



Toward a federal constitution in Nepal: What is the future role and structure of local governments?

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Will Nepal's ongoing restructuring of the government improve the performance of the public sector? The signs are not positive. The process of restructuring is driven by ideological and perceived political opportunity, rather than by an analysis of the public services that the government provides to society.

In 2006, Nepal's decade-long civil war came to an end with a power-sharing arrangement between the traditional political parties and the Maoist insurgents. One of the main drivers of the conflict was the contention by the insurgents that the high degree of centralization of government power and resources failed to serve the needs of the people. As a result, an important element of the Comprehensive Peace Accord reached between the former combatants in November 2006 was that the structure of the state would be drastically reformed, with the intent that Nepal would become a federal state. The future federal structure of Nepal was enshrined in the Interim Constitution of 2007, which sets as a directive principle for the restructuring of the state that "the state shall be made inclusive and restructured into a progressive, democratic federal system" in order to "bring an end to discrimination based on class, caste, language, gender, culture, religion and region by eliminating the centralized and unitary form of the state." (Article 138)

Several years into the state restructuring process, however, progress toward a permanent federal constitution has stalled. To the extent that discussions about state restructuring are still ongoing, the discussions almost singularly focus around the number and composition of the new states or provinces, while the assignment of functional responsibilities to the future government levels is left for later discussions. Proposed state or provincial jurisdictions tend to be based on regional political and socio-ethnic boundaries. While some maps propose to divide the country into 11 or 12 states or provinces, other proposals reflect a greater degree of fragmentation, with up to 24 new states. This means that the average population size of the proposed states falls somewhere between 1 and 2 million people, with the smallest states generally expected to have a population of less than 100,000.

Not much else is clear about the structure of the future federal democratic republic of Nepal. The policy debate is eerily silent when it comes to the subnational structure beneath the federal states. It is highly likely, however, that if local governments are to exist at all in a federal Nepal, they are most likely to survive at the lowest local level—the municipal and village levels.



In this short Policy Brief, we posit that the lack of emphasis placed on the local government level—and the possibility that the district level might disappear in a future federal structure—is likely to worsen the already poor performance of Nepal’s public sector in terms of providing responsive, effective, and accountable public services. This argument is built around four core points:

1. In Nepal’s current local government structure, the district level is the most likely platform for effective local public service delivery. The political economy of decentralization, however, has historically favored the village level.
2. The current sequence in which the restructuring debate is tackled—by first focusing exclusively on the structure of the new state level—is likely to result in an inefficient federal structure.
3. In fact, the proposed state government level would not be well-positioned to deliver key public services, and is likely to result in more bureaucracy rather than more service delivery.
4. Therefore, in order to effectively empower the people in a future federal Nepal, attention should be shifted away from the state level, to a greater focus on the empowerment of local governments.

1. The political economy of decentralization in Nepal has historically favored the village level over the district level

The current territorial-administrative structure of Nepal comprises two levels. The district level is formed by 75 District Development Committees (DDCs), with a population of roughly 300,000 people each. The lower local government level is formed by municipalities (58) in urban areas and Village Development Committees (VDCs) (3,915) in rural areas. Although an attempt was made in 1990s to pursue meaningful decentralization by devolving functions, authority, and financial resources to local bodies at both levels, no local elections have taken place in more than 10

years. DDCs and VDCs are effectively deconcentrated central government bodies.

From a technical viewpoint, districts in Nepal are the most suitable platform for improving public service delivery.¹ Due to their relative size, districts have the potential administrative capacity to administer key sectoral services (such as education and health services) and are big enough to achieve the scale economies that are necessary to deliver these functions efficiently. At the same time, there are sufficiently few districts so that it is possible for line ministries to directly interact with them, to provide policy guidance, and to monitor their performance. Despite these technical advantages, the ambitious decentralization reforms of the 1990s focused most of their attention on devolution to the village level, largely ignoring the role that the district level could play in a more decentralized public sector.

A romantic notion of communal self-reliance and grassroots democracy in Nepal has systematically favored the village as the level where the interaction between the people and the public sector should take place and where public services should be delivered. In line with this conviction, the Local Self Governance Act (LSGA) of 1999 assigned many important service delivery functions, including the operation of schools and health clinics, to elected VDCs across the country. With similar enthusiasm, the bulk of intergovernmental fiscal transfers was—and continues to be—directed to the village level.

