Giving Money Away? The Politics of Direct Distribution in Resource-Rich States

Alexandra Gillies

Abstract

The governments of resource-rich states have several options for how to allocate oil and mineral revenues, including the direct distribution of revenues to their citizens. This paper discusses the political feasibility and political implications of such cash transfers in the specific context of resource-rich states. Identifying the contexts in which this policy is mostly likely to emerge, and understanding the potential governance risks and benefits, will help policymakers to consider the desirability of cash transfers as an allocation choice. Cash transfers could have positive political and governance effects, but they should not be taken for granted. Possible benefits include the creation of a constituency in favor of sound natural resource management, a more level playing field between the state and the citizens, the emergence of broad-based taxation and its positive accountability effects, and less of the principal-agent problems that currently keep resources from serving the public interest. These effects may not play out in all resource-rich states, as transfers could end up reflecting rather than reducing the extortion and rentierism that frequent these contexts. Careful country selection, strong understandings of the context, and politically aware program design could increase the likelihood that cash transfers contribute to more favorable governance outcomes.

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Giving Money Away:
The Politics of Direct Distribution in Resource Rich States

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Foreword

The discovery of oil in a developing country is potentially beneficial and, simultaneously, potentially calamitous. While countries could put oil revenues toward building much-needed schools and roads, fixing and staffing health systems, and policing the streets, many resource-rich states fare little better—and often much worse—than their counterparts. Too often public money is misallocated and funds meant to be saved are raided, and those living in poor resource-rich countries pay the price. While this so-called resource curse is well established in the literature, solutions to counteract its corrosive effects remain highly elusive.

CGD is exploring one policy option that may address the root mechanism of the resource curse: using cash transfers to hand the money directly to citizens and thereby protect the social contract between the government and its people. Under this proposal, a government would transfer some or all of the revenue from natural resource extraction to citizens in universal, transparent, and regular payments. The state would treat these payments as normal income and tax it accordingly—thus forcing the state to collect taxes, fostering public accountability and responsible management of the natural resources.

This paper by Alexandra Gillies, commissioned by CGD as part of our Oil to Cash initiative, addresses the political feasibility and political implications of such a scheme.[1] Under what conditions is direct distribution even possible? What political conditions would facilitate its implementation? What would be the possible impact of such a scheme on political institutions and public accountability? While the answers to some of these questions remain speculative and mixed, Gillies provides key insights into the political calculations of natural resource rents by highlighting some potential obstacles, as well as some promising possibilities, for implementing just such a direct distribution scheme.

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[1] http://www.cgdev.org/section/initiatives/_active/revenues_distribution

Executive Summary

The governments of resource rich states have several options for how to allocate oil and mineral revenues, including the direct distribution of revenues to their citizens. This paper discusses the political feasibility and political implications of such cash transfers in the specific context of resource rich states. Identifying the contexts where this policy is mostly likely to emerge, and understanding the potential governance risks and benefits, will help policymakers to consider the desirability of cash transfers as an allocation choice.

Leaders who enjoy large resource rents often distribute them in ways that protect and augment their own positions of power. Therefore, leaders are most likely to adopt direct distribution when they value the political support of the majority, as citizens constitute the greatest beneficiaries of this policy choice. Cash transfers become most likely, therefore, in several scenarios: the arrival of new resource rents or a new political dispensation; a democracy or other broad-based system in which the majority determines political outcomes; a post-conflict period in which leaders seek to generate citizen buy-in; or a country led by individuals who seek to improve their reputation or legacy. In each of these scenarios, the costs of allocating revenues to citizens will be lower if the leader enjoys some autonomy from inter-factional political competition and if the resource rent is sustainably large.

Cash transfers could have positive political and governance effects, but they should not be taken for granted. Possible benefits include the creation of a constituency in favor of sound natural resource management, a more level playing field between the state and the citizens, the emergence of broad-based taxation and its positive accountability effects, and less of the principal-agent problems that currently keep resources from serving the public interest. These effects may not play out in all resource rich states, as transfers could end up reflecting rather than reducing the extortion and rentierism that frequent these contexts. Careful country selection, strong understandings of the context, and politically-aware program design could increase the likelihood that cash transfers contribute to more favorable governance outcomes.

Introduction

The governments of oil and mineral rich countries face the decision of how best to allocate the revenues earned from their natural resources. In contexts where resource revenues constitute a significant portion of the economy, allocation decisions both determine and are determined by the prevailing political environment. The interplay between allocation decisions and politics becomes crucial to understanding the policymaking environment in resource rich states as well as the impact that selected policies will have.

One allocation option is to distribute all or a portion of natural resource revenues directly to citizens. Known as direct distribution or cash transfers, this idea has gained increasing prominence in international academic and policy circles (Palley 2003; Tierney 2003; Birdsall and Subramanian 2004; Sandbu 2005; Shaxson 2008; Moss and Young 2009; Segal 2009; Devarajan, Le et al. 2010), and has been implemented to some degree in locations including Alaska, Bolivia, Timor-Leste and Mongolia. Proponents argue that cash transfers will help countries to avoid the negative economic and political outcomes associated with the resource curse. In addition to bolstering household incomes, these advocates propose that cash transfers would distribute resources from the ruling few to the majority, correcting imbalances in both wealth and power.

The decision to directly distribute revenues and its potential to generate positive effects will depend on the political environment of the country in question. Like many economic policy instruments, it is relatively easy to discuss its desirability in abstraction. But when would a resource-rich government actually choose to allocate revenues to the public rather than through the typical channels of government spending? And, in resource rich environments, would transfers generate the predicted political benefits of greater accountability and better governance?

This paper will first examine the **political feasibility of direct distribution**. A perfectly crafted economic policy tool will have little effect if no government chooses to implement it. Direct distribution represents a high-cost policy choice as it deprives the state of revenues. The first section of the paper identifies several scenarios in which a leader might implement cash transfers. These all relate to the central feasibility dilemma that faces direct distribution: a leader will only choose to allocate resources to the majority if the majority represents a more valuable stakeholder than alternate recipients, including the ruling faction itself.

