

Market-Based Governance and the Challenge for Rural Governments: U.S. Trends

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Abstract

Privatization and decentralization represent market-based approaches to government. Designed to increase efficiency and responsiveness of government, these approaches also limit the potential for redistribution. A key question is how will rural governments compete in such a market based system? Will they be favored, as their reliance on market provision for public goods is higher due to the smaller number of services provided by government? Or will they be less able to compete due to the costs of sparsity which may make them less attractive to market suppliers? Data from the United States covering the period 1992-2002, show that rural areas are not favored by either of these trends – privatization or decentralization. Managerial weakness does not explain the shortfall. Rural areas are not as attractive to market suppliers and thus are disadvantaged under market based service delivery approaches. Although national policy continues to advance a privatization agenda, policymakers should be concerned about the uneven impacts of such market based approaches.

Keywords (please provide) privatization, decentralization, rural development, local government

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Introduction

Around the world enthusiasm for market based approaches to government, especially privatization and decentralization, is gaining interest. Little research has addressed specifically the challenge to rural governments of this market based approach. Why the silence on rural impacts? What is the importance of rural local government in the 21st century? Should we worry about differential effects if they exist? This paper addresses these questions drawing from data in the United States covering the period 1992-2002. We find rural areas are not favored by either of these trends – privatization or decentralization. Policymakers should be concerned about the uneven impacts of such market based approaches and what this may mean for rural policy in general.

Market Approaches to Government and Rural Competitiveness

Privatization and decentralization are both trends that promote competition as a source of governmental efficiency (Tiebout 1956, Savas 2000). Shifting from state to market via privatization of local government service delivery, and shifting from national to local levels of provision via decentralization are designed to increase local voice and local control over service delivery (Bennett 1990). Technical efficiency is enhanced by linking service delivery and revenue raising so that fiscal equivalence (you get what you pay for) is reached. U.S. local governments, as part of a federal system, have some of the highest levels of local government autonomy in revenue raising and service delivery responsibility of any country in the advanced industrialized world (Conlan 1998). This autonomy encourages efficiency, fiscal responsibility and competition among local governments (Musgrave 1959, Oates 1998). While there is little doubt that fiscal federalism encourages productive efficiency, there is considerable concern about whether it also promotes allocative efficiency (Prudhomme 1995). Decentralized and privatized systems require a level of technical capacity, both managerial and financial, to ensure that efficiency is reached. They further require a level of citizen engagement to ensure accountability of government.

U.S. local governments are perhaps in the best position to be successful under decentralized systems because of a long history of autonomy in a federal system (Musgrave 1959, Conlan 1998). Property taxes, which are by and large controlled locally, account for the major source of local government revenue. Communities can select their tax and expenditure levels according to local preference – much as Charles Tiebout described in his model of competitive local government (1956). The theory of Public Choice argues this creates a healthy competition that keeps costs down and limits over-production in the public sector. It also focuses local government on economic development rather than redistributive priorities (Peterson 1981, Schneider 1989, O'Connor 1973).

This developmental focus has benefits and costs. One of the costs is the emergence of a destructive competition as local governments compete with each other to attract economic development through tax breaks that undermine the public infrastructure basis for long term economic sustainability (Donahue 1997, Conlan 1998). Although

meta analysis of research shows that investments in public infrastructure have a more positive impact on economic development than tax breaks (Bartik 1996), the most popular policies among local governments in the U.S. continue to be tax breaks (Lynch 2004, Warner 2001a).

Those concerned with allocative efficiency point out that under this competitive local government system there are winners and losers. Places with economic development have stronger tax bases and more revenue to invest in further development. This virtuous cycle is contrasted with a vicious cycle in places that have weak economic development, limited tax bases, and limited capacity for investment. Under decentralization we find the places most likely to be caught in these vicious cycles are high poverty rural and inner city areas (Warner and Pratt 2005). Reeder and Jansen (1995) labeled these places, poor governments and showed how poor governments are associated with poor places. If government is to play a countercyclical role, then decentralization undermines the possibility for redistribution.

Under globalization, many geographers have heralded the resurgence of the city as local governments can engage directly with global economic forces to promote their own economic competitiveness (Brenner 1999, MacLeod 2001, Swyngedouw 1997). The nation state, weakened relatively by global power and local resurgence, becomes less focused on redistribution and more focused on promoting growth (Brenner 2004). But what does this portend for rural places, which are not growth centers? Will they continue to capture national interest? National rural policy has traditionally been justified by an equity-based redistributive strategy which views the nation's role as equalizing the inequalities of market based economic development (Edwards 1981, Hansen et al. 1990, Brown and Warner 1991). At a minimum, national investment was used to promote equality in basic infrastructure through programs to ensure that electricity (Tennessee Valley Authority, Rural Utilities Service, rural electric cooperatives), telephones, highways (interstate highway system, and Federal transportation aid) and water systems (through the Rural Community Assistance Program) were extended to all parts of the country. But the new technological advances in telecommunications have met with no such federal commitment and many rural areas are literally off the grid for fiber optics and cable for high speed internet (Grubestic and Murray 2004).

