



# HOW TO LEAD SUCCESSFUL BUDGET NEGOTIATIONS?





Network of Associations of Local Authorities of South-East Europe

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## RECOMMENDATIONS FOR LOCAL GOVERNMENT ASSOCIATIONS ON THE RULES AND PROCEDURES OF BUDGET NEGOTIATIONS

Developed by the NAMRB Expert Team within the framework  
of the NALAS Task Force on Fiscal Decentralisation



NALAS Task Force on Fiscal Decentralization  
Hosted by the National Association of Municipalities from the Republic of Bulgaria



**How to lead successful budget negotiations?  
Recommendations for local government associations  
on the rules and procedures of budget negotiations**

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# FOREWORD



The National Association of Towns and Municipalities of the Republic of Bulgaria (NAMRB) is the host association of the NALAS Task Force on Fiscal Decentralisation (TF FD). As the other NALAS Task Forces, TF FD provides a platform for permanent exchange of experiences among local experts from NALAS member countries, performs comparative analysis and produces recommendations in the field of local finances. The results of its activities are being published and presented on the NALAS website within the Knowledge Center.

The publication *How to lead successful budget negotiations? - Recommendations for local government associations on the rules and procedures of budget negotiations* sets the conditions, objectives and modalities of successful cooperation during the budget negotiations process: no matter how well a framework legislation defines the rules governing municipal revenues and expenditures, there is always a need for structured continual dialogue between the national government and local governments. Therefore, the procedural rules of budget negotiation between the National Association of local governments and the Ministry of Finance are extremely significant tools in achieving fiscal objectives and protecting municipal interest in the course of drafting the annual national budget act. The recommendations presented in the publications were elaborated by the NAMRB Expert Team, with support of other NALAS members.

This publication comprises several parts:

- ▶ The principles and guidelines on institutionalisation of the budget dialogue and procedural rules on budget negotiations, including subject of budget negotiations, information required for negotiations, timing of budget negotiations, participants, forms and pattern of negotiations;
- ▶ Proposal for the structure of the Memorandum on agreements and differences to be signed between the Association and the Ministry of Finance, as well as the summary of budget negotiations process, including legal provisions, agreement with the Ministry of Finance and calendar for national budget planning;

- ▶ Recommendations on legal regulations regarding budget negotiations in NALAS countries and sample regulations on budget negotiations in NALAS countries;
- ▶ Polish example on institutionalizing a continual dialogue between the national government and local governments, described by Tony Levitas, as well as comparative evaluation of alternate institutional arrangements.

The publication was commented by the Editorial Board, constituted of three recognised international experts. Therefore, NALAS is particularly thankful to the members of the Editorial Board that contributed to the quality of the publication:

- Mr. Gabor Peteri
- Mr. Dieter Falk
- Mr. Tony Levitas.

Finally, the publication could not be prepared without the valuable inputs of NALAS member associations and the members of the Task Force on Fiscal Decentralisation: the guidelines were presented and discussed at the meetings of the Task Force held during 2007. Additionally, the country experts from 6 NALAS members besides NAMRB, associations of Macedonia, Slovenia, Republic of Srpska, Serbia, Romania, Montenegro and Kosovo, provided information and material on the situation in their countries.

Guinka Tchavdarova  
NAMRB Executive Director



# NALAS TASK FORCE ON FISCAL DECENTRALISATION

As the network of associations of local authorities of South Eastern Europe, NALAS brings together 13 national associations which represent over 4,000 local authorities, elected by more than 80 million citizens of this region. At the heart of NALAS are the Task Forces, gathering competent association staff and professionals employed in the local government administration.

The NALAS Task Force on Fiscal Decentralisation (TF FD) tackles the common problems of local governments in the field of local finances, from budget negotiations with the central government, improvement of the property tax administration, estimation of costs of municipal services, to municipal finance databases, local borrowing and municipal program budgeting. A part of comparing the situation in the countries of the region and identifying best practices, the activities of TF FD are focused on capacity development programs both for associations of local authorities and local governments.

The National Association of Municipalities of the Republic of Bulgaria (NAMRB) is the host association of the FD Task Force. Besides NAMRB, as the host association, the associations of Serbia and Romania took the lead in developing and implementing the first projects in the field of fiscal decentralisation.

### Experts of the Fiscal Decentralisation Task Force

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# ABOUT THE PROJECT

The NALAS Fiscal Decentralisation Task Force has launched a project on the assessment and improvement of negotiations between the local government associations and the relevant partners in the national government. The project was lead by the expert team of the National Association of Municipalities of the Republic of Bulgaria (NAMRB).

The overall goal of the project is to improve the local governments' negotiation position during fiscal planning and budget implementation process. More specifically the project aims to improve the responsiveness of intergovernmental transfers on municipal priorities, to make grant allocation more transparent and more predictable and to establish clear fiscal equalization system.

The foreseen project outputs were to:

- ▶ Elaborate negotiation procedures
- ▶ Recommend models for cooperation between the Ministry of Finance and the associations
- ▶ Develop training modules for elected officials, associations' staff and the media
- ▶ Train member associations' experts and politicians.

# FRAMEWORK FOR LOCAL GOVERNMENT BUDGET PLANNING

A continual, institutionalized dialogue between national and local governments is critical for the stable and healthy development of any decentralized political order. At the same time, however, it is important to recognize that the goal of reformers in decentralizing societies should be to remove as many critical financial issues from annual negotiations as possible, and in particular to separate to the greatest degree possible the determination of the national budget from the actual planning of local government budgets.<sup>1</sup>

The best way to do this is to have a Law on Local Government Finance that specifies in permanent framework legislation the following:

1. The nature and type of all local government own fees, charges and taxes and the nature of their rate setting powers.
2. All shared taxes and the methods (rates, formulae) at which they will be shared with local governments
3. The nature of all categorical grants (earmarked, block grants) for permanent delegated or devolved functions (like primary education).

The rules governing such categorical grants for current budgets should specify the following:

- ▶ How the size of the grant pool shall be determined every year?

Such rules radically delimit the sphere of uncertainty surrounding major categorical grants and decouple the local governments from the annual determination of the national budget. To remove this issue from annual budget negotiations the rules specified in the law should “anchor” the size of the grant pool in some easily calculable way, that the grant pool should be:

- ▶ No less than the size of last years grant pool adjusted upwards for inflation and GDP growth;

<sup>1</sup> Separation, however, does not mean, that the two types of budgets are not interconnected: for example the ongoing and future processes of the European Integration in the NALAS countries bring us to the fact that most regional development funds must be absorbed and co-financed– by local governments, meaning that if local government finances are in bad state and not well regulated, then the absorption of the EU funds will be less than optimal.



- ▶ No less than X% of the central government revenues for taxes A,B,C (or all) for the previous fiscal year ;
- ▶ No less than Y% of the GDP from the previous fiscal year.
- ▶ How will the specific grant allocation formula work if used? What are the basic principles behind the formula that will be used to allocate the grant? In this case the law should specify when and between whom the formula will be discussed and ultimately approved.

### What is the timing of the budget negotiations?

For example the formula for the Ministry of Education will be to submit a draft formula for the allocation of the categorical grant for education to the Municipal Association by June 15th of the year prior to the FY in which the formula will be applied. The submission of the formula will show the allocation of the categorical grant for all jurisdictions based on clear assumptions about the size of the grant pool for the concerned fiscal year and will include a justification of any changes in the formula from the previous year. The Association will have 15 days to review the formula before discussions of it are held. By July 30th the Ministry will present a final version of the formula to the Association and for allocation purposes only. By Sept. 15th, the Ministry of Education will send a budget circular to all local governments informing them of the amount of their education grants based on the most current assessment of the size of the grant pool.

The nature of all general grants, including equalization grants.

As with categorical grants for delegated purposes the rules should make the size and the allocation of these funds more or less automatic by specifying how the grant pool should be determined, and by defining at least the basis on which the formula is to be allocated.