The second section discusses the **political implications of direct distribution**, and identifies some of the complexities which will condition the emergence of its predicted benefits. Countries with resource dependent economies vary widely in economic performance, levels of conflict and quality of governance.[2] Research indicates that attributes of a country's political landscape help to determine whether the government chooses prudent economic policies and whether the chosen policies are successfully implemented (Dauderstadt 2006; Smith 2006; Lewis 2007; Dunning 2008; Morrison 2009). For instance, natural resource savings funds—a policy

[2] For instance, Malaysia and Indonesia leveraged their petroleum wealth to diversify their economies; Nigeria and Gabon have not. Botswana remains a peaceful democracy, in contrast with fellow diamond producers Angola, Sierra Leone and Liberia. Unlike many countries such as Mexico and Russia, Chile effectively safeguarded its economy from the recent commodity price fluctuation.

instrument often recommended to resource rich states—work well in Norway but failed in Chad. The performance differences stem more from divergent political and institutional contexts than from the design of the fund itself (Humphreys and Sandbu 2007). Similarly, how direct distribution intersects with a country's political environment will determine whether the policy succeeds expanding the public benefits derived from resource wealth.

Some direct distribution advocates believe that cash transfers to citizens can actually alter the country's political incentive environment to favor better outcomes. Unlike saving funds, transparency and other recommended policies that only tend to work in conducive political contexts, direct distribution can help to create a more conducive context by creating a broad-based constituency for responsible revenue management (Sandbu 2005). It would empower citizens, instigate greater accountability through increased taxation, and eliminate principal-agent problems (Sandbu 2005; Moss and Young 2009; Devarajan, Le et al. 2010). However, as discussed here, these arguments depend on causal assumptions that may not apply to many resource rich political environments.

To clarify the scope of this paper, direct distribution is conceived here as the allocation of a portion or all natural resource revenues to each citizen of a country or a resource-rich region. The analysis focuses on developing countries whose economies are dominated by revenues from oil, gas or mining industries, referred to collectively as natural resources. Given the focus on resource revenues, more general cash transfer systems (i.e. not explicitly tied to natural resource revenues) including the extensive conditional cash transfer programs in Latin America are not thoroughly reviewed, though their experiences contain relevant lessons. Finally, given its focus on the *political* feasibility and implications, many important economic, socio-cultural and administrative issues go unaddressed. Along with political determinants, the success of cash transfers will depend on whether people efficiently receive the transfers, what they do with the money, the macroeconomic effects of these usages, and its benefit relative to other possible allocation options.

I. FEASIBILITY

A number of studies address how natural resource wealth shapes a country's political system. Two themes run throughout the majority of these inquiries. First, as "point" industries, petroleum and mineral sectors result in the concentration of resources and power in the hands of the top officials who control the state apparatus (Auty and Kiiski 2001; Eifert, Gelb et al. 2002; Ross 2004; Snyder and Bhavnani 2005; Soares de Oliveira 2007a; Collier 2007b).[3]. This centralization limits constraints on executive decision-making and increases the desirability of holding power (Auty and Gelb 2001; Eifert, Gelb et al. 2002; McGuirk 2010). Therefore, it is appropriate to focus on when a state's leader might choose to implement direct distribution, rather than any more consensus-based form of decision-making. Second, as laid out in the "rentier state" literature (Beblawi and Luciani 1987; Luciani 1987; Beblawi 1990; Yates 1996),

[3] The ownership of petroleum and mining industries is usually vested in the state. This centralizes influence and resources through two effects not present in other sectors like agriculture or manufacturing. First, the government decides how the resources should be extracted including identifying which companies will perform the work. Second, the government receives sizeable direct revenues from this enterprise in addition to taxes on company earnings.

leaders distribute resources so as to protect and augment their positions of power. Recipients gain wealth and influence, but those who control the actual distributive channels wield the greatest control over the political system. As Smith (2006) explains, "Politics in oil-rich countries is fundamentally… about to whom state controlled rents go. In other words, holding the state means acquiring a monopoly or near monopoly on discretionary rent allocation."

These fundamental traits—the centralization of power and the dominance of rent distribution in political affairs—together constitute the most convincing explanation for the observed "proclivity of [resource rich] states to adopt and maintain transparently suboptimal economic policies (Ross 1999)." In weak institutional environments, these proclivities towards suboptimal policy choice worsen still (Mehlum, Moene et al. 2006; Robinson, Torvik et al. 2006). Suboptimal policy choices represent rational decisions by those in power to prioritize their political goals over the economic needs of the country. Thanks to steady supplies of resource wealth, leaders face few obstacles in the pursuit of their interests: extortion and patronage lessen the influence of accountability actors like legislatures and opposition parties, and often undermine democracy as well (Collier 2006; Ross 2009).

While countries vary in the degree to which they exhibit these two tendencies, direct distribution will face them to at least some extent in resource rich political environments. The question is therefore: In a context where those in power enjoy significant degrees of leverage, and use the distribution of resources to improve their political position, when would a leader choose to allocate resources to population rather than through more targeted and malleable channels of public sector spending?

The greatest "winner" of direct distribution is the citizenry, that majority of the population most disserved by the suboptimal proclivities mentioned above. The greatest "loser" would be those rent-seeking elites who would otherwise receive the resources. The feasibility of distribution increases when the leader, as the dominant actor in a resource rich state, places greater value on the winner than the loser.

When might this happen? Below, partially drawn from the ideas of Sandbu (2005) and Shaxson (2008), I present **four scenarios** in which cash transfers might represent an attractive policy option. These are not necessarily mutually-exclusive—a country might exhibit more than one at the same time. I then identify **two factors** which help to determine feasibility across all of the scenarios. Figure 1 provides a summary.

