



## Fiscal Decentralization Practices in Federal System: An Evidence from Some Countries and Western Hill, Nepal

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### **Abstract**

This paper examines the fiscal decentralization practices of some federal countries and perception from public regarding the overall federal system in Western hill of Dhawalagiri region selecting Baglung municipality, Beni municipality and Kusma municipality as a sample purposively from Gandaki Province of Nepal. This research work follows a mixed methods approach. For this, available literature as a secondary sources are reviewed from abroad countries adopted federal system into practice. Similarly, for assessing the perception of respondents regarding the issues such as institutional powers, people trust in the overall system, inter-governmental relation, autonomy, responsibility and accountability, 100 key informants were selected based on stratified random sampling representing at least 30 sample from each municipality covering equal proportion of key informants from both public and local representative of the study area. The results are analyzed descriptively. The study found that local governments lack sufficient authority to make financial decisions (54 %) and lack adequate resources (41 %). Fiscal responsibility transfers are found well-structured. Coordination between government levels is found effective. Autonomy has improved and operate transparently. There is found high public participation in decision making. Fiscal decentralization is seen as a tool to enhance service delivery and reduce inequality. However, the study found institutional barriers and resource constraints. Lastly, the results of the study have synthesized to formulate policy recommendations and disseminated to the concerned authorities of the sample area. This study will helpful for government and further researchers.

**Keywords:** fiscal, decentralization, resources, federal system, western hill, Nepal

## 1. Introduction

Transferring financial control from central to subnational governments, comprising intergovernmental transfers, revenue assignment, and expenditure assignment, is referred to as fiscal decentralization (Bahl, 2008). Decentralization refers to the real transfer of authority and responsibility to local governing bodies. It also refers to the absolute involvement of people in the government of the country at the local levels. It is, furthermore the planning from below, granting authority to the local institutions to mobilize local resources, using local technology, knowhow and materials, making bureaucracy accountability to the elected officials and inviting non-governmental organizations in the local development activities (Sainju, 1994).

Decentralization concept emerged especially in 1950's and early 1960's and newly independent developing countries adopted unified, centralized and regulatory government system due to mainly two reasons. First, the centralized political, administrative and economic systems were the direct legacies of the erstwhile colonial power. Second, the political leaders of the third world countries found the centralized administrative and economic mechanism as a convenient tool to reinforce their political power. However, since the late 1960's many developing countries initiated and implemented the decentralized development and management systems due to unsatisfactory centralized planning and management system, realized the significance of participatory approach in development strategies to raise the living standard of all segments of the society, considering partial solution to their growing financial and economic problems caused by their decreasing exports, diminishing foreign assistance, considering the decentralization as the underlying rationale of international development strategies during the 1970's and realizing it as the bottlenecks of centralized development and management system (Shrestha, 1996).

Ebel & Yilmaz (2002) mention that the decentralization process is widespread in both developed and developing countries pursuing to challenge central governments' monopoly of decision-making power. It is an effective tool for reorganization of the government in order to provide public services cost effectively in the post-welfare state era, in the western world. In Eastern Europe, decentralization of the state is the direct result of the transition from socialist system to market economy and democracy. In Latin America, it is the political pressure from the people for Democratization. Decentralization has served as a path to national Unity in Africa. Now, developing countries are spinning to decentralization to escape from the traps of ineffective and inefficient governance, macroeconomic instability, and inadequate economic growth.

The principle justification of decentralization in developing countries are: (i) the political dimension in which the decentralization strengthens local government institutions by equipping them with required powers and functions, minimizes the negative trend of bureaucratization, discourages the bureaucratic ways of administrative behavior, facilitates the administration to the door steps of the people; (ii) administrative dimension in which decentralization is expected to improve administrative efficiency, make government quickly responsible to the needs and aspiration of the people, enhance the quantity and quality of services which government provides to the people and (iii) development dimension in which decentralization can be rationalized to fulfill the basic needs of all segments of the society in general and that of poor in particular and can be considered as an instruments to advance and

enhance national development to fulfill national interests, public demand and social needs as well.

Several developing nations are also looking to various forms of fiscal decentralization as a potential means of avoiding the problems of macroeconomic instability, insufficient economic growth, and ineffective and inefficient governance that have occurred so many of them in recent years (Bird & Vaillancourt, 1999). Fiscal decentralization is considered to be a supportive in per-capita growth, resource generation and allocation, revenue sharing, infrastructure development, employment opportunities generation at the local level in Nepal. Thus, this article has focused on to observe this reality.