Support for regional policy in the United States has waned in recent decades. In the 1980s, Reagan promoted a „new federalism“ designed to pass responsibilities, but not revenue to local governments (Nathan and Lago 1990). As states and localities complained of unfunded mandates, the Clinton Administration responded by allowing more state and local control over policy determination, particularly in areas like welfare entitlement and service levels. Design and entitlement levels in basic programs like health care, welfare and job training now have substantial state and local variation (Weinstein 1998, Powers 1999). Michael Katz (2001) has termed this the „price of citizenship“, noting that this creates a variegated landscape of resources and benefits that accrue to citizens based on where they live. The role of the sub-national regional government becomes more important under decentralization and in the US, research has found state aid to be redistributive (Johnson, et al 1995, Reeder and Jansen 1995, Warner 2001b). However, rural researchers worry about the decreased emphasis on rural areas (Brown and Swanson 2003, Lobao et al 1999).

Privatization may offer a partial solution to this retreat of federal government involvement. Private providers could potentially offer rural areas the economies of scale they lack at the local government level. Certainly as Clean Water Act standards rise and rural local water systems become fully depreciated, the technical needs of meeting rising environmental standards, and the financial reinvestment costs to replace deteriorated public systems might be well met by private providers. Indeed, one of the goals of the General Agreement on Trade in Services, currently under negotiation, is to expand foreign private investment opportunities in basic local government services such as water (Gerbas and Warner 2007, Appleton 1994).

Rural residents in the United States are used to relying more heavily on private suppliers for many services which might be publicly provided in more urban places. Thus one would expect strong public opinion in favor of private delivery. However, recent research focusing on the transactions costs of contracting, points to the need for strong managerial capacity, the ability to structure the market to ensure competition among alternative suppliers, and the need for monitoring to ensure service quality and attention to public values (Sclar 2000, Nelson 1997, Lowery 1998, Hefetz and Warner 2004, Brown and Potoski 2003). Whether rural areas have the capacity to manage private markets for service delivery is an empirical question.

The overall concern is that these competitive approaches to basic local government services delivery will undermine both the political and economic basis for redistribution. Privatization and decentralization encourage a privatized view of public services and the revenue streams to support them (Frug 1999). If rural areas are disadvantaged under both systems, then the prospects for rural development dim as we look forward to the new century.

This paper uses national survey and census data to assess how rural areas are faring under privatization and decentralization. Results show rural areas are disadvantaged under both systems and this disadvantage both results from and creates structural impediments to market competitiveness for rural areas.

Data: Local Government Restructuring by Metro Status

This analysis is based on data from two sources: the International City/County Management Association surveys of alternative service delivery, and the United States Census of Government Finance files. Each of these surveys is administered quinquennially and this analysis includes data from the 1992, 1997 and 2002 surveys. The ICMA surveys are conducted every five years and cover all counties with more than 25,000 population and cities over 10,000 population. In addition, a sample is drawn from one in eight cities and counties from 2500 to 9,999 population and from those under 2,500 (total sample frame in 1997: 4,952). Roughly a third of all governments contacted respond (31% for 1992, 32% for 1997 and 24% for 2002). Cities (which include villages, towns and townships) vastly outnumber counties, but counties are more heavily represented among the rural respondents. Of the roughly 1,200 to 1,400 responding governments in any given year, roughly 350 are non-metropolitan. We use a repeated cross section analysis to preserve sample size.

Governments are differentiated by metro status according to the following criteria. First, rural-urban continuum codes developed by the U.S. Dept. of Agriculture distinguish municipalities by metropolitan and non-metropolitan status. Non-metropolitan

municipalities are further differentiated as adjacent or non-adjacent to a metropolitan county. For municipalities within metropolitan counties, we differentiate core metropolitan municipalities from outlying suburban municipalities using Office of Management and Budget criteria. Core cities have 40 percent of their residents working in the central city of the Metropolitan Statistical Area and employment residence ratios of at least 0.75. All other metropolitan cities are classified as outlying--suburban.

The ICMA surveys measure direct public provision and six alternative forms of service delivery (for-profit, non-profit, inter-municipal cooperation, franchises, subsidies and volunteers) for 64 different services in seven broad areas: public works and transportation, public utilities, public safety, health and human services, parks and recreation, culture and art, and support functions. The surveys also measure government managers' responses to a range of managerial and structural factors believed to be motivators or obstacles to alternative service delivery. We supplement these factors with socioeconomic and government expenditure data drawn from the City/County Data Book, based on Census of Population and Housing for 1990 and 2000 and the Census of Government Finance files for 1992, 1997 and 2002.

