipalities, this system was framed by two Management Models: 1) the Management Model of Municipal Service Quality that defined three "management levels" through a scoring system; and 2) the Model for the Progressive Improvement of Municipal Management, a simplified version of the first model targeted to municipalities with intermediate or low "management levels". The system was structured around a set of procedures and methods to support, guide, and encourage municipalities to undertake

continuous performance improvements. Its multi-step certification process started when a municipality enrolled voluntarily in the programme. The main goal of this monitoring and evaluation programme was to certify governance processes that met quality standards. It also provided essential support to municipal actors responsible for public service provision.

Substantial progress has also been made to continuously diagnose local management of service provision. To complement the implementation of management models, SUBDERE has implemented four rounds of the National Diagnosis of the Quality of Management (*Diagnóstico Nacional de la Calidad de la Gestión*), which provides a complete picture of the current state of local management (Box 4.6). With 78 questions for municipalities, it provides a diagnosis of 12 different issues, among them leadership, capacities, well-being at work, and municipal budget. Two specific programmes to improve service quality are directly linked with this diagnosis – the Programme for the Continuous Improvement of Service Quality (*Programa de Mejoramiento Continuo de la Calidad de los Servicios Municipales*) developed by SUBDERE with the ACHM, the ASEMUCH and the National Centre of Productivity and Quality ChileCalidad (which no longer exists) in 2007 and the Programme of Progressive Improvement of Municipal management (*Programa de Mejoramiento Progresivo de la Gestión Municipal*) of 2009 (Figure 4.10). The diagnosis of 2015 shows that municipalities that have applied these programmes obtain better management results than those that did not.

Box 4.6. **Diagnosis of the Quality of Municipal Management**

Within the framework of the Quality Management Programme for Municipal Services, SUBDERE, in collaboration with the National Centre for Quality and Productivity ChileCalidad, designed in 2010 the instrument "Diagnostic of the Quality of Municipal Management", with the purpose of measuring management levels of municipalities. The diagnosis considers 12 areas of management with 78 self-assessment questions. The questionnaire has been conducted four times since 2010 and, from 2015, on a yearly basis with a high rate of respondents each time. Since 2015, the data compiled through this questionnaire, serves as an input to assign the Incentive Fund for Municipal Management (*Fondo de Incentivo a la Gestión Municipal*). The three main objectives of this instrument are: 1) know and assess current management quality so it can improve in the future; 2) promote the creation of spaces of collaboration within the municipality linked to organisational improvements; and 3) build information to design a roadmap to overcome management gaps and improve service provision.

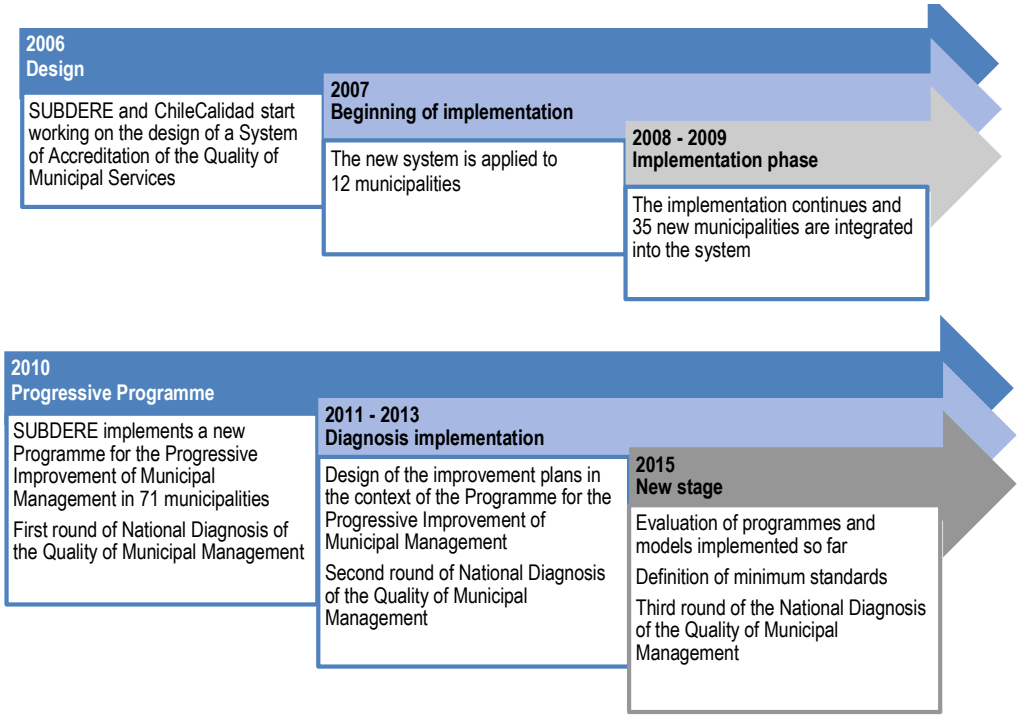
The two areas that typically receive the highest scores are "Leadership", which refers to how municipal directors conduct and evaluate internal performance, and "Municipal Revenues", which refers to how the municipality manages its revenues so it can ensure that efficient processes safeguard the long-term sustainability of its finances. The two areas that have received the lowest scores since 2010 are "Training", which refers to the way in which the municipality manages staff education and training, and "Service Provision Processes", which refers to the key aspects of the processes of service delivery. Municipalities that have applied the *Modelo Gestión de Calidad de los Servicios Municipales* always receive better scores.

Source: SUBDERE (2016a), *Análisis de Resultados Diagnóstico Nacional 2015*, Calidad de la Gestión Municipal.

As part of the decentralisation reforms, SUBDERE is moving towards a new paradigm of performance management and service delivery at the local level. In 2015, as part a presidential priority, the government started the revision of the Certification System

moving towards a System for Strengthening and Measuring the Quality of Municipal Services (herein after the System of Municipal Services) in order to create a structure that better meets the needs and requirements of municipalities (RIMISP, 2016). For this, the government signed in 2014 Memorandum of Understanding (MoU) between SUBDERE, the ACHM and the ASEMUCH for the modernisation of the Municipal System and set up a Municipal Technical Advisory Committee (Comité Técnico Asesor Municipal, CTAM, see Chapter 1). CTAM involves other institutions such as the National Committee of Councillors (Comité Nacional de Concejales), the IADB, the ILO, the Centre of Public Studies (*Centro de Estudios Públicos,* CEP), among others. This new system, while not yet officially implemented, seeks to resolve some of the shortcomings in the Certification System, recognising the continuity and progression of these reforms. The new System of Municipal Services focuses particularly on the definition of guaranteed minimum standards to reduce territorial disparities (see below) as part of a presidential commitment.

Figure 4.10. **Progress of the management of municipal services**



Source: Created by the OECD based on information provided by SUBDERE.

Health and education services at the local level

Two of the most important services provided by municipalities or municipal corporations are primary and secondary education and primary health (see Chapters 1 and 2). Both services follow national guidelines defined by line ministries.

Quality in education is outlined by the National System of Quality Assurance (*Sistema Nacional de Aseguramiento de la Calidad, SNAC*), which provides Indicative Performance Standards for educational establishments. These standards are a set of references that constitute a guiding framework for the evaluation of the educational

management processes of the establishments and their supporters. These are included in the requirements stipulated by the SNAC, and were designed with the purpose of supporting and orienting establishments in their continuous improvement processes (Ministry of Education, 2014). The Indicative Standards are the basis of the Indicative Performance Evaluation conducted by the Education Quality Assurance Agency (*Agencia de la Calidad de la Educación*) whose remit is to provide recommendations for institutional improvement and a framework of best practices in education management.

The institutional framework and standards for education services are clearly defined and allow some autonomy for local management. For the development of education standards, the SNAC has a clear institutional landscape. The system includes four institutions responsible for ensuring the quality of education, the continuous improvement, and the promotion of management capacities: The Ministry of Education, the oversight body Superintendence of Education (*Superintendencia de Educación Escolar*), Education Quality Assurance Agency, and the National Council for Education (*Consejo Nacional de Educación*). The standards and recommendations provide a guiding framework and are therefore not mandatory. The non-mandatory nature of the Indicative Standards is one of the guiding principles of the SNAC providing a certain degree of autonomy to the education establishments over their management process. In this scenario, when municipalities manage a school, they can determine which measures respond better to their reality to improve performance (Ministry of Education, 2014).

For health services, municipalities must also uphold standards defined by national entities. Municipalities are responsible for managing primary care centres (*Atención Primaria de Salud*), which are also subject to standards and evaluations from the Ministry of Health. Health services in Chile are framed by the Guaranteed Plan of Health (*Plan Garantizado de Salud* GES/AUGE). The plan clearly lists services that are universally guaranteed for all citizens. Here, municipalities play a key role as the primary health clinics (*Consultorios de Atención Primaria*) are seen as the "entry point" of the GES/AUGE system. The final objective is that all health providers need to pass through an accreditation process in order to offer the guaranteed services (GES). The Superintendence of Health is in charge of the accreditation of primary health centres with the aim of improving health services and guarantee standards for citizens regardless of the municipality they live in. The implementation of this model has been slow; the mandatory requirement for a health centre to provide GES services has been postponed several times and few health centres have actually been accredited (RIMISP, 2016).

The fragmentation of municipal services could play against the effective management of municipal services. With differentiated budgets for education, health and other municipal services, municipalities are responsible for providing services that follow different guidelines and standards that are also poorly co-ordinated. As mentioned in Chapters 1 and 2, in practice Chile has not 346 municipalities but more than 1 000 in terms of budget and management. To turn municipalities into real local governments, Chile should move towards the integration of these different services into a single management model. For this, an appropriate institutional setting needs to be put in place. Better co-ordination of service provision - in a "whole of government" perspective - does not mean that just one single institution should be responsible for assessing municipal service delivery, but that co-ordination among the different institutions needs to be put in place to ensure consistency.

Ensuring minimum standards of municipal services to reduce territorial disparities

How to guarantee minimum standards for municipal services?

An important concern in decentralisation reform is a potential increase in territorial disparities as heterogeneity and differences in local capacities and performance can result in greater disparities across the country. It is argued that wealthier municipalities have greater possibilities to offer and provide better services to their citizens than poorer municipalities. In this regard, more autonomy for subnational governments would exacerbate such differences.

To deal with the risk of widening disparities among municipalities, some countries have implemented a methodology of minimum standards. For instance, Indonesia introduced, in 2005, the Minimum Service Standards (MMS) as a central element of its decentralisation reform (Box 4.7). The MMS sets the same outputs and targets for a minimum quality of basic public services that should be fulfilled by different districts throughout the country. By studying the MSS of the health sector, some evidence suggests a potential correlation between the definition of minimum standards in the health sector and a reduction of territorial inequalities in these services as the quality of health services steadily increases towards the minimum level of service quality required by MSS (Roudo and Chalil, 2016).

Box 4.7. **Minimum Service Standards in Indonesia**

The decentralisation process in Indonesia started in 1999 and has been characterised as a "big bang" policy with a rapid and significant devolution of power to local governments, transforming Indonesia into one of the most decentralised countries in the world. The reform had two main objectives: fair allocation of resources and improvement of the quality of public services as well as administrative, political, financial and spatial economic decentralisation.

Against this backdrop, and in response to significant territorial disparities, Indonesia introduced in 2005 the Minimum Service Standards System as a way to improve the performance and accountability of local governments. The System - a kind of measurement of local government performance - provides guidelines to line ministries to set indicators and targets for MSS, and at the same time it provides guidance for local governments on how to implement these minimum standards defined by different sectors. In 2012, Indonesia defined 15 MSS at the district level and 9 at the provincial level, consisting of 65 services and 174 indicators and targets. In 2014, the system was simplified and reduced to 6 MSS. Accountability is a key element of the MSS System as the definition of these minimum standards are supposed to put pressure on local governments to achieve the defined targets and improve their performance.

Institutionally the system is complex and requires major co-ordination efforts. Different actors intervene simultaneously in the design and assessment of the MSS at the central and local level. The ministry of Home Affairs spearheads the system as is responsible for providing the legal basis and guidance to sectoral ministries to set their own MSS. Line ministries define their own indicators and targets and monitor and evaluate its implementation; they are also responsible for feedback and capacity building for local governments with low performance. Other national actors also intervene in the process such as the National Development Agency and the Ministry of Finance. Local actors such as the Regional Secretary, the Local Development Agency, Local Finance Agency, among others, are responsible for the implementation and consideration of local regulations and development plans.

Box 4.7. **Minimum Service Standards in Indonesia** *(continued)*

The process includes a self-assessment by local government of their achievements, which must be validated at the central level where different actors intervene: the Ministry of Home Affairs, some sectoral ministries, the Ministry of Finance and internal and external auditors.

For example, the MSS on Health Services consists of four types of services and 18 target indicators. The implementation mechanisms stated by an official decree comprises a socialisation phase, building of baseline data, setting annual targets, costing and integration of the MSS into the planning and budgeting of local governments. Using self-assessment data a study shows that overall quality of health services increased from 2010 to 2013 while still remaining far from the minimum standard targeted. Even if the accuracy of data is limited, the study suggests a potential correlation of the definition of minimum standards in the health sector and a reduction of territorial inequalities in these services as the quality of health services in the sample areas steadily increases toward the minimum level of service quality required by MSS. Not surprisingly, the study also shows that fiscal capacity is correlated with achievement of MSS targets as local governments with greater financial capacity are more likely to achieve minimum standards.

The Asian Development Bank provided technical assistance to Indonesia for setting up the MSS and helped the central government understand the issues and constraints surrounding the implementation before issuing detailed implementation guidelines. Some of the key recommendations they provided included the need to differentiate levels of responsibility and to clearly divide regional government obligations between those that are obligatory and those that are optional. The MOHA needed to be strengthened to co-ordinate effectively the design and monitoring of obligatory functions and MSS responsibilities. In particular, as costing and budgeting were only partly taken into account in defining obligatory functions and MSS, financing is a critical area that needs to be addressed. One mechanism of financing could be through general purpose transfers. However, adequate capacity-building is needed for central and local government agencies to be able to properly cost obligatory functions and MSS.

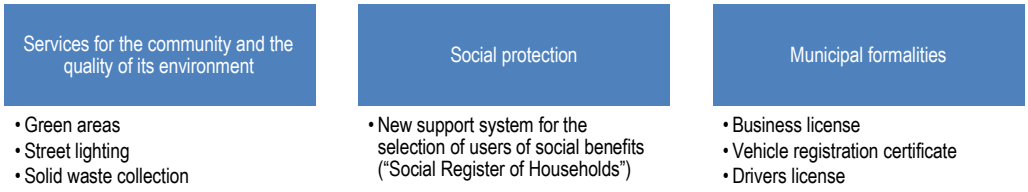
Source: Roudo, M., Chalil, T., M., (2016), Depolarization in Delivering Public Services? Impacts of Minimum Service Standards (MSS) on the Quality of Health Services in Indonesia; Asian Development Bank (2005), Technical Assistance Completion Report.

Australia has also developed standards for service delivery for homelands and outstations of the Northern Territory. Australian Homelands are small aboriginal communities where residents live in order to fulfil their cultural obligations to their inherited country and its underlying traditional law (Northern Territory Government, n.d.). The Northern Territory Government (NTG) committed to improving services and living conditions on homelands and has specific funds allocated to service providers to support the delivery of municipal housing and employment-related services to outstations/homelands, communities and Town Camps across the Northern Territory. The government developed a Programme of Minimum Standards by identifying the minimum expected levels of servicing, maintenance and standard of infrastructure on all homelands. Service providers are to utilise funds to undertake the minimum standards of service delivery to achieve the outcomes of the programme. To monitor the programme, and manage and assess service delivery, they designed reporting templates that are required to be filled in and submitted to the department on a regular basis.

Following the same rationale, a key piece of the reform of the municipal management system in Chile is setting minimum standards for municipal services (*Servicios Municipales Garantizados,* SEMUG) to reduce horizontal disparities among

municipalities. The SEMUG comprises, at least initially, seven municipal services - called by SUBDERE, "the first generation of guaranteed minimum services" that represent either a high impact for the community, or high costs or income for the municipality (Figure 4.11). These minimum standards have been defined as a basic level of provision in terms of quantity and quality, which has been conceived to be guaranteed by all municipalities in the country – a common set of services to which all citizens should have access regardless of where they live (PUC, 2016). The seven selected services include 22 standards and 47 indicators. For the definition of baseline values for each indicator, SUBDERE is working on a pilot implementation programme with 60 municipalities.

Figure 4.11. **Basic services for minimum standards**



Source: OECD elaboration based on information provided by Subdere.

Beyond the potential reduction of disparities in local government performance, other advantages of introducing a system of minimum standards are easy to identify. The SEMUG can potentially increase municipal accountability by making local governments more transparent and responsive to both central government and citizens. In this scenario, it can increase the efficiency and effectiveness of public service delivery. However, while the definition of minimum standards is necessary, it is not sufficient. To reduce disparities, these normative guidelines should be accompanied by the right incentives to follow them. At the same time, concrete progress could be better achieved with a real partnership between municipalities and citizens, where the latter make requirements but also collaborate with the local governments.

Setting minimum standards and indicators also helps national and subnational authorities to clearly identify the scope of their responsibilities, which are sometimes unclear. More importantly, it can help to identify and clarify municipal responsibilities for citizens who can demand responsiveness from their local government in a concrete manner. This should indeed, be accompanied by a clear definition of responsibilities across levels of governments (see Chapter 1). Otherwise, goals set for municipal services can be hampered by decisions taken at the central level obstructing accountability. This is one of the core elements of decentralisation reforms: reinforcing democracy by making local governments more accountable. This in turn, can potentially improve the performance of local governments through commitment in delivering better services to their constituencies.

Chile should pursue efforts to define minimum service standards in order to ensure a common set of services is provided to all citizens throughout the country. Yet, this process should be seen as an intermediary step toward greater municipal autonomy. The definition of SEMUGs can be an interesting exercise for Chilean municipalities as a way to strengthen decentralisation.

Still, while designing and implementing a system of minimum standards, Chile needs to be aware of some potential risks this policy entails. First, if framework conditions are not appropriate (see below), requiring minimum standards may result in a strong burden for local governments. This in turn, can create more municipal dependency on central government transfers and resources (Roudo, 2014). Defining minimum and homogeneous standards to be guaranteed by municipalities may also create some rigidity and lead to excessive control. Bardhan and Mookherjee (2006) argue that local government is the most efficient way to deliver public services since it can best match local preferences and supply services as well as gain real and accurate information from local people in a short time. One of the leitmotivs of decentralisation reforms is in fact to provide local governments with the necessary autonomy for them to meet local needs better. This is why it is necessary in a long-term perspective, to ensure some flexibility over prioritising the delivery of services that best meet citizen needs.

Service Charters to ensure standards of service delivery

To overcome the risk of excessive central control, some OECD countries have gone beyond the definition of minimum standards by developing service charters. This tool is a suitable instrument to promote the continuous improvement of public services and to make clear commitments to the quality standards that citizens can expect. Service charters are documents that inform citizens of what to expect of a given service and commit the institution to a certain quality standard. Service charters make public the conditions, requirements, legal basis, and cost of a certain formality or service (OECD, 2016b). It is important to pay close attention to the design process of service charters as the breadth and effectiveness of these instruments lie precisely in this process. The charters cannot follow a uniform or pre-defined prototype but ensure they can be adapted to local realities; at the same time they need to be conceived as reviewable documents that can be updated periodically to permanently reflect improvements and new citizens' expectations (Junta de Andalucía, 2004).

The European Commission includes service charters as part of their toolbox to improve service delivery. It defines services charters as unilateral declarations by the public service provider – municipalities or others – whereby they define a number of standards with a promise of expected quality from the service. The European Commission describes its main purpose as "a radical idea to give rights to the clients of public services". These rights are not statutory, but the pressure of the promise is such that the organisation will do a great deal to fulfil the commitments it has made. With this approach, the user charter helps the client switch from a relatively passive role of waiting for what the organisation has in mind for him or her. The offered rights stimulate the idea that the organisation treats them with respect. This gives the client a certain dignity. It also helps to build trust in the administration" (European Commission, 2015).

Box 4.8. **User charters in healthcare: The Netherlands and the United Kingdom**

The concept of the service charter was originally developed in commercial organisations and was then adopted by public services and healthcare. In the United Kingdom, the concept has been used in all National Health Service hospitals since 1991 in the form of the Patient's Charter. Healthcare organisations in Italy, the United States and the Netherlands have also adopted the concept. In several Dutch healthcare services, the multi-attribute specific service charter is used. This consists of a number of promises covering the patient's journey from general practitioner referral through to discharge from the hospital and follow-up arrangements.

Box 4.8. **User charters in healthcare: The Netherlands and the United Kingdom** *(continued)*

The specific goals in implementing service charters are: increasing the responsiveness of healthcare services to the wishes of patients; making healthcare services more accountable; ensuring patients know what to expect so that they can become more equal partners in the healthcare process; being used as a listening mechanism; increasing feedback from patients; improving patient satisfaction.

In the Netherlands, an integrated regional stroke service involving five organisations has developed and implemented a single service charter. Integrated care is an organisational co-ordination process that seeks to achieve seamless and continuous care that is tailored to the patient's needs and based on a holistic view of the patient.

Three phases of the integrated stroke service can be distinguished: 1) acute care involving the emergency department and stroke unit of the regional hospital; 2) rehabilitation involving rehabilitation centres, specialised nursing homes and home care; and 3) long-term support. Delivering optimal care with this range of providers requires a complex mix of collaboration at operational and individual levels involving streamlining information flows and the transfer of acute patients. At a tactical level, this can involve performance indicators on the care-chain level and, at the strategic level, financial and logistical agreements. These interventions aim to improve patient care and medical outcomes, objectives that fit into the general goals of care integration: Enhancing patient satisfaction and quality of life, efficiency and outcomes.

Source: OECD (2017), *Better Service Delivery for Inclusive Growth in the Dominican Republic*, OECD Publishing, Paris.

To improve municipal service delivery in the long run, Chile could consider reinstating service charters at the subnational level. The model of *Cartas Ciudadanas* of 2011 did follow the principles previously stated; reconsidering this model by learning from past experience can represent an important step forward. Indeed, moving forward in decentralisation reforms in Chile means to ensure minimum standards but also ensure appropriate flexibility and autonomy municipalities need to ensure their policies match local preferences. While doing that, service charters also enhance a bottom-up approach to service delivery and empower citizens to play an active role in monitoring their local government's commitments. This model is more flexible than the SEMUG as municipalities can adapt their standards to their local realities, while ensuring a minimum baseline.

Box 4.9. **What does a service charter looks like? The example of Andalucía and Jalisco, Mexico**

The Junta de Andalucía defines the structure and content of service charters. Each charter should have three parts that shall be written in a brief, clear and simple manner and in terms that can be easily understood by citizens:

- **General and legal information**: Identifies the provider and the entity responsible for the service, the objectives, the services to be provided, regulations involved, actors involved, etc.
- **Quality commitments**: Explicit definition of quality levels, indications that facilitate access and conditions of the service provided, systems in place to ensure the quality of service to provide, reference indicators.

Box 4.9. **What does a service charter looks like? The example of Andalucía and Jalisco, Mexico** *(continued)*

- **Additional information**: Any additional data in order to provide better and more complete information to users.

In Jalisco, the General Direction for Regulatory Improvement is working on the implementation of service delivery charters pertaining to four municipal formalities dealing with starting and operating a business. The charters emphasise quality standards that public offices must meet and include citizen participation mechanisms. They include 12 sections: general information about the formality, objective of the formality, length of the permit or license, offices in charge of the formality, citizens' responsibilities, requirements, costs, service commitments, complaint mechanisms, improvement commitments, complementary information, and signature by the official in charge.

Sources: Junta de Andalucía (2004), Manual de Elaboración de Cartas de Servicios; García Villarreal, J.P. (2010), Successful Practices and Policies to Promote Regulatory Reform and Entrepreneurship at the Sub-national Level.

Integrating standards into a comprehensive management model

Towards a model for quality management

The municipal landscape in Chile varies strongly across the country and the differences in management and service provision between wealthier municipalities – mostly in urban areas – and poorer ones are large. These differences are not only due to weak financing or capacities – as discussed at length in this report – but also result from a strong fragmentation of responsibilities within the municipality and the lack of a comprehensive and "whole of government" management assessment.

Service provision is crucial but it is only one piece of municipal management. To ensure that the SEMUG are achieved they should be part of a more comprehensive assessment of municipal performance, one that integrates elements such as governance, citizen participation, resources management, planning, etc. The proposal made by RIMISP (2016) working together with SUBDERE goes in this direction (Box 4.10). This new model proposes to move from a service delivery focus to a more global and comprehensive approach that considers all the key areas of municipal management and integrates the accomplishment of the indicators associated with the minimum standards to the self-assessment process (RIMISP, 2016).

Box 4.10. **Model for Quality Municipal Management: A proposal by RIMISP**

RIMISP has developed a new structure for a quality assurance model for municipal management structured around eight criteria related to processes and results:

1. Leadership and governance: It considers the actions taken by the leaders to "sustain" the institution. It also considers the governance system and how the institution fulfils its legal, ethical and environmental responsibilities.
2. User management and citizen participation: It refers to the way in which the municipality determines user requirements and expectations, how the municipality builds the relationships with citizens and how it determines satisfaction levels. It also considers how the municipality encourages citizen participation.

Box 4.10. **Model for Quality Municipal Management: A proposal by RIMISP** *(continued)*

3. People management: This criterion refers to how the institution evaluates the competencies and capacities needed and builds a work environment that fosters high performance. It also considers how it commits, manages and develops employees in order to align their potential with the needs of the institution.
4. Local development strategy: It refers to how the municipality manages strategic decisions, the operations and projects that enable local development and improve quality of life.
5. Delivery of municipal services: How the municipality designs, manages, improves and innovates service provision.
6. Resource management: How the municipality manages financial resources to ensure efficient processes, transparency and the sustainability of municipal finances.
7. Planning, information and knowledge: It refers to the processes of strategic planning, how the municipality manages information for performance measurement and how it manages internal knowledge for institutional learning.
8. Results: Examination of level and tendency of main indicators and measures that reflect municipal results considering the seven previous criteria.

Source: RIMISP (2016) Sistema Nacional de Fortalecimiento y Medición de la Calidad de los Servicios Municipales – Informe Final – SUBDERE.

Reinforcing municipal responsibilities goes together with greater monitoring and control over municipal performance. A comprehensive performance measurement tool, based on an integrated management model, can support Chile in the process of quantifying the output and outcomes of government policies. It can also help municipalities and their staff in identifying objectives and support incentive mechanisms (OECD, 2009). In addition, when these objectives are clearly communicated to citizens, they can help stakeholders determine the impact of policies and programmes and whether public authorities are meeting clearly-identified objectives. Performance measurement, however, requires the capacity and will to set and monitor objectives by all levels of government, and to communicate performance openly and in a way that is relevant to citizens.

Defining indicators for a performance assessment

Successful performance measurement requires solid performance indicators, and ones that can promote learning and orient stakeholders towards results. The use of indicators can help municipalities to address information asymmetries that arise between different levels of government or between the government and stakeholders, including citizens. Suitable indicator systems can be effective tools for helping local governments and other stakeholders to monitor progress. As it is the case for minimum standards, the definition of a set of indicators for performance assessment requires a clear definition of the roles and responsibilities of the different levels of government. If indicators are associated with service management where municipalities do not have autonomy to manage them, then such a system would represent a burden for local governments (see Chapter 1).

Well-identified indicators can also reinforce accountability at all levels of government by improving transparency. A set of indicators, which will ultimately feed a performance assessment, can also be used to support budget management, the attribution of subnational grants, and contribute to understanding policy outcomes. This would make it easier to identify when policies or programmes may require adjustment. When carefully combined with specific incentive mechanisms and realistic targets, indicators can stimulate and focus actors' efforts in critical areas (Mizell, 2008).

Indicators associated with a management model need to be clear and measurable. While it might seem obvious that indicators can aid in evaluating performance, there are many impediments in designing and using an indicator system, including a wide array of technical issues. The design of an indicator system depends on the objectives to be achieved: allocation, control, or efficiency in the use of resources, transparency, etc. The objective of such an indicator system can be to transform the quality of services by attaching targets and specific results to indicators, by monitoring and supporting local capacity to deliver service, or both (OECD, 2009). But it can also combine different objectives. For example, it can stimulate competition by comparing a ranking service delivery among different municipalities in order to enhance cost effectiveness (OECD, 2009). A system that seeks to monitor and control financial flows will emphasise input indicators with a focus on resources allocated to committed programmes. By contrast, while a system aims at monitoring "how things get done" it may be focused on process measures that indicate if intended activities are undertaken, by whom, and at what pace (OECD 2009). Yet, indicators linked to processes risk the creation of too complex control systems with no clear impacts on results; in contrast, results indicators allow the direct and visible improvement of services and municipal management with clear and direct impact for citizens.

A crucial step in the definition of indicators is to include the relevant actors at all levels of governments. Indeed, a purely top-down approach when designing and selecting indicators is likely to encounter two important challenges: 1) the indicator system may fail to reflect municipal specificities precisely because the central government does not possess perfect knowledge about local actors or the context in which they operate; 2) seen purely as a requirement imposed from above, regional actors may comply with reporting requirements but fail to use the information produced by indicators for achieving real performance improvement (OECD, 2009).

Collaboration among all levels of government can increase the relevance and usefulness of indicator systems. The various levels of government may be motivated to collaborate if they perceive it will lead to new or better information for enhancing service delivery, improve policy effectiveness, or if they can share the additional resources which result from efficiency gains (OECD, 2009).

The definition of targets for minimum standards by consulting municipalities in Chile follows this rationale. The design of a comprehensive performance monitoring system should follow the same strategy; it is crucial that the actors that will be involved in delivering the outputs and outcomes are involved in the selection of indicators that will be monitored and the targets that will have to be achieved. This collaborative process also implies difficulties and risks that Chile needs to be aware of. The case of Local Public Service Agreements in the United Kingdom illustrates some of the challenges encountered by both central and local governments when agreements and collaboration are necessary (Box 4.11).

Box 4.11. **Indicators and incentives: Local Public Service Agreements in the United Kingdom**

In 2000, the United Kingdom introduced voluntary incentive-based performance agreements with the local governments as part of its effort to improve local public services. Called "Local Public Service Agreements" (LPSAs), these three-year agreements with upper-tier local authorities (LAs) established 12 outcome-based "stretch targets" in multiple service areas. Three categories of incentives were incorporated into the LPSAs. First, "pump-priming grants" were offered upfront to enable local authorities to invest in capacity-building to meet their targets. Second, if a local authority met at least 60% of the stretch target after three years, it could then receive a performance grant of up to 2.5% of its net annual budget. The amount received equalled the proportion(s) of the target(s) achieved up to 100%. Finally, they were offered capacity for additional borrowing and the possibility of relaxing administrative requirements.

On the positive side, LPSAs appear to have strengthened incentives for local public service delivery, due in part to the financial rewards and in part to the fact that local authorities participated in the establishment of the specific targets. They also strengthened local partnerships (as some targets could only be achieved collaboratively), and contributed to local capacity development and learning. Financial incentives were useful, particularly prime pumping grants, for investing in capacity-building, encouraging partners to participate, and leveraging additional funds.

With respect to challenges, a few stand out: first, negotiating targets proved to be time consuming for the central government and local authorities. The central government perceived some "gaming" in the sense that LAs pushed for targets that would be easy to achieve. Second, limited understanding of causal mechanisms and inadequate data may have hampered the LAs' ability to set realistic targets. Third, although LAs were involved in target selection, the process was centrally-driven, often resulting in targets that did not necessarily reflect local priorities. Finally, administrative flexibility proved harder to deliver than anticipated. Second generation LPSAs were launched at the end of 2003. One significant change was greater local involvement to increase the relevance of indicators and targets. In 2007, the LPSAs were integrated as an incentive mechanism into Local Area Agreements as part of an effort to streamline the number of agreements. The central government also plans to cap the number of indicators (198) to be monitored at the local level. From this set of 198, local authorities had to select 35 against which targets would be established in negotiation with the central government.

Finally, criticised by the new government as bureaucratic tools, they were abolished in 2010.

Sources: Box originally appears in Mizell, L. (2008), *Promoting Performance: Using Indicators to Enhance the Effectiveness of Sub-central Spending*. It draws on Blake, J. (2007), "Local Public Service Agreements and Local Area Agreements: the UK Experience"; DCLG (n.d.), "National Targets for Local PSAs"; ODPM (2005), "National Evaluation of Local Public Service Agreements: First Interim Report"; ODPM (2003), "Building on Success: A Guide to the Second Generation of Local Public Service Agreements"; DCLG (2007), "The New Performance Framework for Local Authorities and Local Authority Partnerships: Single Set of National Indicators".

There are many examples of government developing successful indicator systems to keep citizens informed of how their government – national, regional and local – is performing, and how it intends to continue meeting their needs. At a national level, Australia undertakes a review of government service provision in order to compare the performance of government services and share service reforms that have been implemented or are under consideration. The review outlines agreed national performance standards for government services. It also analyses service provision reform. Among the services covered in the review are care of the elderly, child services, emergency management, health and housing.

Regionally, the Scottish government, through "Scotland Performs," has been a leader in performance measurement and accountability to citizens, providing an online up-to-date tool to understand government activity, the results it has achieved, and where more work needs to be done. The Scottish system of Single Outcome Agreements is a particularly comprehensive system of performance management. Both the Scottish government and all local authorities seek to improve mutual accountability and achieve a wide range of societal outcomes, which is quite unique (Scottish Government, 2016; European Congress of Local and Regional Authorities, 2015).

At the municipal level, the Danish Joint Municipal Management Information System (FLIS) is a performance information system, updated every month, which provides an overview of a city's own data, with the ability to compare this data with other municipalities, regions and the national average. In Norway, performance measurement also supports municipal public service provision and capacity. This has indeed been one of the benefits Norwegian municipalities have received from Norway's KOSTRA system, which publishes the results electronically, within a month of receipt from the municipalities. Canadian provinces, such as Nova Scotia, Ontario, and Quebec are also adopting performance reporting systems for their municipalities to support municipal and provincial decision makers (Buckstein, 2009). Finally, New York City is leading a purely municipal level initiative to build accountability through indicator systems (Box 4.12).

Box 4.12. **Performance measurement in Norway, Ontario (Canada) and US cities**

The Norwegian KOSTRA system has been widely recognised in the OECD area as a best practice. Used for performance monitoring of local services, it is an electronic reporting system for municipalities and counties. It can publish input and output indicators on local public services and finances and provide online publication of municipal priorities, productivity and needs. KOSTRA integrates information from local government accounts, service statistics and population statistics. It includes indicators of production, service coverage, needs, quality and efficiency. The information is easily accessible via the Internet and facilitates detailed comparison of the performance of local governments. The information is frequently used by local governments themselves and by the media and researchers. Although individual local governments could use KOSTRA more efficiently (e.g. by systematic benchmarking), the system has helped facilitate comparisons of municipalities, thereby promoting "bench-learning" or "bench-marketing".

In 2000, the Province of Ontario, Canada, introduced the Municipal Performance Measurement Programme (MPMP) as an accountability mechanism and to help local authorities make more informed decisions, and its use became mandatory in 2001. Ontario's 444 municipalities – regardless of their size – are all responsible for reporting on 12 core service areas, resulting in 54 measures of efficiency and effectiveness. These service areas are: local government, fire, police, roads, transit, waste-water, storm-water, drinking water, solid waste management, parks and recreation, library services, and land-use planning. The government has considered adding building services, housing, long-term care and museums to this list as well. The MPMP has not only improved reporting, it has also given provincial and local authorities a solid database of information, supporting multi-year trend analysis and budgeting processes. Municipalities report performance data annually by 31 May.

In addition to MPMP, in 2001 Ontario introduced the Ontario Municipal Benchmarking Initiative in order to support city executives in measuring progress and sharing data and practices with respect to: the efficiency with which resources are transformed into good and services; their quality; their associated outcomes; and the effectiveness of services delivered.

Box 4.12. **Performance measurement in Norway, Ontario (Canada) and US cities** *(continued)*

The initiative includes 15 member municipalities, and it publishes an annual report, available to the public. This report presents information in 27 service areas with an aim to help citizens be more informed about their municipality and the services it offers, and how their municipality compares to others.

New York City's strategic development plan – One New York (OneNYC) – is supported by a series of performance indicators aligned with the city's four-pronged strategic vision. Each one clearly states the indicator, the performance target and data for the most recent year as a baseline. For example, its "sustainable city" section is supported by a goal to improve air quality, which in turn has three indicators and associated targets – for example air-quality ranking among major US cities is one indicator and its target is to be ranked first, currently it is fourth. Details regarding the lead agency responsible for accomplishing each initiative, funding status and source are also available. This set of indicators is published in print, and supported by an online tool (#OneNYCProgress) where citizens can find information on how the city is performing with respect to its stated goals, make comments, and download reports.

The city of Bellingham, Washington in the United States has established a series of performance measures designed to keep the public informed. It provides data related to nine long-term community goals: clean, safe drinking water; a healthy environment; a vibrant, sustainable economy; a sense of place; a safe and prepared community; mobility and connectivity; access to quality of life amenities; equity and social justice; quality, responsive city services. Each of these goals is associated with a series of strategic commitments and a scorecard that rates the city's performance. Citizens are asked to annually rate the city's performance on key areas that help measure progress in the objective. For example, the goal of "access to quality of life amenities" is linked to the strategic commitment "to maintain and enhance publicly-owned assets." Among the metrics used to measure this is how well the city maintains parks and trails. Thus, every two years citizens are asked to rate how well the city is doing in this effort. For example, in 2013 90% of the citizens rated that the city was doing a "good" or "excellent" job. Other measures are not based on citizen perception but are data based, such as the total number of permits issued, an indicator used for measuring the objective of a vibrant, sustainable economy, and supporting the strategic commitment "to support a thriving local economy across all sectors". In this case, the city also states its goal for the commitment (to continually see year-on-year increases). It did not however, establish targets for this, and it is very clear that this is the case. All of this information is available on a user-friendly, easy to understand website.

In an approach similar to that of Bellingham, Seattle, Washington also makes performance information available to citizens, in an easy to access, easy to understand, online format. Called "Performance Seattle" the website uses current data to monitor the progress against the city's established goals in seven areas: public safety; utilities and environment; transport; housing, human services and education; community and economic development; operations and innovation; parks, recreation, library, Seattle Centre, and the arts. Each of these areas is associated with specific goals and the results are monitored. For example, under "transport" one objective was to ensure that potholes are quickly repaired (80% or more within three days of notification). City measurements indicate that 96% are repaired within three business days after they are identified. The website goes on to explain why the goal is important and what progress is being made towards accomplishing it. It also provides websites and telephone numbers for more information relevant to the city's action on the issue (e.g. a "Pothole and Street Repair Hotline", an online "pothole map", etc.).

Source: OECD (2010), *OECD Territorial Reviews: Sweden 2010*; Buckstein, J. (2009), "Municipal Performance Indicators are gaining in Stature and Efficiency across Canada"; Government of Ontario (2015), "Municipal Performance Measures"; OMBI (2011), "What is OMBI", Ontario Municipal CAO's Benchmarking Initiative, Ontario, Canada; City of New York (n.d.), *One New York: the Plan for a Strong and Just City,* City of New York; City of Bellingham (n.d.), "Performance Measures", Government, City of Bellingham; City of Seattle (n.d.), "Welcome to Performance Seattle", Performance Seattle.

While acknowledging their value, many governments are challenged to establish effective performance measurement systems, in part due to difficulty in building meaningful indicators and fostering a performance management culture (Box 4.13).

Box 4.13. **Common obstacles to building meaningful performance indicators**

Performance measurement quantifies the output and outcomes of activities and/or programmes and can help build accountability, promote learning, or to steer initiatives. Its success rests on the ability of government to successfully obtain good quality data to inform decision-making and to develop appropriate indicators. Among the most common obstacles governments face when building indicator systems are:

- The lack of a high-level goal (i.e. a strategic objective), for example, to reduce poverty among youth.
- Organisational cultures which inhibit broad-based co-ordination and building ownership.
- Insufficient appreciation of the relationship and links between strategies, policies, targets, outputs and outcomes.
- Policies that are not clearly articulated.
- Indicators that are imprecise.

Source: Adapted from OECD (2013d), *Poland: Developing Good Governance Indicators for Programmes Funded by the European Union*.

In addition, setting up a performance measurement system can sometimes also become a counterproductive endeavour linked with increased bureaucracy and high costs (e.g. abolition of the Audit Commission in the United Kingdom and the replacement by another system) (Box 4.14).

Box 4.14. **Abolition of the Audit Commission (United Kingdom)**

According to the UK government, the decision to abolish the Audit Commission was made because it was a wasteful, ineffective and undemocratic programme: "What should have been a voice for taxpayers became a creature of the central state". The Audit Commission was regulating, micromanaging, and inspecting, forcing local councils to spend time ticking boxes and filling in forms rather than getting on with the business of local government. The objective is to save GBP 1.2 billion over 10 years and reduce bureaucratic public bodies.

However, the United Kingdom has not abandoned the idea of measuring performance and has implemented a more robust, accountable and efficient way of scrutinising local council activities (Local Audit and Accountability Act 2014, which came into effect from 1 April 2015) with a new local audit framework and procedures. The objective is to pass power down to people through more local choice and transparency. The new system replaces the centralised arrangements with a more local approach, giving local entities the freedom to appoint their own auditors from an open and competitive market; manage their own audit arrangements, with appropriate safeguards to ensure auditor independence; and retain the same high audit standards. As a result, audit services will be better matched to local bodies' individual needs.

The system is also adapted to local capacities. Parish councils with small budgets are exempt from the new local audit regime and are subject to different transparency requirements. Finally, the new Act makes provision for directions to comply with codes of practice on local authority publicity. It also makes provision about council tax referendums.

Source: UK Government (2017), Information page on Audit Commission closure.

In Chile, both the SEMUG and the system of municipal services should be accompanied by a sound indicators system. To this end, and echoing the recommendation given by the PUC, Chile could consider integrating the system of indicators with the existent SINIM (*Sistema Nacional de Información Municipal*), a good practice reference for OECD countries (see Chapter 2) which could provide a platform or starting point for a tool of this type. In the long run, to complete a comprehensive System of Municipal Services Chile could create an independent platform for this special purpose linked with the SINIM.

Creating the conditions to improve municipal services

Strengthening capacities for an effective system of public service management

An efficient system to ensure and assess management performance at the local level in the Chilean context requires efforts from the central government to provide municipalities with the financial, human and technical means to effectively use the system. In fact, such a system could rapidly become a burden for a number of municipalities, particularly small ones, which are unable to cope with these new tasks.

Whenever municipalities are asked to increase the list of services it provides, it is only natural that its financial resources increase at a commensurate level. However, the opposite is also true. In some cases, poor service provision can be explained by poor management but in other cases, insufficient resources can be the main problem. Sometimes it is a combination of both. To ensure minimum standards and effectively reduce territorial inequalities as a basis for a long-term public service management model, initially the central level should ensure resources for municipalities to meet this objective, as was recommended by the Asian Development Bank to Indonesia (Box 4.7). As in the current Chilean context increasing resources allocated to municipalities in the short term is hardly possible, the central level could envision reallocating resources to ensure municipalities can meet minimum standards.

As proposed by Centre of Public Policy of the Catholic University as a first step (PUC, 2016), a contract between the central and local government can ensure a minimum level of resources for service provision. The re-allocation of resources can also be tied to improvements in the results of indicators associated with the SEMUG and the System of Municipal Services; this in turn, will generate the appropriate financial incentives for municipalities to improve service delivery. As a first step (and considering the strong territorial heterogeneity in Chile), for municipalities that do not meet the minimum required, the central level should reward progress with respect to baselines. Proper fiscal transfer can help in reducing territorial inequalities, at least partially.

Human capacities are also a key lever for effective service provision. More financial resources need to be completed with the human resources capable of managing them. Appropriate capacity levels are crucial both at the municipal level but also at the central level to define standards, manage, monitor and evaluate performance. At the local level, municipalities should take advantage of the recently approved law that injects flexibility in the recruitment process (see Chapter 4), which enables them to hire professional staff particularly for improving overall performance and meeting minimum standards. In parallel, a capacity-building process should be put in place driven by the central and/or regional governments. The capacity-building process should integrate specific training on the indicators associated with the SEMUG and to the assessment of the System of Municipal Services (PUC, 2016).

Improving service delivery at the local level is part of a broader policy. Other relevant policy drivers such as digital governance, innovation or administrative simplification directly influence access to public services (OECD, 2016b). These complementary tools need to be fully developed if Chile wants to effectively improve service delivery. Initiatives such as Digital Municipalities (*Municipios Digitales*) go in this direction (Box 4.15) and should be integrated in the model of a comprehensive system of municipal services.

