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FISCAL SPENDING AND THE ENVIRONMENT: A CASE OF DECENTRALIZATION IN ASIA (CHINA & PAKISTAN)

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In large number of countries, government has legal mandate to directly spend sizeable amount of the national income which could vary from 25% to 45% of GDP. The priorities of many governments in terms of resource spending undergo expansion and revision to arrest deepening economic crises. The changes in the fiscal spending in terms of its composition mostly remain stable where as the increase in government expenditure may be impermanent. The need to develop theoretical and empirical model that explain the impact of government spending on natural resources in terms of pollution is more pronounced. The relationship between fiscal expenditure and its composition with economic growth also calls for systematic evaluation of policy for fiscal spending and its link with the sustainability of development. This could be a positive contribution in literature.

The realization of high social and economic costs, particularly health risks of degrading environment as a result of increasing production and economic activities is taking roots in many Asian countries. These countries have started giving serious consideration to sustainable development. They recognize the fact that the conventional route to economic growth is now detrimental for future growth. Several efforts at the state levels like establishment of public institutions (Ministry of Environment and adjunct departments) to protect environment and natural resources are among some of the forward looking steps. The enforcement of environmental laws is somehow a weak subject for almost all developing Asian countries with very few exceptions. One of the many reasons is scarce resource allocation for this purpose by the state authorities. Public institutions often remain ill-equipped in fulfilling their various tasks related to effective implementation of laws and in designing new laws and regulations. Special tasks of doing inspections and monitoring that are integral components of effective enforcement of regulations fail to provide required results due to under capacity of institutions. Environmental Protection Agency in Pakistan is somehow seen as an ineffective entity.

Over the past three decades, many Asian countries have decentralized in the allocation and responsibility and have shifted control over resources and decision making to local governments and enterprises. This devolution of decision-making to local levels and enterprises has placed environmental stewardship in the hands of

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local officials and polluting enterprises. ZhongXiang Zhang says that, under the current evaluation criterion for officials in China, local officials typically have been promoted based on how fast they expand their local economies. This distorted incentive system tempts officials to disregard environmental costs of growth. Moreover, objectively speaking, the current fiscal system in China plays a part in driving local governments to seek higher GDP growth because that system makes it hard to reconcile the interests of the central and local governments. Since the tax-sharing system was adopted in China in 1994, taxes are grouped into taxes collected by the central government, taxes collected by local governments, and taxes shared between the central and local governments. All those taxes that have steady sources and broad bases and are easily collected, such as the consumption tax, tariffs, vehicle purchase tax, are assigned to the central government. VAT and income tax are split between the central and local governments, with 75% of VAT and 60% of income tax going to the central government. As a result, the central government revenue increased by 200% in 1994 relative to its 1993 level. This led the share of the central government in the total government revenue to go up to 55.7% in 1994 from 22.0% in the previous year. In the meantime, the share of the central government in the total government expenditure just rose by 2%. By 2009, local governments only accounted for 47.6% of the total government revenue, but their expenditure accounted for 80.0% of the total government expenditure in China. To enable to pay their expenditure for culture and education, supporting agricultural production, social security subsidiary, etc., local governments have little choice but to focus on local development and GDP. That in turn enabled them to enlarge their tax revenue by collecting urban maintenance and development tax, contract tax, arable land occupation tax, urban land use tax, etc. Therefore, effective environmental protection must be placed in this context of government decentralization. In this regard, local government's cooperation is crucial to the overall outcomes. As often is the case, what the center wants is not necessarily what the center gets. An old Chinese saying goes, 'the mountains are high, and the emperor is far away'. Central governments need to let go of the notion that they should or even can do it all. Instead, they need to recognize that without local governments 'cooperation to get these policies implemented, it is meaningless to set and defend national environmental goals, no matter how stringent they are.

Taking China as a focus and in the context of government decentralization, we consider variety of tactics that the Chinese central government has been using to incentivize local governments. There is a clear need to carefully examine those objective and subjective factors that lead to the lack of local official's cooperation on the environment, and provides some suggestions for appropriated incentives to get their cooperation.

Incentives for local governments need serious consideration to be more environmentally responsible. While China has been calling for energy saving since the early 1980s, the country has set, for the first time, the goal of cutting energy intensity by 20% in its current five-year (2006-10) economic plan. Industry accounts for about 70% of China's total energy consumption so that this sector is crucial for China to meet its own set energy-saving goal. To that end, China established the 'Top 1000

Enterprises Energy Conservation Action Program' in April 2006. This program covers 1,008 enterprises in nine key energy supply and consuming industrial subsectors. These enterprises each consumed at least 0.18 million tons of coal equivalent (tce) in 2004, and all together consumed 33% of the national total and 47% of industrial energy consumption in 2004. The National Development and Reform Commission (NDRC) of China stop economic planning agency, sets energy-saving target for each of these enterprises, and all together these enterprises are required to achieve the overall energy saving of 100 million tce cumulatively during the period 2006 – 10, thus making a significant contribution to China's overall goal of 20% energy intensity-improvement (NDRC 2006). In May 2006, empowered by the State Council (China's Cabinet), the NDRC signed energy-saving responsibility agreements with governments of 31 provinces or equivalent to allocate the overall energy-saving target of those Top 1000 enterprises in each province or equivalent. These governments in turn signed with those Top 1,000 enterprises located in their region. To ensure that the goal is met, achieving energy efficiency improvements has become a criterion for job performance evaluations of the heads of these enterprises. This help them realize that they should take their jobs seriously because they have a very real stake in meeting energy-saving goals.

During economic crises, governments often increase fiscal spending to stimulate the economy. Pakistan has shifted control over resources and decision making to provincial governments and as a result of the 18th amendments in the constitution of Pakistan and economic reforms over the past decades. The devolution of decision – making to local levels has placed environmental stewardship in the hands of local officials and polluting enterprises who are more concerned with economic growth and profits than the environment. Therefore, effective environmental protection needs their full cooperation. Against this background, the research note suggest a variety of mechanisms that the federal government has been using to bestow incentives upon provincial governments and required market based instruments supporting economic policies, and governmental performance rating. In this regard, the case of China could be worth studying and emulate by Pakistan, which predicts a reallocation of government spending composition towards social and public goods that reduces pollution. However increasing total government spending without altering its composition does not reduce pollution.