

A Blueprint for Municipal Finance in India



We need to locate Municipal Finance in the overall context of governance of India's cities

1. Municipal Corporations are **glorified service providers, not the 3rd tier of government** as envisaged by the Constitution; Cities are tightly controlled by States, **legitimate political leadership at a city-level is absent**
2. **Municipalities in India are weak institutions**
 - Handle only few functions, with the State covering several critical functions, services
 - Staffing is a critical and weak link; both quantity and quality
 - Finances are scarce, most MCs are not financially self-sufficient; exacerbated by absence of robust performance measurement and audit/accountability mechanisms
 - Opacity in finances and operations, and lack of accountability for performance and service levels; absence of citizen participation

Pillars of Municipal Finance Reforms

What's objective of municipal finance reforms?

1. Financial sustainability i.e. municipalities have adequate finances to deliver citizen outcomes and
2. Financial accountability i.e. municipalities are able to provide assurance on their sound financial position and performance

What are the components of municipal finance reforms?

1. Fiscal Decentralisation
2. Revenue Optimisation
3. Fiscal Responsibility and Budget Management
4. Institutional Capacities
5. Transparency and Citizen participation

Issues, Solutions and Pathways

1. Fiscal Decentralisation

Issues

- Inadequate quantum
- Lack of predictability in quantum, timing
- Buoyant sources like GST, Stamp duties, MV regn charges etc. not devolved

Solutions

- Strengthen SFCs
- Frameworks to estimate expenditure obligations, funding mix

Pathways

- Digital grant management systems

Issues, Solutions and Pathways

2. Revenue Optimisation

Issues

- Valuation
- Enumeration
- Assessment
- Billing and collection
- Reporting

Solutions

- Focus on fees and user charges
- Improve collection efficiencies

Pathways

- Incentivising own tax revenue collection
- Unified revenue collection

Issues, Solutions and Pathways

3. Fiscal Responsibility & Budget Management

Issues

- Budget variances
- No MTFPs
- Weak financial controls
- No/poor quality audited a/cs

Solutions

- A 21st c. public finance framework for cities incl NMAM 2.0
- Comprehensive digital PFM system covering all aspect of financial management

Pathways

- XBRL based reporting

Issues, Solutions and Pathways

4. Institutional capacities

Issues

Shortage of

- staff
- skills
- org design
- performance management

Solutions

- Overhaul cadre and recruitment rules

Pathways

- Municipal Shared Services Centres
- Municipal Finance Officer's Association

Issues, Solutions and Pathways

5. Transparency and citizen participation

Issues

- all round opacity
- no voice and agency for citizens

Solutions

- Enforce public disclosure law, community participation law

Pathways

- Participatory budgeting
- Ward Quality Score

Fiscal Decentralisation – Issues (1/2)

State	Own revenue	Grants and Assigned revenues	Others	Borrowings	Total
Karnataka	27%	71%	-	2%	100%
Chhattisgarh	53%	29%	-	18%	100%
Gujarat	47%	43%	-	10%	100%
Jammu and Kashmir	9%	85%	6%	-	100%
Meghalaya	73%	27%	-	-	100%
Maharashtra	62%	22%	15%	1%	100%
Manipur	4%	95%	1%	-	100%
Nagaland	92%	8%	-	-	100%
Punjab	83%	15%	1%	1%	100%
Sikkim	42%	58%	-	-	100%
Tripura	6%	54%	-	40%	100%
Uttarakhand	11%	89%	-	-	100%
West Bengal	20%	76%	3%	1%	100%
Total	49%	41%	7%	3%	100%

Contribution of sources of funds for ULBs
for the year 2017-18

1. Fiscal Decentralisation remains a nascent reform agenda
 1. What revenue powers to devolve and how much, to begin with, should be a function of extent of functional decentralization.
2. There is no empirical basis for estimation of expenditure required to meet pre-defined service levels for different functions discharged by the ULB.
3. Grants and assigned revenues from the central and state Governments need to be predictable in quantum and timing

Fiscal Decentralisation – Issues (2/2)

ULBs authorised to raise borrowings without state government/central government approval?	Bhubaneswar, Jaipur, Patna, Ranchi
ULBs not authorised to raise borrowings without state government/central government approval?	Ahmedabad, Bengaluru, Bhopal, Chandigarh, Chennai, Dehradun, Delhi, Guwahati, Hyderabad, Kanpur, Kolkata, Lucknow, Ludhiana, Mumbai, Pune, Raipur, Surat

