

Justice, land, and infrastructure

chapter 8

It takes more than building human capacities to broaden people's opportunities. People also need complementary assets, access to the marketplace, and security of person and property. This chapter starts with a description of justice systems, showing how critical they are in ensuring a level playing field and fair returns. It then turns to policies for expanding access to the complementary assets of land and infrastructure. Promoting fairness in markets is addressed in chapter 9.

Building equitable justice systems

Society's rules, and the institutions that establish, maintain, and transform them, govern market and nonmarket interactions. They determine people's endowments, their rights and obligations, and their ability to generate fair returns. Reflecting and producing the distribution of power among groups, good institutions (so necessary for prosperity) emerge only when the distribution of political power and enforceable rights is equitable.

Legal institutions play a key role in the distribution of power and rights. They also underpin the forms and functions of other institutions that deliver public services and regulate market practices. Justice systems can provide a vehicle to mediate conflict, resolve disputes, and sustain social order. But inequitable justice systems may perpetuate inequality traps by maintaining or reproducing elite interests and discriminatory practices. Equitable justice systems are thus crucial to sustained equitable development.

Building more equitable justice systems runs into three main challenges—often interrelated and reinforcing. First, legal institutions may be open to capture by elite interests or may discriminate against certain groups. Second, these institutions are often

inaccessible, because they are incompatible with local norms and customs and they are physically or economically inaccessible, or because people lack the knowledge or capacity to navigate the system. Third, elite capture and the inaccessibility of the legal system may mean that policies relating to crime and personal security are inequitable and perpetuate crime-related inequality traps.

Combating elite capture and discrimination

Political and economic elite interests often coincide at the expense of a disempowered majority. When power is in the hands of a narrow elite, the rights of most citizens are unstable. A century of banking in Mexico, outlined in chapter 6, illustrates how deals between the political and economic elite led to the establishment of banking monopolies and laws that maintained a system of rent-sharing between banks and governments.¹ Another striking example of elite capture comes from the transition economies and the rise of oligarchs who manipulated politicians and shaped institutions to get rich.² Legal systems that cater to narrow interests also tend to discriminate against other groups through inequitable laws and practices.

Ensuring equality before the law and securing both personal and property rights for a broad section of the community give individuals the incentive and the opportunity to take part in economic and political life. This requires an independent and accountable judiciary and laws and practices that protect citizen's rights in a nondiscriminatory way.

Enhancing judicial independence and accountability. In many countries, a rule of

law system—administered by multiple arms of government—constrains political power.³ In this system, an independent judiciary acts as a safeguard against abuses of state and nonstate power. Because judges are also open to elite capture and corruption, accountability mechanisms are a key aspect of legitimate judicial independence.⁴

In many developing countries, shifts toward an accountable and independent judiciary require a change in culture and institutional practice. Ethiopia established an independent judiciary for the first time in 1995.⁵ In Vietnam “telephone justice” was common, with party elites habitually contacting judges to direct decisions.⁶ Changing ingrained institutional practices in both countries has been a slow process. Poor conditions of judicial service in many countries can increase corruption.⁷ For example, low remuneration for magistrates in Kenya made them open to alternative funding for their services; Kenya removed almost one-third of judicial staff for corruption in 2004.⁸

Promoting judicial independence without establishing accountability mechanisms can further entrench elite interests. Institutional safeguards, transparency, and the existence of a civic constituency are key to both accountability mechanisms and judicial independence. Institutional safeguards include providing for security of tenure for judges; rigorous and transparent appointment and disciplinary processes; transparent mechanisms of case allocation and case management; transparent and open hearings; appeal rights and the publication of judicial decisions; and public information about the courts.⁹ Many countries have enshrined judicial independence in the constitution or state laws.¹⁰ Bolivia has established open competitions for judgeships and ethical standards for judges. Courts in the Philippines have a performance management system for judicial and nonjudicial personnel.

Public information campaigns can enhance the independence and accountability of the courts, increasing public confidence in and commitment to the system, and enhancing people’s capacity to demand better governance and hold those in positions of power

accountable. In Colombia public information centers in major courts disseminate information and help people use the court. In Venezuela information is provided to the public through an Internet-based judicial portal for the Supreme Tribunal.¹¹

Strengthening the relationship among civil society, the media, and the courts has also improved public awareness and scrutiny of the judicial system. Bad judges have resigned because of high-pressure media campaigns, such as the recent media scrutiny in the Philippines.¹² The media can also disseminate information, such as the “My Rights” television show in Armenia (box 8.1). Similar shows have been developed in other parts of Eastern Europe. In Georgia, an NGO disseminating information about the courts increased public satisfaction with the courts.

The existence of an independent and accountable judiciary is not enough to protect citizens against abuses of state power. Adequate laws and institutional mechanisms are also needed. In Thailand, for example, separate administrative courts were established for the first time in 2001 to protect citizens against arbitrary uses of state power. The courts aim to ensure that state authorities act in accordance with state laws and regulations. They also aim to enhance citizen participation in public policy formulation and oversight. In the first three years, the courts processed almost

BOX 8.1 *Increasing legal literacy and public awareness: “My Rights” on Armenian public television*

Many people in Armenia have no understanding of the legal system or the rights afforded them under the law. And distrust of the courts is widespread. In a recent public awareness campaign, the government funded a television show to provide citizens with examples, advice, and information on their legal rights.

“My Rights” uses mock trials to depict real-life disputes in Armenian courts. The television judge is a deputy minister of justice, and the parties are often those in the real dispute. The topics—such as rental and property disputes, customs issues, and family law matters—are timely and of broad interest. A live studio audience of judges, lawyers, legal officials, and others discusses the trials on air.

The show airs once a week on Armenia’s state television channel. After only five or six shows, “My Rights” became the number one show in Armenia. There have been numerous reports of viewers requesting legal documents and decisions from notaries, judges, and other legal officials based on what they learned from the show. And when the power went out in one village a few minutes before “My Rights” was going on the air, the people in the town marched on the mayor’s office and accused the local officials of intentionally cutting the power so that people could not watch the show!

Source: Decker and others (2005).

17,000 cases, most concerning corruption or other unlawful acts by public officials. Many of the cases made front-page news in Thailand because of their social impact.

Combating discriminatory norms and practices. Laws that reinforce exclusionary practices in norm-based institutions perpetuate unequal power relations. Some laws may discriminate against particular groups, such as laws affecting indigenous people or the laws in apartheid South Africa. The absence of laws can also reinforce unequal power relations as for domestic violence, often relegated to the nonlegal private realm.

In many countries, antidiscrimination and equal opportunity laws have reduced discriminatory practices. Historical disadvan-

tage may mean, however, that legal equality is not enough. Some countries have passed laws that discriminate in favor of certain groups, creating affirmative action programs on the basis of race, ethnicity, and gender or for people with disabilities. An assessment of two of the most widely implemented affirmative action programs, in India and the United States, suggests mixed impacts (box 8.2).

The mere existence of “equitable laws” for affirmative action does not guarantee their equitable implementation or enforcement. For example, in Peru and Honduras, gender discrimination in judicial decisions and treatment by police and judges discourage women from using the system to resolve disputes.¹³ Such disadvantaged groups are more likely to experience the law-and-order side of the law than the protection of their rights (as discussed below under crime and personal security).

BOX 8.2 *Affirmative action in India and the United States*

The affirmative action program in India is based primarily on caste and gender and that in the United States primarily on race. Before independence in India, the British government introduced affirmative action to address discrimination against “untouchable” castes (now known as Dalits) and “tribals” (now known as Adivasis). After independence in 1947 the policy of reserving 22.5 percent of seats in education institutions, government jobs and electoral seats was written into the constitution. Since 1991, a further 27 percent quota has been introduced for other low castes (called Other Backward Castes), but with no constitutional guarantee. And since 1993, 33 percent of the seats in local governments have been reserved for women, Dalits, and Adivasis (Deshpande 2005).

In the United States, slavery was pervasive for more than two centuries, and not until 1866 were blacks granted citizenship rights. The system that replaced slavery was only marginally better, with several features similar to the Indian caste system: segregation, denial of education, restrictions to low-paid, menial jobs, social and economic discrimination, negative stereotyping, and violence. The Civil Rights Act of 1964 and subsequent legislation, Supreme Court rulings, and executive orders in the 1970s introduced affirmative action into the political, judicial, administrative, and economic spheres of American society. Starting with the label “equal opportunity,” selection procedures incorporate compensatory correction to ensure adequate representation of

minorities in education and employment (Deshpande 2005).

The programs in both countries have become centerpieces of political battles over race and caste. Critics argue that they tend to benefit the upper echelon of minority groups, and they are difficult to end. In India, the programs are said to apply to sub-castes that have not traditionally faced discrimination (Sowell 2004). They may also reinforce negative stereotypes by placing minorities in positions they are not qualified for (Coate and Loury 1993). Despite these weaknesses, India’s program has provided formal sector employment and higher education for many Dalit and Adivasi families, freeing them from subservient roles. With the reservations in local government, elected women leaders make decisions in line with women’s needs (Chattopadhyay and Duflo 2004). Low-caste representatives in state assemblies increase the allocation of quota-based jobs to low-caste constituents (Pande 2003). And Dalit representatives in village government improve the targeting of benefits to Dalits (Besley and others 2004).

In the United States, disparities between blacks and whites continue to be significant on all economic indicators, and there is evidence of discriminatory gaps in earnings. But affirmative action in jobs has increased black employment and enrollment in higher education (Holzer and Neumark 2000, Bowen and Bok 1998). But the U.S. program’s quasi-voluntary element means that litigation can dilute the program, and black representation in government bodies continues to be very low.

Making justice accessible

People’s legal rights remain theoretical if the institutions charged with enforcing them are inaccessible. Accessibility depends on how compatible laws are with the norms and understandings that shape people’s lives. Legal institutions need to be physically and economically accessible and people need to have the knowledge and capacity to claim their rights.

Addressing the compatibility of state and customary justice systems. Forms of customary or nonstate law operate in a majority of countries.¹⁴ Yet they are often neglected in justice sector reform policies. Engaging with customary systems is an important part of equitable reform strategies for two main reasons. First, customary law is often a fundamental part of a community’s identity and belief system; thus, a lack of recognition can be intrinsically discriminatory and serve to exclude communities from the wider state system. Second, a failure to engage with customary systems may leave inequitable and inefficient practices at the local level unchecked.

Where state and nonstate systems have developed in tandem, they often complement each other and reinforce socially accepted codes and rules. But in communi-

ties where the state systems lack legitimacy and political reach, customary systems often act independently from the state legal system, which may be rejected, ignored, or not understood. Real difficulties arise when local customary systems are at odds with the rights and responsibilities articulated in state law.