Box 4.15. **Digital Municipalities in Chile**

The initiative *Municipios Digitales* focuses on the transfer of technology and best practices to build awareness and capacities in order to facilitate standardisation of formalities at the local level. SEGPRES signed agreements (*convenios*) with the municipalities so that when a formality or information is digitised it can be uploaded to the Chile Atiende platform. Thus far, the approach has been to identify where advancements could be expected at the local level in the mid and long term and to build capacities to identify the formalities to digitise. They started prioritising the most widely used formalities. The second set of services imply that a payment is involved, which means that they are often more business related (these were identified in connection with the BD).

The initiative looks at the service experience from the user's perspective. There is a need to standardise the formalities in all municipalities, indicate on the webpage all the formalities to be digitised, and provide this information to the different municipalities. They are looking into prioritisation of services (e.g. certificate of good standing of social organisations) with the goal to help all municipalities to develop technologically and be able to use technology to improve public management and foster collaboration in particular with the smaller municipalities.

Source: OECD (2016b), "Regulatory Policy in Chile, Government Capacity to Ensure High-Quality Regulation".

Appropriate multi-level governance arrangements

Municipalities offer a wide range of services and have sometimes been identified as a "service supermarket" (Bernstein and Inostroza, 2009) given the magnitude and variety of services provided. Although local governments are, in the end, responsible for organising and executing the delivery of these services, other public or private actors or external stakeholders are usually involved in some aspect of their regulation, financing, management, delivery or assessment. This is particularly true in Chile's highly-centralised context where central institutions such as the Ministry of Health, Superintendence of Education, Ministry of Public Works, Ministry of Social Development, among others, intervene. In this context, overlapping mandates and weak vertical co-ordination amongst the institutions involved in service delivery and performance evaluation can undermine the effectiveness of Chile's institutional landscape. Horizontal co-ordination also represents an important challenge, especially for metropolitan areas. Several municipalities have decided to partner with their neighbours to provide services; this is the case, for example, of the Association of Municipalities of the Province of Llanquihue for Sustainable Waste Management (see Chapter 6). In fact, in certain circumstances, effective management of basic services requires closer co-operation between local authorities and other levels of government

Effective service delivery thus requires appropriate multi-level governance arrangements and institutional and legal frameworks that clearly define the roles and

responsibilities of all levels of government involved. This goes hand in hand with a clear re-definition of responsibilities of the national, regional and local level (see Chapters 1 and 6). To institutionalise such arrangements (see below) the first step is to set clear and consistent responsibilities for each actor involved in the SEMUG, which implies that there is a consistent and clear division of power and responsibilities among the different levels of government.

Comprehensive institutionalisation of local public services management

The decentralisation process implies a gradual adjustment of the institutional setting. To reduce the potential risk of the SMUGs and a System of Municipal Services, Chile needs to ensure institutional arrangements and conditions that will help the country efficiently improve public service provision**.** The process of designing a comprehensive model to assess and evaluate service delivery has encountered several challenges, notably linked to political priorities, which have resulted in discontinuity or replacement of the programmes oriented to improve service delivery at the local level. Consequently, improvement of municipal management – a process that takes time – has not necessarily met expectations. These constant changes do not only affect an appropriate framework for service management, but also gives unclear signals to municipalities; this can result in an excessive burden for local actors. This could be mitigated by an institutional framework that depends less on political will and effectively institutionalises the system of municipal services.

The complexity associated with implementing a system of municipal services –actors involved, fragmentation and unclear definition of responsibilities, amongst other – goes hand in hand with an institutional setting overhaul. It is complex to identify which institution should define standards and goals, supervise and assess performance, assess penalties if minimum standards are not met or if there is inappropriate conduct during implementation, etc. Auditors/inspectors have essential roles in measuring the performance of public services and ensure the organisation will be on the right track to achieve the goals that have been mandated to them (e.g. United Kingdom) (Game, 2006; Martin et al., 2013). Both recommendations of the PUC (2016) and RIMISP (2016) suggest the re-allocation of responsibilities in a new institutional landscape with the superintendence of Guaranteed Municipal Services focused on the SEMUG (PUC, 2016) or with the creation of a National Commission for the Certification of Subnational Governments under a scenario where, in the long-run, the objective is to certify all subnational governments. In this new institutional landscape, ensuring co-ordination mechanisms and coherence with education and health entities is key. In both cases, and as a direct result of decentralisation reforms, the role of SUBDERE needs to be adapted. Yet, this new scenario should recognise SUBDERE as the institution with the expertise to support municipalities in the process of setting standards and indicators and performance management improvements.

A scenario in which a particular institution as described above is responsible for defining standards, gathering information, monitoring and evaluating should integrate both municipalities and regional governments. At present, a Model for the Quality of Regional Governments is in place within SUBDERE. This model also contemplates the definition of minimum standards that seek to align the regional government management with the new competencies they will have if decentralisation reforms are approved. As is the case for municipalities, these minimum standards should meet a basic level that sustains the devolution of competencies to regional governments. A new institutional framework with a formal entity that sustains this process should ensure that minimum

standards at both levels and an eventual certification system are aligned and co-ordinated. As proposed by the Presidential Advisory Commission for Decentralisation and Regional Development, an autonomous institution should be responsible for the certification of the quality of institutional management and services of both regional governments and municipalities.

Box 4.16. **Key recommendations for enhancing the quality and efficiency of municipal services in Chile**

1. Strengthen municipal services management in Chile, by:

- Developing a municipal services management model ("System of Municipal Services") and conducting a comprehensive overview of municipal management in the aim of overcoming the fragmentation of service delivery. For this, Chile should promote co-ordination and coherence among the different heads of service delivery at the national and subnational levels including education and health services.

2. Ensure minimum standards for municipal services to reduce territorial disparities:

- Pursue the implementation of SEMUG as a way to reduce territorial disparities in service provision; increase municipal accountability by making local governments more transparent and responsive to both the central government and citizens.
- The SEMUG should be seen as an intermediary step towards flexible service provision management, thus boosting municipal autonomy. This will allow municipalities to prioritise service delivery and meet citizen's needs better.
- Encourage service charters at the subnational level as a means to promote minimum standards while ensuring flexibility and autonomy for municipalities

3. Integrate standards into a comprehensive management model:

- Develop a comprehensive management model that integrates and goes beyond the definition of SEMUGs. This model should integrate elements such as governance, citizen participation, resource management, and planning.
- Design a suitable indicators system that is clear and measurable. The design and selection of indicators needs to involvement relevant actors across all levels of government following the methodology already in place for the definition of minimum standards and related indicators.
- As a starting point, Chile could envision integrating the indicators system into the existing SINIM (*Sistema Nacional de Información Municipal*). In the long run, to complete a comprehensive System of Municipal Services, Chile could consider creating a new independent platform especially for this purpose.

4. Create the appropriate conditions to improve municipal services:

- As a first step, the central government should provide municipalities with the financial means to effectively implement a comprehensive municipal service management system by:
  - Creating financial incentives through re-allocation of resources tied to improvements in the results of indicators related to the SEMUG and the System of Municipal Services.

Box 4.16. **Key recommendations for enhancing the quality and efficiency of municipal services in Chile** *(continued)*

  - For municipalities that do not meet the minimum requirements, the central level should reward progress with respect to baselines. It is important that the rewards system privileges reaching the minimum standard over progress to avoid minimum efforts/progresses (perverse effect).

- The central government should also provide municipalities with the human and technical means to effectively implement a comprehensive municipal service management system.
- Municipalities should hire professional staff that will help them to meet minimum standards and improve the overall performance of the municipality, taking advantage of the recently-approved law that injects flexibility into the recruitment process.
- The central government and/or the GOREs should conduct capacity-building activities to effectively improve performance and service provision. The capacity-building process should integrate specific training on the indicators associated with the SEMUG and to the assessment of the System of Municipal Services.
- Improving service delivery should be complemented by other activities such as digital governance, innovation or administrative simplification.

5. Towards the institutionalisation of public service management:

- Adjust the institutional landscape to design an effective and sustainable System of Municipal Services by re-allocating responsibilities. Set up an independent body – in the form of superintendence or a national commission – that would oversee municipal management performance, as a future step.
- A new institutional framework needs to ensure co-ordination mechanisms with actors responsible for education and health services.
- Strengthen the role of SUBDERE which is the institution with the expertise to support municipalities in defining standards/indicators and to support performance management improvements.

Notes

1 Unlike municipalities, employees of regional governments are subject to the same administrative statute as central government employees and have the same pay scale, the *Escala Única de Remuneraciones* (EUR).

2. For further information see: Government of Chile (2015), *Electoral Service and Municipal Management*, www.gob.cl/2015/05/20/electoral-service-and-municipal-management-discover-the-latest-measures-to-be-put-in-place-as-part-of-the-probity-agenda/ accessed on 20 January 2017.

3. Law No. 20.723 of January 2014, which amended the Law No. 19.803 of 2002 to align municipal bonuses with central government bonuses provided by the law 19.553 establishing the "Programa de Mejoramiento de Gestión" which introduced into the remuneration structure an incentive system aimed at taking into account better institutional and individual performance of civil servants.

4. Law No. 20.624 of 2012 on base salaries scale increased municipal base salaries to harmonise them with the central government. The cost to reduce the gap was estimated at about CLP 24 billion.

5. Calculations for the central government include the 236 736 of civil servants (*personal civil*) and 47 577 of temporary staff (*honorarios*).

6. For further information see: Le Portail de la Fonction publique: www.fonction-publique.gouv.fr/rapport-annuel-1 accessed 23 January 2017.

7. For further information see: www.sinim.cl.

8. Auxiliaries, technical and administrative staff.

9. It must be noted that "*profesionalización*" in Chile and Mexico does not refer to the same thing. Whereas in Chile *profesionalización* means having academic degrees or training certificates, in Mexico it means the development of a career as a professional in the public service regardless of academic titles. The number of *profesionistas* does not equate to *profesionalización* in Mexico.

10. For further information see: SELOR www.selor.be/fr/a-propos-de-selor/.

11. For further information see: CNFPT www.cnfpt.fr/content/accueil?gl=ODUwMGE2Y2I.

12. See SINIM www.sinim.cl.

13. For further information see: Catálogo de Perfiles Ocupacionales, Unidades de Competencia Laboral y Actividades del Sector Municipal, accessed at www.subdere.gov.cl/sites/default/files/documentos/catalogo_perfiles_ocupacionales_sector_municipal_2012.pdf.

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Chapter 5

The participatory challenge: Strengthening participatory governance at the local level

The fifth crucial dimension of decentralisation reform is community participation and democracy at the municipal level as a means to building a more inclusive and more democratic society through formal mechanisms but by promoting transparency and accountability practices and greater citizen participation. The chapter begins with a brief overview of the state of participatory governance in Chile using engagement, community, voter turnout and trust in government as indicators. It then presents the country's main levers for promoting transparency, accountability and participation, and identifies some of the key issues surrounding their implementation. Following this is a discussion of what may help address the primary challenges, and the chapter concludes with a series of recommendations for action.

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

Introduction

Chile's government has a clear objective to broaden and deepen democracy by enhancing participatory governance as a means to build a more inclusive and more democratic society. It is actively doing so by boosting transparency practices and introducing tools to promote greater citizen participation – defined as a co-operative process between the state and citizens (Republic of Chile, 2014). However, the results it is seeking, including greater political accountability to citizens, stronger local democratic practices, and more active population in decision-making processes, are difficult to consolidate - particularly at the local level.

This difficulty is concerning both from a political and a public governance perspective. From a political perspective, improving participatory governance is fundamental for the second Bachelet administration to reach its strategic objectives of democracy and inclusiveness, which if unmet could further weaken trust in government. A recurring theme in the 2014-2018 Government Programme is citizen engagement without which - it bears repeating - territorial equity will be harder to achieve (Government of Chile, 2013). If the government cannot fulfil its political promise, then citizen trust in government, already a problem in Chile, will continue to be undermined. A persistent deficit in participatory governance is concerning from a public governance perspective because it points to the likelihood that it will be difficult to partner with citizens, which is also critical in meeting the government's objectives since such a partnership not only builds trust and strengthens democracy but can also promote compliance; leverage knowledge and resources; yield better policy outcomes, at lower cost; ensure equity of access to public policy making and services; and provide more innovative solutions to policy and service delivery problems (OECD, 2009; OECD, 2001).

Participatory governance combines citizen rights to express their opinion by casting a vote during elections with the ability to express their opinion through "voice." It is this combination of vote and voice that distinguishes participatory governance from representative democracy and deliberative democracy. While also vote-based, representative democracy implies the delegation of decision making to elected officials, thus eliminating the "voice" dimension. Deliberative democracy makes room for voice and vote but does necessary connect citizen vote to the need for binding decisions or action on the part of government (Wampler and McNulty, 2011). Meanwhile, participatory governance consists of state-supported institutional processes that permit citizens to have their voice heard in addition to voting, which then leads to the implementation of public policies effecting change in citizens' lives. It provides a framework for institutional practices that include transparency and accountability tools such as access to information, citizen engagement, and local government arrangements, and permits citizens to contribute to the policies, programmes and processes that directly affect them. Citizens engage in public venues at different times throughout the year, and policy cycle, allowing them to be involved in policy formulation, selection and oversight. Such inclusion results in constant contact with government officials, thus generating greater social capital by promoting new forms of interaction among citizens as well as between citizens and government authorities. Participatory governance allows the voice of the people to be heard and contribute directly to policy outcomes, most often at the local level (Wampler and McNulty, 2011). Governments often turn to participatory governance as a means to strengthen or correct the perceived shortcomings of representative democracy including poor government performance, inefficient and

ineffective use of public resources, and poorly empowered citizens, be it at the national or subnational levels. Governments that promote participatory governance often do so to improve the quality of democracy, social well-being, and the overall functioning of the state (Wampler and McNulty, 2011).

Participation can better ensure government transparency and accountability through citizen oversight, and build social capital by strengthening ties between members of a community, as well as strengthening ties between communities and government officials. This in turn can have a positive impact on a community's resilience – an important consideration in all countries, and particularly in countries, such as Chile, where there is a high risk of natural disasters and social inequality is prevalent. Meanwhile, a government can use participation as a means not only to understand public opinion, but also to challenge it, helping better inform and shape preferences. It gives policy makers a chance to "test" how people will react to a proposal and adjust it if necessary and it can help legitimise government decisions and policies (Holmes, 2011).

Research highlights three enabling factors for citizen participation in the Latin American region (ELLA, 2013): 1) legal frameworks favourable to participation; 2) political will; and 3) an active and vibrant civil society, able to demand its rights, conduct independent assessments, and take part in the participatory space created by government. Chile is strong with respect to legal frameworks favouring participation. However, political will, particularly at the local level, is often weak. Meanwhile, civil society is fragmented and narrowly focused, and there appears to be limited space or opportunity for proactive participation by citizens.

Multi-level governance practices can influence these factors and play a significant role in the municipal level's ability to actively and fruitfully engage with citizens. The managerial style of governance, typified by Chile, emphasises local government's role as an efficient service provider, and accountability to citizens is oriented towards this and the realisation of central government programming objectives. This approach is associated with limited transparency in local government administration, and citizen participation is considered one of many tool to help improve services. The emphasis is placed on enabling citizens to choose between mechanisms of service delivery, while the ability to exercise "voice" in policy design and resource allocation is minimal as it can interfere with national level priorities (Nickson, 2011). Thus, Chile's "managerial" approach to multi-level governance relations (Box 5.1) (Nickson, 2011) may be one of the fundamental barriers to more "participatory" governance.

Box 5.1. **The "managerial" and "governmental" typologies of local government administration**

In municipal systems characterised as "managerial" the primary objective is to deliver public services efficiently. Competences are defined and regulated by law, and local government is often perceived as purely administrative. In this typology, there is an implied political subordination of local government to central level directives/dictates, and a subsequently conflictual relationship between government levels. Finance tends to be marked by large intergovernmental transfers, which are often earmarked. Relations tend to be characterised by confrontation rather than consensus. Here, municipal level accountability to citizens is focused on cost-efficient service delivery, reflecting the central government's aim.

Box 5.1. **The "managerial" and "governmental" typologies of local government administration** *(continued)*

Municipal systems that are classified as "governmental" also emphasise service delivery but there is more room for local government to represent the community's shared interests and to make policy choices for it. In these systems, there is a greater sense of shared responsibility between the central and local levels for service delivery, and local government generally has significant decision-making authority over local taxes and tax rates. Multi-level relations reflect greater negotiation and consensus than conflict. Accountability of local government is to citizens rather than to the central government, and the focus is on consultative or participatory practices channelled through civil society organisations (CSOs), which represent local interests in the policy-making process.

These typologies are, of course, stylised, but elements of the "managerial" group can be found in the English system, as well as that of Australia, New Zealand, Japan, and some countries in Northern Europe. Evidence of the "governmental" typology is more visible in France, Italy, the Nordic countries, and Spain for example. In Latin America, while local governments reflect characteristics emblematic of both systems, the general tendency is toward the "governmental" typology, except in Chile where the municipal government system is squarely in the "managerial" camp.

Source: Nickson, A. (2011), "Where is Local Government Going in Latin America? A Comparative Perspective," Working Paper No. 6, Swedish International Centre for Local Democracy (ICLD), Visby, Sweden.

There have been many studies evaluating participatory practices in Chile, and the OECD has addressed Chile's multi-level governance dynamic in numerous past reviews. In light of this, the current chapter limits itself to the mechanisms currently in place to promote greater participation as applied at the central and subnational levels, highlighting the multi-level governance practices when appropriate. Chile has the legal frameworks in place to support greater participation, however, the introduction of such frameworks does not ensure they become embedded in policy practice. Furthermore, the multi-level governance architecture does not support greater citizen-driven accountability or participation at the local level. Current practices are significantly top-down, municipal decision-making and policy-making activity is limited, budget flexibility is minimal, and citizen engagement is approached not from a policy perspective but rather as one of many tools to further a programming agenda.

Moving forward, if Chile wishes to strengthen accountability and citizen engagement, it will need to consider how present and future multi-level governance practices affect the capacity of government authorities and citizens to engage as partners in the governance process. In the absence of such a partnership, stronger participatory governance will remain difficult to realise.

As part of a government wide effort to reduce inequality and reform the relationship between the state and citizens, the Subsecretariat for Regional Development and Administration (Subsecretaría de Desarrollo Regional y Administrativo – SUBDERE) has developed a municipal modernisation programme that includes building community participation (*participación communal*). Through such activity, SUBDERE is seeking to improve service delivery by better understanding citizen needs, and to strengthen the social fabric through greater local government accountability to citizens. Doing so could also help address issues of real and/or perceived corruption, build trust in government,

and ideally improve inclusiveness. However, overcoming the difficulties faced in consolidating participatory practices may involve better matching mechanisms to ambitions. Overcoming such difficulties can also require better aligning participatory governance goals with multi-level governance, or adjusting the practices overall. In other words if the goal is to address problems of corruption and misuse of resources, then it may be best to emphasise mechanisms that support greater transparency and accountability. If the objective, is to strengthen citizen voice in the policy process, then the mechanisms used need to emphasise bringing citizens into the policy cycle early in the deliberation process (Wampler and McNulty, 2011). Ultimately, in order for Chile to make strong inroads in realising its ambitions for participatory governance, it may first need to address some of its most pressing multi-level governance challenges, including municipal finance as well as autonomy in establishing and acting on municipal priorities. Currently, the system is not set up to promote a more involved citizenry, much less to foster greater collaboration between government and citizens or to empower citizens as policy actors.

For the purpose of this chapter, "citizen" is broadly applied to include individuals, civil society organisations (CSOs), private sector entities, academia, etc., unless otherwise specified. Citizen engagement covers the full spectrum of government and citizen interaction, including transparency, accountability and participatory practices. The chapter begins with a brief overview of the state of participatory governance in Chile using engagement, community, voter turnout and trust in government as indicators. It then presents the country's main levers for promoting transparency, accountability and participation, and identifies some of the key issues surrounding their implementation. Following this is a discussion of what may help address the primary challenges, and the chapter concludes with a series of recommendations for action.

The current state of participatory governance in Chile

Chile appears to be facing a deficit in participatory governance. This is illustrated by a number of markers: low levels of citizen engagement, a weak sense of community, low voter registration and turnout, and low trust in government. Of course, participatory governance is more complex than these four dimensions, but they help orient decision-makers to where citizens stand with respect to their government.

Citizen engagement is low

Chile scored 1.3 for civic engagement in the most recent version of the OECD Better Life Index, placing last among OECD countries (OECD, n.d.1). Civic engagement is one dimension of citizen well-being and is a composite indicator based on voter turnout and stakeholder engagement for developing regulations. While Chile does not score too poorly on the latter (ranking 28 out of 38 countries, and scoring 1.5 on a 0-4 scale),[1] it is voter turnout where the score is particularly low, as Chile ranked 37 out of 38 countries. Broad public engagement in decision making is important for holding the government accountable and for maintaining confidence in public institutions; and voter participation is currently one of the most frequently used measures of civic and political engagement (OECD, n.d.1).

A weak sense of community, which can limit social capital

Community, or the strength of the social network, is also important for well-being. It provides emotional support and helps individuals access jobs, services and other

opportunities. In Chile, 82% of the people believe they know someone they could rely on in a time of need. This is somewhat less than the OECD average of 88%. Comparatively, Chile ranks 35 out of 38 countries in this dimension of well-being, coming just ahead of Hungary (82.2%), Korea (75.8%) and Mexico (75.3%). New Zealand scored highest with 98.6%. A weak social network can result in feelings of isolation; and socially isolated individuals have a difficult time integrating into and contributing to society. Studies also indicate that stronger social networks translate into higher degrees of social capital among members of a community, and can help that community better manage an unexpected shock (e.g. natural disaster) or crisis. In Chile, it is considered that associative networks that strengthen the sense of community are stronger in rural communities than in urban centres. Gender and education levels appear to have an incidence on community as well – where, in general, a slightly higher percentage of women believe they can rely on someone in a time of need than men, and more people who have completed tertiary education report having someone to rely on than those who have completed only primary education (OECD, n.d.2).

Voter registration and turnout levels have been falling

Voter registration and, particularly, voter turnout can reflect citizen engagement in the political process and is used as one indicator of an individual's involvement in democracy. Lower levels of voter turnout can signal a general distrust of government by citizens (OECD, n.d.1).

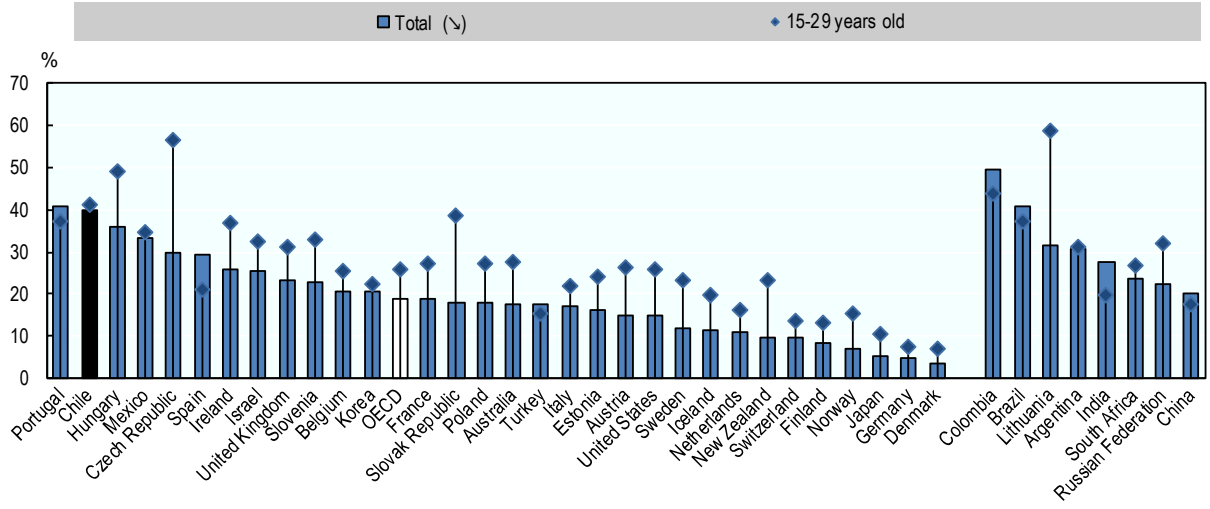
In Chile, levels of voter registration (i.e. the number of people signed up to vote) and voter turnout (i.e. the number of people who cast a ballot) have been declining for more than two decades. This is true in national elections where the number of voters dropped from approximately 7.2 million to 5.7 million between 1990 and 2013 (date of the last presidential election). In the most recent general elections for which data are available, voter turnout averaged 68% in OECD countries, while in Chile it was 49% – one of the lowest figures in the OECD area (OECD, n.d.1). A strong decline is also evident in municipal elections where voter turnout fell from about 6.9 million in 2004 (86% of eligible voters) to 4.9 million in 2016 (35% of eligible voters). It is true that in 2012 Chile shifted from a system of compulsory voting to a system of voluntary voting. While this can contribute to the decline – and after the 2016 municipal elections there is some debate as to whether voting should become compulsory once again – it does not fully explain the phenomenon. Determining factors in voter turnout generally include age, level of education, socio-economic status, identification with the political parties, the size of municipality, etc. (UNDP, 2014). One of the main reasons cited for not voting in Chile's 2012 municipal elections was because "…politics do not interest me" (30%) (UNDP, 2014). In the 2016 municipal elections, one factor that reportedly affected voter turnout included corruption, which has undermined the credibility of candidates (Buenos Aires Herald, 2016). It should be noted, however, the dataset since voting became voluntary is too small to determine if the pattern is one of general decline or if it will stabilise at approximately its current level. If the decline is persistent, it presents a red flag with respect to participative democracy and governance. It signals that people are choosing not to use voting as a mechanism of engagement in civic life, and implies that future elected governments may not accurately reflect the broadest possible segment of the population.

The situation in Chile is all the more concerning given the level of decline in voter turnout among youth and young adults. Only 38% of eligible voters under 40 years of age had registered to vote in January 2009, compared to 91% of those over 40 (Saldaña, 2009; Delamaza, 2015). In addition, Chile's youth, aged 15-29, report one of the highest levels

of disinterest in politics among OECD countries (Figure 5.1). To help build greater awareness of the importance of civic rights and duties at a young age, Chile introduced the Plan for Civic Education in Public Educational Establishments Law No. 20.911 (*Ley 20.911 El Plan de Formación Ciudadana para los Establecimientos Educacionales Reconocidos por el Estado* (Box 5.2). This law directly addresses the UNDP finding that early exposure to electoral participation has a positive incidence on voting as an adult (UNDP, 2014). If successful, the law might help correct this downward trend in the medium and long term.

Figure 5.1. One in four young people in the OECD is not at all interested in politics

Share of people reporting to be not at all interested in politics, by age group, 2012-2014



Source: OECD (2016c) *Society at a Glance 2014: OECD social indicators*, http://dx.doi.org/10.1787/888933405767.

Box 5.2. **Chile's Plan for Civic Education in Public Educational Establishments Law No. 20.911**

Effective as of the 2016-2017 school year, Law No. 20.911 requires state-recognised educational establishments to develop and implement a Plan for Civic Education (*Plan de Formación Ciudadana*). The intention is to build civic awareness beginning at the pre-primary school level continuing through secondary school. Over the years, the plans should prepare students to be responsible citizens in a democratic system that promotes social justice and progress, to be part of a society oriented to individual betterment and to get involved in the country's development. Each establishment is free to set their plan's contents as long as the plan(s) conform to the law's established objectives and the possible implementation mechanisms it outlines.

The law aims to:

1. Promote the concept of citizenship and its associated rights and duties with the aim of educating a citizenry that actively exercises and complies with these rights and duties.
2. Encourage students to be citizens that are analytical, responsible, respectful, open and creative.

Box 5.2. **Chile's Plan for Civic Education in Public Educational Establishments Law No. 20.911** *(continued)*

3. Promote the knowledge, understanding and analysis of local, regional and national laws and institutions, and the formation of civic virtues.
4. Promote students' knowledge and understanding of and commitment to the human rights recognised in Chile's constitution as well as in international treaties the country has ratified, with a special emphasis on the rights of the child.
5. Encourage students to value the country's social and cultural diversity.
6. Encourage students to participate in matters of public interest.
7. Guarantee the development of a democratic culture and ethic in schools.
8. Promote a culture of transparency and integrity.
9. Promote tolerance and diversity among students.

In order to reach these objectives and as means to implement the plans, the law identifies actions that schools can consider, including through the curriculum, extracurricular workshops and activities, teacher training, activities that open the school to the community, activities that promote a culture of dialogue and healthy conversation in school, strategies that encourage student representation and participation, and others as considered relevant by the school administration and educators.

Source: Ministerio de Educación (2016), *Ley 20.911 el Plan de Formación Ciudadana para los Establecimientos Educacionales Reconocidos por el Estado*, Chile, www.leychile.cl/Navegar?idNorma=1088963.

The aims of Law No. 20.911 also align with the conclusions and recommendations of an in-depth study undertaken on youth participation in Europe, which noted that not only is political education at the core of participation, but making political education compulsory at a young age is essential (LSE, 2013). In Los Ríos, civic education forms part of the rehabilitation/reinsertion programme in the city of Valdivia's youth/juvenile detention centre (Ministerio de Justicia y Derechos Humanos, 2017). It will take a while to see the full impact of this law on youth participation, and Chile may need to consider action that could yield more immediate results. Chile could complement the law by supporting greater youth civic participation at the national, regional and local levels. This can be achieved, for example, by identifying ways to promote youth voter registration and encourage voting, by helping local leaders promote youth engagement, as well as encouraging the establishment of municipal youth councils, either by the municipalities or by youth themselves (Box 5.3).

Box 5.3. **Approaches to promoting greater youth participation in civic life: The United States, Canada and France**

Promoting youth voter registration through candidate fora with youth

Organising candidate fora with young people can directly engage youth in the electoral process and hold candidates accountable to young constituents. Such fora permit youth to bring to the surface issues of importance to their community and peers, question candidates and educate themselves and others about the voting process. For example, during the 2010 election campaign in the State of Massachussetts (US), 400 youth leaders participated in the gubernatorial candidates' forum on youth issues. Sponsored by an NGO, the forum focused on funding, legislation, and policies related to providing youth with experiences that promote healthy development and prevent youth violence. It was co-chaired and moderated by youth leaders, and received state and local media coverage.

Promoting Municipal Youth Councils

The Canadian government provides guidelines for municipalities to build civic participation among youth with its Municipal Youth Engagement Handbook. The Handbook covers different aspects of youth engagement (i.e. educate and inform, engage and participate, recruit and retain) and was developed to be tailored to the local context, municipal resources and objectives. Encouraging youth to become active and engaged citizens is the handbook's primary objective, but through this, the Canadian Government also hopes that youth will also consider careers in the municipal public sector. Youth Advisory Councils can help ensure young voices are heard and integrated into local public policy decisions. In Windsor-Essex, Canada, 13 young people form the Mayor's Youth Advisory Committee and seek to identify the issues that matter most to their peers and establish a dialogue. The Committee encourages youth activism and advocates on behalf of young people to the City Council. Its objective is to represent the voice of youth and build relationships in the community in order to better serve the youth constituency. In London (Ontario) the Youth Council was established by a youth who saw the need for a channel for youth voice, and it currently has 15 members (one for each ward plus one for the students at Western University). Youth councillors discuss and put forth reports on issues ranging from education, transit, urban agriculture, carding and policy checks, building healthy communities, etc. The London Youth Advisory Council has a strong relationship with the City of London and is recognised as its official Youth Advisory Council but remains an independent, not-for-profit organisation.

In France, the *Association Nationale des Conseils d'Enfants et des Jeunes*, is the national federation for a network of more than 2 500 youth councils around the country. The councils aim to support representative democracy, and were created by local communities (municipal, inter-municipal, department, regional levels). They highlight proposals brought forward by the youth constituency to improve their area, and promote the co-creation of public policies in their specific areas. These councils not only promote greater civic awareness among youth and develop local democracy, they also represent the diversity of youth in a community.

Source: CSSP (2011), *Results Based Public Policy Strategies for Promoting Youth Civic Engagement*, www.cssp.org/policy/papers/Promoting-Youth-Civic-Engagement.pdf; Federation of Canadian Municipalities (n.d.), *The Municipal Youth Engagement Handbook*, www.fcm.ca/Documents/tools/FCM/Municipal_Youth_Engagement_Handbook_EN.pdf; Mayor's Youth Advisory Committee (n.d.), " About Us", Mayor's Youth Advisory Committee, www.windsoryouth.com/; London Youth Advisory Council (n.d.), "Home", https://lyac.ca/; Association Nationale des Conseils d'Enfants et de Jeunes (2017), "Participation et Conseils: Présentation generale", http://anacej.asso.fr/lanacej/.

Low trust in government

A decline in voter turnout can also signal a general distrust in government or disillusionment with the political process. In Chile, citizen confidence in the national government dropped to 32% in 2011,[2] 11 percentage points lower than in 2007, and below the OECD average of 40% for the same year[3] (OECD, 2013a). Between 2011 and 2015, trust in Chile's public sector was low, scoring 4.2 out of 10 points in 2015, and never rising above 4.4 (in 2012) on a 10-point scale, with 10 indicating a "high level of trust" (MORI, 2015). It can also result in a lower turnover of elected officials (i.e. high re-election rates). This is one interpretation of the high renewal (re-election) rate of acting mayors in the 2016 municipal election. Not only was voter turnout low – according to some sources potentially the lowest since 1963 – 73% of the mayors up for re-election won their constituencies. While this can signal the high popularity of an official, combined with low voter turnout in Chile it may be reflecting apathy toward institutional politics on the part of the electorate, in itself signalling discomfort or uneasiness with democratic institutions, such as political parties. Such uneasiness grows with problems of corruption and a decline in trust or confidence in the various institutions (UNDP, 2016).

Low levels of trust in government are also reflected in the low level of trust people have in the information that government provides. Only 40% of people surveyed indicated that they trusted information provided by public sector institutions, with 53% of respondents indicating that they did not agree with the question: "If a person requests information from a public sector institution, the information received will be reliable" (MORI, 2015). Online information is considered to be even less reliable. In 2015, only 33% of respondents felt they could have confidence in the information made available online by public institutions. In general, solicited information is perceived to be confusing or unclear (35% of respondents); not truthful (22%); not transparent (hidden) (20%); or incomplete (20%) (MORI, 2015).

Strengthening trust in government can require building trust through policies and actions and also paying attention to the "how", "for whom" and "with whom" of public policy, in addition to "the what". Thus, it is just as important to include citizens in the policy development process, as it is to ensure strong policy results (Bouckaert, 2012; OECD, 2013a). There is a bit of a "chicken and egg" dynamic here, however: greater participation comes with greater trust, as citizens may choose not to participate if their level of trust is low (Wampler and McNulty, 2011); and greater trust generally yields greater participation and stronger networks.

Participatory governance frameworks, institutions and actors in Chile

The deficit in participatory governance that Chile is experiencing is not for a lack of laws – one of the enabling factors for greater citizen participation – mechanisms, guidelines or effort. Since 2008, Chile has made significant additions to its normative frameworks for promoting participatory governance (Box 5.4). While these changes impact activity at all levels of government, there are concerns regarding their effectiveness, principally at the local level. The frameworks and tools introduced are all dependent on multi-level governance for their successful implementation. However, there are significant differences in how firmly rooted they are in government, due in part to political will at the national and subnational levels to support them and in part to the length of time they have been in place. While the need for more effective citizen engagement has been discussed for more than a decade, with the exception of transparency practices, implementation of the various engagement levers has been seriously underway since the introduction of Law 20.500 Associations and Citizen

Participation in Public Management (*Ley 20.500 Asociaciones y Participación Ciudadana en la Gestión Pública*) in 2011 and the 2014 Presidential Instruction 007/2014 (OECD interviews).

Box 5.4. **Chile's government frameworks and implementation mechanisms to support participatory governance**

Chile has a series of legal frameworks to support participatory governance, ranging from its constitution to newly passed laws for citizen participation. These mechanisms, however, vary in their strength and degree of adherence.

Constitution – the foundation for participative democracy at all levels of government. It guarantees freedom to express opinions (§12), the right to assemble peacefully (§13), the right to petition authority (§14), and the right to associate (§15). Article 113 stipulates that the Regional Council is responsible for ensuring citizen participation at the regional level; and article 118 makes municipalities responsible for delineating how and in what ways the community will participate in municipal activities, including in its economic, cultural and social development.

Law No. 18.695 "Municipal Organic Law" *(Ley 18.695, Ley Orgánica Municipal)* – the organising law for municipalities, it establishes the structure of local government, with the mayor as the highest authority, the municipal council and other supporting bodies such as the Council of Civil Society Organisations and the Council for Public Safety. It also requires each municipality to establish an ordinance (*ordenanza)* governing citizen participation. Updates to the municipal council's role, as well as municipal transparency and probity practices, were introduced in 2014 through Law No. 20.742 Improving the Oversight Role of the Municipal Council; Strengthening Transparency and Probity in Municipalities; Establishing Posts and Modifying Norms for Personnel and Municipal Finance (*Ley 20.742, Perfecciona el rol fiscalizador del consejo; fortalice la transparencia y probidad en las municipalidades; crea cargos y modifica normas sobre personal y finanzas municipales).*

Law No. 20.285 Access to Public Information *(Ley 20.285 Sobre Acceso a la Información Pública)* – passed in 2008 and commonly referred to as the Transparency Law (*Ley de Transparencia)* it establishes citizen access to information at all levels of government and from various public entities, including state enterprises. National and subnational governments, including municipalities are subject to this law equally, which requires publication of information on procurement, budgets, audits, transfer of funds, organigrams, personnel levels and types, staff remuneration, citizen participation mechanisms, etc. Importantly, the law also sets up a national-level Transparency Council (*Consejo para la Transparencia*) to which people can lodge a complaint against any public body that does not make information permanently available (through an electronic site), as required by the law.

Law No. 20.500 Associations and Citizen Participation in Public Management (*Ley 20.500 Asociaciones y Participación Ciudadana en la Gestión Pública*) – introduced in 2011 to better support civil society and reinforce citizen participation practices. The law establishes a national registry of non-profit entities and a fund for strengthening public interest organisations (*Fondo de Fortalecimiento de las Organizaciones de Interés Público*). It also modifies other legal frameworks supporting citizen participation, including Law No. 18.575 regulating the State Administration, and Law No. 18.695, the Organic Law of Municipalities. This law requires that central government entities ensure citizen participation; publish policies, plans, programmes, etc.; publish an annual report on public participation; and establish Civil Society Councils (*Consejos de la Sociedad Civil*) serving as advisory bodies, on which sit representatives from NGOs and CSOs active in their specific sector. At the municipal level, the law replaces the formerly required Economic and Social Council (*Consejo Económico y Social*) with a municipal Council of Civil Society Organisations (*Consejo Comunal de Organizaciones de la Sociedad Civil* – COSOC).

Box 5.4. **Chile's government frameworks and implementation mechanisms to support participatory governance** *(continued)*

It specifically covers organisations of public interest (*organizaciones de interés público*) which are defined as non-profit entities whose purpose is to promote the general interest in the areas of citizen rights, social assistance, education, health, environment and any other public good, and which are in the national registry. Volunteer organisations also fall under Law No. 20.500.

Presidential Instructive No. 007/2014: Policy for Citizen Participation – intended to support Law No. 20.500 was introduced in 2014. The document seeks to clarify and further support the implementation of participatory mechanisms by articulating the government's rationale for stronger civil society and citizen participation, setting out the government's objectives for citizen participation, and establishing implementation guidelines for Law No. 20.500 directed to ministries and other state bodies. It also identifies tools for greater participation that could be added to the existing menu of possible activities, including: public audiences, participatory budgeting, territorial and sector-based citizen councils (*Cabildos ciudadanos, territoriales y sectorales*), fora for participative dialogue, and digital platforms for participation. Like Law No. 20.500, it give ministries, their dependent bodies and public services a six month timeframe to: 1) implement specific instructions including rules for citizen participation; 2) create a Unit for Citizen Participation in each state body; 3) establish Civil Society Councils (*Consejos de la Sociedad Civil*) in each state body, to ensure that citizens' voices are heard throughout the policy cycle; 4) develop a reporting mechanism on public participation (*cuenta pública participative*); and 5) establish the National Registry for Non-profit Entities.

Sources: Republic of Chile (1980/rev 2015), *Constitución Política de la República de Chile*. 1980 (rev. 2005), www.constituteproject.org/constitution/Chile_2015?lang=en; Ministerio del Interior (2006), *Ley 18.695, Orgánica Constitucional de Municipalidades*, Subsecretaria de Desarrollo Regional y Administrativo, www.subdere.gov.cl/sites/default/files/documentos/ley_18.695_municipalidades_-_abril_2010_5a_ed.pdf; Ministerio Secretaría General de Gobierno (2011), *Ley 20.500 sobre Asociaciones y Participación Ciudadana en la Gestión Pública, División de Organizaciones Sociales*, www.leychile.cl/Navegar?idNorma=1023143; Republic of Chile (2014), *Instructivo Presidencial No. 007, de 6 de agosto de 2014*, *Instructivo Presidencial para la Participación Ciudadana en la Gestión Pública, Presidencia*, www.guiadigital.gob.cl/sites/default/files/instructivopresidencialparticipacion2.pdf.

A strong institutional approach enhances transparency

The primary driver in Chile's move towards greater transparency is Law No. 20.285 on Access to Public Information (*Ley 20.285 Sobre Acceso a la Información Pública*). Commonly referred to as the Transparency Law (*Ley de Transparencia*), it is fundamentally an access to information law, applicable to all levels of government as well as various public entities, including state enterprises. Importantly, the law established a national Transparency Council (*Consejo para la Transparencia*) that is responsible for promoting national and subnational government transparency, ensuring that the law is properly implemented, conducting audits, rendering judgement on complaints or denials of information, and sanctioning poor compliance (SEGPRES, 2008). Citizens can lodge a complaint against any public body that does not make information permanently available (through an electronic site) as required by this law.

Critical players in the transparency initiative at the central level include the Modernisation and e-Government Unit/Commission for Integrity and Transparency (*Unidad de Modernización y Gobierno Electrónico/Comisión de Probidad y Transparencia)* within the General Secretariat of the Presidency (SEGPRES), and the

Transparency Council mentioned above. Regionally, deconcentrated central-level bodies are also required to provide information, and locally, municipal administrations must ensure access to information.

Chile's approach to promoting transparency is relatively streamlined and flexible: a national council was established with oversight and sanctioning capacities, government bodies, together with local authorities, were clearly tasked with the how, where, and what of making information available, and, while the channels for access may not fully align with citizen preferences or capacity, there has been significant investment in ensuring that information is available and accessible. This is in contrast to the frameworks established to institutionalise citizen engagement, which are top-heavy (i.e. more present at the central level than at the local level), fragmented, and sometimes unclear, or contextually not appropriate.

The legal framework for citizen participation lacks compliance incentives

The normative (legal) framework and requirements for citizen engagement have been established over time in a series of different binding mechanisms, as presented in Box 5.4 above. Through these, co-ordination responsibility has been clearly assigned, internal structures to promote implementation have been established, and mechanisms to foster a more participatory approach have been identified. In addition, the presidential instruction clearly defines citizen participation as a co-operative process through which the state and the citizenry, together, identify and discuss public challenges and potential solutions, and use methodologies and tools that create an opportunity for reflection and collective dialogue with aim to incorporate citizens in the design and implementation of public decisions (Republic of Chile, 2014).

Law No. 20.500 and the Presidential Instructive 007/2014 identify ways that central government authorities can help foster greater participation, including public audiences, participatory budgeting, plebiscites/referenda, territorial and sector-based citizen councils, participative dialogue, and digital platforms for participation. While authorities are not limited to these mechanisms, they are encouraged to at least give these considerations.

Neither Law No. 20.500 nor the Presidential Instructive are as prescriptive with the municipal level as they are with the central level. They do, however, require that municipalities update their municipal ordinances to include citizen participation. Legally, these ordinances must include the participatory mechanisms mandated by the Municipal Organic Law and Law No. 20.500, specifically: an office for citizen complaints (*Oficina de Reclamos, Información y Sugerencias* – ORIS), public audiences, a consultative dimension to the municipal Regulating Plan (*Plan Regulador),* the PLADECO, and to public accounts. Municipalities must also establish a municipal Council of Civil Society Organisations (*Consejo Comunal de Organizaciones de la Sociedad Civil* – COSOC) as an advisory body. Municipalities are required to ensure that their citizen participation ordinances mention the types of organisations that should be consulted and kept informed, including the dates or periods when this information must be shared. In addition, the ordinances must specify the mechanisms and means by which participation will be achieved, with consideration being given to participatory budgeting, citizen consultation and other methodologies (MSGG, 2011).