### **1.1 Research question and objectives**

Powers and functions can be delegated to the local bodies using various ways. They are political decentralization, administrative decentralization and fiscal decentralization. Of them, this study is mainly focused on fiscal decentralization. Under this decentralization, economic rights such as tax and non-tax collection, grants and loans collection systems, taxing and spending rights, collection, allocation and management of resources have been delegated from higher level central government to local level governments. Numerous studies have examined the fiscal decentralization practices. However, there is a current research gap in understanding the practice of it in the study area. In this study, author's main concern is how central government granted some fiscal autonomy at the local level and how is the perspective of concerned authorities and local people regarding the issues such as institutional powers, public trust in the system, inter-governmental relationship in resource utilization, autonomy, responsibility and accountability? Here, first issue has focused on some federal countries where as both issues have assessed considering Nepal into account.

## **2. Literature Review**

Cheema & Rondinelli (1983) argue that decentralization refers to transfer of planning, decision making or administrative authority from the central government to its field organization, local government or non-governmental organization. White (1931) opines that decentralization is the process of conferring authority-legislative, executive and judicial- to the lower branches of government.

Similarly, Sherwood (1969) mentions that centralization as involving the concentration of power at the top of the pyramid within a given hierarchical structure and decentralizations as indicating the dispersal of the powers throughout such structure. It can be defined as a means and as a philosophy. As a means it is a process of transferring functions and powers from central to local government units and organization. As a philosophy, it entails the sharing of powers and functions between and among various levels of government and other public and non-public organization and agencies as per the constitutional provision and other legal stipulations.

Bahl and Linn (1992) mention the three general arguments might be given in support of fiscal decentralization:

First, if the expenditure mix and tax rates are determined closer to the people, local public services will improve and local residents will be more satisfied with government

services. Second, local governments will contribute to nation-building because people can identify more closely with local than central government. Lastly, overall resource mobilization will be increased because local governments can tax the fast-growing parts of their economic base more easily than can the central government (p. 386).

## **2.1 Theoretical Underpinnings of Fiscal Decentralization**

Fiscal decentralization and fiscal federalism, both terms have the same meaning. Both relate with who does what, who impose taxes, how to collect and mobilize revenue and how to remove imbalanced situation between revenue and expenditure. It has been adopted worldwide with the guarantee of improving democratic representation, public sector efficiency and socio-economic welfare (Martinez-Vazquez, 2008). For the successful of fiscal decentralization in any country of the world, it requires expenditure assignment principle, revenue assignment principle, inter-governmental transfer or grants and loan management as the necessary condition. Similarly, efficient system is also the basic organs of fiscal decentralization in developing countries like Nepal. Regarding fiscal decentralization, there are some theories as follows:

**The subsidiary principle:** This principle is a guiding principle for the assignment of responsibilities among the local bodies of the world. The main assumption of this principle is that taxing, spending, regulatory functions should be exercised by lower levels of government unless a convincing case can be made for assigning them to higher level of government. As mentioned by Shah (2006), this is the base of decentralization which evolved from social teaching of the Roman Catholic Church and first proposed by Pope Leo Xiii in 1891 (p. 4). Consequently, Pope Pius Xi highlighted this principle as a third way between dictatorship and a laissez-faire approach to governance.

**Fiscal Equivalence Principle:** Equating the political jurisdiction with the benefit area is called the fiscal equivalence principle. Olsen (1969) opines that if a political jurisdiction and benefit area overlap the free-rider problem is overcome and the marginal benefit equals the marginal cost of production, thereby ensuring optimal provision of public service (Shah, 2006, p. 4).

**The Decentralization Theorem:** This theorem really advocates fiscal decentralization. For the practical implementation of this, it requires a large number of overlapping jurisdiction. Regarding this theorem, Oates (1969) mentions that:

Each public service should be provided by the jurisdiction having control over the minimum geographic area that would internalize benefits and costs of such provision, because (i) local governments understand the concerns of local bodies, (ii) unnecessary layers of jurisdiction are eliminated, (iii) inter jurisdictional competition and innovation are enhanced, and local decision making is responsive to the people for whom the services are intended, thus encouraging fiscal responsibility and efficiency, especially if financing of services is also decentralized (Shah, 2006, p. 4).