In many developing countries, customary systems are the dominant form of regulation and dispute resolution. In Sierra Leone, about 85 percent of the population fell under customary law as of 2003.¹⁵ Customary tenure, discussed below, affects 90 percent of land transactions in Mozambique and Ghana.¹⁶ Customary justice depends on local traditions, as well as the political history of a country or region. Ethiopia officially recognizes more than 100 distinct “nations or peoples” and more than 75 languages.

Customary systems can be incompatible with economic, social, and civil rights. Many forms of customary law are seen to discriminate against marginal groups. In much of Sub-Saharan Africa, for example, customary systems systematically deny women’s rights to land, assets, or opportunities.¹⁷ Customary practices are also seen as archaic and rigid—not amenable to modernization, efficient market relations, or broader development goals. They are often seen as overly localized and complex, making more generalized reform initiatives difficult. They can lack legitimacy at the local level. For example, many systems in Sub-Saharan Africa have been substantially distorted by colonial rule, which often used local chiefs to maintain control and established more authoritarian and ethnic-based structures than previously existed.¹⁸

However, it is wrong to presume that all customary law discriminates against marginalized groups—or that western law does not. For example, in the AmaHlubi community of KwaZulu Natal Province in South Africa, women and men are considered equal, with both entitled to own property.¹⁹ Furthermore, there are often good reasons for people to choose to use customary systems. The state systems may lack legitimacy or be seen as mechanisms of control used by oppressive regimes. Or the state systems may

lack capacity, be inaccessible, or dramatically increase transaction costs.²⁰ In rural Tanzania, a perception that state institutions can not supply law and order has led to the emergence of “new” forms of organized village defense groups called *sungusungu*. While technically illegal, the *sungusungu* are often informally supported by the state, given their success in reducing crime.²¹

Ignoring or trying to stamp out customary practices can also have serious negative implications. Top-down reform can undermine informal institutions without providing viable alternatives, and the vacuum can lead to power grabbing, lawlessness, or even violent conflict. When neither formal nor informal mechanisms are functioning, human rights abuses and serious conflict are more likely. For example, a study in rural Columbia found the incidence of vigilantism, “mob justice,” or lynching to be five and a half times greater in communities in which informal mechanisms are no longer functioning effectively and the state presence remains limited.²²

A failure to engage with customary systems may mean that discriminatory practices go unchallenged. While state law officially protects women’s rights in many countries, local norms and power structures continue to make it almost impossible for women to claim these rights.

Considered attention to customary systems in broader institutional reform is fairly new. But many governments, such as South Africa, have begun working toward integrating customary institutions into wider state frameworks (box 8.3).²³ Many countries have attempted to integrate customary land systems into formal land law systems (box 8.7). Local NGOs and community groups have also helped empower marginal groups to challenge discriminatory norms at the local level.

Establishing adequate and open legal institutions. Even when formal systems do exist, they often lack adequate infrastructure or are so institutionally weak that citizens cannot claim their rights. Formal institutions may exist only in large cities, and even then excessive delays, unfair procedures, or unreasonable costs may leave

BOX 8.3 *State frameworks and customary institutions in South Africa*

The coexistence of various official state laws in South Africa began as early as the 1830s when chiefs in Cape Colony were granted authority to enforce indigenous law (subject to review by a colonial official).²⁴ At the end of the apartheid era there were approximately 800 officially recognized traditional communities and traditional leaders, 12,000 headmen, and 12 kings.

Since 1994, South Africa has worked toward bringing traditional systems into the state framework. Traditional institutions and laws are all officially recognized in the 1996 constitution. After a long political process, the national Traditional Leadership and Governance Framework Act was promulgated in 2004, setting out the roles and responsibilities of different levels of traditional leaders and institutions, and their relationships to the different levels of government.

Many celebrated the constitutional and administrative recognition of customary law, but there clearly are difficulties. Customary practices have been criticized as incompatible with rights in the constitution and the new South African Bill of Rights.²⁵ Of 800 traditional leaders recognized by the state in South Africa, only one is female. In an attempt to deal with this, the state issued a regulation in early 2005 that female participation must be at 30 percent by the end of the year, but there is no consensus on how this might be achieved. Recognizing the difficult task of effectively integrating the different systems, the South African model aims at “progressive alignment” with the constitution.

Source: Adapted from Chirayath and others (2005).

BOX 8.4 *The impact of legal aid in Ecuador*

As in much of the rest of the world, Ecuador's poor face numerous barriers in using the legal system. Women considering claims against their former spouses may face an added obstacle: physical violence.

As part of a larger judicial reform effort, three local NGOs—Centro Ecuatoriano para la Promoción y Acción de la Mujer, Corporación Mujer a Mujer, and Fundación María Guare—provide legal information and representation as well as psychological counseling and referrals to shelters. A survey in 2002 revealed that women's use of legal aid clinics reduced the probability of severe physical violence after separation by 17 percent. Legal aid clients also

attained better legal and economic results than nonclients, raising their chances of obtaining a child-support award by 20 percent and their chances of receiving a child-support payment by 10 percent.

Receiving assistance from the legal aid clinics also had intergenerational impacts. Child-support payments increased the probability of the child attending school (by 4.8 percent) as did the lower incidence of violence. Anecdotal evidence also suggests that the payments, a small but important source of family income, were used to pay for food.

Source: World Bank (2003g).

them inaccessible to much of the community.²⁶ Institutions can also be inaccessible if people do not know their rights and cannot navigate the systems charged with protecting them.

A large array of information campaigns has informed citizens about their rights (discussed above). But even if people know their rights, they may have limited capacity to navigate the system. Access to legal services is often restricted or costly. In Honduras, legal fees to obtain a monthly alimony of 100 lempiras (US\$5.30) in a

child-support case could amount to as much as 2,000 lempiras (US\$106.00), or almost two years of alimony. Adding to the costs are requirements that parties be represented by lawyers. For example, most Latin American countries do not permit self-representation, effectively denying access based on economic status. Legal aid can increase people's access to basic legal services and the courts (box 8.4). So can community mediation centers, lay judges, and mobile courts. The mobile courts introduced in remote areas of Brazil in 1999 have been replicated in the Philippines and Mexico. In Guatemala, 24 mediation centers have been created, employing mediators fluent in Spanish and local Mayan languages.²⁷

In some situations, social movements provide the support for people to use the courts and claim their formal rights, as with the landless peasant movements in Brazil and Mexico. In Argentina, too, unemployed factory workers have occupied closed factory sites and pursued their rights through the courts and the legislative process. In other cases, civil society organizations have assisted groups in claiming their rights—as in the “right to health” cases discussed in chapter 10.

Civil unrest and conflict may further weaken legal institutions. In Sierra Leone, a decade of civil war left the justice system in shambles: courthouses were destroyed, and judges, lawyers, and police officers were killed or forced to flee. During the conflict in Liberia, more than three-quarters of the population left their homes.²⁸ In Bosnia, 2.3 million people—more than half the country's population—fled their homes during and immediately after the war. To prevent the return of minorities, many property records were destroyed or tampered with.

Reestablishing legitimate legal institutions is crucial to restoring such people's personal and property rights and enhancing confidence in newly established governance structures. In postwar Bosnia, the Dayton Agreement established the Commission for Real Property Claims of Displaced Persons and Refugees, which collected claims for 318,780 properties. As of June 2003, it had issued about 290,000 final decisions on property titles.²⁹

Improving crime and personal security policies—breaking crime-related inequality traps

The cycle of inequality, crime, victimization, and discrimination exemplifies the processes by which inequality traps, outlined in chapter 2, are perpetuated. Marginal groups are not only more likely to move into criminal behavior, they are also more likely to be victims of crime. Furthermore, discriminatory practices in the justice sector mean that marginal groups are more likely to experience the law-and-order side of the legal system—black men in the United States are incarcerated on drug charges at a rate 13.4 times that of white men, bearing little relation to differences in offenses³⁰—and are less likely to have access to institutions charged with protecting them. At the same time, given their role in shaping these processes, legal institutions are also places for change—that is, vehicles for challenging inequality traps.

Breaking the cycle of inequality, crime, and violence. Traditional approaches to reducing crime and violence based on increasing mechanisms of control and harsher sanctions have failed to reduce crime. By contrast, promoting protective strategies and minimizing the risk of crime have more success at lower cost.³¹

To target the many risk factors of increased crime, crime prevention programs often require support from the judicial services, social services, health, education, media, police, local government, civil society organizations, and the private sector (box 8.5). Local governments and police services often coordinate such programs.³²

Many more effective interventions target children and adolescents, who are seen as particularly at risk of falling into criminal behavior.³³ Preventative interventions include family support and parenting skills programs, early childhood development programs, special needs programs, after-school care, antibullying programs, life skills and cultural programs, and community participation programs.³⁴

School-based interventions have targeted youth crime and have kept young people in schools in many countries.³⁵ *Tilsa Thuto* is a school crime prevention program imple-

BOX 8.5 *Bogota, Colombia: civic culture program*

Unlike most Colombian cities, Bogota—a city previously considered unsafe and violent—has seen a huge reduction in crime since the early 1990s and a substantial increase in citizen perception of safety.

The city's administration targeted civic culture and education, urban planning and safety, and the regeneration of public spaces. Individual and community behavior were changed by establishing a citizen disarmament program; restricting alcohol consumption and use of fireworks; increasing the number of social service centers; enhancing awareness through media campaigns and educational programs; preventing domestic violence and child abuse; strengthening the capacity of the police and the judiciary to deal with crime, violence, and victimization;

enhancing neighborhood watch programs; and revitalizing urban public spaces. Employment and educational programs were introduced to support populations most at risk.

No longer one of the most dangerous cities in the western hemisphere, Bogota has seen remarkable results. The homicide rate fell from 80 per 100,000 inhabitants in 1993 to 22 in 2004, with homicides related to intoxication falling dramatically. By 2001, 6,500 weapons had been turned in and gun confiscations fell from 6,000 in 1995 to 1,600 in 2003. Arrests for homicide, assault, and car theft rose by 500 percent between 1994 and 2003 (with no increase in police personnel).

Sources: Llorente and Rivas (2005), World Bank (2003a).

mented in 42 schools in Soweto, South Africa, in 2000, in areas known for high levels of crime, unemployment, and poverty.³⁶ The program—established in partnership with the department of education, community organizations, and local police—creates safer schools through the active participation of students, teachers, parents, school administrators, and the local community in different training modules. Both teacher and student attendance at school increased by some 70 percent, acts of violence and aggression fell by 67 percent, and the pass rate increased by an average of 78 percent.