Implementation is a challenge at the local level. By the end of 2015, 287 of Chile's 345 municipalities (approximately 83%) had updated their citizen participation ordinances (SUBDERE, 2015b), and 63% had an established COSOC as required by law[4]

(MSGG, 2015). In no region is there 100% compliance with respect to establishing a COSOC (MSGG, 2015). Ensuring that the COSOC has the resources necessary to operate, including a budget, is a municipal responsibility per Law No. 20.500, which could be a contributing factor.

The top-down approach with legally-binding compliance is clearly unsuccessful as a means to ensure implementation, particularly at the subnational level. Non-compliance with the Transparency Law can be sanctioned by the National Transparency Council, however there is no such sanctioning mechanism – either for non-compliance or lax compliance – associated with Law No. 20.500 or the Presidential Instruction. Research suggests that when participatory governance is promoted in a heavily top-down manner, there is often a gap between what is established by higher levels of government and the needs and demands of the local level. It can generate a "self-interested" or short-term approach to participation, wherein local officials "go-along" with whatever programme is on offer in order to secure funds, but there is little associated incentive for them to adopt a long-term approach to participatory governance (Wampler and McNulty, 2011).

Chile may need to consider incentive mechanisms to make compliance more appealing or non-compliance more risky. Financial incentives or fiscal sanctions are often the most effective. However, it would be important to ensure that incentive mechanisms do not limit results by rewarding municipalities that only superficially apply the law – i.e. take a short-term or self-interested approach in order to access funding or to "box-tick" citizen participation. In addition, it is important to understand what is really behind a lack of compliance. While financial incentives could help those communities where finances are limited, there is some evidence to suggest that resources are not the only determining factor behind poor compliance[5] (SUBDERE, 2015b). It may also be generated by a lack of citizen awareness of the law and their right to participate, a poor understanding of the long-term advantages of participatory governance on the part of officials and citizens, a perceived threat to established power contributing to limited political will, and/or a lack of human resource capacity. It can also be out of the hands of the municipalities themselves. There are some local authorities reporting that their call for COSOC representatives went unheeded (OECD interviews), both local officials and COSOC or potential COSOC representatives attribute this to the strictly advisory nature of the body, resulting in a lack of stakeholder interest given a general feeling that participation on an advisory level will yield few tangible results (OECD interviews).

The institutional approach is centrally driven and top heavy

The government itself may be limiting the effectiveness of Law No. 20.500 through its institutional approach. The Division for Social Organisations (*Departamento de Organizaciones Sociales* – DOS) within the Government General Secretariat co-ordinates government activity for citizen participation. This includes producing an annual report on citizen participation, establishing relevant mechanisms to co-ordinate participatory initiatives, publishing information on citizen engagement practices and results, reinforcing links between government and civil society, and promoting greater participation in the policy cycle. The Secretariat for Regional Development (SUBDERE) is responsible for promoting the formation of the COSOC in municipalities, providing any necessary counsel. Line ministries, meanwhile, promote engagement within their own sector (e.g. environmental protection or healthcare).

As per Law No. 20.500 and Presidential Instruction 007/2014, central government bodies, including line ministries, are required to set up Civil Society Councils (*Consejos*

de la Sociedad Civil) as part of their governance structure. Their role is to ensure that their sector has adequate and appropriately organised citizen consultation practices on matters concerning policies, programmes, plans and budgets, throughout the policy cycle (Republic of Chile, 2014). Some sectors created one council for the ministry and its dependent bodies, while other entities created one council per entity attached to a ministry (i.e. ministry and dependent bodies). The actual functioning of these councils and their effectiveness depends on the parent ministry or agency. Each entity of state administration is also required to establish Citizen Participation Units (Republic of Chile, 2014). These units are responsible for ensuring the necessary conditions for the proper functioning of the Civil Society Councils, providing resources and space for their sessions, and managing and executing training sessions for their representatives, among other capacity-building measures (Republic of Chile, 2014). In addition, there are two national level councils to support citizen participation – the National Council for Citizen Participation and Strengthening Civil Society (*Consejo Nacional de Participación Ciudadana y Fortalecimiento de la Sociedad Civil*) and the National Council for the Fund to Strengthen Organisations of Public Interest (*Consejo Nacional del Fondo de Fortalecimiento de las Organizaciones de Interés Público*) (Box 5.5). Unlike the National Transparency Council, these entities do not have the capacity to sanction non-compliance or unsatisfactory compliance.

Box 5.5. **National councils to support citizen participation**

The National Council for Citizen Participation and Strengthening Civil Society (*Consejo Nacional de Participación Ciudadana y Fortalecimiento de la Sociedad Civil*) was established by the Presidential Instruction007/2014 and made operational by Presidential Instruction in January 2016. On it sit 24 councillors from diverse CSOs. Among its tasks is to reform Law No. 20.500 so that it takes into consideration this new body, and to provide a first report on citizen participation in Chile that will be the basis of a future citizen participation index. It is also responsible for promoting the right of citizens to participate, and is able to audit participation, encouraging public entities to adequately meet their participation obligations. In January 2017, the Council released its report on the state of citizen participation in Chile that included recommendations for strengthening the legal framework for participation – for example by introducing constitutional reform to recognise citizen participation as a human right, and by modifying Law No. 20.500 to recognise the Council, to introduce a Subsecretariat for Citizen Participation, and to better define COSOC. In addition the report recommends establishing a series of standards for citizen participation.

The second council is the National Council for the Fund to Strengthen Organisations of Public Interest (Consejo Nacional del Fondo de Fortalecimiento de las Organizaciones de Interés Público). It is comprised of high-level ministerial representatives as well as presidential appointees, and members of six registered organisations of "public interest" (civil society). In addition to the National Council, regional councils (whose structure mirrors that of the national level) are primarily responsible for approving and adjudicating the financing of national (and regional) level projects to promote citizen participation.

Source: MSGG (2015), *Cuenta Pública 2015*; Consejo Nacional de Participación Ciudadana (2017), *Estado de la Participación Ciudadana en Chile y Propuestas a la Reforma de la Ley 20.500 sobre Asociaciones y Participación Ciudadana en la Gestión Pública: Informe Final*; MSGG (2011), *Ley 20.500 sobre Asociaciones y Participación Ciudadana en la Gestión Pública*.

It appears that the government is creating a large bureaucratic and administrative structure to implement this law and paradoxically, it seems that the government is placing

oversight units to oversee oversight units. This structure risks creating administrative burden, confusion, overlap, and significant fragmentation, which can impact the law's effectiveness. The entities are also inward looking (ensuring participation at the central level) rather than being focused on setting standards or identifying mechanisms to clarify and guide citizen participation in their sectors at the local level. They can also fragment citizen participation by sector, rather than promoting a broader, cross-sector, society-wide approach to participation. France, with its Economic, Social and Environmental Council has taken an approach that may be valuable to Chile, not only at the national level, but potentially translated to the regional level as well (Box 5.6).

Box 5.6. **The Economic, Social and Environmental Council in France**

France's Economic, Social and Environmental Council (Conseil Économique, Social et Environnemental) is a "constitutional consultative" assembly. It represents economic, social and environmental activity, and aims to promote co-operation between diverse social and professional interest groups, ensuring also that they are part of the public policy process. Covering five main areas it: 1) advises the government and the parliament and participates in the development of economic, social and environmental policy; 2) promotes dialogue between diverse socio-professional groups to identify areas of common interest and concern in order to shape proposals in the public interest; 3) contributes to the review of economic, social and environmental public policy matters; 4) promotes constructive dialogue and co-operation with consultative bodies at the local level, as well as with international and EU counterparts; and 5) helps keeps citizens informed. It receives petitions not only from the government and both houses of the legislature, but from citizens as well.

The Council is comprised of 233 members, all of whom are active in civil society and appointed for a five-year term. Of these members, 140 represent economic matters and social dialogue, 60 represent social and territorial cohesion and communities; and 33 represent environmental matters and nature conservation. Within these three categories there are representatives from diverse interests, such as family associations, youth and student groups, experts in sustainable development, the craft industry and private industry.

The Council operates in a manner similar to that of a parliamentary assembly, holding plenary sessions, functioning in sections (thematic work groups) that prepare studies and draft opinions in their respective fields (e.g. the sustainable management of territories; economy and finance; education; labour and employment; culture and communication; and agriculture, fisheries and food).

Source: ESEC (2011), "About the ESEC", Conseil Économique, Social et Environnemental, Paris, France, www.lecese.fr/en.

Ability to promote and ensure participatory practices varies significantly among actors

Chile's central-level actors channel their efforts to building participatory governance through the legal framework provided by Law No. 20.500 and the Presidential Instruction, as well as capacity-building through manuals, guides and workshops. Law No. 20.500 does not extend to regional governments (MSGG, 2011; MSGG, 2016a). Nevertheless, some regional governments, such as that of Bío Bío, are pursuing regional-level initiatives to build citizen participation. At the municipal level, the primary actors focused on building participatory governance practices are locally elected officials, including municipal councillors, COSOC representatives, civil society, and citizens.

Elected officials and local public administration can play a powerful role

Studies of citizen engagement practices in Chile underscore the power of the mayor in promoting participatory government and implementing engagement mechanisms. Bringing citizens into the decision-making process may be a perceived threat to power. Thus, the degree of citizen engagement in a municipality will depend considerably on the mayor, and could conceivably shift if a new mayor takes office. The uncertainty that this can cause might be minimised in a number of ways: 1) by educating local officials about the benefits of participatory practices; 2) by increasing citizen awareness of their right to participate, generating a demand for participatory practices, and ensuring that citizens feel sufficiently empowered to demand follow-up to their input; and 3) by ensuring that citizen engagement practices become institutionalised in the fabric of the municipal governance structure (e.g. through a municipal citizen participation policy, by requiring and facilitating specific practices such as participatory budgeting), thereby minimising dependence on the will of the mayor and the vagaries of electoral cycle. Shifts of this nature, however, are often cultural, take time, and can require adjustments in resource allocation for municipalities (e.g. to facilitate participatory budgeting).

The role of municipal councils in local participatory governance could be stronger

Municipal councils are generally considered to be the highest governing body in a municipality. Depending on the country, municipal councils play a greater or lesser role in defining and implementing their municipality's strategic direction, policies, plans, programmes, and services, as well as the budget and administration. In some countries, they also have clear responsibility for ensuring the accountability and transparency of municipal practices. Municipal councillors represent the interests and well-being of their own constituents and the community at large. They are often keenly aware of their community's needs and how to address them most effectively. Chile's municipal councils have limited influence over municipal budgeting, strategic and planning processes, and establishing priorities for municipal development (as well as monitoring implementation), which limits their effectiveness as a conduit for participatory governance.

In Chile, municipal councillors are directly elected every four years and are eligible for re-election with no term limits. The number of councillors varies between 6 and 10, depending on the size of the municipality. In 2015, there were a total of 2 240 municipal councillors in Chile, an average of 6 per municipality. This is somewhat low when compared to a significant number of OECD countries (Table 5.1), casting doubt over the breadth and depth of citizen representation in local government bodies.

Table 5.1. **Average number of municipal councillors in select OECD countries, 2015**

Country	Average number of municipal councillors per municipality	Number of municipalities	Total number of municipal councillors
Hungary	5	3 163	16 841
Chile	6	345	2 240
Portugal	7	308	2 086
Iceland	7	74	504
Slovakia	7	2 911	20 830
Spain	7	8 078	59 136
Czech Republic	10	6 234	62 137
Italy	11	7 794	87 746
Latvia	14	119	1 618
France	14	36 756	524 280
Estonia	15	198	2 951
Turkey	15	1 364	20 538
Slovenia	16	212	3 365
Poland	16	2 475	39 959
Belgium	22	589	13 072
Denmark	25	98	2 442
Norway	25	429	10 785
The Netherlands	27	340	9 175
Greece	30	325	9 691
Finland	30	320	9 674
Ireland	31	31	949
Sweden	44	291	12 763
United Kingdom	53	400	21 166
Germany	60	402	23 278

Source: European Commission - http://ec.europa.eu/justice/gender-equality/gender-decision-making/database/politics/municipal-councils/index_en.htm.

The structure and implementation of Law No. 18.695, the Municipal Organic Law, subordinates the council to the mayor who is responsible for municipal administration. On paper, Chile's municipal councils play an extensive role as they advise, regulate and supervise the mayor's actions and conduct. Their remit also extends to fostering the participation of the local community in government, which can also overlap with COSOC responsibilities (see Chapter 1). In practice, their influence in shaping local development strategy, policy, or use of funds is limited. There is no significant system of checks and balances and the result is an unequal balance of power.

Municipal councils could be influential in participatory governance, particularly as one of their responsibilities is to ensure community participation. In addition, they must approve their municipality's Municipal Regulating Plan (*Plan Regulador Comunal* – PR)[6] that requires citizen consultation (Republic of Chile, 1980/Rev. 2015; Ministerio del Interior, 2006). However, their actual role in participatory practices appears to be minimal

– one that depends on the participatory mechanism used. For example, they can have an incidence on participatory budgeting since municipal councils must approve the budget. However, they cannot execute a line item veto on the budget (be it the general budget or participatory). Either they approve the budget in its entirety or they reject it outright. They cannot request that the percentage dedicated to participatory budgeting, for example, be increased; nor can they request that funds be reallocated.

In 2014, Law No. 20.742 ushered in changes to the Organic Law that strengthened and expanded – to some extent – the role of municipal councils, particularly in their oversight, transparency and probity enforcement functions. For example, they can now submit matters to the council for consideration unless these matters have an incidence on the budget; they can contract external auditors at the beginning of each new mayoral term in order to evaluate the municipality's financial situation; they can request to meet with directors of municipal offices in order to formally question them and obtain information (one third of the council members must vote for this) (Richard, 2014). This falls short, however, of giving municipal councils a role in ensuring accountability to citizens and supporting the development of social accountability where citizens play a role in ensuring the accountability of their elected representatives. In addition, the law does not address some intrinsic imbalances: including the lack of checks and balances between the executive and the council (i.e. there is no sanctioning capacity if the mayor improperly executes his functions). In other countries, for example, in the Netherlands, the municipal council supervises an executive committee (a body composed of municipal councillors and presided over by the mayor), and the council has the right to question, criticise and sanction this committee (though not the mayor who is a Crown appointee) (Association of Netherlands Municipalities, 2007).

Furthermore, the new law does not alter the advisory nature of the council, thus failing to increase its capacity to serve the mayor as an active partner in municipal development and strengthen the role of councillors as a voice for their constituencies and the community as a whole. Such a role is seen more strongly among municipal councils in other OECD countries, such as in Australia, Canada and France, where the roles and responsibilities are broader and combine oversight with strategic, policy, administrative and constituency advocacy functions. For example, municipal council responsibilities in these countries can include policy making, ensuring the effective use of resources by defining objectives, setting priorities, establishing clear administration practices, ensuring transparency and accountability in local government practices, monitoring municipal activities and the management of municipal assets, developing financial strategies, facilitating citizen participation, creating and supervising municipal public service delivery, provide support for local development strategies and programming, etc. (Good Governance Guide, 2012; Ministry of Municipal Affairs and Housing, 2014; République Française, 2016).

Municipal-level Councils of Civil Society Organisations have limited impact

While Law No. 20.500 stipulates that each municipality must have a Council of Civil Society Organisations (*Consejo Comunal de Organizaciones de la Sociedad Civil* – COSOC), the law remains vague as to their purpose. They are to consult with citizens on behalf of local authorities on matters selected by local officials, and keep CSOs and other relevant entities apprised of the operations of the municipality (MSGG, 2011). Each municipality establishes the organisation, composition, competences and functioning, etc. of their COSOC (MSGG, 2011). There is logic to this since municipal officials are closest to the CSOs in their localities. The municipal government is required by law to provide

the resources – financial and structural – necessary for operation. However, there are reports that many COSOC are under-funded, and/or limited in how funds can be used and there are no provisions in the law to support the municipalities in this endeavour (OECD interviews). As advisory bodies, COSOC have no power to sanction the mayor or municipal council for failing to implement participatory measures in a satisfactory manner. The mayor presides over the COSOC (MSGG, 2016a), which could create a degree of conflict of interest, and COSOC representatives are community organisations and organisations of public interest in the local area. At the same time, despite the fact that the COSOC must agree to the regulation (*reglamento*) that governs their structure and operations, the law gives significant leeway to the mayor to create a relatively weak organisation, especially if there is little political will to implement participatory mechanisms.

The impact of the COSOC depends on the municipality itself. In some localities they are highly relevant, providing opinions and conclusions; in others, especially poorer municipalities, it is more difficult. A 2015 report published by the Division of Social Organisation within the *Secretaría General de Gobierno* indicated that in practice COSOC are usually given a limited role in municipal governance – often limited to commenting on the management of public accounts by the mayor and the general progress of the municipality, the Municipal Development Plans (PLADECO), municipal investment plans, and modifications to the Municipal Regulating Plans (PRC) (MSGG, 2015). Thus, while the COSOC weigh in on matters important to the municipal administration (e.g. the budget) the matters on which they are most frequently consulted are those where consultation is required by law. They do not necessarily have room to directly (or indirectly) influence critical issues relating to citizen participation and municipal functioning, such as municipal services, specific municipal investments, the municipality's development trajectory, the use of development funds, etc. (Table 5.2) (SUBDERE, 2015b; MSGG, 2015).

Table 5.2. **Municipal matters in which COSOC have had input or participated (2015)**

Municipal responsibility	% of total	Number of responses
Mayor's public account (Cuenta Pública del Alcalde)	53.1%	68
Draft municipal budget	43.0%	55
Municipal Development Plans (PLADECO)	42.2%	54
Municipal Regulating Plan (PRC)	35.2%	45
Coverage and/or quality of municipal services	24.2%	31
Specific municipal investments	21.9%	28
Unable to participate in any process or municipal event	3.1%	4
Naming municipal streets and alleys	2.3%	3
Modification of Law No. 20.55	0.8%	1
Prioritisation of projects for the Regional Fund for Local Investment (*Fondo Regional de Inversión Local)*	0.8%	1
Municipal annual education plan (Plan Anual de Desarrollo de Educación Municipal – PADEM)	0.8%	1
Potable water	0.8%	1
Do not know	2.3%	3

Note: N = 128; Respondents could select more than one topic.

Source: MSGG (2016b), "Sobre Asociaciones y Participación Ciudadana en la Gestión Pública", Informe del Proceso de Consulta Participativa Ley 20.500, Dirección de Organizaciones Sociales.

Another challenge facing COSOCs, in addition to unclear or highly restricted mandates and dependence on the political will of their mayors, is a poor and potentially competitive relationship with the Municipal Council. A 2015 SUBDERE survey indicated that almost 42% of responding municipalities did not have a formal or informal agreement establishing meetings between the COSOC and the council, and neither entity invited representatives of the other to their meetings. Despite a small sample size (128 municipalities), the trend is significant. In addition, only 13% of the COSOC indicated that they meet with the Municipal Council in plenary sessions (SUBDERE, 2015b). This may be due to unclear mandates, and/or a potential (real or perceived) overlap of roles and responsibilities, leading to a degree of territorialism or competition between the entities. Moving forward, clarifying the role and mandate of COSOCs will be essential for them to function properly and become valuable partners for municipal leaders, both for elected officials and civil society representatives.

The civil society landscape is dense but fragmented and lacks partnership capacity

Participatory governance often focuses on the participation of individuals, for example in citizen consultation or in providing and obtaining data and information. However, it is also strongly supported by civil society organisations (CSOs) and their capacity to represent the interests of citizens before government or other powerful actors, as well as to help monitor accountability and transparency vis-à-vis policies and programmes in their areas of activity. Thus, a dynamic and effective CSO community is critical for participatory governance. When CSOs are weak, they tend to be more reliant on government, and thus are not sufficiently strong to act as true partners. In addition, citizens may bypass them, relying on their own access to government officials, such as municipal councillors, especially in clientelistic environments (Wampler and McNulty, 2011). Unfortunately, Chile's CSOs are currently unable to provide the necessary counterweight to government.

There has been very rapid growth in the number of Chilean CSOs, certainly since 1986, but especially since 2006 – almost 50% of the total number of CSOs were established in the period from 2006 to 2015 – possibly a reflection of the impact of Law No. 20.500 and an increasing demand by citizens to be involved in the governance process (Universidad Católica, 2016). In 2014, the government's registry of legal entities with a non-profit status listed approximately 182 000 legal non-profit organisations[7] (MSGG, 2016b). Using a broader definition of CSOs, another study identified just over 234 500 CSOs[8] in 2015, yielding an average number of 13 CSOs per 1 000 inhabitants in the country. By comparison, Australia had 6.7 CSOs per 1 000 inhabitants (in 2013), and the US 4.8 CSOs per 1 000 inhabitants. Total population figures in 2013 for these countries were 17.6 million in Chile, 23.1 million in Australia and 316.5 million in the United States (Universidad Católica, 2016). It is clear that there is no lack of opportunity to participate in a CSO given the sheer number, and volunteer levels are high. According to the World Gallup Poll about 15% of the population volunteered in 2013 (OECD, n.d.2). Volunteerism in Chile is particularly high among students[9] – 40.7% – placing Chile well above the OECD average (29.7%) (OECD, 2015a). Volunteerism is an important factor when considering citizen participation because participation often involves the unremunerated time of individual citizens. Chileans are clearly willing to contribute to their community, build greater solidarity, and donate their time as well as their money – and there is ample opportunity to do so through civil society. Thus a lack of CSOs or a lack of volunteerism in Chile does not explain low citizen engagement rates.

Rather, citizens may be disinclined to engage if there is a feeling that their voice – unless in response to a threat – does not make a difference to decision makers, thereby diminishing the incentive to engage with government, despite the high number of CSOs and volunteerism rates.

The distribution across activity sectors is also revealing (Table 5.3), particularly the low activity level seen in the category of law, advocacy and politics (i.e. traditional and formal avenues for participation) versus quite high levels in development and housing, and culture and recreation (63.7% of all CSOs).[10] Legally, the majority of Chile's CSOs (79.8%) are thematic community organisations (*Organizaciones Comunales Funcionales*), neighbourhood committees (*Juntas Vecinales*), and unions or associations of these groups (*Uniones Comunales*).[11] These organisations encompass a diverse number of activities (e.g. workers' groups, chambers of commerce, sports clubs, centres for mothers, youth organisations). Yet, a significant proportion – 76.9% – are divided between those dedicated to social development and housing (38.8%) and culture and recreation (38.1%), followed - in a distant third - by CSOs dedicated to education and research (10.7%) (Universidad Católica, 2016).

Table 5.3. **Percentage of civil society organisations active in Chile classified by INCPO[1] categories**

ICNPO Classification	%
Development and housing	32.1
Culture and recreation	31.6
Education and research	13.3
Business and professional associations, unions (including trade and labour unions)	11.5
Social services	5.4
Law, advocacy and politics	2.4
Health	1.4
Environment	0.9
Philanthropic intermediaries and volunteerism promotion	0.2
International organisations	0.1
Other	1.1

Notes: The International Classification of Non-profit Organizations (INCPO) was developed by Johns Hopkins University to categorise the groups and subgroups of diverse CSOs. Other here includes religious organisations, following the Universidad Católica study. The original INCPO categories put religious organisations as separate from "other" or "not elsewhere classified".

Source: Adapted from Universidad Católica (2016), Mapa de las Organizaciones de la Sociedad Civil, 2015, Centro UC Políticas Públicas, Universidad Católica; Salamon, L.M. and H.K. Anheier (1996), "The International Classification of Nonprofit Organisations: ICNPO-Revision 1, 1996," Working Papers of the Johns Hopkins Comparative Nonprofit Sector Project, No. 19, http://ccss.jhu.edu/wp-content/uploads/downloads/2011/09/CNP_WP19_1996.pdf.

Neighbourhood committees[12] have a well-defined scope of action, with the law stipulating that they can: 1) represent the community (neighbours) before the authorities in order to come to agreement about the community's development; 2) represent the community in resolving a problem before the authorities; 3) propose and implement projects of benefit to the neighbourhood; and 4) identify infrastructure and other deficits (e.g. sewage systems, lighting). These committees are funded through fees paid by each member of the committee, and they are eligible to apply for competitive funds, primarily

through the municipal FONDEVE (Box 5.7) to implement neighbourhood projects (e.g. a sports project or training programmes). The activities/projects that they can develop include those related to sports, the environment, education, training, recreation, or culture, for example remodelling a park or organising a sports competition; collaborate with the municipality in matters relating to citizen safety, auditing outlets that sell alcohol, or community plans that will increase the well-being of citizens (BCN, 2014).

Box 5.7. **Fund for Neighbourhood Development (*Fondo de Desarrollo Vecinal* - FONDEVE)**

Law No. 19.419 established the Fund for Neighbourhood Development (*Fondo de Desarrollo Vecinal* – FONDEVE) to encourage organised community participation in supporting ideas and projects that solve specific problems faced by neighbourhood committees (*juntas vecinales*). It is administered by the municipality and is financed through contributions from the municipal budget, neighbourhood residents, and some central level funding.

The objective of the fund is to support CSOs so that they can organise, prioritise their needs, and develop projects based on their area of activity. It is also intended to support the creation of projects (and particularly in the areas of culture, sport and education), that have local level impact and meet community needs, improve the quality of life, and contribute to the development and strengthening of community life.

Different municipalities include different types of projects that can receive funds from FONDEVE. These may range from improving common public spaces in the neighbourhood (painting, installing children's playgrounds), training in maintaining a clean environment (physical and natural), building community or neighbourhood infrastructure, promoting sports, recreation, and tourism by residents, citizen safety, etc.

Source: Lampa (2011), "Que es el FONDEVE?", www.lampa.cl/inicio/wp-content/uploads/2011/08/BASES_FONDEVE_2011.pdf; Las Condes (2016), "Proyectos Fondeve" Las Condes, Chile, www.lascondes.cl/servicios/destacado_dvecinal.html; Municipalidad de Temuco (2011), "XVI Fondo Desarrollo Vecinal, 2011" Municipalidad de Temuco, Chile, www.temucochile.com/thepublicidad/fondeve/basesfondeve2011.pdf.

For the most part, these are all very concrete activities where the CSO is a neighbourhood organisation whose role is less that of a broad advocate or partner in the delivery of services and more of a source through which to obtain funding to address a specific neighbourhood's needs. Overall, and in keeping with the managerial typology of municipal management in Chile, it appears that the majority of CSOs have little capacity or space to influence decisions or local policy or programming – instead they concentrate on projects within a limited geographic area and are supported financially for activities that focus primarily on infrastructure and social activities. This high level of activity within the confines of a neighbourhood boundary, rather than at a community-wide (i.e. city or town) level, further fragments networks and their activity. Thus, it can prevent building "strength in numbers" required to advocate on the behalf of citizens and ensure accountability on the part of government. It also limits their ability to become strong partners with government rather than potential adversaries.

Adjusting transparency techniques and building accountability for stronger participatory governance

Chile has focused on building greater transparency by making government information more available and more accessible. It is also a strong performer in Transparency International's *Corruption Perceptions Index* – ranking 24th out of 176 countries in 2016, with a score of 66 out of 100 possible points; thus coming in just behind France and at the same level as the United Arab Emirates (Transparency International, 2017). Significantly Chile is one of Latin America's two top performers in this index (Uruguay ranked 21st)[13] – reflecting higher degrees of access to information about public expenditures, stronger standards of integrity for public officials, independent judicial systems and freer presses than its regional counterparts (Transparency International, 2017). Chile also has standards and online procedures for officials to declaration of conflict of interest, which are also made public. Despite this high international ranking, and the fact that Chileans do not perceive a lack of transparency to be a significant issue,[14] Chileans perceive corruption to be a key problem in the country. In one 2015 study measuring the problems facing the country, corruption was rated as the most significant problem by 5% of respondents and placed sixth in importance, after unemployment (8%) and the economy (6%). The three most important issues according to people surveyed were health (20%), education (17%), and delinquency (15%) (MORI, 2015). Another study, also published in 2015, asked respondents for the three most pressing issues they think government should address. Here, corruption is the fourth most frequently mentioned; and, significantly, it was mentioned 28 times in April 2015, but only 9 in November 2014 when the same survey was conducted. In addition, 52% of people surveyed[15] feel that cases of corruption have been more frequent in the past decade than in the previous one, while 35% feel the frequency has not changed; and 74% of respondents felt that corruption is easier to detect than 10 years ago. In this same study, an average of 52% of respondents felt that the reaction of government, congress and political parties was "bad" when confronted with instances of corruption (CEP, 2015). This dichotomy between international and in-country perception is requires attention. What lies behind it is unclear, and could be due to diverse factors, including the lack of confidence in government.

Greater transparency can certainly contribute to citizen confidence in government. However, it seems that Chileans are significantly less concerned with their government's transparency, and more concerned with real or perceived corruption. In order to meet participatory governance and government objectives, attention may need to shift from strengthening transparency mechanisms to building accountability. Doing so would speak more directly to citizens' concerns, help address the concern with corruption, and contribute to building citizen confidence in the government. Such a shift would require reassessing the way in which the government is being transparent: the way it provides information, the type of information provided and to whom, and the links it makes between transparency mechanisms and accountability techniques, particularly since greater transparency does not automatically translate into greater accountability.

Accessing information from the central and local government levels

The government actively ensures transparency online, and there are multiple transparency portals available. At the central level, there is the Transparency Council portal (www.consejotransparencia.cl), the government's transparency directory (www.gobiernotransparentechile.cl), a general government transparency portal run by the

Transparency Council to support meeting transparency requirements by diverse entities who have signed up to the platform, including municipal associations and corporations, ministries, foundations, political parties, universities, etc. (www.portaltransparencia.cl), as well as Transparency International's website (www.chiletransparente.cl). Individual ministries also provide transparency information. All ministries provide a link to the *Gobierno Transparente* site (which then offers links to information dedicated to that ministry) and the websites of individual ministries offer additional transparency-oriented information of their own, such as links to their Civil Society Council, participation reports, request for information pages, updates on citizen participation initiatives promoted by the ministry, etc. A basic scan of Chile's key ministries indicates that with varying degrees of clarity they are making information available, in compliance with the transparency law, and in a few cases they are also taking a proactive approach to strengthening their online citizen participation activities.

Compliance with access to information laws is improving significantly at the local level. While high levels of transparency at the national level are important, when seeking information Chileans turn most often to local authorities. Municipal authorities were the most frequent recipients of requests for information (42%), compared to public services (22%), ministries (11%), other institutions (11%), and SEREMI (4%). In addition, people sought information most often from their municipalities (33%), versus ministries (23%), etc. (MORI, 2015). This citizen preference renders municipal-level compliance with transparency requirements critical, particularly if confidence in government is a concern. While in 2012, 59% of municipalities had a low level of compliance with the transparency law, and only 6% a high level (Marin and Mylnarz, 2012), 2015 data indicates that an average of 76.9% of Chile's municipalities were in compliance with "active transparency"[16] requirements – representing a 12.2% increase over 2016. Compliance problems centred on out-of-date or non-existent information on budgets, citizen participation and matters affecting third parties (Consejo para la Transparencia, n.d.). What is behind past and present compliance challenges is unclear. Factors could include a lack of municipal resources to implement online tools, a lack of human resources (time or number) to respond to citizens who arrive in person requesting information, the possibility that the requested information is unavailable, or a lack of political will to prioritise transparency measures and meet transparency requests.

Despite these initiatives and improvements, there are three concerns with how information is being provided and the nature of the information itself. First, the multiplicity of transparency portals creates fragmentation and could cause confusion for users. Second, the information available – often a link to a specific law – is dense and not necessarily user friendly. This might be helpful as a repository of government documents and useful to those needing access to such documents for professional or academic reasons. However, it is not necessarily the type of information a majority of citizens seeks, nor is it necessarily provided through channels accessed by or available to a majority of Chileans. Thus, it may not be meeting citizen needs directly enough. As mentioned during OECD interviews with government officials, often the information made available is not what citizens want, for example the government may be providing technical details about a ministry or service while the citizen is seeking practical ones. Finally, there is little attempt to increase accountability through greater transparency, especially when the information provided is dense and/or difficult to understand. The United Kingdom and Canada share information with citizens in an easy to access, consolidated, "one-stop-shop" manner, creating a single point of entry to government information for citizens. Information is presented in a user-centred manner, and combines

access to information and transparency with accountability and citizen engagement mechanisms, thereby linking transparency mechanisms with accountability, particularly in the case of the United Kingdom (Box 5.8). Chile's government portal (www.gob.cl) is a strong step in this direction, also set up in a "one-stop-shop" manner and which provides citizens with information on government activity. However, it may wish to consider more strongly emphasising the government's ability to provide online information reflecting what citizens need (rather than what the government does). In this case, further streamlining the approach to limit fragmentation and increase user-orientation may be helpful.

Box 5.8. **Government information sharing online in the United Kingdom**

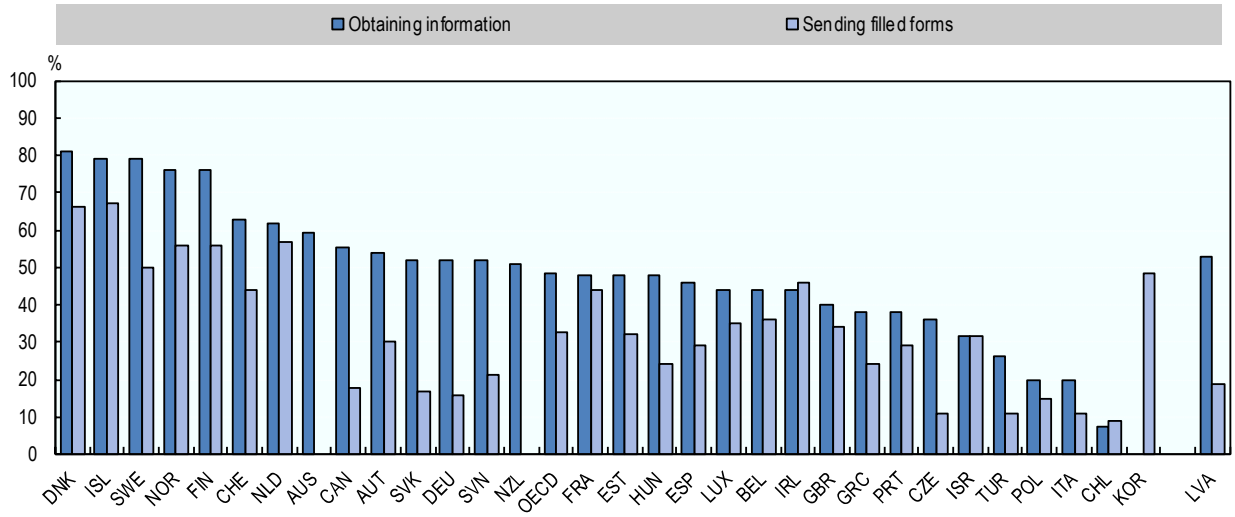
The UK government portal – www.gov.uk – is an online "one-stop-shop" for government information. Through one portal, users can link to the sites of all 25 ministerial departments and 374 agencies and public bodies. They can access government policies, announcements, publications, statistics and consultations, find out how government services are performing, and the levels of user satisfaction for these services. In addition, government services and information are divided into easily-identifiable categories according to user interest, e.g. "education and learning", "births, deaths, marriages, and care", "working, jobs and pensions", "housing and local services". Finally, it provides visitors with a list of the most popular links making it potentially faster and easier for citizens to get the information they want or the services they need, for example on job searches, vehicle tax rates and booking driving tests.

Source: UK Government (n.d.), "Welcome to gov.uk", Government of the United Kingdom, London, England, www.gov.uk/ (accessed 12 September 2016).

Better aligning transparency mechanisms with citizen behaviour and preferences

Chile's emphasis on transparency is laudable, and Chileans demand a right to access information, despite the fact they may not exercise this right. However, awareness of the key transparency mechanisms – the 2008 Transparency Law, the National Transparency Council and the Transparency Portal – has been low. In 2015, seven years after its introduction, only 26% of people surveyed responded that they knew about the Transparency Law, and in general the law was considered only moderately useful (MORI, 2015). One reason behind this lack of awareness may be a lack of alignment between the government's approach and citizen behaviour. It is certainly most efficient – for both the provider (government) and end-user (citizen) – if a maximum amount of information is available electronically. However, this assumes that people have a preference for obtaining information over the Internet and have access to it. Neither of these are the case in Chile. Data from 2015 indicates that Chileans tended to go in person to request information (38%) rather than use the Internet (13%) or use a public institution's webpage (4%) (MORI, 2015). This may be driven by habit, but it is also certainly a function of low Internet access. The most recent OECD data available indicates that in 2009 43.9% of Chilean households had access to a computer at home, and the Internet reached 30% of the population (OECD averages were 77.2% and 66.2% respectively in the same year) (OECD, 2016a). In addition, individual behaviour for using the Internet to obtain information and submit completed forms to public authorities is low – only 7.3% of Chileans surveyed use the internet to interact with public authorities, and slightly more – 8.9% – use it as a means to submit information. This is significantly below the OECD average of 48.6% and 32.8% respectively (Figure 5.2).

Figure 5.2. **Individuals using the Internet to interact with public authorities by type of activity (over the past 12 months), 2014**



Notes: Data for Japan, Mexico and the United States are not available. For Australia, data refer to 2012/13 (fiscal year ending in June 2013), and to individuals aged 15 and over. Data for Canada refer to 2012 for obtaining information and 2009 for sending filled forms. For New Zealand, data refer to 2012 for both interaction and sending filled forms. For Israel, data refer to 2009, and to all individuals aged 20 and over who used the Internet for obtaining services online from government offices, including downloading or completing official forms. Data for Chile and Korea refer to 2012 Information on data for Israel: http://dx/doi/org/10.1787/88932315602.

Source: OECD (2015b), *Government at a Glance 2015*, http://dx.doi.org/10.1787/gov_glance-2015-en.

The concern with Chile's approach, therefore, is two-fold. One is the high level of emphasis and investment directed to making information electronically available when it is: 1) not how people tend to access information; 2) not considered reliable; and 3) not within the reach of many Chileans. This links directly to the aforementioned concern of whether the government is meeting citizen needs. It also results in a question of inclusiveness (there have been whispers of "elitism" with respect to access to information). The second concern focuses on municipal implementation capacity. Despite improved compliance, on average nationwide, there are issues of information not being current, or simply not made available. This may reflect a lack of municipal resources to maintain data up-to-date (because of staffing issues, for example) just as it may reflect a lack of political will.

The government may need to reconsider how it is spending transparency resources given this lack of alignment between the information people want and how they wish to receive it, versus the information provided or available and how it is made accessible. One way to address this may be by increasing citizen participation in identifying what information they wish to receive. Greater use of open government data could further support transparency and empowers citizens to make the information and data more directly applicable to their needs.

Ensuring that the information provided is the information sought

Chile's government provides citizens with a wide array of information, ranging from staff remuneration, to budget levels and allocation, to citizen participation mechanisms. However, as mentioned during OECD interviews in Chile, often the information that

citizens seek is not necessarily the information available. While knowing staff remuneration is important, citizens may be more interested in knowing municipal working hours, for example.

Chile's various levels of government, particularly the municipalities, may need to expand the menu of options for obtaining information on municipal services and programmes, as well as how to contact municipal councillors. The city of Santiago has been a pioneer in this domain with its call centre "AlóSTGO Santiago" (phone 800203011). It is open 24 hours a day and offers citizens a platform for making a report or lodging a complaint (www.municipalidaddesantiago.cl/). Some cities in the United States and Canada have adopted dedicated 311 non-emergency service numbers, along with an associated website and apps that can be downloaded to tablets and smartphones. In Toronto, Canada citizen preference for "personal" interaction when requesting information mirrors that seen in Chile, with 83.6% of service requests in 2014 made by telephone, followed by online requests (8.4%), and then email (Box 5.9) (City of Toronto, n.d.1).

Box 5.9. **"311-Toronto" and other non-emergency service numbers**

In Toronto, Canada, a single phone number – 311 – is the city's public information and non-emergency service number. It is available 24 hours a day, seven days a week. Staff provide information about city services and programmes, and also how to contact a city councillor. In addition, the service is available online at www.toronto.ca/311. Citizens can request help by phone or online with public services (e.g. waste collection; property issues; water services; services related to animals and trees); register or request services (e.g. recreational programmes, child care, certifications); pay fines, licenses and renewals; monitor the household's accounts for utilities and taxes. In the case of service support requests, once the request has been submitted, the status of the request can be tracked by phone or online. In addition, the city has included a complaints and comments option where citizens can lodge a complaint against the city, compliment a 311 service or staff, make suggestions, etc. The programme provides information on locations and working hours of municipal administration centres (e.g. city hall).

The 311 website also includes a performance monitoring and evaluation mechanism wherein citizens are able to monitor the service's effectiveness and support accountability. It gives citizens a month-by-month evaluation of the weekly call volumes received, the achieved service level (i.e. the percentage of received calls that were answered within the 311 service goal of 75 seconds, with the goal being to answer 80% of calls within this time period), the nature of service requests by division (e.g. solid waste, water, animal services). This mechanism is useful for accountability purposes as citizens can see if the city is meeting its service goals, and but it also permits citizens and municipal leaders to identify where there may be service delivery problems based on the number of calls received.

By 2014, almost 300 US cities (and some counties) had 311 call systems or were using a similar technology. Many of the cities not only provide service information but are using 311 to also send information out to citizens – for example to alert community residents about repairs to utilities such as water or to inform about specific new services the city offers. In some cities, officials are using 311 to help them track work, measure performance, support citizen engagement, and make more informed decisions regarding services, budgets, and policy.

Box 5.9. **"311-Toronto" and other non-emergency service numbers** *(continued)*

Providing information through a 311 service can be costly as there are infrastructure, human resource and technology requirements to be met. In the future, regional versions of this type of service are expected to be rolled out. Despite cost constraints, however, governments do not appear deterred, acknowledging that the investment provides a wealth of data that helps develop management reports and improve city performance, identify how to better use scarce resources, and improve transparency. When planning to develop its 311 service, Seattle WA interviewed city staff, residents, and staff from other cities. Officials interviewed in other cities indicated that their city's 311 number helped build respect for city government, increase access to services and government, and improve accountability as well as the overall relationship between government and citizens. Meanwhile 86% of citizens surveyed felt it was a good idea and 76% agreed with the use of tax revenue for such a service. The 311 call number also made it easier for citizens to identify whom to contact for information or non-emergency help.

Source: City of Toronto (n.d.1), "311 Toronto", www1.toronto.ca/wps/portal/contentonly?vgnextoid=86d3ba2ae8b1e310VgnVCM10000071d60f89RCRD; Newcombe, T. (2014), "Is the Cost of 311 Systems Worth the Price of Knowing?", www.governing.com/topics/urban/gov-311-systems-cost.html; DuComb, D. (n.d.), "Seattle 3-1-1: Creating a Customer Centred Organization", PowerPoint Presentation, www.seattle.gov/customerService/docs/csb311121207.pdf.

There is also some concern with how much or how often Chilean authorities, both central and subnational (including local), share critical information about central or municipal government programming or plans that will affect specific neighbourhoods – for example the construction of a major road through a community, or of a shopping centre, etc. (Sagaris, 2014; Spoerer, 2014). Citizens do not always obtain the information from the proactive communication of government officials but because they heard about it and sought out the information. Improving how government communicates with citizens – not only the mechanisms but the frequency and the type of information shared – could help build greater confidence in government. This means identifying ways to communicate local and central government – intentions more effectively, not only by electronic media, but using channels through which citizens tend to participate, for example via community leaders (e.g. leaders of *juntas vecinales*), or by better partnering with CSOs in relevant sectors. Such initiatives could help boost citizen confidence in government, and increase the government's transparency in a direct way. It could also allow the government to better understand how a community will react to its intentions, ultimately supporting a more efficient use of financial and human resources.