- ▶ *For example, Serbia's Local Government Finance Law specifies that the size of the general/equalization grant is pegged to 1.8 percent of the previous years GDP and also includes the formulas that govern its allocation. The rules should also specify when initial estimates of each local government are to be made. Macedonia's rules define the general grant in terms of a specific percentage of the national yield of the VAT, and state the general principles by which it should be allocated, but leave the determination of the formula up to the Ministry of Finance, following discussions with the municipal association.*

And as with categorical grants for major delegated functions the rules in the law should set schedules for the presentation of draft formulas (if any) and for sending LGs information about their expected grants by some time in the early fall of the year prior to the FY in which the formula will apply.

➤ *It should be noted that some revenue equalization formulas do not require the specification of a grant pool, and are still automatic. Poland's system is a good case in point. Here, all local governments whose per capita revenues from shared taxes are less than 90 percent of the national per capita average are entitled to a per capita equalization grant equal to 85% of the difference between their per capita yield from these shared taxes, and 90% of the national average.*

In specifying such a formula it is important to specify whether the grant will be calculated on the basis of last year's actual performance (adjusted upward for inflation and GDP); the projected performance for the concerned fiscal year; or the actual performance during the concerned fiscal year. Here too, however, the Ministry of Finance should be required to submit to LGs an estimate of the yield of their individual grants some time in the fall of the year prior to the concerned FY.

The nature and procedures by which all categorical grants for specific (one time) purposes will be determined and allocated. For example, there are often many categorical grants for specific types of investments. And often there are many different line ministries or agencies of the government who award them to local governments.

To help make this area more transparent the Local Government Finance Law should require that all agencies:

- ▶ Consult with the municipal associations in determining grant schemes (e.g. matching grants), procedures, and selection requirements, including co-financing payments prior to announcing the availability of the grants.
- ▶ Publish these schemes, schedules, procedures, and selection requirements.
- ▶ Issue year end reports on the use of the grant funds by individual jurisdictions.

The nature of any debt limitations to remove these limitations from annual discussion and to avoid the need for the pre approval municipal loan or bond issues by the Ministry of Finance.



The law should require the Ministry of Finance to submit to the municipal association(s) by the middle of the second quarter of every fiscal year the revenue and expenditures of each and every local government by line item in detail and in accordance with the full chart of accounts for the previous fiscal year.

The law should require the creation of a negotiation forum, e.g. an intergovernmental finance commission, to discuss on a regular basis all new legislation ordinances that effect local government revenues or their expenditures.

The targeted audience of these recommendations is primarily the countries of South Eastern Europe, where typically local government associations are strong, large and unified ones. Most of the techniques proposed here will work only in these unitary states with one tier local government system. We focused mostly on the annual budget preparation process, so the local government association's role in the budget implementation, amendment of the annual budget and tax laws, in budget reporting, etc. are not discussed here.

We could not take into consideration the specificities of intergovernmental fiscal relations, so the complexity of fiscal regulations is not reflected by these recommendations. Instead of influencing local tax laws, national tax sharing schemes, municipal borrowing regulations, capital investment grants, regional development programmes, we concentrated on the preparation of the annual budget document. However, all these other decisions are closely related to the design of the actual budget law, they are usually discussed in one package, so they could be part of this negotiation procedure.

Within this area of annual fiscal planning we did not discuss the impact of budgeting techniques on local governments, so we assumed that national budget appropriations are based on incremental budgeting. We did not deal with the not concentrated and delegated functions, our main focus was on the devolved tasks, where local governments have autonomy in defining local spending priorities and these services are financed by a mixture of national budget revenues, shared and local taxes.

# INSTITUTIONALISING THE BUDGET DIALOGUE

No matter how well framework legislation defines the rules governing municipal revenues and expenditures, there is always a need for structured continual dialogue between the national government and local governments. Developing the institutional framework for such a substantive dialogue takes time and is often an uneven process. It is often and unfortunately also dependent on the willingness of the governing coalition to take local governments seriously.

Depending on the constitutional and political system of a country there are various options for institutionalized dialogue. In some countries any laws related to municipal issues have to be commented by the local government associations (e.g. Hungary), while in others there are permanent fora for discussions (e.g. Poland, see Annex III.). Results of these negotiations are obviously legislated by the Parliament.

The procedural rules of budget negotiation between the National Association of Local Governments and the Ministry of Finance are extremely significant tools in achieving fiscal objectives and protecting municipal interest in the course of drafting the annual national budget act. We might say that the outcome of such negotiations is the criterion to measure the ability of the Association to support their members and the willingness of the government to listen to what municipalities have to say.

Ever so often the practice of budget negotiations suffers from certain deficiencies related to:

- ▶ vague and opaque criteria applied to determine the allocation pattern of national budget transfers among municipalities ;
- ▶ insufficient time to discuss existing issues and define adequate measures to solve them;
- ▶ the Ministry of Finance proposes solutions to a specific problem without discussing these within the framework of other measures and probable consequences;



- ▶ frequently changing or amended regulatory framework on municipal finances ;
- ▶ incomplete and outdated fiscal data base of the Association of municipalities ;
- ▶ a lack of means for information exchange.

Therefore, there are several conditions for successful cooperation during the budget negotiation process. The first imperative is, that based on clearly defined principles permanent procedural rules are approved and adopted. Opportunities should be sought after to define the powers of the association to participate in budget negotiations pursuant to permanent legislative acts. Participants of bilateral talks have to be precisely designated. All relevant information should be shared and schedules of budget negotiations have to be defined in timely manner.

The Association of Municipalities will certainly benefit if assistance from independent experts is sought after. Advice can be obtained from independent experts who are usually not directly involved in municipal work or in the national agencies, from international organizations and NGOs, when drafting proposals for legal amendments, monitoring reports on results, training of staff, etc.

It is equally important that the Association establishes and adheres to a practice where common position is established following previous discussions, seeking of consensus to overcome conflicting interest between municipalities of diverse scales. It is important that the entire process involves the participation of a wide range of experts and elected representatives of local governance, efficient interaction with ministries and governmental offices is maintained and the indispensable assistance of the parliamentary lobby and representatives of civil society is sought.

# PROCEDURAL RULES ON BUDGET NEGOTIATIONS

## Principles of budget negotiations

The budget negotiations between local government associations and the Ministry of Finance should be based on the principles of:

1. Mutual trust by all actors and respect towards negotiation partners;
2. Equal access to information;
3. Transparency of negotiations (participants, agenda, information, agreements);
4. Agreed principles on publicity and relations with the media;
5. Clear authorization: making commitments that are in line with powers and actual capacity of participants;
6. Sufficient timing.

On the other hand, even though important, these principles should be translated to certain procedural rules in order to address the structural imbalance between the power of the national government (and the Ministry of Finance in particular) and local governments. Examples of these detailed procedural rules are, as follows:

- ▶ Regular meetings every month;
- ▶ A calendar for the discussion of particular issues, e.g. national government's budget memorandum and its implications for local governments (which is usually regulated by the budget laws);
- ▶ Establishment of a permanent secretariat, responsible for providing necessary information to the members of the commission/committee before meetings;

- 
- ▶ Explicit provisions that the costs of the commission, including per diems and travel funds for members, will be covered by the state budget.

### Subject of budget negotiations

Depending on the provision of general legislation on local government finances, the political and constitutional system, these negotiations should focus on the following issues:

Municipal draft budget at aggregate level:

- ▶ Total revenues, allocation by main type and by of own, shared revenues and by categories national transfers;
- ▶ Total expenditures, allocation of expenses by types of expenditures (functional, economic, administrative categorization).

National budget transfers to municipalities:

- ▶ Amounts of various types of transfers;
- ▶ Criteria and mechanisms for allocation of national budget funds;
- ▶ Separating transfers for current and capital expenditures;
- ▶ Rules for local authorities to manage intergovernmental transfers;
- ▶ Specific financial regulations for municipalities during the budget year;
- ▶ Detailed regulations on planning annual local government budgets;
- ▶ Other issues to be defined by mutual agreement, for example, growth of local taxes.

