



CENTRE  
FOR CIVIL  
SOCIETY

# Social Change & Public Policy

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PARTH J SHAH

LIBERTY  
& SOCIETY  
SERIES

7

# LIBERTY & SOCIETY SERIES

**C**entre for Civil Society organizes seminars for students, professors, journalists, and NGO leaders all across India. These seminars began with the Liberty & Society Seminars (LSS) for college students, which have since been renamed ipolicy. These four-day residential seminars engage students in vital issues of public policy, involve them in creating a new vision for India, and ultimately help them become better citizens. They provide participants with a greater understanding of the larger world—society, economy, and culture—within a liberal framework, which emphasizes limited government, individual rights, rule of law, free trade, and competitive markets.

The challenging of conventional wisdom and the excitement of discovery experienced at these seminars have been described by participants as ‘once in a lifetime’ experiences. The success of the Liberty and Society Seminars, and now ipolicy, in creating new thinkers and leaders suggested the idea of publishing key lectures so that others might partake of the intellectual adventure. The lectures are a synthesis of research studies and various arguments that are by nature polemical. This series of publications seeks to make these stimulating lectures from various CCS programs available to a wider audience: the Liberty & Society Series!

This particular publication has been published in partnership with Friedrich-Naumann-Stiftung für die Freiheit.

## LSS TITLES

1. *Why is India Poor?*
  2. *Education Policy: Choice & Competition*
  3. *Environment: The Tragedy of the Collective*
  4. *Private & Political Markets: Introduction to Public Choice*
  5. *Ethics of Liberty*
  6. *Courage, Fear & Immigration*
  7. *Social Change & Public Policy*
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Printed December 2011

ISBN: 81-87984-01-5

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# Social Change & Public Policy

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Parth J Shah\*

**W**e all want to bring about social change. In today's talk I will argue that among all the options, public policy is the most effective tool for real, lasting social change.

Let me give a quick example of the power of public policy: The Indian Forest Act classifies bamboo as a tree. All the rules that apply to trees apply to bamboo and the Forest Department controls its use. As a result, only some connected contractors have access to forest bamboo. If it were classified as a grass, however, as it scientifically is, then the bamboo would be out of the Forest Department's control. Tribals would be able to access it as a resource to earn their livelihood. A large scale use of bamboo would also save trees and timber, a tremendous environmental benefit.

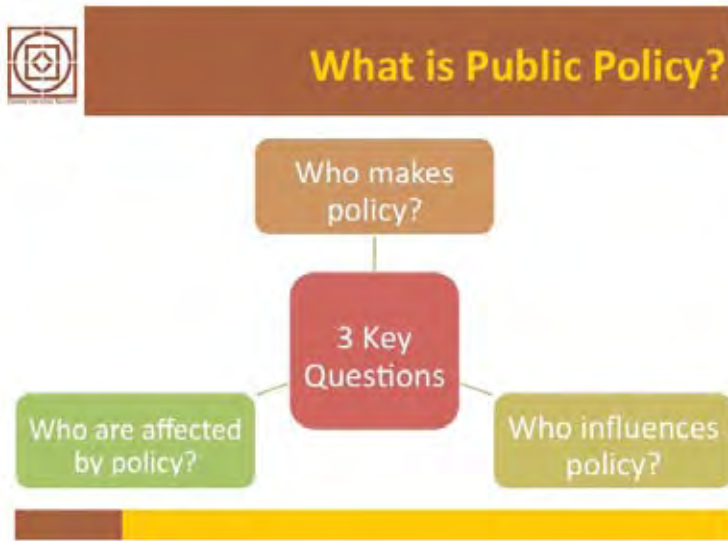
To bring about this policy change, CCS ran a campaign: *Bamboo is Not a Tree*.<sup>1</sup> What would be the impact of this small change in policy? It would help millions of tribals all over the country whom we don't even know. It might save millions of trees too. That's the power of public policy.

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\*Special thanks to my colleagues Andrew Humphries for helping transcribe and edit this document and Bhuvana Anand for developing the slides.

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**Section 1: Public Policy: What, Who, Whom?**



**W**hat is public policy? A public policy is basically a law or rule that is enforced by any level of government, whether central, state, or local. Our activist judiciary also makes public policy: that all public transport in Delhi must run on CNG, for example, was a Supreme Court decree.

Governments frequently make broad statements about the future direction of development in a sector, also generally called 'policy.' The New Education Policy of 1986 or the Telecom Policy of 1994 are examples of 'policy' in this sense. Various tiers of government also formulate a variety of schemes and programs. When I say 'public policy,' I include all of the above: schemes, programs, sectoral policies, rules, regulations, laws, as well as judicial policy-decisions.

**Who makes policy?** It's clear from the above definition of public policy that it is made by different tiers of government as well as the judiciary.

**Who is affected by public policy?** By penalizing some forms of behavior and rewarding others, policies change the costs and benefits of different directions of action. Policies can be thought of as 'rules of the game' of everyday life. These rules affect the way people choose to pursue their goals and thus influence the combined, overall, and unintended results of everyone's actions.

Policies mainly affect the individuals under the jurisdiction of the government that makes and enforces the rules. However, as we shall see in a moment, who exactly is effected by policies and how is not as clear and straightforward as you might expect.

**Who influences public policy?** This is an interesting question. The first answer people usually give is that, in a democracy, citizens influence policy. This is true. In a representative system of government, policy makers' ability to hold office ultimately rest on their ability to acquire votes from their constituents.