The focus of the previous decentralization efforts on the village level ignored an important reality: With 3,915 VDCs with an average population of less than 6,000, VDCs are simply too fragmented and lack the scale economies to

¹ Despite the district’s potential as a territorial-administrative platform for the delivery of key local public services, its role is not free of challenges: From a governance perspective, the district level could be seen as too far away from Kathmandu to be upwardly accountable, while being too far removed from the grass roots to be downwardly accountable.

deliver meaningful public services. In fact, each VDC has only a single formal public servant, and even that employee—the VDC secretary—is in reality a district-based public servant who is rarely seen within the VDC.

In this context, making the village level the focal point for public service delivery is simply a nonstarter. So why has the political economy of decentralization in Nepal historically favored the village level over the district level? Beyond the enthusiasm for grassroots democracy and community involvement, central government politicians as well as central bureaucrats may have preferred empowering VDCs rather than DDCs for more self-interested reasons.

Central government politicians likely preferred to empower VDCs rather than DDCs, as a relatively small grant to a VDC could result in substantial political leverage. In contrast, shifting a substantial share of financial resources to DDCs would likely create politically empowered district political leaders, who would compete for power and resources with nationally elected officials.

The notion that the VDC rather than the DDC should form the primary level of self-governance and local public service delivery likely suited central bureaucrats well. During the implementation of the 1999 LSGA, it was easy for line ministries to convince policymakers that—romantic notions notwithstanding—VDCs lacked the capacity and were too small to be the recipient of meaningful functions and resources. In practice, therefore, these functions and resources largely remained with the center, with limited deconcentration to the district-level line ministry offices rather than devolution to the elected DDC.

In the absence of any major public service delivery responsibilities, the DDC was relegated the role of more-or-less functionless intermediate administrative body, and was left to fend for itself with few or no real financial or human resources. As far as district finances, most of the resources that are received by the DDC simply pass through, with the DDC

functioning like a post office: Earmarked resources are passed through either to VDCs and municipalities or to the deconcentrated units of line ministries operating at the district level.

In the absence of real functional responsibilities, the appetite for having elected councils at the local level was short-lived, with central bureaucrats taking control over district and village decisions in 2002 from the councils that had been elected in 1992 and 1997. In the absence of elected councils, under current circumstances, district activities are provided without oversight and accountability from either top or bottom.

In short, despite a policy strategy of decentralization by devolution and despite the enactment of the LSGA of 1999, national politicians and bureaucrats appear to have been unwilling to meaningfully empower the local government level—politically, administratively, or fiscally—at the expense of national institutions. As a result, public service delivery in Nepal has remained weak, and is likely to have been a contributing factor in the national conflict.

2. Focusing on the state level first is likely to result in an inefficient local government structure beneath the new federal states

The current sequence in which the restructuring debate is tackled—by first focusing exclusively on the structure of the new state level, and only then contemplating the structure of the local government level and the assignment of functional responsibilities—is likely to result in an inefficient federal system. In fact, it is likely that if this sequence is followed, the future federal structure will emerge without a meaningful district level.

The predicted elimination of the district level in a future federal Nepal has little to do with whether districts could play a meaningful role in public service delivery. Nor is the predicted elimination of the district level driven by increased opposition to district-level local governments by the central bureaucracy.

Instead, the political empowerment of the new state level is likely to cause the further disempowerment of the district level.

The last time the local government level formally registered in the state restructuring debate was in July 2008, when Section 139 of the Interim Constitution was amended to read that “Election shall be done to set up local self governance bodies on the basis of principles of decentralization and devolution of power by creating a congenial atmosphere for the exercise of the people's sovereignty and thereby ensuring maximum peoples’ participation in the country’s governance, to provide services to the people at the local level and for the institutional development of democracy.”

Although the Interim Constitution does not state it explicitly, it can reasonably be argued that ensuring “maximum people’s participation” is not done at the district level but rather at the village level. In other words, the Interim Constitution endorses a local governance level that has already proved to be too weak and too fragmented to meaningfully deliver public services.

The likely demise of the district level is driven by the political economy of state-local relations. The vertical and horizontal distribution of power and resources in the new federal structure is seen as a zero-sum game. Thus, given the prevailing maps being drawn by politicians today, no politician fancying himself or herself in a leading role at either the national or state level in the future is likely to favor elected district-size local government jurisdictions that would compete with the new states (or with the center) for authority and scarce resources within the public sector.