### Information required for negotiations

The *Ministry of Finances* shall provide:

- ▶ Updated three-year forecast and macroeconomic framework;
- ▶ Draft legislation on the planned changes the revenue and expenditure sides of municipal budgets;
- ▶ Budget instructions to municipalities as to how budgets should be constituted;
- ▶ Information on the amounts of national budget transfers;
- ▶ Assessment of financial impact of all new legislation on local governments;
- ▶ Presenting empirical studies and research preceding the drafting of specific laws.

The *National Association of Local Governments* shall provide:

- ▶ Substantiated proposals on the fiscal relations between local and the national governments' budget;
- ▶ Opinion and proposals on the state budget draft bill;
- ▶ Analysis on the issues related to the financial status of municipalities;
- ▶ Issues in current execution of municipal budgets and proposals on the amendments of the annual budget law.



## Timing of budget negotiations

The calendar on budgeting has to be regulated by law. Within this timeframe, a minimum of three rounds of negotiations are needed. First, on the principles of budget preparation and fiscal strategy (t-6 months); secondly, on the detailed budget concept, allowing sufficient time for budget hearings (t-3) and thirdly, on the final draft budget law, presented to the Parliament (preferably a minimum one month before the start of the budget year (t)).

## Participants, forms and pattern of negotiations

The negotiations should be carried out at two levels: at expert and at political levels<sup>2</sup>. Expert level negotiations should precede political negotiations and should be used to prepare a common position and draft solutions to be finalized at the political level meetings. Representatives to participate at both levels are to be assigned by the Minister of Finance and the political leadership of the Association (e.g. Board of Directors).

The expert team of the Association can be comprised of the respectable experts from municipalities, administrative staff of the Association and independent local finance experts from partnering organizations. Simultaneously with approving members of the negotiation team, the political leaders of the Association sets the objectives, tasks and the framework to be followed by the expert team members while negotiating with the representative of the national government (the Ministry of Finance and other central governmental agencies).

The objectives and tasks of the Association's negotiating team should be derived from documents, adopted by the Association, e. g:

- ▶ a middle- and long-term strategic plan;
- ▶ an annual programme of the Association;

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<sup>2</sup>. In practice, the perennial issue of materials being supplied late and incomplete by the government make the recommended concept of separate political and expert talks difficult to implement in practice. Also, the politicians may fear that if experts go into rooms on their own, deals will be struck behind peoples' backs, something that could be very divisive given that there is almost no solution to any problem that will fully satisfy all participants. Finally, the documents developed by experts can become non-transparent and incomprehensible to the average mayor. The Association should be aware of these challenges and minimize it and try to strengthen the connections between two levels, expert and politicians. In some NALAS countries, where the local governments (usually one in a country) have a strong voice, large staff, support from donors, they can be influential at expert level (as it is the situation with the Standing Conference of Towns and Municipalities and NAMRB). They are strong advocacy organisations.

- ▶ decisions of the Board of Directors and the General Assembly of the Association on key issues of local governance development;
- ▶ analysis on the financial status of municipalities;
- ▶ forecasts on development of local finances, etc.

During the budget negotiations the experts and politicians from both sides usually discuss the issues together. The purely technical problems are very rare, so politicians will always look at the debated topics differently than the experts. This is an argument for letting the politicians listen to their own (and perhaps other experts) and then letting them argue. The real solution is not to put the Associations experts in a room with the governments' experts and hope that they can narrow the range of differences to an acceptable level. Each side is supposed to listen to their own experts, and then to use that knowledge to reformulate their own positions, or sharpen their attacks.

In order to make the Association's negotiation power stronger, the following steps have to be made:

- ▶ hiring of their own, competent experts;
- ▶ the experts prepare materials, that explain what the government's position is likely to be;
- ▶ the materials presented by the experts make clear recommendations for what the Associations position should be, including the effect of the position on different members of the Association;
- ▶ the Association members discuss the expert recommendations among themselves before negotiating with the government;
- ▶ Association experts can participate in the work of the intergovernmental body and its committees.



## Tasks and working procedures of the expert team

Following the closure of annual accounts for the previous budget year, the Association draws its conclusions and disseminates an analysis on the municipal budget execution among the municipalities. Findings and conclusions are based on the factual content of municipal reports derived from individual municipal budget execution data. Data contained in the analysis should be used to point out deficiencies and outline general trends in municipal financial status as a whole and by groups of municipalities. Thus their attention should be drawn to existing reserves to be utilized and should assist them in formulating opinions and proposals to be used in drafting budgets for the coming budget year. Recommendations are formulated and options for changes in the forthcoming budget year are outlined by using this analysis. It is advisable that the draft analysis is subjected to discussion at large-scale municipal meetings and conferences.

Usually separate expert groups of the Association negotiate with the Ministry of Finance and with other governmental agencies. Their activity is coordinated and monitored by the members of the Association's political leadership or mayors that are professionally trained and have the expertise to deal in the respective area of negotiations;

In some countries the groups of experts might agree with the respective ministries on the required information exchange and schedules of working meetings at expert level. The tasks of such an expert group are considered complete with the signing of bilateral protocols describing agreements reached, differences and proposals. Based on such protocols, the respective head of ministry delegation shall draft and submit a report accompanied by draft decisions to the Ministry of Finance - alternatively to the Government or the Prime Minister - on the results achieved in the expert negotiations.;

From time to time, the expert teams of the Association shall advise their own political leadership, the specialized committees of the Association and the municipalities on the current status of negotiations in an appropriate format. Based on municipal proposals and negotiation outcomes with the respective ministries, the team of experts shall prepare a draft common position on all existing issues and submit it for adoption by the Association along with a plan of measures.

After completion of the budgetary procedure and following the promulgation of the draft budget act a working group of financial experts of the Association might start preparing a consultative paper aimed at assisting municipal councillors, mayors and municipal financial officers to draft and adopt municipal budgets for the coming financial year. This consultative paper shall focus on new developments in the regulatory environment; provide practical advice and instructions on budget drafting, but having only an advisory nature.

Every municipality will independently prepare its own budget, and apply the budget regulations according to their individual objectives, specifics, municipal agendas and priorities. It is recommended that the Association organizes training seminars for municipal financial officers jointly with the Ministry of Finance on preparation of draft municipal budgets.

### Activities of the Association at the political level

The Association's political leadership shall review the results from the expert level negotiations and adopt a common position of the Association on the draft budget's items related to municipalities. In the course of the budgetary procedure, the representatives of the two negotiating parties shall hold several meetings at the political level in the Parliament, at political parties, etc. As part of the national budget preparation process, at the launching meeting, the Minister of Finance is supposed to present the national economic policy and priorities for the forthcoming budget year and the macro indices of the state budget and in particular objectives on municipal finances. NAMRB, the Bulgarian local government association organizes a "National Dialogue Day" for making its policies and views public (see the box below).



#### *National dialogue day in Bulgaria*

*The National Dialogue Day between the legislative and municipal authorities is organized in Bulgaria. This event is held by regions and involves the participation of Members of Parliament, municipal councilors, mayors, governors, NGOs, the media and citizens. At such meetings the Association informs the MPs of the most urgent issues, of commitments municipal authorities are willing to undertake and the support expected from MPs. In the course of the meetings the Association usually seeks the assistance of the MPs to support the common position and municipal proposals on the budget relations during the forthcoming year.*

At the closure of the budgeting process the two parties shall present their positions, justify their proposals, try to reach agreements on the issues discussed or at least to clearly formulate the diverging opinions. The budgetary negotiations of the Associations shall be finalized with the execution of a Memorandum of Understanding (Protocol) listing agreements and/or differences (see the following chapter).