Borrowing powers of ULBs*

4. ULBs need powers over municipal borrowings, budget-setting and support from states to access municipal borrowings
5. ULBs require support from states for strengthening their capacities to engage with the market.
 1. Few ULBs have accessed municipal bonds (aggregate issuances less than Rs 3,500 cr with another Rs 3,000 cr in the pipeline) or pooled finance or finance leases..
6. ULBs need to be given greater degrees of ownership and control over their land and property, and capacity building support to leverage them

Fiscal Decentralisation- Recommendations

1. State governments need to **devolve more own revenue streams to ULBs** and give them greater powers over such revenue streams.
2. **State Finance Commissions (SFC) need to be overhauled into credible institutions**, and state governments need to be held accountable for timely consideration and response to their Action Taken Reports (ATR).
3. **Empirical framework for estimating expenditure obligations and corresponding devolution of revenue streams**, recommend appropriate formulae to ascertain percentage share that could be considered for assignment to ULBs
4. **Central Finance Commission (CFC) and SFC grants being made available to ULBs need to form part of medium-term fiscal plans of cities**. Actual disbursements against awards should be tracked and reported.
5. Other than own revenues and grants which are predominant sources of revenue, ULBs have not yet leveraged municipal borrowings particularly through finance capital investments. **A Comprehensive Debt Limitation Policy (CDLP) or equivalent provision for municipal borrowings needs to be introduced in all municipal acts, to open up municipal borrowings within a framework of fiscal prudence.**
6. A systematic and comprehensive effort needs to be undertaken **to give greater powers over land and property to ULBs**, through appropriate amendments to state municipal acts

Revenue Optimisation of Own Revenues- Issues (1/2)

1. Enumeration

1. First, there is no provision for regular update either by mandatory linkage to building plan sanction systems or otherwise.
2. Second, there is no institutional mechanism to ensure continuity beyond a one-time exercise, including knowledge transfer and creation of capabilities within the ULB or state intermediaries.
3. **Of the 21 states we evaluated, 12 state municipal acts do not have clear provisions for regular enumeration of properties. In several other cases, enumeration can be undertaken at the discretion of states or ULBs with varied time intervals.**

2. Valuation and Assessment

1. The municipal acts generally contain only high-level provisions on property tax. Few states have not yet moved to a self-assessment scheme.
2. There is also no integration between the databases of the stamp duties and registration department and the revenue department of ULBs.
3. **Of the 21 states we evaluated, only 5 had transitioned to UAV method and the rest were following ARV method.** Leaving room for discretion in estimating rental value

Revenue Optimisation of Own Revenues- Issues (2/2)

3. Billing and Collection

1. Collection efficiency is directly dependent on completeness of billing and also administrative efficiencies in the collection process. In many ULBs, there are no processes in place to ensure completeness of billing, timely billing and issuance of reminders for payment
2. Several ULBs continue to maintain manual records making them vulnerable to errors and frauds. Adoption of online payment of property tax has been relatively slow.
3. We also found in certain cases significant staff vacancies in revenue departments directly impacting collection efficiencies.

Collection efficiency of property tax ranged from 32% to 72% for the states of Karnataka, Madhya Pradesh, West Bengal, Himachal Pradesh, and Jharkhand for which data was available from CAG audit reports, for the period 2011-12 to 2015-16. **While in Karnataka, Madhya Pradesh and West Bengal, the collection efficiency was in the range of 65-81%, in Himachal Pradesh it was 52% in 2013-14, the only year for which data was available, and 32% in Jharkhand for the period 2011-12 to 2015-16.**

Revenue Optimisation of Own Revenues- Recommendations (1/2)

1. Enumeration of property

1. **Provision for periodic enumeration should be a part of state municipal acts.**
States need to provide for a **state-wide GIS facility for municipalities** to access, through a specialised entity like the urban infrastructure development finance corporation or equivalent.
2. **Database integration across government databases such as power supply, gas agencies etc.** should be considered to enable smooth update of property records on an ongoing basis.

2. Valuation and assessment of property

1. **Unit area valuation (UAV) and self-assessment methodology should be progressively adopted across states and ULBs.**
2. **Property tax board should be constituted in all states to provide independent advice and recommendations to ULBs** on enumeration, valuation and assessment. Exemptions from property tax should be rationalised and always accompanied by details of underlying rationale and revenue foregone.
3. **The property tax register of the ULB should be published online** with details of property, area, property type, guidance value, property tax amount, payment details, pending dues etc. with due safeguards built-in for privacy.

