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Institutional Drivers and Governance Mechanisms of Debt Accumulation in Local Authorities: A Critical Review of the Literature with Reference to Zambia

Mutale Mulenga Kelvin[1], Dr. Norman Kachamba[1], Dr. Nsama Musawa[1], Daniel Chisanga[1]*

[1] *Copperbelt University, Zambia*
* Corresponding Author

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Abstract

Arguments for the devolution of financial control to local authorities as a means to achieve a more efficient, accountable and responsive local service provision are widespread, yet many local authorities in the developing world have continued to accrue unsustainable debt under reforms aimed at strengthening their finances. In this article, we synthesize and critically assess the theoretical and empirical literature on the institutional drivers and governance mechanisms of local-authority debt accumulation, as illustrated by Zambia. We identify that, despite being diverse, these literature streams converge on a single point: that it is institution-and governance-based factors, not just resource endowment, which influence varied debt accumulation pathways. However, the literature remains fragmented across disciplines, levels of analysis and country contexts. We discuss three theoretically informed approaches: institutional theory which elucidates the persistence and routinization of debt producing practices; agency theory, which explores the accountability failures that transform a situation of structural vulnerability into measurable debt; and fiscal federalism, which provides the context of intergovernmental relations within which the municipalities operate. The empirical material is structured by the following themes: perceptions of debt among officials, impact of institutional quality on subnational debt, moderating effect of governance mechanisms, and comparative institutional analysis. We find that a substantive gap remains; there is no council-level, mechanism-specific, mixed-method comparative evidence available from Zambia. In conclusion we suggest an integrative conceptual framework wherein institutional drivers are conceived as antecedents to debt, with governance mechanisms operating as moderators of it and councils as context-specific entities shaped by scale.

1. Introduction and Background

One of the most persistent challenges of fiscal management within decentralized countries is subnational debt. A situation where expenditure responsibility is allocated to local authorities much faster than revenue-raising capacity or administrative competencies leads to an imbalance between vertical powers which may results in the build-up of liabilities, unpaid arrears and statutory non-compliance (Bahl and Bird 2008, Rodden 2006). These situations are not isolated to one specific region; comparable dynamics of municipal and regional indebtedness have been observed in the US (Gunter and Siodla 2022), China (Chen and Wang 2019, Liu, Zhang and Cao 2022) and Russia (Timushev 2022) as well as throughout Sub-Saharan Africa. What distinguishes these differing contexts is the consistent finding that it is not the resource endowment alone which influences whether local government remains financially solvent or experiences chronic debt stress, but rather the structure of intergovernmental relationships and the quality of local governance.

Zambia provides a prime example of the mismatch between the ideals of decentralisation and the performance outcomes at the local government level. Despite the existence of the Decentralisation Policy and the Local Government Act No. 2 of 2019 that impose prudent financial management responsibilities on councils, liabilities in the sector amounted to approximately K4.6 billion across all 116 councils by 2023 (a roughly 68% increase from 2020) with average debt-to-revenue ratio of approximately 194% (OAG 2022, UNICEF Zambia and ZIPAR 2025). These figures do not reconcile with the fiscal autonomy and accountability that decentralisation was expected to foster and they lead us to the question: in what way do councils, ranging from a large metropolitan authority like Lusaka City Council to smaller town councils such as Kapiri Mposhi Town Council despite their disparate revenue bases and administrative profiles, exhibit similar patterns of indebtedness?

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In this article we attempt to answer this question by critically reviewing and synthesising the relevant literature on institutional drivers and governance mechanisms of local-authority debt accumulation. Rather than merely describing the existing studies, we explore how these strands are shaped by the underlying explanatory logic of how debt arises and accumulates, discuss the agreements and differences in these literature sources, and asses how effectively findings obtained in high-capacity settings can be transferred to the low-capacity contexts that characterise much of Sub-Saharan Africa. The discussion will unfold in five movements: conceptual background to local government finance and the debt problematique; the dominant theoretical approaches; the themes emerging from empirical studies; a synthesis of the arguments made, inconsistencies and gaps; and an integrated conceptual framework built from the literature.

2 Literature Review

2.1 Decentralisation, Local Government Finance and the Debt Problematique

Local-authority debt falls within the domain of public sector accounting and public financial management (PFM) literature, defined as how governments plan, allocate, spend and account for public funds while considering sustainability, accountability and transparency (Allen, Hemming and Potter 2013). Applied to local governments, PFM literature explores how councils raise revenue, expenditure and liabilities and the mechanisms through which accountability is fostered with both citizens and higher government levels. Debt accumulation, therefore, cannot be viewed as an accounting consequence but rather as evidence of the design and functioning of these particular institutional mechanisms.