# MEMORANDUM ON AGREEMENTS AND DIFFERENCES

At the end of the process of the budget negotiations, a Memorandum of Understanding on agreements and disputes between the Association and the Ministry of Finance should be signed. An example of this protocol from Bulgaria is presented in the box below:

- *Protocol signed in Bulgaria specifies the differences, rather than agreements reached on the draft budget act. Benefits of this type of memorandum are, as follows:*
- 1. All final agreements are reflected in the draft budget act or in the draft governmental regulation and other legislative acts;*
  - 2. Focusing on differences between the association and the ministry of finance in the course of the negotiations will allow a more precise definition of the most essential differences in the approaches and proposals of the negotiating parties on the relations between the state budget and the municipal budgets. It will be the basis for proposing careful examination at the government and at the parliament when the draft annual budget act is debated and adopted.*
  - 3. Clear definitions of the positions of the association on existing differences at this stage of the budget procedure shall enhance their opportunity to seek the assistance of the parliamentary lobby, the public and the media for their resolution. This is extremely important in the process of seeking and finding solutions within the mandatory balance between independent exercise of local choice and the financial stability at national level.*

This type of protocol on the differences between the opinion of the Association and the Ministry of Finance will usually comprise of substantive issues, such as:

- ▶ Types and amounts of intergovernmental transfers to the municipalities;
- ▶ The allocation mechanisms of municipal transfers;
- ▶ The relation between legally delegated responsibilities to local governance and their financial bases;
- ▶ Financial conditions to expand the range and improve the quality of services (performance standards) provided to the public by the municipalities;
- ▶ Limiting the powers of local governance authorities to actually determine local revenues;
- ▶ Constrains on municipal autonomy in determining the level of expenditures and independently manage intergovernmental transfers, in accordance with local specifics and local public interest;
- ▶ Providing resources to finance the measures planned by Strategies, Government Programs and other legal acts for developing local governments.

It is advisable that the protocol does not list all existing differences; rather, it should contain major divergences of position that exert a decisive impact on the interrelations between the central and municipal budget negotiators. Optionally, the preamble to the Memorandum of Understanding may describe some major agreements reached as a result of the negotiation process. It is unrealistic for any unified Association or when several associations exist to expect that disagreements over fiscal policy issues can be prevented within its membership. Issues concerning the allocation of public funds almost inevitably produce winners and losers across jurisdictions -even when grant pools are increased. These are real issues and real conflicts of interest. So rather than try to ignore these real conflict of interests, the Association has to be able to take a position that they can argue to their members which is the best reasonable compromise and to stand above the interests of particular groups and to represent the whole.

Agreements would generally include:

- ▶ Positive changes introduced in the macro frame of municipalities;
- ▶ Rights and responsibilities of local governments related to intergovernmental



transfers (grants, subsidies) that are not of earmarked nature;

- ▶ Requirements to harmonize criteria, prerequisites and pattern of distributing governmental budget funds among municipalities allocated to municipalities. Such earmarked funds may be allocated for various purposes, such as: assistance of underdeveloped municipalities of actual budget deficit; assistance to municipalities in providing public services to vulnerable or risk population groups; co-financing of municipal projects under national and donor programs; harmonized measures to increase investment capacity and local powers to implement local investment policy;
- ▶ Execution of annual independent monitoring to achieve the objectives ensuing from the agreement of cooperation between the Association of local governments and the respective authorities of central executive and legislative power;
- ▶ Other arrangements in accordance with national and local specifics;

The Memorandum of Understanding on these issues signed by the Ministry of Finance and the President of the Association of Local Authorities preferably shall be reviewed by the government and submitted to the Parliament as an annex to the draft governmental budget act. This should allow MPs to have a correct idea of existing differences, work out their own opinions, positions and proposals on existing issues and submit them for debates at the hearings of parliamentary commissions and in plenary meetings.

In addition, to facilitate their work, the Association might prepare and provide all MPs with specific financial data to support financial forecasts on proposed measures and solutions. Municipal proposals, reflected in the Memorandum of Understanding on the differences shall be presented, substantiated and defended at debates of the Parliamentary commissions by representatives of the Association designated to represent the Association at political level. When necessary, the Association requests and agrees on meetings with the parliamentary groups of political parties elected to the Parliament.

# BUDGET NEGOTIATIONS: A SUMMARY

Institutionalizing of budget negotiations may be ensured both by implementing legal regulations and through specific agreement with the government or the Ministry of Finance. In this concluding chapter the most important elements of successful central-local budget negotiations are summarized.

## Legal provisions

Local government associations should promote general legal reforms primarily in two areas:

- ▶ Legislating a municipal (or public) budget act in such a way as to clearly separate the national budget process from the local one and by radically constraining the issues that need to be discussed on an annual basis.
- ▶ Establishing a regular negotiation mechanism, preferably in the form of a permanent intergovernmental affairs commission. This forum should have sufficient administrative capacity: secretariat, regular meeting schedule, permanent committee, government/local government co-chairs, etc. This institution might be used for discussing all other pieces of legislation that bears on the functioning of local governments or the services they provide.

The legislation on local governments or on public sector budgeting should guarantee the powers of the Association to:

- ▶ Develop proposals to amend and streamline the legal base of local governance;
- ▶ Come up with opinions and proposals on the draft national budget items related to municipalities;



- ▶ Make substantiated proposals on the total amount of funds available for local governments and the rules of intergovernmental fiscal relations;
- ▶ Express opinions and make proposals on the draft budget act the items related to municipalities;
- ▶ Carry out consultations with the Minister of Finance on the draft governmental budget act based on legally defined principles;
- ▶ Sign bilateral Memorandum of Understanding (Protocol) on agreements and differences with the Ministry of Finance. Such Protocol should constitute an annex to the draft budget act, reviewed by the government and to be submitted to the Parliament.

### Agreement with the Ministry of Finance

An agreement between the local government associations and the Ministry of Finance could be drafted and executed in two main forms. The purposes, content and impact of these agreements depend on the goals to be achieved, the level of institutionalization of budget negotiations and the cooperation on the non-budgetary issues.

#### **OPTION ONE: Agreement to carry out negotiations.**

Such an agreement is drafted and approved, provided that the regulatory framework for budget negotiations procedure is not in place or the practices of its application are unreliable and contradictory. Should such be the case, the procedural rules described by model procedural rules may be applied.

The draft agreement could be prepared by a team of the Association or by a joint working group involving representatives of the Ministry of Finance or the government.

It is advisable that in the process of preparing a draft agreement the following issues are taken into consideration:

- ▶ Potential benefits for the Ministry of Finance ensuing from the execution of such an agreement are outlined. The Ministry will be able to carry out budget negotiations with a reputable partner of national standing, that is committed to solve the complicated task of making proposals on behalf of all municipalities, while at the same time takes into account the specifics of their circumstances;
- ▶ Persuade the Ministry that the Association will urge for the support of the

Parliament, the media and the general public to meet the expectations of the citizens for improved public services;

- ▶ Commitment to complete those tasks, that the Ministry of Finance will also benefit from, such as improvement of fiscal discipline and audit, support to municipalities lacking administrative capacity, organization of training , etc.;
- ▶ The Association undertakes the responsibility to mobilize resources at local level, which would help to execute the adopted budgets and to summon wide participation of civil society in the management of municipal finances.

The Agreement shall be signed by the Minister of Finance and the chairperson of the Association and shall enter into force within the agreed timeframe. It is advisable that the document is widely publicized in the media, among the national executive and legislative powers, municipalities and civil society organisations. Subsequently, opportunities should be sought to institutionalize the clauses of the Agreement by virtue of a law or a legislative provision of the government.