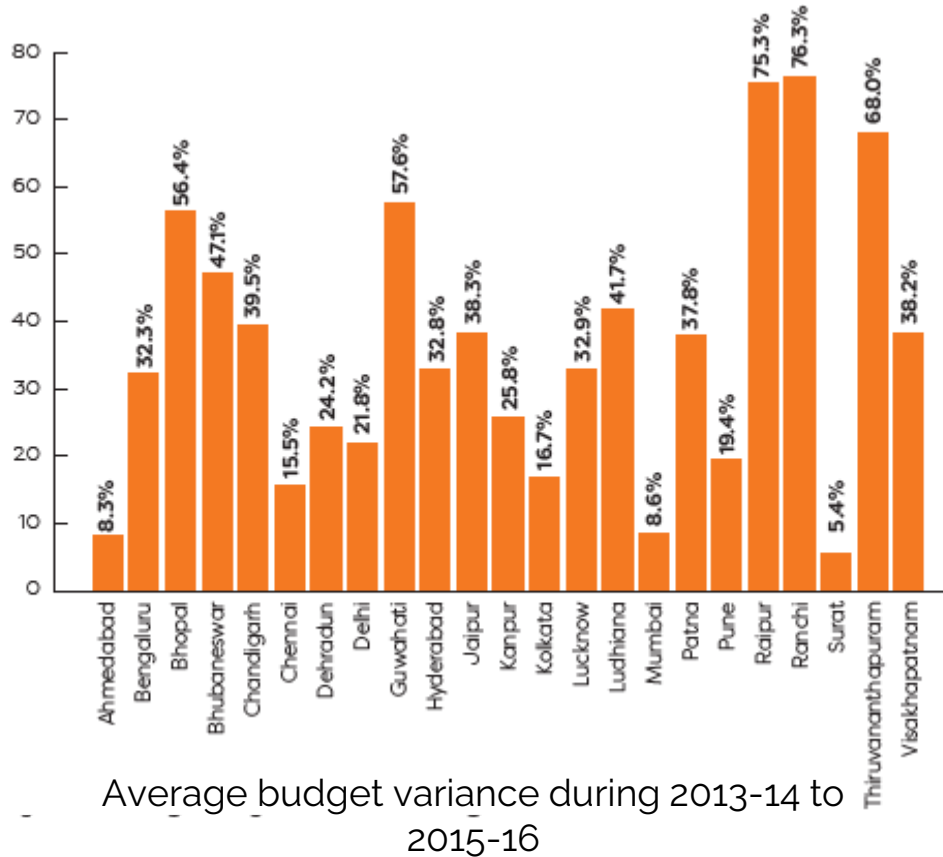
Revenue Optimisation of Own revenues- Recommendations (2/2)

3. Billing and collection of property tax

1. ULBs should adopt end-to-end integrated information systems for property tax which provides for regular billing and reminders, online payments, digital records, integration with GIS system and property tax register, and facilitates monthly/quarterly property tax MIS. The experience of Ranchi and other ULBs in Jharkhand in this regard may be instructive.
4. In the case of all fees and user charges, there is a need to adopt functional costing whereby the cost of service delivery is compared to corresponding fees and user charges and the revenue gap ascertained and published.

Fiscal Responsibility and Budget Management- Issues

(1/2)



1. Budgets of ULBs are not realistic, comparable or provide more actionable information

1. Budgets across states are incomparable in the absence of a national standard, notwithstanding the requirement to follow the national municipal accounting manual.
2. Most often budget documents only provide operational cost lines (e.g. salary, rent) and not functional/service delivery cost lines (e.g. solid waste management, roads, streetlights etc.) thus impairing their utility

Fiscal Responsibility and Budget Management- Issues

(2/2)

- 2. Outcome budgets are being introduced at the central and state-levels, there is in fact greater relevance and need of outcome budgeting at the municipal level**
 1. Presently, ULB budgets are not linked to outputs and outcomes which they seek to achieve
 2. Particularly at the ULB level (as against state and central government levels), it is easier and more relevant to track the direct benefit arising out of public expenditure, in the form of physical infrastructure and services (outputs) and in terms of quality of life of citizens (outcomes).

- 3. Budgets are annual projections, need to be anchored in medium-term fiscal plans.** The Karnataka Local Fund Authorities Fiscal Responsibility Act 2002 and The Karnataka Municipal Accounting and Budgeting Rules 2006 present a model that is worth emulating across states.

Fiscal Responsibility and Budget Management- Recommendations

- 1. Checks on budget variance, to ensure realistic budgets are drawn up by ULBs and variances are explained in detail along with next year's budget**
- 2. Standardized budgets that are comparable** and provide information on both operational and functional cost-types, including geographic allocations within the ULB (at a zone or division or ward level) to the best extent possible
- 3. Outcome budgets that indicate outputs and outcomes corresponding to expenditure outlays**
- 4. Systematic citizen participation in budgeting** accompanied by public disclosure of actionable financial and operational information
- 5. Medium-term fiscal plans with annual explanatory statements, alongside annual budget, for variances from medium-term fiscal plan.**

Institutional Capacities- Issues

- 1. There are four essential ingredients to human resource management in ULBs, which are missing today**
 1. ULBs need to **have normative standards for number of people they need in each function** commensurate with underlying key drivers such as population, road length, tonnage of solid waste, number of properties/households, number of motor vehicles etc. and benchmark service levels they need to deliver.
 - 2. Technical skills and behavioural competencies** required in each role need to be updated to 21st century urban requirements.
 - 3. Organisation design** should be fit for purpose, and aspects such as span of control need to be attended to.
 - 4. Performance management policy** at an organisational, departmental and individual level needs to be defined with quantitative metrics.

