

Local Government Finances, Planning, Land and Investments Programming in SEE

Experiences from Local Governments Self-Assessment Tools

Catherine Farvacque-Vitkovic

The World Bank

Challenges

Challenges: Municipal Finances at a Glance

- **Decentralization in SEE: Still work in progress**
 - All SEE countries have embarked in decentralization
 - Soul searching for the best arrangements (Albania Territorial Reforms)
 - Disconnect between revenues assignments and expenditures assignments: LGs are asked to do more with less
- **On the revenue side:**
 - Local budgets average 3 to 8 % of GDP and account for 12 to 27% of total public revenues (low)
 - As in the rest of Europe, LGs derive majority of revenues from general or unconditional grants, earmarked or conditional grants and shared taxes (50%)
 - Conditional grants are the most utilized (financial dependence issue) while unconditional grants are underutilized (equalization issue)
 - Own source revenues account for 30 to 40 % of total local revenues.
 - Strongly linked to real estate market and disproportionately concentrated in capital cities
 - A large share of own revenues comes from land based instruments (real estate transactions, land development fees, construction permits): volatility/vulnerability as shown during the 2008 financial crisis
 - Among own revenues, the Property Tax still produces low revenues (equal to less than 1% of GDP or 7% of current revenues) Does not come close to EU average
- **On the expenditure side:**
 - LGs are spending higher proportions of their income on investments than their counterparts in the EU, despite receiving significantly lower shares of total public revenue
 - Investment spending is below EU average
 - Local governments are not major actors in public investments (1/3 of all public investments are happening at the local level compared to 67% across EU countries)
 - Debt service burden: 6 % of current revenues (mainly in capital cities)

- **LG Rev: From 3 % to 8 % of GDP and 12 % to 27 % of public revenues**
- **Contribution to National Inv. Effort: from 25 % to 30 % of local budget**

Key findings

| in million EUR 2011 | GDP | Public Revenue | Local Gov. Revenue | Local Gov Rev/GDP | Local Gov Rev/State Gov. Revenue | Local capital investment exp. | % total local Gov. exp. |
|--------------------------------|----------------|---------------------------|-------------------------------|------------------------------|---|--|--|
| Albania | 9 535 | 2 384 | 296 | 3,1% | 12,4% | 98 | 33% |
| BIH | 17 434 | 8 099 | 991 | 5,7% | 12,2% | 185 | 28% |
| Serbia | 30 155 | 12 364 | 1 689 | 5,6% | 13,7% | 95 | 29% |
| Montenegro | 3 300 | 1 221 | 191 | 5,8% | 15,7% | 490 | 29% |
| Macedonia | 7 484 | 2 147 | 434 | 5,8% | 20,2% | 50 | 26% |
| Croatia | 48 010 | 17 668 | 2 977 | 6,2% | 16,8% | 109 | 25% |
| Kosovo | 3 721 | 1 047 | 283 | 7,6% | 27,0% | 625 | 21% |
| Total/average | 119 639 | 44 929 | 6 861 | 6% | 15% | 1 661 | 26% |

Source: NALAS and IMF

Challenges : City Planning and Land at a glance

❑ Growing urbanization and increasing demand for urban services and infrastructure

- Fast growth of capital cities: Skopje 32%, Tirana 28%, Podgorica 10%
- Loss of public spaces and incompatible land uses



❑ Problematic sustainability of spatial patterns

- Excessive land consumption via urban sprawl
- Urban sprawl significantly increases infrastructure costs and complicates delivery of municipal services

❑ Systemic risk of eroding the “rule of law” society

- 15 years of no regulations
- Massive informal and illegal construction by the private sector:
Estimated share % of illegal housing units in the total housing stock (NALAS Study, 2011) *Croatia – 25% , Montenegro – 30% , Serbia – 40% , Albania – 40%*
- The C word.....Corruption and lack of governance
- A legacy of failed regularization programs

Land registration: work in progress. Cadastres: not the Panacea

Challenges : City Planning and Land at a glance

The transition from state-owned land to municipal owned land and the 15 years of no regulations during the 90's have led to an explosion of private construction by individuals and firms who ignore existing regulations. The result is sprawl and unsustainable development

Urban planning remains top-down, defined by central government laws and regulations and ignoring/underestimating implementation costs and local specifics

Smaller LGs don not have capacity and funding to produce all required planning documents and ensure compliance

Urban planners continue to believe that they are sole guarantors of the public interest, while missing opportunities to be part of the decision process and to connect the dots with budget and investment programming

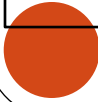
“Big picture” problems of delayed modernization

Public and private sector urban planners benefit from the current system of overregulation because they are the only ones who know how to work it. They have limited incentives for radical change

Urban planning is often disconnected from management of municipal land and infrastructure planning and finance

