STRENGTHENING INSTITUTIONAL FRAMEWORKS FOR LOCAL GOVERNANCE

Benchmarking local finances

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Why to benchmark local finances?

1. ***It is a mirror***: comprehensive analysis of local finances and financial management
2. ***What is done well:*** successes, innovations
3. ***What to change:*** areas of improvement
4. ***Ranking tool:*** positioning a country/city
5. ***Lessons for policy makers:*** need for change, lacking capacities, wrong incentives, missing regulations
6. ***Learning from each other:*** internationally (Eastern Partnership); within your country

Evidence based analytical and diagnostic tool!

Basis: CoE Recommendations on financial resources and management

I. Financial resources (2005)

II. Financial and budgetary management (2004)

Recommendations => bases of benchmarking:

    a) central authorities, on local finance systems:

- 76 items on financial resources
- 43 items on financial management

    b) local (regional) authorities, on local practices

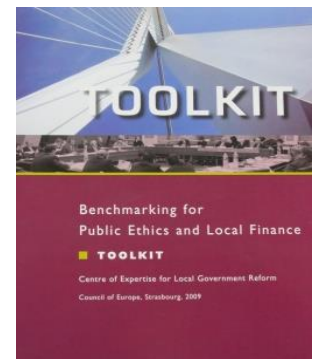- 31 items on financial resources
- 43 items on financial management

Financial resources, financial management at national and local level

Areas of local finances	a) National systems (decentralization)	b) Local (regional) authorities
1.Financial resources	Statistical data Institutional review	Data analysis Assessment
2.Financial management	Institutional review	Review Evaluation

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Areas of standard finance benchmarks

1) Financial resources:

- Local taxation: sufficient, diverse, locally administered
- Fiscal equalization: spending needs and revenue capacities, transparent, predictable
- Grants to local governments: general vs. specific grants, incentives created
- Fees, charges: significant, local autonomy, cost recovery, social policy
- Borrowing: for capital financing, debt limits
- Local property: inventories, management

TOOLKIT

Benchmarking for
Public Ethics and Local Finance

■ TOOLKIT

Centre of Expertise for Local Government Reform
Council of Europe, Strasbourg, 2009

Areas of standard finance benchmarks *(2)*

2) Financial management:
- Fiscal strategy: multi-year, discussed
- Budgeting framework: regulated procedures, openness, local implementation autonomy, methods and capacity
- Budget implementation: regulations on commitments, transactions, recording, accounting, adjustment, control and monitoring, balanced budget
- Financial monitoring system: transparency, accuracy of fiscal information, audit capacity

National systems or local government practices

External evaluation and not self-assessment!

Benchmarking: scoring by areas of recommendations

0.   Defining critical areas of local finances, financial management

1.   Section ➡ area ➡ components ➡ sub-categories
2.   Specifying the activities, indicators measured
3.   Identifying sources of verification, documents
4.   Scoring (interval scale: 0-10)
5.   Interpretation of the results:
       low scores ➡ factors behind the differences?

An example: local taxation

SECTION, AREA, COMPONENT	ACTIVITY, INDICATOR	VERIFICATION STATEMENT, DOCUMENT	SCRORE, WEIGHT
SECTION: *II. Local taxation*			
AREA: **Local tax policy design**			
COMPONENT: b) Local taxes should produce high yield (R9) c) Local taxation should be operated at low administrative costs (R9)	•Local tax revenues in % of total/current budget •Local tax revenues in % of local own source revenues •Total tax administration costs in % of local expenditure on administration •Tax yield compared to total costs of tax administration (for all and by taxes)	Municipal fiscal statistics Local budgets	0–10

Measurement techniques

1. Expert judgement, peer review (qualitative)
- Analysis of documents, local practices
- Performance indicators
- Secondary analysis of surveys, assessments