#### **OPTION TWO: Agreement of interaction and cooperation.**

The Agreement shall contain procedural rules on the implementation of budget negotiations and major issues between the Ministry of Finance and the Association with regard to the local finance reform, such as:

- ▶ Cooperation to implement decentralization strategies and agendas in the management and financing of public services;
- ▶ Long and mid-term measures to expand the revenue base of municipalities;
- ▶ Changes in the distribution of financial responsibilities between state and municipal power in the area of public service provision;
- ▶ Streamlining the system of intergovernmental transfers and the criteria for their allocation among municipalities;
- ▶ Measures to increase the investment capacities of municipalities;
- ▶ Cooperation between the revenues administrations on a national and local level;
- ▶ Improve the exchange of information between the Ministry of Finance, the Association and the municipalities;

- 
- ▶ Support for enhancing the involvement of civil society in the decision making process on municipal financial policy and the exercise of public control over the spending of public financial resources;
  - ▶ Procedure for the Association's involvement in drafting and adoption of legislative acts related to municipal finances;
  - ▶ Organizing joint training and media events;
  - ▶ Other issues of mutual interest.

### Calendar for national budget planning

It is extremely important that the Procedural rules on budget negotiations between the Association of Municipalities and the Ministry of Finance are reflected in a national budget calendar for preparing the draft governmental budget proposal.

As a minimum, this national budget calendar should be adopted by the Government, but the critical steps of budget procedures might be regulated by legal documents. The calendar makes provisions on the following issues:

- ▶ Responsibilities of institutions in preparing the draft governmental budget act (the Council of Ministers, the Ministry of Finance, other ministries, governmental agencies, local councils, mayors, etc.);
- ▶ Major factors that help to improve the management of public finance;
- ▶ Relevant information and deadlines for the participants in the budget preparation process to provide information to the Ministry of Finance, the Council of Ministers and the Parliament;
- ▶ Obligations of ministers, responsible for the respective areas of activities, to advise in advance and to discuss with the Association of municipalities specific governmental policies, related to municipal budgets;
- ▶ Obligations of the Minister of Finance to sign a Memorandum of Understanding on the differences and agreements ensuing from the budget negotiations with the Chairperson of the Association of Municipalities.

# MEETING OF NALAS MEMBERS' PRESIDENTS

"MUNICIPAL BUDGET NEGOTIATIONS"  
Budva - Becici, June 27-28, 2008

## RECOMENDATIONS

NALAS Members' Presidents, present at the meeting on budget negotiations held in Budva on 27-28 June 2008, agreed on the following:

1. The Presidents of NALAS Member Associations endorse the draft document and recommendations on Municipal Budget Negotiations produced by the Task Force on Fiscal Decentralisation, lead by NAMRB.
2. All NALAS members will use the proposed recommendations, with the necessary adjustments to specific circumstances of individual countries.
3. In those countries where the adequate legal framework does not exist, the process of amending the laws should start immediately, in order to ensure the participation of Local Governments Associations (LGAs) in budget negotiations.
4. Additionally, a Memorandum of Understanding that regulates in more details the process of negotiations should be signed between LGA and the Ministry of Finance, as well as with the Parliament.
5. NALAS recommendations for draft amendments and MoU should be used.
6. LGAs have to overcome any differences among their members and to formulate common positions. In that way, the Associations will build the necessary trust with its membership.
7. The Negotiation Team of the LGA has to have a clear mandate and to represent common positions on behalf of all municipalities, not the position of their own municipality.
8. The roles of LGAs and the Ministry of Local Self-Government should be clearly defined and divided, since only the associations can speak on behalf of the municipal interests.



9. The capacities of LGAs as well as of municipalities should be strengthened, in order to be able to conduct municipal budget negotiations with central government.
10. All LGAs should have their own databases that would comprise all relevant data, including budgets of all municipalities in their country. The LGA analytical capacity is a precondition for effective negotiations.
11. The associations should actively involve media in the process of budget negotiations and use them to get support of the public.
12. Budget negotiations should finish by signing the Protocol of agreements and disagreements with the Ministry of Finance.

### List of participants

Association	Representative
AAM	Refik Rrugija, President
AAM	Fatos Hodaj, Executive Director
AKM	Bajram Rexhepi, President
AKM	Sazan Ibrahim, Executive Director
NLAMM	Ion NEAGU, Vice-President
NLAMM	Viorel Furdui, Executive Director
SGOFBiH	Nedžad Koldžo, President of the International Affairs Committee
ALVRS	Radomir Kezunovic, President
SOS	Mirko Brulc, mayor of Nova Gorica
SCTM	Milivoj Vrebalov, Mayor of Novi Becej
SCTM	Djordje Stanicic, Secretary General
NAMRB	Penka Penkova, Vice-President
NAMRB	Ginka Chavdarova, Executive Director
ZELS	Andrej Petrov, President
ZELS	Dusica Perisic, Executive Director
UOM	Veselin Bakic, President of the Assembly
UOM	Zarko Pavicevic, President of the Executive Board
UMMR	Bulent Hamdi Cingil, Mayor
UMMR	Murat Daudov, Head of EU & International Relations Centre
NALAS	Tarzan Milosevic, President
NALAS	Kelmend Zajazi, Executive Director
CoE	Michel Rivollier, NALAS Liaison Officer

## ANNEX 1: RECOMMENDATIONS ON LEGAL REGULATIONS REGARDING BUDGET NEGOTIATIONS IN NALAS COUNTRIES

These standard recommendations target typical countries of South Eastern Europe. Possible use of these regulations should be adjusted to the domestic political, legal administrative environment in a specific country.

### General Powers of the Association

It is recommendable these powers to be regulated under the general law on Local Self-government.

*Art. ... The Association of Local Authorities:*

1. *Represents its members before the National Executive and Legislative Authorities*
2. *Develops standpoints and proposals on draft-laws, related to the activities of the local authorities, as well as on country State budget in its part for the municipalities.*

### Powers of the Association on Budgetary procedure

These powers to be set in the law regulating local finances.

*Art. ... In the frame of the budgetary procedures for the respective year, the Association of Municipalities makes a motivated proposal on general amount of inter-relations between municipal budgets and state bud ce.*

*Art. ... Following the preparation of the State draft budget, the Association of municipalities prepares a standpoint and proposal on the draft law in its part for the municipalities.*

*Art.... The Minister of Finance accomplishes consultations with the Association of municipalities on proposals made by them under the above mentioned articles.*

*Art. ... Consultations under the article above are conducted in compliance with the rules on mutual respect, confidence, equality, transparency and publicity, taking a responsibility in accordance with the adequate power and real capacities of central and local authorities.*



*Art. ... Dissension from consultations is set in a bilateral signed protocol and it is attached to the draft law on state budget and then shall be presented to the Parliament together with the draft law.*

### *The case of Bulgaria*

*Regarding the equalising mechanism: Negotiations on the general amount and distribution criteria of the transfers*

*Art. ... The criteria on the allocation of state transfers under the equalising mechanism are settled through negotiations between the Minister of Finance and the Association of Municipalities.*

*Regarding targeted investment transfers - negotiations on general amount and criteria of distribution:*

-  *Capital expenditures for municipal infrastructure*
-  *Expenditures on main municipal activities: education, healthcare, social activities, culture and sport.*

*Art. ... The criteria for the allocation of target investment transfers on capital expenditures for municipal infrastructure are settled through negotiations between the Minister of Finance and the Association of Municipalities.*

Note: Regarding determination of the general amount of all kind of transfers to the municipalities - they shall be bound to stable objective indicators, for example the share of GDP, or of state tax income, etc.

The following text shall be developed separately (with eventual specific in form) for every municipal activity, covered by State transfers - for example education, healthcare, culture, sports, social activities, etc.

*Art. ... The Association of Municipalities together with the Minister of ... (the respective line minister shall be pointed) develop norms/methods for evaluation of the activity costs for ... (the particular activity shall be included).*

On this basis they prepare together a motivated proposal to the Minister of Finance for the establishment of a general amount of the earmarked investment transfers to municipalities as well as the amount of transfers to the respective municipality.

### ➤ *The case of Serbia*

A possible approach is establishing a permanent intergovernmental authority (State-Association) with consultative and monitoring functions, often called Grant Commissions. It can be implemented by legislative text (as in case of Serbia) or by agreement between the Association and the Government or the Ministry of Finance.

