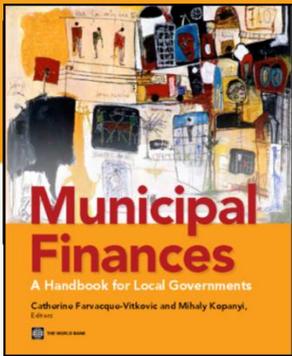




Municipal Finances

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Challenges and Opportunities in Developing Cities



Municipal Finances, A Handbook for Local Governmnts

- **Takes Sides:** the side of mayors and municipal managers, geared to respond pragmatically to daily issues faced by municipalities
- **Takes Positions:** reviews lessons learned on what works and what does not in managing cities and in financing infrastructure and services
- **Sets Standards:** supports a universal MF language
- **Provides cutting-edge knowledge:** shows instruments at work and guides their use and application
- **Calls for Action:** provides a framework for municipal finances self-assessment to help evaluate situations honestly and pragmatically, to draw conclusions, and move forward on the path of reforms

Chapter 1

Intergovernmental Finances in a Decentralized World

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Metropolitan Governance and Finances

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Achieving Greater Transparency and Accountability: Measuring Municipal Finances Performance and Paving a Path for Reforms



Intergovernmental Finances in a Decentralized World

- **Decentralization, the good and the bad:** Many countries have embarked on a decentralization process, bringing local governments closer to their constituents and thereby more responsive to their needs. But, in many ways, this process remains incomplete as devolution of functions has not been supported by adequate devolution of resources. No match between transfer of technical responsibilities and transfer of financial resources.
- **Transfer formulas, Equity and Performance issues:** Important to get it right and to watch for too much leniency: introducing incentive mechanisms is not always the best way to incentivize collection of local own-source revenues and may contribute to increased dependency of LGs on transfers. Performance grants such as municipal contracts have been shown to be effective in fostering good intergovernmental partnerships.
- **The intergovernmental finance relations generate the governance framework, the playing field,** thereby setting them right is of upper most importance for managing revenues, expenditures, assets, and external resources and for measuring performance.



Metropolitan Governance and Finance

Metropolitan areas are becoming the new 'normal'

- More than 3.5 billion people live in cities
- 27 megacities with more than 10 million
- 500 metropolitan areas of more than 1 million

Many governance models: Often too many actors and no clear distribution of tasks and functions (cooperation, regional authority, metro government, consolidated LGs); Choice of models influenced by scale economy, access by residents to their governments, and politics

Financing arrangements: (tax sharing, cost sharing, and coordination of revenue mobilization). Depends on clarity of functions.

Table B2.11.1 Transfers to Local Governments in Dar es Salaam Metro Region 2009/10 (T Sh millions)

Municipal Council (MC) and City Council (CC)	Ilala MC	Kinondoni MC	Temeke MC	Dar es Salaam CC	Metro region
Education grant	20,852	31,062	19,733	6	71,654
Health grant	10,859	7,106	5,998	273	24,237
Other sector grants	740	618	299	241	1,898
General purpose grants	6,621	2,923	2,483	2,157	14,184
Total recurrent grants	39,073	41,709	28,514	2,677	111,973
Subventions	1,506	2,838	4,196	0	8,540
Recurrent transfers	40,578	44,547	32,710	2,677	120,512
Development grant	6,514	5,368	8,513	10,075	30,471
Total transfers	47,092	49,916	41,223	12,753	150,983

Source: www.logintanzania.net/report4b.asp.





Municipal Financial Management

What gets Measured gets Managed !!

- Municipalities across the world are faced with some tough questions: *How to meet a growing list of needs with limited resources? How to make sure that spending of public resources are done in a transparent and accountable manner? How to ensure value-for-money in each rupee, dollar or dinar spent?*
- **Understanding the basics of Financial Management** helps the municipality to: (1) keep track of its revenues, expenditures, assets, and liabilities; (2) manage its revenues and expenditures to finance service delivery in a sustainable manner; and (3) ensure transparency in its financial affairs and be accountable to its stakeholders.
- Though financial management is a multifaceted subject, what is important is to see the “big picture” (enabling municipalities to be financial sustainable by piecing together the various financial management processes), which is what the Handbook aims to achieve.
- No Wheel of Fortune ! Budgeting, Accounting, Financial Reporting, and Auditing are key building blocks of FM.