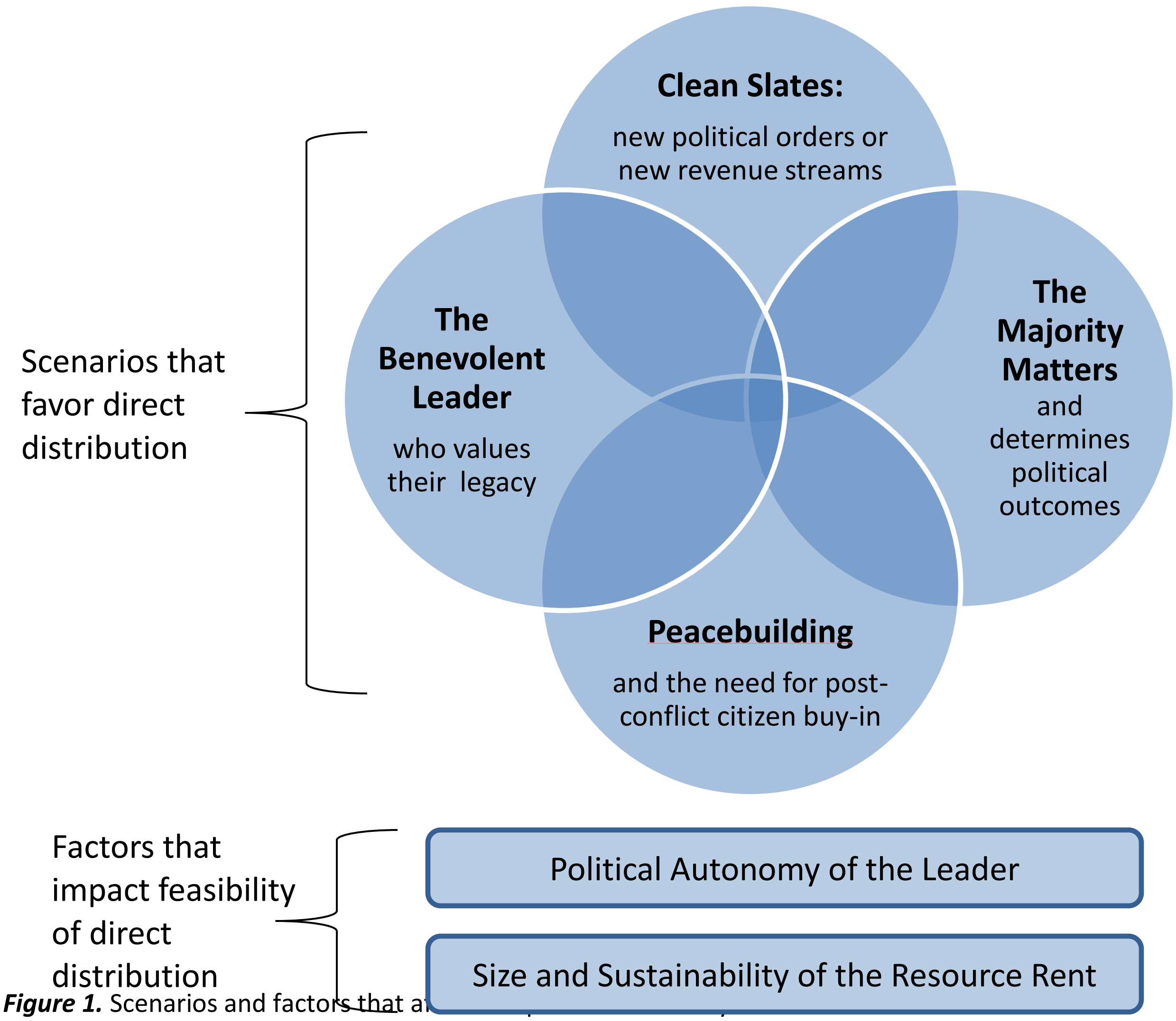

Figure 1. Scenarios and factors that a

Scenario 1. Clean slates

Resources not already allocated to vested interests can be more easily distributed to the population. The losers in the "clean slate" (Shaxson 2008) scenario are only prospective ones—no actor will be forced to relinquish a benefit to which they are accustomed.

One type of clean slate is a **new political order** that lacks pre-established channels for allocation. This would generally arise after a conflict or revolution, such as in Iraq and Timor Leste. New governments usually create constitutional provisions and laws for the management of natural resources, and could enshrine the principle of universal direct distribution in these new legal instruments (Birdsall and Subramanian 2004). **New revenue streams** also create clean slates as they have no previous beneficiaries. Examples include the oil production which will soon debut in Ghana, Liberia, Sierra Leone and Uganda, new natural gas production in Papua New Guinea, and the expected increase in mining revenues in Mongolia. This point should not be overstated. Though less entrenched, expectations attached to new revenues or in a new political order will still exist. Interest groups, including resource producing regions, political factions and recipients of existing oil or mineral revenue streams, will anticipate receiving their perception of a fair share.

Scenario 2. Political competition where the majority matters

In many rentier states, politics is the reserve of elites, and the will of the majority does not determine outcomes. However there are three types of situations in which the majority—the winner of direct distribution—might determine the political fortune of the leader. In these scenarios, the leader might choose cash transfers in order to improve his or her political position.

First, in **a competitive democracy** with free and fair elections, the will of the majority determines who stays in power. The stronger the democracy, the more the majority matters to those who seek office. In Mongolia, promises of cash transfers featured prominently in the 2008 parliamentary elections as the parties vied for the favor of the electorate (Daly 2008). In Alaska, direct distribution was adopted in 1982 following popular disgust at government's wasting of initial oil revenue inflows (Cowper 2007).

Second, **a challenger to the incumbent** could use the offer of direct distribution to gain popular support (Sandbu 2005). This is more likely if the challenger does not benefit greatly from rent-seeking (i.e. if the challenger is not also a loser). Allocating funds to the population would be used to generate support against vested interests and the political status quo. Kazakh opposition party Ak Zohl proposed distributing 75% of all oil taxes to citizens in the 2004 parliamentary elections (Jandosov 2009), and Iranian opposition leader Mehdi Karroubi also proposed cash transfers in 2009 campaign (The Economist 2009). Along with opposition leaders, coup-makers could use this strategy to galvanize popular support.

Third, **a broad political base** can raise the value of the winner, even in the absence of competitive democracy. Governments that rely on support from a broad constituency are more likely to prioritize the well-being of the majority in their economic decision-making. Resource wealth sometimes frees leaders from their reliance on certain constituencies, such as the diminishing role of the merchant class in the politics of Kuwait and Qatar (McGuirk 2010). But in other cases, such as Suharto's reliance on the rural agricultural population and commercial classes of Indonesia (Lewis 2007), such constituencies maintain enough influence to result in improved policymaking. Consensual political systems, such as in Botswana (Shaxson 2008), can serve the same purpose. In either case, the leader could value direct distribution as a policy which appeals to his or her political base.

Scenario 3. To promote peace and unity

Direct distribution could be used to help secure a peace deal by soliciting buy-in from a restive population or a group that seeks secession. Cash transfers represent tangible benefits of the new post-conflict order, and their redistributive nature can reduce grievances (Holmes 2009). In Timor Leste, the provision of cash payments to veterans, the internally-displaced and poor households provided a peace dividend with the aim of stabilizing the country following the 2006 conflict (Pires 2009). Palley (2003) argues that cash transfers could serve a similar purpose in the new Iraqi state, enhancing unity and reducing incentives for inter-factional disputes over the distribution of oil wealth. Limited cash transfer and cash-for-work programs have formed part of peacebuilding strategies in Afghanistan, Nepal, Sierra Leone, and Somalia (Holmes 2009).