The positive arguments for decentralisation are based on the presumption that positioning fiscal decision making closer to the citizenry enhances allocative efficiency and responsiveness (Oates 1972, Musgrave 1959). However, Bahl and Bird (2008) temper this optimism by underlining the fact that gains from decentralisation are dependent on coherent assignment of revenue powers, well defined responsibilities for expenditures, predictable intergovernmental transfers and credible mechanisms for enforcement of fiscal discipline. In the absence of such conditions - for example, when councils are vested with authority but lack the corresponding funding, or when they depend on unpredictable late transfers - decentralisation may in fact exacerbate fiscal problems rather than remedy them. This is the case in Zambia, where councils have nominal revenue-raising authority but remain overly dependent on transfers from the Local Government Equalisation Fund (LGEF) which are unpredictable and insufficient relative to mandated responsibilities (MLGRD 2022, Mwanza 2024).

The problem of local government indebtedness has been empirically established beyond doubt. OAG (2022) report identifies statutory liabilities amounting to K3.52 billion across 109 councils, of which Lusaka City Council held the highest proportion; substantial amounts are also held by smaller municipalities. The majority of these liabilities comprise unremitted contributions to the National Pension Scheme Authority and Local Authorities Superannuation Fund, alongside arrears to the Zambia Revenue Authority (UNICEF Zambia and ZIPAR 2025). In spite of the documentation on debt magnitudes and distribution through audit and policy papers, the literature often stops short at detailing the actual institution-and governance-based processes by which debt is produced, routinized and upheld; this explanatory vacuum has led us to review the theoretical and empirical literature on this problem.

2.2 Theoretical Framework of Local- Authority Debt

There is a vast academic tradition concerning the theoretical understanding of local government finance which includes institutional theory, agency theory, fiscal federalism and public choice and decentralisation theory. However, this article focus on three of the most relevant to sustained debt: institutional theory (as the main framework) supported by agency theory and fiscal federalism. Each theory addresses a separate part of the explanatory chain; each has its own weaknesses, to be addressed by the other two.

Institutional Theory

According to institutional theory (Scott, 1995; North, 1990; DiMaggio & Powell, 1983), organizations (including public organizations) are shaped not just by efficiency considerations but by three types of institutions: regulative rules, normative expectations and taken-for-granted cognitive assumptions. Where these institutions are unstable, conflicting or weak, practices often become normalized even if they are ineffective. For local government finance, institutional theory provides an argument for the persistence of council debt in Zambia despite successive rounds of PFM reform. While formal institutions, like the Local Government Act No. 2 of 2019 and output-based budgeting, offer some structure, lasting behavioral change is only enabled by supporting financial-management cultures, internalised accountability and a shared recognition of the costs of debt accumulation. Without adequate accountability and where a culture of political appointment, poor record-keeping and weak supervision predominates, formal rules may be only symbolically upheld, generating a disconnect between policy and behavior as predicted by institutional theory.

A limitation of the institutional perspective is that it provides the strongest explanation of inertia. However, it is unable to account for why two organizations under identical formal institutions will respond differently to the same pressures. If Lusaka City Council and Kapiri Mposhi Town Council operate under the same legislation yet pursue different debt paths, a sole institutional approach to analysis cannot provide a complete picture and must be supplemented with other perspectives, specifically agency theory and fiscal federalism.

Agency Theory

Originating in the work of Jensen and Meckling (1976) and adapted to the public sector by Eisenhardt (1989) and Broadbent et al (1996), agency theory helps to explain accountability issues that arise when principals delegate tasks to agents who may not perfectly share principals' goals under conditions of differing interests, asymmetric information, and imperfect monitoring. Local governments have multiple layers of principal-agent relationships (citizens-councillors, council management-departments, councils-central monitoring agencies). Agency theory helps to understand several aspects of local government debt. Firstly, it helps to explain how accrued statutory arrears could accumulate over time when deductions have already been collected - weak oversight allows delayed payments without immediate identification. Secondly, it predicts circumstances in which accountability will be weak; that is, when there is limited transparency in reporting, when audit recommendations are ignored and when citizens lack access to financial information. Finally, it hypothesizes that various governance tools, such as internal audit, committee oversight and external reporting can help to reduce agency costs and decrease the rate of debt accumulation. The main critique of the approach is that it does not account for factors like organisational culture and political affiliation as explanations for behavior but relies too heavily on narrowly defined self-interest.