However, to have a deeper understanding of who influences policy, we must ask: who has an *interest* in the outcome of a policy?

Most policies are constructed to favor particular groups, but may not actually be beneficial to the greater population.

Policies create benefits and costs to different groups. Individuals in these groups thus have an incentive to try to influence the final shape of the policy environment. It is important to realize that this incentive is greater for some groups than others.

Definite groups, such as businesses in the same industry, unions, bureaucrats, lobby to influence policies in their favor. They plead with politicians for a policy and give money for campaigns, perhaps even direct or indirect bribes of one kind or another. Groups that experience highly concentrated benefits or costs and that can easily organize their members will tend to have a greater influence on policy.<sup>2</sup>

So-called 'special interest groups' are also more likely to know how policies will affect them than average citizens are. As a consequence, in a democracy (where politicians compete for votes), most policies are constructed to favor particular groups, but may not actually be beneficial to the greater population.<sup>3</sup>

**The Role of Think Tanks** In addition to groups that attempt to influence policies for their own material benefit, there are also policy or idea organizations called 'think tanks.' Think tanks advocate for one kind of policy rather than another, not because of material benefits or costs to themselves, but because they believe certain policies are morally superior and/or more effective in promoting the interests of the general population. Centre for Civil Society is an example of such an organization.

**What I will argue is that if you want to achieve sustained social change on a large scale, the best way is to create better public policy.**

In a moment, I will describe the difference between two ways of working to help address social problems: the one is direct action, working on a problem directly, the other is policy action, working through policy to influence the way in which others act to address a problem. This could mean removing a bad policy, revising an existing policy, or creating one where none exists.

But first let's start by looking at the root causes of some persistent social enigmas.

## Section 2: Common Problems and their Causes

The infographic features a brown header with the text "Some Common Problems Financing of Films" in yellow. Below the header, on the left, is a photograph of a man with a mustache sitting in a chair. To the right of this photo is a white text box with a drop shadow containing the text "Bollywood producers borrow from Dawood Ibrahim to finance new films". Below the first photo is a smaller photo of a man with glasses sitting at a table with a water bottle. To the right of this second photo is a yellow starburst shape with the word "WHY?" written inside in black. At the bottom of the infographic is a horizontal bar with a brown section on the left and a yellow section on the right.

### FINANCING OF FILMS: NEXUS BETWEEN BOLLYWOOD & THE UNDERWORLD

#### *The Issue:*

Bollywood producers like Mahesh Bhatt used to meet regularly with people from the underworld, like Dawood Ibrahim, to raise money for their film projects. Why was this the case? You don't see this with most other industries, so why in the film industry?

#### *Common Response:*

Is it because there is something inherently different about movie projects *per se*? Perhaps it is because filmmaking is a risky enterprise and no one else would invest in it.

#### *Discussion:*

Indeed, a lot of money is involved in a film project and there is no guarantee that it will succeed. There is obviously a very high risk. But if this were the answer, wouldn't we see similar problems arising in the film industries of other countries like the US, England, and Pakistan?

Moreover, if films are not a good investment, why would underworld investors be willing to fund them with so much of their own money? Presumably Dawood Ibrahim lends his money because he believes film proj-

ects will make him money.

Other industries are risky too. In those industries, there are venture capitalists who lend money to fund risky, but potentially profitable, ventures. Mukesh Ambani is able to raise capital to build refineries. There is no guarantee that these expensive projects will be profitable, either.

So 'risk' itself is not a reason why filmmakers would look for money from the underworld, especially when we consider the danger related to underworld 'collection' methods. Why would someone put his life on the line rather than seek legal capital?

### *Policy Perspective:*

What happens when, instead of looking at the unique aspects of the film industry to find the cause of the problem, we look at the government policy that regulates the industry?

Here we find the answer. For many years, film was not a 'legally recognized industry.' The Industries Act of India 1951 listed all the industries recognized by the government and only those industries were allowed to borrow money from formal financial institutions. Unfortunately, Bolly-

Problems that seem quite unrelated to policy on the surface often have government policy as their root cause.

wood was not on that list. Film producers were forced, because of the government policy, to choose between not making their movies or going to dangerous, underground venture capitalists.

Bollywood was given official industry status in 2001. Now the film industry is recognized and is legally allowed to borrow from formal institutions. As a consequence, in the past several years, stories about the nexus between Bollywood and the underworld no longer appear in the news.

This was a simple solution. When this was going on, there were always sociological commentaries about what it was in particular about film that connected it to the underworld. The literature didn't mention the nexus between the Industries Act and the problem. What I'm trying to demonstrate is that problems that seem quite unrelated to policy on the surface often have government policy as their root cause.





## Some Common Problems School/College Admissions

- Long queues for admissions
- Donations & capitation fees
- Interviews of parents and children



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### SCHOOL ADMISSIONS: WHY SO FEW GOOD SCHOOLS?

#### *The issue:*

I'm sure you've seen this in your city. I've seen this in Delhi every year: long queues for school admissions and parents paying huge fees, bribes, 'donations.' I've witnessed this going on for over ten years. News articles denounce the way schools are taking advantage of parents, accusing them of extortion: every year the same long lines, the same harassment. This happens not only for one or two years; it happens year after year after year.

