

INSTITUTIONAL DEVELOPMENT: ISSUES IN REFORM

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Policy Reform and Institutional Development.

During the last decade, economic policy reforms in many DCs concentrated on:

- (i) achieving macroeconomic stability;
- (ii) opening international trade;
- (iii) achieving domestic deregulation and liberalization;
- (iv) providing adequate regulatory and legal frameworks.

These policy reforms aim at providing the private sector with a favorable **enabling environment**:

- greater efficiency will be encouraged by a market-oriented system that enhances incentives under increased competition.

Enabling Environment for the Public Sector

- The enabling environment combines an incentive mechanism (free prices and trade to seek profits) with a control mechanism (competition).
- Lot of thinking has been devoted to develop this enabling environment for the private sector.
- But very little work has been done to develop an equivalent enabling environment for the public sector.
- In contrast with the few staff required for the design and enactment of policy reforms, the implementation and sustainability of economic policy reforms over time require strong Government management and administrative capacity.

Enabling Environment for the Public Sector

- This capacity, however, has eroded in many countries during the 1980's and 1990's .
- Due to Macroeconomic mismanagement and the subsequent need to correct fiscal imbalances, many countries have low government salaries at all levels, which in turn led to high staff turnover.
- As a result, many governments now lack an adequate number of skilled, managerially talented people in their ministries and agencies.
- In addition, the appropriate and desirable role of government institutions has changed significantly during the last decade, with the shift towards more market-oriented development strategies.

Market-Oriented Strategies

- These new strategies imply a re-orientation of many public agencies from a focus on rigid and detailed control to that of monitoring and support.

These changes suggest:

- the elimination of some institutions in the public sector;
 - the restructuring of others to operate in liberalized and more competitive environments.
- Given the inadequacy of current government institutions in many developing countries, there is the risk that their economic policy reforms will be undermined over time.
 - Institutional development is a key element to consolidate and ensure the sound implementation and sustainability of policy reforms over time.

Defining Institutional Development Work

- What should be the span of Institutional Development work? How do we define it?
- In practice, the term institutional development has used by different people in different contexts:
 - At one extreme, a narrow definition equates institutional development with the process of strengthening individual government organizations or entities.
 - At the other extreme, a broader view defines institutional development to include improvements in both public and private organizations as well as in the rules, regulations, practices, values, and customs that shape and influence an entire society.

Multilateral Agencies and ID

- Multilateral Agencies have traditionally pursued ID in the narrow sense in virtually every project.
- While this practice was necessary it has also proven insufficient to achieve sustainable results.
- Typically, attempts to strengthen institutions in a given sector in connection with a project fail,
 - either because of factors such as poor civil service pay scales that go beyond the particular sector.
 - or they fail when the ad hoc arrangements created to assure implementation of the project expire.

...Multilateral Agencies and ID

- When a strong government institution is created, it is often at the expense of other weaker ones.
- For example, creating a strong "Project Unit" to overcome the inefficiency or corruption of line and regulatory agencies may enable it to get its job done.
- But it will also get in the way of attempts to strengthen the regular line and regulatory agencies.
- A more sustainable work on "Institutional Development" would be one which includes not only the process of strengthening individual government organizations but also the more systemic efforts to create an improved institutional environment for the public sector.
- Ultimately, institutional development goal should be to improve the way a government works.

Scope of Work in Institutional Development

More specifically, ID should try to achieve a government that is:

- leaner in terms of the number of staff,
- better equipped in terms of the motivation, quality and productivity of staff,
- with a role concentrated only on those activities that warrant government involvement, and
- more effective and efficient in delivering essential services and carrying out the basic functions of government.

ID should improve the Government's ability to operate on a day-to-day basis, to innovate, to address changing conditions, and to deal with unexpected outcomes without external assistance.

Elements of ID

To achieve its objectives, work on ID includes three elements:

- (i) the enabling institutional environment for the public sector;
- (ii) organizational and management strengthening;
- (iii) dealing with corruption.

(1) The Enabling Institutional Environment

- The goal of an **enabling institutional environment** is to create “automatic” (e.g., unsupervised”) *incentives* and *controls* that would influence positively the behavior of individual government organizations.
- The principal actions on the Enabling Institutional Environment agenda are as follows.

Incentives and ID

(a) Improving Incentive Systems.

- One of the major goals is to restore incentives for proper performance.
- An adequate incentive system is required to attract talented people to key posts, to retain them and to encourage their behavior towards efficiency in optimizing institutional objectives.
- International experience shows that the incentive system will require an un-biased and professional processes for staff **recruitment, selection, and promotions**. This process should be delegated to a Civil Service Board and should be isolated from political pressures (such as party “quotas”).
- A second key of the incentive system is adequate compensation “linked” to measurable and quantifiable performance.