Although the Census of Government includes all governments and thus could be a better data source for analyzing rural governments, it has undergone considerable structural revision from survey to survey, making trend comparisons difficult. In addition, the Census of Government does not cover as broad a range of services. Only 14 services were consistently measured in all three years and three of these are rarely provided by rural municipalities: airports, public transit and hospitals. Neither does the Census cover as broad a set of service delivery alternatives. Contracting out is the only service delivery alternative measured by service in 1992 and 1997, and inter-municipal cooperation was only differentiated by service in the 2002 survey. Many governments in the US Census of Government provide no data about service provision. Although the ICMA sample size is much smaller, the greater consistency in survey design, and greater coverage of services and service delivery alternatives make it a better source for comparing rural and urban service delivery patterns over time.

Figure one shows the average use of the three major forms of public service delivery, differentiated by rural, outlying suburban and metro core places. The top set of graphs in figure one show that rural governments' use of for-profit privatization has dropped dramatically since 1997. Rural areas tracked suburban and metro trends from 1992 to 1997 (albeit at a much lower level), increasing their levels of for-profit provision by almost a third (from 12 to 16 percent of service provision on average). However, they diverged after 1997, dropping back down to 12 percent, while suburban use leveled off at 20 percent and metro use of privatization rose to almost meet the suburban level (19 percent). These data suggest that rural areas explored privatization but could not compete well in market based approaches. The leveling off in suburban and metro areas suggests that privatization has limited scope even in urban areas. Indeed overall trends in use of privatization over the twenty year period from 1982 to 2002 show that 1997 is the peak year and privatization never exceeds more than 20 percent of local government service delivery in the U.S.

Figure 1 about here

Inter-municipal cooperation is the next most common form of alternative service delivery but it has been on a downward trend since 1992. The drop in cooperation is most significant for suburbs (from 20 percent to 13 percent) which appear to be substituting privatization for inter-municipal cooperation. Metro core places exhibit a similar drop although their cooperation level is lower to start with due to large internal economies of scale. For rural areas, by contrast, use of cooperation was stable from 1992 to 1997 prompting the suggestion that rural areas might depend more on a cooperative public market of intergovernmental contracting than the competitive private market of for profit privatization (Warner 2003). But the 2002 data do not continue this trend. From 1997 to 2002 rural use of cooperation drops significantly from 15 to 11 percent. Suburban use of cooperation remains the highest of all three metro groups for the entire period. As in the case of for profit contracting, suburban areas are the most favored by inter-municipal cooperation.

The final graph shows direct public service delivery declines for suburban places in 2002 after a slight increase in 1997. Metro areas show a steady drop in public delivery. But rural places exhibit a dramatic increase in direct public delivery, rising from 60 to 66 percent of all service delivery. This return to public delivery, after experimentation with privatization, provides additional indication of problems with access to alternative market forms of service delivery – especially for rural communities.

Modeling: Structural or Attitudinal Constraints?

What explains this divergent behavior of rural municipalities: structural or attitudinal constraints? Rural areas may lack the structural characteristics to be attractive market players. They are higher cost and offer a smaller, less attractive market for potential private providers (Reeder and Jansen 1995, Warner and Hefetz 2003). Suburbs, by contrast have lower costs and offer a larger market. Some argue that limited managerial capacity or opposition might reduce use of privatization (Niskanen 1971, Savas 2000). Table 1 compares the service delivery pattern of local governments as well as differences in managerial and structural factors that may be important in the restructuring decision. Differences in subgroup means and their Duncan multiple range rankings¹ for metro core, rural and suburban governments are compared for all three years. A discriminant analysis model is used to test whether rural municipalities can be distinguished from metro core and suburban municipalities based on service delivery characteristics. In addition, the model controls for structural and attitudinal variables outlined below.

Table 1 about here

Structural Explanation: Market Attractiveness

Will rural municipalities be attractive markets for private suppliers? Previous research has found suburbs to be the most favored (Warner and Hefetz 2002), and problems with supply of private providers in rural (Kodrzycki 1994) and urban areas (Hirsch 1995). Theory and prior empirical analysis suggest a U-shaped cost curve with high costs for rural areas with low density (the cost of sparsity), and for urban areas with high density (the cost of congestion) (Reeder and Jansen 1995, Warner 2001b). Figure 2 uses average per capita expenditure data from the Census of Government Finance and clearly shows this U-shaped cost curve. Rural municipalities expenditures are almost as high as metro core places on a per capita basis even though they provide a much smaller

range of services. Although there has been a steady decline in real expenditures per capita since 1992, the U-shaped cost curve has persisted. High costs would be a deterrent to both for profit private providers and to neighboring municipalities. Market solutions are voluntary, and rural areas are less attractive to alternative providers. Suburbs, because of their lower costs and larger market (large number of municipalities in each region), provide an excellent market for both privatization and inter-municipal contracting.

Figure 2 about here

Higher poverty and lower income should also reduce the attractiveness of rural areas to market providers. Data from the US Census of Population and Housing conducted in 1990 and 2000 show that per capita income is relatively flat in real terms over the time period but always lowest for rural areas and highest for suburbs. Similarly, percent poverty is highest for rural areas and lowest for suburbs although poverty drops slightly for rural areas in the 2000 Census. See Table 1.