The existence of persistent long lines indicates that there is a *shortage*: the quantity of schooling supplied in the market is less than the quantity demanded. One would expect, however, that these lines and high prices would induce other potential providers to enter the market over time, to increase the quantity supplied, and to bid down the price to attract parents. This is what happens in basically all other industries. We see it with electronics, restaurants, clothes. But the shortage in schools is basically endless, so you have to ask yourself, *why?*

#### *Common Response:*

Education is different from electronics and restaurants, you can't really compare them. It's not an issue of the quantity of schools *per se*. Parents only want their children to go to 'good schools,' ones that have established reputations.

*Discussion:*

Every industry is different from every other. Each one has unique qualities and has to overcome problems that are peculiar to it, but the principles of supply and demand are the same for all of them.

Isn't having a good reputation desired in all industries? Think about medicines, hotels, restaurants. Having a good reputation is needed in all of them. But the advantage of a good reputation doesn't cause persistent shortages in these industries.

Each industry has unique qualities and has to overcome problems that are peculiar to it, but the principles of supply and demand are the same for all of them.

In other industries, established businesses expand to meet unmet demand and new organizations enter the market. Such new businesses have to face some risk, advertize, and build a new reputation to attract consumers. Why don't those who have good reputations in schools expand their brands and why don't more schools emerge to meet demand?

*Common Response Continued:*

Isn't it because we lack good teachers? You can't enter the market if you don't have what you need to supply the service.

*Discussion Continued:*

Consumer demand for products and services causes producers to demand the inputs they need to produce those products and services. Demand for new schools, for instance, should create demand for more teachers. This is how the market works. Granted, the market process takes time. This may mean that increasing the supply of schools will take time, too. But why, for over ten years, have school entrepreneurs not increased the number of teacher professionals available through training and higher salary offers? Expanding the supply of good teachers would allow them to reap the profits from providing a competitive alternative to all of these parents who spend hours in line with forms filled out and money in-hand.

*Policy Perspective:*

Once again, what happens when, rather than trying to find something inherent about the industry that causes this problem, we look to public policy for the root cause?

When we look at the policy environment, we see that in Delhi, for instance, it takes 15 different licenses to open a new school, which is actually more

than the number of licenses you need to open a refinery—a much bigger project than opening a school!<sup>4</sup>

So what happens as a result? Many people who want to open a new school find it too costly or even impossible to do it without inside connections. This is also why so many schools and colleges are started by people who often know little or nothing about education but are well connected. That's why we see in Maharashtra, for instance, that so many colleges are owned by politicians. On the other hand, many people who are educators and care deeply about education, but who have no government connections, find it much too difficult to start a formal school.

Secondly, schools must be non-profit by law. This means that it is much harder for those who don't already have significant capital to finance a new school. If schools could be for-profit, it would be easier for promising start-ups to get money from venture capitalists. We see that venture capital is much less prevalent in schooling than in other forms of business.

Under the License Raj, schools are not run by those who could deliver the best service, but by those who have the best contacts and vast capital. It is no surprise we have shortage of good schools!



## Some Common Problems Street Vendors

For 20 years sitting in the same place with the same size business



Photo Source: Jijun Jia

### INFORMAL SECTOR ENTREPRENEURS: WHO KEEPS THEM DOWN?

#### *The Issue:*

You see street hawkers all around us. It may be that you or your family have bought your goods from the same woman in the same place for the past 20 years. Nothing has changed in her business for all that time.

She is a businessperson, right? Many people don't think about her that way, but that's what she is. She is an entrepreneur who started her own business. Dhirubhai Ambani is a rags to riches story. He started with very little, selling soap from door to door to build his Reliance brand. So why can't this hawker and so many others expand their businesses even a little?

What do you think? Are all these street hawkers inherently incompetent? Is it because they don't know how to grow the businesses they started 20 years ago?

#### *Common Response:*

Maybe it is because they don't have enough income to save and invest in expanding their businesses.

#### *Discussion:*

These guys make enough to keep replenishing their inventory for 20 years or more. They are probably capable of saving or borrowing from family

and friends to expand their businesses little by little, but they don't. So why don't they?

*Policy Perspective:*

Once again, is there something inherent about all of these street vendors that causes them to remain in the same position? Or is someone else the cause—someone who makes policies that affect their lives?

You can guess by now that the persistence of the problem is the result of bad policy.

I know you have seen the policy unfold in front of your own eyes. I've seen it often in Delhi. In the markets there are dozens of hawkers selling their wares when, suddenly, municipal officers arrive accompanied by the police. All the hawkers grab their goods as quickly as they can and run off. If they're too slow, they get caught by the police and all of their goods are expropriated. This is officially called a 'clearance operation.' After an hour or so, the police van leaves, and the hawkers filter back into the market. Life moves on, until the next 'clearance operation.'

What this means, if you think about it, is that if a hawker has a business bigger than the reach of his arms, the next time the police come, he'll only

Inclusive growth requires inclusive reforms.

be able to grab some of his inventory and lose the rest to the police. The bigger the business he has, the more he will lose. It doesn't make sense for him to expand.

*The size of his business cannot be bigger than the reach of his arms.* If he has a business of the same small size for 20 years, how much can he increase his income?

Some hawkers have told us that they're happy to pay bribes to the police as 'rent' to use the public space. The problem is, even though they pay a significant amount in bribes, they still don't acquire a protected right to operate—they remain 'illegal' or 'informal.' They continue to operate in an environment of insecurity and constant threat of loss. It's not that they don't have the skills or the vision to get out of poverty, but that the policy environment is stacked against them.