**The Correspondence Principle:** This principle is also called matching principle and it requires a large number of overlapping jurisdictions. Frey & Eichenberger (1995, 1996 and

1999) argue that jurisdictions could be organized along functional lines while overlapping geographically and that individuals and communities could be free to choose among competing jurisdiction. They (individuals and communities) express their preferences directly through initiatives and referenda. The jurisdiction has authority over their members and the power to raise taxes to fulfill their tasks (Shah, 2006). Similarly, this principle is related with the revenue collection from benefited, the provision of power to collect revenue along with expenditure, and linkages responsibilities with revenue collection powers.

**The Clarity Principle:** This principle is related with the division of functions. This really focused on the devolution of powers and functions between the central and local levels.

**Voting by Feet Principle:** This principle was propounded by Charles Tiebout in 1956. As said by him, people consider tax costs and the public services menu offered by a jurisdiction in deciding where to live. This principle leads to the formation of jurisdictions, creating a market analog for public services provision. Similarly, Oates (1969) argues that if people vote with their feet, fiscal differentials across communities are capitalized into residential property values (Shah, 2006; Shrestha, 2008). This principle has maximum applied in developed countries, not in developing countries like Nepal.

### 3. Methods and Materials

This study is mainly based on Western hills of Gandaki province of Nepal. Baglung municipality from Baglung district, Beni municipality from Maygdi district and Kusma municipality from Parbat district are selected purposively. For examining the fiscal decentralization practices in the sample area, available literature are reviewed from abroad countries adopted federal system into practice. Similarly, for assessing the perception of respondents regarding the issues such as institutional powers, people trust in the overall system, inter-governmental relation, autonomy, responsibility and accountability, 100 key informants are selected based on stratified random sampling representing at least 30 sample from each municipality. While selecting key informants from the total sample, 50 percent from public and 50 percent from local representative are selected purposively.

This research work followed a mixed methods approach. Quantitative method has employed to observe fiscal practices of within and abroad countries adopted federal system. Similarly, qualitative methods involve semi-structured interviews with key respondents (general public and local authorities) to delve nuanced experiences and perceptions regarding the overall system in the study area. For this, five-point Likert scale questionnaires are applied. Thematic analysis as well as statistical software are employed for the analysis of data obtained from both sources. Ethical considerations has also maintained throughout the study. Lastly, the results of the study has synthesized to formulate policy recommendations and disseminated to the concerned authorities of the sample area.

### 4. Results

Fiscal decentralization has exercised in both federal and unitary system of the world. Denmark, Finland, France, Italy, Netherland, Sweden and Japan are the developed countries

having unitary system, whereas America, Spain, Switzerland are the developed countries having federal system. Similarly, China and Indonesia are the developing countries having unitary system whereas India, Ethiopia, Nigeria, Malaysia and South Africa are the developing countries having federal system. Nepal is recently adopting federal system in practice. In this research, fiscal decentralization exercises in some federal countries and perception from both public and local authorities of Western Hill, Nepal regarding the overall system have discussed.

#### **4.1 America**

Constitutionally in America, there are two level of governments such as central level and state level but practically other local governments like Counties, Municipalities, Townships, School District and Special Districts are also in operation there. Most states have attempted to grant autonomy to local governments in discharging their specified functions through home rule provisions (Shah, 2006, p. 20). American model recognizes local government as a handmaiden of states and provinces but attempts to grant automatically to local governments in their specific areas of responsibility-predominately delivery of property oriented services (Shah, 2006). In America, local governments perform an intermediate range of functions. Central and state governments both are mainly dependent on individual and institutional income tax. Central government provides loans, grants and tax subsidy to the state and local governments. State governments have imposed interest tax, estate tax, income tax, use tax, fuel tax etc. Property taxes are the dominant sources of local revenue. Local government expenditure constitute about seven percent of GDP in America.

#### **4.2 Spain**

Spain is a developed country having federal system where there are three level local bodies. Fiscal system of autonomous bodies is prepared along with staying central government in every five years. Local governments can collect revenue from personal income tax, property tax, inheritance tax, vehicle tax, fuel tax etc. Besides this, local bodies can collect revenue creating new tax. Local governments can fix the rates based on the boundary determined by central government. In the context of Spain, property tax is the mainstays of local finance which covered approximately half of municipal revenue.