Public participation in spatial / urban planning continues to be passive, ex – post or limited to “legitimizing” overly detailed plans

Social trust is low, limiting cooperation between and across citizens and their governing institutions, including planners. Lack of trust in government produces low tax compliance and a vicious circle of underperformance in service delivery



Challenges : Investments Programming

- **Multiannual planning** of capital investment expenditures (CIP) started from budget year 2013 in some SEE countries (Serbia)
- **CIP** for the next three fiscal years is an integral part of the Decision on Budget Plan
- **However**, the link between CIP and Budget Plan is not established in all LGs and multi-annual budgeting and planning remains a challenge:
 - Cities lack mature projects to populate sound investments programs
 - Local government revenues are still unpredictable and therefore programming remains problematic
 - Projects are subject to political mandates (lack of continuity and lack of strategic planning)
- Capital investment spending: **40 %** of total LGU expenditures (high), but mainly in Belgrade and capital cities : 70 % Podgorica, 44 % Belgrade, 40 % Tirana. Different story elsewhere
- **50 % of capital investment** financed by operating surplus, but 25 % of the cities have operating budget in deficit.
- There has been a drastic increase in operating expenditures (goods and services) versus capital

opportunities

UPP 1 : The unlikely journey: Urban Partnership Program (joint Austria-World Bank Program)

- **Offering 1:** A platform for discussion on topics of common interest: The City to City Dialogues

December 2011 - Budapest (Hungary): Improving Municipal revenues

May 2012 - Mavrovo (Macedonia): Modernizing Local Public Expenditures Management

June 2012 - Tirana, Albania: Modernizing Legal and Regulatory Framework for Urban Planning in SEE

November 2012 - Budva, Montenegro: Guided Urban Development: Reconciling public and private Interests

January 2013 - Vienna, Austria: Towards Greater Transparency and Accountability: A Mayors Dialogue

June 2013 - Dubrovnik, Croatia: From Local Government Self-Assessment to Implementation

December 2013 - Skopje, Macedonia: From MFSA to Municipal Investment Programming: The Urban Audit

- **Offering 2:** Application and customization of two self-assessments:
 - **Municipal Finances Self-Assessment (MFSA)**
 - **Urban Audit (UA)**

For Local Governments , by Local Governments....

MFSA Approach

MFSA methodology

- was developed by the World Bank
- was customized by international and local experts to some regional context (most recent: South East Europe)
(common understanding of the terminology and clarification of budget items on revenue and expenditure sides)

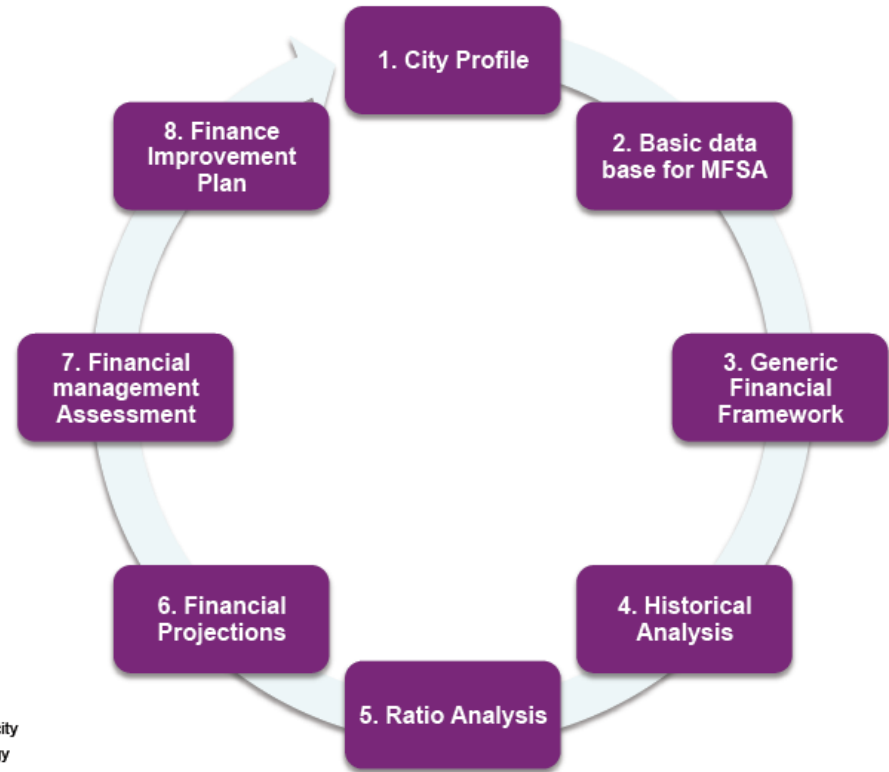
MFSA template

- has been developed and validated by all stakeholders
- includes eight steps organized in four complementary modules