Government policy can play a redistributive role, helping to reduce the negative impact of the rural structural deficits. Although US local governments rely primarily on locally raised revenues (property taxes, sales taxes and user fees), state aid is the second most important source of revenue for local governments. Federal aid to place, at less than three percent of total revenue, has dropped so much under decentralization, that it ceases to be significant for many local governments. State aid, after rising slightly for suburban and metro areas from 1992 to 1997, dropped to below 1992 levels in real terms by 2002. State aid, which was higher for rural areas (than metro or suburbs) in 1992, at \$190 per capita, has dropped steadily over the ten year period and is now only \$155 in real terms.ⁱⁱ Although rural areas still receive more state aid per capita than suburbs, they now receive less than metro core areas, as the attention is focused on promoting urban growth centers over lagging rural areas.

Rural economies remain relatively dependent on governmental employment (Singleman and Deseran 1993). The percentage of rural employment in public administration dropped significantly from 5 percent in 1997 to 3.5 percent in 2002, but rural areas continued to have higher dependence on public employment than their suburban or metro core counterparts.

A state rules index is based on local government managers attitudes about the impact of state limits on taxation and state rules encouraging inter-governmental financing on their restructuring decisions. The importance of these state rules drops over the three time periods, and in each time period, a lower percentage of rural governments reports that state rules are a factor in their decision to restructure.

Attitudinal Explanation: Managerial Capacity and Opposition

A second explanation for limited rural privatization could be managerial or attitudinal constraints. Although rural areas tend to be pro-market, they may lack the managerial capability to manage market contracts. But limited capacity could encourage rural areas to out source services to the private sector. We see in Table 1 however, that rural areas have service provision levels similar to suburbs. Governments with a professional appointed manager and an elected council are assumed to have more

managerial capacity. While two thirds of suburbs have this council-manager form of government, less than half of rural municipalities do, and the number is dropping. This reflects the high cost of professional managers and short supply. The drop in council manager form of government in metro core areas reflects the rise in use of elected executives to manage both the political and managerial concerns that arise in more complex and heterogeneous metropolitan areas (Hambleton 2002).

Rural areas are less likely to have opposition to privatization. The opposition index is constructed from five ICMA survey questions that ask managers to identify factors important in their decision to restructure: internal opposition from employees, department heads and elected officials, restrictive labor agreements and external opposition from citizens.ⁱⁱⁱ Opposition is highest for metro core municipalities and lowest for rural areas. Opposition shows a slight rise for rural areas in 1997, with the rise in privatization, but it is always lower for rural areas than for suburbs or metro places.

Government attitudes to reduce costs of service production are measured by two ICMA survey questions: has the government studied the feasibility of alternative service delivery, and is it motivated to decrease costs. Concern about costs is highest among metro core places which have the highest average expenditures. Suburbs, which are most likely to be in a competitive Tiebout-style market competing with their neighbors to attract mobile residents are next, and rural areas are lowest.

To ensure savings from the contracting process requires an external monitoring system. Metro core areas show the highest levels of monitoring – a reflection of their more heterogeneous service demands and the complexity of urban service delivery systems. Even though metro monitoring levels have increased over the ten year period, less than half the governments monitor their contracts. This may help explain why privatization levels have not grown dramatically - performance management systems have not evolved to the level required to support higher levels of contracting. The level of contract monitoring is lowest for rural areas. Suburbs have moderate levels of monitoring that have not risen with a rise in contracting. They face a more competitive market of private service providers and may be able to rely more on competitive market pressures among alternative providers to ensure efficiency gains.

Analysis

Building upon a discriminant analysis first conducted by (Warner and Hefetz 2003) for the 1992 and 1997 surveys, this paper adds the 2002 data to look at differences over time. The discriminant analysis determines if there are differences by metro status in use of alternative service delivery mechanisms (public delivery and contracting to for profit, inter-municipal or non profit providers). Structural factors of market attractiveness (expenditure, income, poverty, state aid, and state rules), as well as managerial factors (professional managers, opposition, governmental attitudes and monitoring) are included.

Discriminant analysis determines which variables discriminate maximally among fixed categories (metro status in this case). The analysis produces functions (one fewer than the number of fixed categories) which are analogous to regression equations except that only the predictor variables are random.^{iv} The discriminant analysis shows that local government restructuring behavior can be differentiated by metro status. Interestingly, the factors cluster into groups that distinguish structural from managerial factors. For the

1992 and 1997 (and to a lesser extent 2002) models, the first function captures most of the structural variables and shows a strong correlation between high income, low poverty and high privatization – suggesting that privatization is primarily driven by the market attractiveness of a place. These structural variables explain from 82-86 percent of the variance in all three of the model years. See Table 2.

Table 2 about here

Managerial variables which cluster as government attitude, monitoring, opposition, state rules and council manager, explain 14-18 percent of the variance. Rural areas rank highest on the structural function and lowest on the managerial function in all three models suggesting that structural factors are more critical in differentiating rural restructuring than managerial factors. Classification results show suburban places are most likely to be classified correctly (72 - 74 percent of the time), whereas metro and rural are correctly classified 55-58 percent of the time. When misclassified, metro and rural places are more likely to be confused with each other than with suburban places. These results suggest it is structural market constraints, not managerial attitudes that explain differences in the levels of privatization by metro status.

