

Programmatic Cooperation Framework for
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**STRENGTHENING INSTITUTIONAL FRAMEWORKS FOR LOCAL GOVERNANCE PROGRAMME
2015-2017**

STUDY
**Finance Benchmarks: areas and options for assessing
local financial resources and financial management
in Moldova**

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Executive Summary

Until 2014, the local authorities in Moldova had limited fiscal autonomy and fiscal potential. The budgets of lower levels were strictly dependent on higher levels of governments (matryoshka), while the transfer system was highly inefficient, unpredictable, and non-transparent, providing little if any incentives for fiscal responsibilities to local authorities (i.e. the transfers were reduced if the municipality collected more local revenues). LPAs were highly dependent on the state budget (70% excluding Chisinau and Balti municipalities), making them financially weak in performing their responsibilities. As of 2014, the old system of local finances has been improved and implemented in three pilot districts or rayons (Basarabeasca, Ocnita, and Rascani) and in the Chisinau Municipality. The improvement aims at insuring a fiscal and budgetary autonomy of local authorities, maximizing efficiency and equity in allocation of resources while maintain fiscal discipline. As of 2015, the new system of local finances is being implemented across the entire country. This report summarizes the current situation and identifies key areas for local finance benchmarks implementation.

The administrative territorial division of Moldova could be considered as very fragmented and the average population size of local governments in Moldova is rather small. Territorial fragmentation is usually pointed out as one of the key barriers to a qualitative provision of the public service provision. The current small size of many villages (communes) is considered not economically viable in terms of self-governing units due to the narrow economic base and lack of economies of scale in terms of service production and provision. Furthermore, a large number of villages (communes) implies lower efficiency - high cost for administration, technical support, capacity building - as it promotes stronger supervision of local governments from the higher level of public administration and central government. While the decentralization reform has been adopted and implemented across the entire country as of 2015, a territorial-administrative reform of Moldova is a must for the authorities in the period to come.

The actual structure of local government functions is more or less a “classical” one for the transition countries, even the assignment of all the local functions is dissipated among a lot of normative acts (laws, government decisions, or other regulations). A critical feature of the assignment process of functions to local government in Moldova stands out, namely the assignment is very fragmented, a lot of sub-functions, arbitrary separated from the main functions, being transferred to local government units by a lot of normative acts in a very un-systemized way.

In terms of local budgets, transfers stand out as the largest component of revenues at aprox. 70% in 2014 for both, level 1 and 2 local governments. Own revenues are at 13% and 6%, respectively. As there are no preliminary data for 2015, a recent report which analyzed the effect of fiscal decentralization in the pilot regions shows that the new reform generated a number of interesting trends where shared taxes decreased significantly while transfers increased in the pilot regions. This tendency is primarily due to the modified inter-budgetary relations where income tax of legal entities is no longer shared. Public institutions are now financed via special transfers, which were introduced with the new law.

Capital revenues are predominantly used by LPA to cover their budget deficits when necessary. Revenues from sale and privatization of public property take 90% of the capital revenues structure and have accounted for over 236 mln MDL which is by far the largest share. Over 62.7% have been collected by LPA I while the rest by LPA II. Revenues from local property management are relatively evenly distributed throughout the country. While in rural areas, revenues from land taxes are dominant, in urban areas building taxation is the main revenues driver. It is important to note that local tariffs and user charges are set based on political, rather than economic, principles. These, in most cases, do not cover expenses and as such most of the service provision enterprises risk bankruptcy. For the Chisinau Municipality, local tariffs and user charges are set by the National Agency of Energy Regulation of the Republic of Moldova.

Management of public property is characterized by a medium level of inventory and registration of public property. Most public land and real estate are inventoried by municipalities at a rate of 60-80%, but their body cadastral registration records a much smaller proportion. The entire public patrimony is managed by City Hall and its subordinate institutions. Public tenders are organized for sale of municipal heritage. The resources obtained from auctions are usually used to cover the budget deficit. Records show low recovery of public assets through investment projects.

Special means represent revenues obtained by public institutions, under conditions approved by the regulatory acts, from the work undertaken and services delivered, as well as donations, sponsorships and other funds properly come into possession the public institution. These financial means represents up to 5% in total revenues of local governments. Financing through grants is generally considered as being unfavorable to local autonomy in that local governments remain dependent upon the authority allocating these grants. However, transfers from the central state form the largest share of grants received by local governments. So not the mere size of central budget grants, but more the methods of allocation define the local fiscal autonomy. Interestingly, even under the new fiscal decentralization law, the rules of grant allocation are not clear, as a straightforward formula is yet inexistent. Finally, loans as one of sources for local government capital investments are virtually inaccessible to local public administrations.