Institutional Capacities- Issues

Municipal staff vacancy

City	Total sanctioned strength	Total permanent staff	% vacancy
Ahmedabad	21,375	11,199	48%
Bhubaneswar	1,439	1,088	24%
Guwahati	3,810	1,536	60%
Hyderabad	6,746	5,538	18%
Jaipur	9,745	6,161	37%
Mumbai	163,183	105,263	35%

Staff per lakh population

City	Total Staff (including contract and deputation)	Population (in Lakhs)	Staff per lakh population
Bengaluru	26,800	84.4	317
Hyderabad	32,746	67.3	486
Mumbai	1,16,697	124.4	938
London	2,40,000	81.7	2,936
New York	4,92,300	83.3	5,906
Johannesburg	32,546	49.4	659

2. Staff vacancies in ULBs are endemic

1. While vacancies compared to sanctioned strength are significant, the sanctioned strength itself is not based on normative standards and not updated periodically based on an enabling policy.
2. When compared to the population they service and global peers, Indian ULBs come across as very poorly staffed.

3. Use of information systems in ULBs continue to lag potential by a long distance, can potentially be a game-changer

Institutional Capacities- Recommendations

- 1. Cadre and recruitment (C&R) rules of ULBs need to be comprehensively updated, particularly in respect of revenue and finance functions.** Normative standards need to be established for each role in revenue, finance and engineering functions. Skills and competencies need to be defined in contemporary terms. Performance measures need to be laid down. Workforce requirements in ULBs need to be reviewed at periodic intervals based on the growth of the city and the ULB through a medium-term workforce plan.
2. Draw up **certification-based online skilling programs** for revenue and finance staff. State governments should mandate completion of different levels of these programs for different levels of staff.
- 3. Municipal Services should be identified as a sector under the Skills Mission,** so dedicated sector skill council can be created and jobs in revenue, finance departments and engineering given a thrust.
4. Undertake a serious evaluation of **Municipal Outsourcing or Municipal Shared Service Centres** which can surmount the challenge of staffing in ULBs, and also deliver significant benefits in terms of lower costs and better services.
5. To make available **standardised software for revenue and finance functions for use by ULBs** who have been unable to utilise the same. It should also lay down standards for such software. State governments should facilitate fast-track adoption of the software by its ULBs.

Transparency, accountability and citizen participation - Issues

1. ULB budgets are presently insufficient to meet benchmark levels of infrastructure and services in cities.
 1. **In order to ensure that limited resources of the ULB are targeted effectively (i.e. towards required needs, both service-wise, and location-wise) and efficiently (i.e. towards optimum citizen outcomes), there is a need to facilitate citizen participation in ULB budgets.** However, such participation cannot just be in the form of open-ended public consultations.
 2. **ULBs are over-audited, but not necessarily rightly audited;** ULBs need to put in place risk-based auditing of internal controls
 3. Audit of annual accounts is the sine qua non of sound financial management, **ULBs need to be mandated to publish their audited annual accounts in a credible, timely and standardised manner.**
 4. **The accounting function in ULBs is outdated** in terms of accounting standards, accounting manuals and standard operating procedures.

Transparency, accountability and citizen participation - Recommendations

- 1. Systematic citizen participation in budgeting accompanied by public disclosure of actionable financial and operational information at a work/contract level and street/ward level.**
- 2. Formalise citizen charters that state service levels** building on MoHUA's SLB framework, turnaround time and grievance redressal procedures.
3. Implementation of **National Data Sharing and Accessibility Policy (NDSAP)** to facilitate easier access of data for citizens.
- 4. Risk-based internal audit function in ULBs reporting directly to the elected council.**
- 5. Publication of audited annual accounts** that are credible, timely and standardised.
- 6. Implementation of accounting standards for local bodies** issued by the Institute of Chartered Accountants of India in preparation of such audited annual accounts.
- 7. Adopt eXtensible Business Reporting Language (XBRL).** MCA21 of the Ministry of Corporate Affairs, regulatory reporting by banks to the Reserve Bank of India, filing of Income Tax returns etc. all adopt XBRL methodology and standards.

Thank you!