Alternative ways of dealing with young offenders have also been effective in breaking the cycle of crime. Interventions include diversion programs, restorative justice, alternative sentencing, and reintegration projects. Diversion programs aim to move young offenders into welfare-based programs, as with attempts in Africa to keep street children out of prison. Restorative justice programs, such as community conferencing, mediate between offenders and those affected by the crime, helping to reintegrate young offenders into their communities. Noncustodial sentencing, such as community service orders, is used in different parts of Africa today to promote the reintegration and rehabilitation of offenders.³⁷

Increasing personal safety. Appropriate and accessible police and support services for all

are crucial. Violence against women, a huge problem in many parts of the world, is exacerbated by underreporting, inadequate support systems for victims, discriminatory practices within justice sector institutions, and the lack of adequate sanctions for perpetrators. Many governments have attempted to address the problem by introducing more severe sentences for perpetrators, establishing remedial programs for offenders, and running gender-sensitive training programs for police and the judiciary.

More recently, some countries, including Argentina, Brazil, Colombia, Peru, and Uruguay, have set up women's police stations. Other countries have set up police cells for women in regular police stations. These services have shown mixed results.³⁸ Women's police stations have increased reporting of abuse and the likelihood that women will receive medical and social services. But critics argue that services encourage regular police to abdicate responsibility for crimes against women and that women officers have not necessarily demonstrated better attitudes toward victims of violence. Where stations are working fairly well, their efforts are often undermined by other parts of the justice system, as prosecution rates remain unchanged.

The notion that the physical environment can increase personal safety has been an integral part of many recent crime prevention strategies,³⁹ and it has been applied to city-planning, public transport systems, parks and recreational spaces, low-income housing, and downtown areas where people feel most vulnerable to violence and crime.⁴⁰

Toward greater equity in access to land

Land is a key asset for poor people. Owning it provides a means of livelihood to many, facilitates access to credit markets, has an insurance value, determines influence in local politics, permits participation in social networks, and influences intrahousehold dynamics. That is why inequality in the ownership of land has such far-reaching consequences for the distribution of well-being and the organization of society for generations to come. Yet landownership in many countries is highly unequal, substantially more so than income or consumption.

Building on chapters 5 and 6, we argue here that there are strong equity and efficiency reasons for addressing inequalities in land distribution—both rural and urban—and then discuss the experience with land reform and options for broadening access to land: providing security of tenure, improving the functioning of land markets, and implementing cost-effective land redistribution.

Equity and efficiency reasons to address inequalities in land distribution

Inequalities in landownership in dozens of countries can be traced to interventions over the past 500 years to establish and support large farms at the expense of indigenous peoples and the local peasantry. This historical discrimination against certain groups—or more generally a lack of legitimacy for the prevailing pattern of landownership—offers a rationale for equity-enhancing reforms. Additional motivation comes from the fact that the landless are among the poorest in developing countries.⁴¹

Access to land can give the poor more voice in the political arena and can lead to higher investments in children's education, arresting the intergenerational transmission of poverty. Galasso and Ravallion (2005), in their study of the Food for Education program in Bangladesh, find that villages with more unequal distribution of land were worse at targeting the poor. This is consistent with the view that land inequality is associated with less power for the poor in village decision making. Land inequality has also been found to impair the ability of communities to engage in socially optimal collective action, resulting in the underprovisioning of public goods. It also contributes to social tensions that can lead to considerable upheaval, as in Southern Africa.⁴²

Inequalities in landownership can weigh particularly heavily on women. Land rights (and control of other assets) often reside with the head of household, which has implications for intrafamily bargaining power and control of resources. Women with secure land rights (including inheritance on the death of a husband) are more likely to engage in independent economic activity, a result that has positive economic

and equity implications for the household. Inheritance rights that disadvantage women are of particular concern in Africa, where they are often based on customary institutions that conflict with constitutional norms and international conventions on women's rights. In fact, insecure inheritance rights pose an additional burden on widows who lose their husbands, often through HIV/AIDS.⁴³

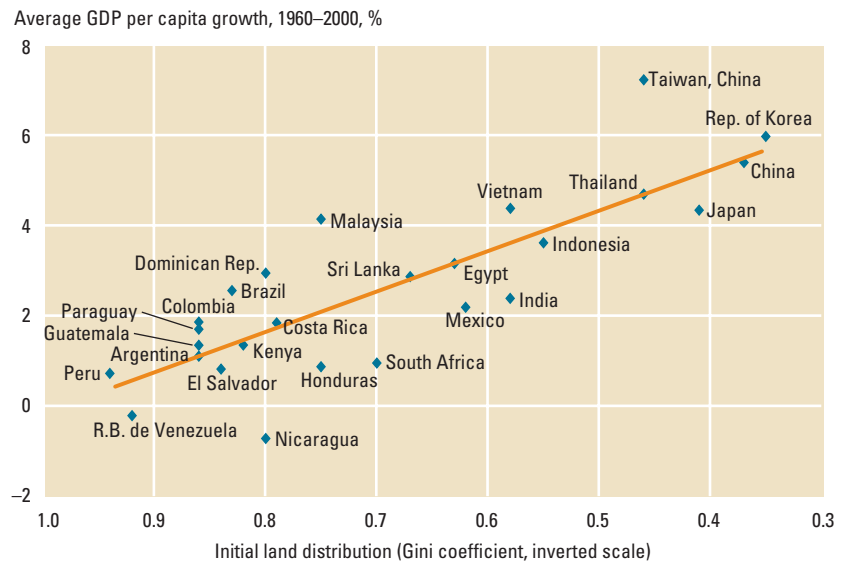
There are strong efficiency reasons to address inequalities in land distribution. Pervasive imperfections in land and financial markets in developing countries reduce investment in land and keep countries from efficient land allocations (chapter 5). These effects—together with lower human capital investment, reduced social cohesion, and distorted political power—are consistent with a positive association between more unequal land distribution and lower GDP growth (figure 8.1).⁴⁴

Experience with land reform

The discussion here implies that redistributing land could enhance equity and efficiency. This is likely to be true, but there are significant hurdles in practice. For instance, the specter of land redistribution can also worsen efficiency, because farmers are reluctant to invest in land that they might lose. Or political imperatives can override sound program design. Successful land reforms—such as in Japan, the Republic of Korea, and Taiwan, China—are rare and often associated with exceptional events, such as war or political upheaval. Indeed, the history of land reforms is littered with partial successes and failures.

In India, abolishing the land rights of rent-collecting intermediaries⁴⁵ has been highly successful, whereas the implementation of landownership ceilings and laws to protect tenants was, with few exceptions, half-hearted. The absence of political leadership has been identified as the “prime reason for the poor implementation of land reforms in India.”⁴⁶ Still, where tenant protection was implemented seriously—primarily in West Bengal—it helped improve productivity.⁴⁷ But restrictions on subleasing land by beneficiaries (or their children) tend to reduce the scope for productivity-enhancing land trans-

Figure 8.1 Unequal initial land distributions go together with slower economic growth



Source: World Bank (2003i).

Note: Land distribution is measured using the Gini coefficient.

fers. And the fact that both tenants and landlords have rights to the same plot of land severely undermines investment incentives.⁴⁸

In Latin America, where the potential for land reform should have been highest given the high inequality of landownership, reforms have generally been “incomplete.” Beneficiaries have often lacked the tools to become competitive and, as a result, the impact on poverty has been disappointing.⁴⁹ In Kenya and Zimbabwe, postindependence reforms were quite effective but short lived for political reasons.⁵⁰ In South Africa, the government’s land redistribution program in the late 1990s fell way short of its targets but recently gathered steam (box 8.6). Clearly, both the politics of land reform and its implementation are complex.

Why the rather disappointing results from attempts at land reform? First, given that the motivation for land reform is often to address political grievances, efficiency and poverty reduction tend to be secondary. Guided by short-term political objectives, bureaucrats often targeted high-productivity areas rather than high-potential areas, resulting in costly land acquisition and limited scope for sustained productivity impacts. Central administration of the programs also often meant that a large portion of land reform budgets was spent on the

BOX 8.6 *Land reform in South Africa: picking up steam*

To redress apartheid-era asset inequality, South Africa embarked on land reform in 1994 with a program that rested on redistribution, restitution, and tenure. Targets for redistribution were ambitious: the government aimed to transfer 24 million hectares of agricultural land (30 percent of the total) to about 3 million people between 1994 and 1999. Under the program, self-selected groups use grants to purchase land from willing sellers and to invest in the land's development. But by February 2005, only about 3.5 million hectares had been redistributed to 168,000 households. Restitution proceeded at a snail's pace—only 41 of 79,000 claims were settled between 1995 and 1999. And progress on tenure in the former "homelands" was equally slow.

After this sluggish start, some key changes accelerated the restitution and redistribution programs. The Restitution Act was amended to allow for negotiated settlements, speeding the process considerably; previously all claims had to be settled in court. By March 2005, more than 58,000 claims were settled, and all claims are scheduled to be resolved by March 2008.

The redistribution program was improved in 2001, making it more flexible and decentralized. The grants for land purchase and farm development now follow a sliding scale, depending on the contribution by the beneficiaries, and can be obtained

by individuals as well as groups. Approval authority is now delegated from the minister to the provincial directors of land affairs. As a result, redistribution has significantly increased. For the first time since 1994, land delivery is now constrained only by the budget for it.

But some big challenges remain. Pressure is growing from civil society on government to meet the revised target of redistributing 30 percent of agricultural land by 2014. Restitution settlements can be complex when rural claims target highly productive, capital-intensive farms and the claimants refuse, as is their right, to accept financial compensation, instead of the physical restoration of the claimed land. The agricultural impact of the redistribution scheme has been stunted by an inappropriate emphasis on collective farming and a lack of beneficiary power in decision making. The land market continues to be biased against family farming through costly restrictions on subdividing agricultural land and a regressive land tax dating from 1939. A new land tax based on the value of unimproved agricultural land could provide incentives for large farms to sell unused or underused parcels. New legislation that transfers communal lands from state to community ownership is now in place, but it still needs to be implemented.

Sources: World Bank (2003i), van den Brink, de Klerk, and Binswanger (1996).

wages and salaries of civil servants rather than used to benefit the poor. The prospect of gaining access to valuable real estate, instead of having to put in sweat equity to develop a piece of land, undermined the self-targeting properties of reform programs, often politicizing beneficiary selection.

Second, the relationship between farm size and productivity depends on the type of crop, quality of land, degree of mechanization, and such associated factors as marketing and credit. For most crops, under normal availability of mechanical services, production is neutral to farm size. But when management requirements are substantial (labor-intensive crops, erratic weather conditions, frequent pest incidence) family farms—as opposed to larger, wage-labor farms—can be more efficient because of advantages in supervising labor. By contrast, large farms often have better access to input and output markets, financing, and technical

assistance. Such advantages can be countered if small farmers coordinate their efforts through cooperatives.⁵¹ If policymakers do not properly account for all these conditions in land reform schemes, efficiency can suffer.

Third, many traditional land reform efforts failed to provide beneficiaries with secure long-term rights backed by a well-functioning and equitable legal system. Affordable channels to adjudicate land access and ownership claims must be open to everyone. Without such channels, disadvantaged groups cannot take full advantage of tenure security, land market, and distributive reforms. Even with full property rights, underdeveloped credit and insurance markets limit the use of land for collateral.

