

The impact of partial decentralization on the Local Development. The case of Poland

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Does fiscal decentralisation make fiscal policy more „development-oriented”?

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Aims and motivation

- **Research questions:**
 - Does fiscal decentralisation change the shape of fiscal policy towards a more development-
 - Does fiscal decentralisation increase the share of public investment?
 - Does it influence fiscal deficit?

Aims and motivation

- Why study (fiscal) decentralisation?
 - Decentralisation at the theoretical level is often seen as a policy that promotes efficiency and development.
 - While the theoretical arguments are quite persuasive, the empirical evidence is inconclusive – see for example the meta-analysis by Baskaran & Schnellenbach (2016)
- Why study Poland?
 - Very large (over 2400 local territorial units) and rich database for the local Polish government
 - Polish territorial units have different revenue autonomy, making PL an interesting „laboratory”
 - Distinction between „de facto” & „de iure” measures of fiscal decentralisation

Benefits from decentralisation

- Decentralisation is often seen as a mechanism that introduces competition between local territorial units (Tiebout, 1956)
 - Decentralisation creates a „public goods market“, where people can choose the best offer (made by the local units)
 - Local units try to attract human and physical capital; hence they conduct „better“ policies
 - BUT: decentralisation may lead to inefficiently low taxation and inefficiently low supply of public goods (as local govts. try to attract mobile capital)

Benefits from decentralisation

- Decentralisation allows the government to „be closer” to citizens and to tailor policies to the diverse, local needs (Oates, 1972)
- Decentralisation curbs corruption and political rents
- Decentralisation promotes political innovation („political laboratory” at the local level, the voters compare and choose the best outcome)

Costs of decentralisation

- Decentralisation leads to inefficiencies –
 - Local policymakers may be less qualified than the policymakers at the central level
 - Scale economies
 - Soft budget constraints
 - „Partial” decentralisation can be related to soft budget constraints and common pool problems; resulting in inefficient policies
 - Decentralisation is not a 0-1 phenomenon; depending on the revenue structure (the share of „own” taxation relative to transfers from the centre); decentralisation can bring completely different results

Empirical research

- This work concentrates on the experience of more than 2400 Polish municipalities; over the years 2002-2014:
- Data from Ministry of Finance, Central Statistical Office & State Elections Committee
- Methodology: system GMM (lagged dependent variable and possible endogeneity)

Variables; municipality level

- Measures of decentralisation: share of own revenues in total revenues (most important: property taxes)
- Exact data on „own” revenues (i.e. revenues where the local units can control the tax rates and tax base)
- Distinction between „de facto” & „de iure” own revenues
- Control variables:
 - unemployment at the local level or PIT&CIT per capita
 - Population; share of young in the population
 - Time dummies
 - Elections
 - Political variables: political competition (based on Herfindahl index (0-1); higher value denotes stronger competition)

Share of investment spending

	(1)	(2) CITIES	(3)	(4) CITIES	(5)
L.y	0.389***	0.256	0.390***	0.267	0.388***
Decentralisation (de facto)	0.142***	0.132***			
Decentralisation (de iure)			0.111***	0.103***	0.111***
Pitcit_pc	1.45e-05***	3.78e-05***	2.11e-05***	3.73e-05***	2.12e-05***
Polit_compet	-0.0561***	-0.0736***	-0.0557***	-0.0771***	-0.0551***
Unempl	-0.00102***	-0.000798	-0.000963***	-0.000879	-0.000961***
Young	0.160***	0.153	0.140***	0.0905	0.133***
Elections	0.0201***	0.0197***	0.0205***	0.0200***	0.0205***
No. of obs	29,350	3,648	29,339	3,647	29,339
No. of municipalities	2,448	305	2,448	305	2,448
HANSEN STAT (p- values)	11,7 (0,3)	13 (0,2)	11,8 (0,3)	13 (0,2)	11,8 (0,3)

Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1

Budget deficit at the local level

VARIABLES		CITIES		CITIES
L.y	0.683*** (0.0689)	0.453*** (0.153)	0.673*** (0.0680)	0.454*** (0.154)
Decentralisation (de jure)	0.224***	0.208***		
Decentralisation (de facto)			0.277***	0.259***
PIT&CIT pc	7.66e-06**	4.32e-05***	1.87e-05***	4.30e-05***
Polit.comp	-0.0292***	-0.0477*	-0.0307***	-0.0387
Unempl	-0.000350**	0.000265	-0.000472***	0.000449
Young	0.219***	0.196*	0.251***	0.310***
No of obs.	29,339	3,647	29,350	3,648
No. of municipalities	2,448	305	2,448	305
Hansen	6,63	13,7	6,73	13,6

Conclusions

- The presented empirical estimations suggest that the degree of fiscal decentralisation has a significant impact on local public finances.
- Using a large sample of Polish municipalities and detailed data on local public finances over the years 2002-2014 and differentiating between de facto and de jure decentralisation, we have shown that:

Conclusions

- Higher degree of revenue autonomy (fiscal decentralisation) results in „better” fiscal outcomes – higher share of investment & lower budget deficits
- This result is robust to changes in sample coverage and de jure & de facto measures of fiscal decentralisation
- Political competition results in „worsen” outcomes – lower share of investments & higher budget deficits