Chapter 1.

Contextualising public governance in Costa Rica

This chapter provides an overview of Costa Rica's recent politico-administrative, socio-economic and demographic changes and describes how these are putting pressure on the country's governance mechanisms. Costa Rica's political and economic model has been characterised for decades by high political stability and stable economic growth, allowing the country to perform well on social development deliverables like education and health. However, inequalities are on the rise, important economic pillars like the high-tech industry and tourism have come under pressure, a fragmented public sector is struggling to deliver policies and services effectively, and citizens are increasingly losing trust in public institutions and the political system. This chapter therefore underlines the need to strengthen the country's governance capacity in different areas.

The rise of a stable and well-performing country

The Republic of Costa Rica is one of the most stable democracies of the Americas. Free and fair elections, peaceful alternations of power and the guaranty of extensive human and democratic rights have characterised the country's political system for a long time. The establishment of a solid institutional framework has guaranteed social and political stability. Costa Rica as it stands today is built on the Political Constitution of the Republic of 1949. Abolishing the army, the Constitution fostered the creation of a solid basic social welfare system, a robust system of checks and balances, and a strong rule of law.

Strong mechanisms to oversee state action as well as to protect and guarantee human and democratic rights were progressively installed. The constitutional reform of 1989 was instrumental in this respect, by introducing the Constitutional Chamber (*Sala Constitucional*) that has become a protector of peoples' rights. The creation of the position of the Ombudsman in 1992 strengthened the ability of citizens to voice their complaints regarding administrative acts. The Comptroller General Organic Act of 1994 enhanced external control functions over the budget, investment and financial management of the state. In 2012, Costa Rica became a member of the Open Government Partnership, making a strong commitment to openness, transparency and accountability of the state.

Political stability has been supported by overall positive economic growth, despite occasional dips, and by relative monetary stability. According to the World Bank (2014a), Costa Rica's economic growth was 5% on average throughout the 1990s. While slowing down in the 2000s, it remained significantly higher than in other Latin American countries. The average tariff rate declined from over 60% in 1985 to 11.7% in 1995 and 5.9% in 2004 (Ministry of Foreign Trade, 2013), and from the 1990s on free-trade zones were established. Since the 1990s, the relatively open economy has been able to attract large sums of foreign direct investment (FDI), principally in knowledge-intense sectors, creating more and better paid jobs for the growing number of well-educated Costa Ricans. The number of jobs created by FDI rose from 7 758 in the period between 2003 and 2005 to 34 385 between 2009 and 2011 (OECD, 2012). The good endowment of human capital and natural amenities have helped the country diversify its economy.

The Costa Rican political and economic model has historically delivered strong social development with commendable achievements in the areas of education, environmental protection and health. The implementation of social reforms in the period of the late 1940s and the 1950s provided broad-based access to education for Costa Ricans. Illiteracy rates are low (UNICEF, 2013) and investment in education is the highest in Central America (Programa Estado de la Nación, 2014). In the 2009 results of the OECD Programme for International Student Assessment (PISA) that benchmarks skills and knowledge outcomes among 15-year-old students across countries, Costa Rica scored well with respect to the OECD average (OECD, 2011). Costa Rica also offers universal healthcare. Largely due to the considerable spending by the state on different social programmes, the average life expectancy at birth of Costa Ricans is significantly higher than in other Latin American countries, increasing from 66.8 in 1970 to 75.7 in 1990 and 79.7 in 2012 (UNICEF, 2013). Between 1980 and 2012, the country made important progress on the Human Development Index, and is now classified as being in the "high human development" category (UNDP, 2013).

Thanks to the combination of economic growth and public investment in social services, most Costa Rican households have managed to improve their living conditions in the past 20 years (Programa Estado de la Nación, 2014). New economic opportunities created by economic growth as well as the existing social security networks have contributed to social mobility. While the middle class represented 18% of the population in 1992, this percentage had already risen to 31% in 2002 and 40% in 2009 (UNDP, 2014).