Changes in the variable clustering over the three model years show state aid and local expenditure clustered with the structural variables in both 1992 and 2002 but clustered with managerial variables in 1997. Recall from Figure 2 that the U-shaped expenditure curve showed less expenditure differences by metro status in 1997. State aid was rising for suburbs and metro core areas from 1992 to 1997 which could have given managers more flexibility. Another shift was percent employment in public administration which became part of the structural function for 1997 and 2002, as its importance for rural areas, relative to other places grew.

The level of for profit and total public service delivery clustered with the structural variables for the first two time periods, but became more of a managerial choice in 2002 and the management function rose in its explanatory power to 18 percent. But rural places continued to rank lowest on the managerial function (centroid value of -0.31 to -0.46, while the suburban value was near zero, and the metro value near +0.50). See Table 3. While suburban managers may be able to exercise more managerial discretion in their choice of privatization, rural areas still appear to be driven primarily by structural market attractiveness constraints (+0.82 for rural compared to -0.78 for suburbs).

Table 3 about here

Discussion

From 1992, when the book *Reinventing Government* by Osborne and Gaebler was first published (and widely read by local officials), to 1997 we see a significant increase in experimentation with privatization. But the leveling off in 2002 for suburban and urban areas, and the precipitous drop for rural areas, suggest problems with the market. Unlike the United Kingdom and Australia (which had compulsory competitive tendering), privatization was not required of local governments in the United States. Recognizing that privatization is not a one way street, the 2002 survey of the International City County Management asks specifically why local governments have brought previously privatized

services back in house. The answers dealt primarily with problems with service quality (73 percent) and lack of cost savings (51 percent). Political concerns ranked much lower in the list of reasons (22 percent) (Warner and Hefetz 2004).

Cost studies of privatization are difficult to find. George Boyne (1998) in his meta analysis of such studies from the U.S. and Europe demonstrated that one could not conclude privatization saves money. Before and after comparisons are hard to find, model specification is poor, and coefficients range from positive to negative to non-significant. This is reflected in the case study data which show both successes and failures (Sclar 2000, Savas 2000). A more recent meta analysis of privatization and costs in water distribution and waste collection finds little evidence of cost savings, especially in the more recent studies (Bel and Warner 2006).

For rural areas, one of the main challenges may be lack of market access. Rural areas are less attractive to private for profit providers, and they have less managerial capacity to engage in market forms of service delivery. Williamson (1996) points out that internal production (hierarchy) will be preferred to contracting when there is high uncertainty, high costs of contracting (including search costs) and lack of competitive markets. These reasons may explain the drop in use of for profit contracting among rural places.

Although privatization among local governments has leveled off and is actually dropping for rural governments, at the national level privatization remains an important political project. The Workforce Investment Act of 1998, for example, specified that local governments should use private providers for workforce development services (Hipp and Warner 2006, King 1999). For many rural areas this proved difficult and undermined any potential for competition, since there were too few jobs to accommodate all the welfare leavers and private employment training providers were concentrated in the cities and suburbs where the jobs are (Weber et al. 2002).

Support for privatization is one of the goals of the new generation of free trade agreements. These agreements are negotiated by national governments but have critical impacts on local government authority over service delivery (Warner and Gerbasi 2004). Beginning with the North American Free Trade Agreement (NAFTA) between the U.S. Canada and Mexico, passed in 1995, we see a new set of market governance arrangements which may further weaken local government authority.

In order to use market approaches to public service delivery, local governments must be able to negotiate and monitor contracts and have access to a common dispute resolution mechanism should disagreements arise (Gerbasi and Warner 2007). However, the arbitration mechanism used under NAFTA is private, not subject to any public accountability or freedom of information act rules, and open only to nation states and private foreign investors (Grieder 2001). NAFTA reinterprets government action as potential barriers to trade, and local laws regarding residency requirements, local purchasing requirements or bonding fall outside the narrow cost and quality criteria deemed appropriate for regulation (Schweke and Stumberg 2000). Furthermore, local governments wishing to impose regulations that respond to unique local conditions may be challenged for reducing potential foreign profit or market share. This biases the playing field further in favor of foreign investors, over rural local governments, and is

likely to make it even more difficult for rural governments to achieve public service delivery through privatization.

For example, a rural town in Mexico, which refused to issue a building permit for a toxic waste facility, was required by a NAFTA tribunal to reimburse the US based firm, Metalclad, for all of its investment costs in building construction (Tysoe 2001).

The U.S. was recently challenged for allowing the State of California to regulate MTBE, a gasoline additive that had contaminated many local community water supplies, because reducing MTBE was not the „least trade restrictive approach to protecting ground water. The Canadian manufacturer, Methanex, argued that controlling the thousands of underground storage tanks across the state would be less trade restrictive (although more costly and less effective in protecting the public health) (Lazar 2000) . Although the Canadian case recently failed (U.S. Dept of State 2005), neither the State of California nor its affected municipalities were allowed to be the party to arbitration proceedings about their own laws.