The government may need to balance providing the qualitative and quantitative information that citizens demand the right to access, with greater openness in communicating information that citizens want to know. This could result in a more effective and more efficient approach to transparency, and help support greater accountability. Doing so, however, is likely to require consulting first with a broad base of stakeholders (i.e. individual citizens across the socio-economic spectrum, CSOs, private sector, academia, etc.) regarding what information is desired, from whom they wish to obtain it (e.g. municipality, community leader, regional government, ministry), in what format, and how they want to access it (e.g. in-person interaction, telephone, electronic media, print media, community meetings, municipal announcements). At a local level, COSOC could play a valuable role. It is unrealistic to think that everyone's wishes will be able to be met, but - at the very least - the government will have sufficient input to adjust its approach so that it resonates more strongly with a wider array of

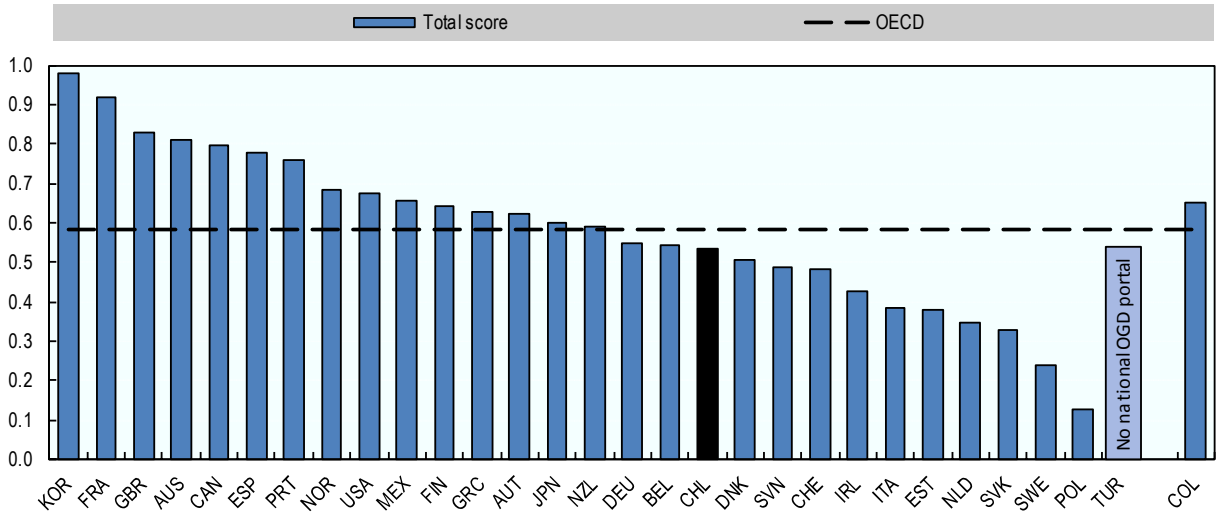
citizens. Creating a more inclusive dimension to the transparency framework could help significantly in its uptake, and reach traditionally less empowered sectors of society.

Enhancing open government data could support additional transparency and citizen participation

Open government data can promote greater transparency and accountability. This is based on the assumption that an absence of data in the public domain allows public servants to engage in corrupt behaviour. It can also support public accountability by making existing information easier to analyse, process, and combine for a new level of public oversight. In addition, open government data serves as a tool to promote citizen engagement and empowerment. By creating a framework for participation that enables users to be active contributors and designers of content and services, not just passive consumers, it invites stakeholders into a more participative and empowering relationship with government. This can extend to planning and land use; service design and delivery; community building; and broader public policy. Furthermore, open government data can foster greater innovation, efficiency and effectiveness in government services, and in public sector operations. For example in the United Kingdom, discussions between the Department of Transport and the Association for Train Operating Companies (ATOC) led to free access to the fare databases in early 2013 (Ubaldi, 2013). This enabled the development of price comparison websites and mobile phone apps for the benefit of passengers who could then access accurate information and find the ticket they needed at the best price.

Chile's open government data initiative appears to be generally on par with that of other OECD countries: like 20 other OECD members, by 2014 Chile had a single (central level) open government data strategy; and like 29 countries it had a national open government data portal (www.datos.gob.cl) that is extensive in breadth and offers a wealth of information. However, unlike 24 member countries, Chile does not regularly consult users regarding their needs for data releases, nor is it possible for users to receive notification when new datasets are added. It also does not systematically facilitate data re-use and support, for example through the organisation of co-creation type events (e.g. "hackathons"), or training for civil servants to build capacities for data analysis and reuse (OECD, 2015b). Overall, Chile scores below the OECD average on the "OURdata Index" which is a composite index measuring the openness, usefulness and reusability of government data (Figure 5.3) (OECD, 2015b). While all countries face data challenges, and this is true in Chile as well, officials may wish to revise the approach to open government data, considering it not only as a transparency tool, but also using it to help build engagement. This can mean more proactively engaging existing users, for example via asking about their data needs, building capacity for use and reuse, etc. as well as educating citizens (i.e. potential new users) about open data and its use.

Figure 5.3. **OURdata Index: Open, Useful, Reusable Government Data, 2014**



Notes: Data for the Czech Republic, Hungary, Iceland, Israel and Luxembourg are not available. This index is a "pilot" version (see Annex E of OECD, 2015b for full methodology) covering the following dimensions: data accessibility and data availability on the national data portal, and government's efforts to support data re-use.

Source: OECD (2015b), *Government at a Glance 2015*, http://dx.doi.org/10.1787/gov_glance-2015-en.

Building and supporting initiatives such as 311-non emergency numbers, or more widespread and society-driven use of open government data certainly requires an active approach by the central government. At the same time, they require municipalities that are empowered and sufficiently resourced to act. In other words, unless a municipality has the funds, infrastructure capacity and staffing flexibility to implement a non-emergency number, the intention to set targets, and the political will to show how well the service is performing, such an initiative may not succeed. Greater investment and activity in open government data can help the national level, but if it is also to be used by citizens at a local level, municipal authorities must be able to respond to needs or demands that arise, including making local data and information easily available.

There is increasing activity at the subnational level with respect to open government and open government data. For example, in 2016 the Open Government Partnership (of which Chile is a member) launched a 15 member[17] subnational pilot programme to reach regions, provinces and cities (Open Government Partnership, 2016). With respect to open government data at the municipal level, such cities as Barcelona, London, Madrid, Melbourne, and Montevideo have open government data portals where people can find data in a variety of categories (e.g. environment, population, jobs and economy, health, transport, community safety, infrastructure), and datasets in categories ranging from housing (Ayuntamiento de Barcelona, n.d.) and household waste (Greater London Authority, n.d.) to the number of traffic accidents (Ayuntamiento de Madrid, n.d.), and services for women (City of Melbourne, n.d.). In addition, local governments, such as the City of London, are using open government data not only to improve transparency, but as a tool for building accountability and promoting citizen participation in key policy issues (Box 5.10).

Box 5.10. **The London DataStore to promote transparency, accountability and participation**

The London Datastore is a free, open data-sharing portal facilitating access to data relating to the capital. The site provides citizens, businesses, researchers and developers over 600 datasets to help understand the city and identify solutions to London's problems. In addition to being able to access a wide variety of datasets in numerous formats (XLS, CSV, PDF, XML, etc.) for open use, the Datastore's portal provides up-to-date statistical information on the city's performance in nine areas: jobs and economy, transport, environment, community safety, housing, communities, health, London as a world city, and performance by the Greater London Authority. This function is structured to build transparency as well as accountability. First, each category provides information on the city's priorities (e.g. in transport it is to upgrade most parts of the Underground and Overground, encourage cycling and walking), and then offers easy-to-understand graphs that use available data to highlight performance. For example, in the jobs and employment category it highlights, among other things, the growth in the number of apprenticeships in London versus the rest of England since 2008/09. In an objective and transparent way, the Datastore does not hide negative results – for example in the environment category it shows that recycling in London is down, while it is still a growing trend in the rest of England. Finally, the website also supports greater citizen participation by offering "data challenges" – encouraging citizens to use open data and smart technologies to help solve some of London's key challenges, for example crowd-sourced data to manage population health, the Future of Generation Y, and how to better deliver adult social care services in London.

Source: Greater London Authority (n.d.), "London Datastore" https://data.london.gov.uk/.

A shortfall of data availability, data points, and data dissemination is a challenge confronting many of Chile's municipalities with respect to open government data. This is due in part to the multi-level governance structure that emphasises their administrative role, where action focuses on executing nationally driven, often strongly sector-based, priorities, and does not consider local level performance measurement. A lack of resources may also be a significant obstacle. Improving subnational data capacity, however, and building open government data at the subnational level could help municipalities grow in their partnership capacity regarding higher government levels, contribute to performance measurement and build accountability.

Building accountability mechanisms to compliment transparency

Chile's approach to promoting accountability has been less dynamic than its approach to building transparency. In order to meet its objective of boosting citizen oversight of local authorities as a means to support accountability, strengthen the social fabric and build inclusiveness, current transparency practices will need to be complemented with stronger accountability mechanisms, particularly at the local level. This includes promoting accountability frameworks, building stronger performance measurement systems, and encouraging local government to publish municipal service and quality of life objectives and ideally work with citizens in setting and meeting these.

Developing accountability frameworks to guide accountability expectations

Accountability frameworks are the composite of various tools that governments use to ensure greater accountability and transparency, and they serve as a guideline for what is expected of authorities with respect to accountability mechanisms. Such frameworks offer

an institutional dimension to ensuring government accountability, including through an audit institution, an ombudsman, regular annual performance reporting, etc. Canadian cities, such as Ottawa and Toronto have clearly-established and articulated accountability frameworks (Box 5.11). These frameworks are applicable at the regional/territorial level as well. One example is in Canada's Northwest Territories where the Municipal and Community Affairs Office has an Accountability Framework for Community Governments offering a way for municipalities to monitor the performance of their organisations, and to report the performance of community governments in the delivery of municipal programmes and services (Department of Municipal and Community Affairs, n.d.). These frameworks also depend on established performance measures and targets.

Box 5.11. **Building municipal accountability frameworks in Canada**

For the City of Ottawa, Canada, being accountable and transparent means the city is committed to measuring and showing its performance in all areas of its responsibility, ranging from financial reports and human resource management to service delivery. To support its accountability framework, it has adopted a series of accountability and transparency practices, including establishing an integrity commissioner, adopting an accountability and transparency policy, producing the City of Ottawa Annual Report, developing a comprehensive human resource plan, participating in the Ontario Municipal Benchmarking Initiative, and adopting the principles of open government and establishing the Open Data Ottawa site for citizens to access municipal datasets.

To more actively involve citizens in the accountability process, the City of Toronto, Canada developed a "learning guide" that outlines the principles of good governance and clearly delineates the primary accountability mechanisms that the city has established, including:

- Accountability officers who are independent from the city administration, are appointed by the city council, responsible for producing an annual report, and report to the city council.
- The auditor general who focuses on the city council and city administrators and is there to help the city council hold itself and its administration accountable for public funds and for achieving value for money in city operations and within the city operational units (divisions, agencies, boards, commissions and offices).
- The integrity commissioner, who focuses on members of council and members of local boards, and is responsible for providing advice, resolving complaints and educating members of the city council and members of local boards on the city's Codes of Conduct and other bylaws, policies and legislation governing ethical behaviour.
- The lobbyist registrar, who promotes and enhances transparency and integrity of city government decision making via public disclosure of lobbying activities and regulating lobbyist conduct.
- The ombudsman, who serves as an impartial investigator of citizen complaints about the administration of city government, including agencies, boards and commissions.

Source: City of Ottawa (n.d.), "Accountability Framework"; City of Toronto (n.d.2), "Accountability" Get Involved.

Explicit accountability frameworks do not exist in Chile. While they can require capacities that municipalities do not have at present (e.g. resources to support

accountability officers or an integrity commissioner), a first step towards building local level accountability frameworks could be to expand upon available performance information, adjust how it is used, and continue to develop performance-oriented initiatives – such as the proposed System for Guaranteeing Quality Public Services (SEMUG see Chapter 4) – with this type of use in mind. To realise this, however, municipal authorities would need support in building indicator systems, which means articulating and communicating strategic objectives, associating these with realistic output and outcome targets, and identifying the data needs to help establish indicators (OECD, 2013b).

Building the accountability quotient by measuring the performance of municipal services

Performance measurement – i.e. the monitoring and evaluation of policy and programming – is a fundamental tool for building accountability while also promoting greater transparency. As an ongoing activity and when effectively communicated, indicators and performance measurement can show citizens how government is meeting its stated objectives, how it is using its resources, and how its policies are performing. Performance measurement techniques do not appear to factor into Chile's approach to participatory governance, particularly at the local level. Measurement tools exist in Chile (see Chapter 4) but performance measurement practices remain weak.

Communicating and sharing progress on objectives and indicator results with stakeholders and citizens, for example through a dedicated website, would be helpful for accountability as well as for increasing citizen confidence in government activities, spending and performance. Not only will this help accountability and transparency, it can also help determine the effectiveness of service programming and delivery, highlighting whether changes need to be made. Successful indicator systems require clarity with respect to lines of responsibility, openness and the ability to set objectives, and a willingness to be transparent about performance. They also require human, financial and infrastructure resources, and the Chilean central government may wish to focus first on strengthening accountability mechanisms at the national level. Municipal activity in this area is crucial, but may require greater capacity and autonomy in decision making, objective setting and prioritisation, resource allocation, and performance data than municipalities currently have.

Building accountability by involving citizens in municipal planning and objective setting

Often, participatory mechanisms are used to help shape municipal spatial and development plans. Involving citizens in planning processes is one way to link transparency, accountability and participatory governance. It can give officials at all levels of government an idea as to what citizens are prioritising, their perception of community needs, and their expectations of government. With such information, government is better placed to design policies, plans and the use of space. When citizens participate in such processes, they develop expectations of government, and it is government's responsibility to communicate how these expectations will be met, and why they cannot be met if such is the case.

In Chile, municipal governments are required to involve residents in the approval of the municipal Regulating Plans (*Plan Regulador* – PR). These plans regulate land use, construction and the physical development of urban areas (OECD, 2013c). It is reported,

however, that the participatory dimension often comes late in the development process, limiting room for citizen input. Another limitation is the fact that changes to the PRs are lengthy processes and occur on an irregular basis. Another type of municipal plan, the Municipal Development Plan (*Plan de Desarrollo Comunal* – PLADECO) can offer a more comprehensive perspective to municipal development as their objective is to promote integrated municipal development and programming, and their design should include a participatory dimension (OECD, 2013c). In addition, incorporating a monitoring and evaluation function that can be tracked by citizens (and government) online would also be beneficial and help promote government accountability to citizens. While citizen participation in the development of a PLADECO is required, and common, developing and implementing a PLADECO is not required, but is, rather, a voluntary planning mechanism.

These local planning processes provide a participatory platform and could be strong accountability mechanisms, but the use of participation and its impact is mixed for a number of reasons. First, consultation – if it is carried out – is generally reported as occurring late in the planning process, and thus there is little room to influence the shape of the plan. Second, there is a problem of "consultation fatigue" with respect to the Regulating Plans and the PLADECO. Consultation fatigue can occur if citizens are "over-solicited"– i.e. asked for their opinions in planning and processes repeatedly over short periods of time without knowing how their input is used. This has been noticed for example in the consultation process for the PLADECO in Villarrica (Box 5.12), and should be considered as a potential issue throughout the country. The tendency to over-consult can be particularly accentuated in systems, such as Chile's, where the emphasis is placed on involving residents in short-term (e.g. one election cycle) programmes and projects rather than on gathering input for developing a longer term policy. The third issue arises from a weak civil society and accountability that tends to be more political (i.e. higher levels of government) than social (i.e. individual citizens and civil society). In some municipalities, citizen participation is becoming obligatory, for example in Puerto Montt (as of 2017). Yet for the most part citizen input is not obligatory and non-binding. This is not a problem in and of itself. However, the fact that citizens do not follow-up and ask why their input has not been taken into consideration or acted upon, means that they are not holding local decision makers accountable for the participatory process and the information it generates. This is an issue and one that stems from low incentive to be accountable to citizens combined with weak civil society (OECD interviews). It is exacerbated by the lack of a monitoring and evaluation system that could also highlight performance shortfalls.

Box 5.12. **Balancing active consultation and consultation fatigue**

Many municipalities, regardless of the country where they are located, seek citizen input and insight into their planning process. In Chile, individual municipalities, such as Villarrica in the region of Araucanía, consult with citizens on the municipality's development plan, particularly the PLADECO. Leaders of the consultation process highlighted several positive dimensions to the interactions, including a better understanding of the challenges faced by citizens, identifying new variables to consider (e.g. cultural diversity), and a greater capacity to align action with possible instruments available to the municipality. It also provided the municipality with an opportunity to build understanding that it is not the only actor responsible for solving problems, and the support of other actors (e.g. central and regional levels and the private sector) is needed as well. At the same time, "consultation fatigue" became evident with people questioning what happened to the information gathered from previous consultative exercises. People also expressed dissatisfaction with having been called to give an opinion and then not knowing anything more about the initiative or how their opinion was used. While gathering citizen insight and input is valuable, if it is not coupled with active communication it can discourage and diminish the capacity of citizens and civil society organisations to participate.

Source: Valdivieso, G. (2012), "¿Para qué sirve el PLADECO?" Planeo, Instituto de Estudios Urbanos y Territoriales (IEUT), http://revistaplaneo.uc.cl/2012/10/09/para-que-sirve-el-pladeco/.

When citizens are brought into the community planning process early on, citizens have a stake and/or greater interest in ensuring objectives are realised and that actors (public and private) comply. This principle was behind New York City's OneNYC plan. The city undertook a community engagement process to build its evidence base by surveying residents, holding community meetings, meeting with civil society organisations, involving neighbouring cities and administrative jurisdictions, and involving a broad range of government stakeholders in the plan's design process. The result was a plan with wide and diverse input, a clear picture of the issues New Yorkers consider to be the most important (e.g. housing, education, infrastructure, health), and a good understanding of what residents thought were the city's most important assets (e.g. diversity, transport, culture). It also prompted the city to unequivocally state that it would aim to become a "resident-centred" government, and establish an indicator system for citizens and government to monitor whether objectives are being met (City of New York, n.d.).

Citizen-driven accountability mechanisms can also help define municipal goals and hold local government accountable for achieving them. In the city of Córdoba, Argentina, the Our Córdoba Citizen's Network (*Red Ciudadana: Nuestra Córdoba)* established a set of 10 quality of life indicators[18] with quantitative and qualitative data to measure the city's performance over time in relevant dimensions (e.g. green space, particulate matter, wealth distribution, number of licensed vehicles). Our Córdoba also proposes a potential "Plan of Objectives" (*Plan de Metas)* to the city government for its consideration, in this way bringing the aims that citizens have for their city to the attention of public officials (Box 5.13) (OECD, 2016b).

Box 5.13. **Our Córdoba Citizen Network and the *Plan de Metas***

The Our Córdoba Citizen Network (*Nuestra Córdoba*) is a non-partisan, non-governmental network that works with more than 200 citizens and 60 organisations (academia, civil society organisations, foundations, private enterprise, research institutes, etc.) in the city of Córdoba, Argentina. It is associated with the Latin American and the Argentinean Networks for Fair, Democratic and Sustainable Cities and Territories. Its objective is to promote a city that is more fair, democratic and sustainable.

Municipal Ordinance No. 11942 (spearheaded by Our Córdoba) requires the municipal government to adopt a set of objectives in order to enhance the clarity and transparency of the government's proposed plans and actions. It requires that, before completing 120 days in office, the mayor presents their goals, the strategic actions that will be taken by each branch of the municipal government in support of these goals, and the performance indicators to facilitate monitoring and evaluation. Under the ordinance, the mayor must provide an annual performance report (before 10 March) with respect to the goals and indicators. Unfortunately, there is no requirement to provide a summary report at the end of the mayoral mandate.

To support this strategic planning and reporting requirement, and as part of its activities, the Our Córdoba Network presents the City's mayor (at the beginning of each mayoral term) with a proposed "Plan of Objectives" (*Plan de Metas*) for the administration's consideration and adoption. The 2015-19 proposal was developed with the participation of over 200 citizens, and covers three themes, each of which is broken down into sub-dimensions and quantifiable objectives: sustainable urban development (20 objectives); institutional development (19 objectives); inclusive development (10 objectives).

Source: Nuestra Córdoba (2015), "49 Metas para Nuestra Ciudad: Una propuesta de la ciudadanía para el Plan de Metas 2015-2019," www.nuestraCordoba.org.ar/; Nuestra Córdoba (n.d.), "Plan de Metas", www.nuestraCordoba.org.ar/.

One of the critical differences in citizen input in Chilean municipal planning is that neither the plans nor the participatory aspect is linked to performance or outcome objectives that could be used for accountability purposes. If Chile were to do so, it could provide government and citizens with insight into service delivery performance, as well as help identify if participatory mechanisms (e.g. a *plan de metas*) are having a positive impact. Establishing indicators that can help quantify change in areas where citizen input is sought – for example in public works, social service programmes, and other public goods in categories where measurement is most common, such as education, health, transport and the environment – could be useful. Care would need to be taken, though, to make sure that citizens actually are deliberating on issues that can improve their well-being (Wampler and McNulty, 2011), rather than on a restricted menu of preapproved projects or programmes that would be undertaken regardless of whether citizens are brought into the process.

Conclusions

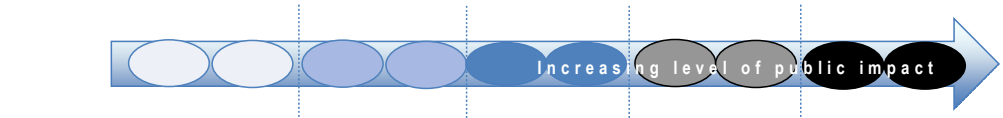
Chile's transparency mechanisms are solidly in place and align with international practices. However, it may need to broaden its approach to transparency by building in an accountability component. It could use existing information to begin developing a better accountability framework while supporting municipalities to do the same. It is also important to ensure that citizen expectations with respect to information – i.e. what they want to know – is aligned not only with their right to access information but also with their capacity, ability and preferences for doing so.

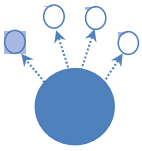
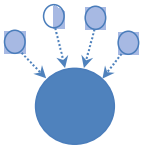
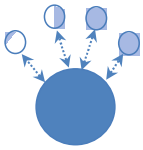
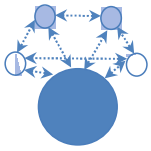
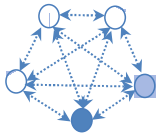
Involving citizens in the information gathering and disseminating process, for example through stronger open government data practices, could be helpful to build awareness and stimulate the use of government information in a way that is relevant to citizens. Building capacity and supporting municipalities to be more transparent and accountable is critical. It is at this level where citizens are more likely to search for information, where they interact most directly with government, and where trust and engagement are more directly nurtured. Greater effort could be placed on ensuring citizen input early in the policy or planning cycle, and using performance measurement as an accountability tool.

Citizen engagement: Activating the local level for stronger participatory governance

Citizen engagement practices fall along a spectrum of interaction (Figure 5.4), where each level of exchange builds on the prior level and becomes increasingly complex. The most basic interaction is a one-way exchange with either the government providing information to citizens (inform), or citizens providing information to government (consult). Interaction becomes increasingly complex, and arguably richer, when the exchange goes in both directions and promotes dialogue between the parties. As one moves further to the right on the spectrum of public engagement practices, the level of public impact increases, together with the level of government commitment to citizen input. At the same time, it is important to recognise that each level of participation is associated with a specific aim and is supported by distinct methods or tools. Thus, it is important to match the objectives with the level of participation, the degree to which the government is willing to commit to participatory outcomes, and the participatory methods that are realistically within a government's capacity to undertake.

Figure 5.4. **The spectrum of public engagement**



	Inform	Consult	Involve	Collaborate	Empower
Interaction					
Aim	To provide the public with balanced and objective information to support its understanding of a problem, alternatives, opportunities and/or solutions	To obtain public feedback on analysis, alternatives and/or decisions	To work with the public throughout the process, ensuring that public concerns and aspirations are understood and considered	To partner with the public on each aspect of the decision, including the development of alternatives and a preferred solution	To create governance structures that place decision making and/or work directly in the hands of the public
Government commitment	We will keep you informed	We will keep you informed, listen to and acknowledge concerns and goals, and provide feedback on how your input influenced the decision	We will work with you to ensure that your concerns and goals are directly reflected in the alternatives developed and provide feedback on how public input influenced the decision	We will look to you for advice and innovation in formulating solutions and incorporate your advice and recommendations into the decisions to the maximum extent possible	We will implement what you decide
Methods	• Fact sheets • Websites • Open houses	• Public comment • Focus groups • Surveys • Public meetings	• Workshops • Deliberative polling	• Citizen advisory committees • Consensus building • Participatory decision-making	• Citizen juries • Ballots • Delegated decision
Description	**Participation** The first two public participation levels – inform and consult – typically occur when a decision has already been made and government wants to either communicate the decision to the public, or seek opinions on the decision.		**Engagement** The third and fourth public participation levels – involve and collaborate – have two-way information flows and include sharing information within and across stakeholder communities during the decision-making process. When undertaking engagement, decision makers commit to using stakeholder feedback to inform the decision and shape the outcome.		**Empowerment** The fifth level – empower – is also often referred to as co-production, where decisions are made jointly between government and the community. This is typically when decision-making authority has been delegated to a group, including members from both the government and the community/ industry.

Sources: Adapted from IAP2 (2007), *IAP2 Spectrum of Public Participation*, http://c.ymcdn.com/sites/www.iap2.org/resource/resmgr/foundations_course/IAP2_P2_Spectrum_FINAL.pdf, VAGO (2015), *Public Participation in Government Decision-Making: Better practice guide*, www.audit.vic.gov.au/publications/20150130-Public-Participation-BPG/20150130-Public-Participation-BPG.pdf.

Chile's participatory practices tend to reinforce the "inform" and "consult" forms of interaction, with some degree of involvement. While this can be beneficial, it has limited public impact since communication often occurs once a decision has been made, rather than in order to make a decision. The level of government commitment is also significant, as participation with higher levels of engagement is associated with greater degrees of government commitment to act on citizen preferences. Chile's emphasis on mechanisms that inform and consult, with a limited number that promote involvement, collaboration or empowerment is in keeping with the managerial classification of municipal administration and multi-level governance approach.

Also in keeping with this is Chile's approach to building stronger citizen engagement. It focuses on engagement as a tool to improve service delivery rather than to support strategy, policy and planning processes. It is top-down and inward looking, emphasising formal councils and oversight units at the national and local levels, as well as government programmes and government training, rather than outward looking, anticipating and responding to when and how citizens want to participate and ensuring their capacity to do so. This may be one reason why there appears to be little room for citizen "voice" in policy or programme design and implementation. It can also link to consultation that comes too late in the planning process as well as to a governance and management system where strategic development planning is not a strong component of the municipal portfolio. Unfortunately, Chile's ambitions with respect to citizen engagement – i.e. processes that create a stronger partnership between all levels of government and citizens – is not aligned with its multi-level governance framework, one that limits municipal autonomy in decision-making, programming prioritisation, and resource management. Nor is it fully aligned with the more bottom-up, fluid character of citizen participation, which by its very nature requires decentralised activity and a degree of flexibility to choose and adjust the participatory method applied based on objectives, on circumstance, and capacity. Citizens also have to be motivated to partner with government. Overall, this disconnect is troublesome since it is generally easier for citizens to engage at the local level and with local institutions, and it is critical that local institutions be politically willing, properly guided, sufficiently capacitated and appropriately resourced to work with citizens.

Ensuring citizens become proactive rather than reactive participants

It is incorrect and unfair to say that engagement is missing in Chile's municipalities. In many communities, there is a solid history of involvement in government programming, for example in Chile's neighbourhood recovery programme: *Quiero mi Barrio* (Box 5.14). In Valparaíso, actively partnering with community residents led to programme outcomes reflective of citizen needs, desires and aspirations, more appropriate prioritisation of action and funds, a more efficient use of resources and, ultimately, more effective policy making.

Box 5.14. **Community involvement in Chile's neighbourhood recovery programme: *Quiero mi Barrio***

In 2006, Chile's Ministry of Housing and Urbanism (MINVU) launched an on-going nationwide programme, *Recuperación de Barrios: Quiero mi Barrio*, aimed at recovering disadvantaged neighbourhoods. Programme implementation requires management plans to be submitted by the relevant communities. National and regional government authorities in Valparaíso, Chile's second largest metropolitan area, noticed that in communities where programme results were poor, no inclusive *ex ante* planning had been undertaken by community leaders. Communities with strong results had established plans based on *ex ante* participation among representatives from the community, the municipal administration, and regional government. These stakeholders came together to identify the problems that needed to be addressed and to develop a list of priorities. Based on the difference in results between plans developed with and without community involvement, the regional government has since solicited citizen participation in other initiatives.

Source: Adapted from OECD (2013c), *OECD Urban Policy Reviews, Chile 2013*; original source Ministry of Housing and Urbanism/SEREMI (2012), OECD interview, June 2012, Valparaíso, Chile.

There is also evidence that citizen action in Chile is strong enough to result in successfully impacting the policy agenda once a problem is perceived. Two examples are the anti-highway campaign that mobilised neighbourhood groups against the building of a major highway through communities in Santiago in 2000 (Sagaris, 2014), and the Barrancones environmental conflict wherein citizen action stopped the development of a hydroelectric plant in 2010[19] (Spoerer, 2014). Other examples include citizen action taken to stop the development of a shopping centre in one of Santiago's most affluent municipalities, and community involvement to ensure that an existing park remained easily accessible to all residents (Fernández Prajoux, 2013). There are also more high profile instances, such as the student movements of recent years.

Despite these and other examples of citizen activism, there appears to be a misalignment between the forms of participation sought by government, and how citizens participate, or what is understood as participation. The government is strengthening citizen participation with laws, top-down frameworks, and prescribed participatory mechanisms. Meanwhile, citizens are engaging to solve an imminent problem or to tackle a perceived threat, acting at a grassroots level where participatory mechanisms are selected and adapted to meet the need at hand. For example, to be heard with respect to the planned shopping mall, or the changes to the park, citizens held community meetings or community fora to discuss the issues and concerns among themselves, they communicated with the public and with public officials through flyers, emails, letters to public officials, and they established opportunity for dialogue with the public sector, private sector and community stakeholders. In both cases, all of this activity led to the call for public referenda – one of the participatory mechanisms required by the Municipal Organic Law. The referenda were supported by the relevant mayors with a statement that they would respect the outcomes. In the case of the highway and of the thermoelectric plant, the processes were more complicated, but still depended heavily on residents becoming informed, debating among themselves, communicating with stakeholders, using media and social media to support their cause, etc. The action taken by citizens does not necessarily take the forms sought or established by government, and it seems to occur most effectively when it is reactive – i.e. to solve a problem or tackle a threat – rather than being proactive in contributing to a policy or programme agenda before problems arise. Seeking blame or responsibility for this disconnect, however, may be unjust to both the government and citizens.

In order to ensure that engagement does not simply occur when a problem is perceived, more effort may be needed to create room for citizen voice. This can mean improving communication at the early stages of planning so that its programmes do not reach the "threat" stage. One way to do so is by bringing relevant stakeholders into the process early on. This is certainly antithetical to the current multi-level governance structure as it can put government plans at risk. However, it can also better support trust and avoid incurring unnecessary costs of "undoing" a project very late in the process if citizen influence is strong enough.

The comprehensive use of citizen engagement requires that government organisations be transparent about what they do and responsive to what citizens tell them. It also means that a government needs to shift its perspective about the relationship between citizens and public policy, from one where citizens are the recipients (objects) of public policy to one where citizens are the reason for - or focal point (subject) - of the policy. This can mean a significant amount of cultural change in a government organisation. Centres of expertise on citizen engagement can promote a supportive engagement culture, better institutionalise citizen engagement practices, and serve as a useful resource for decision

makers. A centre of expertise helps build the body of knowledge and experience gained from citizen engagement, and commit it to institutional memory. It can also help ensure that practice is evidence-based and evolves over time. Such centres can support the evaluation of proactive engagement, test new approaches, develop a business case for engagement, spread relevant knowledge and skills, and eliminate organisational barriers. At the same time, centres of expertise complement but do not replace the need for government officials to develop their engagement capabilities (Box 5.15) (Open Government Partnership, n.d.).

Box 5.15. **Centres of expertise on citizen engagement in Canada, Denmark, and the United Kingdom**

The city of Edmonton, Canada, in co-operation with the University of Alberta established the Centre for Public Involvement (CPI). The centre's aim is to advance research and learning with respect to public involvement in order to improve decision making at all levels. It is a non-partisan, independent organisation that focuses on building the motivation and capacity for innovation in public involvement, facilitating collaboration and identifying good practices. It identifies and tests new models and processes of engagement in partnership with public involvement professionals, researchers, organisations and the public.

The Danish government established the Centre for Collaborative Democracy (CfSD) to strengthen Denmark's tradition of democratic dialogue and co-operation among citizens, elected officials, experts, the private sector, and organisations. CfSD offers advice to municipalities, regions, agencies, ministries, associations, organisations and companies on planning and implementing participatory processes and on using the results of these processes. CfSD's goal is to improve decision-making culture by offering professional involvement. The Centre's purpose is to apply the knowledge obtained and methodological expertise in areas that do not necessarily have to do with technology – for example, through participatory budgeting, by involving employees in innovation in the welfare sector, urban planning, corporate social responsibility and other areas.

In 2007, the UK government established a centre for public engagement specifically for science – the Sciencewise Expert Resource Centre. It co-funds and provides expert advice and support to government departments and agencies in their effort to develop and commission public dialogue activities in emerging areas of science and technology. Its aim is to foster capacity among policy makers to commission and use excellent public dialogue with a view to improving policy making in science, technology and innovation. It offers information online, as well as advice and guidance and support services. It also helps build capacity, promote good practices, and provide general dialogue training and mentoring to policy makers in all government departments involved in science and technology policy issues.

Source: Involve (n.d.1), "The City of Edmonton has Set up a Centre for Public Involvement", www.opengovguide.com/country-examples/the-city-of-edmonton-has-set-up-a-centre-for-public-involvement/; Involve (n.d.2), "Denmark set up a Centre of Expertise on Collaborative Democracy, Starting with a Focus on Technology Issues", www.opengovguide.com/country-examples/the-city-of-edmonton-has-set-up-a-centre-for-public-involvement/; Involve (n.d.3), "The UK Government set up a Centre for Public Engagement on Science Policy following a National Controversy", www.opengovguide.com/country-examples/the-city-of-edmonton-has-set-up-a-centre-for-public-involvement/.

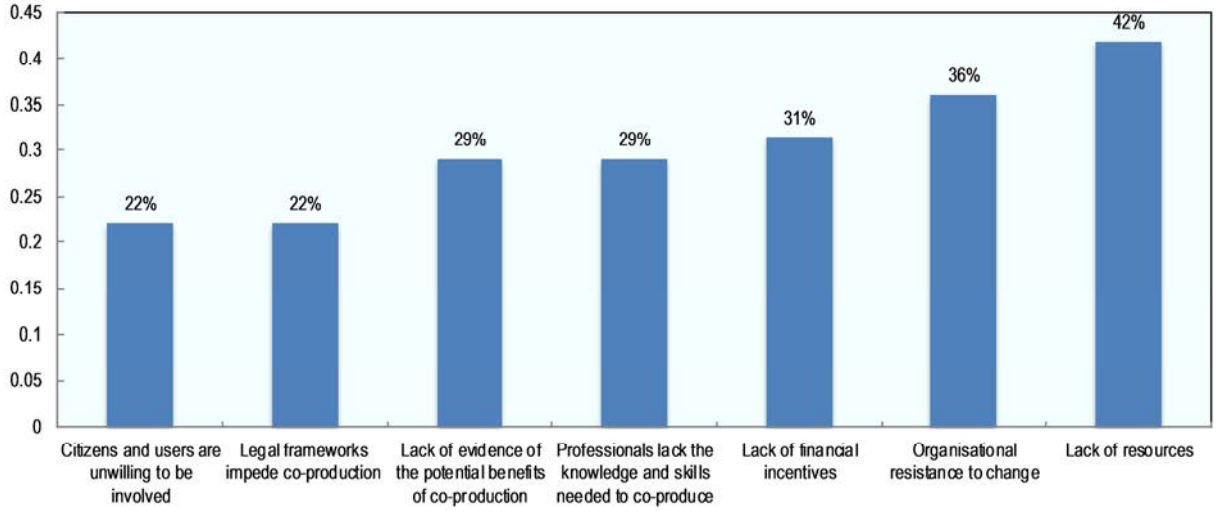
Boosting citizen engagement in Chile, and through it participatory governance, may not require more new laws or more tools. Instead, it may rest on a re-evaluation of what is already in place, better aligning government and citizen approaches and expectations, building political will among local elected officials, and strengthening CSOs. More could be done to address resource and capacity challenges, support municipalities in taking a

policy-oriented approach to participatory governance, and promoting a more effective use of participatory mechanisms.

Strengthening engagement with resources, political will and greater local capacity

Among many OECD countries, the issue of resources is one of the primary obstacles in promoting greater openness and inclusiveness in government practices. In a 2009 OECD survey, 45% of respondents indicated that the "resource" principle for open and inclusive government was the hardest to meet (Annex 5.A). This principle states that adequate financial, human and technical resources are needed for effective public information, consultation and participation. Government officials must have access to appropriate skills, guidance and training as well as an organisational culture that supports traditional and online tools (OECD, 2009). OECD countries have also indicated that a lack of resources is one of the leading factors that hold back partnering with citizens in service delivery – a form of participation that straddles collaboration and empowerment on the engagement spectrum. Organisational resistance to change as well as several other factors, including lack of incentive, are other reasons cited as obstacles to partnering with citizens (Figure 5.5) (OECD, 2010a).

Figure 5.5. **Barriers to partnering with citizens in service delivery (2010)**



Source: 2010 OECD Survey on Innovation in Public Services in OECD (2011), *Government at a Glance*.

In Chile, financial and human resources, as well as organisational capacity, may be among the most significant obstacles to stronger participatory practices. All of Chile's key actors in participatory governance face challenges in their ability to undertake participatory mechanisms and strengthen engagement, ranging from limited financial resources, to limited practice of pro-active engagement, to low political will.

Financial resource management is promoting a fragmented approach to participatory initiatives

Actively undertaking citizen engagement initiatives in a sustainable fashion – be it throughout the policy cycle or as part of a specific programme or project – can be a costly

undertaking. The government supports participatory initiatives through a series of specific funds targeting communities and community projects. These include the Fund for Neighbourhood Development (*Fondo de Desarrollo Vecinal* – FONDEVE), available to neighbourhood committees and discussed earlier (Box 5.7), as well as sector specific programmes established by line ministries, such as the Participatory Paving Programme (*Pavimentos Participativos)* introduced by the Ministry for Housing and Urbanisation (MINVU, 2014). While municipalities can apply for funds from these central level sources, they do not receive government transfers to engage in or promote greater participation. Thus, while the competence is mandated, it is unfunded as there is no dedicated resource support. This is illustrated, for example, by the COSOC, which by law must be given an operating budget by municipalities from the municipal budget. This is not to say that the central level must forever fund local participatory governance through transfers. However, the current municipal finance system – where municipal governments are highly dependent on transfers and where the majority of local governments have a shortfall in own source revenue – does not appear sufficiently robust to support more participatory practices.

The issue of municipal financing is complex and the central and municipal levels share responsibility for problems in local financial management and often under-resourced local governments – explored at length in other chapters of this report. This said, until necessary adjustments are made in revenue collection, debt management, and greater fiscal autonomy, it is unlikely that municipalities, even large ones, will set aside adequate budget for greater participation as this may be seen as a "luxury" rather than a "necessity". For example, in Valparaíso, it is reported that only 1% of the municipal budget has been dedicated to supporting participatory practices.

Chief among the government funding mechanisms for CSOs is the Fund for Strengthening Public Interest Organisations (*Fondo de Fortalecimiento de las Organizaciones de Interés Público*). It is financed through the annual national budget law, and can also receive funds from other state entities, as well as donations, etc. The fund supports national, regional and local level programmes that promote public interest organisations in their activities, and financing for these is available through a competitive bidding process. Funds are also available through competitive funding options from line ministries.

There appears to be no dearth of funding sources. However, there are some problems with how the funds operate, and the consequences of the funding structure. First, key funds, such as the Fund for Strengthening Public Interest Organisations, are fed by allocations from the national budget. If the funding for this line item stagnates[20], capacity to support citizen participation over time is limited – in fact, it represents a *de facto* budget cut. Second, some of the funding programmes established by line ministries to increase citizen participation, such as the Participatory Paving Programme, could be interpreted not as truly encouraging participation, but rather cloaking a method by which communities are paying for services or infrastructure that technically should be funded by government. Third, with the exception of direct transfers, access to funds is competitive: municipalities, communities and CSOs must develop and present programme or project plans to relevant authorities that then decide if the initiative will receive funding. This puts municipalities with less capacity at a disadvantage and can fuel clientelistic behaviour by elected officials. Fourth, funds like FONDEVE, while certainly beneficial for financing a neighbourhood priority, do not support a more participatory process in municipal programming or policy development and implementation. Rather they fulfil the demand and meet the priorities of a specific neighbourhood, and focus on improving

infrastructure or sponsoring events – instead of building participatory processes within the context of municipal (or community) management. In addition, they can further entrench clientelistic practices and can co-opted by those responsible for attributing funds.

This type of funding structure aligns with and reinforces the fragmented, competitive, project-based financing method that is traditionally used in Chile, which in turn limits the ability to take a longer-term, policy-based perspective to solve problems or create change. This structure can be limiting for under-resourced or disadvantaged municipalities, thereby constraining inclusiveness. It may also inhibit building a culture of broad participation, as it associates participation with a specific project or programme in a neighbourhood rather than involving citizens in improving the quality of life, services and programming in their municipality overall. It may also be further weakening CSOs. The majority of CSOs are dependent on government funds for at least part of their financing. However, if they receive funds and these go unused within an established time frame (about a year), the CSO can never again receive funding. This causes several problems, not the least of which is stability in the CSO community. The funding mechanism can favour larger, more well-established CSOs that have an extensive portfolio of projects and penalise younger, newer or under-resourced CSOs, especially if they depend also on winning funds from competitive sources in order to implement their initiatives. Finally, by reinforcing the already strong project-based approach to engagement, it is not encouraging CSOs to remain active, build long-term relationships with citizens and government officials, and prove their capacity to be active civic partners. Overall, the system creates "winners" and "losers", which affects confidence and capacity (OECD interviews).

Political will for citizen engagement could be stronger, particularly at the local level

If political or other leaders, including within CSOs and the private sector, perceive their power to be threatened though participation, then they will tend to disregard the frameworks in place and not promote participatory mechanisms (Wampler and McNulty, 2011). It has been noted, for example, that in Victoria, Australia, while the provincial government actively investigated consultation and community building strategies, debate surrounding participatory and deliberative decision-making possibilities was more restrained (Aulich, 2009).

Low levels of political will with respect to participatory practices are acknowledged among Chilean officials and non-government representatives (OECD interviews). It is evidenced by the lack of uptake or compliance with Law No. 20.500, and while resource shortfalls may be one explanation it cannot be the only one. This is illustrated, for example by the difficulties facing COSOC. As mentioned, some municipalities have difficulties establishing such bodies, but the reason for this when speaking both to municipal officials and COSOC representatives has generally to do with the low impact, real or perceived, of COSOC activity. Their influence and successful operation depends generally on the willingness of the mayor and municipal council to be open to COSOC participation and advice, budget allocation, and allocation of general resources (OECD interviews). It is also evident in studies on participatory budgeting. In the majority of cases where participatory budgeting has been considered successful (i.e. lasting more than three consecutive years), the initiative and support has come from the mayor (Montecinos, 2011). Conversely, the practice failed to take root in municipalities where the mayor was not supportive, as it is ultimately the mayor who decides how much

money is dedicated to the mechanism (Montecinos, 2011). This reticence has also been observed among CSOs that tend to perceive participatory budgeting as a threat to their direct ties with government officials and a limiting factor in their ability to influence project selection for their communities (Montecinos, 2011). Participatory budgeting also threatens the more clientelistic dynamic associated with competitive funding. Municipal councillors can influence the decision with respect to which organisation will receive funds (particularly from the FONDEVE) to finance activities and projects for equipment or community infrastructure (Montecinos, 2011). Not only do these examples indicate a lack of political will, they highlight a structure that can discourage or limit fundamental participatory mechanisms.

The level of understanding that leaders have with respect to participatory practices plays a role in their tendency to accept or reject related mechanisms (Wampler and McNulty, 2011). Building deeper understanding and awareness of the political gains that can be associated with greater participatory governance may be necessary for local leaders to shift their perspective and better integrate participatory mechanisms into their decision-making practices. If they perceive participation as a political threat, then political will is likely to be low. If they perceive participation as a way to do a better job, improve quality of life and well-being for citizens, promote greater inclusiveness, and help them realise their political aspirations, they may be more willing to adopt a participatory perspective.