#### **4.3 Switzerland**

Switzerland consists of 26 cantons, 2842 communes and 3000 municipalities. All of them have the taxing power. Each canton has its own constitutions, parliament, government and courts. They have strong power in taxing, spending and ruling as compared to others, even central government. The communes are handmaidens of the cantons. They perform some delegated tasks such as population registration and civil defense, but they have autonomous competencies in education and social welfare, energy supply, roads, local planning and local taxation (Shah, 2006 p. 23). Local government can collect revenue from income tax, property tax, value added tax, direct tax, service fee, vehicle tax, tax on dog, entertainment tax, and play tax, loans and grants as well. Local government in Switzerland can impose personal income tax and corporate profit tax too. They are autonomy not only in fiscal matters but also in immigration, citizenship, language and foreign economic relations. For this they follows subsidiary principle of fiscal decentralization.

#### **4.4 India**

In India, there are 10 lakhs local governments under its 28 states. There is one of the oldest traditions of strong self-governance at the local level. Central government functions and local government function of India are similar to Nepal. Central government and state government collect revenue through individual and corporate income tax, fees, fines, value added tax, land tax, tax on agriculture income, property income, registration fee, vehicle tax etc. Similarly, there are three fiscal commissions i.e. central fiscal commission at center, state fiscal commission at state and local fiscal commission at local level (Shah, 2006). At the local level, revenue and its sources are determined by the state fiscal commission.

#### **4.5 Ethiopia**

Ethiopia is a developing country having federal system. Constitutionally, there are four levels of governments but practically, two levels are in operation. Tax rates and tax base all are determined by central governments which indicates that unitary system is also exercised there. Approximately, 80 % to 90 % of total revenue is collected by central government. In Ethiopia, local government can collect revenue as national loans too after taking approval from ministry of finance (Shah, 2006).

#### **4.6 Nigeria**

Nigeria is a country having federal system. Separate powers and functions of different level of governments pertaining to taxing, spending, planning, management and resource mobilization are determined constitutionally. In Nigeria, federal government can collect revenue from corporate income tax, petroleum profit tax, value added tax, education tax, profit tax and tax impose on personal income of police, military and non-residents. State government collect revenue from personal income tax without police and military, play tax, road tax, business registration fee, individual development fee, market fee etc. Similarly, local government can collect revenue from business tax, slaughter house fee, birth registration fee, parking fee, domestic animal license fee, vehicle tax, animal tax, entertainment tax, radio-television license fee, bus license fee, public toilets fee and hoarding board fee (Shah, 2006). Local government in Nigeria can also collect revenue as loans.

#### **4.7 Nepal**

Nepal is a developing country having almost rural economy. As per the adoption of federal constitution 2015, Nepal has turned into federal system and has become new Nepal. This framework divides powers and financial responsibilities among three tiers of governments (federal, provincial – seven provinces and local – 753 units) to address historical inequalities and decentralize resources. In Nepal, fiscal federalism is formed on four key pillars (expenditure assignment, revenue assignment, intergovernmental fiscal transfers and public debt management). The Constitution of Nepal (2015) provides power for each government level (Acharya, 2020). It assigns specific responsibilities to each tier. Revenue rights of local government are relatively broader compared to provincial government. Provinces in Nepal rely heavily on federal transfers, averaging 13.58 percent of provincial budget in fiscal year 2021/022 (The Asia Foundation, 2021). Similarly, provinces and local governments heavily depend on federal transfers, with own source revenue remaining low 1.6 percent in Karnali

Province to 41.2 percent in Bagmati Province in fiscal year 2023 (The Asia Foundation, 2021). There is also found a mismatch between expenditure responsibilities and revenue generating capacity. This dependency risks fiscal imprudence. Regarding spending, provincial governments underspent by 34 percent and local governments by 24.4 percent in fiscal year 2023 due to poor alignment between plans and budgets and vague allocation (World Bank, 2024).

In Nepal, Provincial and local governments have gained autonomy in budgeting and planning, fostering completion and resource mobilization. The intergovernmental financial management Act (2017) allocates 70 percent of value added tax and excise duties to the federal government, with 15 percent each to provinces and locals (World Bank, 2024). Similarly, intergovernmental transfers have been substantial, with provinces and local governments receiving 36.7 percent of the federal budget in fiscal year 2021, amounting to 64.8 percent of their revenue (World Bank Blogs, 2023).