MFSA objectives

- **Accountability** - to promote financial self-assessment as part of the change management process of local administration
- **Transparency** - to help LG share information with other LGs, and to inform central government, LG Association and citizens about their situation (open data)
- **Prioritization** - to encourage municipal financial and technical departments (asset management, urban planning, strategic planning, mayor's office) to work together on strategic and capital investment planning anchored in financial realism
- **Efficiency** - to monitor and act on a set of key actions aiming at improving mobilization of local resources, rationalization public expenditures and improving financial management practices
- **Access to external funding** - to share common methodologies and international indicators and facilitate negotiations with banking institutions and external donors

MFSA methodology and cycle



Legend

| | |
|------------------------------------|---|
| 1. City Profile | <ul style="list-style-type: none"> Summarize through key data the institutional position of the city Complete with preliminary data from Urban Audit methodology List the main urban management & development challenges |
| 2. Basic database for MFSA | <ul style="list-style-type: none"> Put together basic data to perform self-evaluation Involve the different municipal departments |
| 3. Generic Financial Framework | <ul style="list-style-type: none"> Assess the ability to generate gross saving and operating surplus Calculate capital investment effort |
| 4. Historical Analysis | <ul style="list-style-type: none"> Conduct a detailed analysis of revenues and expenditures composition and trends Assess the level of financial autonomy Assess the level of service provided |
| 5. Ratio Analysis | <ul style="list-style-type: none"> Review the economic & financial performance through main indicators Compare with benchmarks |
| 6. Financial Projections | <ul style="list-style-type: none"> Identify budgetary applications of the policy decisions (ex: investment plan, recurrent costs, tax pressure, etc.) Fix the financing needs for investment Identify the expected changes in existing regulation with impact on the city budget |
| 7. Financial Management Assessment | <ul style="list-style-type: none"> Review briefly budget credibility (Based on PEFA methodology) And quality of the reporting: Comprehensiveness, transparency, predictability |
| 8. Finance Improvement Plan | <ul style="list-style-type: none"> List the key measures to adopt to improve financial management and financial performance |

MFSA Outcomes in South East Europe

UPP1: Cohort 1

- **25 Cities/Municipalities of the Region actively contributed to the experience (ranging from small municipalities to capital cities)**
- **15 Cities/Municipalities successfully prepared Financial Improvement Plan based on MFSA and 13 cities presented their data profiles in MFSA brochure**

UPP2: Cohort 2

- **More municipalities are ready to engage (see list)**
- **Drill down the implementation of the Improvement Action Plans and Strengthen link with investments (Urban Audit)**
- **Lay the foundations for Local to Central dialogue**

Urban Audit

Objectives

- To identify key investment needs in a rational and consultative way
 - To select priority investments depending on available resources (MFSA)
-

UA Preparation

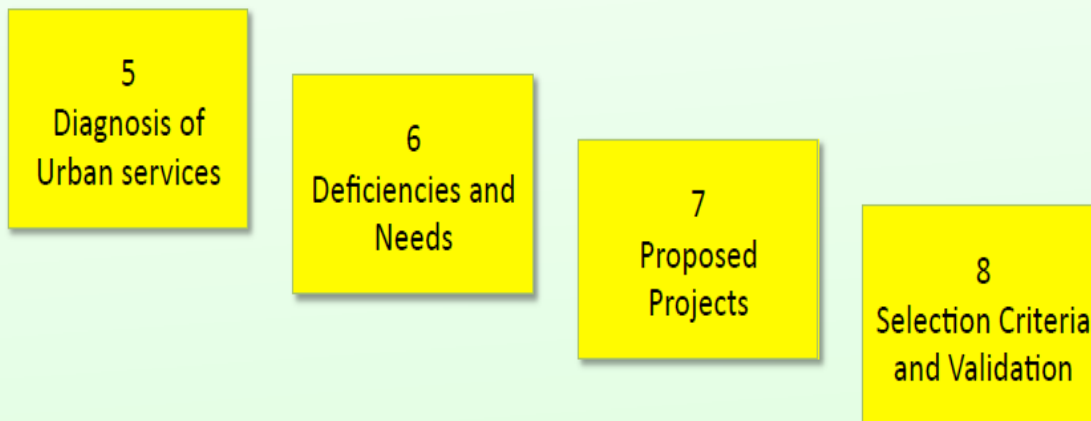
- The UA is typically conducted in parallel and in concertation with a MFSA and enables the Municipality to match its investments needs with its capacity to finance and maintain its existing and projected infrastructure and services.
- The UA is produced **by the municipal services**, (possibly with the support of a consultant). It is prepared for a period of 5 years and is annually updated.
- The UA is **based on the available data**, that municipal services can collect and preserve. (Its implementation can not wait for the completion of a database or GIS.)