Fourth, the full productivity benefits of land reform cannot be realized without complementary inputs and training; putting land in the hands of inexperienced farmers without the needed support often led to high rates of desertion.⁵² More generally, a broader rural development strategy is required to complement land reform because rural households get their livelihoods from several different sources. This has implications for the design of land reform (for example, determining viable farm size) and highlights the importance of investments that can facilitate off-farm employment, such as education.

Broadening access by improving the security of tenure

The benefits of secure tenure for rural households are well known: higher productivity, greater access to credit, higher propensity to invest in physical assets (figure 8.2) and the education of children, and time and effort saved in securing land rights.⁵³ Further benefits arise from removing the discretionary power of bureaucrats to decide on the allocation of land (improved local governance was mentioned as a benefit of property rights reforms introduced after 1992 in Mexico).⁵⁴

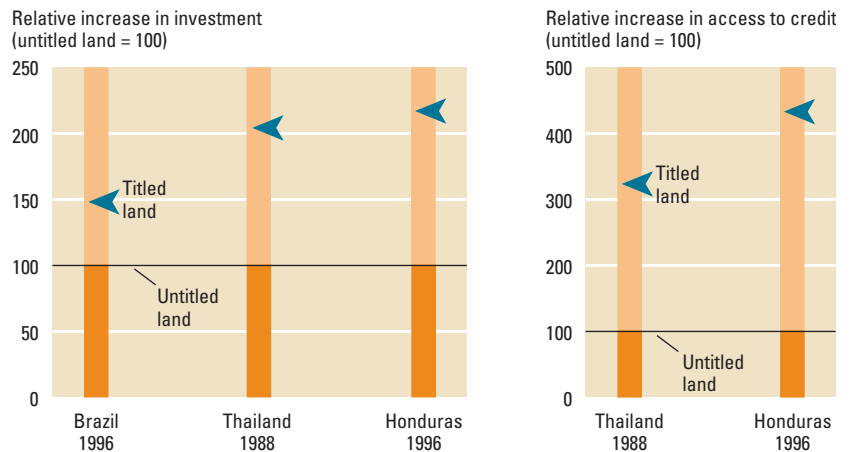
These benefits are observed also in urban contexts. Capitalizing on a natural experiment that allocated land titles to some squatters but not others in a poor suburban area of Buenos Aires, Galiani and Scharrodsky (2004) found significant effects of

titling on housing investment, household size, and school achievement. The quality of houses in titled parcels was higher. Titled households had fewer members (even though their houses were larger), and they seemed to invest more in their children's education. In India, unclear land titles combined with unreliable courts were found to limit the supply of land and discourage investments. Southern states tend to have higher tenure security, which increases the share of modern retailers. Evidence from a massive urban squatter titling program in Peru suggests that titling resulted in more work done outside the home and substitution of adult for child labor.⁵⁵

Formal land titling is one way to provide for secure tenure, but titling takes time and can be expensive. Thailand, the first country with a national program, completed the program this year, 20 years after its inception. One solution is to allow alternatives to conventional private land titles, especially in urban areas.⁵⁶ In Trinidad and Tobago, a 1998 law authorized three incremental levels of statutory security, each requiring additional documentation and commitment from the settler and the government. In one year, an estimated 80 percent of informal settlers on state land had applied for the lowest level.⁵⁷ Because many of these instruments do not require prior physical planning, infrastructure servicing, and surveying of settlements, they can offer widespread coverage at lower costs. The limitations on transfer associated with many of these instruments also check the tendency of some informal dwellers to capitalize land subsidies immediately through land sales.

Several countries have taken steps to require joint titling of land in the names of husband and wife, bolstering women's effective right to land, particularly during their husbands' absences. Vietnam has targets for the joint titling of land as part of the Vietnam Development Goals, incorporated in its Poverty Reduction Strategy. Attention to women's land rights is particularly important when women are the main cultivators, when out-migration is high, when control of productive activities is differentiated by gender, or when high levels of adult

Figure 8.2 Title to land increases investment and access to credit



Source: Feder (2002).

mortality and unclear regulation could undermine a woman's livelihoods in case of her husband's death.⁵⁸

Despite potentially large benefits from titling, there are challenges in urban and rural contexts. In urban areas, access to credit may not increase if banks are unwilling to accept titled shanties in marginal areas as collateral. And where squatters' land is valuable, titling programs can be subverted by powerful interests who use the opportunity to relocate squatters to marginal areas—for example, in Phnom Penh, Cambodia. This does not reflect a problem with titling per se, but suggests that when the urban poor lack voice and governance is weak, titling programs can backfire.⁵⁹ One way to protect squatters from predatory urban developers would be to grant them group land rights as a first step toward individual titles.⁶⁰

Some studies indicate that formal land titles in several African countries did not bring the expected benefits in higher incomes and investment. This may reflect weaknesses in the institutions responsible for registration and recordkeeping and for the adjudication of rights and resolution of conflicts. In some cases, it appears that indigenous tenure was already sufficiently secure.⁶¹ It may thus be more appropriate and more cost-effective to strengthen the security of tenure through institutions that combine legality with social legitimacy. This

BOX 8.7 *Clarifying how customary rights fit with formal systems*

Customary land tenure is created, maintained, and protected by norm-based customary systems at the local level. Rights to land, whether communal or individual, are generally based on family lineage or membership in a particular cultural grouping. Exchanges through sales or rentals are limited to members of the community. Customary systems are dominant in most African countries and in indigenous areas of many Latin American and Asian countries. Having evolved over long periods in response to local conditions, they are often quite flexible. Problems arise when transfers to outsiders become widespread or internal land dispute resolution mechanisms become inadequate.

There have been many efforts to make the transition from collective or customary systems to more individual landholdings. But the transition, if not properly managed, can end in disaster, such as in Kenya. Because the elimination of lineage rights and the legalization of land sales were not accepted by rural populations, conflicts over land, sometimes violent, ensued between those claiming land under customary norms and those seeking to enforce the new rules.

Botswana has had more success. Since 1970, the authorities have gradually strengthened individual rights, starting with the right to exclude other people's animals and to fence arable lands. Common law residential leases for commercially valuable land have been introduced, as have laws allowing the allocation of land to all adult citizens, whether male or female, married or single (Adams 2000 and Toulmin and Quan 2000 in World Bank 2003i). South Africa is

just starting down the road to communal land reform, having recently passed legislation that will transfer state-owned land to communities and create democratic, transparent, and secure property rights regimes in these areas.

Mexico made a hybrid transition from collective land—known as the *ejido* sector—toward more individual landholdings. *Ejidors* are rural communities modeled after a mixture of soviet-style collectives and precolonial indigenous social structures. Reforms in 1992 strengthened the self-governance of *ejidos*, allowing them to choose a property rights regime. Each *ejido* could choose whether land would be held under communal or individual ownership and issue property rights certificates accordingly. By 2001 the program had issued property certificates to more than 3 million households and given secure land rights to more than 1 million households that previously had no formal recognition of occupancy rights (World Bank 2001d).

Clarifying how customary rights—in rural and urban areas—relate to the formal system of property rights protected through modern law is important for millions of people. It is also important for expanding the scope for outside investment, particularly in urban areas. Experience with managing the intersection between the two systems suggests the importance of effective dispute resolution mechanisms and a transparent and well-defined trajectory for transition, with the extension of secure landownership rights to an entire group as an effective and low-cost first step (World Bank 2003i).

approach is particularly pertinent where customary tenure practices predominate. Recognizing customary rights and institutions in the law helps protect large populations that are governed by them and builds a bridge to the formal system (box 8.7). Clearly, the complexities of engaging with customary justice systems outlined earlier in the chapter need to be considered—and when formalizing customary rights, care should be taken not to simply codify existing inequities, particularly for women.

Broadening access by improving the functioning of land markets. Land markets, both in sales and rentals, can in theory do

much to equalize land access. In practice, however, land sales/purchases are generally not an avenue to expand access by the poor and may actually reduce it. High transaction costs, undeveloped credit markets, and high prices for land, reflecting its collateral value and any government subsidies to crops, lead to thin sales markets that keep poor farmers out altogether. This suggests that land sales markets will not contribute to greater equity in landholdings, especially in settings characterized by long-standing discrimination against specific groups, unless the government relieves the savings constraints of the poor through subsidies (as we will see in the next section).⁶²

Distress sales of land by the poor can occur in risky environments where small landowners do not have access to insurance. Thus, they are unable to smooth consumption through mechanisms other than land sales, such as safety nets.⁶³ In a comparison of land transactions in Indian and Bangladeshi villages during 1960–80, Cain (1981) found that poor farmers who had access to safety net programs used the land market to augment their landholdings and undertook productivity-enhancing investment. Distress sales to obtain food and medicine predominated when safety nets were absent.

While government interventions to impose restrictions on the transferability of land can undermine investment incentives and depress off-farm activity, they can play a role, especially during periods of transition. In many Commonwealth of Independent States (CIS) countries the unrestricted transferability of land led to a concentration of landholdings in the hands of a small number of farm bosses, as poorer rural households were enticed to sell their land in conditions of uncertainty and incomplete markets and information.⁶⁴ Initially limiting the transferability of land to lease transactions rather than outright sales would have been better.

A gradual transition may be preferable in cases in which an equitable distribution of land has been the primary instrument of social protection, as in China and Vietnam. Governments in both countries rightly perceive the tensions in active land sales markets, which could lead to efficiency-enhancing

consolidation but also run the risk of increasing the number of landless poor. In China, the government is considering moving on several fronts, including developing safety nets and rural finance and eliminating residency-based restrictions (*hukou*) on labor mobility.

While land sales markets have ambiguous impacts on equity, the equity case for broadening access to land rentals appears more clear-cut. When farmers do not have access to credit that would enable them to purchase land outright, rental markets are an important avenue for enhancing productivity and equity by facilitating low-cost transfers of land to more productive producers (chapter 5). Rental markets also enable landholders with low agricultural skills (or no desire to farm) to seek employment in the nonfarm sector while still earning a return on their land.⁶⁵ Evidence from Sudan suggests that land rental markets do transfer land to smaller producers. And in Colombia, rental markets have been more effective than government-sponsored land reforms in bringing land to productive and poor producers.⁶⁶

If land rental markets have so much potential to improve equity and efficiency, why is there such a large variation in the incidence of rentals across countries? One reason is a lack of tenure security—or trust that the security will last. Without it, landlords are unwilling to rent out their land for fear that they will not be able to reclaim it. Other reasons include current or past government interventions to restrict tenancy, the availability of reliable conflict resolution mechanisms, and imperfections in information.⁶⁷ While concern about exploitation in sharecropping arrangements may be justified,⁶⁸ tenant protection and rent ceilings can backfire. Such restrictions on land rentals often push transactions into informality or lock poor farmers into less efficient and less equitable wage-labor arrangements. Estimates indicate that new tenancy legislation in India was associated with the eviction of more than 100 million tenants, causing the rural poor to lose access to about 30 percent of the total operated area.⁶⁹ Interventions to enhance the bargaining power of the poor—including better access to financial

markets, off-farm employment opportunities, and equitable contract enforcement mechanisms—are likely to be preferable.