Building engagement capacity among civil servants, citizens and politicians

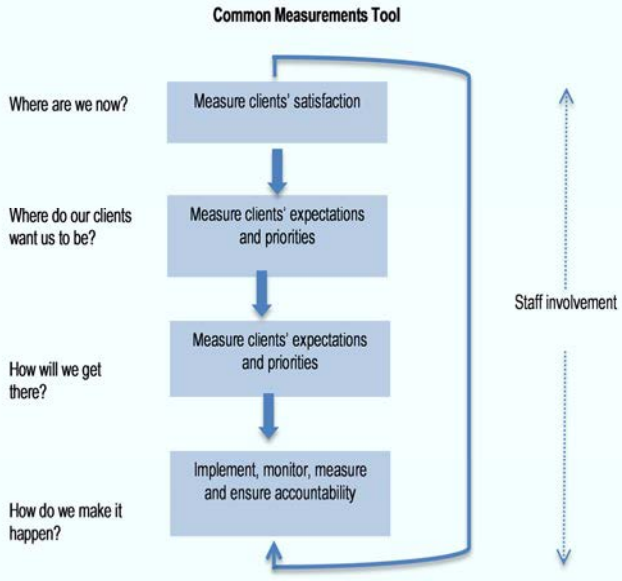
For Chile to progress in its engagement practices, it will need to consider a broad approach to capacity building, and target all primary actors – i.e. civil servants and citizens, including CSOs, and also politicians. The result could be a stronger, more "partnership" oriented relationship between government and non-government actors.

Building capacity to support participatory practices at the local level starts with a willingness for politicians and civil servants alike to listen to and speak with citizens, and to see citizens as more than just a voter but rather as a partner in generating positive policy outcomes. Civil servants may often be reticent to engage with citizens. Incorporating management and training activities focused on dialogue between local public servants and citizens serves as a channel for adjusting the attitude of public servants, thereby contributing to shifts in organisational culture. In Australia, for example, "Value Creation Workshops" are undertaken with citizens so that public servants and policy designers can hear their stories. This interaction helps shape service design and offerings. In Canada, public sector managers at all levels of government use the Common Measurements Tool to better understand citizen expectations, assess levels of satisfaction with interaction and service provided, and identify opportunities and priorities for service improvement. The instrument helps government create links between public sector staff and citizens, and opens space for listening, learning and adjusting. In Finland, an active approach of visiting medical clinics to listen and learn from citizens helped the Kainuu regional government better address citizen needs associated with their healthcare. Officials discovered that solving one of the most pressing concerns was as simple as providing a phone number (Box 5.16).

Box 5.16. **Learning from citizens to improve service delivery in Canada and Finland**

In **Canada**, the Common Measurements Tool (CMT) was first designed in 1998, and has become an internationally-recognised innovation in public management, receiving the Silver Award for International Innovation by the Commonwealth Association for Public Administration Management (CAPAM) and a Gold Award for Innovative Management by the Institute of Public Administration of Canada. It is now used at the federal, provincial and local levels, and has been adopted by governments in other countries. The CMT permits public sector managers to better understand citizen expectations and needs, and adjust service capacity accordingly. The tool helps evaluate citizen satisfaction with services delivered in person, by Internet or by telephone, and creates the space for active listening, learning and adjusting on the part of the public sector, creating a dynamic and positive feedback loop, as illustrated in the figure 5.6 below.

Figure 5.6. **Common measurements tool**



In **Finland**, the Kainuu Regional Council developed the "Happenings" programme to identify and respond to the needs of healthcare users. Under this programme, the healthcare team visited all municipal health clinics twice. During the first meeting, open to all citizens who wished to participate, the team presented the different services available at or through the clinic, followed by a question-and-answer period with the regional healthcare team, the clinic service providers and the municipal residents. After approximately ten days, the team returned to the municipal clinic for an evening session, where they shared the input and feedback they had heard during the previous visit. They then worked together with citizens to identify solutions to some of the most pressing concerns. The team noticed that sometimes the small things mattered most. For example, the healthcare providers at both the regional and municipal levels believed that everyone knew the telephone number for a 24/7 nurse call centre. This, however, was not the case, and a quick, low-cost solution was found to ensure that all citizens were aware of and had easy access to the appropriate number. Through "Happenings", the Kainuu healthcare team built awareness among citizens of the variety of services available to them. In addition, rather than depending strictly on feedback from clinic practitioners, the team listened directly to the end users of the services.

Box 5.16. Learning from citizens to improve service delivery in Canada and Finland *(continued)*

This allowed the development of more targeted and community-tailored solutions, increasing the effectiveness of the services provided, as well as their efficiency. Because reform to healthcare systems at any level is a highly sensitive issue, by developing a two-way communication channel and acting on citizen input, the council increased the potential for residents to feel that they had a role in the process. This, in turn, could increase trust in the reform process and a sense of ownership of the services available in their community.

Source: Institute for Citizen-Centred Service (n.d.), "About the Common Measurements Tool" https://iccs-isac.org/resources-tools/common-measurements-tool adapted from OECD (2010b), *Finland: Working Together to Sustain Success*, OECD Public Governance Reviews.

Often, policy makers need support in identifying when and how to consult, as well as how to commission, monitor and evaluate citizen engagement exercises. Generally, what is sought is access to other people and their knowledge – most easily supported by peer groups and one-to-one mentoring. Here again, Centres of Expertise may be of value, as well as developing communities of practice for public engagement, as seen in the United Kingdom. A community of practice provides policy makers with a network to share challenges and successes, and to communicate with each other on public engagement matters. In the United Kingdom, such a network holds regular meetings and events to meet the need for face-to-face networking. In addition, it uses technology (e.g. email bulletins) to share information and insight on new innovations, best practices, and training opportunities in public engagement (OECD, 2009).

Barriers to engagement can vary in type and by participant group. Research in the United Kingdom indicates that citizens hold back because they often feel they do not have the knowledge and/or skills necessary to participate effectively, or that their involvement has little impact on policy outcomes. Other barriers identified were a lack of time; a lack of confidence and resistance to change in the civil service; difficulties associated with weighing and reconciling stakeholder, expert and political views; and budget constraints. "Consultation fatigue", often arising from a lack of co-ordination among participatory initiatives, is another limitation, especially among government officials (OECD, 2009). Efforts to "up-skill," encourage, and empower citizens to participate are important for building citizen confidence in their capacity to contribute. Also in the United Kingdom, the Department for Communities and Local Government initiated the "Take Part" project (www.takepart.org), which provides active learning programmes to help people acquire the skills, confidence, and knowledge they need to dynamically contribute to their communities and influence public policies and services. The department also published an Action Plan for Community Empowerment: Building on Success, produced in partnership with the Local Government Association. It sets out 23 actions undertaken by the Department to enable people to play a more active role in decisions that affect their community – for example participatory budgeting, developing local charters (voluntary agreements between the local authorities and communities), measures to empower young people, and strengthening the role of local councillors (OECD, 2009).

Some governments also identify ways to match resources and community needs in a participatory manner. Again in the United Kingdom, the Ministry of Justice's "Innovation

Fund" is dedicated to developing new tools that facilitate easy dialogue between government and citizens, and between citizens with similar interests. The "fix-my-street" programme is one such initiative, where through a single portal, citizens anywhere in the United Kingdom can alert their local government of a local problem that needs to be addressed by the government. Problems can range from a collapsed gate to an abandoned vehicle, broken pavement, burnt-out street lighting, etc. (OECD, 2009). Fix-my-street websites are found also in Canada, France, and Ireland, for example, and are applicable not just at a regional level, but at a city level as well, for example in Brussels. Finally, there are ways to support participation among specific and important demographic groups such as youth (Box 5.17).

Box 5.17. **Building participatory capacity in among youth in the United Kingdom**

To help build confidence and participatory capacity among youth in the United Kingdom, the English Secondary Schools Association (ESSA) – a student led organisation, run by and for students aged 11-19 years – offers training, guidance and resources designed to support and promote youth involvement in decision-making processes at a local, national and international level. Its activities include trialling citizen juries in schools, and in 2007 it released an online toolkit for students and teachers

The HeadsUp online forum (www.headsup.org.uk) gives 11-18 year olds a space to discuss political issues, while also developing the analytical, negotiation and debating skills necessary to participate in democratic processes. It also gives politicians a chance to interact with youth on current issues, such as lowering the voting age, or who benefits from globalisation. An evaluation of the initiative showed that 60% of under 18-year-olds said they were more likely to vote after taking part in the Forum.

Source: OECD (2009), *Focus on Citizens: Public Engagement for Better Policy and Services*.

Moving forward, it would be important for Chile to continue building participatory capacity and develop incentives that address any reticence to implementing participatory mechanisms, particularly among local officials and civil servants. Continued opportunities to learn are one way to address this (Suggett, 2012). Such opportunities could serve as fora for exchange of good practices as well as sharing challenges – addressing the general desire to access people and knowledge and share experience. Ultimately these exchanges should not be limited to civil servants. For example, a meeting of COSOC representatives and municipal councillors to exchange good practices, identify common challenges and develop practical solutions could be a useful learning mechanism. However, care needs to be taken so that these opportunities remain constructive and do not devolve into sessions focused on criticising the system or each other. It would also be helpful to provide engagement framework models for the various departments and councils – the lack of guidance and standards with respect to participatory mechanisms often surfaced during OECD interviews. Such frameworks could help identify key principles for engagement, e.g. the OECD Guiding Principles for Open and Inclusive Policy Making (Annex 5.A). They can also provide guidance for when and how to engage: the Public Engagement Spectrum introduced in offers such support.

Encouraging a strategic approach to citizen participation

Chile has done a good job identifying and promoting the development of key participatory tools such as transparency websites, improved access to information, participatory budgets and citizen councils. However, there appears to be greater emphasis on the use of participatory practices as a tool within the context of a specific project or programme rather than considering citizen engagement overall as powerful policy lever to identify, prioritise and support the realisation of broader municipal development ambitions. This is consistent with Chile's tendency toward programme or project-based approaches to implementing government objectives, rather than policy-based ones.

A policy-based approach to engagement can institutionalise participatory practices

A stronger policy-based, rather than tool-based, approach to citizen engagement at the municipal level could help to institutionalise participatory practices. Chile's municipalities are often limited in their ability to implement their own priorities, much in keeping with the managerial multi-level governance typology. When confronted with real or perceived low decision-making autonomy, there may also be little ambition to encourage citizen participation, since there are few options to discuss, and the capacity to influence is low.

Evidence suggests, however, that municipalities that consider citizen participation as a transversal activity and apply a more policy-oriented perspective – in other words, taking a consistent approach to engaging with citizens – are more successful in their engagement practices, as measured by their use of participatory budgeting. For example, municipalities with "high" participation rates in participatory budgeting – i.e. more than 10% of the population participating – are also characterised by citizen participation that is supported by local officials over time. In these cases, there is an effort made by municipal authorities to tie together the diverse engagement mechanisms (e.g. participatory budgets, consultative bodies, local planning instruments).[21] in a coherent whole, rather than considering them as individual tools. There is also a clear policy of openness and of linking citizen decisions to local planning and programming, which favours greater participation (Montecinos, 2011). Such activity may help generate a "participatory governance public" and strengthen the government/civil society partnership dimension that is currently weak. These "publics" are generally comprised of civil society representatives[22] and government officials that engage with each other in public venues and exchange information – thereby providing government with access to demands and needs of citizens, while citizens gain access to information about the government, its resources and its decision-making processes (Wampler and McNulty, 2011).

For participatory governance to become more firmly embedded in local governance, municipalities will need either more support or greater incentive to use participatory practices as a policy lever in a transversal, integrated fashion rather than as a project implementation tool. Accomplishing this could include developing and implementing a municipal participatory governance policy rooted in clear objectives, relies on evidence-bases, clarifies what constitutes participation and what does not. It could teach which tools to use and when, how to evaluate results and incorporate citizen perspective into the decision-making process, and encourage compliance with incentive mechanisms. Participatory practices need to be supported by multi-level governance practices. This might be one of Chile's greatest challenges. If local governments are weak, it is less likely they will be able to produce strong participatory outcomes, especially if expected to

use complex and costly mechanisms (Wampler and McNulty, 2011). Thus, consideration must be given to strengthening local government in order to build the participatory governance quotient. This includes not only building capacity for participation, but also strengthening civil society and developing the tax base (Wampler and McNulty, 2011).

Better aligning participatory governance objectives with multi-level governance realities

SUBDERE's objective with respect to participatory governance at the municipal level is two-fold: to address problems of corruption and through this low trust in government by bringing citizens into the accountability process, and to build a more inclusive society by engaging citizens in improved delivery of local services. Critical to consider however, is whether the current multi-level governance conditions are suitable to accomplish these goals. The objective to build citizen participation for the better delivery of local services is in keeping with the managerial typology characterising Chile's multi-level governance relations. However, doing so while also meeting objectives of greater inclusiveness and empowerment through participatory mechanisms requires space for citizen voice, which is not aligned with this typology and is not characteristic of participatory governance in Chile. Thus, there would need to be a shift in multi-level governance practices wherein local authorities have more room to represent their community's shared interests, and greater autonomy to make policy choices that affect the community. This would mean a greater sharing of responsibility between the central and local level for service delivery and greater accountability of local government to citizens as opposed to the central government. In other words it means a shift toward practices more closely aligned with the "governmental" typology of municipal management.

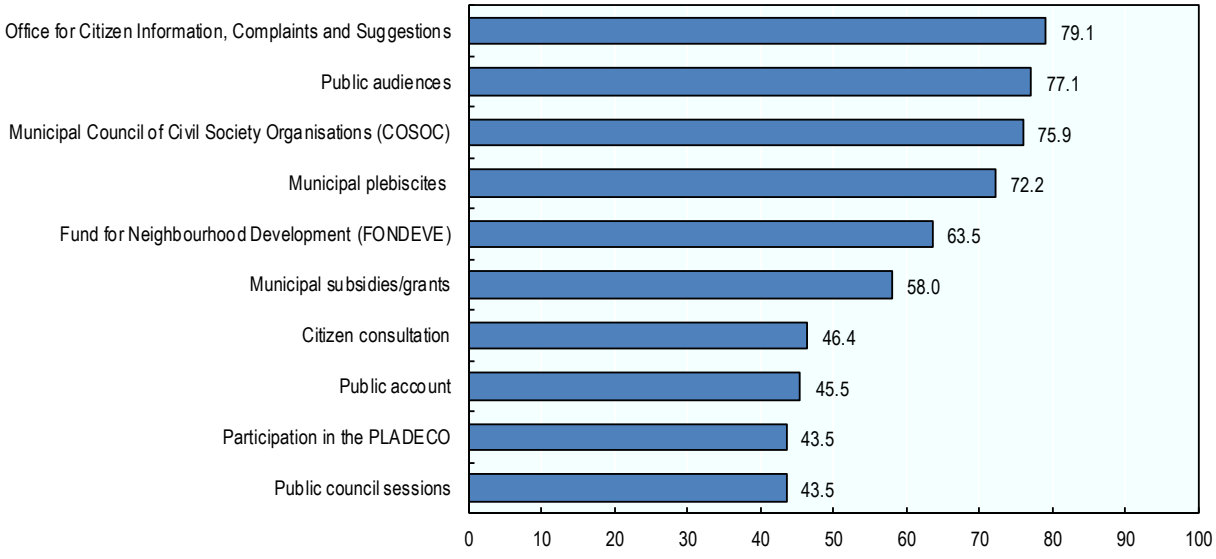
Such a shift in multi-level governance practices takes time, and successfully achieving both objectives simultaneously will likely require greater trust on the part of citizens, as greater trust built through greater accountability will likely engender greater participation. Thus, consideration should be given to a more clearly sequenced approach to building participatory governance. In other words, it may be best if the government first emphasises and promotes mechanisms that support greater accountability (in addition to transparency), in order to build trust. This can structure and reinforce local capacity in fundamental engagement practices focused on informing, consulting and basic involvement. The introduction of more complex participatory mechanisms (i.e. those that promote greater involvement, collaboration and empowerment) could follow, particularly as municipal and civil society leaders begin to see the benefits of participation, become more adept at managing it, and the multi-level governance mechanisms become more supportive, particularly with respect to local level capacity and autonomy in prioritisation, decision making, and resource management. Without these elements in place it may be much more difficult to expect fruitful and empowering participation. Of course, municipalities may be at different stages in terms of enjoying the trust of their residents and in their engagement capacity, thus an approach tailored to the individual realities of Chilean municipalities and their heterogeneous capacities will be important.

Long-term success in this area, however, will require multi-level governance mechanisms that support local level capacity and autonomy in prioritisation, decision making, and resource management. It will also hinge on making room for citizen voice early in deliberation processes and the policy cycle (Wampler and McNulty, 2011). Without these elements in place it may be much more difficult to expect fruitful and empowering participation.

Municipalities focus on mandatory participation mechanisms but do not completely embrace them

In their participation ordinances, municipalities are most likely to include those participatory mechanisms that are obligatory (e.g. consultation for PLADECO) and will tend to exclude non-obligatory ones. Significantly, however, the incorporation of legally-required mechanisms does not reach 100%, as evidenced by the top ten mechanisms cited in participatory ordinances (Figure 5.7). For example, municipalities are required to establish offices for citizen information, complaints, and suggestions (*Oficinas de Reclamos, Información y Sugerencias* – ORIS) but in 2015 less than 80% had done so (SUBDERE, 2015b). What is also striking is that the mechanisms cited do not necessarily promote higher levels of public impact in terms of involvement, collaboration, or empowerment in the policy or programming process. ORIS, while very important as a mechanism for information exchange, do not necessarily provide citizens with more voice in the decision-making process. Plebiscites permit citizens to express satisfaction or dissatisfaction, but are also one-way communication (consultative). Municipal subsidies and the FONDEVE are not participation mechanisms but rather financing mechanisms, which may or may not be used to meet citizen demands. Meanwhile, mechanisms that do promote higher levels of public impact (e.g. participative dialogue, participatory budgets, opinion polling) are incorporated into the ordinances of less than 50% of the municipalities (8.4% and 25.2%, 32.2%, respectively) (SUBDERE, 2015b).

Figure 5.7. **Top 10 engagement tools included in municipal ordinances for citizen participation in Chile % (2015)**



Note: N=310.

Source: SUBDERE (2015), "Evaluación: Ordenanzas de Participación Ciudadana y Conformación de los Consejos Municipales de la Sociedad Civil (COSOC): Informe Final".

Several concerns arise with a heavy reliance on normative (legally-mandated) participatory mechanisms. First, local officials can hide behind the law and legal requirements. While they may establish and apply a minimum requirement or embed required frameworks into their ordinances, there is nothing to ensure that it is actively

pursued. Because civil society is weak and citizens do not fully exercise their right to participate, officials may not be held accountable if they fail to implement the noted participatory mechanisms. It also allows local officials to blame-shift a lack of compliance, evoking the argument that the municipality is under-resourced and thus cannot implement the requirements. This puts the onus of participation on the central level and limits the engagement that takes place, or it makes engagement a reactionary activity.

Second, the mechanisms stipulated as obligatory may be beyond the capacity of some municipalities and thus are limited in their inclusiveness. For example, plebiscites have been facilitated by relaxing technical requirements but they remain a costly mechanism. They are generally used only by the wealthiest municipalities, and often to vote on the Municipal Regulating Plan (PRC) (UNDP, 2014). Participatory budgeting is a tool that is considered to be highly inclusive, but given that: 1) not all municipalities have enough discretionary income to allocate a percentage to a participatory budget; 2) those that do tend to allocate less than 1%, which limits the impact of ensuring that citizen priorities are met; and 3) they can foment clientelistic behaviour on the part of municipal councillors as discussed earlier, this mechanism appears to be limited in its capacity to activate participation (Montecinos, 2011). While having laws that favour participation is one of the three enabling factors for greater participation (ELLA, 2013), laws that state which sort of participatory mechanisms to use can be limiting or even bypassed.

Finally, the array of participatory mechanisms available to governments and CSOs is extremely broad, and while identifying key practices through the law can indicate which practices the government perceives to be most important or relevant, this approach leaves little room for innovation, experimentation or adaptation to specific circumstances or contexts. Considering that Chile's municipalities are having difficulty not only implementing the participatory mechanisms required by law but clearly defining what is a participatory mechanism and what is not, some additional "soft" guidance may be necessary. Box 5.18 below, identifies a broad range of national and subnational engagement practices in OECD countries and provides examples of their implementation. Chile may wish to consider helping municipalities better understand what constitutes a participatory mechanism and build capacity in their use. This could help clarify expectations and better frame processes.

Box 5.18. **A sampler of methods for strengthening citizen engagement practices**

Citizen Fora: Provide a means to deliver policy proposals generated by citizens or their representative organisations (e.g. civil society organisations) directly to policy makers.

In December 2006, thousands of current and former residents of **New Orleans, Louisiana** were invited to an unprecedented Community Congress that took place at 21 meeting sites across the United States (half of the residents of New Orleans had not yet been able to return home). More than 2 500 people, representing the demographic diversity of pre-Katrina New Orleans, took part in the deliberative forum. Linked together by satellite and the Internet, residents struggled with the tough choices facing the city and articulated a set of collective priorities for rebuilding their home city. One month later, 1 300 people came back together to review a recovery plan that had been developed based on their priorities. Support for the plan was overwhelming; 92% of participants agreed that the plan should move forward. For the first time, community leaders had a public mandate to act. Building off this support, the city's recovery plan was soon approved by the city and the state and has begun to be implemented.

Box 5.18. **A sampler of methods for strengthening citizen engagement practices** *(continued)*

Citizen juries: Allow a group of citizens – selected to reflect the general population – to question experts and to offer recommendations after deliberation.

The Department of Sustainability and Environment in **Victoria, Australia**, and the **United States** Environmental Protection Agency (EPA) have both established guidelines for citizen juries as part of larger citizen engagement toolkits. These are intended to involve citizens in a decision-making process. Citizens are generally selected at random or in a stratified way, and provided with a detailed brief of the issue at hand (i.e. a policy or project that has an impact across the community and where a representative or democratic decision-making process is required), its background and current opinions and positions on the issue. They are then asked to discuss potential approaches and the potential impact on the community. The jury might be presented with possible alternatives to consider and asked to pick the option that is the most attractive for the community. They are asked to deliver a report, as in legal juries, which could include recommendations for future action or directions. These juries can be used to broker a conflict or provide a transparent and apolitical perspective on the matter. It is expected that the jurors will add -value based on their own knowledge and personal experience, and the juries will provide an opportunity to build knowledge and exchange ideas.

A study in Australia on the use of a citizen jury in matters of food policy regulation indicated that the method provided policy makers with an effective way to gain insight into the public's view of a controversial policy matter (in this case a proposal to ban food and drink advertising and/or sponsorship at children's sporting events). It also suggests the jury increased participant knowledge of the issue and supported a reflective dialogue on the proposal.

Dialogue processes: Enable governments to engage large number of citizens directly in identifying needs and developing policy solutions.

In 2008, **Bilbao, Spain** launched a highly successful renewal project to transform from an industrial city to a service-based one. In addition to establishing a clear vision and an implementation plan sufficiently flexible that it could be changed if the situation warranted, it also had leadership that was committed to ensuring citizen participation when preparing and implementing policies and programmes. Public consultation opened the door for citizens to express their concerns and discuss potential solutions to the problems the city faced, including unemployment, slow economic growth, poor quality education, etc. This provided the city with an overview of citizen priorities and the issues and challenges that a plan had to address. The city was committed not only to speaking with citizens but also to listening. At the same time, citizens had to be willing to enter the conversation. This often required them to trust that they would be heard and that they would see for wants and needs reflected in project plans and outcomes. This is particularly sensitive and important at the subnational level, where actors often know each other, community interests and individual interests may not align, and outcomes directly impact individual households.

Bilbao's mayor not only listened carefully to the needs of citizens, but also explained potential solutions to problems, acknowledging that the citizens should be heard and brought into the decision-making process. Communicating transparently with citizens meant not only informing about what the government intended to do, it also meant explaining why something was or was not being done, why some policies were favoured more than others, etc. The challenge was to do so in a way that diverse audiences could understand and accept. The lessons stemming from Bilbao's experience is that policy makers not only need to communicate their plans, but they also have to remain open-minded about criticism and scrutiny of the decisions they make, and to be ready to accept responsibility for the outcomes of their decisions.

Box 5.18. **A sampler of methods for strengthening citizen engagement practices** *(continued)*

Consensus conferences: Enable a panel of non-experts (with access to a range of experts) to discuss a complex issue over several days and report on their conclusions.

In the mid-1980s, **Denmark's** Board of Technology developed the consensus conference technique and used it until 2011. These conferences allowed citizens to provide informed input into technical and complex subjects. More than 20 consensus conferences were organised by the Board, based on a standard model: about 16 randomly-selected "lay-persons" (non-experts) were invited to meet over a four-day period around a pre-selected issue, first to hear experts' and policy officials' views, and then to deliberate among themselves. On the final day of the conference, they presented their agreed upon, or "consensus" views. A final document could be written by "lay" participants and was generally aimed at communicating with members of parliament, other policy- and decision-makers, and also the general public. The Danish Board of Technology published these contributions in a series of reports and distributed them to interested parties. These documents have contributed to informing politicians and policy makers on citizen views and attitudes towards new technology.

Norway's National Committees for Research Ethics and the Norwegian Biotechnology Advisory Board applied the consensus conference model in 1996 in order to gain the views of citizens on the issue of genetically-modified food. The conference was held over a four-day period. It consisted of a "layman's" panel of 16 people (eight men and eight women), aged 18 to 72, living in various parts of the country, with diverse backgrounds, and with no ties to organisations or professions with established policies on the topic. The objective of the panel was to: 1) give co-ordinated advice on genetically-modified food to politicians, authorities, and the food industry; 2) to establish a forum for dialogue between experts and non-experts; and 3) to contribute to an all-encompassing and well-informed public discussion on the subject. A follow-up conference on the same topic and with the same panel was held four years later. While subsequent evaluation of the processes highlighted that it was difficult to assess the direct influence of these conferences on the government and parliament, it also underscored the potentially positive psychological impact on public opinion arising from the fact that authorities included laymen in the decision-making process surrounding a complex and politically sensitive policy issue. Additional benefits of the conference include raising public awareness of genetically-modified food. This initial experience in consensus conferences in Norway paved the way for greater use of this mechanism, particularly in the areas of medicine and technology.

Citizen panels: Assess public preferences and opinions, and are often used for assessing service needs and identifying local issues; they can be useful for engaging stakeholders with the development of new policy areas.

In **Bristol, England**, 2 200 panellists reflecting the city's population were recruited through random sample and interviews to form the Bristol Citizens' Panel. It keeps the council informed about public opinion. Since it started in the late 1990s, the panel has been asked more than 600 questions on topics ranging from recycling to changing the selection process for the city's mayor. Panel members receive up to four questionnaires annually, that they can complete on paper or electronically. Results from the panel enrich the decision-making process.

Participatory strategic planning: A consensus-building approach to help a community (or an organisation) articulates how they would like their community (or organisation) to develop over the next few years. It can be used to help a group agree on where they want to go, and how they are going to get there. It is particularly useful to generate a sense of ownership and commitment in a group, and to build consensus.

Box 5.18. **A sampler of methods for strengthening citizen engagement practices** *(continued)*

Participatory strategic planning was used by **Ponders End, North London** to empower and enable residents and the communities to address local economic, social, and environmental concerns, and improve their quality of life. This four-stage process served as a reference point for the Community Development Trust in its movement forward, and helped the Trust find and deliver a programme of community events and infrastructure based on the agreed plan.

User panels: Regular meetings of service users. These panels help identify the concerns and priorities of service users and can help identify problems or generate ideas for improvement. These can be particularly helpful for constituencies whose voice is not usually heard (e.g. children, the aged, etc.) and is a good way to establish two-way dialogue between service providers and service users.

In **Scotland** since 1992, Age Concern Scotland's Fife User Panels have provided an opportunity for the ageing population to influence the delivery of services that can help them maintain an independent lifestyle, for example an enhanced cleaning service for home care clients, and good practice for hospital discharge.

Sources: OECD (2001), *Citizens as Partners: Information, Consultation and Public Participation in Policy Making*; Department of Sustainability and Environment (2016), "Citizen Juries", Effective Engagement, Department of Environment and Primary Industries; United States Environmental Protection Agency (2015), "Public Participation Guide: Citizen Juries", International Co-operation; Henderson, et al., (2013), "Evaluating the use of Citizens' Juries in Food Policy: A Case Study of Food Regulation"; OECD (2014a), Breakout session 2: "Open Government at the Local Level" presented by Ibone Bengoetxea Otaolea, Deputy Mayor, Bilbao, Spain, during the OECD International Forum on Open Government; Grundhal, J. (1995), "The Danish Consensus Conference Model", Public Participation in Science: The role of Consensus Conferences in Europe; The Loka Institute (n.d.), "Tracking Danish-Style, Citizen-Based Deliberative Consensus Conferences Worldwide: An Innovative Way to Involve the Public in Science & Technology Policy Deliberations"; Involve (2016), People and Participation: How to put citizens at the heart of decision making, Involve, London, England.

The mechanics of engagement: Matching aims and means

Consideration must also be given to supporting municipalities identify or define their objectives for participation and align mechanisms to these. This could help streamline the extensive list of mechanisms that municipalities include as participatory (currently over 40) (SUBDERE, 2015a), help limit "consultation fatigue", and prevent a "box-ticking" exercise whereby municipalities include mechanisms because they are required (e.g. plebiscites) or suggested (e.g. participatory budgets) without having sufficient capacity to implement them.

Not all citizen participation methods work in the same way or will achieve the same results, and when building an engagement component into local policy or programming processes there are several questions to ask which can affect the structure of engagement and outcomes.

First, it is important for local leaders to identify the strategic aim of engagement in a concrete manner. In other words, why are citizens being engaged? For example, is it to know what they think about a planned or existing project or service? Is it to increase citizen control over public policies and government spending in order to reduce corruption and improve accountability? Is it to design more legitimate, effective and sustainable public policies and programmes? Table 5.4 provides examples of the types of

engagement mechanisms used in various Latin American countries, aligning these with the concrete aim of facilitating the engagement process.

Table 5.4. **Examples of engagement aims and mechanisms that support their achievement**

Aim of engagement	Engagement mechanism / tool
Increase citizen control over public policies and government spending in order to reduce corruption and improve accountability	• Citizen collaboration with Supreme Audit Institutions in overseeing public spending • Participating in procurement processes • Citizen oversight of social programmes (conditional cash transfers – CCT) • Citizen assessment of service delivery • Social auditing • Citizen observatories • Public funds to finance and promote civil society activities
Design more legitimate, effective and sustainable public policies and programmes	• Citizen consultation • Participatory budgeting • Local citizen councils (neighbourhood or community councils) • Multi-actor/stakeholder dialogue

Source: Adapted from ELLA (2013), "Citizen Participation in Latin America: Innovations to Strengthen Governance", http://ella.practicalaction.org/wp-content/uploads/files/130516_CitPar_GOV_GUIDE.pdf.

Once the aim is clear, desired outcomes should be matched to the purpose of the engagement mechanism or what it can actually provide. If, for example, a local authority wishes to better understand current opinions about an existing issue then it is important to select a participatory mechanism that helps map opinions. Table 5.5 provides examples of common needs and outcomes that can influence the choice of participatory mechanism (Involve, 2016).

Table 5.5. **Examples of engagement activity outcomes matched to mechanism results**

Engagement activity outcome	What is needed from the mechanism
Identifying current opinions about an issue	Map existing opinions
Creating better informed opinions through deliberation	Map informed opinions
Improving relationships by revealing common interests	Improve relationships
Building community cohesion by creating a common or shared vision	Develop/identify a shared vision
Producing new ideas or visions for change	New ideas
Encouraging a more active role by citizens in decision making by giving skills and building confidence	Empowered participants

Source: Adapted from Involve (2016), *People and Participation: How to put citizens at the heart of decision making*, www.involve.org.uk//wp-content/uploads/2011/03/People-and-Participation.pdf.

Equally essential is to match the selected engagement mechanism with the desired outcome and understand where this falls on the spectrum of public engagement (Figure 5.4). This last point is fundamental. Where the selected mechanism and its potential outcomes fall on the spectrum has an incidence on the government's commitment to citizens, and can influence citizen expectations. For example, citizen panels help map

existing opinions and are a useful interaction for informing and consulting – interactions that aim to provide information and to obtain feedback. Depending on whether they are used to inform or to consult, they are associated with greater levels of government commitment regarding the citizen. A community empowerment network, meanwhile, requires interaction that involves citizens and promotes collaboration and empowerment. It is a mechanism that can be used to improve relations, identify a shared vision and empower participants. This generates a different level of commitment from government to citizens; and citizen expectations of the participatory exercise and of government will be higher. The mechanism applied should match the expected outcome. Its placement on the spectrum of engagement should be coherent with the purpose for the engagement exercise.[23] Finally, government must be comfortable with its level of commitment to citizens. If, for example, the selected mechanism is associated with higher levels of citizen empowerment than the government is comfortable with, then the mechanism should not be pursued as the government will not be able to live up to its commitment, undermining citizen confidence in the process.

Table 5.6. **Matching citizen engagement mechanism to outcomes desired**

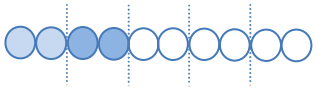
Mechanism	Description	Outcomes the mechanism can generate	Placement on Participation Spectrum
Appreciative inquiry	A mechanism to create a vision and the plan to achieve it; creates an understanding and appreciation of the past as a basis to imagine the future.	• Map: existing opinions • Improve relationships • Shared vision • New ideas	
Citizen jury	Allow a group of citizens – selected to reflect the general population – to question experts and to offer recommendations after deliberation, delivering a "verdict"	• Map: informed opinions	
Citizen panel	Assess public preferences and opinions, and are often used for assessing service needs and identifying local issues; they can be useful for engaging stakeholders with the development of new policy areas; tend to be large and demographically representative of the community.	• Map: existing opinions	
Community empowerment network	Established by government to help civil society play an equal role with the public and private sectors in local partnerships. More than a method it is a government initiative and is included because it illustrates one way to manage capacity building	• Improved relationships • Shared vision • Empowered participants	

Table 5.6. **Matching citizen engagement mechanism to outcomes desired** *(continued)*

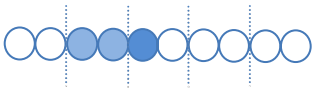
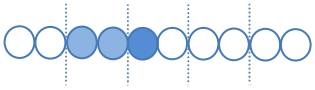
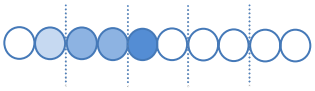
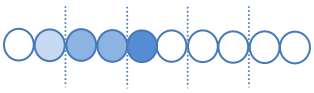
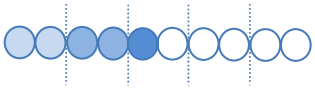
Mechanism	Description	Outcomes the mechanism can generate	Placement on Participation Spectrum
Consensus building/dialogue	Enables governments to engage large numbers of citizens directly in identifying needs and developing policy solutions; helpful to resolve conflicts, improve relationships among diverse groups and build inclusiveness in decision making.	• Improved relationships • Shared vision	
Consensus conference	Allows citizens to discuss an issue and question experts on a particular topic, and their recommendations/conclusions are then shared	• Map: existing opinions • Map: informed opinions	
Deliberative mapping	Brings experts and the public together, combining different approaches to determine how participants rate policy options against established criteria.	• Map: existing opinions • Map: informed opinions • Improved relationships	
Deliberative polling	Measures what the public might think about an issue if they had time to reflect and observe the views of other citizens. These polls are more statistically representative than other approaches given their large scale.	• Map: existing opinions • Map: informed opinions	
Deliberative meeting of citizens	A conversation game that permits small groups to discuss public policy issues.	• Map: informed opinions • Shared vision • New ideas	
Electronic/digital processes	These can range from websites for information to interactive processes that permit a “two-way” exchange	• Map: existing opinions • Improved relationships • New ideas	
Future search	A mechanism to help communities or organisations create a shared vision for their future.	• Improved relationships • Shared vision • New ideas	
Open space technology	A meeting framework that enables an unlimited number of participants to discuss a specific theme.	• Map: existing opinions • Improved relationships • Shared vision • New ideas • Empowered participants	

Table 5.6. **Matching citizen engagement mechanism to outcomes desired** *(continued)*

Mechanism	Description	Outcomes the mechanism can generate	Placement on Participation Spectrum
Participatory appraisal	Strives to build community knowledge and encourage grassroots action.	• Map: existing opinions • Map: informed opinions • Improved relationships • Shared vision • New ideas • Empowered participants	
Participatory strategic planning	A consensus-building tool to help articulate how a community (or organisation) would like to develop. It can help a group agree on where it wants to go, and how it is going to get there. Particularly useful in generating a sense of ownership and commitment.	• Improved relationships • Shared vision • New ideas	
"Planning for real"	Participants make a 3 dimensional model of their local area and place suggestions on how they would like to see their community develop; these are then prioritised in a group and an action plan is created for decision makers to take away.	• Map: existing opinions • Improved relationships • Shared vision • New ideas • Empowered participants	
User panel	Regular meetings of service users that help identify the concerns and priorities of service users and can help identify problems or generate ideas for improvement. Particularly helpful for constituencies whose voice is not usually heard and a good way to establish two-way dialogue between service providers and service users.	• Map: existing opinions	
Youth empowerment	Involving youth is no different than involving the community overall, but engaging with young people may require different approaches. While mechanisms vary, the common belief is that youth have a right to be involved in the decisions that impact their lives	• Improved relationships • Shared vision • New ideas • Empowered participants	

Source: Adapted from Involve (2016), *People and Participation: How to put citizens at the heart of decision making*, www.involve.org.uk//wp-content/uploads/2011/03/People-and-Participation.pdf; OECD (2001), *Citizens as Partners: Information, Consultation and Public Participation in Policy Making*, http://dx.doi.org/10.1787/9789264195561-en.

Resource capacity must also be taken into consideration. Effective engagement practices can be costly for municipalities, so it is important to ensure that the mechanisms selected align with budgets. If they do not, or if there are insufficient resources to

undertake engagement exercises, it can be used as an excuse not to implement a mechanism. It is also costly for citizens to participate in such initiatives (e.g. in terms of transport, time, and absence from work, particularly for the poor) (Wampler and McNulty, 2011). Finally, thought should be given to demographics (Involve, 2016). For example, youth do not necessarily view participation in the same way as older generations, with traditional forms of engagement such as activity in political parties being replaced by participation via "sit-ins", social media, etc. (OECD, 2014b).

For the moment, Chile may not need to develop more engagement mechanisms. However, it could be valuable if the central government and the municipalities took a more strategic approach to identifying and selecting engagement mechanisms (including better defining what is and what is not an engagement tool). This would entail evaluating engagement objectives, the mechanisms that can help meet these, the degree of commitment government is willing to undertake, and the resources involved.

Conclusion

Enhanced citizen engagement practices can help improve the quality and responsiveness of public policies, help put issues on the political agenda and increase citizen control and oversight of government spending and actions, which all contribute to reducing opportunities for corruption (ELLA, 2013). Chile's government appears to seek this sort of impact from its engagement initiatives. It has the legal frameworks in place to favour participation, despite being potentially limiting in terms of their normative structure and inclusiveness. However, it is falling short with respect to the other two enabling factors for stronger public engagement. Political will appears to be lacking, particularly at the local level where citizen engagement may have the most impact, and civil society, despite a strong presence in numbers, appears to lack weight in its capacity to influence decision making and be a genuine partner alongside government, unless it is acting in an antagonistic manner.

Political will aside, many of the challenges facing Chile's municipalities with respect to improving participatory governance stem from the multi-level governance model and the associated managerial typology of municipal management. If Chile's municipal modernisation programme succeeds in increasing municipal autonomy in prioritisation, programming and financing, and in addressing the shortcomings of the municipal finance system, it may be able to create the space necessary for greater compliance and more citizen voice. Creating the space however, will not be enough – there is work to be done to strengthen the culture of participation, reduce fragmentation among CSOs, and look at engagement as a strategic partnership between government and citizens.

Conclusion and recommendations

Chile's deficit in participatory governance appears paradoxical. On the one hand, there is low voter registration and turnout, low trust in government, low levels of compliance in implementing transparency and engagement practices, particularly at the municipal level. On the other, there is a demand for the right to access information, a strong effort on the part of government to build and promote transparency and engagement practices, and evidence that citizens can successfully make themselves heard in the decision-making processes that affect their communities.

One of the key questions, therefore, is what impedes reconciling these two opposing sides of the same coin? The answer may lie in Chile's current multi-level governance

practices and the managerial typology that characterises municipal administration. While effective for ensuring national priorities and policies they leave little room for local governments to identify, implement and fund their own programming, resulting in minimal space for citizen voice beyond information exchange and consultation. The norms, institutions and tools currently in place, while numerous, alone do not appear able to overcome the more structural impediments in the public governance system.

Specifically with respect to transparency and accountability at the subnational level, to date Chile has emphasised the former, yet it is the latter that may better address citizen concerns regarding corruption. Improving transparency by making government information more available and accessible is very important. However, greater transparency does not necessarily automatically mean greater accountability, and it is here where there is more work to be done. Accountability frameworks could be established for example, and performance measurement techniques could be further developed at the national and subnational level. To this end, national and subnational governments in Chile will need to advance in their ability and/or willingness to establish strategic objectives, to associate these with measurable targets/performance indicators and to communicate these broadly. In doing so, it permits citizens to see what government is doing, how funds are being spent, and how government action aligns with public sector and societal objectives for development and well-being.

The government has been focused on building citizen engagement by introducing or reforming laws, identifying participatory mechanisms, and establishing institutional frameworks. These efforts are taking root slowly, however, and activity at the local level, where it is arguably most important, is inconsistent. It is here where the impact of current multi-level governance practices and the managerial typology, particularly with respect to municipal autonomy in decision making and finances, may be most acute. Chilean municipalities may not need more participatory techniques but rather a more strategic approach to identifying and applying them – and this could begin with a better understanding of citizen needs and preferences with respect to engagement (as well as accountability). In addition, there is still work to do in terms of understanding why engagement is important, when it should be used, and building capacity to match objectives with engagement tools. If this is accomplished, it may help address the current problems associated with low political will.

To move forward, Chile may need to step back and consider how it wants to proceed in strengthening participatory governance through greater transparency, accountability and engagement. It has many of tools and institutions to support transparency and engagement, and does not really need any more; it may just need to use what it has differently. Because engagement can depend on levels of trust in government, an approach focused first on building trust, including with techniques that require greater engagement, could be helpful. In other words, concentrate first on mechanisms that support greater accountability – i.e. those that inform, consult and involve citizens – and then consider techniques with stronger public impact such as those that promote collaboration and empowerment. Ultimately, Chile will need to evaluate the architecture of its multi-level governance relations and identify where adjustments could be made that would encourage more participatory governance. The municipal modernisation programme may be a step in this direction.

Box 5.19. **Key recommendations for strengthening participatory governance in Chile**

1. Strengthen Chile's participatory governance institutions and frameworks

- Introduce incentive mechanisms for greater compliance with legal frameworks, particularly Law No. 20.500.
  - Consider providing the National Council for Citizen Participation and Strengthening Civil Society with stronger oversight functions, including sanctioning power, as is the case with the National Transparency Council.
  - Consider a financial incentive that rewards successful implementation of participatory mechanisms in a strategic fashion (e.g., support for municipalities implementing participatory budgets associated with citizen established outcomes or targets; or support for municipalities implementing a citizen-driven municipal development plan with measurable objectives).
- Streamline the number of institutional oversight bodies and make their purpose clearer at the national and local levels.
  - Promote an integrated, cross-sector approach to citizen participation at the national level either by:
    - Expanding the mandate for the National Council for Citizen Participation and Strengthening Civil Society to promote co-operation among diverse civil society actors and sectors for the economic growth and well-being of citizens.
    - Complementing oversight functions of National Council for Citizen Participation and Strengthening Civil Society with an entity inspired by France's Economic, Social and Environmental Council, which actively promotes dialogue on economic, social and cultural matters among diverse civil society actors, bringing its findings to the attention of policy makers, and thus making citizen objectives and priorities known and ensuring cross-sector/cross-society input into government decision making.
  - Reduce confusion, administrative burden and activity overlap by streamlining the number of required participatory councils in line ministries and sector agencies.
    - This could be accomplished for example by providing guidance for ministries to establish one such council or committee per sector rather than per administrative institution.
    - Make clear what is expected of these committees, including who should compose them, their intended value added, etc.
- Strengthen participatory governance at the local level through elected officials and representative organisations.
  - Support the capacity of municipal councils to contribute to the overall development and management of their municipalities, shifting them from serving as advisory or auditing boards to being partners in municipal governance. This can mean:
    - Adjusting the balance of power between the mayor and the municipal council by introducing a mechanism of checks and balances, in this way supporting municipal councils to actively represent constituent “voice”.

Box 5.19. **Key recommendations for strengthening participatory governance in Chile** *(continued)*

  - Broaden municipal council functions to include (shared) responsibility for strategic, policy, administrative, investment and constituency advocacy functions, with active contributions to strategic action, programming, etc.
  - Give municipal councils a stronger role in policy making, ensuring the effective use of resources by defining objectives, setting priorities, establishing clear administrative practices, ensuring transparency and accountability, managing public assets, facilitating citizen participation together with COSOC, supervising municipal public service delivery, and supporting local development strategies and related programming.