After the fiscal federalism practices in Nepal, service delivery has found improved compared to the pre-federal era (World Bank Blogs, 2023). In this research, overall perception of service providers and perception of service receivers are measured on the basis of institutional powers, intergovernmental relationship, and autonomy, public trust in the system, responsibility and accountability.

**Table 1:** *Demographic characteristics of the sample area (N=100)*

Factors	Variables	Percent
Gender	Male	65.0
	Female	35.0
Marital status	Unmarried	16.0
	Married	84.0
Age	Age 30-40 years	26.0
	Age 40-50 years	46.0
	Age 50-60 years	24.0
	Above 60 years	4.0
Education	Basic level up to 8 class	50.0
	Secondary level class 9-12	48.0
	University education	2.0
Family size	2-4 persons	10.0
	4-6 persons	52.0
	More than six persons	38.0
Involvement periods at local level	Two years	6.0
	Three years	6.0
	Four years	64.0
	More than four years	24.0

**Source:** *Field Survey, 2025.*

Table 1 presents that 65 percent of respondents are male. Eighty- four percent of the respondents are married. Nearly half of those surveyed are between the aged of 40-50 (46.0 %) years and 50 percent have only a basic level education. As per the responses of the respondents,



62 percent have six members in their family. Similarly, 64% are found to be involved as local representatives.

**Table 2:** *Perception of service providers*

(Strongly disagree = 1, disagree = 2, neutral = 3, agree = 4, strongly agree = 5)

Indicators	Statements	Responses (%)				
		1	2	3	4	5
Institutional powers	Governments at local level have sufficient authority to make fiscal decisions.	5.0	54.0	9.0	32.0	0.0
	The transfer of fiscal responsibilities is clear and well structured.	2.0	11.0	12.0	55.0	20.0
	The governments at local level have adequate resources to exercise their institutional power effectively.	0.0	41.0	13.0	46.0	0.0
	The legal framework regarding to revenue sharing from natural resource supports the fiscal functions of local government effectively.	0.0	13.0	1.0	78.0	8.0
	Local governments have to face institutional barriers to implement fiscal decentralization policies.	0.0	11.0	6.0	76.0	7.0
	Now, local governments are strong compared to before.	0.0	0.0	34.0	66.0	0.0
Intergovernmental relationship	The roles and responsibilities for resource generation, allocation and mobilization between different levels of government are well defined.	0.0	2.0	5.0	68.0	25.0
	There is coordination between different levels of government that ensures optimum resource mobilization.	0.0	0.0	46.0	54.0	0.0
	Overlapping responsibilities between different levels of government affect resource generation and mobilization efficiency.	0.0	4.0	1.0	80.0	15.0
	Provincial guidelines are helpful in managing resources at the local level.	0.0	0.0	10.0	90.0	0.0
	Resource dependency on higher level limits the efficiency of local governance.	0.0	0.0	12.0	76.0	21.0
Autonomy	Governments at local level have sufficient autonomy to fulfill local needs.	0.0	11.0	10.0	60.0	19.0

Local authorities are equally responsible in their functions.	0.0	0.0	11.0	71.0	18.0
Local governments are free to generate resources as per their local requirements.	9.0	12.0	25.0	53.0	1.0
Fiscal autonomy helps to prepare and implement the development projects as per local requirements.	0.0	0.0	10.0	66.0	24.0
There is sufficient autonomy compared to before.	0.0	0.0	0.0	41.0	59.0

**Sources:** *Field study, 2025.*

Table 2 presents the mixed perception of service providers regarding the mentioned issues. Local governments are perceived more powerful than they were previously. Most service providers (54 %) think local governments lack sufficient authority to make financial decisions and 41 percent think they lack adequate resources. However, 55 percent of respondents think that fiscal responsibility transfers are well-structured. Fifty four percent of respondents believe that coordination between government levels is found effective. Similarly, 80 percent of respondents agree that overlapping roles between the government levels hinder their efficiency. Dependency of resource on the higher levels is still a constraint (76 %). Regarding autonomy, 59 percent of respondents believe that autonomy has improved and 60 percent think local governments can meet local requirements. According to the study's findings, there is a new style of thinking that can help modernize governance capability and is practically significant for improving China's official evaluation and governance systems (Min, 2021). On the whole, the findings indicate progress in fiscal decentralization but highlight institutional barriers and resource constraints.