Well-functioning rental markets can be a rung in the ownership ladder, but they probably are not in circumstances of extreme inequality in landownership and power. In these instances, options for directly redistributive policies need to be exploited.

Options for cost-effective land redistribution to broaden access

Improving tenure security and promoting land rental markets are good for both equity and efficiency. Analysis and experience indicate that land redistribution is not nearly as straightforward. It can be costly in program resources and reduced productivity, and it can be an instrument of political patronage. Substantial personnel and financial resources are necessary to assess and purchase (or expropriate) land, select beneficiaries, and supply training and credit.

When does land redistribution make sense? In some countries, redistribution could be a necessary political step to address historical inequities and stave off violence. In others, it could simply be a tool to shift underused land to more productive uses while enhancing equity. In countries where state landownership is high, land redistribution could involve limited budgetary costs if bundled into a one-time transfer of state land to private ownership. Conversely, in countries with strong traditions of tenure security, just the threat of redistribution could undermine investment.

The feasibility of land redistribution also depends on the instrument. Expropriation is likely to be the most disruptive. Divesting state lands and recuperating illegal settlements may be two cost-effective alternatives. For example, the mayor of Brasilia (Brazil) identified lands with uncertain titles and negotiated the surrender of part of those lands. In exchange, official titles were granted to the remaining areas. Expropriating with compensation and assisting land purchases and rentals—for example, through community-driven land reform—are also feasible alternatives. Subsidizing land purchases can be costly, however, because land is often overpriced relative to its income generation

potential from productive use (reflecting its speculative, insurance, and status value). Also, subsidies are difficult to justify if the current pattern of landownership is not considered legitimate.⁷⁰

Market- or community-driven land reforms are a potential option. The reforms tend to be decentralized and transparent, allowing community members to obtain resources for land access. They can be flexible, allowing for land rental or purchase according to the willing-buyer-willing-seller principle. Community-driven land reforms often give beneficiaries full property rights and involve coordination between local government and NGOs to provide access to training, technology, and credit. A community-driven approach has been tried in several countries, including Brazil, Columbia, Guatemala, Honduras, India, Malawi, and South Africa. But the programs are relatively new, so rigorous impact evaluations are not yet available.

A land tax, possibly combined with an output tax, can be an important complement. It can generate revenues to purchase land to redistribute or encourage redistribution by disproportionately taxing large landholders or owners of unused or underused land, both rural and urban (box 8.8).

Regardless of the instrument, common lessons can be drawn from previous attempts at land redistribution.

- *Complementary investments—training and credit.* Evidence from Latin America⁷¹ and Africa indicates that simply redistrib-

uting land does little. Beneficiaries must be provided with a package of assistance to ensure self-sufficiency and maximize productivity. The right package will vary by country but could include training and credit. Technical assistance, such as help elaborating farm plans and crop budgets or instruction on new technologies, can be a success factor for subsistence farmers and those who lack commercial farming expertise. Credit can allow beneficiaries to make productivity-enhancing investments, for example in irrigation, fencing, tools, or draft animals.

- *Beneficiary selection and targeting.* When beneficiary selection is politicized, redistributed land will not always go to the most needy and capable farmers. The solution is to have transparent rules that allow communities to understand exactly how and why each beneficiary was chosen. Self-targeting—where potential beneficiaries seek out land for sale at low cost and then apply for grants and/or loans—can also be effective.
- *Tenure security.* Those who gain access to redistributed land should be given clear ownership rights. In some instances, it may be enough to have less than full ownership (such as a certificate of control or long-term lease) to reduce uncertainty, encourage investment, and promote the benefits discussed above.

Providing infrastructure equitably

Infrastructure in most developing countries is characterized by low and unequal provision—about 2 people of every 10 in the developing world were without access to safe water in 2000, 5 of 10 lived without adequate sanitation, and 9 of 10 lived without their wastewater being treated⁷²—with many families suffering from inadequate access especially in rural areas.

Economic opportunities are strongly shaped by access to infrastructure. Much infrastructure is traditionally government provided and so is driven by the political process. Financing constraints and technical design challenges are very real but perhaps easier to overcome. When more equal voice

BOX 8.8 Land and output tax combinations

Taxes on land can be an effective, nondistortionary tool for collecting local revenue and facilitating land redistribution. They can also encourage productive land usage by taxing underused land at higher rates. This can be attractive when large unproductive plots of land (often held for speculative reasons) create artificially high land prices and limit land access for poor farmers. But administering a tax on land requires data on the size, value, ownership status, productive capacity, and output of each plot. Because it is hard for the government to measure the actual degree of land use, especially for large landholders, there is a strong incentive for tax evasion.

One way to limit evasion by large landholders is to use a mix of land taxes and a value-added tax (VAT). A VAT can have much lower rates of evasion and facilitate accurate reporting of cultivation levels. Knowledge of true cultivation levels would then limit the scope for overreporting the degree of land use to evade higher tax rates for underused land. In the absence of insurance markets, a mix of VAT and land taxes can also reduce the risk facing smallholders because tax burdens would be correlated with output fluctuations.

Sources: Assunção and Moreira (2001), World Bank (2003i).

or the political interests of the governing regime make for more broadly accountable policies, infrastructure is provided in ways that are supportive of the economic interests of poorer groups—for example, in East Asia’s intensification of irrigation and transport (see focus 4 on Indonesia). In more unequal societies, those without influence receive less and lower-quality access to public services—this often means the poor. This inequitable access also applies to remote regions and excluded groups, and sometimes it has a gender dimension. Even worse, some infrastructure services (utilities especially) often become instruments of patronage and riddled with problems of inefficient provision and corrupt practices.

As in the case for land, more equal access to infrastructure would be good for equity and will often be good for growth. This requires addressing difficult financing issues, constraints that limit the poor’s ability to access infrastructure, and major accountability issues through institutional designs that support more equitable response to needs.

More equitable access to infrastructure is good for growth and equity

There is solid evidence that infrastructure investments broaden opportunities for people and communities by integrating them into regional and national systems of production and commerce, and by improving their access to public services. Location strongly influences household market participation in Vietnam. And households with the same characteristics and endowments yield different returns in different geographic settings in parts of rural China.⁷³ Leipziger and others (2003), based on a sample of 73 countries, find that a 10 percent improvement in a country’s infrastructure index is associated with a 5 percent reduction in child mortality, a 3.5 percent reduction in infant mortality, and a 7.8 percent reduction in maternal mortality, controlling for incomes and the availability of health services. Microevidence from rural India lends support to these cross-country findings: the prevalence and duration of diarrhea among children under five are significantly lower for families with piped water.⁷⁴

Investments in basic water and energy infrastructure can improve gender equity. Around the world, the burden of gathering and transporting fuelwood and water traditionally falls on women and girls. In Ghana, Tanzania, and Zambia women account for two-thirds of all household time devoted to water and fuel collection, while children—mostly girls—account for between 5 and 28 percent of time spent on these activities. In rural Morocco, having wells or piped water increases the probability that both girls and boys will enroll in school, with larger impacts for girls, who are responsible for collecting water. Studies in Pakistan show that poor access to firewood and water in rural areas means that women work longer hours and have less time for income-generating activities, with impacts on the intrahousehold balance of power. Women and children are also more subject to health risks from indoor air pollution, given the disproportionate amount of time spent inside the home. Electricity in the home can reduce the need to burn polluting fuels for light and cooking. And improvements in electricity and gas distribution can eliminate time spent collecting traditional fuels.⁷⁵

Improving rural transport infrastructure can reduce transactions costs, expand access to markets, and improve rural incomes. It is estimated that nearly two-thirds of African farmers are effectively insulated from national and world markets because of poor market access.⁷⁶ In contrast, substantial investments in Indonesian roads over the last three decades have allowed poor households to successfully enter the market economy.⁷⁷ And many of the roads were built as labor intensive public works, making jobs available to unskilled labor. Similarly, investments in rural infrastructure (roads, bridges, culverts, and marketplaces) in Bangladesh have deepened the vibrancy of the rural economy for both agriculture and non-agriculture. Investing in rural roads is an example of how expanding access to infrastructure can benefit equity and efficiency in the long run, especially in areas with large numbers of poor people and agro-climatic potential.⁷⁸

BOX 8.9 *Lagging infrastructure in Africa*

Infrastructure development in Africa is abysmal, lagging behind the rest of the world in terms of quantity, quality, cost, and equality of access. Only 16 percent of roads are paved, the average waiting time for a telephone connection is three and half years, transport costs are the highest of any region, and fewer than one in five Africans has access to electricity. What can explain this tremendous underdevelopment?

- *Difficult geography and complex history.* Distance from major markets, the Sahara Desert, a shortage of natural ports, and vast tracts of landlocked areas all increase transport costs. Infrastructure development during colonial times focused on building transportation from resource sites to a port. And the postcolonial division of Africa into many small states drives up transport and energy costs, with cumbersome border crossings, little regional cooperation on water and power projects, and incompatible rail systems, among other factors.
- *Financing constraints.* Lack of investment has led to a deterioration in infrastructure, especially road transport. For instance, in nine East African countries, maintenance spending could cover only 20 percent of current networks. Lack of disposable income means low demand for infrastructure, and small and

scattered populations make economies of scale difficult and require higher investments. Widespread subsidies that go to the relatively wealthy (the poor generally do not have connections to networked utilities) undermine governments' ability to expand access.

- *Bad policies and poor accountability.* Licensing, competition barriers, and corruption also impede affordable infrastructure provision.

Despite the difficult geographic and structural factors, there are opportunities to improve Africa's infrastructure. One necessary step is to boost investment, especially in rehabilitation and maintenance. Higher public investment will be needed. Private participation can help finance some investments and increase efficiency, but it is unlikely to solve Africa's infrastructure problem. A sound institutional and policy environment is required to attract fresh investment and use it effectively.

Macroeconomic stability, freedom to repatriate capital, competitive taxes, contract enforcement, low corruption, and adherence to transparent rules are all important to private investors, especially given the long payback periods of many infrastructure investments. In contexts in which policies are sensible but foreign private investment is hard to attract, foreign aid can provide both financing for pub-

lic provision and guarantees to help foster private participation. Prudent oversight, regulation, and contract design can also ensure that public and private financing are equitably and efficiently used.