- Strengthen the role of COSOC in the municipality, including by:
  - Improving the guidelines for their establishment, composition, budget allocation, use of funds, and activities.
  - Increase their independence and reduce potential conflicts of interest by allowing them to elect their own president (with the mayor being one option).
  - Increase their influence by giving COSOC a greater role in presenting civil society's position on municipal priorities, objectives, issues relating to participation, public services, municipal investments, etc., by consulting with them from the start of the policy/programming cycle and integrating them into the process, including evaluation and monitoring of impact and results.
  - Establish regular meetings between the municipal council and COSOC so they learn to work together – and not separately – for their communities and constituencies.
- Reduce the fragmentation of civil society organisation networks and activity by:
  - Reconsidering the funding structure to ensure greater stability among CSOs.
  - Support CSOs to become advocates for the communities and constituents in addition to being a conduit for implementing neighbourhood specific projects, by bringing them into the policy and programming deliberation process early in the cycle, explaining clearly how their input will be used and if it is not used, why not.

2. Adjust or expand transparency techniques to better include accountability mechanisms

- Make accessing information easier for citizens and ensure that the information is relevant to them:
  - Create a single point of entire website for all government information with "one-stop-shop" functionality, streamlining the current system.
  - Combine information provided with accountability and citizen engagement mechanisms to better link transparency with accountability.
  - Support municipalities in their ability to meet transparency requirements, to keep information up-to-date, and to respond to "in person" requests for information.
- Better align transparency mechanisms with citizen preferences and behaviour, ensuring that the information provided is the information sought:

Box 5.19. **Key recommendations for strengthening participatory governance in Chile** *(continued)*

  - If the objective is to maximize the amount of information available online, support citizens in their capacity to access information with greater internet coverage, higher levels of household access to computers and Internet, and individual capabilities in using online tools.
  - Understand why citizens do not trust information that is available online and do not use online opportunities to complete transactions, in order to better address these.
  - Make sure information available on line and in person is relevant to citizens by first consulting with them as to the information they want to access, how they want to access it (e.g., online, in the press, through juntas vecinales, at municipal offices), and then present the information in a user-centred rather than government-centred manner.
  - Consider piloting a "311" number in metropolitan area municipalities.
  - Improve national and subnational government communication on programmes, plans and works that will affect individual communities before contracts are signed and the work gets underway at a minimum by consulting, but ideally by actively discussing plans, potential impact and intended outcomes or benefits, with citizens. This can be done for example through *juntas vecinales*, COSOC, CSOs, relevant associations or federations, or other citizen bodies in the appropriate sector(s). It could boost citizen confidence in government, increase transparency, and support accountability. It will also support a more effective use of financial and human resources.

- Enhance open government data practices at the national and subnational levels by:
  - Regularly consulting on user needs for data release.
  - Sending notifications to users when new data sets are made available.
  - Systematically facilitating data re-use and support, and train civil servants to build data analysis and re-use capacities.
  - Support municipal capacity in open government data by:
    - Helping municipal governments build data availability, data points and data dissemination capacities -- this could be established as a pilot programme with selected municipalities.
    - Tap into the Open Government Partnership's subnational pilot programme.
- Build greater accountability of local authorities to citizens:
  - Support municipal authorities in the design and implementation of performance measurement/indicator systems, expanding upon available performance information, how it is used, and pursuing the development of performance-oriented initiatives currently underway.
  - Promote the ability for municipal governments to develop accountability frameworks.

Box 5.19. **Key recommendations for strengthening participatory governance in Chile** *(continued)*

- Bring citizens into the local level planning process early on. This can include:
  - Building evidence bases for programming by surveying residents, holding community meetings, meet with CSOs, and involving other stakeholder in the dialogue and design process before decisions are made and for generating plans based on broad and diverse input, that clearly takes into account what is important to citizens. Articulate objectives and indicators of performance, and make it possible for citizens and government officials to follow progress in an openly communicated way.
  - Support the piloting of an initiative that generates citizen driven accountability mechanisms, such as the "Plan de Metas" in Córdoba, Argentina.

3. Strengthen the use of citizen engagement practices at the local level

- Give government officials at all levels a stronger understanding of engagement frameworks and the aims and implications of diverse engagement mechanisms by:
  - Disseminating framework guidelines for participation. These could include:
    - The OECD Guiding Principles for Open and Inclusive Policy Making.
    - The Spectrum of Citizen Engagement.
    - A clear list of what is considered a participatory mechanism (when to use it and why) and what is not a participatory mechanism.
  - Build capacity among civil servants and decision makers to engage with citizens. This can include:
    - Establishing centres of expertise to better institutionalise citizen engagement practices.
    - Incorporating management and training activities focused on dialogue between local public servants and citizens similar to Australia's "Value Creation Workshops" or Canada's "Common Measurements Tool".
- Promote "proactive" rather than "reactive" participation, including by:
  - Better communicating plans that affect a community before decisions are made, thereby creating room for citizen voice, identifying potential problems, avoiding costly "fixes" later in the project, and developing solutions acceptable to all parties.
  - Strengthen the voice of the upcoming generations through municipal youth councils, candidate youth fora, etc.
  - Support citizen participation capacity by matching resources and community needs in a participatory manner, for example through a "fix-my-street" programme and by "upskilling".
- Make sure that municipal capacity in staff, resources and knowledge match the government's participation objectives.
  - Build a deeper understanding of the value of citizen engagement at the local level to overcome obstacles associated with political will.

Box 5.19. **Key recommendations for strengthening participatory governance in Chile** *(continued)*

- Consider a workshop with mayors and other local officials, and CSOs, to highlight experiences of those municipalities where participatory practices are undertaken with a "policy-based" approach and integrated into the functioning of the municipality rather than used as a tool for a specific project.
- Consider establishing dialogue fora for COSOC representatives, municipal council members, and other local officials, to exchange good practices, identify common concerns, and to develop practical, integrated solutions to municipal challenges, including participation.
- Include a citizen participation module in the training provided by the Academy for Public Administration, open to local officials, as well as COSOC, CSOs, etc., where practical skills are taught on how to match engagement mechanisms to objectives, when to select a specific engagement mechanism, how to evaluate the benefit and costs of different mechanisms, and how to use participatory outcomes, manage participant (citizen) expectations, etc.

Notes

1. The OECD average on this scale is 2.4.
2. Data refers to the percentage of "yes" answers to the question: "In this country, do you have confidence in each of the following or not? How about national government?" Data for Chile are for 2011 rather than 2012 (OECD, 2013a, original source: Gallup World Poll).
3. There was an average drop of 5 percentage points in the same four-year period.
4. Of those remaining, it is unclear if they do not have a COSOC or if they did not report back to SUBDERE, which carried out the inquiry.
5. In a recent study undertaken by SUBDERE, among 128 municipalities responding and categorised in six levels according to level of urbanisation and development, 46.3% of municipalities in Level 25 (often those with more resource capacity) and 38.5% in Level 3 either had not established or were in the process of establishing a COSOC (SUBDERE, 2015a).
6. Municipal Regulating Plans (*Plan Regulador Comunal*) govern the spatial development of a single municipal entity. Each municipality must ensure that the development (expansion and densification) established by its PRC can be effectively supplied with the necessary public services (i.e. sanitation, transportation, energy infrastructure and other services). The plan is developed and approved by the Municipal Council (*Consejo Municipal*) after a process of public consultation with the community, including public hearings in those neighbourhoods that might be the most affected by the plan. After the local government approves the plan, it must be approved by the region's SEREMI of the Ministry of Housing and Urbanism (*Ministerio de Vivienda y Urbanismo* – MINVU).

7. These legal entities are non-profit but have rights and an ability to undertake civil obligations and be represented judicially or extra-judicially. The registry however is reported to have a delay in updates and so figures cited would generally reflect the previous six months.

8. This count assumes a broader base of organisations, not just those that are in the national registry of legal entities with a non-profit status.

9. Percentage of students who declared having volunteered formally in the preceding 12 months (students, in grade 8, aged approximately 14).

10. The ICNPO groups are further divided into subgroups, where Law, Advocacy and Politics includes Civic and Advocacy Organisations, Law and Legal Services, and Political Organisations; Development and Housing is comprised of CSOs active in economic, social and community development, housing, employment and training; and Culture and Recreation is divided into subgroups of culture and arts, sports, other recreation and social clubs (Salamon and Anheier, 1996).

11. CSOs can also have a legal status as trade unions or associations (*asociaciones gremiales*), indigenous communities (*comunidades indígenas*), political parties (*partidos politicos*), student groups (*agrupaciones estudiantiles*), etc. (Universidad Católica, 2016).

12. Neighbourhood committees (together with community organisations and community unions) were made possible in the 1980 Constitution and are supported by the 1995 Law No. 19.418 on Neighbourhood Committees and other Community Organisations (*Ley 19.418 Normas sobre Juntas de Vecinos y Otras Organizaciones Comunitarias*) (Ministerio del Interior, 1995).

13. This does not take into account French Guyana which as a region of France shares the country's score.

14. In a 2015 national level study on transparency, less than 2.6% of respondents considered transparency to be the country's most significant problem (N=2 854). Respondents could provide more than one answer to the question: "Of the following list of issues, in your opinion, which are the four most important for the country?"

15. N=1 434 in 134 municipalities throughout the country.

16. Chile breaks transparency down into two categories: active and passive. Active transparency is achieved when the government makes information available to citizens without prior request. Passive transparency refers to the right of individuals to request and receive information from government institutions without having to provide an explanation as to why the information is being requested or for what it will be used (Archivos Chile, 2010).

17. The 15 governments are: Austin, TX, US; Buenos Aires, Argentina; Jalisco, Mexico; La Libertad, Peru; Ontario, Canada; Sao Paulo, Brazil; Egeyo-Marakwet County, Kenya; Kigoma Municipality, Tanzania; Sekondi-Takoradi, Ghana; Madrid, Spain; Paris, France; Scotland, UK; Seoul, Korea; Tiblisi, Georgia.

18. These indicators are: environment; participative democracy; socioeconomic development; urban development and housing; education; health; budgeting; safety; transparency and access to information; and transport and urban mobility.

19. There was an issue of transparency in the Santiago and Barrancones cases as communities discovered government plans only after they were made; there was no discussion with the communities regarding plans that would affect them.

20. For example, if it remains constant over time despite inflation or larger government budgets.

21. These are considered participative mechanisms as the *Plan Regulador* are one of the few municipal responsibilities requiring citizen consultation.

22. Often such "publics" will depend greatly on the characteristics of civil society prior to the institutionalisation of participation (Wampler and McNulty, 2011).

23. For example, a mechanism that focuses on gathering the opinions of a small and homogenous group should not be used for making decisions or creating a vision that will affect a whole population (e.g. an entire city) (Involve, 2016).

Annex 5.A.

Guiding principles for open and inclusive policy making

OECD countries recognise that open and inclusive policy making increases government accountability, broadens citizens' influence on decisions and builds civic capacity. At the same time, it improves the evidence base for policy making, reduces implementation costs and taps wider networks for innovation in policy making and service delivery.

These guiding principles (OECD, 2009) are designed to help governments strengthen open and inclusive policy making as a means to improve their policy performance and service delivery.

1. **Commitment**: Leadership and strong commitment to open and inclusive policy making is needed at all levels – politicians, senior managers and public officials.
2. **Rights**: Citizens' rights to information, consultation and public participation in policy making and service delivery must be firmly grounded in law or policy. Government obligations to respond to citizens must be clearly stated. Independent oversight arrangements are essential to enforcing these rights.
3. **Clarity:** Objectives for, and limits to, information, consultation and public participation should be well defined from the outset. The roles and responsibilities of all parties must be clear. Government information should be complete, objective, reliable, relevant, easy to find and understand.
4. **Time:** Public engagement should be undertaken as early in the policy process as possible to allow a greater range of solutions and to raise the chances of successful implementation. Adequate time must be available for consultation and participation to be effective.
5. **Inclusion:** All citizens should have equal opportunities and multiple channels to access information, be consulted and participate. Every reasonable effort should be made to engage with as wide a variety of people as possible.
6. **Resources:** Adequate financial, human, and technical resources are needed for effective public information, consultation and participation. Government officials must have access to appropriate skills, guidance and training as well as an organisational culture that supports both traditional and online tools.
7. **Co-ordination:** Initiatives to inform, consult and engage civil society should be co-ordinated within and across levels of government to ensure policy coherence, avoid duplication and reduce the risk of "consultation-fatigue." Co-ordination efforts should not stifle initiative and innovation but should leverage the power of knowledge networks and communities of practice within and beyond government.

8. **Accountability:** Governments have an obligation to inform participants about how they use inputs received through public consultation and participation. Measures to ensure that the policy making process is open, transparent, and amenable to external scrutiny can help increase accountability of, and trust in, government.
9. **Evaluation:** Governments need to evaluate their own performance. To do so effectively will require efforts to build the demand, capacity, culture and tools for evaluating public participation.
10. **Active citizenship:** Societies benefit from dynamic civil society, and governments can facilitate access to information, encourage participation, raise awareness, strengthen citizens' civic education and skills, as well as to support capacity-building among civil society organisations. Governments need to explore new roles to effectively support autonomous problem-solving by citizens, CSOs and businesses.

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Chapter 6

Strengthening strategic co-ordination within and across levels of government

This last chapter deals with the need to strengthen strategic co-ordination and co-operation among and across levels of government. Co-ordination and co-operation are all the more necessary due to the decentralisation process which will profoundly transform the Chilean multi-level governance framework. It is, therefore, essential to ensure that: 1) reforms at the central, regional and municipal levels are well co-ordinated; 2) the governance framework is well-balanced and coherent; and 3) the role of municipalities is adequately acknowledged. This chapter focuses on the need to build a coherent multi-level institutional framework which implies managing institutional fragmentation at both national and subnational levels, as well as reinforcing regions for more efficient and stronger municipalities. It also looks at instruments that could be able to strengthen multi-level co-ordination and dialogue, as well as those that could better support horizontal co-operation between municipalities, including municipal associations and better metropolitan governance.

Building a coherent multi-level institutional framework

The institutional and administrative structure of central government, regions and municipalities in Chile and their relationships generate significant challenges for multi-level governance and in particular for co-ordination across levels of government. In many OECD countries, and Chile is no exception, overlapping and concurrent responsibilities across the different levels of government generate ambiguity, lack of visibility and accountability, and reduce efficiency regarding public policies and service provision.

To improve the efficiency of governments, many OECD countries, including Chile, are reviewing and restructuring multi-level governance systems (OECD, 2017a). While some progress has been made in clarifying and reassigning responsibilities to the regional level – in particular with the Constitutional Organic reform of 2009 – it is crucial for Chile, on its path towards decentralisation, to both clearly define the roles of and interactions between the different actors involved in the design and execution of policies and ensure co-ordination.

Managing institutional fragmentation at the national level

The breakdown of responsibilities across sectors in Chile is particularly complex, leading sometimes to overlapping competences and confusing accountability about who is in charge of implementing policies and investments with territorial impact (see Chapter 1). In addition, in Chile, local development policies, planning instruments and local priorities tend to be centrally defined by sectoral ministries, which work within their area of expertise. Line ministries work within somewhat insulated silos with limited mechanisms for ensuring alignment and integration across policy areas and investments and weak mechanisms for consultation on subnational needs (OECD, 2017b).

At the national level different ministries deal with regional, urban and rural matters. The Sub-Secretariat for Regional Development and Administration (SUBDERE) collaborates with the Ministry of Interior regarding the co-ordination and promotion of regional and local development issues (Law No. 18.359). SUBDERE is also responsible for the promotion and design of institutional decentralisation reforms that contribute to an effective transfer of economic, political and administrative responsibilities to the subnational level. SUBDERE also manages investment funds and implements the progressive transfer of sectoral programmes to subnational governments within the current decentralisation agenda. Finally, SUBDERE is in charge of strengthening technical, institutional and human capital capacities in regional governments and municipalities for the design and implementation of regional and local development policies. In turn, urban and rural responsibilities are also fragmented among several national ministries and subnational actors. While the Ministry of Housing and Urbanism (*Ministerio de Vivienda y Urbanismo* – MINVU) has overall responsibility for urban policy and planning, the Ministries of Public Works (Ministerio de Obras Publicas, MOP) and the Ministry of Transport and Telecommunications (*Ministerio de Transporte y Telecomunicaciones*, MTT) also play a strong role in the urban space, particularly with respect to infrastructure and transport policies. In contrast, SUBDERE, which is responsible for co-ordinating regional affairs, has no direct involvement in urban development matters.

In parallel, as in many countries, rural policy in Chile is not the sole responsibility of a specific ministry or public agency. Chile's Ministry of Agriculture (MINAGRI), the institution in charge of the design, implementation, administration and regulation of

national policies related to agriculture, livestock, forestry, food and rural development, implements its policies through twelve public agencies (OECD, 2014a). However, several other ministries intervene in rural policies; MINAGRI does not oversee or co-ordinate rural development in broad terms, and does not intervene or exercise much authority in other policies directly related to rural development. SUBDERE also implements several rural targeted programmes including the Programme of Rural Sanitation (*Programa de saneamiento rural*) and the Programme of Rural Infrastructure for Regional Development (*Programa de infraestructura rural para el desarrollo territorial*, PIRDT).

The national fragmentation of responsibilities on territorial matters has direct consequences for regional and municipal management in issues that can play a key role in local well-being. For example, in Calbuco – where part of the municipality is an archipelago – connectivity between the different islands is crucial for development. Investing in a ferry is a matter of the Ministry of Transport, while investing in a ramp for the ferry to function efficiently depends on the Ministry of Public Works. At the same time, how often the ferry transports passengers to the mainland is a decision taken at the central level after negotiating with the private sector company that will operate the ferry. All this time, consultation with subnational actors is limited or non-existent. This has resulted in incomplete connectivity projects with frequencies that are not necessarily adapted to local needs. Decision making on road transport also illustrates the lack of intra and inter sectoral co-ordination. The MOP is responsible for planning, building and maintaining the intercity network while planning for multi-modal logistics, including road freight, and urban transport are competencies of the Ministry of Transport and Telecommunications and responsibility for planning and executing investments in urban roads lies within MINVU (OECD, 2017b).

Collaboration among the different sectors and levels of governments to develop a coherent approach is particularly relevant in this scenario where responsibilities are fragmented, but also sometimes fuzzy and overlapped. Cross-sectoral co-ordination at the national level should ensure that regional policies contribute to the pursuit of common development goals, limiting the scope of overlapped projects, promoting synergies between policies and investments, and ensuring that projects and local investments are mutually reinforcing. The new Inter-ministerial Commission of City, Housing and Territory (COMICIVYT), created in 2015, is tasked to promote and ensure co-ordination of territorial affairs and regional development, including urban and rural issues. However, given its recent creation its concrete role and scope are still unclear due to institutional immaturity.

While co-ordination is crucial to respond to unclear roles and responsibilities, a first response should involve mapping the distribution of responsibilities both in terms of sectors and functions and if necessary readjusting responsibilities across sectors and levels of government in order to reduce the need for co-ordination (see Chapter 1).

The current decentralisation project seeking to devolve more responsibilities to regions is a good opportunity to re-think and map the distribution of responsibilities also across the different levels of government but also centrally. While decentralisation reforms are often associated with increased duplication and overlapping of competences and services generating administrative overheads, in Chile the devolution of responsibilities might be an appropriate opportunity to diminish these duplications, transforming the risk into a valuable opportunity. The distribution of responsibilities across national and subnational government in the OECD and beyond is diverse and in many cases the breakdown can be particularly complex, leading sometimes to competing

and overlapping competences (see Chapter 1). Building a greater coherence in territorial policy, an objective that has been highlighted by previous OECD reviews, could involve placing the responsibility for territorial development – regional, urban and rural – under one ministry (OECD, 2013d). Indeed, co-ordination across sectors at the subnational level and between the national and subnational governments could be supported by strengthening the role that the SUBDERE plays in the institutional landscape. SUBDERE, in practice, has a very limited role to co-ordinate regional and local policies. Sectoral initiatives follow a top-down approach, with very limited consultation and co-ordination with SUBDERE (OECD, 2009). Within this framework, benefitting from SUBDERE experience and the scope of its responsibilities, it could act as a "moderator" to facilitate and foster co-ordination. Strengthening the role of SUBDERE would facilitate the necessary interaction between different ministries and institutions, and help to integrate the territorial dimension and bottom-up perspective from the regions and municipalities (OECD, 2014a). SUBDERE's role should be reinforced and validated by different ministries as a legitimate interlocutor as it is the "natural" broker between the central and subnational governments in the Chilean institutional landscape.

While strengthening and clarifying the role of SUBDERE at the national level, the new COMICIVYT would also be bolstered. Chilean national and subnational stakeholders do not necessarily have a clear understanding of the role that this institution plays in regional development issues. Mapping responsibilities and competences should also involve clarifying the scope of the COMICIVYT while strengthening its role as a forum for dialogue, with decision-making authority in territorial matters, avoiding overlaps with SUBDERE. To move in this direction, concrete steps should be taken, starting for example, by a web platform that clarifies the role and actors involved in the Committee, its main duties and responsibilities, etc. This would help public civil servants, civil society and other relevant stakeholders to understand how regional development responsibilities are assigned at the national level.

Managing institutional fragmentation at the subnational level

Chile's central government compartmentalisation is played-out at the subnational level bringing with it responsibility overlap and complex accountability relations between subnational entities. This happens across state deconcentrated bodies as well as between these and subnational actors. The *Intendente* (intendant), the regional council (CORE), the representatives of line ministries (SEREMI) and the regional agencies (*Servicios Públicos Regionales*) all intervene in regional and local development with few and limited instances of co-ordination.

SEREMI and regional agencies have little incentive to co-operate and tend to work separately. This is due in part, at least, to the complexity of accountability relations, and mirrors what happens at the national level. SEREMI implement their sector initiatives and answer directly to their national ministry but in the region they also report to the intendant; regional directors of regional agencies are nominated and depend on their national public agency and ministries whilst, in the regions, they have a certain degree of autonomy over the use of resources and implementation of policies in their jurisdiction. They report to both the SEREMI and the intendant (OECD, 2014a).

The presence of too many agencies and instruments makes inter-institutional co-ordination and the generation of synergies more complex. As an example, in the region of Bío Bío there are currently 68 regional branches of national public agencies involved in different regional, urban and rural issues (OECD, 2014a). The lack of formalised inter-

institutional co-ordination tools at the regional level makes it more complex to generate synergies between the broad variety of the programmes and institutions that impact territorial development. Collaboration tends to be the exception rather than the norm; it results from the combination of ad hoc initiatives and the capacity and relationships established between the heads of different public institutions (OECD, 2009). The fact that the heads of public institutions frequently rotate, and that some policy programmes do not overlap policy periods, leaves this ad hoc inter-institutional co-ordination in a precarious position. (OECD, 2014a).

The recently approved reform in January 2017 that allows the democratic and direct election of the new regional governor - replacing the former intendant - represents a step forward in the clarification of roles and the delegation of responsibilities to the GORE. At present, the intendant's mandate is two-fold: to serve as the president's representative and as head of the GORE. As an elected body, a new regional governor would respond directly to the interests of the region together with the elected council and will be the counterweight of the future presidential delegate who will still represent the central government level in the region. To fulfil appropriately his role the central government will need to transfer competences and resources; otherwise regional autonomy would be constrained.

The effective role and power of the "presidential delegate" has raised eyebrows, especially regarding relations with the future elected regional governor. A two-headed region could be risky if the responsibilities and scope of the future presidential delegate are not clearly defined. This risk can be more challenging if a future elected governor is from a different political background than the presidential delegate; this can, in practice, block or slow decision making at the subnational level, thus generating a complex interaction system harming accountability. This dual model of power for the regions seems to replicate the French experience of the 1980s (Valenzuela Van Treek, 2015), which has at the regional and departmental levels a prefect, representing the state (*préfets de département* and *préfets de région*) and elected regional and department executives. Other OECD unitary countries also have similar high-level representatives at the territorial level. However, in contrast with Chile, they are generally senior civil servants representing the state but not the executive. They have no political role. Their mission is to ensure a certain vertical co-ordination between the central government and subnational authorities as well as to co-ordinate the deconcentrated services of the central government in the region. A presidential delegate in Chile will play a political role by definition representing the executive power instead of the state. The presidential delegate should indeed be neutral – a state civil servant – in charge of co-ordinating state services in the region (Box 6.1).

Box 6.1. **State representatives at regional and local levels in some OECD countries**

Several OECD countries have set up state representatives at the territorial level (prefects in Poland, county governors in Sweden, Italy, Finland, Turkey, Hungary, Greece, Estonia, etc.). They may continue to play a key role in the context of decentralisation reforms - to varying degrees, however, depending on the country – including the implementation of national policies at the local level. They generally ensure that these policies are in line with subnational policies, and sometimes supervise local government actions. Having in-depth knowledge of local realities, the state territorial administration plays a co-ordination role between the different stakeholders. It acts as a "pivot" in the administrative system, facilitates multi-level government dialogue on the ground, and sometimes acts as an advisor and "mediator", able to reconcile different perspectives.

In France for example, despite 1982 decentralisation reform and successive reforms, the central government is still very present on the local scene as it has maintained, at both the regional and departmental levels, a prefectural administration led by a *préfet,* a high-ranking civil servant, as well as local directorates of various ministries placed under his authority, so-called "deconcentrated services". Decentralisation has substantially transformed the role of the prefect and deconcentrated administrations. However, they still have significant power and authority. According to the Constitution, the prefect represents the government at the local level and is responsible for national interests, administrative supervision and compliance with laws. The prefect also remains in charge of public order. He/she is the direct representative of the prime minister and every minister at the departmental level, implementing government policies' development and planning. Prefectural administration is also responsible for supervising local government activities (*a posteriori* legality control).

Source: OECD (2017a), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, http://dx.doi.org/10.1787/9789264272866-en.

The relationship and degree of co-ordination of regional actors with municipalities remains weak and tends to occur in an ad hoc manner. While at the local level, municipalities are legally autonomous and its responsibilities might overlap with regional competencies, there are few formal co-ordination instances in which municipalities and regions can participate together. Participation of municipalities in programming contracts (*Convenios de Programación*) for instance, is very limited. The relationship between national, regional, and local actors is often arranged for budget assignment purposes as the practical autonomy of municipalities in fiscal and financial management is limited (see Chapter 2). Co-ordination or collaboration between regions and municipalities often depends on the strength, independence and regional attachment of the intendant or head of the public service, or in the relationships or the capacity of the given municipality or mayor to influence the decision of national institutions (OECD 2014).

Fragmentation at the national and regional levels has a direct impact on municipalities, which need to deal with various actors and entities. SUBDERE is the main central entity in charge of establishing direct links with municipalities and it is the initial contact point for municipalities with the national level. However, other ministries are in direct contact with municipalities as well (or through their SEREMI) in all other areas of shared competences, i.e. education, health, social protection, environment, civil protection, employment, etc. Several national public agencies that deliver key public services have also developed linkages with municipalities such as CORFO, SERVIU, INDAP and FOSIS. (see Chapter 1). The execution of multiple projects depends on agreements with the SEREMI, the public agencies and the GORE, causing a major problem for municipalities known as "red tape" or administrative burden. Dealing with

multiple actors for different purposes increases the costs and barriers for municipalities to undertake any project. Administrative burden combined with low capacities at the subnational level in many municipalities may hamper local management and service provision.

Reinforcing regions for more efficient and stronger municipalities

Regional governments are in a key strategic position to co-ordinate policy priorities vertically with the central and municipal governments, and horizontally among municipalities within its jurisdiction. However, in the current institutional framework, regional governments have limited autonomy in terms of responsibilities and funding and act mainly as vehicles of central transfer to municipalities; their role as brokers to channel effectively local demands and better communicate local priorities to the central level is weak.

Managing relations between different levels of government is a necessity and the regional government is in the best position to manage this vertical relationship. The GORE Planning Divisions could support and facilitate the co-ordination of planning and budgeting processes with the municipalities that are within its jurisdiction in a multi-level and multi-year perspective, while preserving municipal autonomy. They could be supported by their investment units, which were established to evaluate if projects actually contribute to the achievement of Regional Development Strategies initiatives (OECD 2013a). Stronger GORE can favour territorial priorities over sectoral ones taking advantage of their position: a much more direct relationship with municipalities than the central government and at the same time greater negotiation power – due to its size and political strength – than municipalities.

As established by Law No. 19.175, regions might also be key partners for municipalities providing technical, administrative and financial support that better suits local challenges. Regions have generally more technical and administrative capacity than municipalities and municipalities can benefit tremendously from this. Technical assistance to prepare investment projects or planning instruments, management support to implement programmes, projects or investments can be done by regions, which are aware of local context and closer to their concerns than the national government. When regions participate in capacity building for municipalities or municipal associations the results are usually meet local needs better. Indeed, the modernisation of the municipal system, especially regarding the reinforcement of municipal capacities, cannot be designed in isolation; it needs to go hand in hand with a greater role for regions.

Regions could also take a more pro-active role in supporting critical projects that require cross-jurisdictional co-operation acting as regional integrators in particular regarding weaker and rural municipalities. They could be charged with incentivising municipal co-operation for investment projects financed through FNDR or other sources with technical support and as a political facilitator. There are some indications that regional portfolios increasingly integrate projects that involve two or more municipalities in the region (OECD, 2013a) but they need to be pursued further. While strengthening the planning unit of GOREs is necessary, this needs to go hand in hand with bolstering ERDs as master plans that effectively guide and frame infrastructure investments at the regional and local levels. At the same time – as conceived by the decentralisation reforms being discussed – boosting the role of regional governments may let them anchor municipal-level urban governance models and support urban constraints of urban areas, especially medium-sized and small ones (OECD, 2013a).

The current decentralisation agenda suggests a move towards greater emphasis on a territorial dimension strengthening planning and implementation competences of regions (Box 6.2). Like several OECD countries, the current administration has prioritised the decentralisation agenda with the aim of providing subnational governments with the tools, capacities and legitimacy to improve their autonomy and performance. The package of decentralisation reforms promoted by the government is based on four main bills; three focus on strengthening the regional tier. In a scenario where regions have more autonomy to plan, design and implement regional policies, there is a risk of increasing the complexity of the governance structure, imposing more co-ordination and higher transaction costs. Hence, it is also crucial to avoid implementing decentralisation by centralising decisions at the regional level. Co-ordination tools are thus fundamental to attenuate these risks.

Box 6.2. **Regionalisation bills and regional pilot programmes**

The organic constitutional law on the definition of regional responsibilities (Pillar 2 of the decentralisation agenda) is discussed in joint commission at the Congress (at the time of publication). The law on regional financing and fiscal responsibility (Pillar 3) should be presented in 2017.

Pillar 5 is dedicated to the launching of pilot experiments. They aimed at testing the incremental transfer of competencies with selected regions in order to gradually strengthen regional capacities and learn from the experiences. SUBDERE together with other ministries and agencies are in charge of co-ordinating the initiative. The pilot experiments started in 2015 with the regions of Antofagasta, Bío Bío and Los Ríos, which were charged with implementing the pilot experience in the area of productive development, involving the Ministry of Economy and the services of CORFO and SERCOTEC (Chilean Technical Co-operation Service). In 2016, inter-sectoral co-ordination started to define competencies in the pilot programmes pertaining to social and human development as well as in infrastructure and transport. As of December 2016, there were 12 regional governments implementing pilot experiences in the areas of productive development, social and human development, and infrastructure and transport. Pilot experiences are also being conducted in the metropolitan areas as the bill gives the regions the responsibility of managing metropolitan areas, becoming the "metropolitan regional government" (SUBDERE 2016c).

In this process, the Chilean government has defined three types of competences:

- Those that are defined by the current law (LOCGAR 19.175), i.e. 23 regional responsibilities.
- Those new ones that are contained in the bill on transfers of competences i.e. 49 new responsibilities, including the metropolitan areas, the Programming Contracts (*Convenios de Programación* which will be compulsory) and the Regional Plan for Land-Use (*Plan Regional de Ordenamiento Territorial* - PROT).
- And those that are tested with each ministry and service (e.g. FOSIS, SERCOTEC, CORFO, SERVIU, INDAP, MTT and the MOP) in the framework of the pilot experiences and which are called "Competencies by Occupation" (*Competencias por Oficio*). SUBDERE has identified 39 responsibilities in this category (SUBDERE 2016).

According to SUBDERE, a total of 111 responsibilities should be carried out by regional governments by 2022.

Source: SUBDERE (2016), *Presentación Seminario Plan de acción estratégico del área metropolitana de Concepción, desafío de una gran ciudad*.

Reinforcing multi-level co-ordination and dialogue through adequate instruments

Establishing coherent planning instruments across levels of government

The planning framework that guides development and investment strategies at national and subnational levels in Chile is complex. For regional, urban and rural development co-ordination and collaboration in policy planning are infrequent and approaches to territorial development and management remain in silos and with limited cross-sectoral dialogue and local consultation. Agreements between different ministries and institutions, as well as between public agencies belonging to the same ministries, often occur on a voluntarily basis and seek to co-ordinate efforts and resources towards a common objective. While this should change in the short term thanks to the COMICIVYT, at least at the national level, concrete progresses is being made at a slow pace.

The confluence of many actors in territorial and local matters in Chile makes it critical to develop planning frameworks that promote a coherent approach. Strategic planning can be indeed a key tool to co-ordinate priorities between different sectors. With a coherent strategic planning of regional development and public investment, Chile could ensure adequate public services and encourage growth and productivity in the entire territory. For this to happen, development strategies should be based on an assessment of regional and local characteristics and specific competitive factors, with investments aligning with regional needs (Mizell and Allain-Dupré, 2013). Indeed, strategic development planning at the regional level would help Chile to attain better productivity levels in the entire territory.

In Chile, there is a strong tendency to address challenges by creating new plans or institutions that adapt to circumstances and address formally the challenge identified. While this is not a problem on its own, at some point it can be harmful and may hinder the legitimacy of such instruments. This has been the case of different initiatives taken by different governments to promote co-ordination both across sectors and levels of government, which have been discontinued or replaced. For example, for the period 2010-2014, the 15 *Planes Presidenciales* that aimed at better co-ordinating the different central government ministries and institutions related to regional development or the now defunct Regional Agendas for Productive Development (*Agendas Regionales de Desarrollo Productivo*), which was formerly driven by the regional development agencies that no longer exist.

Multiple subnational planning instruments

Chile has not yet developed a national strategy for regional development that integrates the country's development and investment strategy and frames regional and local development within a unique coherent framework document. Instead a wide range of planning tools guide regional and local development where national actors play crucial roles in developing, approving, or financing them. True linkages among plans at different levels of government and the extent of involvement of local actors in their design are limited.

Still, Chile has made important progress in co-ordinating its strategic planning framework to align regional and municipal strategies with national priorities. In 2009, an important reform towards regional autonomy empowered the regional governments (*Gobierno Regional*, GORE) to plan regional development via the Regional Development Strategy (*Estrategia Regional de Desarrollo*, ERD). ERDs are long-term strategies that

should guide the different programmes, policies and investments in the region (SUBDERE (n.d. c).

During the last update of the ERD, regional governments have made important progress in involving different stakeholders in the design phase of the strategy: in a vast majority of regions, citizens, provinces, municipalities, and the private sector, among others, are consulted to define regional and local priorities. Gathering municipalities and relevant stakeholders means an important step forward, especially in the relationship and collaboration between regions and municipalities. Some regions have emphasised the ERD and have, subsequently, made progress in defining local priorities, which has sent a powerful signal to move from small and isolated projects to more comprehensive and strategic ones. However, these efforts are mainly driven by external consultants, usually universities, contracted specifically to design the regional strategies - as regions sometimes do not have the adequate capacities to lead this process.

Still, because the ERD is a non-binding instrument, the regional, local and national levels are not required to follow these guidelines. The strategies have not yet achieved a level of maturity that allows them to act as the main umbrella and anchor for local priorities. Some subnational governments still consider it as a pure planning exercise with no real impact on the ground. The current absence of a national-level territorial strategy also leaves ERD without an anchor in higher-level objectives (OECD, 2013a).

At the municipal level, according to the Organic Constitutional Law for Municipalities, the Municipal Development Plan (*Plan de Desarrollo Comunal* - PLADECO) is supposed to guide the development of the municipality (Box 6.3), which in turn should follow the guidelines of the ERD. These plans are the primary instrument for planning, managing and co-ordinating local development. They integrate a diagnosis of the socio-economic characteristics, strengths and challenges of the municipality and identify its main development priorities in such aspects as infrastructure, productive development, education and the environment (OECD, 2013a). Yet, the PLADECO – like the ERD – is not binding and has limited impact on the funding allocated to local projects. Many municipalities perceive the PLADECO as formal instruments with no concrete implications for the municipality; in many cases, designing the PLADECO is more a burden than an asset for municipal development. This is directly linked to the limited knowledge that citizens have about this instrument; a survey in 2010 identified that only 4.6% of the population is familiar with the PLADECO (Universidad Autónoma de Chile, 2010).

Box 6.3. **Regional and municipal development plans**

In 2005, a regional strategic planning competence was devolved to Chile's regional governments (*Gobierno Regional* - GORE). This led to the establishment of a regional planning division within each GORE, dedicated to elaborating comprehensive, long-term strategies for their region's growth and development. Designed by regional governments, these regional development strategies (*Estrategia Regional de Desarrollo* - ERD) are in an excellent position to take into account territorial realities and regional priorities, and to promote greater coherence in regional planning.

PLADECOs are Chile's Municipal Development Plans (*Plan de Desarrollo Comunal* - PLADECO) and are a key development-planning and management tool for local authorities. Their objective is to contribute to the efficient administration of local governments and to promote the community's economic, social and cultural development.

Box 6.3. **Regional and municipal development plans** *(continued)*

Ideally, PLADECOs reflect a strategic vision for the municipality's development and establish a roadmap for achieving this vision. According to article 7 of the Organic Law of Municipalities, the guiding principles of PLADECOs are:

- Participation: the interests of citizens should be taken into consideration through a participatory process in the PLADECO's development.
- Coherence: there should be co-ordination and alignment between the scope and content of PLADECO and the range of public services provided in the municipality.
- Flexibility: the plan should undergo periodic evaluation to permit necessary adjustments and modifications, in line with changes and new challenges in the municipality.
- Strategic: the plan should take into account the actions required to meet community needs and to promote social, economic and cultural advancement.
- Operational: the plan is the leading instrument for municipal development, translating strategic guidelines and objectives into a multi-annual programme of action.

Source: OECD (2013a), *OECD Urban Policy Reviews, Chile 2013*.

While the ERD and PLADECO should guide subnational development in a co-ordinated manner, various other planning instruments, designed to respond to specific challenges, have implications for territorial development. Some of these plans are the Special Plans for Chiloé, Arauco, Rapa Nui, among others, the special plans for outlying areas (Arica y Parinacota, Aysén, Magallanes, among others) or other sectoral plans such as the regional infrastructure plans or the infrastructure plan for connectivity of indigenous rural communities (OECD, 2017b). The myriad planning tools, combined with weak ERD and PLADECO, can constrain effective co-ordination.

Municipal land use plans are piecemeal and poorly co-ordinated

Land use plans can facilitate co-ordination among national and subnational priorities and across sectors as well. These instruments can reduce the scope for conflict between different uses of land aligning regional and local strategies with national guidelines. In Chile, however, while important efforts to co-ordinate these statutory plans (regulating plans) with management/development plans (e.g. PLADECO or ERD) have been made, the coherence among them remains weak.

Chilean municipalities are responsible for preparing municipal regulating plans (*Plan Regulador Comunal*, PRC) while regional governments prepare Regional Plans for Land-Use Planning (*Planes Regionales de Ordenamiento Territorial* - PROT). A third planning instrument, the Inter-Municipal and Metropolitan Regulating Plans (*Plan Regulador Intercomunal/Metropolitano* - PRI/PRM), is prepared by the MINVU's representative in each of the 15 regions and governs the spatial development of urban and rural areas that are integrated into a larger urban unit such as a metropolitan area (OECD, 2013a). Both PRCs and PRI/PRM have to be approved by the CORE. These various regulating plans are meant to provide a spatial dimension to regional and municipal development strategies.

However, a main challenge for land-use planning remains the definition of urban boundaries that do not correspond to functional realities (OECD, 2014a); current plans

create an imaginary boundary between rural and urban planning hindering co-ordinated planning especially where rural and urban territories intersect. The current PRI/PRMs have advanced in this domain but a deeper integration that explores synergies and better integrates sectoral policies is needed. The PROT could also better improve coherence between economic and spatial planning at the regional level. The main goal of the PROT is indeed to give a spatial dimension to the implementation of the ERD with a cross-sectoral perspective and municipal input. However, the coherence and links between land-use tools (e.g. PROT and regulating plans) are insufficient. Moving forward, Chile should ensure that regulatory plans and development strategies are nested into a broader territorial development strategy (OECD, 2014a).

The co-ordination role of the ERD, PLADECO and the regulating plan – especially the PROT– needs to be better defined by specifying the role and relationship of these various planning documents (OECD, 2013a). While the ERD should help to guide municipalities in the formulation of their PLADECO, the PROT should inform the design of the municipal regulating plans. The co-ordination across different sectors (SEREMIS and Services) and municipalities needs to be strengthened as well. To improve planning coherence between regional-level strategic and planning instruments (i.e. ERD and PROT) and their municipal level equivalents (i.e. PLADECO and the various regulating plans) better co-ordination among different authorities is needed (OECD, 2013a); stronger dialogue across the different levels of government when designing these instruments will also benefit the development of the appropriate capacities, especially at the local level.

Municipal plans for education and health

In parallel, for education and health issues, municipalities' strategic planning seems to have limited relevance. Instead of strategic planning tools, municipal plans are more like annual guidelines that, in a few cases, serve as accountability tools for education or health management (Valenzuela J. P., 2007). Since 1995, the main planning tool for education, which must be developed annually by all municipalities, is the Annual Plan for Municipal Educational Development (*Plan Anual de Desarrollo Educativo Municipal* - PADEM). The PADEM evaluates each establishment, analyses supply and demand, sets goals for both the whole municipality and each school, defines programmes to be developed, and sets the annual budget including investments, revenues and expenses. The PADEM must also specify necessary staff, including teachers, to adapt to enrolment demand.

For health services, the main planning instrument is the Annual Municipal Health Plan (*Plan Anual de Salud Municipal o Plan de Salud Comunal*) which should include: 1) guidelines for municipal health policy; 2) updated participatory health diagnosis; 3) evaluation of previously-implemented actions and programmes; 4) most likely scenario for municipal health in the period; 5) prioritisation of problems identified; and 6) activities to address each priority and indicators of compliance with scheduled goals. This instrument contributes to the drafting of a participatory diagnosis and the strategic definition of the main difficulties for municipal health management. However, as it is the case for education, its real impact seems to be limited (Valenzuela J.P., 2007).

Under-exploited potential of subnational development plans

As with many OECD countries, in Chile the usefulness of regional and local planning instruments is constrained. The ERD and PLADECO, for example, likely provide a basis for community deliberation, discussion, and planning, but their non-binding and unfunded

nature appears to limit their usefulness – particularly given the annual, project-by-project budgeting approval process.

Co-ordination in the planning process can generate positive outputs in several ways that enhance territorial productivity. Strategic planning should lead to an investment mix that ensures adequate public services and encourages growth. Planning activities that identify and seek to mobilise regional assets (sources of competitiveness) are integral to effective investment planning. Taking an asset-based approach to planning, versus a need-based one, recognises that regions have "tangible and intangible assets that can act like springboards for and facilitators of economic growth" (Mizell and Allain-Dupré, 2013). For this, involving subnational government in developing strategic planning, and ensuring co-ordinated priorities can favour Chilean productive capacity. However, in Chile, the role of subnational actors still tends to be subsidiary, more focused on approving plans and models previously decided by the national actors than on actively participating in the definition of these plans. Encouraging more active participation of subnational actors in these initiatives would be crucial to reflect the specific territorial needs and realities, and to gain the buy-in and support of local actors to these central government initiatives (OECD, 2009, 2013a, 2014).

Multiple planning tools might generate overlap and potential redundancies, creating confusion more than coherence across the different levels of government and stakeholders. Successful strategic planning requires dialogue and negotiation between the different levels of government, which lays the groundwork for co-ordination to take place. Thus, for planning instruments to effectively serve as co-ordination instruments, Chile should streamline planning tools. This would encourage dialogue among the different levels of government so that local priorities are integrated effectively. ERD and PLADECO should be given further legitimacy, acting as the main engine for co-ordination. However, for this to happen, incentives must be aligned. If co-ordination is not rewarded by effective development and investment policies that benefit local governments, dialogue is unlikely to happen.