Fiscal Federalism Theory

Fiscal federalism (Musgrave, 1959; Oates, 1972; Bahl & Bird, 2008) argues that decentralization will facilitate fiscal discipline under specific structural conditions of autonomy in raising revenue, appropriate assignment of expenditure responsibility, secure transfer systems and budget-constrained local governments with a hard budget constraint. Within Zambia, fiscal federalism suggests that the structural roots of debt accumulation can be identified in the inconsistency of local government functions with resource availability. Although local governments have been devolved spending responsibilities, the inadequate and unreliable nature of transfers to local governments through the Local Government Equalisation Fund create the problem. The idea of the soft budget constraint, where local authorities are conditioned to believe they will receive central government bailout and will therefore borrow with abandon (Rodden, 2006; Sorribas-Navarro, 2011) is central to comparative analyses of local debt. Fiscal federalism can provide the broader structural framework; nevertheless, the theory is very system-centered, and like institutional theory, it is difficult to use it on its own to explain divergent debt paths between councils in a given system.

Toward an Integrated Model of Analysis

While the above theories complement rather than compete with each other, they can be viewed as sequential. Fiscal federalism explains the structural system under which council debt accumulation is possible. Institutional theory helps us to understand how dysfunctional practices become normalized within councils operating under specific conditions. Agency theory helps to fill the accountability gaps across different principals and agents, which result in realized local debt and arrears. Together, structural constraints in fiscal federalism create the condition under which debt is possible, institutional theory explains how this potential translates into an ongoing phenomenon at the organisational level and agency theory addresses the failure of accountability across relationships that results in an actual outcome: the council being in debt. The ensuing framework becomes the basis of the conceptual model developed in Section 4.

2.3 Empirical evidence on the determinants of local government debt

This article reviews the empirical literature thematically according to the logic derived above. Four main themes will structure the analysis of the evidence: perception of local authority officials regarding causes of debt; the role of institutional quality in explaining sub-national debt levels; the impact of governance mechanisms on local authority debt; and cross-national comparative analysis of institutional settings. Finally, it will briefly review literature on the topic specific to Zambia and the region. The aim of the review will be not to present a comprehensive cataloguing of individual studies, but rather to note points of consensus and conflict in the literature and discuss the relevance and transferability to Zambian local government context.

How Officials Explain Debt: Perceptions and Institutional Norms

From studies across Africa, council officials are identified as placing blame on structural factors as opposed to mere inefficiency as cause of indebtedness. Smoke (2015) identifies decentralisation failures, under-funded mandates and unreliable transfers as recurrent explanation of the part of officials and this frame have behaviour implications because indebtedness that is seen to originate outside and unavoidable gives no motivation for reforms in the internal process. The lack of strong accountability mechanism pushes the debt burden to be experienced as normal rather than aberration; this corresponds closely with institutional theory's conception of normalization as observed by Fjeldstad and Heggstad (2018). Using a political economy perspective, Resnick (2017) finds that patronage and electoral pressure within larger urban council push expenditures towards visible projects and away from debt management. In aggregate, these studies concur, but they are heterogeneous on their methodological approach and span; Smoke and Fjeldstad and Heggstad use comparative country study approaches yielding low country-specific council data whereas Resnick focuses on urban cities, therefore leaving the question of whether the result would hold in smaller councils unknown. This studies do not link officials' view to actual councils' finances; this gap is precisely what the Zambia comparative design attempts to fill.

Quality of Institution and sub-national Debt

There exists a vast quantitative literature establishing the link between institutional quality and local debt levels. Institutional quality is defined as clarity of functions, strength of the fiscal rules, and quality of administrative systems. Both Baskaran (2012) and Asatryan et al. (2015) find thatweak and unaccountable budget institutions increase borrowing at the sub-national level across country and within the sub-national level; Baskaran attributes lack of effective financial rules to high level of local borrowing while Asatryan, Feld and Geys, demonstrate thatlack of fiscal rules and oversight, as well as budget discipline and effective administrative systems, leads to increase in borrowing by sub-national governments. Sorribas-Navarro (2011) also demonstrates that Weak administrative capacity, regardless of the revenue side of council budgets, leads to debt accumulation, in consistency with soft-budget-constraint studies.Comparable result can be seen in other settings too where Timushev (2022) argues the cause of regional debt accumulation in Russia is the weakness of the institutions while Martell and George (2006) stress institutional development for shaping sub-national borrowing in bond markets. A significant problem in the previous literature, relative to the problem at hand, is that all of them treat institutional quality as exogenous national or cross-county factor. This is problematic because the degree of institutional development varies even within the same nation state with comparable institutional framework like the singular Local Government Act in Zambia, hence we expect the council level debt outcome to vary significantly and be correlated to council-level institutions instead.