...Incentives

- Salaries should be set at satisfactory levels, in many cases comparable to compensation in the private sector, initially at least for key personnel.
- This would help to reduce undue compression of the ratio between top and bottom grade salaries in most governments.
- The merits of a Senior Executive Corps, modeled after the US Government's SES, should be considered as a short term solution; under this approach in return for higher salaries, job security is given up.
- To motivate performance, a key measure is to link a substantial part of the compensation (about 20%-30% for most staff) to the achievement of measurable objectives.
- This will require defining, measuring, and monitoring **performance indicators**.

...Incentives

- Non-monetary incentives should also be enhanced:
 - the perceived stature and professionalism of Government employment should be strengthened by involving employees in setting objectives and work programs, and
 - by providing them with sufficient autonomy and accountability to produce the expected outcomes.
 - Greater autonomy should be accompanied by increased flexibility to the managers of the agencies in doing their job (for example, by permitting them to contract out services to achieve greater cost-effectiveness).

Control Mechanisms

(b) **Improving Control Mechanisms.**

- First, the control mechanism involves a set of laws and regulations to affect the “**competitive**” environment for public agencies, their behavior, and the way of conducting business.
- Greater competition can be achieved, for example,
 - By permitting open enrollment in schools or health clinics;
 - By using "coupons" for mandatory government services or public schools
 - or by establishing more than one Government agency providing a service in competition among them, with their evaluation based on performance indicators.

...Control Mechanisms

- Second, the control mechanism should include measures to improve information for accountability.
 - Public institutions normally are not subject to the test of the marketplace to evaluate performance and ensure accountability.
 - In the absence of a market test, transparency and openness of information and public processes are the best ways to ensure accountability for performance.
 - In fact, they act as market surrogates.
 - Therefore, open and transparent processes should be developed to define agency performance (with clear performance indicators), outputs and costs, and to measure, monitor and publish them widely.

....Control Mechanisms

- Agency management would be held accountable through "open files" involving the publication & monitoring of such information.
- Lack of performance should be meaningfully penalized, including dismissal of those responsible.
- Use of other competition surrogates -- particularly "voice" (the active participation of clients, users and beneficiaries in agency's activities) and market contestability should be encouraged.
- Emphasis should also be given to enhanced accounting and auditing processes in the public sector through changes in laws and procedures.
- Information disclosure should also aim at building popular support -- among businesses, unions, students, the press, the civil service -- for policy reform and for the role of the Government.

Organization and Management

(2) Organizational and Management Strengthening

- The aim of this second component of ID is to strengthen the management and operations of public sector agencies and public enterprises.
- Organizational strengthening involves:
 - (a) improving the overall government structure;
 - (b) improving the management and operations of government agencies; and
 - (c) improving the management and operations of public enterprises.

(A) Improving the Structure of Government

- Experience has shown that removing redundancies through leaner governments enhances public sector performance.
- This involves rationalizing the *role and size* of the public sector to reorient its role towards "public goods". This rationalization would involve:
 - Privatization.
 - Sub-contracting of activities to the private sector.
 - Decentralization of agencies and responsibilities to local governments, which are closer to the beneficiaries. When the services are managed closest to the users, they will be more inclined to pay for the services. This is the case for most basic services, such as water, sanitation, education, health, etc.
 - Closure or merger of agencies to eliminate overlapping functions as well as measures to improve coordination among them.

Government Structure

- Rationalization would also involve "downsizing".
- The reduction of over-sized government agencies by separating excessive staff is a politically difficult but necessary step.
- Downsizing progress in some countries has been achieved by carrying out a civil service census and functional reviews -- matching tasks and objectives with staff necessary to meet them.
- These actions are intended to eliminate "ghost" employees and vacant positions, freeze recruitment, retrench temporary workers, establish automatic and voluntary retirement programs for some staff, and finally by straight-forward dismissal.
- These staff reduction measures tend to be costly: a Bank study showed that severance packages are the single most important factor in implementing staff reduction programs.
- However, if properly done, over the long term they should yield considerable benefits from a cost and efficiency standpoint.