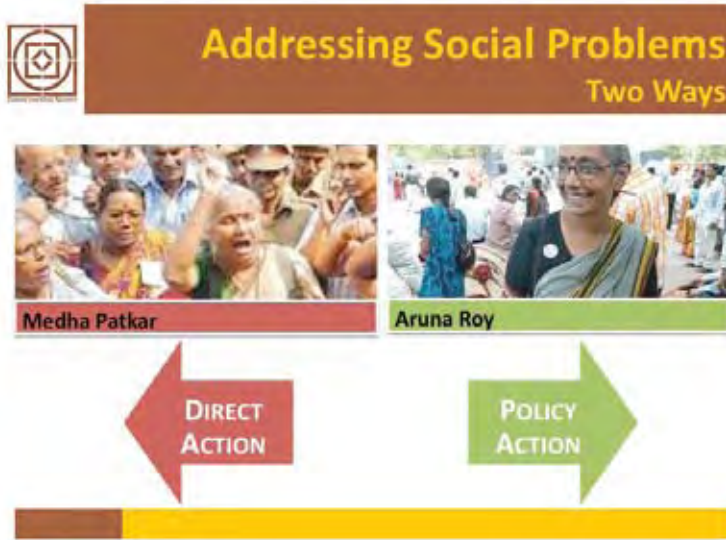
Instead of having to pay bribes, it would be much better if hawkers could pay official rent that would give them legal sanction to operate without being harassed by the police.

We all must emphasize this again and again: although we have removed the burden of License Raj from formal industry, the informal sector is still

suffering under it. This is leading to uneven and unequal economic growth. *Inclusive growth requires inclusive reforms.*

So if you think about public policy, you will start to see that the policy environment is often the root cause of persistent economic and social problems.

### Section 3: Direct Action vs. Policy Action



#### MEDHA PATKAR & THE “OUSTEES”

Medha Patkar has been working to secure the rights of people affected by large-scale development projects. People are forcibly displaced and their livelihoods disrupted by gigantic projects such as dams, highways, factories, SEZs.<sup>5</sup> Patkar seeks compensation and rehabilitation for them by means of hunger strikes and protests. She is working to address specific problems directly. She has spent more than 20 years fighting on behalf of the victims of the Narmada Dam project.

But how many places can she be at the same time? These kinds of projects and problems are everywhere across the country. By spending her time in one place, she can't be somewhere else. Her work is limited to the extent of her limits as an individual.

## ARUNA ROY & PUBLIC WORKS CORRUPTION

Aruna Roy is another social activist. She started trying to address corruption in Rajasthan in public works projects. It is common for people to be listed on the muster roll and get paid, even though they are not actually working on the project. At first, Roy and her organization, MKSS, lobbied government to get copies of the muster rolls.<sup>6</sup> They would then go to public works sites to check and expose the corruption by seeing who was actually there.

Roy knew that this was not just happening in Rajasthan, but all over the country. What would an NGO commonly do to address the wider problem? It

Aruna Roy is the paradigm of policy action, while Medha Patkar is the paradigm of direct action.

would ordinarily expand, trying to get more offices and workers in different places to ask and fight for these muster rolls in a direct fashion.

Roy realized, however, that this was a systemic problem. So instead of trying to organize people to address each and every instance of the problem herself, directly, she worked to pass the Right to Information Act (RTI). This action made everyone of us a potential “MKSS worker,” so to speak. This not only addressed the issue of muster rolls, but designed a law that empowered every citizen to ask questions about all kinds of instances of corruption throughout the country. She enabled



### Addressing Social Problems

Fish, Fish, Fish...



Give fish

Direct Action



Teach fishing

Indirect Action



Keep fishing as a viable livelihood

Policy Action

a decentralized process and network of problem solvers that surpassed her ability as an individual. She worked for a policy that allowed people to address the problems themselves. Moreover, she is now able to move on to address other issues like food security.

Roy is the paradigm of *policy action*, while Patkar is the paradigm of *direct action*.

### THE IMPACT OF DIFFERENT TYPES OF ACTION

You know the saying, 'Give a man a fish, you feed him for a day. Teach him how to fish, and you feed him for life.' This saying is analogous to moving from direct action toward policy action. Teaching someone to fish is less direct, but has a greater impact over a longer period of time. If we take this analogy literally, we can take the logic of this saying one step further. For people to be able to 'fish' for themselves, 'fishing' must remain a viable means of livelihood.<sup>7</sup> This requires policy action. If fishing is not a viable means of livelihood because of bad policy, what's the point in teaching or learning how to fish? Of course, fishing, in this analogy can stand for any form of livelihood.

Engaging in policy action is trying to improve the rules within which all other actions and interactions take place. Without the policy action to keep fishing a viable livelihood, giving fish would eventually be impossible and teaching fishing would be meaningless.





## ENDURING IMPACT OF SOUND PUBLIC POLICIES

The extent and the speed of impact differs between direct action (giving a fish), indirect action (teaching how to fish), and policy action (keeping fishing a viable means of livelihood).

You can see that indirect and policy actions tend to take more time, but impact more people. Direct action impacts fewer people but it does so more quickly. Giving a man a fish affects one person directly and immediately. Teaching him how to fish takes more time, but has a wider impact. Making or keeping fishing a viable source of livelihood takes even more time, but has a much greater impact.