	<i>Unrestricted</i>
<i>Revenues</i>	
Earned revenue	17,200
Contributions	10,250
Program revenues	
Other sources	3,400
Interest and dividend income	1,550
Grants	93,200
Loans and advances	60,300
Released from restricted funds	
Total unrestricted revenue	185,900
<i>Expenses</i>	
Program expense	22,700
Development expense	27,000
Management and general	29,300
Loans and advances	65,400
Other expenses or fund uses	27,000
Total operating expenses	171,400
Change in fund balance	14,500
Fund balance, beginning of period	26,000
Fund balance, end of period (surplus or deficit)	40,500





Managing Local Revenues

- **2008 Financial crisis: Wake up call for Local Governments:**
 - Showed vulnerability and exposure of local finances (impact on local of ripples in global systems)
 - Loss of own revenues: Fall of land based revenues led to 40 to 50 % drop in own revenues
 - Greater dependency on transfers and grants
- **LGs must do more with less.** In many countries, local revenues amount to less than 10% of public revenues with little willingness on the part of many central governments to empower LGs with additional sources of revenues or to pay much attention to the administration and collection of municipal fiscal revenues
- **Be creative, sort out the “Good” and the “Bad” taxes; Tap the Untapped**

Own Resources

User charges
Property taxes
Business tax
Other taxes (land value capture)

- Property tax: a good tax but, requires level of maturity. Represents 35 to 40% of local revenues in US, GB, Canada, Australia, France but only 3 to 4% in developing cities.

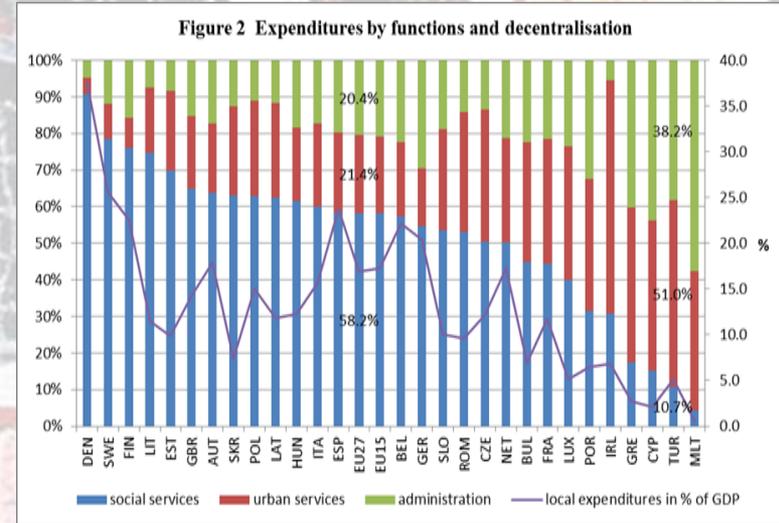
- **Revenue collection is key.** Municipalities should explore alternative ways to capture a tax base and fees billing through instruments, such as Street Addressing, which provides an opportunity to set up a spatially referenced database and street index, while connecting with fiscal registers.





Managing Local Expenditures

- **Urban infrastructure needs: US\$120 billion per year** (huge gap between needs and resources).
- **Prioritization of expenditures is key.**
- **Difficult to do for many reasons: Frontier entry points**
 - Expenditures tracking is commonly done at the central government level- Rare at the local government level.
 - Capital Investments Programming: Mandatory but many local governments do not know how to do it. Need Intermediary steps (urban needs assessments/audits)
 - Disconnect between Planning departments, Utilities and Budgeting office
 - A project-based approach for the city rather than a Program/vision for the city
 - Many competing projects and many constituents to please: Politics
- **Essential to connect Investments Planning with Budget:**
 - Tight and daily control of operating expenditures (salaries and hiring staff), competitive procuring bulk products and services (fuel, energy, maintenance, banking);
 - Competitive procurement in designing and implementing capital investment projects; and forceful contract management. Local governments in the developing world often try to avoid using competitive procurement. Practice makes it easier.