Urban Audit : Framework

I. Overview of the situation

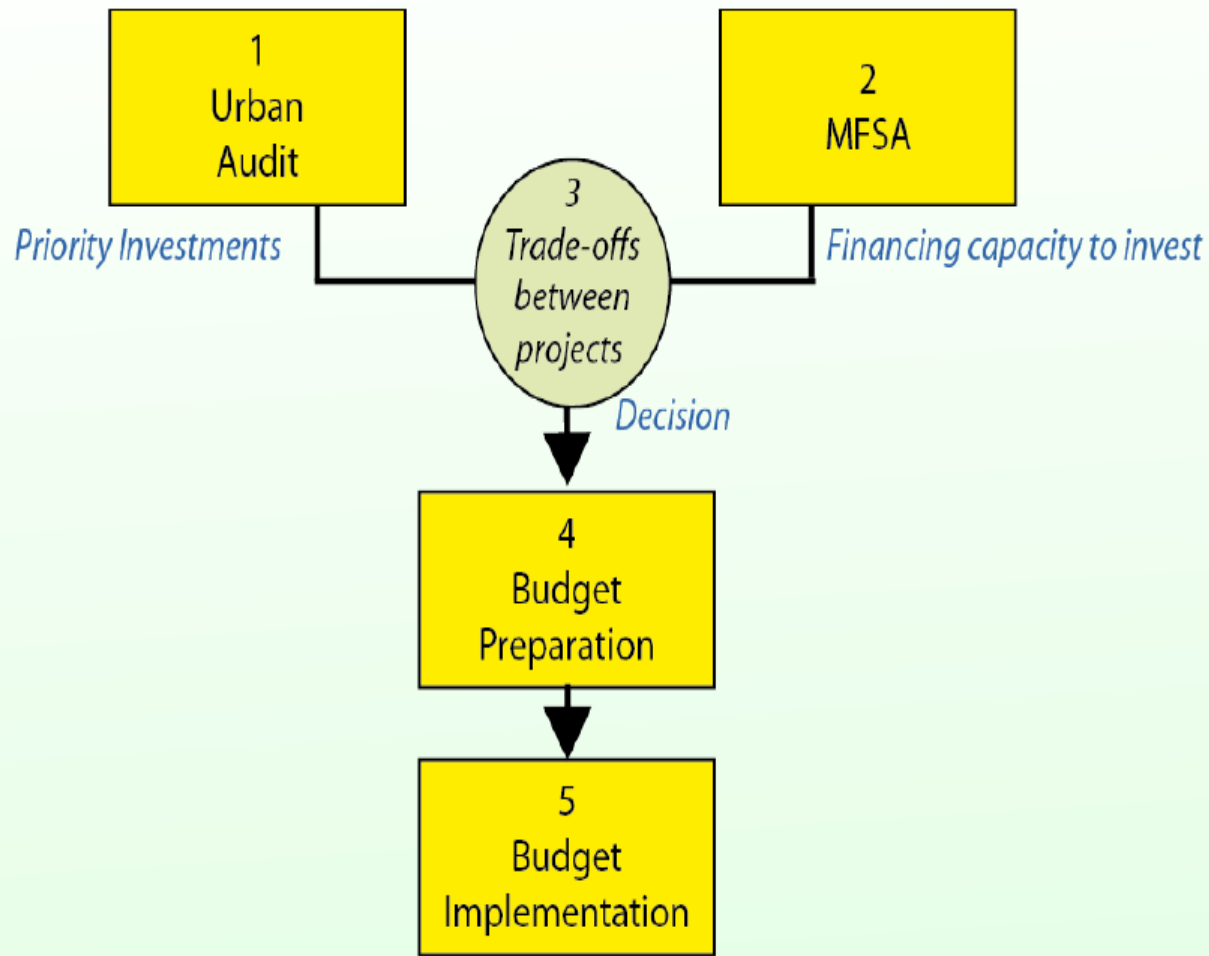


II. Diagnosis of urban services and projects identification



MFSA and UA: The Power of Integration

General framework



Linking MFSA and Urban Audit:

Matching financial capacity and CIP, the case of Belgrade

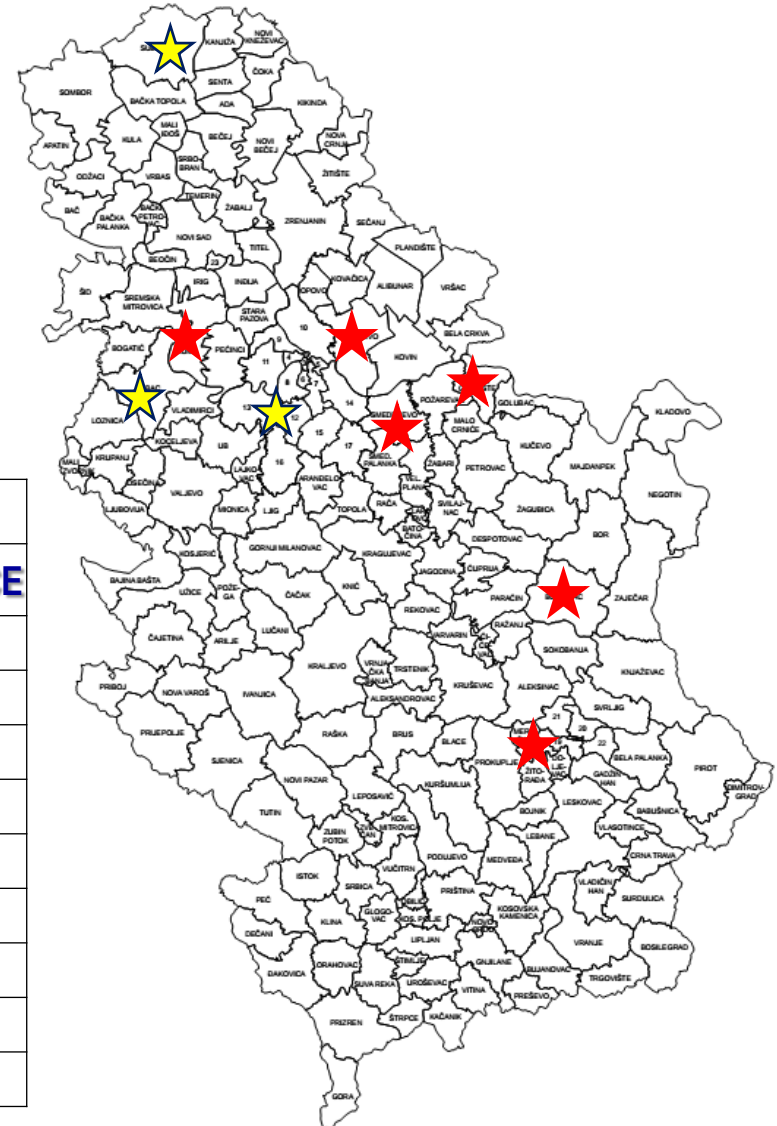


REPUBLIC OF SERBIA

URBAN PARTNERSHIP PROGRAM II

Urban Partnership Program offers the tools and procedures for:

- ✓ Municipal Finances Self-Assessment (MFSA)
- ✓ Urban Audit (UA)
- ✓ Integrity Building (AC/IB)
- ✓ Social Sustainability Assessment (SSCE)