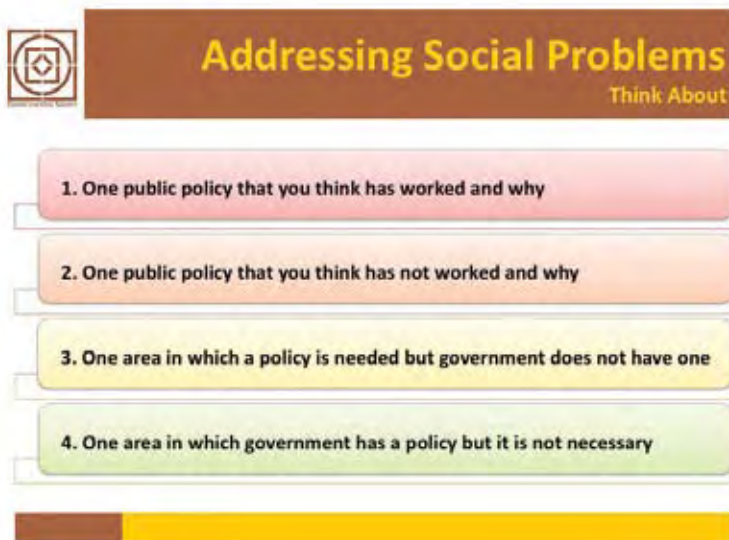
Several points of comparison suggest that effective policy action is often superior to direct action.

I don't want to imply that direct action is unimportant. There are clearly cases where direct action is essential to help alleviate human suffering, as in natural disasters. Direct action, working on the ground, can also help us understand the problem better, suggest sound policy solutions, and help ensure effective implementation of new policy.

In reality, direct action and policy action are complementary. What I am arguing is that in the long term, unless we pay attention to policy, direct action will only help treat symptoms for a short time but will not address root causes of problems.



**Activity 1:** At this point, think about public policies you are aware of. Try to come up with an example for each of the four categories in the slide.



Now, after having made your list, ask yourself: “What do *I* want to do about these policies?”

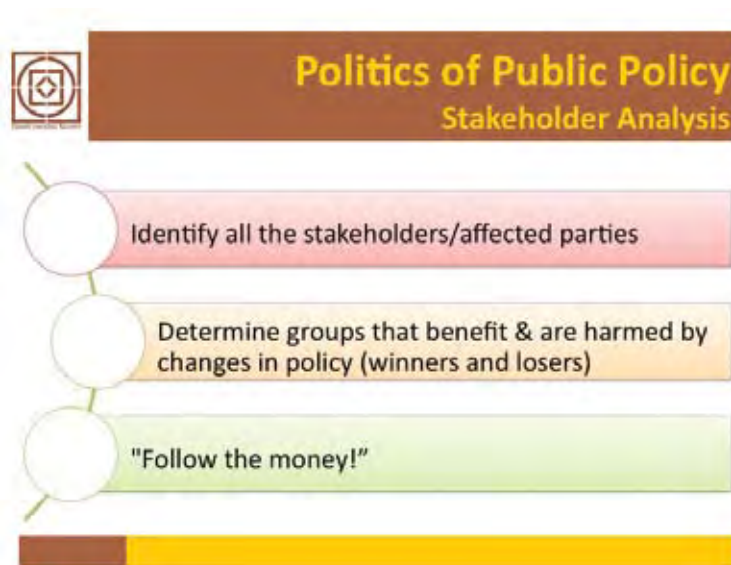


## Section 4: Principles and Politics of Sound Public Policy

After understanding the importance and power of public policy, we need a guide for evaluating policies. Two core ideas I want to discuss with you for evaluating policies are the politics of policy change and the principles of sound public policy.

### THE POLITICS OF POLICY

The politics of policy is defined by the balance of effects a change in policy will have on various groups—the winners and the losers. Even though in the long run a policy may benefit all groups in society, in the short run there are always some groups that are impacted positively while others are impacted negatively.



When thinking about the politics of policy, it is important to do a 'stakeholder analysis.' After identifying all the affected parties, we can see who will be the winners and losers. A helpful tool in this process is the maxim journalists use: follow the money! Consider how changes in policy will change the flow of income to the different groups involved, both directly and indirectly.

When we discuss the principles of sound public policy, we will see some examples that help illustrate the politics of policy change.

## PRINCIPLES OF SOUND PUBLIC POLICY<sup>8</sup>

How can we develop sound public policy? First, do no harm. Before trying to create a new policy to solve a problem, it is essential to research what policies are already in place that may have caused the problem in the first place. When a clear connection between a policy and the problem can be demonstrated, the policy should be removed or changed.

When we think about the kind of society we seek, one that is free and open and one in which prosperity is widely dispersed, there are some general yardsticks we can use to evaluate policies. Policies that result in persistent problems, like the ones mentioned above, tend to be those that undermine the liberal framework of society: individual rights, clear and decentralized ownership and responsibility over resources, the rule of law, freedom of exchange, tolerance, and limited government.<sup>9</sup>

I've gathered ten principles for you to consider when designing or evaluating public policy.



## Sound Public Policy

### 10 Principles

# 1

A sound policy has government do only what individuals and associations cannot do for themselves.



‘A government that’s big enough to give you everything you want is big enough to take away everything you’ve got!’\*

This is the first principle of a free and open society. People should be allowed to do things they can do for themselves. When people are able to care for themselves and others, it is unwise to take away their freedom and responsibility to do so.