Along with securing citizen buy-in during post-conflict periods, direct distribution could be used by central authorities to assuage volatile regions. Senior Nigerian government officials have floated the idea of distributing a portion of petroleum profits to the population of the oil-producing Niger Delta region as part of a post-conflict amnesty deal. The leading advocate of this idea stated that transfers would "give the host and impacted communities a stake in the ownership and sharing of the benefits of petroleum assets (Business Day 2010)." Conceived as such, allocations could serve as a carrot for the cessation of violence.[4]

Scenario 4. The "benevolent" leader

A leader could choose to distribute revenues if they value the acclaim that it would bring. This proposition requires a relatively nuanced view of leader motives. Several political economy analysts seek to categorize leaders by their motivations. In their analysis of resource rich states, Auty and Gelb (2001) differentiate between "benevolent" leaders who seek to advance long-term national interests, and "predatory" leaders who exploit public office for their personal gain. Olson (1993) emphasizes the importance of horizons-- "stationary bandits" invest in their territory in order to maximize returns; "roving bandits" grab as much as possible during temporary stints in power.

Such bifurcated classifications obscure the actual diversity of agendas which impact the selection of policy, including possibly cash transfers. For instance, few would argue that President Teodoro Nguema Obiang of Equatorial Guinea is benevolent; in 2008, his country had Africa's highest GDP per capita at a staggering $28,102, and lowest "control of corruption" and "voice and accountability" scores (World Bank 2010), not to mention negligible efforts at poverty reduction. Yet Obiang employs lobbyists to improve his reputation, indicating that image and prestige also matter to him. Further south in the Gulf of Guinea, the oil-rich Angolan regime of Eduardo dos Santos also records rock bottom governance scores while pursuing an ambitious long-term economic growth strategy.

Put simply, leader motives cannot be reduced to a single agenda. Author and journalist Nicholas Shaxson (2008) describes it well:

> First, it is my belief, based on many years of interviews and on-the-ground observation in Western Africa's oil zones, that some oil-rich African leaders and many of their senior officials do harbour genuine wishes—albeit often mixed with all kinds of other more personalized interests which directly counteract these wishes—to see their countries develop (the fact that they may also be interested in self-enrichment does not negate this).

As such, even leaders of "predatory autocracies" (Eifert, Gelb et al. 2002)—roving bandits who operate with few constraints—could favor cash transfers if they seek public acclaim or a positive legacy. This is more likely if direct distribution resonates with the ideology or vision of development held by the leader. For instance, Bolivian President Evo Morales sought to bolster his populist credentials by introducing the cash transfer of natural gas revenues. Assuming cash transfers do not threaten the leader's agenda, the policy could be adopted to boost a leader's

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[4] In this way, the distribution of revenues to the population of the Niger Delta would broaden the current government policy of paying off militants in order to maintain the ceasefire, a program which has limited sustainability as a peacebuilding strategy and has suffered debilitating administrative problems (Punch 2010).

popularity, safeguard his legacy or to reduce the amount of revenues that future, and potentially less benevolent, leaders will have at their disposal.

The four scenarios represent situations in which a leader of a resource rich state might decide that direct distribution is a desirable policy option. In each of the scenarios, the likelihood of this choice is conditioned by two further factors.

Factor 1. Political autonomy of the leader

In 2008, Libyan President Muammar Gaddafi announced that he would begin distributing almost all the country's oil earnings to the population, and would abolish all but the minimum trappings of the state, handing over responsibilities like education and health to private citizens (Khalaf, England et al. 2008). In the end, Gaddafi backed away from this radical plan. Even an autocrat who has held power since 1969 cannot completely overturn the system which exists around him. However, given the lack of political competition he faces, Gaddafi is perhaps better placed than many leaders to adopt a strikingly new allocation policy like direct distribution.

Political autonomy refers to the level of a leader's independence from institutional constraints and political competition. High degrees of political competition among elite factions, a common occurrence in resource rich environments (Auty and Gelb 2001; Caselli and Cunningham 2009), impairs this autonomy and constrains decisions regarding the allocation of resources. If a leader functions within a factionalized and heterogeneous elite, he or she must use resource revenues to reward allies and appease the opposition. On the other hand, if the leader faces few threats and long horizons, resources will be available for alternate uses such as cash transfers.

Auty and Gelb (2001: 127) draw on this distinction, arguing that a leader in a factional environment "must appease political groupings and thereby risks compromising the coherence of its economic policy", while autonomous leaders "can formulate and pursue its own objectives so that it can implement a coherent economic policy." I agree, mostly. Autonomous leaders are indeed freer to choose optimal economic policy—that does not mean they will do so. Rather, this autonomy must combine with a genuine motive for choosing the optimal policy in question. In the case of direct distribution, an autonomous leader who also encounters one of the four scenarios listed above is the most likely to choose to transfer funds to citizens.

Factor 2. The size of the resource rent

The size of the resource rent will also affect the freedom of policy choice. With large and indefinite resource inflows, a leader can pursue a number of allocations strategies simultaneously. The opportunity costs of direct distribution decrease drastically if enough resources remain for alternate purposes, including patronage.

Moreover, the adoption of ambitious new allocation strategies is more likely during commodity price booms. This tendency explains the relatively unconstrained policymaking in Bolivia, Venezuela and Ecuador during the recent price spike. Weyland (2009: 8) explains:

> Rich natural endowments and the influx of enormous rents in boom times undermine the neoliberal insistence on limitations. Anything seems possible – ultra-cheap gasoline for Venezuelan drivers, subsidized food for consumers in the poor barrios of Caracas, and free health care for all Bolivians, as the Morales government promised in the 2006

constituent assembly campaign. Given seemingly unlimited possibilities, the only issue is political will.

Small or finite windfalls, or those humbled by the country's population size, will not inspire the same kind of freedom of choice.[5] The value of each dollar is higher, increasing the cost of direct distribution beyond what its benefits might bring.

Direct distribution at what scale?

A final point with regard to feasibility is the question of scale. How much of the resource rent will leaders choose to distribute?