Steps to Reform Public Administration

- In many EMs, a bottleneck for the implementation of economic reforms is the inadequacies in the implementation capacity in many government agencies.
- **Public Administration Reform** has a pivotal role in ensuring that government agencies will be able to support this transformation. Central government is burdened with overlapping functions and responsibilities, cumbersome decision making, and lack of transparency.
- Many countries around the world have managed to implement successfully programs to improve public administration. The main steps as follows:
 - (1) **The role of the government in the economy should be clearly re-defined** as one of supporting private sector productive activities, rather than being in competition with the private sector. Whenever an economic activity could be carried by the private sector, it should be clear that the government should not engage in it.

- (2) A Public Administration Task Force should be created** in the Office of the Prime Minister to initiate and control the reform public institutions. This Task Force will develop a “concept” for the reform of public administration, including the proper role of the government in a market economy. The Task Force will also ensure that there is broad political support for the reforms. The outcome would be a reform program widely accepted by stakeholders.
- (3) The reform program should start with a “horizontal functional review”** under which the functions of all government agencies are reviewed centrally in order to eliminate overlapping and duplicative functions and improve decision making across institutions. The principle should that there should be only one agency responsible and fully accountable for a given government function. Government by “committees” do not work well in any country.

- (4) **The next step should be to carry out “vertical functional review” within each public institution** to ensure that their functions are consistent with the redefined role of the government and identify which roles could be eliminated, transferred to lower levels of government, outsourced, or privatized. Each function should be screened by the following questions: (i) does the program/service serve a public interest?, (ii) is there a legitimate and necessary role for the government in this program/service? (iii) is the lead responsibility for this program/service assigned to the right government jurisdiction or level? (iv) could, or should, this program/service be provided in whole or in part by the private sector? (v) if the program/service continues within the existing government context, how could its efficiency and effectiveness be improved? (vi) is the program or service affordable within the existing fiscal realities?
- (5) Once the proper roles of each agency have been defined, **carry out an “operational review”** to improve the efficiency of the agencies, including the adequacy of regulations, government procurement, and operating practices and procedures.

- (6) **Based on the new functions and structures, the reform program will carry out a review of the Civil Service** to ensure that government employees are properly recruited, trained, compensated or separated.
- (7) The reform program should also include the development and implementation of a practical and user-friendly **e-government initiative** to improve accountability, responsiveness and efficiency of the public sector.
- (8) The reform should be extended to local governments. The aim should be to accelerate **decentralization reform** with an aim to build an independent and viable local self-governance. The reform program should included agreement on all necessary amendments to the Tax and Budget Codes that strengthen fiscal autonomy of the local governments. Finally, tariffs for public services, provided by local governments, must be set on a competitive and transparent basis. Essentially, full-cost recovery of these services will ensure long-term feasibility of infrastructure and utilities.
- (9) The reform program should also streamline **state property management and privatization procedures** by improving transparency and competitiveness of the public sector. Perform mandatory, regular and independent audits of all commercial activities executed by the state.

(B) Improving Management and Operation of Government Agencies

Within individual agencies, the main ID task is to strengthen them so that they can effectively and efficiently achieve organizational outcomes.

Work with individual agencies would include:

- (a) An open, transparent, and specific definition of institutional role, goals, objectives and methods.
- This will require establishing expectations and procedures for public agencies to openly and transparently define in a precise manner their institutional role, objectives, delivery mechanisms, methods and work programs.
- In many cases, specific undertakings such as "Contract Plans", "Performance Agreements", or "Consumer Bill of Rights" will be important to establishing and limiting agency objectives.

Government Agencies

- (b) Based on the overall incentive framework for the public sector, improve the quality of management and staffing of individual agencies:
- implement appropriate salaries and incentives to change behavior towards efficiency, with clear transparency, accountability and performance criteria;
 - define staff recruitment and selection criteria and procedures;
 - develop schemes to minimize staff turnover.
- (c) To provide Government agencies with sufficient managerial responsibility and autonomy, many of them should be incorporated under laws that permit them to operate without political interference's.

Government Agencies

- This will be key to provide staff with a solid administrative career, since it will allow for specification of recruitment, training, separation policies, etc.
- (d) Improving Training. In addition to incentives, agencies will require new skills before results are achieved.
- In addition to new staff, training of existing personnel can be crucial to improve the quality of civil service personnel.
 - Agencies need to identify skill gaps, provide training opportunities comparable to the private sector, and evaluate the results.

Training

- Training should be results-oriented and targeted to improve individual skill deficiencies and better match an agency's employee skills to emerging technologies.
- (e) Improve information for internal management, including the quality of planning, operational and monitoring systems, information and decision-support systems and other management support processes.
- (f) Since in most developing countries, fiscal budgets will remain constrained for the foreseeable future, a key to the financial health of many government agencies will be their ability to generate its own sources of revenues.
 - Governments should consider providing some of its agencies with the capability to raise its own resources, through user fees, tolls, tariffs, etc.
 - This has been the case in the most successful public utilities; but it could also be applied to other government services such as roads, education, health, etc, provided that the impact on the poor is not neglected.