Since the discussion on the assignment of functions and expenditure responsibilities is sequenced to take place after the new federal structure is determined (rather than in an iterative process), the impact of the public sector’s structure on the efficient delivery of public services is unlikely to be considered until after the final political decisions regarding

the territorial-administrative structure of the country have been made.

3. State restructuring, scale economies, and the assignment of functions in a federal Nepal

In the current state restructuring process, Nepali leaders have not made any effort to learn from the country’s own experiences with regard to decentralization over the past 13 years.² Little or no attention is seemingly being paid to the importance of scale economies in determining an effective state structure. At the same time, it does not appear that any lessons are being drawn from the political and institutional forces that derailed the previous decentralization effort.

The failure to recognize the importance of scale economies and the role of intergovernmental finances prior to determining the federal structure of the country can have disastrous consequences for the future efficiency of the public sector and the quality of public service delivery. Although proponents of a federal structure readily make comparisons between Nepal’s future federal structure and countries such as India, Pakistan, Canada, or the United States, the small size of the proposed states in Nepal (with an average population in the range of 1 to 2 million) makes the country very different from any of the aforementioned countries.

Instead, having a federal structure can be a major liability—rather than an asset—when jurisdictions’ sizes are inefficiently small and political accountability mechanisms are lacking at the state and local levels. Even though the Federal Republic of Nigeria is several times larger than Nepal, its federal structure is not dissimilar to the federal structure that some are

² The LSGA was motivated by essentially the same pressures behind the current state restructuring process, namely to “[m]ake provisions conducive to the enjoyment of the fruits of democracy through the utmost participation of the sovereign people in the process of governance by way of decentralization.”

advocating for in Nepal: a politically strong state level that is divided into many small, ethnically based states, where state and local jurisdictions are too small to efficiently deliver key public services.³ The poor performance of public service delivery in Nigeria serves as a potent example of what can go wrong in a federal structure where key expenditure responsibilities are assigned to state and local levels that have been fragmented for political reasons, and where critical accountability relationships are missing.

Although the regional political forces that champion the emergence of strong states in Nepal would like the state level to have many functions, the absence of scale economies at the state level would make it highly inefficient to shift the policy responsibility and resources for major social services, such as education or health services, away from the national level to the state level. Placing state-level ministries of education and health in charge of developing state-level school curricula or state-level health standards—rather than applying a single set of policies and norms for the nation as a whole—would result in considerable duplication. Introducing a strong state level would thus require the public sector to divert the already scarce resources currently available to these sectors to fund the administrative overhead at the state level. In addition, assigning such key functions to ethnically based states could result in potential centrifugal forces.

Given the strong power of the central bureaucracy in Kathmandu, it is unclear whether individual line ministries would cooperate with the devolution of their functions to the state level. However, if the main social services such as basic education and basic health services remain national functions, it is likely that they will continue to be delivered in a delegated-cum-deconcentrated manner, where

³ See James Alm and Jameson Boex, *An Overview of Intergovernmental Fiscal Relations and Subnational Public Finance in Nigeria*, International Studies Program Working Paper 02-01, (Atlanta: Andrew Young School of Policy Studies, Georgia State University, January 2002).

the long lines of communication to Kathmandu prevent any meaningful top-down (or bottom-up) accountability from being achieved.

Without a strong claim to being able to take over the entire policy responsibility for key public services from central authorities (which would place states in charge of setting the state-level school curriculum and so on), it is likely that the new states would seek a leading role in the implementation or provision of these services instead. In practical terms, this would likely mean that states would seek to take over the public service delivery responsibilities that are currently assigned to the district (and possibly even village) level, despite the fact that state jurisdictions are too large and too far removed from the people to engage in direct service delivery.

Thus, instead of the introduction of a federal state structure resulting in a process of *decentralization*, Nepal runs a considerable risk of its state restructuring resulting in a new form of centralization of power and resources from the district level up to the state level. In some ways, this is not that different from what appears to be happening in Kenya in the aftermath of its new constitution.⁴

4. Empowering the people by empowering the local public sector

The current drawing of maps and the political wrangling over the state level are distracting from, and may even be counterproductive to, the ultimate objective of state restructuring in Nepal: bringing about a more inclusive, democratic, and responsive state structure. That leaves the question: If we want to avoid a federal constitution that merely serves as a political compromise between national and regional elites without fundamentally fixing the problem of improved public service delivery, then what is Nepal's best hope for a restructured public sector where people are

⁴ For instance, see Jamie Boex and Roy Kelly, *Fiscal Decentralization in Kenya: A Small Step or Giant Leap?* IDG Policy Brief (Washington, DC: The Urban Institute, May 2011).

actually empowered over their public sector? In other words, what constitutional arrangement can counterbalance the power-absorbing tendencies of both national and state-level government officials?