Governance mechanisms as a moderator

A second, important strand, analyzes how governance mechanisms moderate the effects of institutional weakness on debt outcomes. Alt and Lassen (2006) examine how fiscal transparency mitigates debt accumulation and find that similar constraints result in lower debt levels under greater transparency. The role of stronger legislative bodies in reducing debt levels is illustrated by Wehner (2010) who indicates that legislative oversight weakens excessive spending while de Mello and Pisu (2010) show that fiscal rules strengthen the negative link between expenditure pressure and debt growth. All of the foregoing studies suggest that stronger governance mechanisms have the ability to temper structurally influenced vulnerabilities, therefore indicating that good governance does not merely complement institutional constraints but rather moderates their effects. However, these analyses primarily focus on rich countries, where auditing and oversight mechanisms andreporting standards are relatively well resourced and independent. In low-capacity situations where internal audit departments are under-staffed, committee meetings are often irregular and reporting practices are poor, it cannot be assumed that the same effects would manifest identically. It is therefore unclear whether or not good governance has similar effect in African local governments as it has shown in high capacity context.

Comparative institutional Analysis

This line of argument provides a strong basis on which to build the hypothesis that institutional, as opposed to economic size or resource constraints, explains variations in council debt. Rodden (2006) presents a convincing framework for determining local government fiscal discipline/indiscipline, the design of the intergovernmental fiscal relations particularly the hardness of the budget constraints and the level of grant dependence, as a fundamental driver of variations in local debt. Martnez-Vzquez, Lago-Peas, and Sacchi (2017) further reaffirm through a meta-analysis of a wide range of decentralized countries that institutional quality explains better debt management performances. In the African context, Fjeldstad et al. (2019) contribute the most contextually relevant evidence through comparative case studies that show similar local government debt levels despite resource variations depending on the internal governing structure. This finding is particularly important, it implies that differences in debt outcomes between a large and a small local government could arise either from same failures of institution, regardless of size, or from different council-governed institutions. One caveat of these studies though; Rodden (2006) and Martnez-Vzquez et al. (2017) do not provide empirical data on the perceptional and the political mechanisms driving debt levels, as such; Fjeldstad et al. (2019), despite using case studies approach, does not examine if governance mechanism has moderating effects.

Zambian and African Literature

The existing studies of debt at the sub-national level in Zambia are either primarily descriptive or narrowly focused. Mwanza (2024) attributes the current state of council fiscal stress to administrative inefficiency and delayed LGEF flows, but does not adequately demonstrate whether these failures are specific to councils with particular characteristics like scale, or what the link is to the council level debt level. Nyirongo (2024) examines fund management at the level of select local governments, whereas previous studies like Chitala (2012) focus on the national level debt management and Saungweme and Odhiambo (2018) analyze national level public debt servicing patterns and reform initiatives in Zambia. Although data from OAG (2022) and UNICEF Zambia and ZIPAR (2025) provide substantial fiscal evidence at the council level, these sources fall short of establishing any link between governance and institutional mechanisms and council debt levels. At a higher regional level, Abotsi (2023) establishes link between the quality of institution and accumulation of public debt at state level and in many ways echoes the relationship found in the council literature. So, literature confirms the breadth of the problem at state level, but limited context-specific or mechanism-based analyses remain absent.

3 Synthesis: Consensus, Contradiction and Gaps

Three common threads can be discerned from the literature. First, while resources themselves are important, it is the institutional and governance characteristics of a council that truly determines how a council's debt levels behave. In weak-institutional contexts, poor debt accumulation rates can persist regardless of how abundant council resources might be (Baskaran, 2011; Sorribas-Navarro, 2011; Rodden, 2006). Second, governance factors can influence the extent to which these weak institutions will affect debt accumulation. Strong governance, such as enhanced budget control, transparency, and scrutiny can limit how weak institutions lead to poor debt management (Alt and Lassen, 2006; Wehner, 2010; de Mello and Pisu, 2010). Third, officials' own understandings of debt and the need for reform seem to shape whether poor debt practices are seen as endemic and accepted, or as a problem to be addressed (Smoke, 2015; Fjeldstad and Heggstad, 2018).