A changing socio-economic reality

Despite the growing middle class, inequalities in Costa Rica are on the rise. While in most Latin American countries inequality in labour earnings fell substantially between 2000 and 2010, Costa Rica saw an opposite trend, which is also reflected in its Gini coefficient, the global measure for income inequality. Between 2001 and 2011, Costa Rica was one of the only Latin American countries of which the Gini coefficient rose (Programa Estado de la Nación, 2013). According to the Programa Estado de la Nación (2014), this development is mostly due to an existing disparity between "new" (i.e. based on manufacturing and the service sector) and "old" (i.e. based on agriculture) economies.

The economic model built on high-tech industry and tourism has come under pressure from regional competitors and growing labour costs. In sectors such as tourism, other countries from Latin America and the Caribbean are gaining importance. Business activities are hindered by poor transport infrastructure, difficulty in accessing finance and from an only moderate capacity to innovate (World Economic Forum, 2013). This is reflected in the 2015 Doing Business statistics of the World Bank (2014b), in which Costa Rica only ranks 83rd (out of 189).

Increasing financial constraints on government expenditures are putting pressure on the Costa Rican welfare state and jeopardise investments in social services. High levels of growth since the 1950s have guaranteed stable public finances which allowed the state to spend a significant amount of money on services to the population. However, Costa Rica's tax revenue as a proportion of its gross domestic product (GDP) has not grown in a manner consistent with the type of public service that the population expects. When compared with the OECD average (34.1% in 2013), total tax revenue (general government) is fairly low (22.40% in 2013) (OECD, 2015). Furthermore, Costa Rica has one of the largest budget deficits in Central America (OECD/IDB, 2014). The central government's deficit reached 5.4% of GDP in 2013, the highest in the past ten years, while the government had the lowest level of fiscal flexibility, with 95% of government expenses that were pre-assigned (Programa Estado de la Nación, 2014).

Pressure on the political system and the public sector

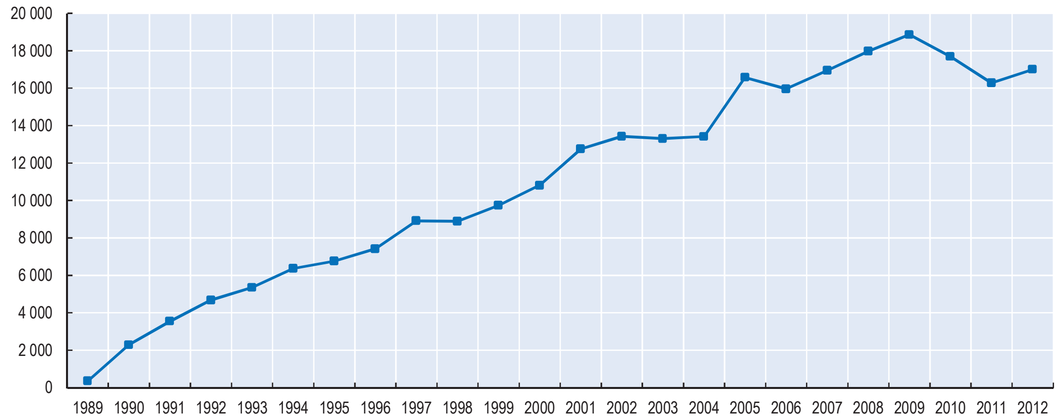
In addition to the changing socio-economic reality, the political system has come under stress from different sides recently, and the public sector is struggling to deliver policies effectively that meet the expectations of the Costa Rican people. The incoming government is facing a new set of challenges. While the country saw a significant extension of rights and liberties, the "democratisation of the Costa Rican democracy" (Programa Estado de la Nación, 2014) was neither accompanied by a growing public budget and institutional efficiency, nor by stronger accountability mechanisms. The political system is deeply fragmented, conflicts between the different powers of the state are on the rise and the number of social conflicts is growing (ibid.).