Even at the national level we are beginning to see some challenges to public subsidy for rural delivery under NAFTA. United Parcel Service, a private US package delivery company, is challenging the Canadian Royal Post's implicit subsidy of rural package delivery by having packages travel in the same conveyances as its letter service. UPS is asking that the implicit subsidy be abolished, or that UPS packages have equal access to the Royal Post trucks and planes for its packages (IISD 2001). Canada, as a large rural country, has a public interest in maintaining communication connections as part of building a national sense of community. While Europe does not have house to house mail delivery, in the U.S. and Canada the tradition of rural free delivery and government supported post offices in *every* rural town has helped to link rural towns scattered across the frontier (Sclar 2000). UPS is challenging a traditional government service and a public decision to subsidize rural areas.

These new free trade agreements make clear that the only criteria on which services can be judged are cost and quality. To create a level playing field there can be no subsidies for public providers that are not extended also to foreign private investors. Although most challenges are still under arbitration, they raise concerns about the ability to retain subsidies for rural service delivery.

The General Agreement on Trade in Services (GATS), currently under discussion, expands the list of covered services to include many public services – education, environmental management, business services, etc. (Appleton 1994, GATS 1995, Gerbas and Warner 2007). However, it is doubtful that opening public service markets to foreign private competition will widen the supply of alternative private deliverers for rural areas given their higher costs. In fact, such agreements may actually narrow the range of public services that rural areas now receive. So we may be faced in the future with a double challenge – rural areas, less attractive to private suppliers will enjoy fewer private services, and any subsidies to ensure continued public service delivery (a form of delivery that is growing in rural communities) may be challenged by those same private suppliers who choose not to serve rural communities.

Cost pressures in the last decade have led to the closure of many basic services in rural communities – hospitals, bus and air service are particularly notable. Increasingly rural areas are becoming disconnected from the wider society at a time when

telecommunications offers the possibility that rural areas might have a new economic role that could overcome the disadvantage of distance. But without public investment to ensure critical extension of telecommunications infrastructure, and lack of profit to encourage private investment, rural areas get left behind. Basic local government services are key to quality of life in rural areas but higher costs, and lower ability to engage alternative market forms of provision, and declining national interest in investments to ensure distributional equity put rural areas at a triple disadvantage.

Conclusion

These trends do not bode well for rural local governments. Increased pressure to be competitive will not, in itself, improve the competitive position of rural governments. As the logic of economic competitiveness and efficiency trumps concerns with local voice and cross jurisdictional equity, we can expect more and more rural places to be left behind. Decentralization works best in contexts where inequality across jurisdictions is low. But in the U.S. we see increasing spatial inequality within regions, in part as a result of decentralization itself (Deweese et al 2003, Johnson et al 1995, Warner and Pratt 2005). Similarly, privatization works best in medium sized suburbs which enjoy both market competition and managerial talent to manage private providers. Rural areas in the US are not favored by either of these trends. Furthermore the new free trade rules privilege foreign investors and market access over citizen voice and local government authority.

Does the capacity and competitiveness of rural governments matter for development in the 21st century? As attention is directed more toward global competitiveness based on investment in centers of growth, the ability to achieve equity and provide basic services in rural areas will become more difficult. There are limits to the applicability of decentralization and privatization, and trends data from the last decade in the United States suggest those limits may have been reached.