*Art. ... A Commission on Budget Co-operation between the central and local authorities shall be established. It has consultative functions in the process for determination of the criteria for the allocation of transfers from the central budget to local authorities. It will make monitoring regarding the activities on implementation of the state budget in its part for the municipalities. Through its activities the Association will have to secure the enforcement of the principles of equality, efficiency and transparency in budget relations with the municipalities and will make proposals for their improvement.*

*Art. ... The Commission has members. 1/2 of them are nominated by the Association of local authority. 1/2 of it members are nominated by the Ministry of Finance. The Commission has two Chairpersons - one nominated by the Association and other nominated by the Ministry of Finance. The Commission shall decide by majority of votes of present members provided that half of Commission members plus one are present at the session.*

*Art. ... The Commission shall conduct its sessions at minimum once every three months. The Commission is obliged to present statements on budgetary relations for every stage under the budgetary procedure, as well as in budget development and during budget implementation.*

*Art. ... The Commission shall make proposals on:*

- ▶ *the criteria and methods for the allocation of non earmarked investment and general transfers to the local authorities;*
- ▶ *the criteria for the allocation of earmarked investment transfers, as well as to national programs for target development, and make statements on application procedures and selection;*
- ▶ *the monitoring of vertical and horizontal balance of the system. Evaluation of system influence towards the horizontal equalization and make proposals for improvement and effective application;*
- ▶ *the Commission makes an annual analytical report on budget relations efficiency with regard to local self-government development and makes proposals on their improvement.*

## ANNEX 2: SAMPLE REGULATIONS ON BUDGET NEGOTIATIONS IN NALAS COUNTRIES

### • BULGARIA

#### Local Self-Government and Local Administration Act

##### Article 9

#### (3) National Association for Municipalities:

represents its members before state authorities;

develop proposals for amendments and improvement of the local self-government legislation;

elaborate country draft budget statements and proposals in its part for the municipalities;

(4) Rights under paragraph 3 shall enter into force, if more than 2/3 of municipalities are members of the National Association;

#### Municipal Budgets Act

#### Interrelations between Municipal Budget Central Budget

##### Article 34

(4) General Equalizing Subsidy for local activities is aimed to secure minimal level of the local municipal services. Criteria for allocation of the General Equalizing Subsidy for municipalities shall be established by the Minister of Finance together with the National Association of Municipalities in the Republic of Bulgaria.

(6) The Minister of Finance and National Association of Municipalities in the Republic of Bulgaria shall set up the amount of Capital Subsidy and criteria for its allocation.

### Article 37

(1) Within the budgetary procedure on elaboration of the draft law on state budget for the respective year the National Association for Municipalities in the Republic of Bulgaria shall develop a motivated proposal on general amount of interrelations between the municipal budgets and central budget and shall present them to the Ministry of Finance.

(2) The National Association of Municipalities in the Republic of Bulgaria shall submit a standpoint and proposal regarding the draft law, developed by the Ministry of Finance, in its part for the municipalities.

(3) The Minister of Finance shall conduct consultations with the National Association of Municipalities the Republic of Bulgaria with regard to its proposals under (1) and (2).

(4) Consultations under (3) shall be conducted observing the principals of mutual respect and confidence, equality, transparency and publicity, taking a responsibility in accordance with the adequate power and real capacity of central and local authorities.

(5) Dissension from consultations under (3) shall be set up in bilateral signed protocol and attached to the draft law on state budget of the Republic of Bulgaria and shall be considered by the Council of Ministers.

## LAW on State Budget of the Republic of Bulgaria for the year 2008

### Article 13

(5) Unused resources for ecological projects under Enclosure #8 shall be forwarded to the Ministry of Finance at the proposal of the Ministry of Environment and Water of Bulgaria in coordination with the National Association of Municipalities in the Republic of Bulgaria for other ecological projects.

### Paragraph 35

(1) Municipalities with objective structural deficit shall be supported under the conditions and order specified by the Council of Minister and coordinated by the National Association for Municipalities in the Republic of Bulgaria.

(2) Council of Ministers shall determine criteria for the municipalities with the objective structural deficit in coordination with the National Association of Municipalities in the Republic of Bulgaria.



## Paragraph 50

Funds stipulated under Art.1, line 2, point 2.1 for the amount of 12 000 thousand BGN for sub financing by the municipalities on particular projects of Social Investment Fund, Program "Beautiful Bulgaria" and other programs and 1500 thousand BGN for Investment project, executed by two or more municipalities shall be distributed by order determined by the Minister of Finance in coordination with the National Association of Municipalities in the Republic of Bulgaria

### BY-LAW Regulation Acts

Decision #142 of Council of Ministers on Budgetary Procedure

*(This act shall be adopted every year with analogous texts)*

2.2.2 May 30, 2008 shall be the deadline for observing the provisions of the Minister of Finances under point 2.2.1 and the approved decisions under point 2.1.4 as follows:

b) the ministers responsible to conduct and coordinate the national strategy and policy in the respective sphere shall work out and present at the Ministry of Finance three year budgetary programs for the period 2009-2011 for the activities, funded by individual budgets, non-budget funds and Enterprise on Management and Activities for Environment Protection, and preliminary consultations shall be made with the respective bodies, and in part for delegated by the State services, funded by the municipality budgets shall be consulted with the National Association of the Municipalities in the Republic of Bulgaria.

c) the Minister of Healthcare and Minister of Culture considered with the Minister of Finance and the National Association of Municipalities in the Republic of Bulgaria shall develop a proposal for standards on costs for State delegated services (hospitals, museums, local libraries) funded by municipal budgets.

d) the Ministry of Education and Science, the Minister of Healthcare, the Minister of Labour and Social Policy, the Minister of Culture in coordination with the Minister of Finance and with the National Association of Municipalities in the Republic of Bulgaria shall develop proposals for municipal budget funding standards on revenues of State delegated services.

Decree # 15 of the Council of Ministers on State Budget Implementation

### Article 39

The Ministry of State Policy for Disasters and Accidents and the Minister of Finance considered with the National Association of Municipalities in the Republic of Bulgaria shall adopt a criteria for distribution of the revenues for the amount 10,000 thousand BGN, earmarked by municipalities for the measure aimed in case of disasters up to March 2008.

### Article 42

(1) The Ministry of Healthcare shall provide a subsidy to the municipal hospitals in rural and risk regions in compliance with criteria and order determined by the Minister of Healthcare and considered by the National Association of Municipalities in the Republic of Bulgaria in the frame of funds anticipated by the law on State Budget of the Republic of Bulgaria for activities in the year 2008.

### Article 61

(2) The Minister of Education and Science up to August 1st and December 20th shall inform the National Association of Municipalities in the Republic of Bulgaria for the execution of the programs under line 1, related to the municipal property.

### Article 76

(1) The Minister of Finance together with the National Association of Municipalities in the Republic of Bulgaria up to February 20, 2008 shall determine order funds distribution for sub financing of particular municipal projects under paragraph 50 from previous final regulations for the Law on State Budget of the Republic of Bulgaria for the year 2008.

## • KOSOVO

Law no. 2003/2 "LAW ON PUBLIC FINANCIAL MANAGEMENT AND ACCOUNTABILITY"  
Low no. 2003/2 "LOW AN PBLIC FINANCIAL MANAGEMENT AND ACCOUNTABILITY"

Excerpts: Section 58.1 "There shall be established a Grants Commission no later than sixty (60) days after the effective data of the present law. The members of the Grants Commission shall be the Prime Minister, the Minister of Finance and Economy, another Minister appointed by the Government, the Chairman of the Budget Committee of the Assembly, and three representatives of the Municipalities nominated by the Association of Kosovo Municipalities and approved by the Government.



## • ROMANIA

Law no. 215/2001, re-published - Law on Local Public Administration

### Article 8

(1) The central public administration authorities shall consult, before adopting any decision, the associative structures of the local public administration authorities, in all matters that directly concern them, according to the law.