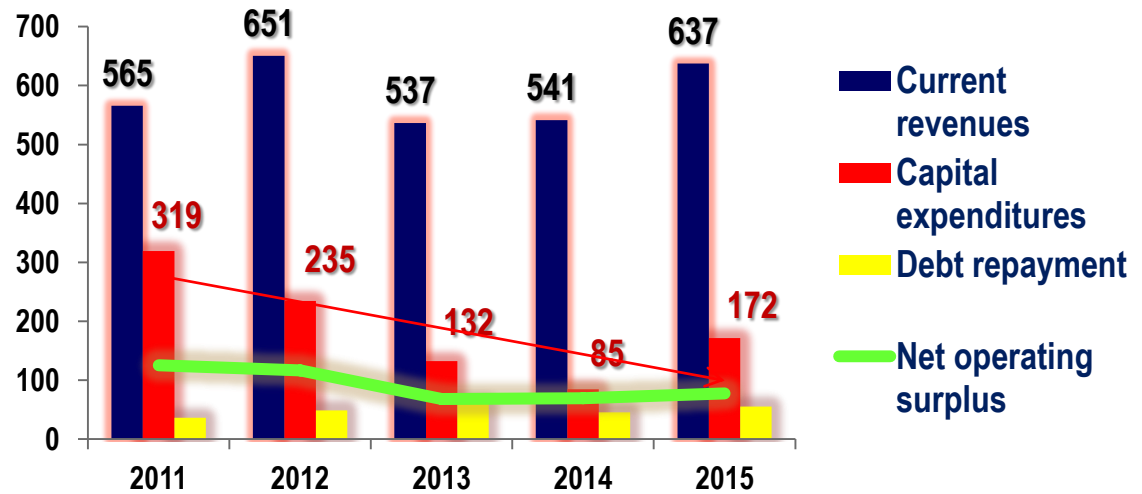


| City/Municipality as a participant of UPP II | Population | Implementation of | | | |
|--|------------|-------------------|----|-------|------|
| | | MFSA | UA | AC/IB | SSCE |
| 1. BEOGRAD | 1,576,124 | ✓ | | | |
| 2. SUBOTICA | 148,401 | ✓ | | | |
| 3. ŠABAC | 126,000 | ✓ | | | |
| 4. NIŠ | 250,518 | ✓ | | | |
| 5. PANČEVO | 123,414 | ✓ | ✓ | ✓ | ✓ |
| 6. SMEDEREVO | 114,613 | ✓ | ✓ | | |
| 7. RUMA | 54,141 | ✓ | ✓ | ✓ | ✓ |
| 8. VELIKO GRADIŠTE | 17,559 | ✓ | ✓ | | |
| 9. BOLJEVAC | 12,865 | ✓ | ✓ | | |

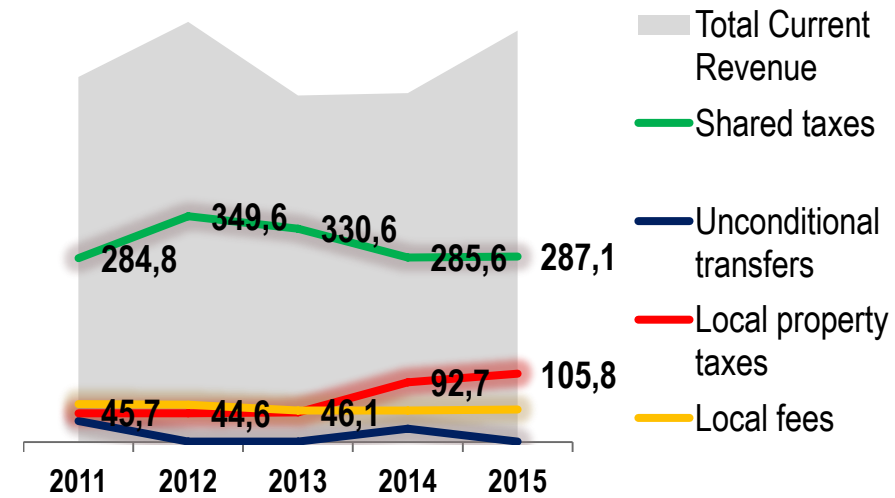


CITY OF BELGRADE

Findings: Financial Situation 2011 -2015 (mil EUR)



| | |
|----------------|---|
| Inhabitants | 1,774,000 |
| Area | 322,268 ha |
| Employees | 4,021 administration, 8,322 pre-schools |
| Founder | 21 public enterprises (11 PUC) |
| Budget | 699.4 mil EUR (2015) |
| Revenue/capita | 356 EUR |
| Debt | 404.4 mil EUR |





CITY OF BELGRADE

A : Financial Ratio Analysis 2011 - 2015

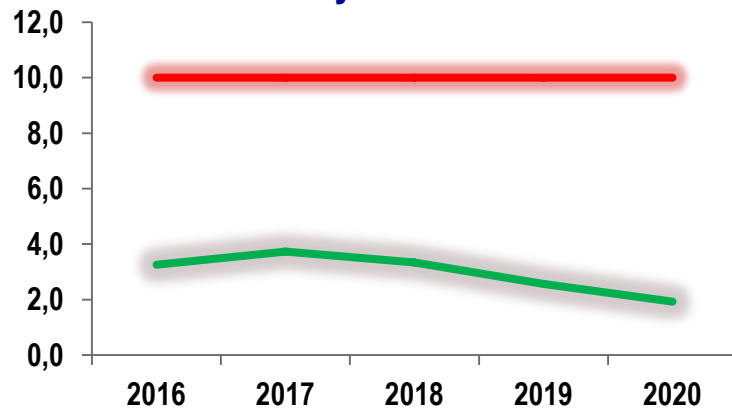
| Criteria / Indicator | Benchmark | 2011 | 2012 | 2013 | 2014 | 2015 |
|---|-----------|-------|-------|-------|-------|-------|
| 1. Credit worthiness | | | | | | |
| Operating savings before interests / Current revenue | > 0.3 | 0.29 | 0.26 | 0.24 | 0.21 | 0.21 |
| Net operating surplus (margin) / Current actual revenue | > 0.2 | 0.22 | 0.18 | 0.13 | 0.13 | 0.12 |
| 2. Indebtedness | | | | | | |
| Debt outstanding / Operating surplus | < 10 god | 2.4 | 2.7 | 3.8 | 4.3 | 3.1 |
| Debt service / Total current revenue | < 10 % | 6.4% | 7.5% | 11.2% | 8.4% | 8.7% |
| 3. Fiscal autonomy | | | | | | |
| Own taxes & unconditional grants / Current actual revenue | > 80 % | 74.7% | 69.6% | 79.7% | 82.9% | 69.8% |
| 4. Capital investment effort | | | | | | |
| Capital investment expenditure / Current actual revenue | > 40 % | 56.4% | 36.1% | 24.6% | 15.6% | 27.0% |
| 5. Level of service | | | | | | |
| Maintenance works expenditure / Operating expenditures | > 30 % | 8.0% | 5.3% | 6.1% | 5.9% | 5.8% |
| 6. Others | | | | | | |
| Salaries / Operating actual expense | > 40 % | 18% | 16% | 20% | 23% | 17% |
| Arrears amount / net cash end of the year | > 1 | 0.4 | 1.8 | 1.2 | 0.5 | 0.4 |
| Total financial resources / Total financial obligations | 1.02 | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 |



