The situation of decentralisation and fiscal relations between levels of government

Highlights from the third edition of the OECD-UCLG World Observatory on Subnational Government Finance

Isabelle Chatry
Head of Unit, Decentralisation, Subnational Finance and Infrastructure
Regional Development and Multi-Level Governance Division
OECD Centre for Entrepreneurship, SMEs, Regions and Cities (CFE)
SNG-WOFI: A multi-stakeholder initiative led jointly by the OECD and UCLG

1st Pilot Edition 2015-2016
With the support of AFD

2nd Edition 2017-2019
With the support of AFD, UNCDF

3rd Edition 2020-2022
With the support of AFD, UNCDF, ADB, CEB, Sida

The Steering Committee of the SNG-WOFI: putting multi-level governance in practice

2017 2018 2022
What does the SNG-WOFI offer?

Database
+ “Compare your country” visualisation tool

Country Profiles
Incl.
19 countries from Latin America and the Caribbean (LAC)

Synthesis Report

www.sng-wofi.org
COVID-19 has put additional pressure on subnational finances

Change between 2019-2020 in real terms (61 countries, unweighted average)

<table>
<thead>
<tr>
<th>Category</th>
<th>Change 2019-2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total revenue</td>
<td>-10.4%</td>
</tr>
<tr>
<td>Tax revenue</td>
<td>-5.0%</td>
</tr>
<tr>
<td>Grants and subsidies</td>
<td>10.4%</td>
</tr>
<tr>
<td>User charges and fees</td>
<td>0.6%</td>
</tr>
<tr>
<td>Total expenditure</td>
<td>2.6%</td>
</tr>
<tr>
<td>Total current expenditure average change</td>
<td>2.7%</td>
</tr>
<tr>
<td>Social benefits</td>
<td>4.0%</td>
</tr>
<tr>
<td>Subsidies and current transfers</td>
<td>24.0%</td>
</tr>
<tr>
<td>Direct investment</td>
<td>-0.4%</td>
</tr>
</tbody>
</table>

Source: OECD/UCLG SNG-WOFI (2022)
Decentralisation and multi-level governance reforms are underway in several LAC countries

- Sample of **19 countries** (14% of the WOFI country sample)
  - 11 « upper-middle income », 5 « lower-middle income », 3 « high income »
  - 15 unitary and 4 federal countries (Argentina, Brazil, Mexico, Venezuela)
- Latin American countries have **one or two levels** of subnational governments
  - Specific cases of Bolivia and Ecuador
- **Decentralisation** processes have been non-linear and at varied paces: a mixed institutional landscape
- **Regionalisation** processes e.g. Chile, Colombia (RAPs)
- **Asymmetric** decentralisation

### Subnational tiers of government by world regions (2020)

- Single-tier countries: Europe (38), Latin America (36), Middle East & West Asia (61), Africa (38), Asia Pacific (36)
- Two-tier countries: Europe (61), Latin America (36), Middle East & West Asia (61), Africa (38), Asia Pacific (36)
- Three-tier countries: Europe (38), Latin America (36), Middle East & West Asia (61), Africa (38), Asia Pacific (36)

Source: OECD/UCLG SNG-WOFI (2022)
Average municipal size in the LAC region

On average, municipalities are larger than those in Europe, but smaller than those in Africa or Asia and the Pacific.

However, average municipal sizes vary widely across LAC countries and within countries.

Inter-municipal cooperation is generally allowed but not very used in the LAC region, and it is progressing (e.g. in Guatemala, Honduras, Brazil, Bolivia).

Source: OECD/UCLG SNG-WOFI (2022)
Subnational government spending in Latin America is below the world average

Subnational government expenditure as % of GDP and as % of total public expenditure (2020)

- Subnational governments in Latin America account on average for 17.8% of total public spending and 6.3% of GDP:
  - Less than the global (21.5% of public spending and 8.3% of GDP), Asia-Pacific and Europe & North America averages
  - More than Africa and MEWA
- Variations across countries
  - Very low in Panama, Paraguay, Dominican Republic (< 1% of GDP and < 1% of total public)
  - Higher in federal countries (Brazil, Argentina, Mexico) and in some unitary countries such as Colombia, Peru and Bolivia
- However, the spending indicator can be misleading and overestimate the real degree of decentralisation.

Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted
Primary areas of subnational spending in the LAC region (9 countries) are general public services, economic affairs (transport), housing and community amenities and health.

The main difference with the global average is education, which accounts for much less in the LAC region.