(2) The associative structures of the local public administration authorities are:

- a) Association of Communes in Romania;
- b) Association of Towns of Romania;
- c) Association of Municipalities of Romania;
- d) The National Union of Municipal Councils of Romania;
- e) Other associative forms of general interest, established in accordance with the law.

## • SERBIA

Law on Local Government Finance

### *Predictability of the Republic Transfers*

#### Article 47

Overview of non-categorical transfers per local government units shall be prepared by the Ministry in cooperation with the Commission for Intergovernmental Finances.

Overview from Paragraph 1 of this article shall be integral part of revised Memorandum.

#### Article 50

A Commission for Intergovernmental Finances (hereinafter: Commission) shall be established to ensure the principle of fairness, efficiency and transparency of intergovernmental finance and to propose recommendations for its improvement.

## Article 52

The Commission President shall convene session minimum once in three months.

The Commission shall decide by majority of votes of present members provided that at least six of the Commission members are present at the session

## Article 53

Commission shall:

1. Analyze criteria and standards for the allocation of non-categorical and block transfers to local government units and setting the amount thereof in line with provisions of articles 37-44 of this Law;
2. Analyze programs for granting categorical transfer in a narrower sense, including application procedures and selection criteria;
3. Monitor the vertical and horizontal balance of the system, the level of debt incurred by local government units and results of changes of the intergovernmental finance system, and prepare annual reports that are due no later than May 30 prepared for the previous year on changes in the system
4. Prepare recommendations for amendment and improvement of intergovernmental finance reform

### • SLOVENIA

#### The Law on Financing of Municipalities

Excerpts: article 12: Before the presentation of the state budget to the Parliament the Government stipulates an agreement with representative associations of municipalities which foresee the kind and size of additional tasks which expense are included in the amount of the "proper size of the expenditure" of municipal tasks (or appropriate expenditure) and the average appropriate expenditure for the next year.



## • REPUBLIC OF SRPSKA

### Preparation of draft budgets for the local authorities

#### Article 21

The municipal body in charge of finance, in accordance with the Memorandum, shall submit guidelines to the budget beneficiaries on the drafting of budgets of the local authorities for the following fiscal year.

The guidelines from paragraph 1 of this Article shall contain:

- ▶ basic economic preconditions and guidelines for the preparation of draft budgets of local authorities for the following fiscal year;
- ▶ description of the planned policies of the local governments;
- ▶ assessment of the budget funds and expenditures of the local authorities for the following fiscal year;
- ▶ proposal framework amount of expenses for every beneficiary of the local authorities' budgets in the following fiscal year;
- ▶ procedure and timeframe on the drafting of budgets of the local authorities.

### Draft budget

#### Article 23

The procedure for determining the draft budget of the Republic shall be:

- ▶ The Ministry shall submit a draft budget to the Government for the following fiscal year;
- ▶ The Government may request additional information or clarifications regarding the draft budget of the Republic from the Ministry;
- ▶ The Government shall decide on the amendments to the draft budget of the Republic;
- ▶ The Government shall adopt the draft budget of the Republic for the following fiscal year and shall submit it to the Parliament for public debate;
- ▶ The Government, in accordance with the conclusions adopted by the Parliament in public debate on the draft budget of the Republic, shall draft a proposal budget of the Republic and shall submit it to the Parliament together with the Memorandum.

- MOLDOVA

The Law on Local Public Administration (28 December 2006):

**Article 6:**

The relationships between different levels of public administration:

The authorities of the central public administration can consult the representative associations of local public authorities on the problems concerning the local public administration.

The Law on Local Public Finances (16 October 2003)

**Article 3:** The guaranties of the financial autonomy:

The authorities of the local public administration shall be consulted in an adequate manner in the issues concerning the procedure of redistribution of the resources to be allotted to them and concerning the changes of the legal framework regarding the functioning of the local public finances system.



## ANNEX 3: INSTITUTIONALIZING A CONTINUAL DIALOGUE BETWEEN THE NATIONAL GOVERNMENT AND LOCAL GOVERNMENTS - POLISH EXAMPLE

In institutionalizing a continual dialogue between the national government and local governments, Poland's development is instructive. In the mid-1990's Poland's Law on Local Government Finance called for the establishment of an Intergovernmental Affairs Commission (called the Joint Commission) composed in equal part by members of Poland's Local Government Associations and members of the government. The purpose of the commission was to discuss all draft legislation and governmental decision that effect the operation of local governments, though it should be added that from a fairly early point in the reform process the Poles succeeded in separating the determination of local government budgets from the determination of the national budget.

The initial idea of the commission was to endow it with a permanent secretariat and a state funded research budget to conduct analytical work needed to assess or amend legislation. In the 1990s this idea however failed. For most of the decade the Commission functioned but with more or less success under different governments. During this period, its Secretariat was "unofficial" and housed in the Union of Polish Metropolitan Cities, the association Poland largest cities (more than 300,000 people). In 2002-3, and as questions of the absorption of EU structural adjustment funds became more pressing, efforts were begun to strengthen the institutional basis of the Commission, efforts that led to a passage of Law governing the purpose, structure and operation of the Commission in 2004.

The following is a loose translation of the most important points of the law:

The purpose of the commission is defined in 5 points that cover:

- ▶ Developing common position concerning the functioning of communal services as well as the functioning of municipal and county self government;
- ▶ Regional development and the functioning of regional self governments;

- ▶ Analysis and appraisal of the legal and financial functioning of local self governments, including the functioning of state supervisory and inspection agencies;
- ▶ Analysis and appraisal local governments in light of European integration;
- ▶ Analysis of information about the preparation of legislation and government programs that bear on local self governments, particular with respect to their financial impact;
- ▶ Assessment of the effects of existing legislation on local governments;

The Commission includes 24 members, 12 from the government side, and 12 from the local government side. The head of the Commission is the Minister for Internal Affairs. (Here it is important to note that in the early years of reform -and before the passage of the Law-- this arrangement did not work because the Ministry of Finance often did not show up. Now, however, it seems to work well)

For local governments there are: 2 representatives of the county (powiats) governments, 2 for regional governments (voivodstwo) and 8 from the municipal governments. (gmina) For municipal governments there are 2 representatives for four types: larger than 300,000 inhabitants; with the legal classification cities; mixed rural urban municipalities; rural gminas.

These representatives are chosen by the relevant local Government Association. (Poland has five.) And the Associations must officially inform the commission of the selected representatives.

The Commission "in principle" presents opinions the reflect agreement between both sides but both sides are empowered to issue differing opinions in the case of a lack of agreement, or when for other reasons, only one side has been asked to comment on something. Both sides have 30 days from the submission of a project or law for consideration to express their differences. The lack of expression of a differing opinion is considered as agreement.

Ministries and government agencies must submit draft legislation and programs to the Commission with an assessment of their financial impact on local governments.

The Commission can create permanent Committees for certain issues, as well as temporary Committees. For both sorts of Committee the Commission can engage experts from outside the Commission. Committees are created on the basis of parity.

The Commission meets on an as-needed-basis but not less than once every two



months (In practice monthly, and meetings last all day. The local government side of the Commission traditionally meet the day before the meeting to work out common positions. The location of meetings is not always in the Warsaw.)

Meetings of the commission and of the committees must be recorded.

The permanent Secretariat of the Commission is responsible for informing members of the Commission and of the Committees of meetings.

The Secretariat is located in the Ministry of Internal Affairs. People travelling to meetings are entitled to per diems in accordance with the labour code. The state budget covers the cost of the Secretariat and other costs of the functioning of the Commission.

The Commission must develop its own statute which must be published in the Official Gazette.

There is a chapter in the law that will not be described that concerns the selection of Polish representatives to the Regional Development Committee European Union.