One of the strongest arguments in favor of direct distribution is as follows. In resource rich countries, large revenues flow from external sources directly to the state. This reduces state incentives to tax the population, thereby eliminating one of the principal mechanisms through which governments come to act on behalf of their citizenry (Sandbu 2005; Moss and Young 2009; Devarajan, Le et al. 2010). Direct distribution would result in a transfer of wealth from the state to the citizens. In order to reclaim resources and fund its operations, the state would then be motivated to tax the population, thereby creating the positive accountability dynamics of taxation. (This argument is discussed further in section II of this paper.)

Direct distribution will only lead to taxation if an adequate proportion of resource revenues are distributed to the population. If a government distributes 20% of its oil revenues, and retains 80%, the incentive to tax will remain low. It is difficult to identify the threshold at which broad-based taxation will become an attractive option. However, it is safe to assume that the feasibility of cash transfers varies inversely with the size of the transfer. For a government to allocate all or a majority of its resource revenues, the strongest possible variants of the scenarios outlined above would be required.

The Alaska model has proven politically sustainable. The Alaska Permanent Fund receives 25% of oil royalties, which only constitutes around 10% of total state oil earnings (Goldsmith 2002); the rest enter the budget for allocation by the elected officials of the day. Several efforts at restricting government access to the *majority* of resource rents have fared less well. In Timor Leste, 100% of oil revenues enter a special fund to which access is restricted. The government is currently working to relax these restrictions which have proven untenable, both politically and economically. In Chad, the government abandoned allocation laws which it found too restrictive—when the regime faced threats to its security, it took money meant for saving and development spending and used it to buy arms. While large scale distribution would create a powerful constituency of support among the recipient population, this only ensues *after* the initial adoption of such a large-scaled program, which would be a decidedly tough sell.

Sandbu (2005) emphasizes the distinction between gross and net transfers. If the state transferred 100% of resource revenues to the population, and then taxed back 90%, the net

[5] For more on how per capita resource production affects policy outcomes, see Myers (2005). In countries with lower per capita oil production, resource rents can distort the economy but, even if used well, will not be large enough on their own to leverage economic diversification and growth.

transfer would be around the same level as the Alaskan model. This transaction could even be virtual, he suggests: citizens would receive statements that reflect the gross transfer, but the 90% would never actually leaves state accounts. This option might face lower political opposition, but many governments (especially those lacking popular legitimacy) would avoid even this symbolic relinquishment of their exclusive claim on such a large portion of public funds.

This question of scale poses an important dilemma for the proponents of direct distribution.[6] If a political scenario supports the introduction of partial allocations, does that still represent a desirable policy choice given that it will not lead to taxation? Are the governance benefits that flow from taxation what make direct distribution a superior choice to, say, saving for future generations or investing in the country's human or physical capital? If only large-scale distribution will generate the desired effects, the political feasibility of its implementation reduces drastically.

II. IMPLICATIONS

Assuming a government begins to allocate revenues directly to citizens, how would this affect the political landscape? Other studies, including those on conditional cash transfers, shed light on the economic and social effects of transfers. This paper examines how cash transfers might alter the relationship between the state and society.

Supporters of direct distribution propose that it would improve governance in resource rich states through four channels. First, the citizenry would become an active constituency for responsible resource management. Second, cash transfers from the state to citizens would give governments a less monopolistic control over resources and influence. Third, as mentioned above, direct distribution would create incentives for the government to increase broad-based taxes which would generate positive accountability effects. Lastly, direct distribution would avoid the principal-agent problems that currently inhibit the effectiveness of public spending. For each of these arguments, I identify some points of strength and weakness.

This discussion on the political benefits and risks should of course be considered alongside the potential impact of cash transfers on economic growth and poverty reduction. Likely gains in both areas would make a compelling case for its adoption. Given the difficulties of translating resource revenues into public benefits in many countries, the potential risks and benefits of cash transfers should be considered against the current reality rather than an unrealistic ideal.

Create a constituency for responsible resource management

Proponents of direct distribution argue that if citizens receive a portion of natural resource revenues, they will have a direct stake in the prudent management of those resources. Moss and Young (2009) argue that Alaska manufactured such a constituency by distributing oil revenues via the Alaska Permanent Fund, and that other countries can do the same. Others

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[6] The economic implications of direct distribution are not discussed throughout this paper, but it worth flagging that the scale of transfers should also be dictated by economic considerations as well, such as inflation and how the transfer amount will affect its usage by individuals.

agree (Palley 2003; Sandbu 2005; Devarajan, Le et al. 2010), and describe how cash transfers would provide citizens with information about resource revenues and motivate greater popular engagement in extractive sector and fiscal policymaking processes.

Many countries that suffer from resource curse effects lack constituencies that can constrain executive decision-making, such as robust private sectors, democratic institutions, viable opposition parties, etc. This absence of constraints constitutes one of the leading political economy explanations for suboptimal policy choice. For instance, the Chadian government faced no viable domestic opposition to its abandonment of an internationally-advocated oil revenue reform program. On the other hand, the governments of Syria, Malaysia, Indonesia and Egypt were disposed towards better governance even after the discovery of oil because their power bases comprised several large constituencies (Smith 2006). In Norway and Botswana, governments were held accountable by democratic institutions and social norms.

In resource rich contexts which lack these constraints, cash transfer recipients might collectively constitute a motivated constituency capable of holding the executive more accountable in its behavior. In order to protect their receipts, recipients would lobby for the clean and effective administration of the transfers as well as the efficient, transparent and prudent management of the country's natural resources. In many resource rich countries, corruption and poor governance reduce government earnings from the petroleum or mineral sectors. In Nigeria, for instance, the institutions which collect tax and royalties fail to maximize state earnings—so bad is their capacity that they permit companies to engage in "unregulated self-assessment" of the payments they owe to the state (Hart Group 2006e; Hart Group 2008a). This governance failure, widely known and acknowledged in Nigeria, might be more susceptible to change if the population saw it as directly affecting their own income levels.

Two factors could inhibit the emergence of this assumed effect. First, a constituency requires certain tools in order to reach informed decisions and influence policy. The population would need adequate information and capacities in order to recognize the deficiencies in current policies and identify preferable alternatives. This presupposes certain education levels and the free flow of information. Once the recipients take a stand, they also need mechanisms through which to influence government. In the absence of democracy, this will be difficult. In the absence of an independent media, civil society, parliament or other avenues for the aggregation and articulation of interests, this might be impossible.