As is the case in a great number of OECD Members, people are increasingly losing trust in public institutions and the political system. Levels of trust in government have dropped from 53% to 40% between 2010 and 2014 (Gallup World Poll, n.d.), more than three times the average decline across OECD Members for the same period (45% to 40%). According to the *Latinobarómetro*, support for the political system fell from 67.6% in 2004 to 55.9% in 2012 (Alfaro-Redondo and Seligson, 2012). Between 2008 and 2012, the levels of confidence of the Presidency of the Republic fell from 60% to 43% (ibid.). While the Catholic church ranks as the most trusted institution (64.7%), the political parties and the Legislative Assembly are the institutions with the lowest levels of confidence from the public (31.5% and 37.9% respectively; ibid.). Even though Costa Rica ranks better than other Latin American countries in the Transparency International Corruption Perception Index (CPI), the perception of corruption in Costa Rica has also worsened in the last few years (Transparency International, 2014): from 2010 to 2013, Costa Rica dropped eight positions in the CPI. A key lever for government to build back peoples' trust is strong overall government performance (OECD, 2013). As such, the 2015-18 National Development Plan shows a strong commitment to fight corruption and strengthen transparency, efficiency and overall public performance.

Partly due to relatively weak constitutional powers of the executive, but also due to the shift from a bi-partisan to a more fragmented multi-party system that has taken place over the past decade, the executive experiences a weakened position to put forward its legislative agenda. Members, or groups of members, of congress have a *de facto* veto on legislative initiatives (Government of Costa Rica, 2014). This results in a unicameral Legislative Assembly that has difficulties in taking decisions according to the majorities as foreseen by the Constitution (Presidential Commission on Democratic Governance, 2013), with members of Congress that have significant veto powers but that lack the power to promote their own constructive agenda.

The creation of the Constitutional Chamber (1989) and the enormous increase in the number of constitutional decisions has resulted in a shift in the distribution of power. The Constitutional Chamber (*Sala Constitucional*) has become one of the most powerful public entities increasingly addressing highly political issues and intruding in policy matters formerly resolved by the political branches (Wise, 2010). The Constitutional Chamber can intervene at different stages of the policy-making process. If any act or decision of the administration or of private persons has constitutional relevance in the wider sense, the judges of the Constitutional Chamber can be addressed. Decisions in constitutional matters taken by the Constitutional Chamber are exclusive, not reviewable and are binding precedents, except for the Constitutional Chamber itself (Barker, 2000). Since the Costa Rican Constitution covers a great variety of areas and is broad in its categories, the Constitutional Chamber can be considered a necessary actor in any major public policy decision, especially those involving legal reform (Government of Costa Rica, 2014). In the first two years after the creation of the Constitutional Chamber, the number of cases it had to address increased considerably (Figure 1.1). Nowadays, the Chamber handles over 17 000 cases each year (Constitutional Chamber, 2014).

Figure 1.1. **Number of cases in the Constitutional Chamber**



Source: Constitutional Chamber (2014), "Number of cases in the Constitutional Chamber 1989-2012", http://sitios.poder-judicial.go.cr/salaconstitucional/estadisticas.htm.

Substantial fragmentation of the public sector puts pressure on the strategic policy-making capacity of the state and its service delivery capacity. While a certain degree of fragmentation is not uncommon in OECD Members (OECD, 2002), this fragmentation poses particular challenges in terms of policy co-ordination. Costa Rica's Constitution not only distinguishes between central government and local government (i.e. "territorially decentralised public sector"), but also establishes the existence of autonomous institutions (Article 188 of the Constitution). As defined in the Costa Rica Public Sector Organigram (Ministry of National Planning and Economic Policy, 2013), the "institutionally decentralised sector" (as opposed to ministries and their subsidiary bodies) encompasses these autonomous institutions, and distinguishes between autonomous institutions and their subsidiary bodies, semi-autonomous institutions, state-owned and non-state-owned public enterprises and non-state public entities that collaborate in the satisfaction of the public interest.

The first entities of the institutionally decentralised sector were created in the 1940s as autonomous institutions with a mandate of policy making as well as service delivery such as health, energy and education. Examples include the Costa Rican Department of Social Security (*Caja Costarricense de Seguro Social* created in 1943), the Costa Rican Electricity Institute (*Instituto Costarricense de Electricidad* created in 1949) and a series of tertiary education colleges created in the 1940s. The creation of many of these was deeply connected to state interventionism in the economy and the import-substitution model. In terms of steering mechanism, these public institutions often dispose of boards of directors that provide both policy and managerial guidance.