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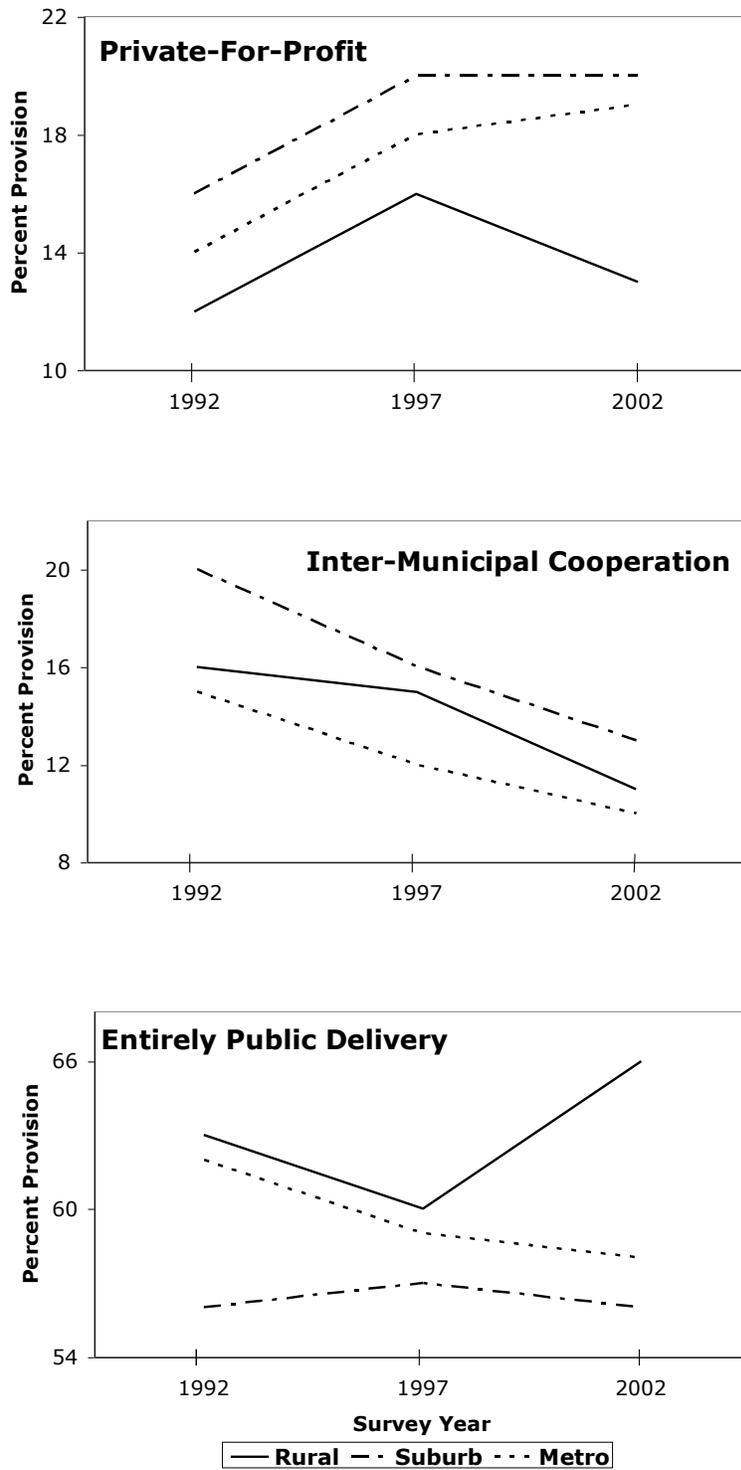
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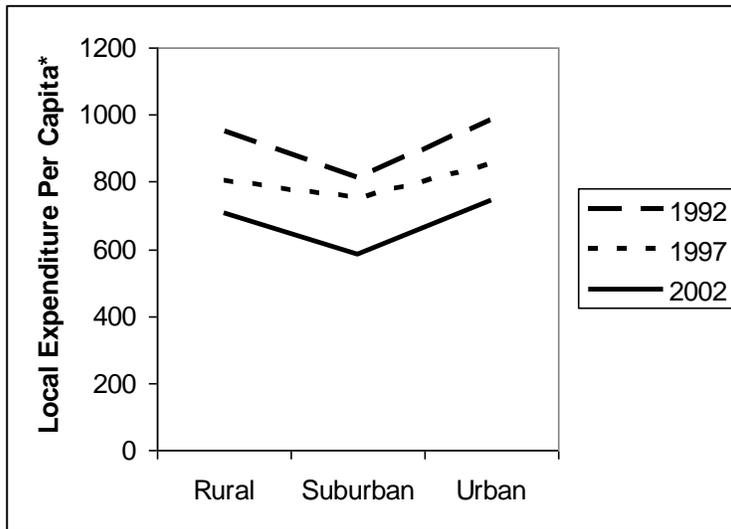
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Figure 1: Rural-Urban Differences in Service Delivery Patterns



Source: International City/County Management Association Alternative Service Delivery Data 1992, 1997, 2002

Figure 2 Trends in U.S. Local Government Expenditure Patterns by Metro Status 1992-2002



Source: Census of Government Finance Files 1992, 1997, 2002 for municipalities responding to ICMA Survey of Alternative Delivery 1992, 1997, 2002