Increasing cross-border and regional cooperation is one way to make African infrastructure more affordable. Streamlined border crossings and improved road and rail links would reduce transport costs. Trade in power and water resources could significantly cut costs as well. For example, it is estimated that South Africa could save \$80 million a year in operating costs by exchanging electricity with its neighbors (Masters, Sparrow, and Bowen 1999). Seeking innovative ways to broaden access is also needed. Mozambique has tested a promising approach: the government set up utility companies using diesel generators in rural areas and then sold them to private investors below cost for continuing commercial operation. Grants from government, NGOs, or donors for community-driven infrastructure projects are another possibility. Regardless of the approach, community and user involvement in infrastructure construction, maintenance, and management is one of the most effective ways to expand access in rural areas.

Source: World Bank (2000a).

Is privatization the answer?

What accounts for the failure of infrastructure services to serve poor people, especially in Africa (box 8.9)? Beyond the important role played by historical and geographic contexts, there are major financing constraints and governance challenges. In most developing countries, the public sector is fiscally strapped—public investment in infrastructure in Latin America dropped from 3 percent of GDP in 1980 to less than 1 percent in 2001⁷⁹—and public spending requires taxes, which can exert a drag on efficiency and can mean forgone investments in other areas. Local financial markets are generally not sufficiently developed to intermediate private savings into long-term, risky infrastructure investments (and, in any case, private savings are often not large). Foreign private capital is interested generally in large markets and even then only when risks (including policy and exchange rate risks) are acceptable. State-owned infrastructure companies in many countries—especially when political inequal-

ities are large—are often inefficient and become instruments of patronage.

The 1990s were characterized by a massive policy redirection toward private participation in infrastructure—reflecting the disappointment with ineffective state-operated utilities, the promise of private funding, and the greater flexibility offered by technological change and regulatory innovation.⁸⁰ But the privatization wave bypassed many developing countries—Sub-Saharan Africa received only 3 percent of total private infrastructure investment in developing countries between 1995 and 2000⁸¹—and even where private capital became the dominant source of investment (as in Latin America in the mid-1990s when private investment was 2.5 percent of GDP), the results for equity were mixed. There were many cases of privatization in which access for the poor improved, especially when competition reduced political capture, but evidence suggests that private operators also focused on wealthier segments of the population (box 8.10).

BOX 8.10 *The distributional impact of infrastructure privatization in Latin America: a mixed bag*

Private participation in infrastructure increased dramatically in Latin America during the late 1990s. It went from \$21 billion in 1995 to a peak of \$80 billion in 1998, dropping back to \$20 billion by 2002 (World Bank 2004f). The distributional impact of private investment depends on how efficiency gains are allocated between public and private interests. In the best cases, privatization can solve patronage problems and lead to greater efficiency and equity. In worse cases, efficiency gains can be shared between government and private operators, or go primarily to the private sector and lead to the consolidation of private monopoly power (as in Mexican telecommunications). The outcome depends on the market and accountability structure, including the effectiveness of regulation. Evidence from Latin America shows that privatizations fall into each of these categories, yielding mixed results for affordable access by the poor.

Research from Argentina, Bolivia, Mexico, and Nicaragua shows that utility privatization increased access and enhanced service quality for poor consumers in some cases (McKenzie and Mookherjee 2003). In Chile, access to power services increased greatly for low-income groups during the first 10 years of private operation (Estache, Gómez-Lobo, and Leipziger 2001). In Colombia, private utilities have connected more of the poorest consumers than their public counterparts (World Bank 2001a). Other research shows that child mortality caused by waterborne diseases fell by 5 to 9 percent in the 30 Argentine locales where water services were privatized, with the strongest benefit—a more than 25 percent decline in mortality—occurring in the poorest neighborhoods (Galiani, Gertler, and Schargrodsky 2002).

Despite the increases in access, there are two reasons why privatization may have had adverse effects on the poor through higher tariffs and connection costs. First, privatization can reduce the scope for cross-regional subsidies. One study (Campos and others 2003) showed that the fiscal cost of utilities increased a few years after privatization. This was the result of “cream-skimming,” as observed in Argentina. In some of the provinces of Argentina, the water concessions were for the large cities only, leaving the responsibility for the small cities and rural areas to the governments. Because the big cities were cross-subsidizing the other regions under public provision, privatization reduced this source of funding and increased the net fiscal costs once the transaction payoffs from privatization had disappeared.

Second, connection costs and tariffs were adjusted to cost-recovery levels following privatization, leading in many instances to higher prices. In the early 1990s, public utilities in developing countries subsidized an average of 20 percent of gas and 70 percent of water costs (World Bank 1994). So when subsidies were cut, services often became too expensive for poor consumers. For the water concession in Buenos Aires, the initial connection charge was set so high that many users could not afford it (Estache, Foster, and Wodon 2001), which was an issue at the center of one of the first major adjustments to the contract (Ugaz and Price 2003). The telecommunications sector in Argentina also saw price increases following privatization, largely to rebalance local and long distance charges. But price increases are not the norm—competition can drive them down. In

Chile, the liberalization of the telecommunications market in 1994 reduced call prices by more than 50 percent. In Argentina, thanks to the entry of 21 new operators in the generation sector, residential electricity customers enjoyed a 40 percent drop in tariffs in the five years after privatization (1992–97) (World Bank 2002b). Ultimately, price changes depend on initial conditions, quality improvements, and regulatory and institutional frameworks that determine profits.

Episodes of privatization can be opportunities to strengthen accountability. They can generate public discussion about the current state of service delivery, the options for reform, the terms of the contract, and the tradeoffs under consideration. Such occasions can be powerful in overcoming collective action problems and mobilizing consumers to express their interests. But there is also the danger that, in the absence of the voice of consumers, the process of privatization may be captured by narrow interests with political connections and better information. Indeed, that might be one reason why the public perception of privatization in Latin America is so negative.⁸² There is evidence that privatization has been associated with increased power for conglomerates and their foreign partners—and with higher profits in noncompetitive sectors. Accusations of corruption during the privatization process, concentrated gains by a few actors (whether made legally or illegally) contrasted with worker layoffs, and unrealistic customer expectations regarding service levels (driven by politicians overselling the promise of privatization) are also probably to blame for privatization’s negative public image (De Ferranti and others 2004).

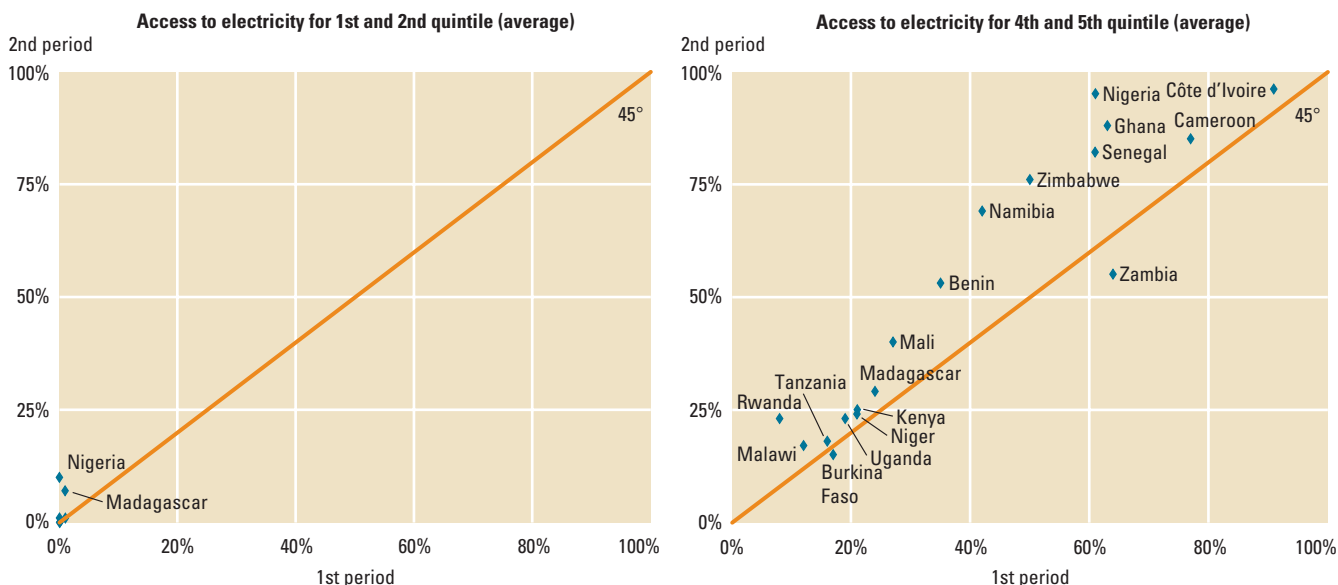
In the end, experience suggests that privatization alone is not the answer. Whether infrastructure services are provided by private operators or public utilities seems less important for equity and efficiency than specific measures to improve access for the poor, the structure of incentives facing providers, and provider accountability to the general public.

Expanding access and making services affordable

Whether expanding general access benefits the poor depends on initial levels of coverage. In many African countries, overall access rates improved over the last decade, but the bottom 40 percent of the population registered no gains at all (figure 8.3). This is not

surprising. Given the low initial coverage in many of these countries, the expansion favored wealthier households. This does not mean, however, that expanding access when overall levels of service provision are low is bad for equity. On the contrary—better to expand access in this case than to focus on upgrading quality, which would benefit only the few who already have access.

To expand access to the poor, policymakers can set service obligations or create incentives for providers. One way is to specify universal service obligations, which is common in the telecommunications sector.⁸³ While this is a worthy social objective, it may not be practical in the short run when starting from low access rates. That is why service obligations should include details on

Figure 8.3 Poor families did not benefit from an expansion of access in Africa

Source: Diallo and Wodon (2005).

Note: First and last observation dates vary for each country. The first observation is in the early to mid-1990s and the last in the late 1990s or early 2000s. The average time between observations is seven years.

time frames and ways to finance the obligation when customers are unable to pay. Defining connection targets is another way to promote access. Targets are easy to monitor and can be enforced by financial penalties. Of course, connection targets can be met only if customers are able and willing to take up the service—and this depends on their ability to overcome impediments, including title requirements and income and liquidity constraints (given the lumpiness of connection charges).

In many countries, new connections are subsidized to meet access objectives and keep providers solvent. New connections can be subsidized from charges to existing users, particularly if the group of existing users is much larger and wealthier than potential new users. The water and sanitation concessionaire in Buenos Aires adopted this type of cross-subsidy after renegotiating an initial contract that charged onerous connection fees to the poor. Government financing for connection subsidies is also an option, as is offering credit to consumers for connection purchases. In Colombia, the law requires that connection charges for poor customers be spread over at least three years.⁸⁴

A complement to connection subsidies are consumption subsidies, either through means-tested transfers financed out of general tax revenues or through lifeline tariffs. Subsidized lifeline tariffs require a transfer from those with high levels of consumption to those with low levels.⁸⁵ When considering lifeline subsidies, care must be taken to set a threshold that is high enough to garner political support, yet low enough that the poor are the primary beneficiaries. For instance, evidence from Honduras suggests that their electricity subsidy is too high—83.5 percent of residential customers benefit from the subsidy (those consuming under 300 kWh monthly). Means-tested vouchers for purchasing services are another subsidy option. They are similar to means-tested tariff subsidies with added flexibility for the user to select a service provider.⁸⁶

Given the liquidity constraints of the poor and the possible seasonality of use and income, introducing flexibility in payment is likely to help expand access. Increasing the frequency of billing is one such option. Prepayment devices, which facilitate budgeting for low-income households, are another. On the downside, prepayment could lead to frequent “self-disconnection.”