Second, would direct distribution create a constituency for good governance, or just for cash transfers? Once instituted, the discontinuation of distributions would indeed be unpopular, or "political suicide" as commented with regard to Alaska (Goldsmith 2002; Moss and Young 2009). But will recipients also mobilize on behalf of sound natural resource management and fiscal policies? They could simply lobby for higher and higher transfers, which would accelerate resource depletion rates and discourage saving and investing in public goods (Sandbu 2005). Devarajan, et al. observe in Alaska a "growing apathy from the population on public spending scrutiny and gradually, investment in public goods is neglected" (2010: 13). Similar questions arise around the proposition that that DD will generate citizen buy-in, particularly in post-conflict settings. This could occur, but recipients might also agitate for increasingly larger pay-offs, stimulating potentially destabilizing patterns of extortion.

Correct imbalances of the rentier state

“When oil revenues constitute a large portion of the economy—as much as 50% of GDP in the case of Iraq—channeling them through government means that effectively government runs the economy” (Palley 2003: 4). Such high levels of resource inflows may exceed the state’s absorption capacity, particularly in weak institutional environments. They also create an enclave of public wealth which is difficult to link up with the broader domestic economy. Moreover, large rents inflate the power of the state and its office holders relative to that of the population. This weakens accountability, and generates zero-sum competition over who holds power.

Taking a portion of the resource rents away from government and giving them to the population would help to correct this imbalance. This “radical democratization of economic decision-making” (Shaxson 2008) represents another possible political benefit of DD. By limiting the resources available for state spending, the cost of spending increases. This could encourage fiscal prudence on the part of the state. Moreover, direct distribution would counteract the patterns of centralization which characterize rentier states, in which those at the top distribute their disproportionate wealth to gain further influence. Resources, and presumably influence, would diffuse as funds spread throughout the population.

Direct distribution will indeed move resources from the center out to the population. However, will this counteract rentier tendencies? In rentier states, revenues are centrally collected and then allocated outward into society, often along personal or patronage lines. In Alaska, the leading implementer of direct distribution, the flow of funds is the same, particularly as Alaskans pay no state income tax. Citizens receive a yearly allocation from the Permanent Fund. As they do not pay state income or sales tax, this constitutes their primary fiscal interaction with the state. As a result, “Some feel that the only interest many Alaskans display regarding public issues is the size of their annual dividend check and their only interaction with the government comes when they cash that check…. [This] fostered the feeling that government exists to distribute cash to its citizens, but that citizens do not need to contribute to public life…distorted sense of the function of the public sector” (Goldsmith 2002: 12-17). Particularly during low revenue periods, such as when oil prices dropped in the 1980s, the use of allocated funds for alternate purposes may have represented preferable economic policy, but faced insurmountable political opposition (Cowper 2007).

Public affairs dominated by deciding who gets how much of the oil revenues do not represent a break from rentier patterns of governance. In countries such as Nigeria, competition over allocation has long-dominated the country’s political life. Direct distribution could exacerbate this “cake-sharing psychosis” (Babangida as quoted in Sayne 2010) by keeping the focus on resource control. As Sayne (2010: 36) writes “The fact is that cash, in the Niger Delta, can be a highly addictive substance. Once the tap of easy payments is turned on, turning it off can seem next to impossible. In some oil-producing communities, the briefest of meetings of locals and oil company staff require some form of *dash* to avoid unrest.” Just as higher levels of sub-national transfers have exacerbated conflicts in Peru (Yanguas 2009) and the Niger Delta, cash transfers could *feed* the existing rentier economy, the conflict economy, and the economy of extortion.

Reinforcing the focus on rents and their capture could further distract attention and incentives away from non-extractive economic activities. Growing more sustainable and employment-generating economic sectors can be difficult in the face of the easy money from petroleum and mineral extraction, a tendency exhibited in many oil and mineral rich states (Boone 1990). Direct distribution risks spreading the focus on resource rents throughout the population. Citizens certainly may pay more attention to natural resource governance issues, particularly those which affect the size of the allocation they receive, but this may come at the expense of their focus on more productive economic activities. While states will control less revenue, the country as a whole may not experience a lessening of emphasis on resource rents, or a greater prioritization of long term development over short term gains, both trends which could further constrain the growth of non-extractive sectors.

While these possible rentier effects bear careful consideration, especially in economies strongly dependent on extractive sectors, Brazil offers some encouraging evidence regarding cash transfers and clientelism (Zucco 2010). President Lula drastically expanded cash transfer programs and experienced a large increase in popularity among the low-income populations which received these funds. Research suggests that voters supported for the project's successful economic effects rather than engaging "pocketbook voting", and therefore did not engage in traditionally clientelist behavior. As such, cash transfers represent a politically attractive program that also advances equity and poverty reduction agendas. It must be noted that these positive effects are wholly dependent on the program's credible and efficient administration.

These concerns about direct distribution and rentier politics increase the importance of going one step further and taxing the distributed revenues (Devarajan 2010), a feature not present in the Alaska case. If citizens are taxed, they would have an interest in not only the size of their transfer, but also how government uses their tax payments. This represents a more robust fiscal relationship between state and society, a concept explored further below.

Generate accountability through taxation

Broad taxation involves the transfer of resources from large segments of the population to the government. In many resource rich countries, the state does not engage in this kind of taxation. Research and historical experience suggest that broad-based taxation advances state-building through two kinds of effects: taxation strengthens the social contract between state and society in which the former provides the latter with public goods and opportunities for representation in exchange for the taxes paid; and the institution-building which is required as a state expands its revenue-generating bureaucracy (Brautigam 2008). The absence of taxation therefore contributes to explaining the poor performance of states in many resource rich contexts (Ross 2001; Palley 2003; Birdsall and Subramanian 2004; Moore 2004; Sandbu 2005; Devarajan, Le et al. 2010).

Taxation creates incentives on both sides of the state-society equation. Sandbu (2005: 3) details the psychological reasons for why "human beings are prone to care much more strongly about money that has passed through their hands." Taxpayers take a greater interest in fiscal policy and hold higher standards for what benefits accrue from public expenditures. As for states, good governance is more likely to emerge if there are costs associated with spending. Unlike oil and mineral rents, which states can treat as "free money", the government incurs a political cost when it collects taxes. This cost dynamic motivates government to value its revenues and spend in ways that better reflect the interests of its tax base (Timmons 2005).[7] Moreover, the state is compelled to generate consensus and cooperation around its taxation policies, which reduces the cost of tax collection relative to purely coercive taxation (Brautigam 2008). Should the state fall short in delivering adequate returns, citizens will demand reforms (Ross 2004). In the resulting "fiscal contract", both state and society hold obligations to the other.