From the 1970s onwards, a new wave of creating public institutions is observable, quantitatively and qualitatively different from the past. For instance, between 1991 and 2010 no less than 60 subsidiary bodies of central government ministries were established. These subsidiary bodies primarily represent "policy implementation shortcuts" to attain greater administrative and budgetary flexibility (Government of Costa Rica, 2014).

The budget of the (territorially and institutionally) decentralised sector – approximately 50% of the general government consolidated spending – falls outside the budget process headed by the Ministry of Finance, and is rather supervised (i.e. compliance check) by the Comptroller General (*Contraloría General de la*

República). The Comptroller General operates as an auxiliary institution of the Legislative Assembly, though with full operational and administrative independence in the performance of its duties (Article 183 of the Constitution).

Table 1.1. **Creation of public institutions by decade and by judicial status, Costa Rica**

Period	Ministries	Autonomous	Semi-autonomous	Subsidiary bodies	Municipalities	State-owned public enterprises	Non-state-owned public enterprises	Total
Before 1900	3	2	0	2	32	0	0	39
1901-10	0	0	0	0	11	0	0	11
1911-20	0	1	0	0	13	0	0	14
1921-30	1	3	0	0	3	0	0	7
1931-40	0	1	0	1	3	0	0	5
1941-50	0	11	0	1	3	1	6	22
1951-60	1	5	0	1	0	1	3	11
1961-70	3	5	1	7	11	0	12	39
1971-80	4	6	4	16	5	4	9	48
1981-90	5	2	0	10	0	0	6	23
1991-2000	1	3	3	39	0	10	13	69
2001-10	0	1	0	27	0	4	3	35
Total	18	40	8	104	81	20	52	323

Source: Ministry of National Planning and Economic Policy (2015), *Organización del Sector Público en Costa Rica,* Área de Modernización del Estado de MIDEPLAN, Ministry of National Planning and Economic Policy, San José.

The way forward

Costa Rica has a high level of human development and its governance system has had strong service delivery for more than 50 years. But the socio-economic challenges and the changes in the political system and the administration are putting pressure on the country's governance mechanisms and constrain its aspirations for enhanced and sustainable prosperity for its entire population.

Fiscal and economic pressures are affecting the quality of public services. An increasingly unequal society, remaining levels of poverty and regional disparities affect the citizens' well-being. The government has to deal with economic pressures and make the country more competitive. However, the margin of its fiscal revenue that it can allocate to advance its own policy priorities is small. At the same time, political realities are changing rapidly and contributing to a loss of steering capacity of central government institutions. The Legislative Assembly is often blocked. The Constitutional Chamber has changed the way people interact with the state and a fragmented public sector contributes to an atomisation and dispersion of governance.

But there is an awareness of the challenges ahead and the administration shows a strong commitment to make change happen. The 2015-18 National Development Plan is a testimony of the government's will to move forward towards a more effective, efficient, participatory, open and transparent government that fosters inclusive growth.

Costa Rica is at a turning point: in order to sustain the important historical achievements the country's governance system needs to shift gear and mirror the changing economy and society. Governance reform is needed. As will be discussed in subsequent chapters, this includes, amongst others, moving from processes to results (and ownership thereof), with mutual reinforcement of results-oriented focus both top-down and bottom-up (shifting from compliance tools to management tools) and identifying opportunities to strengthen a shared identity and organisational culture across the public sector.

This OECD Public Governance Review is an opportunity to make a thorough analysis of the current situation of different governance areas and provide input for a reform process that will lead to a more efficient, effective and accountable public administration that focuses on results, delivers better policies and improves the well-being of the population.

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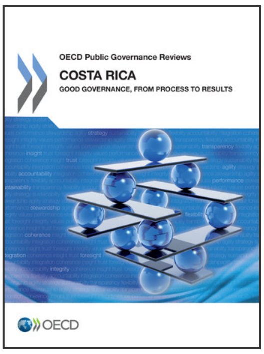

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