Two persistent tensions challenge these agreements. The first tension is regarding the transferability of the above evidence. Most evidence for governance having a mitigating role in this relationship comes from high capacity OECD countries, with auditing, oversight and reporting systems that do not resemble the similar mechanisms that operate in an African local government. Second, there is a tension concerning the level and methods used to study this phenomenon. The quantitative comparative literature considers institutions as a national level variable, and thus cannot provide any evidence on why variation within countries occurs between specific councils, while qualitative studies are adept at uncovering the perceptions and normative frameworks of stakeholders but tend to fall short in connecting these frameworks to objective financial results.

The above tension logically yields the identified research gap: "there is not at present council-level, mechanism-specific, mixed-methods comparative evidence on how institutional conditions and governance arrangements jointly shape debt accumulation in Zambian local authorities". The subsidiary gaps that constitute this larger gap are: the way specific drivers of institutional behavior- fiscal autonomy, administrative capacity, revenue capacity and regulatory constraints- play out at the local authority level in Zambia have not been looked at, governance mechanisms' moderating role has not been testable within the framework of African local authorities and how these perceive the role of such mechanisms has never been combined with objective data from the field in one study. The research gap needs to address this issue beyond a basic audit approach.

4 Proposed Model Based on Literature Review

An integrated framework is presented whereby the main drivers of debt accumulation are the institutional drivers and the role of the governance mechanisms moderating them, council scale and revenue composition are moderating variables, and how this relationship will play out is conditioned by cases (Scott, 1995; Oates, 1972). Institutional drivers such as: fiscal autonomy, revenue capacity, policy and regulatory constraints, and administrative capacity will create the structural weakness for debt. Governance mechanisms will moderate this relationship in the way proposed by Alt and Lassen (2006) and Wehner (2010): with the stronger the controls, the less the role of weak institutional factors will contribute to debt levels. Governance mechanisms are as follows: internal audit quality, external controls (budgetary control, political will, transparency), and accountability mechanisms. The dependent variable, debt accumulation will be proxied by such objective indicators as: ratio of debt-to revenue, accumulation of statutory arrears, payment arrears for suppliers and payment arrears for debt service. The perceptual data generated from qualitative data should only serve as a context for the objective results.

The proposed model replicates the causality identified in 2.4.4 whereby structural fiscal constraints create weakness and inertia within institutions which in turn convert this vulnerability into actual debt via mechanisms of accountability. By clearly delineating institutional drivers, governance mechanisms, and the resultant debt accumulation as analytical categories and by distinguishing perception data from structural factors, the research model accommodates research at the council level and can be adaptable to other African contexts.

5 Conclusion

The literature review has highlighted how institutions and governance matter more than the presence or absence of resources, in determining council-level debt accumulation. The logic comes from institutional theory and explains why such practices are maintained and normalized, agency theory which focuses on the need to fix accountability failures that result in conversion of weakness into actual arrears and the fiscal federalism theory which explains the initial creation of weakness within a council framework. While the evidence has been compelling, two limitations emerge from this body of work when we focus on a context like Zambia. First, evidence regarding governance's moderating effect only arises from contexts with strong institutions;

second, the absence of mixed-methods comparative studies that investigate why different councils reach similar debt levels despite differences in their economic situation. Three consequences arise from the above findings. Firstly, there is a need to test if the governing mechanisms we find in OECD countries can truly affect debt levels within institutional constraints that differ from those present in the developed world. Secondly, interventions in managing local authority debt that are only focused on managing the existing debt or just reporting may not yield sustainable results if institutional weaknesses and governing issues that cause the problem are not dealt with. Thirdly, in order to understand how different local authorities deal with their respective financial constraints and the implications thereof on debt levels, future research needs to be council-level and involve the kind of mixed-methods comparative study that a metropolitan council versus a small town council can illuminate. If this research is undertaken, it will move from just recognizing that local government debt is an issue, toward actually understanding why it continues to grow in the way that it does.

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The Authors declare no competing interests.

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Authors' Contribution Statement

Formulated and designed the study; established the research framework and technique; directed the composition of the initial manuscript draft.

Ethical considerations

The article followed all ethical standards appropriate for this kind of research.

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