2. Data on local governments (quantitative)
- fiscal autonomy: reclassified taxes (OECD FN)
  - local rate setting; legislated sharing ratio
  - transfers: scope of local discretion
- budget size, composition, unit costs of services
- capital investment spending
- local indebtedness

Scoring methods

Importance of the indicator: equal or weighted

Components of scoring

- Legal requirement or non-regulated
- Method applied or missing
- Assessing the quality of the domestic/local practice (low, medium, high)
- Established procedures, evidences exist

Implementing *local* LFB

Bulgaria: 6 pilots (2007)=>70 (2015)
- significantly simplified LFB
- local interest after elections
- transformed to self-assessment tool
- paid service to members
- lessons for legislative changes

Ukraine (2012): 10 city pilots
- ✓ focus on budgeting and transparency
- ✓ unified rules=>diverse implementation
- ✓ lacking local taxing powers, revenue administration autonomy
- ✓ strong data component
- ✓ no host organization

Three country pilot (2013):
➢POR: local elections; GRE: crisis, reforms; ESP: regional differences
➢self-assessment: lacking capacity, need for local support

Basque country (2014-): Bizkaia region

CoE/EU Eastern Partnership Programmatic Co-operation Framework project

Strengthening institutional frameworks for local governance (thematic group)

Local finance benchmarking component (6 countries)

Implementation stages:

1. assessing the legal-regulatory framework ✓

2. adapting the standard LFB Toolkit:
   a) specific conditions for in-country comparison
   b) benchmarking systems (regional comparison)

3. piloting the adjusted local finance benchmarks

+ lessons for systemic reforms

External factors of the LFB survey

- What is a local government: elected, at various tiers
- Wide range by population size: MDA: 2,850-GEO: 49K
- Controlled executive powers by sub-national state units:
  - regional (Oblast, rayon, marz) administration and local excoms
  - revenue (re)allocation; budgeting; supervision; tax administration
- Functions:
  - % of GDP: ARM (2.5), GEO (5.4), MDA (11.2)
  - delegated (centrally funded) and devolved: BEL (19.2), UKR (14.3)
  - autonomy in managing own functions:
    - ARM, GEO *vs*. AZE, BEL , unclear specification: MDA, UKR

What will be evaluated?

1. Own source revenues

‣ Critical for LFB:

  ◦ classification of revenues: autonomy (base, rate, reliefs)

  ◦ capital revenues: sale, rent, lease, dividend, interest

  ◦ tax administration: centralized in BEL, GEO, UKR

‣ Being technical and less sophisticated

2. Municipal property

  ○ exclusively local asset exist?

  ○ local powers: sale, rent, invest

What will be evaluated? *(2)*

3. Revenue sharing

- What is a shared revenue: set ratio, origin based, no compensation for losses
- Reallocation by regional governments
- LFB: origin based, transparent, not earmarked

4. Intergovernmental transfers

- Diverse forms, but how the total is fixed
- Stable, objective, predictable, transparent
- Incentives created: measuring expenditure needs, revenue equalization
- Budgeting process influences allocation

5. Local borrowing: not significant, but well regulated => procedures

What will be evaluated? *(3)*

6. Local financial management: legislation *vs.* real practices

- Budgeting,
  - strategy design
  - autonomous council vs. executive committee
  - centrally driven state budget planning process
- Open, regulated process: but how effective methods?
- Limitation on local management autonomy
- Managing financial difficulties
- Supervision, evaluating budget implementation, technical support
- Disaggregated info: accounting standards, quality of info

Conditions of successful LFB

Good adaptation: selecting areas of local financial autonomy, localizing the LFB Toolkit

Capacity to implement LFB: external evaluation, *not* self-assessment

Creating incentives: in a centralized system with limited local management capacities

Getting support from partners: public awareness, pilots

Balancing confidentiality, publicity: elections, timing

Critical mass of information for comparison: more cases, regular surveys, data availability

Host organization: analytical capacity to formulate recommendations

Sustainability of the LFB program