Governments in rentier states need not tax their population because they already receive a disproportionate share of available resources. Large scale cash transfers would turn the tables. Proponents of direct distribution argue that resource rents first should be allocated to the public, and then taxed back by government. As mentioned, Sandbu argues for the allocation of *all* resource revenues, either into actual or virtual funds held by each individual, from which governments would then assess taxes; "natural resource revenue should not be accessible [to government] except by taxing the incomes of the population (Sandbu 2005)." Devarajan et al. (2010) propose that some resource revenues could enter the budget directly, but agree that the amount distributed to the public must constitute a large enough income stream so as to create the incentive for taxation.

There are two points at which to query the proposed "direct distribution → taxation → accountability" causal chain. First, will direct distribution cause governments to institute broad-based taxation? Natural resource revenues have been proven to reduce the collection of taxes from the domestic population (McGuirk 2010),[8] and states reliant on mineral and petroleum industries tend to develop narrow and weak bureaucracies not conducive to broad societal engagements like taxation. When natural resources constitute a country's leading sector, the authority and capacity to institute taxes fail to develop (Shafer 1994). In some cases, such as Saudi Arabia (Chaudhry 1997), the capacity to collect domestic taxes is even dismantled after the arrival of commodity wealth.

These findings indicate that resource rich countries are predisposed not to engage in broad-based taxation. This point should not be overstated—the concentration of authority and resources in the typical resource rich state does permit the leader to exercise high degrees of agency, and therefore can choose to implement difficult policies (Gillies 2010). However, for direct distribution to instigate broad-based taxation, it must overcome an established tendency against this kind of domestic revenue generation. Even if the state distributes revenues to the population, the leaders could choose to narrow their ambitions and survive off of the remaining revenues. Or they could seek financing elsewhere. Particularly if governments have alternate sources of financing (such as international lending), they will avoid the costly practice of broad-based taxation. Only if all or most resource revenues are distribution is taxation likely to ensue. As discussed above, the political feasibility of distributing such large amounts is much lower

[7] Timmons (2005) finds evidence for government's responsiveness to its tax base, with states providing benefits to those particular groups which carry the larger tax burden: the more a state taxes the rich, the more it protects property rights; the more it taxes the poor, the more it provides basic public services.

[8] In his examination of African economies, McGuirk finds a significant negative relationship between government petroleum revenues and revenues from other domestic sources, with a typical result being that a 1 percentage point increase in hydrocarbon revenue (in relation to GDP) lowers non-hydrocarbon revenues by about 0.2 percentage points.

than a partial direct distribution scheme—the relinquishment of control which it would require represents a towering political hurdle.

Second, if a government does choose to increase taxes, will this generate a more accountable fiscal contract? The idea that taxation will engender a productive social contract came from observations of the European nation state and its emergence. Contemporary rentier states are decidedly different entities, particularly in their reliance on external financing, zero-sum politics, weak institutions and absence of incentives for robust state-building. Moore (2004) agrees that, even in these contexts, there would be some "governance dividend from taxation", but questions whether the tax-accountability causation will be as transformative as its proponents might hope. Accountability benefits might ensue in countries like Ghana that have fledgling democratic institutions through which individuals can articulate their interests. But in more extreme rentier contexts, the assumed link requires more careful consideration.

Recent research suggests that tax systems reflect the economic, political and social contexts from which they emerge. These systems, including compliance by citizens, depend on the institutional environment and social factors like perception of the system's fairness, a sense of moral obligation, trust in the state, civic duty—all attributes which are "conditioned by state-society relations in the past" (Brautigam 2008: 7). In the introduction to an important book on taxation and state-building, Brautigam (2008) emphasizes that, given their unique attributes, developing countries perform very differently than other countries in studies about the determinants of tax structures and outcomes: "All of these [country specific] factors complicate the relationship between taxation and state-building and should cause us to pause before making the assumption that when it comes to the political economy of taxation, developing countries are simply poorer versions of today's advanced capitalist states (15)." Rentier developing countries are even more unique, therefore requiring even greater pause.

Given the contingent nature of taxation systems, and that tax policies are chosen by those individuals who hold power, a further question arises: will resource rich states introduce the kind of taxation system that generates accountability gains? Fjeldstad and Moore (2008) argue convincingly that a tax system will "encourage constructive engagement between governments and citizens" if it is 1) broad-based, and 2) levied in a consensual and transparent way in which the rights of the taxpayer are assured. Accountability gains will ensue if tax collection is predictable, based on consensual negotiations, and avoids "arbitrary assessments, forcible collections and the corrupt use of the tax collectors' power to extort money from citizens and companies." As stated before, institutions generally reflect the environment from which they emerge. In Chad, for instance, an extremely well-designed oil revenue management system ended up reflecting the political-economy environment: it failed to survive as it had no bearing or relevance to the country's power dynamics. One must be realistic, therefore, about the kind of tax system that can emerge in countries which feature high levels of corruption, patronage and abuse of public office. It might not be one that improves accountability.

Avoid principal-agent problems

Government is the agent meant to act on behalf of its principal, the public. In some countries, particularly those with resource wealth and weak institutions, the agent fails to serve the interests of the principal, particularly in its allocation of public funds. Instead, public office provides opportunities for individuals to pursue their own personal or political interests. From leaders to low-level functionaries, officials manipulate transactions and expenditures to the disservice of the public good. High degrees of discretion due to limited constraints on the executive exacerbate these practices.

Direct distribution circumvents this problem by "pre-empting kleptocracy (Palley 2003)"—the agent is skipped and resources are delivered directly to the principal. In environments with limited accountability and public institutions which have been captured by private interests, individual citizens will very likely engage in higher quality spending than government. For the transfer system to work, however, it would need to be adequately isolated from the dysfunctions of the public sector. This would require minimizing discretion in the design and administration of the program, avoiding intermediaries or gatekeepers, and instituting transparency and an external oversight mechanism.

Principal-agent problems do not arise only in rentier states with severe governance deficiencies. The Alaska Permanent Fund was created in 1976 because of the popular perception that the legislature squandered an earlier windfall. Warrack (2007) argues that Alberta's natural resource fund should also regularly allocate funds to citizens like in Alaska, and offers a libertarian expression of this same point: "Instead of politicians and bureaucrats deciding what is best, why not individuals and families?"