**Table 3:** *Perception of service receivers*

(Strongly disagree = 1, disagree = 2, neutral = 3, agree = 4, strongly agree = 5)

Indicators	Statements	Responses (%)				
		1	2	3	4	5
Public trust in the system	Governments at local level are transparent in their fiscal operation and decision making process.	0.0	11.0	15.0	74.0	0.0
	Budget allocation and expenditure patterns are accessible to the public.	0.0	19.0	11.0	70.0	0.0
	There is a public participation in fiscal decision making process.	0.0	0.0	0.0	75.0	25
	People trust local governments to mobilize public funds effectively.	0.0	0.0	0.0	70.0	30.0
	Efforts regarding fiscal transparency have improved public trust in the system.	0.0	0.0	20.0	65.0	15.0
	Local government is closer to people so that they can provide better public services.	0.0	2.0	6.0	86.0	6.0

	Fiscal decentralization leads to lower corruption in different level of governments.	0.0	3.0	7.0	83.0	7.0
Responsibility and Accountability	Accountability mechanism for fiscal management at local level are established.	0.0	49.0	1.0	50.0	0.0
	There is regular audit system for the utilization of public funds.	7.0	21.0	33.0	39.0	0.0
	People can report grievances to the local government authorities regarding misutilization of resources within their area.	0.0	16.0	6.0	63.0	15.0
	Local representatives are accountable in their responsibilities.	6.0	6.0	3.0	74.0	11.0
	Accountability would improve the effectiveness of fiscal decentralization.	0.0	0.0	16.0	56.0	28.0
	Fiscal decentralization reduces inequality by improving government accountability.	0.0	13.0	5.0	76.0	6.0
	Quality of service delivery at the local level have improved.	0.0	28.0	6.0	65.0	1.0

**Sources:** *Field study, 2025.*

Similarly, Table 3 highlights the perception of service receivers on public trust and accountability in local governance of the sample area. A significant majority of service receivers think that local governments operate transparently. There is found high public participation in decision making and public fund mobilization is also found trustworthy. Decentralization is perceived to lessen corruption and efforts to increase fiscal transparency are seen as improving trust. However, nearly half of service receivers (49 %) feel that accountability mechanisms are not well-established. Although local representatives are considered responsible, there exists gaps in auditing system and grievance reporting processes. Overall, fiscal decentralization is seen as a tool to enhance service delivery and reduce inequality. Khanal (2018) concludes that efforts at fiscal decentralization in Nepal contribute to reducing human poverty, though they may not enhance all dimensions of human development. Fiscal decentralization is a significant area of interest for international aid and academic research, emphasizing its economic advantages while occasionally neglecting its ability to improve public governance (Liu, 2017). The research examines the impact of fiscal decentralization on regional public welfare services in relation to income and expenditure. Regression analysis reveals that the effects on public welfare vary depending on the method of fiscal decentralization employed (Yang, 2020). Fiscal decentralization is noted for its potential to stimulate economic growth by facilitating more effective resource distribution. Tarigan (2003) points out that fiscal decentralization can result in macroeconomic volatility, enhance service delivery, and lead to a more effective administration with reduced corruption.

**Table 4:** Paired samples statistics: satisfaction level of service providers and service receivers

Category	Mean	Std. deviation	R	Sig	Mean	Std. deviation	t	Sig.
Public	31.60	2.630	(-.382)	.000	3.940	4.287	9.190	.000
Local authorities	35.54	2.527						

**Source:** *Field Survey, 2025.*

The findings of the study show that there is a substantial disparity in the degree of satisfaction between service providers and service recipients of the study area. The average level of satisfaction for local authorities is 35.54 (SD = 2.527), but the mean for public service providers is 31.60 (SD = 2.630). The adverse association between service provider and service receiver satisfaction levels is demonstrated by the negative correlation ( $r = -.382$ ). According to the t-test value ( $t = 9.190$ ,  $p = .000$ ), the mean difference in satisfaction levels is 3.940 (SD = 4.287). As Tahun (2012) focused that all indicators of fiscal decentralization variables and economic development indicators are valid, according to the study's findings. It designates particular duties to each level. Local governments possess relatively wider revenue rights than provincial governments. In Nepal, provinces depend significantly on federal transfers, which accounted for an average of 13.58 percent of the provincial budget in the fiscal year 2021/022 (The Asia Foundation, 2021). The ratio of regional income to economic development performance is a measure of economic growth and the most significant indicator of the latent variable of fiscal decentralization are found differ. Finally, this difference is statistically significant, resulting that service providers and service recipients have various opinions on the quality of services in the sample areas.