**Regional average for the LAC region (9 countries)**
- General public service: 35%
- Defence: 7%
- Public order & safety: 8%
- Economic affairs: 10%
- Environmental protection: 16%
- Housing & community amenities: 7%
- Health: 3%
- Recreation, culture, religion: 10%
- Education: 1%
- Social protection: 7%

**World average (81 countries)**
- General public service: 23%
- Defence: 15%
- Public order & safety: 5%
- Economic affairs: 8%
- Environmental protection: 5%
- Housing & community amenities: 2%
- Health: 0%
- Recreation, culture, religion: 11%
- Education: 10%
- Social protection: 10%

Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted
Subnational governments in Latin America are a driving force of public investment, but there is scope for them to invest more.

### Subnational government investment as % of total public investment (2020)

<table>
<thead>
<tr>
<th>Region</th>
<th>Investment as % of Total Public Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asia Pacific</td>
<td>47.2%</td>
</tr>
<tr>
<td>Latin America</td>
<td>45.1%</td>
</tr>
<tr>
<td>Europe &amp; North America</td>
<td>42.3%</td>
</tr>
<tr>
<td>ALL (93)</td>
<td>39.5%</td>
</tr>
<tr>
<td>Euro-Asia</td>
<td>38.7%</td>
</tr>
<tr>
<td>Middle East &amp; West Asia</td>
<td>29.6%</td>
</tr>
<tr>
<td>Africa</td>
<td>24.0%</td>
</tr>
</tbody>
</table>

### Subnational government investment as % of GDP (2020)

<table>
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<th>Region</th>
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</thead>
<tbody>
<tr>
<td>Africa</td>
<td>0.7%</td>
</tr>
<tr>
<td>Middle East &amp; West Asia</td>
<td>0.9%</td>
</tr>
<tr>
<td>Latin America</td>
<td>1.1%</td>
</tr>
<tr>
<td>ALL (93)</td>
<td>1.5%</td>
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<tr>
<td>Africa</td>
<td>1.7%</td>
</tr>
<tr>
<td>Europe &amp; North America</td>
<td>2.4%</td>
</tr>
</tbody>
</table>

Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted

- Mobilising public investment at all levels of governments is crucial to face current and future crises:
  - e.g. COVID-19 recovery plans with a territorial dimension, such as Chile’s “Step by step, Chile Recovers” (*Paso a Paso, Chile se recupera*)
There is a need to diversify the basket of subnational revenue to provide subnational governments more autonomy and stability over their revenue.

Subnational government revenue by category (2020)

- **Intergovernmental transfers** represent over half of subnational revenue, although equalisation mechanisms are underdeveloped despite significant regional disparities.

- The share of **tax revenues** (shared and own-source tax) in subnational revenue is low, similar to the global average but there are strong disparities across countries.
  - Tax revenue account for >70% of SNG revenue in Argentina, against <5% in Peru.
  - **Tariffs (user charges) and fees** are slightly less developed than at the global level on average.
  - Importance of revenue from **land and natural resources** (Colombia, Peru, Argentina, Brazil).

Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted
Latin America’s subnational tax revenue is lower than the global average

- Subnational tax revenue as a share of GDP and total tax revenue is particularly low in the LAC region on average, compared to other regions and the global average
  - 2.3% of GDP and 12.4% of public tax revenue in the LAC region versus 3% and 14.5% at the global level

- Tax ratios must be considered with caution as they are not an indication of tax autonomy (shared taxation is prevalent in the region vs own-source tax revenues)
  - Need to devolve more own-source taxes (e.g. property tax)

Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted
The recurrent property tax represents a high share of subnational tax revenue in Latin America, but it accounts for a low share of GDP

- Despite its significant revenue potential, the recurrent property tax remains **underutilised** in most countries across the world
  - At global level, property taxes account for 34.1% of subnational tax revenue, but only 0.7% of GDP on average in 2020
  - In the LAC region, property taxation is the main source of tax revenue, albeit accounting for only 0.5%

- Significant variations across countries in the LAC region:
  - > 60% of subnational tax revenue in Guatemala, Peru
  - < 20% in Brazil, Venezuela, Nicaragua, Bolivia

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**Revenue from subnational property tax as % of GDP (2020)**

**Revenue from subnational property tax as % of subnational tax revenue (2020)**

*Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted*
Subnational government debt in Latin America is below the OECD and world average

- Subnational government debt in Latin America is below the world average, but it varies across countries:
  - > 10% of total public debt in Brazil, Mexico, Colombia
  - <1% of total public debt and/or GDP in Peru, Guatemala, Paraguay
- Over the last 15 years, fiscal and debt rules have been reinforced across the region to promote subnational fiscal responsibility, transparency and broader fiscal stability
- To boost investment, it is necessary to find the right balance between providing enough fiscal space to subnational governments to invest while continuing to manage associated risks via sound fiscal discipline.

Source: OECD/UCLG SNG-WOFI (2022) – All averages are unweighted
Thank you!

Visit our website: www.sng-wofi.org

Isabelle.CHATRY@oecd.org
@OECD_local
www.oecd.org/cfe