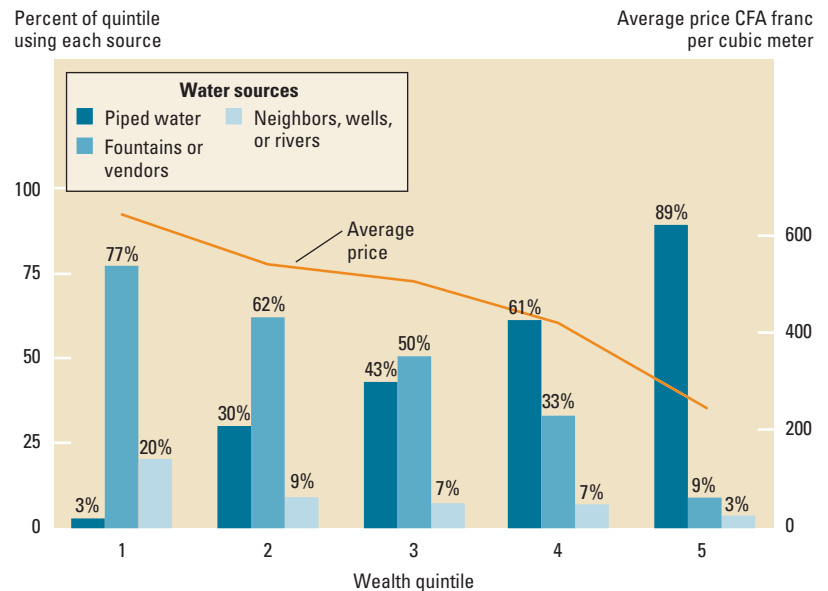
Utilities could also allow customers to choose from a menu of tariffs with different combinations of fixed (standing) and variable charges. Allowing lower fixed charges in exchange for slightly higher variable ones could benefit smaller consumers.⁸⁷

Enabling consumers to make certain quality-price tradeoffs by encouraging lower-quality services is also likely to be beneficial. This can be done by allowing lower standards of formal provisioning in certain poor areas or by encouraging a vibrant network of informal providers that can either operate independently or through subcontracting arrangements with the formal provider.

Water service provides an example. A study using data from 47 countries shows that informal providers such as point-source vendors (kiosks) and mobile distributors (such as tanker trucks and carters) systematically charge more than networked providers, both public and private.⁸⁸ Micro-economic evidence supports this. In Niger, for example, wealthier households are more likely to use networked rather than informal providers and pay less per unit consumed (figure 8.4). But informal providers can offer a valuable service, because many poor users cannot afford connection charges or monthly lump-sum bills or live in areas inaccessible to utilities for legal or technical reasons. Recognizing that private connections for all households may not be a feasible goal in the near term, governments and utilities can work with informal providers. For instance, kiosk services could be improved by subsidizing kiosk connections, increasing competition among kiosks, and introducing performance measures and quality standards.⁸⁹ In Senegal, one study argues for directing subsidies away from private connections toward water provided at standposts or by other informal providers (box 8.11).

High tariffs for the consumer reflect the pricing decisions of the utilities concerned and the taxation decisions of local and central governments. Avoiding exclusivity in contracts and liberalizing entry, including through the participation of independent private providers or communities in non-network services, can help reduce costs.

Figure 8.4 Poorer households have lower-quality water and pay more in Niger



Source: Bardasi and Wodon (2004).

BOX 8.11 *The pro-poor agenda for urban water in Senegal*

In 1995, the government of Senegal launched sweeping reforms in the urban water sector. The bankrupt public sector utility was dissolved. A new state asset-holding company was created to manage the sector. And a private operator was contracted to run the system based on an international competitive bidding process. The reform had positive outcomes for the poor, thanks to strong government commitment, connection subsidies in low-income neighborhoods, and well-designed operator incentives. But tariff inequities and poor targeting of subsidies remain.

Subsidies targeted at the poor take three forms: consumption subsidies, connection subsidies, and construction of standposts in areas lacking private connections. In Senegal, consumption subsidies are delivered through an increasing block tariff with a low "social tariff" for household consumption under 10 m³ per month. The problem with consumption subsidies is that many poor families do not

have a connection at all or share a connection with several other families, which bumps them into a higher consumption block.

Connection subsidies have benefited the poor, but those who could benefit most are likely to be ineligible because they lack title to their land and an established house. The construction of public standposts has expanded access but does not necessarily provide the lowest-cost water. Tariffs on water sold to licensed standpost vendors are considerably higher than the subsidized social tariff and vendors also charge an overhead fee. Analysis of one NGO-run standpost showed that users were paying 350 percent more than the social tariff rate. Given these shortcomings, it would make more sense to direct consumption subsidies away from private connections and into water provided at standposts or by other informal providers who serve the poorest.

Source: Brocklehurst and Janssens (2004).

Moreover, many governments view utilities and telecommunications as cash cows, imposing indirect consumption taxes that tend to be regressive where connectivity to the formal system is high. In Argentina, utilities generate about 1 percent of tax revenue; in addition to the income tax, there is

a 21 percent VAT plus municipal and provincial taxes. So indirect taxes can be as high as 55 percent in some municipalities. Reducing such taxes would reduce tariffs.⁹⁰

Naturally, benefits can be lower and costs higher for investments in poor, remote areas that are short on economic potential. This analysis is not blind to those considerations, but also it recognizes the argument that there can be long-run benefits from greater inclusion of groups that are marginalized because of location or poverty (see focus 6 on regional inequality).

Strengthening governance, voice, and accountability

Infrastructure provision suffers from severe problems of corruption and lack of accountability. Because infrastructure investments are typically large and lumpy, and often exhibit increasing returns to scale or network externalities, they are less amenable to competition in financing and provision and generate significant scope for corruption and patronage. Politicians bribe public utility officials and pursue political goals by transferring resources to politically influential groups, rather than encouraging utilities to expand service and cut costs.

One possible solution is to subject utilities to performance pressures and reduce politicians' willingness or ability to use them for political purposes.⁹¹ The prudent use of

regulation is another way to strengthen accountability and reduce political capture and corruption. Regulators have a key role in ensuring that the public interest is being served. This includes safeguarding the value of public assets, upholding the sectoral norms relating to health and safety, providing information about the performance of the service provider, and enforcing compliance with contractual obligations.

If effective, regulation will have an important impact on efficiency and equity. Evidence comes from a study of the energy, telecommunications, and water sectors in Argentina that separated the benefits of privatization from those of effective regulation. The study found that effective regulation yielded operational gains more than one-third higher than the gains from privatization alone and equivalent to 0.35 percent of GDP, or 16 percent of the average expenditure on utility services. Gains for the lowest quintiles were proportionately higher. Another study of 1,000 concessions in Latin America found that even a moderately well-functioning regulator can temper opportunistic renegotiation of contracts. It concluded that the probability of renegotiation goes from 17 percent in a setting in which a regulatory body exists to 60 percent in settings it does not.⁹²

Positive impacts of regulation are conditioned on the ability to insulate regulators somewhat from pressures coming from politicians and providers. Measures to strengthen the independence of the regulator are paramount, and this may require a separate agency with reliable and ring-fenced funding and staffing. When assets are decentralized, the regulatory agency can be at the level of the central or regional government. In short, regulators should be subject to substantive and procedural requirements that ensure integrity, independence, transparency, and accountability (box 8.12).

In situations in which local provision is more susceptible to capture by local elites, the central government can influence local outcomes by using fiscal incentives to nudge local governments toward broader access and by reducing costs for the poor through contingent intergovernmental transfers. This

BOX 8.12 *Addressing accountability and transparency in telecommunications in Brazil and Peru*

Brazil's National Telecommunications Regulatory Agency has a Web site that provides information on service price comparisons, laws, and operator compliance. Its Advisory Council (with civil society representatives) assesses the agency's annual reports and publishes the findings in the official gazette and on the Web. And an ombudsperson evaluates the agency's performance every two years. In 2000, it became the world's first telecommunications regulator to receive ISO-9001 certification, an international standard for meeting customers' technical needs.

Peru has made similar progress in improving regulation by increasing transparency. The Supervisory Authority for Private Investment in Telecommunications

sets prices, ensures a competitive market, and monitors compliance with concession contracts and quality standards. The agency sets norms through a transparent process. Regulatory proposals must be supported by assessments of welfare benefits and best practices, published in the official gazette, and undergo a 30-day consultation period. Some proposals also are subject to public hearings. In addition, the agency has multiple dispute resolution mechanisms. Independent committees, supported by experts, resolve disputes among service providers and an internal tribunal handles consumer complaints not satisfactorily managed by phone companies.

Source: World Bank (2004).

requires setting performance targets, eliciting competition among local governments, and benchmarking to monitor performance. It also requires sufficient policy autonomy at the local level to meet the specified targets.

Monitoring the performance of providers requires reliable information and performance benchmarks. This is more easily done when there is a management contract or a concession agreement with clear service obligations or when there are performance contracts with similar features for public utilities. Community involvement can help monitor compliance. A national regulator can benchmark local government performance when infrastructure assets and policy decisions are decentralized and provide useful information for intergovernmental fiscal transfers.

Summary

Justice systems can do much to level the playing field in the political, economic, and sociocultural domains, especially when societies press for equitable laws and for transparency and accountability in their implementation. Legal institutions can uphold the political rights of citizens and curb the capture of the state by the elite. They can equalize economic opportunities by protecting property rights for all and ensuring nondiscrimination in the market. They can force change in the social domain by challenging inequitable practices. But

justice systems and legal institutions, embedded as they are in the political and socioeconomic structure of societies, can be hijacked by special interests.

Broadening access to land can enhance people's opportunities to engage in productive activities. The distribution of land rights, especially ownership rights, is skewed in many countries, and challenging this pattern is difficult. Past land reform efforts show the need for a broader menu of policies that go beyond redistribution through expropriation and include improvements to tenure security and the functioning of rental markets. There is also scope for redistribution through channels other than expropriation.

More equitable access to infrastructure also has equity and efficiency benefits. Broadening access to infrastructure brings people closer to markets and services and to the power and water they need for productive activities and daily existence, expanding their economic opportunities. Expanding affordable access for poor people and poor areas requires tackling difficult financing issues, designing subsidies effectively, working with informal providers, as well as making providers more accountable and strengthening the voice of beneficiaries. The challenges of expanding access to justice, land, and infrastructure and rooting out corruption and elite capture remain significant for many developing countries.