## 5. Discussion

Sato (2002) mentions that fiscal devolution motivates local jurisdictions to become fiscally independent and grants more revenue responsibility to the local level. He further points that this helps to improve public sector efficiency and promote democracy. Akai et.al (2009) point that fiscal decentralization reduces regional inequality in low income countries by increasing autonomy at local level. Similarly, they also point outs that it has adverse effect on high income countries.

According to the study done by Lockwood (2005), fiscal decentralization which adopt a political economy approach, can improve government accountability. Tarigan (2003) finds mixed results between fiscal decentralization and economic development. For this, the author has set four hypothesis such as fiscal decentralization allows better efficiency of resource allocation which thus leads to higher economic growth; a better public service delivery; brings macroeconomic instability and a more efficient bureaucracy and thus less corruption.

Devkota et al. (2014) mention that fiscal decentralization has positively impacted on per capita GDP growth in the district of Nepal due to the implementation of the Local Self-governance Act. Shrestha (2002) points that the practice of decentralization in Nepal is almost four decades old which perhaps the oldest decentralization process in South Asia. A research done by him provides an overview of intergovernmental fiscal relations in Nepal and highlights the issues and reform directions for effective fiscal decentralization.

Khanal (2018) finds that the ongoing efforts on fiscal decentralization are supportive and urbanization is good for reducing human poverty in the districts of Nepal. He further finds that fiscal decentralization does not improve all the dimensions of human development.

Both for international aid initiatives and the scholarly community, fiscal decentralization has emerged as a key theme. The economic advantages of fiscal decentralization are the main focus of current research. However, it is frequently disregarded that fiscal decentralization may improve economic performance by enhancing public governance (Liu, 2017).

This study empirically explores the effect between fiscal decentralization and regional public welfare service performance from the perspective of income and expenditure of fiscal decentralization. Regression results surface: from different financial decentralization point of view, found that the impact on the achievement of regional public well-being services results are different (Yang, 2020).

This study investigates the connection between economic development and fiscal decentralization. According to the study's findings, fiscal decentralization promotes greater economic growth by enabling more effective resource allocation. According to Tarigan (2003), fiscal decentralization also results in macroeconomic instability, improved public service delivery, and a more effective bureaucracy with lower levels of corruption.

The process of redistributing fiscal responsibilities among various levels of government (Boadway, 1994; Oates, 1999) has gained acceptance in Asian countries as a way to improve public sector efficiency and promote democracy (Sato, 2004). However, implementing fiscal decentralization in developing and transitional economies presents unique challenges, especially in the context of moving from planned to market economies (Rao, 2001). To address these challenges, a comprehensive approach that involves all levels of government and makes use of tools like conditional grants, regulation, and coordinated decision-making is required. The findings suggest that whereas fiscal decentralization's achievement of separateness in low-income or poor counties helps to reduce inter county inequality, this effect is not as significant as the adverse effect that fiscal decentralization has on wealthy or high-income counties (Akai & Hosid, 2009).

## **6. Conclusion**

This study concludes that there is a notable discrepancy in satisfaction level between service providers and service receivers regarding the local government and fiscal decentralization. Despite the lack of effective accountability systems, service recipients believe in local government and point to decentralization as a way to lessen inequality and corruption at the local level. Similarly, despite the perception of increased authority and transparency, institutional constraints and resource dependency still exist in local governments. Different views of service providers and service recipients on service quality are pointed out by the negative correlation between the satisfaction ratings. Ultimately, this discrepancy is statistically meaningful, indicating that there are differing views on service quality between providers and recipients in the sampled regions. Fiscal decentralization has the potential to create macroeconomic fluctuations, improve service delivery, and foster a more efficient administration with diminished corruption; however, the situation in Nepal presents a different

scenario. Though fiscal decentralization has made improvements overall, issues with financial autonomy and coordination still need to be resolved for better local governance.

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