Government should only assume those tasks which are needed for the general welfare but which are too difficult to coordinate through the market and voluntary association. Society doesn’t need a policy for everything. We expect people to be polite with each other, for instance, but we don’t want the government to make detailed rules about how we will act in this respect and impose fines for rudeness.

Look at the pictures in this slide. We see from these examples that charity and enterprise can usually be provided through voluntary, civil society. However, we probably don’t want to leave the basic police function to private enterprise. It would, therefore, be appropriate to have government organize the police.<sup>10</sup>

\*Along with the ten principles, I have included memorable quotes from Lawrence Reed, Henry Hazlitt, Milton Friedman, and Ayn Rand, which I think express the main point of each principle succinctly.



## Sound Public Policy 10 Principles

# 2

A sound policy considers long-term consequences over all groups of people not just the short term effects on one group.



This should be pretty obvious. Yet, policymakers and the general public often neglect to think carefully along these lines. Policies are usually designed to help one particular group, but other groups end up being harmed because the effects on these unseen groups are not immediate and obvious. Intended beneficiaries are also often harmed when you take a long-term view. F. A. Hayek calls this perverse effect of policy, where intended beneficiaries are actually harmed, ‘the law of unintended consequences.’ When assessing policy, it is essential to try to foresee the consequences to all groups.<sup>11</sup>

‘The bad economist sees only what immediately strikes the eye; the good economist also looks beyond.’

Each of the programs in the slide above is an example of a policy that benefits a small group in the short-term, but fails to take the long-term consequences into view. Each distorts markets, reduces productivity, and makes

capital scarce, which in the longer term lead to higher costs of living and less employment.

Let’s take the case of trade restrictions (the picture in the middle of the slide). Many people argue for tariffs or exchange controls to keep foreign goods from competing with domestic goods. This sounds like a plausible way to create prosperity if we think only about established businesses and their employees. But it doesn’t take into account that consumers and producers who use those goods will have to pay higher prices or that protected producers will have less

incentive to innovate and be responsive to their customers. Nor does it take into account that Indian *exporters* will lose business because foreigners who are able to *sell less to India* are able to *buy less from India*. India experienced years of stagnation due to such trade restrictions. We see the benefits of the opening up that happened in 1991.



## Sound Public Policy 10 Principles

# 3

A sound policy will enhance:

- Choice
- Competition
- Freedom



Civil society is essentially about cooperating for mutual benefit—being free to associate with whomever we wish and being free to offer each other alternatives in the marketplace of ideas, goods, and services. The freer consumers are to choose who serve them and the freer producers are to compete with established providers, the better.

‘Free people are not equal and equal people are not free.’

The 1991 reforms have removed the License Raj for much of the formal sector. We have seen the benefits of reform in several sectors, telecom and airlines, for

example. People have access to more options and better prices and companies are more responsive and accountable to consumers. Entrepreneurs are also less burdened when they wish to start enterprises.

While the 1991 reforms have meant that Mukesh Ambani of Reliance Industries does not need a license to start a refinery, street hawkers still need a license from the municipal corporation. The informal sector suffers from the License Raj even today.





## Sound Public Policy 10 Principles

# 4

A sound policy focuses on measurable outcomes, not just inputs and good intentions.



It is important to recognize the distinction between intentions and actual effects. Good intentions are not enough for sound policy. The Right to Education Act, for example, is motivated by noble intentions. Who would question the goal of promoting quality education for all children? With this intention in mind, parts of RTE require schools to make all kinds of infrastructural improvements, from libraries to toilets and playgrounds. But we also have to consider the *effects* of these requirements: they put many schools out of business which can't afford to meet these requirements.

'The road to hell is paved with good intentions!'

You may not worry about schools going out of business *per se* but you probably do worry about the families these schools serve. Poor parents choose to send their children to these budget private schools because they find them preferable to the alternatives. Parents see the learning outcomes, the RTE focuses only on the inputs into the system. The focus on the inputs reduces poor parents' freedom, choice, and access to education.



## Sound Public Policy

### 10 Principles

# 5

A sound policy aligns incentives by moving up the hierarchy of Friedman's Law of Spending:

- Spend your money on yourself
- Spend your money on someone else
- Spend someone else's money on yourself
- Spend someone else's money on someone else



There are four ways to spend money, as shown in the slide. Compare these types of spending on two criteria: efficiency and effectiveness, that is, how much the spending benefits its beneficiary.

Most of the spending we do fits in the first category. When we buy clothes and food we spend our own money on ourselves. In the second category are gifts and direct charity. In these categories we usually shop around and try to ensure that our money is economized and used for the greatest benefit.

The third category occurs when someone else pays for or reimburses our expenses. Think about this category. In your experience, when people go out to eat at company expense, are they

'Nobody spends someone else's money as carefully as he spends his own.'

as careful about the price of their entrée as they would be if they were paying themselves? Have you ever decided to spend more for yourself when someone else was paying the bill? You probably don't spend other people's money as economically as you spend your own. Even though you don't care as much about the cost (efficiency), you do care about the benefits (effectiveness).

Most government spending falls in the fourth category. There is little incentive to economize or use the resource for the maximum benefit. This is why there is usually so much waste and corruption in this category.

The Nobel Prize winning economist, Milton Friedman, argues that we should

try to design policies so that the parties involved move up the hierarchy, from the fourth to the third type of spending. For an illustration, consider two different ways the government can provide education to students, one, through government schools and two, by means of school vouchers.