An important challenge preventing the ERD and PLADECO from acting as co-ordination instruments is local governments' lack of motivation and/or institutional and technical capacity to use them in an integrated manner, i.e. as strategic tools for defining, implementing and monitoring inter-sectoral initiatives. The challenges linked to the congruent design and implementation of ERD and PLADECO are of uneven magnitude depending on subnational governments, as their capacities differ greatly throughout the country. Some municipalities lack the capacity to design their development plans; many subnational governments have difficulties in building a diagnosis of their needs and defining investment priorities, notably due to weak human resources. Some municipalities lack methodological tools, leading to difficulties in using existing data and in building an integrated strategy. Some municipalities do not recognise the importance of PLADECO and the need to articulate it with ERD, given the fact that it is not recognised as a tool for financing development. This ends with municipalities implementing isolated and often small projects disconnected from any strategy.

A major challenge for Chilean municipalities is to move away from a merely formal exercise and plan strategically in co-ordination with regions and the central level. In general, the disconnect between the PLADECOs, the financing lines and land use plans prevents local governments from recognising the importance of this planning instrument and the need to articulate it with ERDs. The budgeting process is not conducive to coherence among planning instruments. Regional and local strategies are not directly

linked to funding streams, so their implementation is tied to annual regional budget capacity, which depends on central-level grants (OECD, 2013a). Although the ERD and the PLADECO are multi-year plans, the investment funds are allocated annually and on a project by project basis.

The ability to overcome the lack of co-ordination of planning instruments is limited by political cycles that create incentives for national and local actors to prioritise a short-term agenda. In Chile, the challenge is particularly relevant because of the four-year electoral cycle combined with the single presidential terms. At the local level, the problem is even more acute: in the middle of the election of the regional council (at the same time as the president) and the four-year designation of an intendant, municipal elections take place. Regional councillors work with different mayors during their term and the election of mayors is potentially politically captured by the elections of councils. There is a potential risk of local actors becoming political actors that are constantly in campaign mode.

To improve the role of strategic planning in co-ordinating national and local priorities, Chile should better define the role and relationship of the various planning documents - strategic and land use - so that it is clearer how regional and local strategies should interact. For this, Chile should strengthen the role of the ERD as an instrument to guide and articulate regional and local development strategies (OECD, 2017b). The ERD can effectively provide a strategic regional development framework in line with a national strategy, which identifies long-term regional development goals and serves as a guiding document for municipal PLADECO.

Improving linkages between planning and budgeting

To improve co-ordination between the different planning instruments, planning and budgeting need to be better aligned. Financing and budgeting practices need to support subnational development objectives and investment in order to encourage an effective co-ordination among sectors and across levels of government. If there are no monetary or budgeting incentives it is more difficult for co-ordination to take place and a "siloed" or short-term plan will prevail.

Funding mechanisms and the budgeting process in Chile stand in the way of a comprehensive and strategic approach to planning and project prioritisation. Funding for regional and municipal projects follows a sectoral logic, and the various projects comprising an integrated initiative risk being evaluated independently of a master plan. For investment projects, the different approval stages a portfolio must follow, notably the filter applied by the CORE and the final evaluation made by DIPRES, largely take place on a project by project basis (OECD, 2017b).

Some articulation between the ERD and the PLADECO takes place during the budgeting process through the Preliminary Draft on Regional Investment (*Anteproyecto Regional de Inversiones* - ARI). The ARI lists regional investment projects which need to be considered when formulating the region's budget and those of ministries and intends to harmonise investments that will be made at the municipal and regional level. Once the annual national budget law is approved, the ARI becomes the Public Programme for Regional Investment (PROPIR), both are available online *ChileIndica*. The ARI and the PROPIR are supposed to follow regional guidelines established in the regional and municipal strategies (they are not mandatory documents) showing some inter-regional co-ordination and vertical co-ordination with the central government in the budgetary process. The budgetary co-ordination carried out by SUBDERE through its Co-ordination

of Public Expenditure Unit - *Unidad de Coordinación del Gasto Público* aims at reducing divergences or contradictions between sectoral investments. Still, a sectoral and top-down approach to co-ordination dominates. Ultimately, the national budget office (DIPRES) has the final say on which regional investments are integrated in the budget law and this decision is primarily based on a project by project logic.

The ARI and PROPIR are important co-ordination mechanisms that reduce discrepancies between sectoral projects and provide an interesting framework to co-ordinate both vertically between central ministries and across sectors. Yet, the non-binding nature of planning instruments also limits co-ordination as intendants are not required to follow regional and municipal strategies nor to consult local priorities with mayors. Chile should strengthen the ARI and PROPIR to effectively link budget and plans in the medium and long run. For this, some elements of the planning instruments could be binding for them to be included in the final PROPIR. With this, planning instruments are also reinforced to act as effective co-ordination instruments.

Box 6.4. **Articulating planning and funding: The experience of EU funds**

With a budget of EUR 454 billion for 2014-20, the European structural and investment funds are the European Union's main investment policy tool. National co-financing is expected to amount to at least EUR 183 billion, with total investment reaching EUR 637 billion.

The post-crisis period has provided additional motivation for reforming the way the European structural and investment funds are planned and used. In a climate of declining overall investment, maximising the impact of these funds is a top priority, especially as they provide the majority of public investment in many countries.

Following the lessons learned from previous programming periods and taking into account the need for better use of European structural and investment funds, the 2014-20 regulations introduced several key reforms. There is a clear move towards a more focused policy approach, stronger results, solid framework conditions for investments, better co-ordinated use of funding through the common strategic framework, and improved links between EU priorities and regional needs.

Member States are required to draw up and implement strategic plans, with investment priorities covering the five European structural and investment funds. These "partnership agreements" are negotiated between the European Commission and national authorities, following their consultation of various levels of government, representatives from interest groups, civil society, and local and regional representatives.

Partnership agreements outline each country's strategic goals and investment priorities, linking them to the overall aims of the Europe 2020 strategy for smart, sustainable and inclusive growth.

Once the partnership agreements have been adopted, the European Commission and the national authorities agree on programmes, setting out the priorities for each country, region or policy area concerned.

Box 6.4. **Articulating planning and funding: The experience of EU funds** *(continued)*

Combining different funds to finance local investment projects

- Integrated territorial investments make it possible to combine funding from different European structural and investment fund programmes to support the implementation of territorial development strategies. Twenty Member States will use integrated territorial investments in areas ranging from struggling urban neighbourhoods to metropolitan areas, from cultural heritage routes to sub-regions hit by economic restructuring.
- Community-led local development empowers local action groups to implement strategies creating jobs and growth and enhancing social inclusion by combining different EU funds. Over the programming period, multi-fund community-led local development is supported with more than EUR 12 billion. In rural development, more than 2 500 local strategies will reach out to half of the EU's rural population, while the European Maritime and Fisheries Fund will support some 280 related strategies in coastal and inland communities. Seventeen Member States will support local development strategies in cohesion policy.

Source: OECD (2016), *Making the Most of Public Investment in Colombia: Working effectively across levels of government*.

Integrating subnational governments into co-ordination platforms

Platforms where actors from different levels of government and sectors can formally dialogue have proven to be effective in several OECD countries. Beyond co-ordination, platforms for dialogue promote collaboration among its members and also serve to strengthen capacity through information exchange, training, and showcasing best practices (Mizell and Allain-Dupré, 2013, OECD 2013c). When involving the different levels of government, a dialogue fora can help to clarify the main capacity challenges and bottlenecks impeding effective management of subnational policies and/or investments; at the same time they can ensure – or at least promote - that national policies include subnational inputs. Dialogue fora are predominantly set at the national level, involving several sectors for specific purposes. Inter-ministerial committees are for example a leading governance arrangement in decision making regarding regional, urban or rural development. In the OECD, 24 countries have some form of inter-ministerial committee; on average, these platforms involve six ministries with an explicit role for urban policies, the most fragmented among the three policy areas.

Chile has a long tradition of ad hoc or permanent inter-ministerial and/or advisory committees to solve particular issues such as reconstruction after natural disasters or for longer-term purposes such as the definition of the National Urban Policy. Recently, Chile has created a new co-ordinating mechanism, the Interministerial Committee for City, Housing and Territory (*Comisión Interministerial Ciudad, vivienda y Territorio*, COMICIVYT), which initially was created to co-ordinate land use and infrastructure planning across ministries (Box 6.5). The first purpose of the COMICIVYT, which was set up in the 15 regions was the design of Regional Plans for Investments 2015-2022 (*Plan Regional de Inversiones 2015-2022*). The experiences of these committees were uneven; in some cases, genuine real co-ordination took place but in others the regional investment plan was the result of adding another layer of sectoral policies, depending largely on the political will of the actors involved and the intendant (OECD, 2017b). Although the regional strategies have already been defined, remarkably the CORECIVYT

– the regional expressions of the COMICIVYT – are still in place and now involve 12 ministries and some services such as the National Office for Emergences (ONEMI). These regional committees, although they have not yet been formalised in all regions, now have the task of validating the Regional Land Use plans (*Plan Regional de Ordenamiento Territorial* - PROT).

Box 6.5. **Inter-ministerial Committee at the regional level**

The Interministerial Committee for City, Housing and Territory (COMICIVYT) was established by Decree no. 34 on June 5, 2015. The COMICIVYT is responsible for formulating policies relating to land use planning and developing integrated investment plans in each of the 15 regions. Five ministries participate in the infrastructure planning dimension: the Ministry of Housing and Urbanisation, MOP, MTT, the Ministry of State Properties, and the Sub-secretary for Regional Development of the Ministry of Interior and Public Security. The COMICIVYT thereby provides a cross-sectoral platform for prioritising infrastructure investments within regions based on a long-term vision for the region's development. Regional integrated infrastructure plans developed through the COMICIVYT have a five-year timeframe and inform the annual budget discussions held between spending ministries and the Ministry of Finance Budget Department (DIPRES). They, therefore, have the potential to greatly improve the overall coherence of infrastructure planning within regions thus maximising the efficiency and impact of both public and private investment.

Source: OECD (2017b), Infrastructure Governance Review: Chile – Gaps and Governance Standards of Public Infrastructure.

Taking advantage of the long-standing tradition of inter-ministerial committees, Chile should strengthen and further institutionalise the CORECIVYT as it can effectively co-ordinate policies and investment with regional or local impact and foster dialogue over time. With this, Chile would avoid the creation of a new institution reducing co-ordination entity overload. It would also build on past experience with regard to building regional investment strategies. Moreover, OECD experiences show that countries with well-developed and long-standing co-ordination arrangements have a comparative advantage for the introduction and implementation of future reforms, as it takes time to build co-operation arrangements and trust. Thus, such a platform can help Chile to move forward in decentralisation reforms. As is the case with the COMICIVYT, concrete and simple steps should be taken if progress is to be made. These steps could include a web platform that highlights the role and relationship between the COMICIVYT and CORECIVYT. Indeed, communication about the existence of such a platform is a crucial step to bolstering this institution.

For these committees to successfully serve as co-ordination and collaboration fora, the CORECIVYT should include municipalities or municipal representatives - which have been absent so far. In Chile, associations such as the Chilean Municipal Association (*Asociación Chilena de Municipalidades* - AChM) and the Association of Chilean Municipalities (*Asociación de Municipalidades de Chile* - AMUCH) have already been brought into the reform process through the Memorandum of Understanding for the Modernisation of the Municipal System of 2014 and the CTAM, which is a very positive approach (Box 6.6). Now, they could be key partners involved permanently in these platforms for dialogue. Other forms of municipal associations with particular interests could also be part of the platforms either temporarily or permanently. International experience shows that associations of subnational governments are essential to public administration reform processes. As intermediation bodies, they group information and

act as stable negotiating partners for the government, which helps reduce information asymmetries and high transaction costs. The organisation, representativeness and capacities of such bodies, and the quality of the relationships and trust between them and the government are key to the process of building a consensus and rallying potentially diverging interests to support common positions. Nevertheless, which associations or direct municipal representative will sit on the committee will depend on the regions and its particular characteristics; members should not be defined centrally and need to be sufficiently flexible to adapt to regional specificities.

Box 6.6. **Local government associations in Chile**

There are two national associations of municipalities: the *Asociación Chilena de Municipalidades* (ACHM) and the *Asociación de Municipalidades de Chile* (AMUCH). There are also a National Commission of Councillors (Comisión Nacional de Concejales - ACHM) and regional and local associations such as the *Asociación Municipalidades Región del Bío Bío*, etc. Associations of subnational civil servants are also involved in the debate on decentralisation such as the *Confederación Nacional de Funcionarios Municipales de Chile* (ASEMUCH) and the *Unión de Funcionarios Municipales de Chile* (UFEMUCH), or sectoral associations (e.g. National Confederation of Municipal Health Workers (CONFUSAM) and Chilean National Teachers Associations).

Association of Chilean Municipalities: established in 1993, the ACHM is national-level body bringing together 342 of Chile's 345 local authorities (membership is voluntary). The association's mission is to represent Chile's municipalities before public and private entities, whether regional, national or international, and to support its members both politically and technically in advancing democracy, decentralisation and the modernisation and improvement of municipal management. Among its objectives is to strengthen municipal capacity both among elected officials (mayors, municipal council members) and municipal civil servants who participate in a variety of seminars, training courses, workshops and fora. The association develops information products and training on legislative and regulatory updates. It also comprises technical commissions made up of mayors and municipal council members that explore specific areas in municipal management, such as housing, health, education, finance, staff management, and the environment. This expertise strengthens co-operation with the central level for pressing municipal concerns, in particular in the framework of the decentralisation process. The ACHM has been involved in several work groups and committees and has presented several proposals to further modernise the municipal system. The association also promotes the execution of joint development strategies among municipalities. In addition, there are regional chapters and associations of municipalities where regional municipalities have organised to work on specific topics relevant to their territories. Each region has a branch of the association, with its own technical commissions, replicating the national-level structure.

Association of municipalities of Chile: established recently in October 2013, the AMUCH's objective is to represent all Chilean municipalities, defend their interests and promote bottom-up policies. Its mission is "To be a democratic institution, representative and leader of all Chilean municipalities fulfilling a role of promotion of innovation and excellence, through education, training as well as technical and political support with the aim to deepen the decentralisation of the state". The Association also acts as an expertise centre and think tank. It has already published a number of studies, surveys and publications that cover different topics such as municipal health, public education, citizen security, child protection, e-commerce, staff management, electoral participation, migrations, transport and good municipal practices, among others. In 2017, the AMUCH comprises 61 municipality members.

Sources: OECD interviews; OECD (2013a), *OECD Urban Policy Reviews, Chile 2013*; Asociación Chilena de Municipalidades (2012a), "Capacitación 2012: seminarios, congresos y talleres"; Asociación Chilena de Municipalidades (2012b), "ACHM se reúne con secretaría ejecutiva de campamentos del MINVU".

Dialogue across different levels of government has been institutionalised in several OECD countries. Italy, for example, has three levels of "conferences" between the central and subnational governments (Box 6.7), serving as fora for intergovernmental co-ordination: 1) the Conference of State-Regions; 2) the Conference of State-Municipalities and other Local Authorities; and 3) the Unified Conference of State-Regions-Municipalities and Local Authorities, which includes all the members of the two other conferences. Nordic countries such as Norway or Sweden, have also taken advantage of these types of platforms through regular formal meetings between representatives from central and local government and in particular with associations of local governments which are consulted on any legislative changes impacting subnational government, and participate in the dialogue and negotiations with the central government. Portugal has also recently developed a permanent Council for Territorial Dialogue chaired by the prime minister to favour and institutionalise a continuous dialogue between the central government and subnational governments.

Box 6.7. **Co-ordination platforms in Italy**

The main institutional mechanisms to promote dialogue across the different levels of government in Italy are the so-called "conferences"; the 1) the Conference of State – Regions; 2) the Conference of State – Municipalities and other Local Authorities; and 3) the Unified Conference of State – Regions – Municipalities and Local Authorities. The three conferences are held in the prime minister's office and constitute the most important co-operation instrument to co-ordinate between the different levels of government:

The Conference of State-Regions was instituted in 1988 by Law No. 400. It gathers the prime minister (or the Minister of Regional Affairs) as president of the conference, the presidents of the regions and other ministers whenever matters related to areas of their competence are discussed. The central government consults the conference regarding all legislative initiatives related to areas of regional interest. Regional governments play a key role on this platform and in the process of institutional innovation, especially relating to the transfer of functions from the centre to the regions and local authorities.

The Conference of State-Municipalities and other local authorities, which was created by decree of the President of the Council of Ministers in July 1996, sits together the Prime Minister, as President of the Conference, the Minister of Interior, the Minister of Regional Affairs, the Minister of Treasury, the Minister of Finance, the Minister of Public Works, the Minister of Health, the President of the Association of Italian Municipalities (ANCI), the President of the Association of the Italian Provinces (UPI) and the President of the Association of Italian Mountain Communities (UNCEM), 14 mayors and 6 presidents of provinces. The conference carries out the following functions: 1) co-ordination of the relations between state and local authorities; and 2) study, information and discussion on issues pertaining to local authorities.

The Unified Conference of State-Regions-Municipalities and other local authorities, in place since 1997, is the institutional place for relations among the central government, regions and local authorities. It includes all the members of the two conferences (state-regions and state-regions-municipalities and other local authorities). It is to be consulted on any act in fields of shared competence. In particular, the Unified Conference is consulted by the central government on the financial law and on the decrees concerning the allocation of personnel and financial resources to regions and local authorities.

Source: OECD (2007), *OECD Reviews of Regulatory Reform: Italy 2007: Ensuring Regulatory Quality across Levels of Government*, http://dx.doi.org/10.1787/9789264037984-en.

Still, further strengthening the CORECIVYT might encounter some resistance. Setting multi-level dialogue platforms have indeed been a particularly difficult task for certain countries; sectoral ministries are not necessarily willing to collaborate with their peers, or national representatives can see dialogue with subnational governments as an impediment that slows down decisions – the latter can be especially challenging in a highly-centralised country like Chile. Multiple and diverging interests of local actors can also be counterproductive. This is the case in France where many attempts to settle multi-level dialogues have failed. In France, subnational governments are represented by multiple associations each defending the particular - and sometimes diverging - interests of their members (rural municipalities, small cities, mid-sized cities, large cities, urban communities, mountainous municipalities, departments, regions, inter-municipal communities, etc.). This has been an obstacle to reaching consensus and developing a meaningful reform process (OECD, 2017a).

Involvement of subnational actors should not be restricted to permanent platforms but also considered when ad hoc commissions are set up. Involving subnational governments and relevant stakeholders in a permanent or ad hoc dialogue is crucial to gaining legitimacy and improving policies' local impact. The Presidential Advisory Committee for Decentralisation and Regional Development (*Comisión Asesora Presidencial en Descentralización y Desarrollo Regional,* see also Chapter 1) is a good example and showed the willingness of the Chilean government to engage in dialogue with relevant stakeholders, even pushing the boundaries beyond the commission itself thanks to innovative participatory mechanisms (regional dialogues in each region, provincial and local seminars, hearings, web platform, etc.). It is crucial that efforts deployed in this commission continue to exist while implementing the recommendations (Box 6.8).

Some OECD countries have also followed this path. Denmark for example, through the Commission on Administrative Structure, appointed by the government in 2002, performed a critical review of the Danish governance system. The commission was established to provide a technical analysis for decision making, regarding changes in public sector tasks. Its tasks were to assess the "advantages and disadvantages of alternative models for the organisation of the public sector". The commission accomplished its work throughout 2003 and released recommendations in January 2004, proposing six different administrative models (see also Chapter 1).

Box 6.8. **Multi-stakeholder commission to discuss decentralisation reforms in Chile**

In April 2014, the President of the Republic set up a Presidential Advisory Commission on Decentralisation and Regional Development (*Comisión Asesora Presidencial en Descentralización y Desarollo Regional*). The commission, chaired by Esteban Valenzuela, had 33 members, representing the congress, regional and local governments (mayors, councillors, associations), labour federations and professional chambers, think tanks, citizens and civil society organisations, national ministries, intendants, SEREMI, etc.

The commission used a participatory methodology to involve citizens, business, regional and local governments, NGOs, corporations, universities, public officials, media, etc. Fifteen regional dialogues were organised and involved around 4 000 people. In several cases, they were preceded by provincial or territorial workshops, which then led to an agreement on proposals that were later submitted to the commission.

Box 6.8. **Multi-stakeholder commission to discuss decentralisation reforms in Chile** *(continued)*

During these months, representatives of the commission held hearings and meetings with various sectors interested in the subject. In addition, the commission received than 200 proposals for specific measures through a web platform.

The work of the commission was organised into five thematic groups:

1. Political decentralisation: seeking more autonomous power and greater legitimacy.
2. Administrative decentralisation: re-definition of competences across levels of government.
3. Economic fiscal decentralisation: pursuing more autonomous decision-making resources, and territorially better articulated.
4. Strengthening of local and regional capacities.
5. Citizen participation and democracy.

To promote, support the implementation and monitor the recommendations, the commission suggested setting up three specific bodies: an inter-ministerial council for decentralisation inside the government responsible for advising the president of the republic. The council would define the action plan for decentralisation and appropriate implementation instruments. It would also assume responsibility for co-ordinating the different ministries and services concerned; a regional unit in each regional government responsible for supporting transfer of competencies; a citizens' network in charge of leading the process, monitoring its progress and suggesting improvements.

Since the presentation of the report, several measures have been implemented and the decentralisation process has advanced considerably (see Chapter 1). However, according to the commission chairman, the current process has fallen short of the expectations presented in the report. The establishment of a dual model of power for the regions – including the regional governor and the presidential delegate – alongside a limited devolution process to the new self-governing regions stands in contrast to the more ambitious approach promoted by the commission (Valenzuela Van Trek, 2015). The three bodies mentioned, which would support the process, have not been created.

Source: *Comisión Asesora Presidencial en Descentralización y Desarrollo Regional* (2014), "Propuesta de Política de Estado y Agenda para la Descentralización y el Desarrollo Territorial de Chile - Hacia un país desarrollado y justo", https://prensa.presidencia.cl/lfi-content/otras/informes-comisiones/InformeDescentralizacion.pdf; Valenzuela Van Treek E. (2015), *El model dual-incremental de regionalización en Chile: intendentes electors y gobernadores delegados*, RIEM, N°11, año VI, ISSN 0719-1790, pp. 173-194.

Fostering dialogue with key stakeholders

In Chile the private sector plays a significant role at the national level, especially for investments. The concession system, for example, has contributed to a significant improvement in Chile's infrastructure and in access to basic public services, particularly for rural and remote areas (OECD, 2017b). Although investments – in particular infrastructure investments such as highways or ports - have a clear territorial impact yet subnational actors are absent from the decisions regarding these investments. Promotion, preparation, implementation, and supervision are driven by the central government with limited regional or local consultation. Chile should foster dialogue with private actors especially when investments will be made by the private sector. Integrating private actors

in the definition and execution of the agenda, also at the local level, is crucial to manage inter-dependencies and shared responsibilities. For example, the New South Wales government in Australia requires all public-private partnership project proposals to consider environmental and community issues, alongside financial and budgetary factors prior to receiving government support. This ensures that all appropriate stakeholders are involved, including the government, the private sector, and the community (Mizell and Allain-Dupré, 2013).

Yet, dialogue should not be limited to private actors for investment projects. Involving any relevant stakeholder, including citizens and universities, can improve the quality of planning efforts, the impact of policies and investments, ultimately benefiting the productive development of territories. Stakeholder involvement can help in the definition of a shared vision for development, improve assessment of investment and policy needs, reveal the importance of cross-border linkages, strengthen trust in government, and cultivate support for specific projects. For this to happen, a platform such as the CORECIVYT can also consider involving relevant stakeholders in the dialogue, either as permanent members, or depending on the issues to be discussed. This will help foster stakeholder engagement early in the policy process – from the design to its implementation. Capacities for effective stakeholder involvement include, but are not limited to: 1) identifying stakeholders, understanding their "stake" and their right to and capacity for engagement; 2) designing outreach to and consultation opportunities for stakeholder groups; 3) selecting the right technique to involve stakeholders; 4) developing a stakeholder communication strategy (e.g. accessible public reporting of investment plans, implementation progress, and results); and 5) managing grievances (Mizell and Allain-Dupré, 2013).

Enhancing the role of municipalities in co-financing instruments

Contractual agreements between different levels of government and sectors to align priorities and projects are co-ordination tools widely used by OECD countries. Contracts help to address multi-level challenges promoting dialogue and learning amongst the different actors involved. They are effective instruments in identifying common targets, setting clear and transparent objectives, sharing information and making credible engagements. While serving different objectives, contracts might help to ensure that national policies and regional and local priorities cohere and "synergetically" contribute to national development targets (OECD, 2010).

The modalities of contractual approaches to the governance of regional and local development vary widely within OECD countries. In some countries, they are based on non-binding protocols of intent, whereas in others they are based on legally binding instruments. In Chile, the Programming Contracts (*Convenios de programación* - CP) are formal binding agreements between one or more regional governments and one or more national ministries, specifying measures and procedures to be undertaken in projects of common interest over a specified period of time (Box 6.9). These agreements can also include other public or private national, regional or local institutions. While the different participants entering into a CP do not receive additional or complementary resources, but must re-allocate existing funds to invest in the project established in the CP, the Budget Directorate (*Dirección de Presupuestos*, DIPRES) has to approve the CPs before their implementation. These agreements offer a useful legal framework for co-ordinating regional and national priorities and responsibilities. So far, they have been mostly used for shared planning and financing of large infrastructure projects (OECD, 2017b).

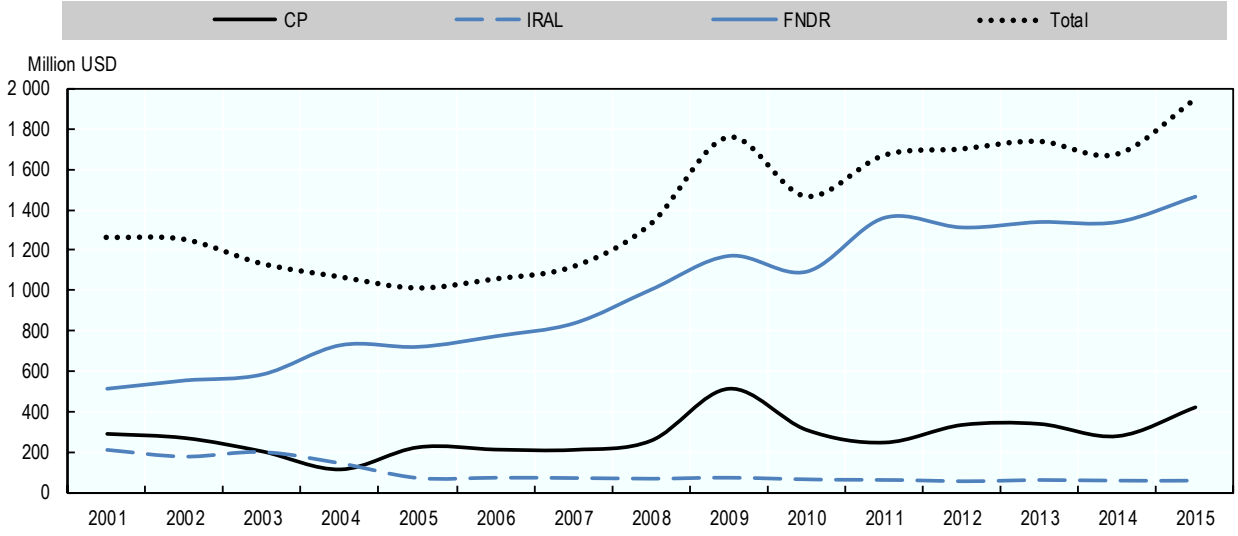
Box 6.9. **Formal steps regarding programming contracts (CPs) in Chile**

Formally, the steps for signing a CP are: 1) identification of projects; 2) signing of a protocol of purpose (*protocolo de acuerdo*) that initiates negotiations between the parties while defining the objectives and areas of intervention and the resources that each institution will contribute; 3) deciding on investments that will be included in the agreement that have a technical recommendation from the SNI); 4) drafting the programming contract and negotiation (technical); and 5) presentation of the agreement to the regional council for approval and signature. After the approval and execution of the agreement, a monitoring and evaluation stage follows during which a technical team with representatives from all parties involved is supposed to monitor its execution. Projects are carried out using the resources of both line ministries and regional governments (grants from the National Fund for Regional Development).

Source: OECD (2017b), *Infrastructure Governance Review: Chile – Gaps and Governance Standards of Public Infrastructure*, OECD Publishing, Paris.

Initially CPs were non-binding contracts, implying that the execution of CPs depended only on the goodwill of the parties. This eroded legitimacy as several CPs were signed but never implemented. To solve this, recent CPs were modified to include a clause establishing the obligation to comply with the contract. However, central government entities have still been reluctant to enter into CPs. Indeed, investments financed through these contracts have not increased in recent years; instead, they have remained relatively stable while other sources of financing regional investments, notably the FNDR, have been increasing (Figure 6.1). The two sectoral ministries that have historically been more prone to use them are the Ministry of Public Works (MOP) and the Ministry of Health (MINSAL).

Figure 6.1. **Regional Investments 2001-2015**



Source: Created by the OECD based on data from Ministry of Social Development (2015).

The role of municipalities in CPs has been very limited and more anecdotic than systematic. The vast majority of contracts have been signed between line ministries and

regional governments; in 2015, the MOP was the only ministry to contract CPs in four regions while the proportion of CPs contracted by MINSAL and MOP accounted for 50% each. As of 2013, only 5 contracts included a municipality (SUBDERE, 2013). This can be directly associated with insufficient municipal resources and capacities to enter into such agreements. Indeed, because CPs bring together not only actors, but also different sources of funds, central government actors that do use CPs, do so mostly to leverage regional resources for activities already in their sectoral plans (OECD, 2013a). As a result, the initiative for CPs often comes from line ministries, which use them to implement planned projects but with the added benefit of shared financing from regions.

Chile should further develop and support CPs as key instruments to boost co-ordination both across levels of government and across sectors and to promote multi-annual budgeting and planning, as recommended by the OECD's recommendation on effective public investment across sectors of government (see Chapter 2). For this, Chile should move towards "territorial contracts" promoting specific territorial goals and regional development priorities. Stronger CPs can also help the country to finance public investment in lagging regions. To further develop contracts, some of the key elements Chile should consider are:

- Specify territorial goals and regional development priorities that will be supported by the contract through a careful assessment of needs and opportunities.
- Rebalance the top-down approach that has been dominant in the current framework with a stronger, bottom-up component; the consultation phase for the establishment of contracts is crucial. The consultation initiates the dialogue across central and subnational governments. It aims at establishing priorities and actions, by assessing regional development needs and impacts on different categories of people. In this consultation, not only national and subnational governments should be involved but also the private sector and civil society. In France for example, a two-year phase consultation allows the central and the regional government to agree on the "Contrat État-Région".
- Encourage CPs across sectors at the national and subnational levels to ensure that the key players involved work together to implement the contract effectively, efficiently and coherently on the ground.
- Set incentives to involve municipalities in CPs. Municipalities should play a key role in the definition of projects to be financed by CPs as they will directly affect their territory. While strengthening consultation with municipalities, financing municipal CPs should be ensured. In parallel, Chile could set monetary incentives for national ministries and regions entering into CPs with municipalities with specific budget lines for this purpose.
- Encourage partnerships with municipal associations to support investments at a supra-municipal scale. This might help lagging regions that do not have by their own the capacity to enter into such contracts. Funding could be dedicated to contracts signed by associations.
- Incorporate in the initial contract monitoring mechanisms and an evaluation phase that assesses the results and potentially the impacts of contracts. Monitoring would help Chile improve management of current contracts. The evaluation phase aims to assess the impacts to ultimately learn from success and failures (Charbit and Romano, forthcoming) and facilitate peer learning. Monitoring and evaluation are crucial to make enforcement possible.

- Incentives could be set for the contract enforcement, for example to allocate part of the funding based on good performance (Box 6.10).

Box 6.10. **Enforcement mechanisms for more effective contracts across levels of government**

One of the main challenges for a contract to be effective is to guarantee the credibility of commitments and their verifiability, which means enforcement and evaluation are crucial. In some cases, it is difficult to measure the actual performance of contracts, especially when contracts are relational and criteria for the achievement of delegated tasks are more difficult to be clearly identified. As a consequence, strategic behaviour and the "opportunism" of one party might lead to administrative inefficiency, redundancy of infrastructure provision, and misalignment of development policies across levels of government. Transparency and integrity are crucial to avoid these risks.

Within the European Cohesion Policy 2014-2020, which provides a framework for financing a wide range of projects and investments, clearer and measurable targets for better accountability have been set. Progress towards achieving targets is to be monitored by referring to four categories of indicators: financial/ input, output, results/ outcome indicators and key implementation steps. The European Commission examines the annual implementation report and informs the Member State of its observations within two months of receiving the annual implementation report. The performance of each programme is also the subject of the annual review meeting for all programmes, convened every year from 2016 (three years after the end of the contracting period) until 2023 and attended by the representatives of the Commission and the Member State.

In achieving the targets, the respective programmes and priorities can benefit from an allocation from the performance reserve (6%), which aims to reward good performance in the implementation of programmes or sanction programmes when performance falls short of expectations. The Commission proposed that programmes and priorities that achieve milestones set for 2018 benefit from the performance reserve after a performance review is undertaken in 2019.

In Italy, under the 2007-2013 National Strategic Reference Framework (NSRF), in addition to 4% of the EU performance reserve which was adopted for the overall budget (EUR 3 billion), the Italian scheme set aside 6% of funds, making access to 10% of regional development policy funds conditional on performance. Not only regions from Mezzogiorno have been rewarded, but also municipalities. In fact, if a region missed a target, municipalities could still receive up to 50% of the resources assigned to an indicator, while the remaining would go to better-performing regional authorities. Various authors convey that such performance schemes are best accompanied by technical assistance to ensure the quality of data and information collection. The aims of the performance reserve were to promote institutional capacity building, co-ordinate financial resources and strengthen the role of monitoring and evaluation practices.

Source: OECD (2009), *OECD Territorial Reviews: Chile 2009*; OECD (2014), *OECD Rural Policy Reviews: Chile 2014*; Charbit and Romano (forthcoming), *Governing together: An international Review of Contracts Across Levels of Government for Regional Development*.

Contracts can benefit different regions and municipalities in Chile, even when initial conditions, and complexity, are different within subnational governments. In practice, contracts should be as flexible as possible so they can adapt to leading and lagging regions, urban and rural regions, and regions rich or poor in natural resources. The key point is to specify the regional development priorities supported by contracts, possibly through a careful assessment of needs and opportunities (Charbit and Romano, forthcoming).

The flexibility should also allow Chile to design contracts between regions and municipalities, following the example of France (Box 6.11), so they can better co-ordinate their priorities and concretely collaborate amongst themselves, independently from the central government. Once regions become more autonomous (i.e. when they have their own resources), contracts between regions and municipalities can be an effective tool to ensure priorities are aligned and to promote development in response to subnational priorities. This type of financing could benefit from more transparency and accountability than the current FNDR as the contract explicitly defines priorities and responsibilities of the parties involved.

Box 6.11. **State-region planning contracts in France**

State-region planning contracts (*Contrat de plan État-région* – CPER) have been in operation since 1982 and are important tools in regional policy in terms of planning, governance and co-ordination. They are characterised by their broad thematic coverage and cross-sectoral nature, with a territorial approach being applied across diverse policy fields including industrial, environmental, and rural issues. The DATAR functions as the main national partner of the regions in developing and implementing such planning documents. The President of the Regional Council and Prefect as the representative of the central government different ministries make the contract. The co-financing of interventions is seen as an important co-ordination mechanism.

2007-2013 planning contracts: a new generation of state-region contracts was introduced in 2007 alongside the 2007-13 Structural Funds programmes, in order to increase links between French and EU regional policies. The new contracts have the same timeframe as the EU operational programmes, are based on a joint territorial analysis, and have integrated systems for monitoring. Similar to the Structural Funds, regions can decide that funding be de-committed 18 months after approval for projects if no commitment has been made. Contracts increased their focus on the Lisbon and Gothenburg agendas. They reflect three priority areas: the promotion of territorial competitiveness and attractiveness, the environmental dimension of sustainable development, and social and territorial cohesion. The emphasis on sustainable development has grown, with a consultation process launched in 2007 (*Grenelle de l'environnement*). Priority is given to soft functions (e.g. education, research and development) as well as infrastructure other than roads.

2014-2020 planning contracts: A new generation of state-region planning contracts was launched covering 2014-2020. Five topics have been selected: Higher education, research and innovation; National coverage by very high speed broadband and development of digital technologies usages; innovation, promising niches and the factory of the future; multimodal mobility; the environmental and energy transition. Being a priority for the government, employment will be treated as a cross-cutting issue in the contracts.

In order to ensure equality between territories within the regions, contracts will mobilise specific resources for priority areas: urban priority neighborhoods, vulnerable areas undergoing major economic restructuring, areas facing a deficit of public services (rural areas), metropolitan areas and the Seine Valley. Inter-regional contracts for mountainous and river basins will be renewed. The preparation of this new generation took place in two phases: a first phase of strategic thinking and co-preparation between the central government and the regions; a second phase of financial negotiations.

Source: OECD (n.d.), *Effective Public Investment across Levels of Government Toolkit*, www.oecd.org/effective-public-investment-toolkit.

Supporting co-operation between municipalities

Encouraging inter-municipal co-operation

Many OECD countries have significantly enhanced inter-municipal co-operation to partially solve municipal fragmentation by taking advantage of economies of scale for investments and service provision. Most countries have recently enacted regulations to encourage this type of collaboration, which varies in the degree of co-operation, from the lightest (single or multi-purpose co-operative agreements) to the strongest form of integration - supra-municipal authorities with delegated functions and even taxation powers (OECD, 2017a). While associations can serve a variety of purposes, such as in France (Box 6.12), inter-municipal co-operation arrangements facilitate internalising externalities in the management of services and benefiting from economies of scale for utility services (e.g. water, waste, energy), transport infrastructure and telecommunications. They also allow municipalities and regions to invest at the relevant functional scale, reducing duplication of investments and taking advantage of spillovers and increasing efficiency through economies of scale. Inter-municipal co-operation thus can result in investments that would not be pursued if subnational governments were not collaborating, and in services provided more efficiently, as underlined by the first pillar of the OECD Recommendation on Effective Public Investment across Levels of Government, dedicated to co-ordination challenges and adopted by the Council in 2014 (OECD, 2014b).

Box 6.12. **Different forms of "sharing and pooling"**

France has different tools to promote services sharing and pooling among municipalities that ultimately depend on the objective sought. The ultimate stage of collaboration is inter-municipal co-operation (*intercommunalité*), that is to say, the creation of a "community" that includes municipalities so that local policies are not the responsibility of one individual municipality, but of a "community of municipalities". Public establishments for inter-municipal co-operation (*établissement public de coopération intercommunale,* EPCI) are the most integrated and complete type of this kind of community and have their own legal personality and own-source taxation regime.

However, there are some intermediary steps which can also be implemented in an inter-municipal framework whose benefits can be seen in the medium and long term by guaranteeing better public services:

- Conventional Service Sharing: This type of co-operation is established within an inter-municipal structure. In this form of collaboration, municipalities can partially devolve some competences to the "community" keeping for them part of the personnel responsible for the performance of services they have kept. In this case, either the community can make its services available to the municipality or the municipality keeps the responsibility for services and can make them available to the municipality.
- Creation of common services: Common services are normally linked to functional services, for example, the HR or legal departments. These services are steered by the community and their functioning structure is agreed by the municipality and the community. Depending on the mission and organisation chosen, officers may be placed under the authority of the mayor or the president of the community.

Box 6.12. **Different forms of "sharing and pooling"** *(continued)*

- Sharing assets: A community can acquire assets to be shared among its member municipalities (e.g. machines or performance halls). The use of these assets is spelled out in a regulation agreed between the community and its municipalities.
- Grouping public procurement: Joint public procurement improves securitisation (a specialised lawyer in charge of procurement can better respond than several people performing this task). This also allows substantial savings.

Source: Contribution from peer-reviewer of France, Marie-Christine Bernard-Gélabert.

Municipal associations in Chile

In Chile, municipal associations have been formally in place for several years, however, collaboration among municipalities has taken a long time to be integrated into local management. This can be partially explained by a weak collaboration culture linked with the fund allocations system in which municipalities are often called to compete against one another. The strong centralism has also discouraged collaboration as big projects that would need co-operation between local actors are mainly decided at the central level. Joint management for projects or service delivery is also hampered by differences in objectives, capacity and constraints, and precludes the efficiencies and synergies obtained through co-operation and economies of scale. In a very diverse and heterogeneous country like Chile, inter-municipal associations might be especially attractive as, while taking advantage of co-operation for specific issues, they allow municipalities to maintain their identity and to continue to provide services that either do not require a larger scale of production or do not affect neighbouring municipalities.

Chile has made considerable progress to foster inter-municipal co-ordination on a voluntary basis. The history of municipal associations dates back to 1993 with the creation of the Chilean Municipal Association (*Asociación Chilena de Municipalidades* - AChM) that grouped, at that time, 96% of Chilean municipalities and whose main objective was the political representation of municipalities to increase their bargaining power (SUBDERE, 2008).

Associations aiming at increasing the efficiency of local service provision and investments emerged in 2009. Since then, through Law No. 20.346, municipalities can come together to establish not-for-profit organisations for different purposes. Between 1993 and 2011, associations encountered a series of administrative and functional barriers to organise themselves as they were not recognised as legal entities (*personalidad jurídica)*, which restricted their autonomy. The Law No. 20.527 of 2011 regulates the existence of municipal associations, allowing them to become private not-for-profit corporations. Since then, associations can have their own capital, enter into financial commitments, compete for funding and receive grants or subsidies from the central government.

In addition to national associations and their regional bodies that represent municipalities politically at the national level, Chile also has two types of associations: 1) territorial associations that group neighbouring municipalities under a joint project and identity in terms of culture or economic activities (this type of association is based primarily on political willingness); and 2) thematic associations grouping municipalities to address a common and specific issue (tourism, mining activities, productive development) or solve common problems such as garbage management, purchase of

health material. Municipal associations have generally been geared towards representing the interests of a group of municipalities vis-à-vis public or private entities but in some cases they have intended to propose more efficient ways of managing programmes or investments (PUC, 2015). A good example of the latter is the Association of Municipalities of the Province of Llanquihue for the Sustainable Waste Management (*Asociación de Municipalidades Provincia de Llanquihue para el Manejo Sustentable de Residuos y Gestión Ambiental*). Since its creation in 2004, it has been an example of good internal management with efficient results (Box 6.13). As of 2016, 53 municipal associations were registered.

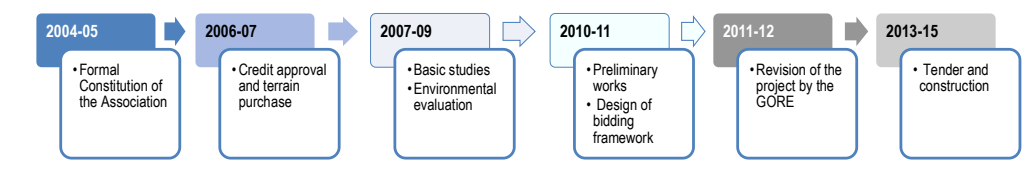
Box 6.13. **Association of Municipalities of the Province of Llanquihue for Sustainable Waste Management**

The Municipal Association of the Province of Llanquihue for Sustainable Waste and Environmental Management (*Asociación de Municipalidades de la Provincia de Llanquihue Para Manejo Sustentable de Residuos y Gestión Ambiental*) was constituted in 2004 by all the municipalities of the province of Llanquihue. Its objective was to address a common problem in the management of solid waste while optimising the use of resources.

For its functioning, the association has a directory that brings together the mayors of participating municipalities, an executive secretary and technical unit are in charge of the operation and administration, and a technical committee gathers professionals from all the participating municipalities and is responsible for the co-ordination and implementation of the agreements.

In the province of Llanquihue, municipalities managed waste management separately for over 35 years under very poor, and sometimes illegal, conditions. Municipalities did not have the appropriate resources or capacity to take care of waste management efficiently, from its collection to its final disposal. At the beginning of the 2000s, the mayors approached the intendant and started a series of actions to obtain resources to finance the joint project. Through the Agency of International Co-operation of Chile (AGCI), they were able to find German technical co-operation and develop studies and evaluations by international consultancies. Based on these efforts, in 2002, the mayors presented the Project for Sustainable Management of Household Waste (*Proyecto Manejo Sustentable de Residuos Domiciliarios* - PMSRD) to obtain financing, in the form of a loan, from KfW Bank, a German lender. However, in order to obtain credit from this bank they had to create a formal association. It took around six years from the drafting of the joint project proposal to the official creation of the association. It was not until 2006, after all the municipal councils had ratified the act of association, that the project was finalised – after various administrative processes (Fig 6.2) – in 2015 and inaugurated in March 2016. At present, and given the widespread acclaim and recognition the project has received (from the central, regional and municipal level), the association is now looking to expand its activities in the areas related to waste management. For instance, it is implementing a programme for recycling, a teaching programme to manage compost, seminars to share knowledge and promote the effective management of waste, eco-friendly networks, etc.