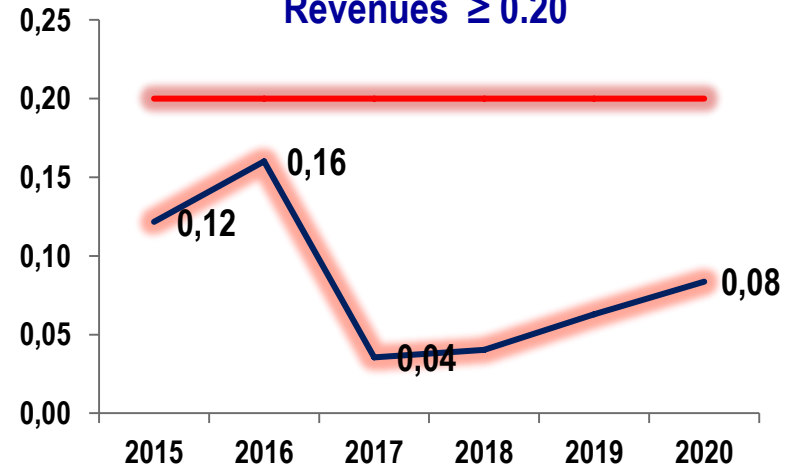
CITY OF BELGRADE

Findings: Financial Projections 2016 - 2020

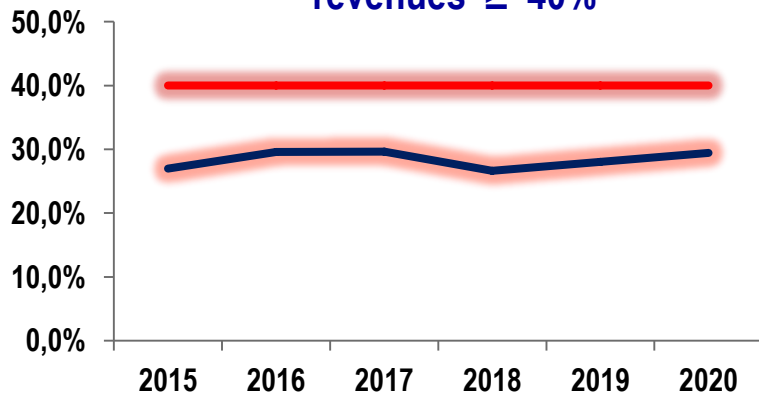
Debt outstanding / Operating surplus < 10 years



Net Operating Surplus / Current Revenues ≥ 0.20



Capital investment expenditures / Current revenues $\geq 40\%$



Threat:

- Reduced capital investment effort in the next period
- Decline in the quality of public infrastructure and services

Solution:

- Revenue generation and cutting the costs
- Rational use of available resources
- Attracting private equity to finance public investments

Summary of CIP

of the City of Belgrade for three budget years

Plan of Capital Expenditures of the City of Belgrade for 2013, 2014 and 2015

(million RSD)

| <u>Direct budget beneficiary responsible for the projects</u> | | <u>2013</u> | <u>2014</u> | <u>2014</u> |
|---|---|---------------|---------------|---------------|
| 1 | Secretariat for Finance | 14,826 | 12,952 | 13,279 |
| 2 | Secretariat for Utility and Housing | 591 | 2,935 | 920 |
| 3 | Secretariat for Transport | 3,889 | 5,085 | 5,615 |
| 4 | Secretariat for Environmental Protection | 64 | 347 | 390 |
| 5 | Secretariat for Culture | 87 | 25 | 20 |
| 6 | Secretariat for Education and Children Care | 30 | 225 | 179 |
| 7 | Secretariat for Sport | 4 | 0 | 0 |
| 8 | Secretariat for Health | 224 | 40 | 0 |
| 9 | Secretariat for Social Care | 159 | 0 | 0 |
| 10 | Agency for Investments & Housing | 10,407 | 13,512 | 13,809 |
| 11 | Agency for Public Procurement | 134 | 55 | 0 |
| Total Capital Expenditures | | 30,415 | 35,176 | 34,213 |