Again, certain caveats apply to this argument. First, as mentioned, policy mechanisms tend to reflect the environment from which they emerge. When I mentioned direct distribution as an allocation alternative in the Niger Delta, a state government official laughed and said, "you can't just run away from the corruption." This speaks to a certain paradox: direct distribution may offer the greatest expenditure efficiency gains in countries where governments fail in providing public goods; however its implementation will be the most difficult in these same contexts.[9]

In a corrupt political environment pervaded by rent-seeking, individuals will likely spend revenues more effectively than the state. However, the distribution process will face the same challenges as any other transaction involving large amounts of money: political manipulation, policy inconsistency, corruption, fraud, extortion, and basic mismanagement. The program's administration would require unprecedented safeguards. While this paper focuses on political rather than implementation issues, the effective administration of cash transfers will very likely face huge challenges in countries with highly corrupt and ineffective public institutions. And administration failures will only lead to the further waste of resources and disenchantment with the state.

Second, the principal-agent argument walks a thin line between pragmatism and fatalism. Should corruption and other governance problems be addressed, or accepted as (semi-) permanent? On one hand, cash transfers may be preferable in states where government has

[9]Even if public sector corruption is under control and political will exists, low-income countries with weak institutions will face challenges administering DD (Sandbu 2005). In Guatemala, Honduras and Nicaragua, for instance, CCT programs have struggled to acquire the kind of coordination, sustainable financing and the sound management that made similar programs a success in richer countries like Brazil and Mexico (Cecchini 2009).

repeatedly failed to serve the public interest. In Nigeria, several different institutions have been created to utilize oil revenues for the development of the Niger Delta region. Due to principal-agent problems, none have delivered results despite the billions of dollars they have received. Perhaps in such circumstances, abandoning the prospect of effective collective action in favor of direct distribution represents the pragmatic decision. On the other hand, bypassing public sector institutions risks further undermining the capacity and purpose of the state, or giving the impression that the state is somehow off the hook for its responsibility to deliver results.

Conclusion

In many resource rich countries, oil and mineral revenues fail to benefit the majority of the population. Such trends render alternate allocation policies including cash transfers worthy of careful consideration. This consideration should include an examination of political dynamics, both with regard to the feasibility of the policy's adoption and, more crucially, its likely impact.

Direct distribution could be politically feasible in certain scenarios. Given the concentration of leverage at the top of resource rich states, its adoption will likely occur at the behest of the leader. Leaders will most likely support cash transfers if they value the support of the majority. New resource rents, or a new political dispensation would make this more likely, as would a political context in which the will of the majority determines who retains office. Direct distribution could be used to solicit citizen buy-in in post-conflict settings, or to boost the reputation or legacy of the leader in power. In each case, the costs of allocating revenues to citizens will be lower if the leader faces limited political competition and if the resource rent is sustainably large.

As for implications, several analysts argue that direct distribution will generate improved governance in resource rich states. These benefits, however, are not automatic or even likely in every political context. The potential benefits discussed here—the creation of a constituency for responsible resource management, the leveling of the playing field between leaders and citizens, the strengthening of accountability via new taxation, and the avoidance of principal-agent problems—rely on causal assumptions which may not hold true in every resource rich country. Rather than assigning direct distribution with generic benefits, the likelihood of these governance gains as well as possible risks need to be evaluated in each individual country.

As to whether direct distribution is a good idea, the answer is, inevitably: It depends. Along with the economic effects of cash transfers, the potential governance risks and benefits should inform the decision to adopt direct distribution and the design of such programs. The discussion above suggests several preliminary recommendations which might assist in deciding where and how to initiate cash transfers. They include:

- Political motives will drive the introduction of direct distribution. However, the design of cash transfer programs should take care to advance long-term governance and development objectives, as well as short-term political ends. These could be contradictory: a leader may seek to use cash transfers to appease a restive faction in order to calm a post-conflict setting, even though such unequal treatment may exacerbate longer-term grievances; or, a leader seeking re-election may promise unsustainably large cash transfers that contradict optimal depletion rates and mediumterm economic objectives. Politically-aware policy design can produce cash transfer models that avoid these problems while still offering political gains.

- The popular resonance of cash transfers may distract attention away from the other facets of effective natural resource management. Successful revenue policies will guard against price volatility and inflation, advance well-conceived economic strategies that increase public goods, build human capital and diversify the economy, and reflect principles of transparency and accountability. Special situations, such as post-conflict scenarios, require an even more robust complex of policies. Cash transfers represent only one component of a viable revenue management strategy, and their allure should not be allowed to monopolize the debate over fiscal and economic affairs.

- Cash transfers will increase citizen interest in the management of natural resource wealth. This could devolve into a singular quest for larger transfers unless the public is provided with information about the breadth of resource revenue management issues (such as those mentioned above). Moreover, in order to serve as an effective constituency, citizens will need channels for articulating their demands to policymakers, such as a representative legislature, viable elections, a free media, an empowered civil society and widespread access to information.

- The political feasibility of introducing cash transfers and of introducing broad-based taxation will diverge in most countries. Initiating both could lead to a more accountable fiscal contract with significant positive governance effects. If this is the goal, steps to advance *both* policies should be taken simultaneously and, ideally, in a contingent fashion. If broad-based taxation is unlikely, the governance benefits of cash transfers will be modest, and the risks of exacerbating rentierism increase. The desirability of cash transfers, and in particular their size, should be considered with this in mind.

- If a country seeks to initiate both cash direct distribution and broad-based taxation, the capacity of the government to credibly execute tax collection must be assessed. Without a major shift in the political order, a fair, consensual and efficient tax system is unlikely to emerge in a country where all other public institutions lack these traits. Therefore taxation will generate governance gains in contexts already characterized by at least moderate levels of accountability and public sector functionality.

- The design of cash transfer programs should deliberately try to minimize the risk of spreading rent-seeking tendencies throughout the population. The size of the transfer should be contained (unless taxation is introduced), and innovative strategies identified for shifting attention away from state handouts to productive, non-extractive sectors of the economy.

- In countries with weak institutions and high levels of corruption, cash transfers will suffer from principal-agent problems if its administrators are allowed to engage in fraud and misappropriation. Extensive transparency, oversight and process safeguards are required, as is the realization that even these protections may not work in the most pervasively corrupt contexts.

These ideas require empirical investigation, drawing from the existing experiences with cash transfers, and are presented here only to stimulate further discussion. Above all, they seek to illustrate the importance of fully integrating country-specific governance and political concerns into the debate on the introduction and design of direct distribution as a strategy for allocating natural resource revenues.

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