Raising revenues for equitable policies

The publicly-provided, equity-enhancing programs outlined in this report, from early childhood development interventions to water supply, have to be financed. The resources to fund them must generally be raised through taxation. In fact, a key ingredient for a well-functioning public sector is a societal understanding that the quality of public services depends on everyone paying their share of the tax burden. Where this perception fails, the social compact breaks down, and tax avoidance and evasion become widespread. This leads to a vicious circle of free-riding and tax rate increases, with adverse consequences for the public finances, the quality of service delivery, and social cohesion.

It follows that the same institutions that influence the quality and breadth of service delivery also affect the overall tax effort. Revenues, like spending, increase with a country's level of income, but the quality of institutions—notably voice and accountability—also matters, even when controlling for income¹ (see figure S5.1). Voice and accountability can strengthen the tax effort, as the services provided become a reflection of the desires of the broader electorate rather than of a privileged few. Lindert (2004) argues that the expansion of voice in twentieth-century Europe was the driving force behind fashioning the social compact that delivered high and equitable growth alongside extensive public provi-

sion of services during 1950–80. In Chile and the Republic of Korea, too, the emergence of representative institutions (and higher incomes and administrative capacity) led to higher taxation and spending.

For similar reasons, high inequality in the distribution of political power and wealth may be prejudicial to the tax effort. The low tax revenues in most of Central America may reflect the low solidarity of the elite with middle- and lower-income groups: the small, wealthiest segment of the population is unwilling to pay more in taxes to provide public services, because the elite can procure many private substitutes for publicly-provided services, ranging from public safety to education and roads.²

Resource rents can relieve the fiscal constraint on spending and in principle provide resources for equitable provision, though they raise a host of governance challenges. The ability of resource-rich states to rely on “unearned” revenues can undermine the accountability embedded in the social compact underpinning sound public finance.³ If not properly addressed, the result may be wasted natural resources, corrupt state institutions, and poorer prospects for long-run growth and equity. A few recent efforts to harness resource rents for broad-based development in countries with poor institutions aim to introduce greater transparency and accountability (see box on next page).

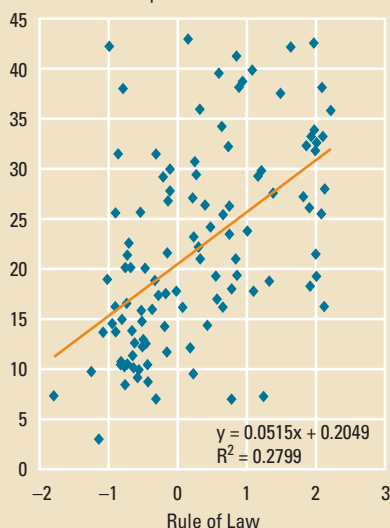
Foreign aid can also weaken the social

compact, in much the same way as resource revenues, by making governments less beholden to civic interests.⁴ Some evidence suggests that higher levels of aid are associated with lower revenue collection, especially among poorly governed countries.⁵ Donors should thus consider ways of supporting accountable institutions in recipient countries—both for spending and taxation (see chapter 10 for discussion of aid).

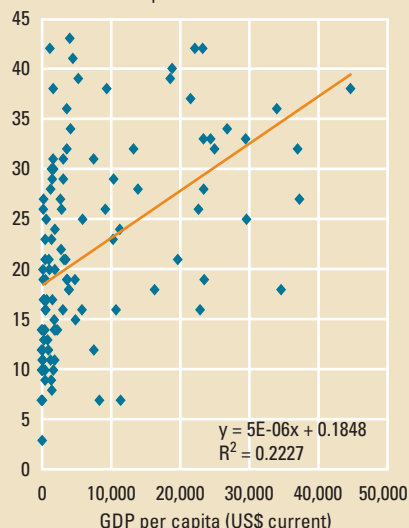
While institutional transparency and accountability and linking good public services to the taxes that fund them are probably the first-order determinants of successful revenue-raising, technical aspects of public finance are important to reduce efficiency costs. Lindert (2004) argues that among industrial countries, high social benefit/high tax societies—most notably Scandinavia—have paid particular attention to tax design to reduce adverse incentive effects for labor effort and capital investment to sustain growth. Tax design is an immense area. From the perspective of equity, the primary contribution of taxation is in providing the resources to fund equity-enhancing spending. For this, the principal criteria are minimizing efficiency costs, administrative feasibility, and political supportability. For specific tax instruments, there can also be potential for positive direct effects on equity. Here we suggest seven basic principles for mobilizing tax revenues in ways that minimize efficiency costs, while not undermining equity.⁶

Fiscal effort increases with income and the quality of institutions

Tax revenue as a percent of GDP



Tax revenue as a percent of GDP



Source: Authors' calculations based on Kaufmann, Kraay, and Mastruzzi (2005).

1. Tax bases should be as broad as possible.

A broad-based consumption tax, for example, will still discourage labor supply on the margin, but choices between tradable and nontradable goods and services will not be distorted, if all are taxed at the same rate. A few items (such as gasoline, tobacco products, and alcohol) may be chosen for higher tax rates, because of their negative spillover effects or because the demand for these products is relatively unresponsive to taxation. As a result, at any given tax rate, efficiency costs will be relatively low and revenues relatively high. Income tax bases should also be broad, treating all incomes, from every source, as uniformly as possible.

2. Tax rates should be as low as possible (as long as they raise sufficient revenue to finance the appropriate expenditures of government). Of course, the broader the

base, the lower the rate needed to generate a given revenue level. Lower rates lower the efficiency costs. The general rule is that the distorting effect of taxes increases proportionally to the square of the tax rate, so halving the tax rate implies a fourfold increase in efficiency. From an efficiency perspective, it is better to impose a single rate on a broad base of taxpayers, rather than dividing that base into segments and imposing different rates on each one. This needs to be balanced against the distributional argument for graduated rate schedules.

3. *Keep indirect taxes from being regressive.* With a few key exemptions, value-added taxes (VAT) can be made less regressive. Bird and Miller (1989) show in Jamaica that exempting just five specific items from VAT halves the burden on the poorest 40 percent of the population. Reducing regressive excise taxes (as well as import duties), on food or kerosene is also desirable. To make up for lost revenue from any of these measures, there are often good reasons for higher taxes on private transport. Export taxes are generally best avoided, both on efficiency and on equity grounds.
4. *Raise personal income tax collections.* Collection from personal income taxes is

low in developing countries. But in the light of the second point, higher revenues should be sought first by closing loopholes and enforcing greater compliance, and only later through higher marginal rates. Income taxes need to apply to persons and to corporations. To keep tax avoidance in check, the top marginal rate of the personal income tax should be fairly close to the rate of the corporate income tax, which means that the rate is not likely to be all that high.

5. *Use property taxes more.* Property taxes account for only a small share of taxes in developing countries. Their coverage is typically not comprehensive, and assessments and collection rates are low. Although nominal rates are also low, governments usually find rate increases in this very visible tax difficult to sell politically. Simply raising the tax rate usually would burden only the few actually paying taxes. Higher nominal rates are likely to be acceptable only with better tax administration, such as more comprehensive coverage, better and more frequently evaluated assessments, and enforced penalties for late payment.⁷
6. *Consider inheritance taxes.* Because heirs have not earned the wealth, taxing gifts,

estates, and inheritances are consistent with this report's notion that predetermined circumstances should not affect a person's life chances.⁸ The efficiency arguments and the evidence are mixed: parents may work more or less to avoid inheritance taxes, and so may save more or less. Although inheritance taxes may be difficult to collect and are likely to represent only a modest reduction in wealth concentration, they may help prevent "extreme concentrations of wealth from being passed from generation to generation."⁹ In addition, a design that restricts transfers of control rights on corporations can be good for both equity and efficiency.¹⁰

7. *Avoid implicit taxes.* In many instances, the most important taxes affecting the poor are not formal ones levied through the tax code, but implicit taxes, including bribes¹¹ and inflation. Other implicit taxes to be avoided include many instances of "regulation as taxation" such as quasi-taxes imposed through controls on trade, prices, credit, foreign exchange, or capital markets.¹²

Managing resource rents transparently and equitably

High overall standards of transparency and accountability are essential if the revenues from extractive industries are to be used well. However, as a second best solution in weak institutions of accountability, many countries, developed and developing, do not pool the revenues from extractive industries with other resources in a unified planning and budget process. Instead, they are channeled to a dedicated fund, with special arrangements to earmark the revenues for specific purposes; define reporting and disclosure requirements; and establish oversight bodies to ensure that the arrangements are properly implemented.

One common objective of such revenue management arrangements is to save part of the revenue stream. The savings may be used for short-term budgetary stabilization, so that expenditures are protected from fluctuations in prices and output. They may also be used to build up financial assets, which can generate revenues over an extended period, in some cases constituting a perpetual fund, so that future generations can benefit from the revenues generated from the depletion of resources. Azerbaijan, Chad, and Kazakhstan

have legislated savings to deflect pressures to spend revenues quickly and unproductively.

Revenue management arrangements can also serve distributional objectives. In Chad, the Oil Revenue Management Law assigns a share of revenues to a "future generation fund" and specifies allocations for poverty reduction. Such earmarked allocations may be anathema to financial managers, but they communicate and underline the government's commitment to prudent and redistributive spending. Nigeria's experience in the Niger Delta during the 1980s and 1990s highlights the resentment and political instability that can result when local communities see no demonstrable benefits from the extractive industries in their midst. The democratic government has responded by creating a Niger Delta Development Commission to fund local development, with statutory contributions from the federal government and the oil companies.

High standards of transparency and accountability are essential if the revenues from extractive industries are to be used for development purposes. To reduce the risk of diversion of revenues, the Extractive Industries Transparency Initiative (EITI), championed by the United Kingdom, calls on governments and extractive indus-

tries to report and reconcile payments and revenues. Some companies have taken the initiative of publishing payments to government in some of the countries in which they operate—for example, Shell in Nigeria and British Petroleum in Azerbaijan. The "Publish What You Pay" coalition advocates more systematic disclosure of companies' annual reports and for home-country legislation to make such declarations mandatory. Equally important are improvements in government reporting arrangements to ensure transparency in the application of revenues generated by large projects, such as the Chad-Cameroon pipeline and the Nam Theun 2 hydropower project in the Lao People's Democratic Republic.

Revenue management arrangements are likely to be more successful when they are the product of a broad consultative process and the rationale is widely understood. Timor-Leste has facilitated broad civil society involvement in the design of the revenue management arrangements for its offshore oil and gas industry. Draft legislation on the industry's commercial and tax regime and legislation on a proposed petroleum fund, have been published and subjected to numerous public consultations.