Main projects of the City of Belgrade over the 3 years

| | | (million RSD) | | | |
|--|--|---------------|---------------|---------------|-------------|
| | | 2013 | 2014 | 2014 | Structure |
| | Construction of the main roads | 9,681 | 7,103 | 7,367 | 24% |
| | Roads with infrastructure | 2,708 | 4,251 | 4,209 | 11% |
| | Repair and maintenance of streets | 3,889 | 5,085 | 5,615 | 15% |
| | Sewerage infrastructure | 2,092 | 1,480 | 1,511 | 5% |
| | Purchase of trams | 4,166 | 0 | 0 | 4% |
| | Other capital projects | 7,879 | 17,258 | 15,511 | 41% |
| | Total | 30,415 | 35,176 | 34,213 | 100% |
| | | | | | |

Sustainability of the CIP financing of Belgrade (MFSA)

| Items | 2013 | 2014 | 2015 |
|--------------------------------------|------------------|------------------|------------------|
| | Plan | Projection | Projection |
| + TOTAL CURRENT REVENUE | 70,718.4 | 74,199.3 | 77,792.0 |
| - TOTAL OPERATING EXPENDITURE | 53,521.0 | 52,713.5 | 52,081.1 |
| = GROSS OPERATING SAVING | 17,197.3 | 21,485.8 | 25,710.9 |
| - DEBT SERVICE | 6,960.5 | 6,949.3 | 7,142.4 |
| = NET SAVING | 12,582.3 | 16,917.8 | 20,793.6 |
| - CAPITAL EXPENDITURE | 33,201.8 | 35,176.5 | 34,212.6 |
| = BALANCE AFTER INVESTMENT | -20,619.5 | -18,258.7 | -13,419.0 |
| INVESTMENT FINANCING | 20,619.5 | 12,088.9 | 9,528.2 |
| Capital transfers | 1,526.2 | 0.0 | 0.0 |
| Investment grants | 130.0 | 200.0 | 200.0 |
| Own capital revenues | 10,613.3 | 8,718.9 | 9,328.2 |
| - Land development & lease fee | 8,190.0 | 8,718.9 | 9,328.2 |
| - Proceeds from non-financial assets | 2,423.3 | 0.0 | 0.0 |
| Loan | 8,350.0 | 3,170.0 | 0.0 |
| OVERALL CLOSING BALANCE | 0.0 | -6,169.7 | -3,890.8 |

UPP 2 : The Journey Forward

- Scale up of work program on Self-Assessments:
 - Drill down on implementation of Action Plans under Cohort 1
 - Enlarge the number of participating cities/municipalities (over 60 across SEE)
- Strengthen the dialogue between central governments and local governments: We need two to tango..
- Engage in policy discussions on fundamental issues/questions
- Strengthen partnerships and collaboration: NALAS, Association of Local Governments: Dashboard, Fiscal Decentralization Report, Institutionalization of Self-Assessment tools.

MFSA and UA in SEE

| | MFSA | UA |
|------------------------|--|---|
| Albania | Tirana (I), Shkodra (I), Kamza (I), Berat (II), Elbasan (II), Kucove (II), Fier (II), Lushnje (II) | Berat (II), Elbasan (II), Kucove (II), Fier (II), Lushnje (II) |
| Bosnia and Herzegovina | Prijedor (I), Banja Luka (I), Novo Sarajevo (City of Sarajevo) (I), Zepce (II), Bugojno (II), Tesanj (II), Orasje (II), Zivinice (II), Odzak (II) | |
| Croatia | Rijeka (I), Crikvenica (I), Krizevci (II), Zapresic (II), Lubin (II), Pregrada (II), Jastrepsko (II) | |
| Kosovo | Pristina (II), Gjakova (II), Peja (II), Gracanica (II), Istog (II) | |
| Macedonia | Gazi Baba (Skopje) (I), Strumica (I), Gostivar (I), Kisela Voda (Skopje) (II), City of Skopje (II), Bosilovo (II), Kocani (II), Kavadarci (II), Debar (II), Kriva Palanka (II) | Gazi Baba (Skopje) (I), Strumica (I), Gostivar (I), Vinica (II), Kumanovo (II), Kocani (II), Kavadarci (II), Debar (II), Kriva Palanka (II) |
| Montenegro | Podgorica (I), Bar (I), Budva (I), Niksic (I), Bijelo Polje (I), Cetinje (I), Kotor (II), Kolašin (II), Mojkovac (II), Žabljak (II) | |
| Serbia | Belgrade (I), Subotica (I), Sabac (I), Nis (II), Pancevo (II), Ruma (II), Veliko Gradiste (II), Bosilegrad (II), Boljevac (II) | |

Thank you