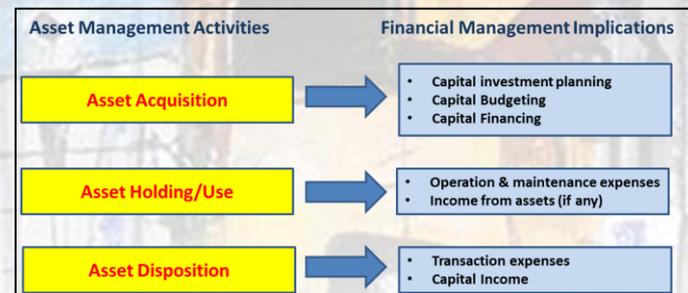


Managing Local Assets

- **Municipal governments across the world control large portfolios of physical assets** (land, buildings, infrastructure, vehicles, and equipment), which is the lion share of local public wealth. Thus, good management of assets is critical for quality and sustainability of local services (e.g. roads, water, schools); for local economic development (e.g. land for private production/business); and citizens' quality of life.
- **Municipal governments, often, do not know what they own, where assets are located, and what is their value.**
- **Best practice include:**
 - Inventorying assets;
 - Using transparent procedures for allocating assets for private use;
 - Assessing market value of assets for decision making;
 - Establishing a depreciation fund for financing asset replacement;
 - Monitoring key performance indicators (e.g. costs and revenues);
 - Planning operating and maintenance expenses ahead when acquiring new capital assets.
- **Municipal staff need to gain expertise** and pay attention to regulatory framework, procedures and analytic tools, and real estate markets.



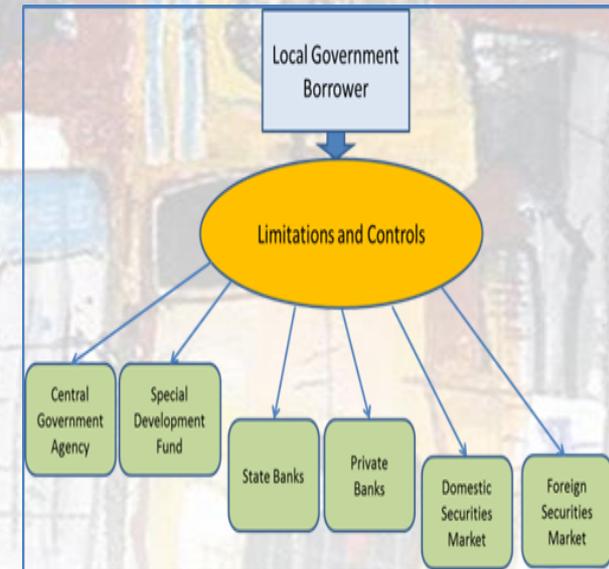
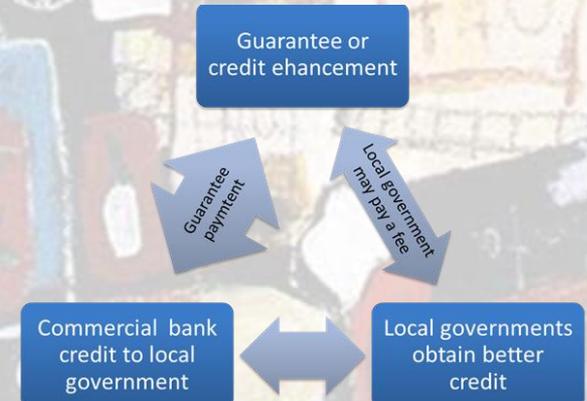
Enforcing Right of Way in Kathmandu 2012





Managing External Resources

- **Local governments investment needs are often much greater than what their annual operating surplus can finance.** Thus, they need external funding:
 - borrowing,
 - bond issuance,
 - private-public partnerships (PPP),
 - Grants, donor aid or philanthropic aid.
- **Again Aftermath of 2008 has shown vulnerability of LGs:**
 - Credit for what?: The “Good” and the “Bad” project
 - Creditworthiness analysis and credit rating are valuable tools to demonstrate that the municipality has the capacity to re-pay a loan or bond on time. But, for this to happen, prudent use of external resources is crucial since it may jeopardize the fiscal situation of a city in years ahead.
 - Many municipalities are not credit worthy right now and should start with unglamorous footwork of getting their books in order.

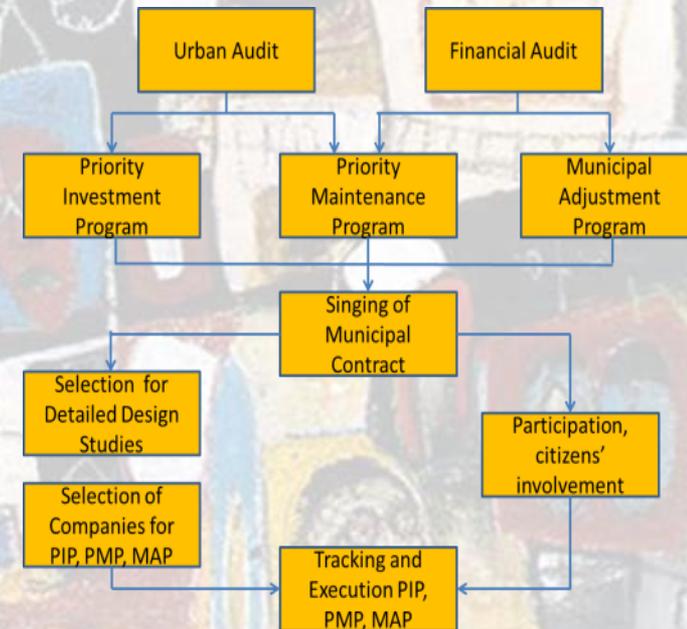




Achieving Greater Transparency and Accountability: When Urban Meet SocialMeasuring Municipal Finances and beyond