Figure 6.2. **Timeline of the Project**



Box 6.13. **Association of Municipalities of the Province of Llanquihue for Sustainable Waste Management** *(continued)*

Despite this success story, the association has encountered a series of setbacks. The first one, and probably the most important one, is the lack of resources allocated to the municipal association combined with scarce municipal resources for waste management (only 12% of the municipal budget is for the collection, transport and final disposal of waste). This is exacerbated by the fact that only 20% of households pay the *derechos de aseo* (80% are exempt). The lack of human and financial resources delays the execution and delivery of projects. At the same time, it makes the association extremely dependent on fees paid by participating municipalities – and thus on political will: if members do not pay, central transfers are its only lifeline.

As noted by the association, the key elements to their success are related to an initial consensus on the problem to be solved – and the political will from mayors in the province of Llanquihue to effectively solve the problem. Another key to success was transparency during the management process – transparency regarding municipal members but also citizens, civil society and the different public actors involved. The flexibility of members to reach agreement and the capability to build a lasting technical task force are also factors contributing to its success.

Source: Asociación Municipalidades Llanquihue (n.d), *Asociación de Municipalidades Provincia de Llanquihue Para Manejo Sustentable de Residuos y Gestión Ambiental* 920160, unpublished presentation, www.asociacionllanquihue.cl/index.php; OECD interview.

The most important challenge faced by municipal associations today is linked to their financing. Municipal associations are financed by member fees intended to cover operational costs. Associations can also access public funding through tendering processes but these remain very limited. SUBDERE has two very small funds exclusively dedicated to these purposes, the Programme to Strengthen Municipal Associations (*Programa de Fortalecimiento de Asociaciones de Municipios*, PFAM) and the Fund for Territorial Development (*Fondo de Capital Semilla para el Desarrollo Territorial*). These initiatives notwithstanding, financial incentives to encourage municipal associations are very limited.

For investment purposes, municipal associations have had a positive impact. With the data available in the Banco Integrado de Proyectos, the UC Public Policy Centre (Centro de Políticas Públicas - UC) has stated that associated municipalities have 46.6% more initiatives with a favourable recommendation (RS from the National System of Investments) when compared with municipalities that are not affiliated with a municipal association. At the same time, associated municipalities invest more using FNDR funds. The difference of approval rate is only significant for low-developed and small municipalities. Small municipalities seem to take greater advantage of associations when designing investment programmes. When it comes to quality of investment projects the study does not show significant differences when municipalities are associated. The quality of proposals has not been improved and as a consequence the execution of these projects remains limited (PUC, 2015).

Beyond encouraging investments that are better aligned with community needs, municipal associations seem to positively impact local capacities. In general, the UC Public Policy Centre concludes that associations help to develop capacities especially in less developed and small municipalities, which have a direct impact on the quantity of investments presented and approved by the SNI. At the same time, municipal associations have more bargaining power than municipalities on their own, and consequently, get more financing from the FNDR resulting from negotiations with the GORE.

Towards stronger municipal associations in Chile

Chile has made important efforts to strengthen municipal associations through the Department for Municipal Reinforcement (*Departamento de Fortalecimiento Municipal*) promoting these arrangements. However, projects or investments conducted by municipal associations remain limited so far, and the experiences vary greatly in the country. Several factors can help to understand why municipal associations are still at their early stages of development. First, the main driver for municipal associations so far has been political; municipal associations result from a common political willingness to tackle issues or projects that are not necessarily high on the agenda of priorities. Their strength often depends on personal links among local authorities, which are fragile and may evaporate with each election. The process is extremely dependent on the political willingness of mayors and councillors. The lack of financial incentives may have also explained to some extent why, overall, associations have not flourished as expected.

In contrast with many OECD countries, in Chile, municipal associations are private organisations. While this was the most efficient way to put in place associations when the law was discussed, it might entail some risks linked, in particular, to the sustainability of such organisations. As private organisations, they depend ultimately on the willingness of its parties to pay their membership dues; it also renders associations extremely dependent on competitive funds from the central government. Indeed, a key element restricting the correct functioning of associations is directly linked to funding as their budget from members' quotas only covers operational costs. This prevents associations, for example, from hiring professionals directly (PUC, 2015). This is unlike the case of France for example, where the EPICs are public organisations with their own budget (Box 6.14). Being a public figure ensures long-term certainty with regard to financing for the inter-municipal structure, which enables them to plan their projects and activities with greater long-term visibility. In the long run, Chile could consider the definition of a public status for associations in order to ensure their sustainability beyond political or personal will, at least for some critical services (such as waste collection and disposal) and for lagging areas.

Box 6.14. **Financing inter-municipal associations: the case of France**

France has more than 36 000 municipalities, which are the basic unit of local governance. Although many are too small to be efficient, France has long resisted mergers. Instead, the central government has encouraged municipal co-operation. There are about 2 145 inter-municipal structures with own-source tax revenues aimed at facilitating horizontal co-operation; almost all municipalities (99.8%) are involved in such structures.

In France, each inter-municipal group constitutes a "public establishment for inter-municipal co-operation" (EPCI or *établissement public de coopération intercommunnale*) with legal status under public law and own-source revenue. In this sense, they differ fundamentally from a citizen association, which is not a public institution and is governed by private law. This distinction is crucial as being public entities ensures long-term certainty with regard to financing for the inter-municipal structures.

Ultimately, this means that, independently of the specific legal form, funding – once it is determined – becomes a "compulsory expenditure". This means, in a very concrete way, that if one of the member municipalities refuses to provide its financial contribution, the prefect could mandate the expenditure in favour of the inter-municipal co-operation.

Box 6.14. **Financing inter-municipal associations: the case of France** *(continued)*

The EPCIs assume limited, specialised and exclusive powers transferred to them by member municipalities. They are governed by delegates of municipal councils and must be approved by the state to exist legally. To encourage municipalities to form an EPCI, the central government provides a basic grant plus an "inter-municipality grant" to preclude competition on tax rates among participating municipalities.

Financing varies depending on structure: 1) it can draw on budgetary contributions from member municipalities; and/or 2) funds can come from their own tax revenues.

The majority of EPCIs are financed through budgetary contributions and the ones that use this financing are mostly associated with the provision of network services such as water, sanitation, household waste. Municipal unions were largely responsible for bring electricity to the French countryside. The contribution depends on the structure of the EPCI, which also defines the financing needed.

The second financing alternative empowers EPCIs with genuine autonomy, as they can levy own taxes collectively instead of each municipality on its own. Communities with their own taxation have full control over their budget and do not depend on the municipality. All French municipalities are now obliged to belong to such a community with its own tax system.

Source: Contribution from peer-reviewer of France, Marie-Christine Bernard-Gélabert.

Making associations stronger on a voluntary basis also depends on defining the right incentives. Setting incentives for municipal associations, either financial or non-financial, is a key element to promote horizontal co-ordination. Some governments have opted to encourage collaboration by providing consulting and technical assistance, promoting information sharing or providing specific guidelines on how to manage such collaboration. Indeed, peer learning can be used by Chile as a tool that would allow the country, 1) to strengthen existing partnerships by sharing best practices; and 2) to encourage other municipalities to enter in such arrangements by showing that, through partnerships, municipalities can achieve more efficient and better results.

The Chilean government might also consider providing financial incentives to support horizontal associative schemes across municipalities, for example by defining specific budget lines, through FNDR or other funds, to finance exclusively municipal association projects or joint investments. Many OECD countries have recently passed regulations to encourage inter-municipal co-operation on a voluntary basis (Box 6.15). For instance, France offers special grants and a special tax regime in some cases and other countries like Estonia and Norway provide additional funds for joint public investments. Slovenia introduced a financial incentive in 2005 to encourage inter-municipal co-operation by reimbursing 50% of staff costs of joint management bodies – leading to a notable rise in the number of such entities. In Switzerland, one-third of funds for regional development policy are reserved for projects involving inter-cantonal co-operation (Mizell and Allain-Dupré, 2013). To complement such financing, or as an alternative, the government could also promote matching grant/co-financing projects between the national government and associations of subnational governments and their entities. Portugal with multi-level contracts or even Japan, where inter-municipal co-operation was not particularly encouraged (amalgamations being the preferred option to consolidate municipalities and increase their efficiency), are now developing a new type of contract encouraging inter-municipal co-operation (OECD, 2017a).

Given the substantial heterogeneity of the municipal landscape in Chile, the government could focus on encouraging the creation of associations between municipalities with different capacities. Big and stronger municipalities that benefit from greater capacities have indeed little incentive to collaborate with smaller municipalities. However, small municipalities can benefit greatly from such arrangements. The Centre of Public Policy of the Catholic University demonstrated that municipal associations indeed favour smaller municipalities, which benefit more from associations when it comes to analysing the number of projects with the approval (RS) of the National Investment System (*Sistema Nacional de Inversiones*, SNI). The same study showed that associations manage to reduce the turnover of specialists such as engineers or architects who play a key role in designing infrastructure projects. At the same time, associated municipalities enhance the capacity to influence the regional government by improving their ability to leverage resources for investments and take advantage of peer-learning. This is especially true for smaller municipalities. Thus, promoting associations among municipalities with different capacities can ultimately translate into greater productive development of lagging territories.

Finally, the provinces could also play a role in this area by supporting co-operation among municipalities within their jurisdiction to address common challenges and needs, in areas such as civil protection and management of natural hazards and emergency systems (floods, avalanches, forests and urban fires, earthquakes, tsunamis, volcanic eruptions, etc.), land registry management or local development (clusters).

Box 6.15. **Incentives for cross-jurisdictional co-operation**

Most of the time, inter-municipal co-operation is promoted on a voluntary basis. Incentives are created to enhance inter-municipal dialogue and networking, information sharing, and sometimes to help in the creation of these entities. These incentives can be financial or can also have a more practical nature (consulting and technical assistance, production of guidelines, measures promoting information sharing such as in Canada, United States, and Norway). Several countries also implemented new types of contracts and partnership agreements to encourage inter-municipal co-operation: Poland (with the introduction of territorial contracts), Portugal (with multi-level contracts introduced in the 75/2013 law), among others.

In Slovenia, inter-municipal co-operation has risen in recent years, in particular with projects that require a large number of users. In 2005, amendments to the Financing of Municipalities Act provided financial incentives for joint municipal administration by offering national co-financing arrangements: 50% of the joint management bodies' staff costs are reimbursed by the central government to the municipality during the next fiscal period. The result has been an increase in municipal participation in such entities from nine joint management bodies in 2005 to 42, exploding to 177 municipalities today. The most frequently performed tasks are inspection (waste management, roads, space, etc.), municipal warden service, physical planning and internal audit.

At the sub-regional level in Italy, there is a long tradition of horizontal co-operation among municipalities, which takes the form of *Unione di Comuni*, intermediary institutions grouping adjoining municipalities to reach critical mass, reduce expenditure and improve the provision of public services. A recent law from April 2014 established new financial incentives for municipal mergers and unions of municipalities. Functions to be carried out in co-operation include all the basic functions of municipalities. All municipalities up to 5 000 inhabitants are obliged to participate in the associated exercise of fundamental functions.

The region of Galicia in Spain has many small municipalities. Many have limited institutional capacity and are spread out geographically, which increases the cost of providing public services. The regional government has taken steps to encourage economies of scale.

Box 6.15. **Incentives for cross-jurisdictional co-operation** *(continued)*

First, it has improved the flexibility of and provided financial incentives for voluntary ("soft") inter-municipal co-ordination arrangements. Investment projects that involve several municipalities get priority for regional funds. "Soft" inter-municipal agreements tend to be popular in the water sector. Local co-operation is also being encouraged in the urban mobility plan for public transport, involving the seven largest cities in the region. The regional government also imposed a "hard" co-ordination arrangement. Specifically, it created the Metropolitan Area of Vigo, an association of 14 municipalities. Although the metropolitan area was defined by the regional government, it was based on a history of "light co-operation" among 12 municipalities (out of 14). Voluntary municipal mergers may be encouraged in the future.

Sources: OECD (2017a), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, OECD Multi-level Governance Studies, http://dx.doi.org/10.1787/9789264272866-en; OECD (n.d.), *Effective Public Investment across Levels of Government Toolkit*.

Governing metropolitan areas

The metropolitan governance gap in Chile

Co-ordination across municipalities is particularly relevant in metropolitan areas. Suitable governance arrangements in urban areas can indeed promote productivity; some evidence has shown that for a given population size, a metropolitan area with twice the number of municipalities is associated with around 6% lower productivity, an effect that is mitigated by almost half when a governance body at the metropolitan level exists (Ahrend et al., 2014). Metropolitan authorities have the potential to alleviate the cost of administrative fragmentation, making urban areas more productive. Enhancing the co-operation and co-ordination of the provision of public infrastructure and services on a metropolitan scale can also improve the quality of life and international competitiveness of large cities (OECD, 2015).

Chilean urban areas – in in the absence of a metropolitan body – might be underexploiting their productive potential, especially Santiago, Valparaíso and Concepción where the metropolitan area is comprised of many municipalities. This challenge will be more acute in the years to come as some forecasts are predicting significant expansion of metropolitan areas in Chile by 2020, including major growth in *I*quique-Alto Hospicio, La Serena-Coquimbo, Rancagua-Machalí, Temuco-Padre Las Casas, Puerto Montt-Puerto Varas (MINVU, 2014).

The metropolitan challenge is twofold: on the one hand, municipalities do not have the right incentives to co-operate, and on the other, differences in administrative and financial capacity accentuate inequalities within the metropolitan areas, including socio-spatial segregation. The metropolitan governance gap has been largely documented in Chile (OECD, 2013a):

- Approximately 40% of Chile's urban areas are a composite of more than one municipality. Managing such fragmentation requires a territorially appropriate framework and the capacity to help reconcile possible differences in development objectives, capacity and capability, and socio-economic disparities.

- The fragmentation of urban management responsibilities across various actors (often with their own policy approach) and the lack of a co-ordinating body leads to task overlap, and negatively impacts accountability and transparency.
- The sectoral approach taken by line ministries and SEREMI in designing and implementing urban programming is consistent with a hierarchical governance structure such as Chile's. However, it inhibits the development of an integrated, multi-stakeholder, "whole-of-city" approach based on shared urban objectives and priorities, characteristics more often associated with forms of network governance.

Fragmentation of urban issues begins in the central government where different ministries and bodies have responsibilities over urban development with the Ministries of Housing and Urbanism (Ministerio de Vivienda y Urbanismo - MINVU), Transport and Telecommunications (Ministerio de Transporte y Telecomunicaciones - MTT) and Public Works (Ministerio de Obras Publicas - MOP) playing a predominant role. These ministries do not have a tradition of working in a co-ordinated or collaborative fashion horizontally at the national level, which leads to overlap and duplication in centrally-generated subnational policy and programming (OECD, 2013b). Institutional fragmentation is also present at the subnational level as a direct corollary of central fragmentation, bringing with it responsibility overlap and confusion with respect to accountability, i.e. who is responsible for what, who is accountable, and to whom a citizen may complain about a given municipal problem (OECD, 2013a). The sector logic of the different ministries and institutions, combined with co-ordination deficiencies among them, and the lack of an urban governance framework at the "whole-of-city" level, makes it extremely complex to achieve territorial coherence and synergies between the different policies and actors involved within an urban area (OECD, 2013a).

A siloed management of urban issues has evident consequences on productivity; a clear example is the current institutional fragmentation in transport policy. In transport, the MOP is responsible for managing urban highways (*vías expresas*), major road accesses to the city and the infrastructure concession programme, which includes several urban road projects. Its responsibility also includes bridges, tunnels and airports. The MINVU (through its regional implementing arm, SERVIU) normally builds and repairs most of the urban road network (*vías troncales* and *vías colectoras*), except minor connecting roads (*vías de servicio* and *vías locales*), which are generally managed and maintained by municipalities (with occasional intervention by the MINVU). The MTT is in charge of transportation operations, including granting bus route concessions, street sign standards and vehicle circulation bans. Prior to the fund allocation, a project must pass the technical and economic analysis of the Ministry of Social Development. Municipal transit and urban directorates also intervene in the approval process, as do state-owned companies directly involved in transportation provision (OECD, 2017b).

Major progress in metropolitan governance in Chile

For several years, Chile has been aware of the need to design some form of metropolitan institution to enhance a more cohesive and harmonious development of metropolitan areas. Improved metropolitan governance in Santiago, which has for decades struggled with metropolitan problems such as public transport or pollution, would be of benefit for the entire country. The National Urban Policy of 2013 recognises the need to develop a metropolitan governance body in charge of metropolitan planning and specifically of transport systems and its administration, equipment and infrastructure,

waste management, water governance, among others. The re-organisation of competences and responsibilities for regional governments to manage metropolitan areas is part of the decentralisation bills currently being discussed in the Congress (see Chapter 1).

Chile has made substantial progress in the governance of its metropolitan areas. The recently approved the Law on Contributions to Public Space may be the first step towards improving the administration and management of urban spaces in Chile (Box 6.16). While this law neither changes governance mechanisms for urban spaces nor accentuates administrative or financial decentralisation, it does recognise the urban impact of infrastructure investments. The law requires that when new urban projects are executed, they contribute to the construction of parks, public spaces, and transport infrastructure needed to host urban growth.

Box 6.16. **Contributions to public space in Chile**

Law No. 20.958 recently launched (in 2016) a new System of Contributions to the Public Space. This law aims at promoting a more balanced development between real estate development, mobility and public spaces. For this, it defines two specific mechanisms:

- Direct Mitigation: Real estate projects (public and private) have to mitigate the urban impacts they generate in their direct environment through an expedited, transparent and objective system that replaces the former impact studies pertaining to the urban transport system (*Estudios de Impacto Sobre el Transporte Urbano*, EISTU).
- Contributions to Public Space: Alternative mechanisms for densification projects that can now fulfil the obligation to cede land for roads and green areas through contributions to public space. 70% of contributions are allocated to finance mobility investments and at least 40% of the contributions collected must be used for investment projects included in an inter-municipal plan, when one exists.

The four guiding principles of this law are:

1. Universality: all public and private real estate projects must mitigate and/or contribute.
2. Proportionality: the mitigations will be proportional to the externalities generated; they will not be responsible for past infrastructure deficits. The contributions will be adjusted to the density and destination of the project.
3. Predictability: the mitigations and contributions will be calculated according to objective methods and based on predefined and standardised procedures and deadlines.
4. Gradualness: the law will remain in effect for 18 months after being passed.

Pilot projects on metropolitan management by GORE also represent an important step forward. The project currently being discussed (see Chapter 1) is debating whether GORE should be able to administer one or more metropolitan areas directly in its jurisdiction; with this, the intendant and future regional governor become the head of the metropolitan area. The law calls for the creation of a Council of Mayors from municipalities that form the metropolitan area; this council would be an advisory body for the metropolitan regional government. The project also specifies the creation of a specialised unit within the GORE to manage the metropolitan area in the following areas: transport, housing, environment and public works, as well as waste management. While being discussed and in order to smooth the transition, SUBDERE together with regional governments and sectoral ministries are implementing pilot projects for metropolitan regional governments.

An "administrative act" provided GORE with some metropolitan competences in the regions of Bío Bío, Los Lagos, Coquimbo and the Metropolitan Region (Box 6.17). However, the project does not specify the transfer of specific resources that will be needed in order to take over these new responsibilities, which can entail an important risk for the effective administration of urban areas. A metropolitan authority should enjoy a degree of decision-making authority over resources to be successful (see below).

Box 6.17. **Bill on regional responsibilities: A new regional governance for metropolitan areas**

The bill on the transfer of competences introduces several provisions concerning the metropolitan areas, implementing partly the article 110 of the 2009 Constitutional regional law. Based on a definition of metropolitan areas (agglomeration over 250 000 inhabitants), the bill gives the regions the responsibility of managing metropolitan areas, becoming the "metropolitan regional government" (Subdere, 2016).

The competencies of the metropolitan regional government would include:

- Preparing a metropolitan urban transport master plan.
- Elaborating an inter-municipal investment plan of infrastructure (mobility and public space).
- Operating the collection, transport and treatment of solid waste (according to agreement with municipalities).
- Traffic regulation of urban roads defined as "inter-municipal", in co-ordination with the Regional Ministerial Secretariat of Transportation and Telecommunications.

The regions involved will establish a dedicated department (*Departamento de Áreas Metropolitanas*), which will be responsible for interacting and co-ordinating with the different central government administrations as well as co-ordinating the metropolitan urban transport master plan and the inter-municipal investment plan of infrastructure. The metropolitan regional government will be advised by a committee of mayors, representing the municipalities making up the metropolitan area. This committee will only have only a consultative role (*Consejo Consultivo de Alcaldes del Área Metropolitana*). The Departamento de Áreas Metropolitanas will act as the executive secretariat of the committee. The bill also calls for the creation of a Metropolitan Investment Fund.

Source: SUBDERE (2016), *Presentation Seminario Plan de acción estratégico del área metropolitana de Concepción, desafío de une gran ciudad*.

Box 6.18. **Metropolitan governance pilot programme in Concepción**

Concepción is a clear example of administrative fragmentation and overlap of multiple plans in force within the metropolitan area. The Metropolitan area of Concepción is made up of 11 municipalities: Tomé, Penco, Concepción, Talcahuano, Hualpen, Chiguayante, San Pedro de la Paz, Hualqui, Santa Juana, Coronel y Lota, all of them in the province of Concepción.

In addition to the PLADECO and PRC of municipalities in the metropolitan area, and a metropolitan and use plan dating from 2003, today Concepción has eight planning instruments that frame the development of the metropolitan area:

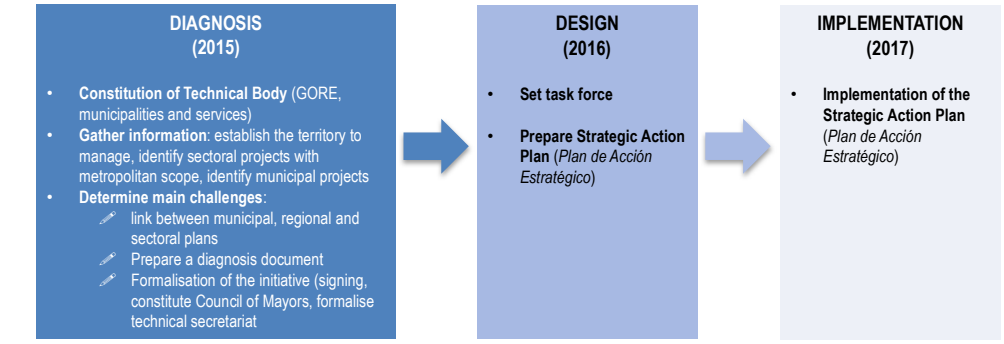
- Regional Development Strategy (GORE Bio Bio, 2015)

Box 6.18. **Metropolitan governance pilot programme in Concepción** *(continued)*

- Regional Land Use Plan (Plan Regional de Desarrollo Territorial, in preparation)
- Regulating Plan for regulating Metropolitan Concepción (MINVU, 2003)
- Urban Transport Plan of Gran Concepción Plan (SECTRA, 2012)
- Infrastructure and Public Equipment Plan (COMICIVYT, 2015)
- Regional Plan for Infrastructure and Management of the Water Resources of the Bío Bío Region until 2021 (MOP, 2014)
- Regional Plan for Solid Residential Waste 2014-2033 (AMRB, 2014)
- Decontamination Plan of Gran Concepción (MMA, 2016).

The pilot project is divided into three stages: 1) diagnosis; 2) design; and 3) implementation, as shown in Figure 6.3.

Figure 6.3. **Stages of pilot project on metropolitan areas in Concepción**



In Concepción, four sectoral ministries, through their regional representative, are part of the initiative (SEREMI MOP, SEREMI MINVU, SEREMI Medio Ambiente, SEREMI MTT). The main objectives of the specialised unit within the GORE that is responsible for managing the metropolitan area are to define the strategic action plan and institutionalise co-ordination among municipalities and public services.

By the end of 2016, the GORE of Concepción had set up eight meetings between municipalities, regional public services, and the GORE for each municipality to define its role, the "vision" of the PLADECO, and a set of main initiatives at the metropolitan level. In this context, the main challenges for the GORE of Bio Bio for 2017 are:

- Design a final strategic action plan.
- Consolidate the unit for metropolitan area within the organisation structure of the GORE.
- Set up the Council of Mayors.
- Manage and put in place a multi-year investment plan following the strategic action plan.

Source: GORE Bío Bío (n.d) (unpublished), "Áreas Metropolitanas, Región del BÍO BÍO", División de Planificación y Desarrollo.

Moving forward with the governance of metropolitan areas

It is not surprising that it is so difficult to make meaningful progress on metropolitan reforms in Chile. As in many OECD countries, political barriers have prevented the government from pushing forward the creation of a metropolitan body in Chile. Indeed, most metropolitan governance reforms in the OECD area have triggered or still cause intense political debates and controversies as they hinge on the specific national and municipal history, and cultural and socio-institutional frameworks. In Finland for example, metropolitan governance reforms for Helsinki and ten other urban areas have been planned for many years, but remain on paper. This slow progress results from a lack of political commitment, a lack of trust between municipalities which have "historically competed over residents, enterprises and jobs", and a lack of support from the resident population (OECD, 2017b). The confirmation of a head of the metropolitan area in Chile also implies a rebalance of power among public servants, sectoral ministries, and elected representatives, which also slows down the implementation of such reforms. However, a metropolitan body does not mean that the national government will fade into the background. Instead, the opportunity is created for the national level to focus on ensuring a more coherent approach to urbanism among central-level institutions – and in their relationship to subnational institutions – through establishing the laws and regulations required for urban governance and acting as a mediator (OECD, 2013a).

As was pointed-out by the OECD Urban Review of Chile in 2013, strengthening GORE by reconsidering their role in urban and metropolitan governance can provide the country with a mechanism to manage the impact of institutional fragmentation, poor alignment between resources and competences, and low capacity (administrative, financial, infrastructure) of functional urban areas comprised of a single municipality. In this sense, the project that aims to devolve metropolitan competences to the GOREs would be progress indeed. Yet, an urban governance framework that relies on the capacity of the GORE to manage urban areas and ensure service provision, as well as one based on municipal-level institutional arrangements, demands an increase in subnational level financial capacity, for example by creating the possibility to raise own revenue sources, or by increasing transfers from the central government (see Chapters 2 and 3 and OECD, 2013a). It also requires moving towards a place-based design and funding of projects and investments that support programme-based initiatives instead of project-based proposals. Still, this arrangement does not eliminate the need for relevant urban-level arrangements (in the form of supra-municipal or joint authorities) able to address administrative fragmentation.

The urban landscape in Chile is heterogeneous and a governance model should indeed take into account this heterogeneity. Challenges faced by Santiago, a large metropolitan area, can be different from those of Coquimbo-La Serena or from those of Puerto Montt or Antofagasta, which are single-municipality urban areas. This is why Chile should envision a flexible (and not a "one-size-fits-all") metropolitan governance model; Santiago could move towards a "hard" model with a supra-municipal body, while Antofagasta could develop a softer model implementing co-ordination bodies such as platforms, associations or strategic planning partnerships, or even sectoral or multi-sectoral agencies whose main functions could cover a particular problem or challenge for the metropolitan area (OECD, 2013a). For this multi-pronged solution to be successful, pilot projects (which Chile is currently implementing) are crucial. Drawing on practical experience in implementing this asymmetric approach will enable stakeholders to successfully roll out decentralisation in the near future. In turn, it can diminish the risks of accentuated disparities.

The governance model needs to be in tune with the structure of the functional urban area. While for certain urban areas empowering the GORE with metropolitan governance responsibilities might be an effective solution, for other urban areas the creation of a new and independent institution might be necessary. Such a supra-municipal arrangement where governance structures are re-shaped to fit or to approximate the functional economic area of the metropolitan region (municipal mergers or metropolitan government) can take different forms. Regardless of its form, the effectiveness of any metropolitan institution will depend heavily on its competence allocation and the structure of its financial and administrative resources provision. A key element is the degree of autonomy: it will have to manage either its own resources, a transfer from the central level, municipal contributions or a combination of all three (OECD, 2013a). Without decision-making authority over resources, any new authority for urban governance will encounter severe restrictions and its effectiveness will be limited.

Alternative metropolitan models have been implemented in different countries. Good examples of metropolitan governance reforms can be found in Colombia where some metropolitan areas, like Medellin or Bucaramanga, have more competences today or access to resources than in many OECD countries (Box 6.19). In Colombia Metropolitan Areas are governed by a Metropolitan Board (*Junta Metropolitana*) consisting of the mayors and a number of council of member municipalities as well as the governor of the department in which the metropolitan area is located. Metropolitan areas have access to various financing sources, including transfers from national, departmental and municipal budgets, betterment levies collected from metropolitan development projects, taxes (including an environmental surtax on property tax), user charges and fees related to public service provision, borrowing and a gasoline surtax. In contrast, Bogotá, which has not yet been organised into a metropolitan area, struggles with its public transport system (OECD, 2016a).

Box 6.19. **Examples of good practices of metropolitan co-operation: Medellin and Bucaramanga**

The Metropolitan area of Medellín (Valle de Aburrá) comprises 10 municipalities including the city centre of Medellín, accounting for 58% of the population of the department of Antioquia (almost 3.7 million inhabitants) and 67% of its GDP (Fitch Colombia, 2014). The metropolitan area of Valle de Aburrá was formed with the objective of promoting, planning and co-ordinating development and service delivery of its member municipalities. To date, the metropolitan area has defined an Integrated Metropolitan Development Plan that aligns municipal territorial plans (POTs), a transport plan and is active in environment and housing development. The MA acts as an environmental authority and has created a Metropolitan Environmental Council which takes care of water resources management, waste collection and management and emission control from industry and transport. It has created a transport authority, in charge of mass transit, in particular of the bus, rail, metro and metrocable systems in the Medellín area. The metropolitan area also promotes co-ordination across levels of governance to align development objectives. For example, a voluntary agreement has been signed between the Governor's office of Antioquia, the Metropolitan Area and the municipality of Medellín—a group called "Comisión TriPartita". Financial management of the Valle de Aburrá metropolitan area is considered as remarkably solid for a voluntary association (WB, 2012). The metropolitan area uses almost every possible source of financing in the framework of existing laws to generate revenue, in particular an environmental surtax of 2 per thousand on the property tax which provided 44% of total revenue in 2013. Contributions from the member municipalities amounted to 22% of total revenue, the major part coming from the city of Medellín representing 85% of all municipal contributions.

Box 6.19. **Examples of good practices of metropolitan co-operation: Medellin and Bucaramanga** *(continued)*

The metropolitan area of Bucaramanga, which is made up of four municipalities with a population of approximately 1.1 million i.e. half of the department of Santander, is also a widely-cited example of effective metropolitan co-ordination on social and economic development issues. Since the creation of the metropolitan area in 1981, quality of life and social indicators have shown marked improvement across member municipalities, with a notable decrease in poverty. There is a high degree of economic integration within the metropolitan area, led by a clear effort to consolidate a common market. However, this integration is not reflected in environmental and planning issues, which are not co-ordinated. This has negative repercussions for the entire area, in terms of pollution for example.

Source: OECD (2016), *Making the Most of Public Investment in Colombia: Working effectively across levels of government*.

The United Kingdom also has an interesting model where urban areas are governed through arrangements between the national and subnational governments by allowing a degree of "tailored" devolution of responsibility to English cities (Box 6.20).

Box 6.20. **The City Deals in the United Kingdom and Netherlands**

In the United Kingdom, City Deals are agreements between government and a city that give the city control to: take charge and responsibility of decisions that affect their area, do what they think is best to help businesses grow, create economic growth, and decide how public money should be spent. These deals allow a degree of "tailored" devolution of responsibility to English cities. City Deals require better horizontal (across departments) and vertical (between the centre and the cities) co-ordination and local capacity.

These agreements between national and local governments give cities control to: 1) take responsibility for decisions that affect their area; 2) design their own strategies to help businesses grow; 3) create economic growth; and 4) decide how public money should be spent. The City Deals are focused on institutional alignments and re-centering local governments as key agents of urban planning

In February 2016, Parliament enacted the Cities and Local Government Devolution Act 2016. The act was intended to provide a national legal framework to simplify the process of devolving more powers to local governments and providing support for the 2016-2017 round of City Deals proposed in 2015. The act grants greater powers to some cities and creates the framework for electing a citywide metro mayor.

The City Deals in the Netherlands are agreements signed between central and subnational authorities and stakeholders as part of the "Dutch Urban Agenda (*Agenda Stat*)". The first City Deal was signed on the development of a roadmap for the 'next economy', the second on climate adaptation and others will follow on sustainable energy, healthy cities and clean technology. The Climate Adaptation City Deal was signed in 2016 between the Ministry of Infrastructure and the Environment, three regional water authorities, five cities (The Hague, Dordrecht, Gouda, Rotterdam and Zwolle) and seven other partners (research centres and companies).

Box 6.20. **The City Deals in the United Kingdom and Netherlands** *(continued)*

The City Deals are examples of contracts where experimentation plays an important role, both for the complexity of the environmental policies and the innovative collaboration among different partners. These contracts can typically offer the opportunity to "learn by doing" on an experimental basis and help identify best practices, to be used for more formal/less experimental next steps, and build administrative capacity or for diffusion to other places once lessons have been learned and best practices identified.

Source: Charbit and Romano (forthcoming), "Governing together: An international Review of Contracts Across Levels of Government for Regional Development", *OECD Regional Development Working Paper*; OECD (2017c), *National Urban Policy in OECD Countries*, OECD Publishing, Paris.

While determining which governance model is more suitable for the different Chilean metropolitan areas, a bottom-up approach needs to be in place, especially for the creation of a new metropolitan governance institution. A supra-municipal entity in Chile for example, could enjoy functional legitimacy stemming from a top-down mandate and competence allocation. However, the new institution could face resistance in particular from the metropolitan area's stronger, wealthier municipalities, which are accustomed to working on their own or negotiating directly with the central government. A consultative bottom-up approach that includes actors at all levels of government, as well as from the private sector could defuse this resistance by building legitimacy at all levels of government (OECD, 2013a).

In the Chilean context, the financial and fiscal autonomy of a metropolitan institution is particularly challenging because in order to be successful metropolitan authorities must enjoy a degree of decision-making authority over resources and own revenues. There is, in fact, evidence that metropolitan institutional structures that can generate own-source revenue (and have control over their finances) tend to flourish, while those that are held in check by their funders face greater difficulties (OECD, 2013a). In general, when unitary countries undertake metropolitan reforms, the central government plays a key role in financing the new metropolitan body. If Chile wants to make real progress in the area of metropolitan area governance, the central government needs to provide municipal areas with the adequate funding to ensure responsibilities (including not only infrastructure but service provision, as well) have adequate funding.

Metropolitan governance tools should go together with incentives for urban municipalities to co-operate. To promote co-ordination across urban municipalities, Chile still has an important role to play in developing incentives to build metropolitan areas. For this, in a context of reforming the entire financing system of subnational governments (see Chapter 2), a new equalisation scheme should consider the metropolitan dimension, as metropolitan areas in Chile are typically marked by wide internal disparities in terms of revenue raising potential, expenditure needs and investment capacity. Equalisation mechanisms could be fostered within metropolitan areas to foster solidarity based on a new tax that could be linked to a metropolitan competence. Pending future initiatives, one way to promote co-ordination in urban areas while working within existing co-ordination tools would be to promote contractual arrangements targeting specifically metropolitan areas committed to improving their governance. Indeed, city contracts can help assign clear roles for the different institutions that participate in urban development/management across a given territory and could help in addressing fragmentation issues more effectively, such as in France (Box 6.21).

Box 6.21. **Contractual arrangements in urban areas in France**

The French City Contracts (*Contrats de ville*) are a tool to enhance collaboration between municipalities and the central government. France's City Policy dates back to 1977, when the first city contracts were established to respond to the need for affordable housing. Since 1994, its scope has been broadened to include other development priorities that aim to foster cross-sector collaboration on urban policy. City contracts run for a period of several years, usually seven, and serve as development programmes for distressed urban areas and encompass a city or larger urban communities. External stakeholders are involved in the process as well, including housing and transportation agencies, various civil society organisations and NGOs.

The 1994-2006 city contracts focused on a range of priorities, from housing rehabilitation to employment and transport. The 2006-2014 urban social cohesion contracts focused on neighbourhoods in difficulty.

In 2014, France updated its City Policy (*Politique de la Ville*), which establishes city contracts among the national government, inter-municipal bodies, and municipalities. The 2015-2020 city contracts act simultaneously on a wide range of levers, organised around three key goals:

1. Development of economic activities and employment - including ensuring the presence of an employment centre, youth employment assistance and support for local entrepreneurs.
2. Social cohesion - including support for investments in education, health, law enforcement, and social, cultural and sports activities.
3. Living conditions and urban renewal - including housing renewal and neighbourhood services and activities, and improving relationships between the police and the community.

The 2015-2020 city contracts are notable for the clear role they give to inhabitants of the target inter-municipalities and cities, who are represented by citizen councils. These councils allow for the exchange of information and for inhabitants to propose initiatives that respond to their needs.

Source: OECD (2013a), *OECD Urban Policy Reviews, Chile 2013*; OECD (2017c), *National Urban Policy in OECD Countries*, OECD Publishing, Paris.

Box 6.22. **Key recommendations for strengthening strategic co-ordination within and across levels of government**

1. Building a coherent multi-level institutional framework

- Manage institutional fragmentation at the national level:
  - Improve horizontal co-ordination at the central level to ensure that regional policies across sectors contribute to the pursuit of common development goals, limiting the scope of overlapped projects, promoting synergies between policies and investments, and ensuring that projects and local investments are mutually reinforcing.
  - Strengthen the role of SUBDERE to co-ordinate regional, urban and territorial policies.
  - Reinforce the institutional foundation of the COMICIVYT and its decision-making authority. A crucial first step would be to improve communication about its role and scope.
  - Take advantage of current decentralisation reforms to re-think and map the distribution of responsibilities centrally, but also across different levels of government.
- Manage institutional fragmentation at the subnational level:
  - Strengthen the role of the future elected regional governor as co-ordinator of regional policies. To fulfil his/her role as the elected head of the GORE, the direct election of the governor should be supplemented by the transfer of competences and resources.
  - Better define the role of the future regional presidential delegate. This new figure should be neutral – a state civil servant - in charge of co-ordinating state services. This will help to better define responsibilities and accountability.
  - Institutionalise co-ordination instances between the SEREMI, services and GORE to align coherently regional and municipal priorities and projects. An institutionalised platform for dialogue at the regional level should include municipal representatives.
  - Reinforce regions for more efficient and stronger municipalities: strengthen GORE (responsibilities and resources) for them to act as key interlocutors to co-ordinate policy priorities vertically with the central and municipal governments, and horizontally among municipalities within their jurisdiction, while preserving municipal autonomy.
    - Reinforce the planning divisions of the GOREs to better co-ordinate regional and municipal planning and budgeting processes.
    - Further develop the role of regions in providing technical, administrative and financial support to municipalities.
    - Encourage a pro-active role of GOREs in supporting critical projects that require municipal cross-jurisdictional co-operation in particular regarding weaker and rural municipalities. This could be done by encouraging municipal co-operation for investment projects financed through FNDR.

Box 6.22. **Key recommendations for strengthening strategic co-ordination within and across levels of government** *(continued)*

2. Reinforcing multi-level co-ordination and dialogue

- Ensure co-ordination through coherent planning instruments at regional and local levels:
  - Better articulate and streamline strategic and land use planning of regions and municipalities to foster dialogue among the different levels of government that effectively integrate local priorities.
  - Strengthen the ERDs as master plans that effectively guide and frame development strategies and investments at the regional and local levels and ensure that PLADECO follows the strategic objectives of the ERDs.
  - Improve planning coherence through a clearer definition of the interaction between regional-level strategic and planning instruments and their municipal level equivalents. This means improving the interaction and co-ordination between regional and municipal authorities, as well as between regional government and line ministries and their SEREMI.
  - Better align regional and municipal strategic development strategies (ERD, PLADECO) with regulating plans, especially by ensuring better coherence through the PROT.
  - Improve institutional and technical capacity for municipalities to use ERDs and PLADECOs in an integrated manner as strategic tools to define, implement and monitor inter-sectoral initiatives. For this, assistance can be provided by the central or regional governments, universities, private stakeholders, etc.
  - Better link planning and budgeting, moving away from project-based budgeting and towards programme-based budgeting that encourages cross-sectoral co-ordination and collaboration across different levels of government.
  - Strengthen ARI and PROPIR to effectively link budgets and plans in the medium and long run. For this, some elements of the planning instruments could be binding.
- Integrate subnational governments into co-ordination platforms and forums:
  - Develop permanent mechanisms that ensure the participation and consultation of subnational government associations at national and regional levels.
  - Institutionalise CORECIVYT as the main co-ordination fora for territorial issues with decision-making power.
  - Include municipalities or municipal representatives in the CORECIVYT permanently. Depending on the issues to be discussed, relevant municipal representatives should be invited to dialogue with permanent members of the CORECIVYT.
  - Ensure regions have the flexibility to define which local representatives will be part of the CORECIVYT; members should not be defined centrally and need to be sufficiently flexible to adapt to each region's unique characteristics.
- Foster dialogue with private key stakeholders, citizens and universities:
  - Foster dialogue between municipalities and private actors especially for investment projects that will be carried out by private actors.

Box 6.22. **Key recommendations for strengthening strategic co-ordination within and across levels of government** *(continued)*

- Integrate private actors in the definition and execution of the municipal agenda to manage inter-dependencies and shared responsibilities.
- Involve any relevant stakeholder, including citizens and universities during the planning, design and execution of projects and/or investments at the local level.
- Include, when appropriate, different stakeholders in the CORECIVYT, either as permanent members or on an ad hoc basis depending on the issues to be discussed.

- Enhance the role of municipalities in co-financing instruments:
  - Further develop and support the Programming Contracts (*Convenios de Programación*) as key instruments to boost co-ordination both across levels of government and across sectors by:
    - Specify territorial goals and regional development priorities that will be supported by contracts.
    - Reinforce the consultation phase with subnational governments, the private sector, and civil society.
    - Encourage the use of CPs across sectors.
    - Encourage the participation of municipalities in CPs through financial incentives; budget could be specifically allocated to CPs that include municipalities.
    - Encourage partnerships with municipal associations to support investments at a supra-municipal level; funding could be specifically dedicated to contracts signed by associations.
    - Incorporating, in the initial contract, monitoring mechanisms and an evaluation phase that allows stakeholders to assess the results and, potentially, the impacts of contracts.
    - Encourage contract enforcement, for example to allocate part of the funding based on good performance.
    - Ensure flexibility for contract agreements to allow, for example, contracts between regions and municipalities in a scenario where regions are reinforced with own revenues.

3. Supporting collaboration among municipalities

- Encourage inter-municipal co-operation:
  - Consider giving public status to municipal associations thus ensuring their financial stability and sustainability at least for some critical services and lagging areas, shielding them from fluctuating political or personal commitments while allowing them to plan over a longer time horizon.

Box 6.22. **Key recommendations for strengthening strategic co-ordination within and across levels of government** *(continued)*

- Develop incentives (financial or non-financial) for municipal associations, is a key element to promote horizontal co-ordination, especially between municipalities with different capacities. These incentives could be to:
  - Provide consulting and technical assistance, promote information sharing or provide specific guidelines on how to manage such collaboration.
  - Define specific budget lines, through FNDR or other funding, geared towards financing municipal association projects or joint investments exclusively.
  - Promote matching grant/co-financing projects between the national government and associations of subnational governments

- Improve the governance of metropolitan areas:
  - Pursue pilot projects that allow GOREs to manage metropolitan areas. For future developments this needs to be accompanied by transfers of specific resources to take over these new responsibilities (by raising own revenue or increasing transfers from the central government).
  - Develop a flexible (and not "one-size-fits-all") metropolitan governance model: supra-municipal entities, co-ordination bodies such as platforms, associations or strategic planning partnerships, sectoral or multi-sectoral agencies. Regardless of the final form, these entities need to have decision-making authority.
  - Ensure a consultative bottom-up approach that includes actors at all levels of government, as well as from the private sector to define which metropolitan governance body is right for which metropolitan area.
  - Provide the adequate funding in order to match responsibilities and respond to their financial needs in terms of infrastructure and services.
  - Foster equalisation mechanisms within metropolitan areas to foster solidarity based on a new tax that could be linked to a metropolitan competence.
  - Promote contractual arrangements specifically targeting metropolitan areas.

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