The Statute of the Joint Commission contains the following provisions:

- ▶ 9 permanent committees:
  - European Politics
  - Public Finance System
  - Education Culture Sport
  - Health and Social Welfare
  - Infrastructure, local and regional development and environment
  - Public Administration and Citizen Safety
  - IT
  - Public Statistics
  
- ▶ Committees should have no more than 14 members:
  - Parity of sides
  - Membership is determined by heads of each side

- Candidates for committee members have to be proposed in writing with recommendations
  - Joint heads of committees are chosen by committee members
- ▶ Meetings of the Commission should be held to discuss upcoming legislation. In principle all work of the Commission should be prepared by the committees prior to discussion at the Commission.
- ▶ Members of the Council of Ministers are required to submit all proposed legislation to the Commission for review.
- ▶ Materials for review by the commission are prepared by the joint chairs of the commission and the secretariat.
- ▶ Joint chairperson call meeting and establish agenda
- ▶ Members of the commission should be informed ten days before the meeting and should receive the appropriate materials for review at the same time.
- ▶ Materials cannot be sent later than three days prior to a meeting of the Commission
- ▶ Chairpersons may if necessary draft an opinion and send it to members of the commission for comments. If comments are submitted they must be included in next version of proposed opinion.
- ▶ Protocols of the Commission are prepared by the Secretariat and must be signed by both chairpersons before being sent to members of the Commission.
- ▶ Opinions and positions taken by the commission are sent to the appropriate ministries 14 days after signing of the protocol
- ▶ The work of committees takes place in accordance with schedules agreed upon by the committee chairpersons.



### Brief Assessment of the Commission and its statute (based on less direct knowledge):

The Commission has become an integral part of the Polish Political scene. How seriously its work has been taken however inevitably differs from government to government. But because Mayors come from all parties, it is hard for any government now to completely ignore.

Nonetheless the government remains the stronger side because it is, and because on many issues there are direct and irreconcilable conflicts of interest between different types of jurisdictions. It is thus extremely important that all types of local governments are represented in the dialogue.

Independent of occasional bad faith, there are still problems with the government submitting legislation to the Commission in due time for serious review. There are also problems on the local government side with members not doing their homework, and reading (or not reading) things on the train to meetings.

So far it is rare that the Commission hires outside experts as a Commission. But both sides of the table engage experts on their own, with the local government side employing expert through the associations. There is however, no expert to expert dialogue, though there are outside experts on the committees and I think in practice they sometimes call the shots.

It has proved incredibly important in practice that the commission have a permanent secretariat with staff paid by the government; ditto for the per diems for travel. It is also important that the meetings have protocol.

The rules of the Commission due not mention access to data. At least with respect to local government revenues and expenditures this is a moot point because the Main Statistical Office Publishes (and sells) a CD containing all revenue and expenditure data for local governments as well as data on various local economic indicators and social services. In a country of 40 million this solution has worked well for all concerned because there are enough buyers to keep the price low (about 100 euros a year, universities and individual researchers buy it as well as local governments and their associations). There is, however, a permanent Committee on Public Statistics, so disputes over other forms of data are continual.

There is remarkable little philosophy of dialogue in either the law or the statute. And the statute has much less procedural detail than expected.

## ANNEX 4: COMPARATIVE EVALUATION OF ALTERNATE INSTITUTIONAL ARRANGEMENTS

In some countries, the expert intergovernmental finance commissions were created and in some cases they are empowered to make legally binding judgments about intergovernmental transfer and grants systems. This is obviously an extreme extension of the idea contained in the paper - to minimize politicking and encourage decision making on the basis of rational third party expertise. Also, the performance of these merely expert commissions has been poor<sup>3</sup>. A central government agency model represents one of the most prevalent arrangements. A national legislature model represents the least common of these arrangements. The first arrangement rests decision making solely in the hands of a central government agency and the second arrangement involves a legislature not just in legislation but also in an executive decision making role. More interesting options for institutional arrangements are represented by intergovernmental forums and independent agency models. In the following analytical comparisons of these two options are made using the Nie framework. It must be noted at the outset that these two options are not necessarily exclusive choices and both arrangements can co-exist. When these arrangements co-exist incremental value added offered by the independent agency must be rigorously examined.

**Intergovernmental Forums:** An intergovernmental forum provides a framework for institutionalized but restricted political bargaining. Bargaining is restricted as the constitution and the legal framework usually define the limits to such bargaining. There is, however, strong peer pressure to strike a bargain. Thus intergovernmental forums are usually successful in defining an explicit political compact acceptable to all parties. As such a political compact cannot be easily reached when complex criteria are put on the table, this institutional model places great premium on simplicity and "rough justice" as opposed to complex but precise justice. Conflicting interests are represented at these forums. Unless the discussions of the forum are conducted in camera, political grandstanding may prevent political compromises.

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3. For an analysis of these expert commissions, and other forms of intergovernmental dialogue and mediation see Anwar Shah: A Framework for Evaluating Alternate Institutional Arrangements For Fiscal Equalization Transfers, World Bank April 2005.

Durability of such compromises is usually assured as all parties stand to lose from a deal that is unravelled. Blame shifting is also not possible as the members of the forum assume full responsibility for their decisions. The forum further enables participating governments representing competing interests and varying commitments on equalization, to reach a broader consensus.

Independent Agency (grants commission) model: An independent agency is usually established to seek an independent, professional, transparent and rigorous view of a complex task of developing recommendations on the determination of the pool, the allocation criteria and distribution of funds among recipient governments<sup>4</sup>. The presumption here is that if such a decision is divorced from politics, then resulting criteria and the associated distribution would serve the broader interests of the nation as well as its constituent units better. These theoretical advantages are rarely achieved in practice.

First, decisions on the standard of equalization e.g.. the minimum level of per capita fiscal capacity to which all jurisdictions are entitled to be brought up to, cannot and should not be divorced from politics. Secondly, such an institutional arrangement creates a number of agency problems as discussed below.

*Mission creep:* To secure its long term existence and enlarge its spheres of influence, an independent agency faces continuous imperatives reinterpreting its terms of reference to enlarge the scope of its activities. Such a mission creep goes unchecked as the politician do not want to be seen curtailing the search of such agencies for a holy grail - the ultimate formula for equitable distribution of federal funds.

*Incentives for complexity:* An independent agency faces powerful incentives to seek ever complex solutions to simplest questions. This is because complexity and associated expertise fuels demand in the external market for professionals serving these agencies. The greater the complexity of the formulae and associated calculations, greater is the premium placed by the market on professional possessing those skills. Interested parties' submissions make it politically imperative to accommodate ever growing complexity. Outside academic experts typically clamour for further complexity to achieve more precise justice. There is no escape from this vicious circle as part time or term employment of members of the commission limits the oversight provided by them. It takes sometimes for term members to grasp the complexity of the allocation rules and by the time they can form their own judgment on their relative merits, it is usually time for them to say good bye.

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<sup>4</sup>. These grants commissions usually operate in large, federal states (e.g. Australia, India) and that is an entirely different constitutional and political system of the NALAS member countries: [www.forumfed.org/en/federalism/by\\_country/index.php](http://www.forumfed.org/en/federalism/by_country/index.php). Shah also argues for forums, which can hammer out "explicit political compact



In any case, the staff would be resistant to any simplification and those recipient governments who benefit from the complexity and associated inequities of the system will likely block any reforms. Independent think tanks and researchers may even call for greater complexity to bring practice in conformity with the theory. In conclusion, constraining influences to keep the system simple and easily comprehensible are stunted by the very existence of an independent agency.

*Fire alarm oversight impractical and costly:* Citizen oversight of such independent agencies becomes infeasible for several reasons. First, more complex the distribution criteria suggested by the agency, the more difficult it is for individual citizens and civil society groups to make informed comments. Further conflicting representation by various citizen groups trying to secure local interests strengthens broad discretion granted to such agencies in the interest of a scientific a-political approach. Even "fire alarm" oversight sought by legislatures becomes too costly and impractical as unhappy constituents make conflicting demands on their representatives.

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