Underpinning quest: Are we doing the right things? Are we doing things right?

- **Canada/US:** Long experience of P.M focusing on workload and outcome ratios. Not so much on efficiency and effectiveness of municipality. One key lesson: COMMUNICATION of performance indicators to citizens.
- **Europe:** To measure performance of municipality through service delivery effort and cost efficiency was not part of the culture. However, financial ratios and financial position of municipalities are under tight control of the mayor, central government and European commission. They are published annually. Very keen involvement of citizens in environment, quality and coverage of services.
- **Developing cities:** New concept for many cities but very much at the heart of change management reforms. Three keys to the lock:
 - Extent of decentralization
 - Extent of involvement of financial partners
 - State of data
- **Social Accountability:** Magic bullet or just Hype? - A flurry of Social Accountability tools (citizen monitoring, score cards, public complaint and grievance, Third party monitoring, Participatory budgeting); -Raise a lot of expectations on the demand side but does not provide answers on the supply side; - Essential that LGs be prepared to present and articulate their financial position and be accountable for the use of public funds.



- **Typically, three types of reporting:**
 - State oversight and monitoring
 - Reporting to financial partners
 - Reporting to citizens

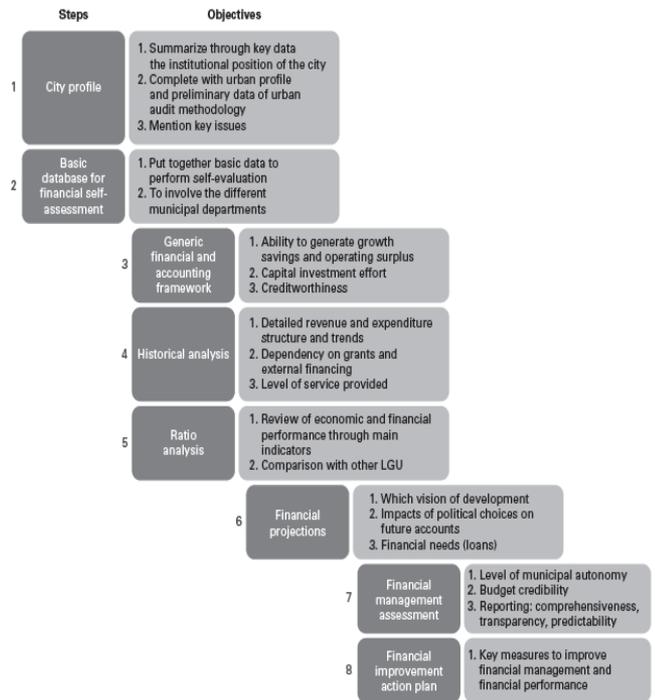
With these objectives in mind, Municipal Finances Self-Assessment (MFSA) presents an opportunity to connect the dots.



Achieving Greater Transparency and Accountability and Performance Measurement (cont.) : Municipal Finances Self-Assessment (MFSA)

- To promote financial self-assessment at the municipal level as part of the **change management process of local public administration** (empowerment)
- To encourage **technical and financial departments to work together** on strategic and capital investment planning anchored in financial realism (prioritization)
- To **monitor and act on a set of key actions** aiming at improving mobilization of local resources, rationalizing public expenditures, and improving financial management practices (reform)
- To help LGs better **communicate** their financial situation to **central governments** (negotiation platform for transfers and credit guarantees) (accountability)
- To help LGS better **communicate with their citizens** (**transparency and accountability on use of public funds**)
- To help LGs better package their investment needs and financial absorptive capacity with financial partners (banks, donors)
- To share common indicators/benchmarks with other municipalities nationally and internationally

Figure 8.7 Modules of the Municipal Finances Self-Assessment



<http://siteresources.worldbank.org/EXTURBANDEVELOPMENT/Resources/MFSA-Template.xlsx>



THANK YOU !!!