Government schools are an example of the fourth category: spending someone else's money on somebody else. Instead, government can give school vouchers to parents who can use them to pay for any school of their choice. Though the voucher is not originally the recipients' money, once the voucher is put in their hands, it becomes their resource. Although, they have little incentive to minimize costs, since the voucher covers the cost of tuition, the parents have an incentive to maximize their benefits by choosing the right school. Likewise, the school would continue to receive money only while parents remained satisfied, otherwise they will go to another school. The school would steward the resources in a way that aligns more closely with parents needs; it would have to offer competitive benefits to parents compared to other schools. Vouchers move parents and schools—the education policy—from the fourth category up to the third on Friedman's hierarchy of spending.<sup>12</sup>

**Sound Public Policy**  
10 Principles

**6** A sound policy would enable governance (like decisions about taxes and expenditures) closest to the people.

When governments handle resources, it's generally best that they be managed at local level where individuals have more information and influence to keep officials accountable. This principle is the basis for the 73rd and 74th Constitutional Amendments about decentralizing functions, functionaries, and finances to the third tier of the government.

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‘The government has nothing to give except what it takes from somebody.’

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This principle complements our first principle above, which stated that only those functions that people can't perform for themselves should be given to the government. Within the

government, we should assign tasks first to the local government. Those functions that the local government cannot handle should be given to the state/provincial government. The central/federal government should undertake only those activities that the other tiers of government cannot. The government is subsidiary to people and central government to state and state to local government. This is also called the principle of subsidiarity.

Decentralization is an effective way to move from representative democracy to participatory democracy. Instead of having all decisions made by elected representatives, we should create space where some of the most critical decisions are made directly by the people. Mature democracies have ballot initiatives or referendums where issues are directly voted upon by the people. Many countries conducted referendums on whether their country should join the European Union; they didn't leave that decision to the parliament. We need to develop such participatory mechanisms in India.

A radical way to implement this principle would be to allow people to decide how their taxes will be allocated among the different functions and departments of government. While some portion of the taxes, maybe half, could be used at the government's discretion, as it is done now, the tax payers could choose where they want to send the rest when they fill out their annual tax return.



## Sound Public Policy

### 10 Principles

# 7

A sound policy would impose the same standards, norms and punishments for non-performance on government as are imposed on non-state providers.



‘Some people are dissatisfied with free enterprise if it doesn’t work perfectly, but satisfied with government if it works at all.’

Ramalinga Raju of Satyam went to jail immediately while Suresh Kalmadi of Commonwealth Games fame is still at large. When private scandals are exposed, we punish transgressors. But we don’t apply the same standards to government officials.

We have heard of civil suits raised against Coca-Cola over contamination. How many times are there similar law suits over poor quality municipal tap water? Public policy must have the same norms and punishments for private as well as government service providers. The Consumer Protection Act of 1986 technically applies to all providers goods and services, private, and government, but rather cleverly excludes goods and services provided ‘free of charge.’ It also excludes statutory functions of the government like education and health. Many government acts expressly deny any liability for poor service, like the Indian Post Office Act of 1878. It exempts government from any liability of lost or stolen post. Since many government services are free at the point of use, the consumers have no legal grounds under the Act to complain. Is this double standard a good argument to privatise government services and provide better protection to consumers?

The recent Madhya Pradesh Public Services Guarantee Act 2010 is a pioneering effort in assuring minimum standards of service. It imposes clear penalties on public officials for dereliction of their duties. Bihar and Delhi have followed up

and several states are considering a similar act. Recently the union government has proposed Electronic Service Delivery Bill which will guarantee quality of all services that are provided electronically. It is promised that the Bill will extend to services provided non-electronically in about ten years.



## Sound Public Policy

### 10 Principles

# 8

A sound policy will not sacrifice the rights of an individual for the interest of many.



'The smallest minority on earth is the individual. Those who deny individual rights cannot claim to be a defender of minorities.'

This principle is one of the most controversial. Many argue, for example, that government must redistribute land from farmers for factories and SEZs. They say that the interests of farmers must be sacrificed for national

development. How can you build a highway or a damn without taking land by force? Some people just aren't willing to sell. Other people 'hold out' until they can demand extortionately high prices because their land is needed to complete a project.

Firstly, yes, there are people who don't want to sell their land at any price, but there are also areas where owners are trying to attract developers. Why can't development happen where people are willing to sell? Also, why can't development take place through more, small-scale projects that reflect voluntary arrangements rather than through a few monolithic projects that require force? People who argue against property rights say that the goal is 'development,' but development for whom? What is the meaning of 'national' development when individuals are sacrificed?

Next, there are effective ways to get around the 'holdout problem' voluntarily. Contingent contracts are an example. When a developer wants to undertake a project that requires a lot of land, he can sign contracts with each interested party that make the purchase contingent on all the other parties agreeing. Under this arrangement, no one seller has special bargaining power. This is only one example. The point is, when people have to work within the framework of individual rights, they think of creative ways to realize opportunities for mutual benefit.

It's interesting to note that the dilution of the fundamental right to property was applauded as a way to help the poor at the expense of the rich at the time of nationalization of industries, banking, and insurance companies. Now the poor feel helpless when the government takes away their land on behalf of some of the rich. When the principle of individual rights, of property rights in this example, is abused, every individual becomes a potential victim of the over-powerful. Today it's 'them,' tomorrow it will be us.

This principle is basically that anyone, including the poor farmers, should have the constitutional right to say 'no' to acquisition by government or private developers. This ensures society is based on consensus and voluntary agreement rather than on force.