*deflated 1992 = 100

Table 1: Subgroup Means with Duncan Rankings
U.S. Cities and Counties

Variable:	Survey 1992			Survey 1997			Survey 2002		
	Rural	Suburb	Metro	Rural	Suburb	Metro	Rural	Suburb	Metro
Service Delivery Options:*									
% Entirely Public ¹	63 ^b	56 ^a	62 ^b	60 ^a	57 ^a	59 ^a	66 ^b	55 ^a	58 ^a
% Private For-Profit ¹	12 ^a	16 ^b	14 ^a	16 ^a	20 ^b	18 ^b	12 ^a	20 ^b	19 ^b
% Cooperation ¹	16 ^a	20 ^b	15 ^a	15 ^b	16 ^b	12 ^a	11 ^a	13 ^b	11 ^a
% Private Non-Profit ¹	5 ^a	4 ^a	6 ^b	5 ^b	4 ^a	6 ^c	4 ^a	4 ^a	7 ^b
Management & Attitudinal Variables:									
Opposition Index ¹	.13 ^a	.17 ^b	.24 ^c	.16 ^a	.17 ^a	.26 ^b	.13 ^a	.15 ^a	.22 ^b
Council Manager ¹ (1=mgr, 0=not)	.53 ^a	.67 ^b	.67 ^b	.46 ^a	.68 ^b	.65 ^b	.42 ^a	.68 ^c	.50 ^b
Government Attitude Index ¹	.53 ^a	.67 ^b	.80 ^c	.52 ^a	.62 ^b	.85 ^c	.45 ^a	.53 ^b	.71 ^c
Monitoring Index ¹	.24 ^a	.38 ^b	.41 ^b	.23 ^a	.37 ^b	.46 ^c	.25 ^a	.38 ^b	.49 ^c
Structural Variables:									
Per Capita Income, 1989 ²	11,228 ^a	17,548 ^c	13,880 ^b	11,256 ^a	17,299 ^c	13,776 ^b	13,241 ^a	20,206 ^c	16,098 ^b
% Poverty, 1989 ²	17.3 ^c	7.8 ^a	14.4 ^b	17.4 ^c	7.6 ^a	14.4 ^b	15.6 ^c	7.7 ^a	14.5 ^b
Provision Level (# services provided) ¹	41 ^a	41 ^a	45 ^b	33 ^a	33 ^a	40 ^b	35 ^a	34 ^a	40 ^b
% in Public Administration, 1989 (civilian) ²	4.8 ^b	4.2 ^a	4.9 ^b	5.0 ^b	4.3 ^a	5.0 ^b	3.5 ^b	3.1 ^a	3.3 ^{ab}
State Aid, \$ Per Capita, dfl 1992=100 ³	190 ^b	130 ^a	180 ^b	180 ^b	150 ^a	200 ^b	155 ^b	116 ^a	178 ^b
State Rules Index ¹	.20 ^a	.25 ^b	.31 ^c	.15 ^a	.18 ^a	.26 ^b	.14 ^a	.16 ^a	.23 ^b
Local Exp. \$ Per Capita, dfl 1992=100 ³	950 ^b	810 ^a	980 ^b	800 ^{ab}	750 ^a	850 ^b	707 ^b	582 ^a	743 ^b
N	358	750	306	390	714	303	278	512	241

Duncan Post Hoc Ranking of subgroup means, based on $\alpha = .05$; a = lowest, c=highest. *F* test found all variables significantly different ($P < .05$) by metro status, except for “% entirely public” 1997

*as percent of provision level

Sources: ¹International City/ County Management Association, Profile of Alternative Service Delivery Approaches, Survey Data, 1992, 1997, 2002. Washington DC: ICMA. ²City/County Data Book, based on Census of Population and Housing 1990, 2000. Charlottesville, VA: University of Virginia. ³U.S. Bureau of the Census. (1992, 1997, 2002). Census of Governments: State and Local Government Finances, Individual Unit File. Washington, DC: US Dept. of Commerce.

Table 2. Discriminant Function Structure: 1992, 1997 and 2002

	1992		1997		2002	
	Function 1 Structural Factors	Function 2 Managerial Factors	Function 1 Structural Factors	Function 2 Managerial Factors	Function 1 Structural Factors	Function 2 Managerial Factors
% Poverty 1989	+		+		+	
Per Capita Income 1989	-		-		-	
% Entirely Public	+		+			-
% Private For-Profit	-		-			+
State Aid, Per Capita	+			+	+	
Local Government Expenditure Per Capita	+			+	+	
Government Attitude Index		+		+		
Opposition Index		+		+		+
Monitoring Index		+		+		+
Service Provision Level		+		+		+
State Rules Index		+		+		+
% Private Non-Profit		+		+		+
Council Manager		+		+	-	+
% Cooperation		-		-	-	
% in Public Administration 1989		+	+		+	
Percent Variance Explained	86.1	13.9	83.4	16.6	81.8	18.2

* Largest absolute correlation between each variable and any discriminant function

Table 3. Centroid Values by Metro Status

	1992		1997		2002	
	Function 1 Structural Factors	Function 2 Managerial Factors	Function 1 Structural Factors	Function 2 Managerial Factors	Function 1 Structural Factors	Function 2 Managerial Factors
Rural	.95	-.31	.94	-.35	.82	-.46
Suburban	-.66	-.06	-.73	-.07	-.78	-.09
Metro	.49	.51	.51	.60	.71	.58

Endnotes

ⁱ The Duncan multiple range method tests the hypothesis that one subgroup mean is significantly larger than another. Group means are clustered and ranked based on a 0.05 significance level.

ⁱⁱ State aid and local government expenditures in 1997 and 2002 are deflated using the GDP Implicit Price Deflator for state and local government expenditures. 1992 = 100 is the base year (Economic Report of the President 2005).

ⁱⁱⁱ This index and the other indices used in this paper are created by summing positive responses to component questions and dividing by the total number of questions in the index. $\frac{\sum_{i=1}^N f_i}{N}$, where $f_i = 1$ if checked yes to question and 0 if not, and $i = 1, 2, \dots, N$ for questions.

^{iv} Logistic regression is not appropriate in this case because regression requires the dependent variable to be random and our dependent variable, metro status, is a fixed category.