The experience with the LSGA has shown that there is limited political will at the central level to truly empower the local public sector. It could be argued that the resistance at the central level to empowering the local bodies was in fact because an effective and efficient local public sector would offer a counterweight to its own centralizing tendencies. Now that a loss of central power and resources is all but unavoidable for central institutions under a new federal constitution, it may make sense to follow the constitutional mandate to “eliminate the centralized and unitary form of the state” not by replacing the central monopoly over power and resources with state-level monopolies over power and resources, but rather, with a strong local government level in the context of a three-tiered federal system.

How would one go about establishing a strong and effective local government level as part of a three-tiered federal system? A first lesson from the current intergovernmental system in Nepal is that a local government level comprising almost 4,000 village areas is not a suitable basis for a robust local government level, neither in terms of political, administrative, or fiscal positioning, nor in terms of service delivery capacity. However, as noted above, it is unlikely that the political champions of the new state level will accept a local government level at the current district level. A possible compromise may be to focus a future elected local government level below the current district level, but well above the current VDC levels. One could imagine a local government level that has roughly double or triple the number of jurisdictions as the current districts level; say, 150 to 250 urban and rural local authorities. This would create a local government level that would not be a political threat to the state level, while still providing sufficient scale to be a meaningful provider of key public services. Rather than retaining the VDC as a separate government level (or rather

than eliminating it altogether), the current VDC structures could be used to form the foundational level (e.g., the ward level) of the future rural local authorities.

A second observation, based on international experience, is that if placed hierarchically under a strong state level, the local government level is likely to be suffocated, politically and administratively as well as fiscally.

Therefore, not unlike the South African model of federalism, the local public sector in Nepal could be constitutionally shaped as a separate sphere of government that is coequal with the national government and state governments (rather than a local government level that is politically inferior to the federal and state levels). In such a triangular (rather than vertical) division of responsibilities and powers, local governments would have the responsibility to administer key public services (such as basic education, health services, agricultural extension, and so on) with continued policy direction and financial support from the national level, but also with oversight and guidance from state authorities.

What does this mean for local bodies today?

The vision being set forth here of a federal structure with three spheres (federal, state, and local) has completely different implications than the (essentially) two-tiered federal system currently under consideration in the politically motivated restructuring debates. Rather than focusing on political maps at the regional level, and the subsequent construction of associated governors’ mansions and state administrative infrastructure, it means that the main focus of attention will be on restructuring the local public sector and improving public service delivery.

In practical terms, the proposed state structure requires that the management of local bodies at the national level needs to be elevated from a function falling under the Ministry of Local Development and should be placed under the Prime Minister’s Office or within the National Planning Commission.

The proposed setup further means that the main focus of current efforts to build local institutional capacity, local management structures, and local accountability mechanisms should gravitate away from the VDC level toward the DDC level.

A third implication of having a separate local government sphere in the federal constitution is that it would be prudent to protect the financing of the local level against predation from the higher levels. Although the mechanism to fund the local government level should be defined in the Constitution, considerable international experience suggests that it would be unwise to specify any resource shares in the Constitution itself.

However, it is likely that—in addition to some own revenue sources—a strong local government level would rely on a combination of unconditional block grants (perhaps specified as a fixed percentage of the federal budget) in addition to formula-based sectoral grants provided by the national government that are linked to the responsibilities assigned to the local level. Of course, these resources could be supplemented by state-level grants, to the degree that new state governments would like to provide further support to the public services that are delivered by the local bodies within their state.

A final thought: A focus on local government may break the political stalemate

The current political debate regarding state restructuring seems to have reached a stalemate. Beyond the inherently greater focus on public service delivery of a three-sphered federal structure that takes into account federal, state, and local governments, it is possible that introducing a dramatically different proposal may prove to be a “game changer” that breaks the current political stalemate and reinvigorates the efforts to achieve a grand political compromise with regard to Nepal’s future federal structure.