## Sound Public Policy

### 10 Principles

# 9

A sound policy is based on the premise that people are responsible, resilient, and self-governing given the right set of incentives and framework of law.



When making policy, we often fall into the conceit that we are in a better position to make practical and moral decisions for other people. We, the more 'educated and enlightened,' want to decide who has access to alcohol and when, how people must spend their money, how many children a family can have.

Democracy rests on the principle that voters are responsible enough to elect their representatives. We respect people's political decision-making rights. We should also respect their economic and social decision rights.

'Trust the consumer in using her money vote in the private market just as you trust her as a voter in casting her ballot vote in the political market (election).'

Family, friends, the market, and civil society each has a role in helping people face challenges of life. Ultimately, however, respect for the humanity of each individual means that each must be free to choose what he does with his own life and should bear the responsibility of the choices he makes.





## Sound Public Policy

### 10 Principles

# 10

A sound policy should often have an expiry date (sunset clause).



Once a policy is on the books, it becomes very hard to change. Sunset clauses make it easier for policies to elapse that have outlived their usefulness. Of course, we would want some laws forever, like those against murder or theft. However, a vast majority of schemes and regulations should have an expiry date.

A sunset clause does not mean that the policy must end after a certain period of time, but that the policy must be reviewed and reapproved after a pre-determined period in order to

‘Nothing is as permanent as a temporary government program.’

stay on the books. For example, the Indian Constitution made a provision for caste-based reservation in government jobs, schools, and colleges but included an expiry date of 10 years. Every ten years, the parliament is required to review and revote to continue the policy.

Many policies on the books are seen by officials as outdated or irrelevant and are, therefore, not enforced. Why should anyone be concerned about this? Precisely because some official at some point in time can decide to enforce them at will. This makes the law a potential weapon for those in office to use against those they wish to harm or control. Some will go free and some will be punished, all at the discretion of the official. This is the opposite of the rule of law.

For example, police often used the anti-sodomy law (section 377 of the Indian Penal Code of 1860) selectively as a tool of harassment and extortion against homosexuals. It is off the books now, but if it had had an expiry date, it would have been reviewed long ago.





## END NOTES

<sup>1</sup> In 2011, Jairam Ramesh, the Minister of Environment, issued an executive order to rectify this. We are still waiting to have the states conform to this order.

<sup>2</sup> For an in depth discussion of why some groups have more influence over government policy than others, see Mancur Olson's *Logic of Collective Action*.

<sup>3</sup> See Bruce Yandle's *Bootleggers and Baptists*: <http://www.cato.org/pubs/regulation/regv7n3/v7n3-3.pdf> and *Bootleggers and Baptists in Retrospect*: <http://www.cato.org/pubs/regulation/regv22n3/bootleggers.pdf>

<sup>4</sup> This number is based on CCS research done in 2001.

<sup>5</sup> Special Economic Zones

<sup>6</sup> MKSS stands for Mazdoor Kisan Shakti Sangathan.

<sup>7</sup> If we take the analogy literally, fishing actually provides a prime example of the importance of public policy. People almost everywhere are fishing at unsustainable levels, even though most fishers are aware that their collective actions will result in a collapse of fisheries. It is well understood among economists that over-fishing (along with a host of other environmental problems) is the result of what is called 'the tragedy of the commons.' The tragedy of the commons occurs when no one has a property right, i.e., the authority to exclude others from consuming a resource. Attempts of any individual to conserve the resource by lowering his own consumption are futile because others will take what he has left behind in the commons. In this case, if fisherman choose to catch less or throw back small fish, there is no guarantee that the next fisherman would do the same. Thus, all fishermen keep all that they catch, depleting the fishery.

A sound policy for fisheries will establish clear property rights among individuals or small communities who have the power and incentive to conserve the resource. Two excellent publications on this matter: *Fishing for Solutions* by Michael de Alessi <http://www.iea.org.uk/publications/research/fishing-for-solutions> and *Overfishing: The Icelandic Solution* by Hannes H. Gissurarson <http://www.iea.org.uk/sites/default/files/publications/files/upldbook16pdf.pdf>

<sup>8</sup> This part of the talk was inspired by Lawrence W. Reed's *Seven Principles of Sound Public Policy*. His article can be found here: <http://www.mackinac.org/archives/2010/7Principles2009FINALweb.pdf>

<sup>9</sup> For a comprehensive statement of the idea of Liberalism, see *Liberalism* by Ludwig von Mises <http://mises.org/books/liberalism.pdf>

<sup>10</sup> A classic philosophical exposition of this idea can be found in *On Liberty* by John Stuart Mill [http://files.libertyfund.org/files/347/Mill\\_0159\\_EBk\\_v6.o.pdf](http://files.libertyfund.org/files/347/Mill_0159_EBk_v6.o.pdf)

<sup>11</sup> *Economics in One Lesson* by Henry Hazlitt is an excellent resource for an extended exposition of this principle. The book trains its reader to think like an economist and to apply this principle to various common topics [http://www.fee.org/pdf/books/Economics\\_in\\_one\\_lesson.pdf](http://www.fee.org/pdf/books/Economics_in_one_lesson.pdf)

<sup>12</sup> For a discussion of Friedman's Law of Spending and the voucher idea, see Milton Friedman and Rose Friedman's *Free to Choose: A Personal Statement* and Milton Friedman's *Capitalism and Freedom*.

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