(C) Improving Management and Operations of Public Enterprises.

- Public enterprises that cannot be privatized in the near or medium term will require ID work different from that applied to government agencies. This type of ID work includes:
 - (a) **Development of a competitive or transparently regulated environment.**
- The steps to be taken here are largely in the area of policy reform (e.g., price liberalization, transparency of regulation, labor and other factor market liberalization, freedom of entry and exit).
- But they need to be complemented by ID activities such as converting public enterprises to independent, limited-liability companies.

(b) **Management Autonomy and Accountability.**

- This will mean shifting Government oversight of public enterprises from ex-ante control to ex-post assessment of performance based on previously agreed criteria.
- The complementary roles of the Government, the board of directors and management will have to be defined along their respective responsibilities as shareholders, policy-makers and operators.
- Performance agreements should be established with substantial incentives linked to results.
- Management information systems should be upgraded to permit assessment of performance.

(c) **Financial Autonomy and Accountability**

To ensure financial accountability, state enterprises must be subjected to "hard budgets".

- Fiscal subsidies must be eliminated.
- With improved financial planning, state enterprises should be allowed to raise resources on a commercial basis, without government guarantees.
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(3) Dealing with Corruption

In many countries, corruption is at the root of Government inefficiency.

- An Anti-corruption Program should be based on three elements: (a) prevention; (b) enforcement; and (c) public awareness

A. PREVENTION.

- The focus of prevention is: (i) to reduce opportunities for corruption, and (ii) to make corruption more difficult to undertake by improving transparency and accountability.

Corruption Prevention

Prevention would involve:

- Privatization of Government enterprises and services to minimize corruption opportunities.
- De-regulation, to reduce number of licenses and registrations that require individual intervention of officials.
- Eliminate Government discretionality, by eliminating “exemptions” to laws and regulations and making laws more precise.
- Streamline tax collections and audits.
- Introduce competitive procedures for public procurement.
- Reduce the size of the Government and re-focus its role to minimize opportunities for improper interventions and corruption.
- Decentralize Government functions to bring decisions closer to the public and improve accountability
- Reform the Civil Service to make it more professional, including (i) increasing salaries of key government officials; (ii) rotate frequently public servants in “vulnerable” positions; (iii) mandate public servants to declare their income/assets.

Corruption Enforcement

- **B. ENFORCEMENT**
- Develop the legal framework to ensure discipline and strong prosecution. This would involve:
 - Development of adequate avenues for “appeals” of Government decisions, including a system for review of tax decisions.
 - Develop effective channels for complains of Government actions.
 - Develop a strong “watchdog” agency (Audit).
 - Ensure that the laws will clearly define penalties for corruption.
 - Improve the court system (Judiciary) to expedite the processing and resolution of cases.
- Strengthen Enforcement agencies, such as FBI equivalents.

Corruption and Public Awareness

- **C. PUBLIC AWARENESS**
- Make people aware of their rights and the rules of the game.
For this:
- Improve Government Information Systems at all levels to keep the Government and the public informed of payments, expenditures, subsidies, etc.
- Publish widely Government rules, such as Tax Bulletins, customs regulations, quality certifications, etc.
- Enlist the support of the Press and NGOs in dealing with corruption.
- Use surveys of opinions to disseminate widely concerns on corruption.

ID Priorities

- **ID Priority Focus**
- Institutional development concerns the reform of the Government and therefore has many political implications.
- Therefore, ID work can only be successful if there is strong Government commitment from the highest levels of Government.
- Securing this commitment should be the first step to get successfully involved in a more comprehensive approach to ID.
- Local country conditions will determine the best approach, sequencing and priorities to achieve institutional development.

Therefore, it seems that the first step in many countries should be to carry out a broad analysis of institutional issues and weaknesses.

The work would include:

- (a) identification of the main constraints to institutional development, including generic institutional weaknesses, major bottlenecks, the quality of institutional resources, etc.
- (b) prioritization of issues to be addressed, with emphasis given to systemic issues that command broad-based support in the country.
- (c) determining where action should be focused and agreeing on a Plan of Action for ID. In the plan of action, innovative approaches should be encouraged. It should also include the development of tracer and monitoring schemes to facilitate learning from the reform experience.



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