To better align the local government functions as well as compare these on a regional, national, but also international level, this report also proposes a comprehensive list of local finance benchmarking areas. Particularly, the report recommends that benchmarking own revenues, shared revenues, municipal property management, intergovernmental transfers and grant allocations as well as local borrowing is required to fasten growth at local and regional level in Moldova. However, benchmarking these areas might also suffer a number of obstacles, among which lack of incentives at local and national levels, lack of competence of civil servants, and limited public interest are critical.

On one hand, local civil servants might have *insufficient competences and skill* to fully understand the complexity of LFB implementation and as such the benefits it might bring to local and national development. On the other hand, not being fully aware of the benefits and the essence of LFB implementation might minimize the incentives local governments have to fully adhere to an objective local, national, but also international comparison.

These problems could be overcome but increasing the public awareness of the population about the LPA's activities. However, as a recent UNDP survey shows, while a vast majority of population (around 70%) knows their rights to be informed about the LPA's activities, only about 10% of the population actually does so. Thus, more intense policy initiatives are required to facilitate citizen's involvement in the local government's activities. Building comprehensive benchmarks and overcoming these obstacles is a challenge to be addressed in a follow up report.

1. Political and Administrative Structure of the Republic of Moldova

1.1. General data

Republic of Moldova:	Parliamentary Republic
Population:	2.913 million, excluding Transnistria (2014 census)
Territory:	33,843 sq. km
Borders with:	Ukraine, Romania
Capital City:	Chisinau (population 761.9 thousand)
Currency:	Moldovan Leu (MDL); 1 MDL=0.048 EUR; 1 EUR=20.78 MDL (as of July 31 st , 2015)
Language:	Romanian

1.2. Administrative-territorial division and local governments

Local governments in Moldova are organized in a two level (tier) system. According to the Constitution of the Republic of Moldova (article 110) the territory of the Republic of Moldova from the administrative point of view is structured in districts, towns and villages. Certain towns may under the law be declared municipalities.

The administrative-territorial unit is a legal entity of public right and it disposes of a property separate from that of the state and of other administrative-territorial units, according to the law.¹ The first level (primaria) local governments are presented by local governments in cities and villages. There are 898 first level administrative-territorial units – cities and communes (comprised of more villages) - in Moldova.

The second level local governments are the 35 administrative territorial units - 32 districts (rayon), two municipalities – Chisinau and Balti, and one autonomous territorial unit - Gagauzia. The average number of population in the first level local government is 2,850². The largest by population local government is the capital city Chisinau (761.9 thousand), but the smallest local governments have less than five hundred residents (Ochiul Ros, Anenii Noi) and many have under 1,000 inhabitants.

Table 1: Number of first level local governments and population by size (2014)

Population number	Number of primaria	Number of primaria, %	Population	Population, %
<500	4	0.4	1552	0.05
501-1,000	96	10.7	76,058	2.23
1,001-2,000	328	36.5	482,299	14.13
2001-5000	365	40.6	1,085,019	31.79
5001-10000	69	7.7	439,410	12.87
10001-20000	27	3.0	370,290	10.85
20001-50000	7	0.8	196,260	5.75
>50,000	2	0.2	762,338	22.33
Chisinau Municipality			761,9	
Total	898	100	3,556,000*	100

Source: Elaborated by author according to the report on the execution of administrative-territorial units budgets year 2014

*including Transnistria

¹ Law on Local Public Administration, No.436, Article 4.

² Osoian I., Sirodoev I., Veverita E., Prohnitchi V. Analytical Study on Optimal Administrative – Territorial Structure for Republic of Moldova. Chisinau, 2010.

Although the Law on Administrative - Territorial Organization sets the minimum required number of residents of the administrative territorial unit – 1,500,³ there are less than 1,500 residents in almost one third from total local governments. Significant part of those “exceptional cases” in Moldova are geographically rather close or even adjacent, and could be merged.⁴

The rayon (rayon or district) is an administrative and territorial unit, which includes villages (communities) and cities that are territorially bound by economic, social and cultural connections. The average district size by population is 77.3 thousand inhabitants. The largest by population districts are UTA Gaugazia (141.7 thousand), Orhei (115.5 thousand), Cahul (111.5 thousand), Hincesti (110.4 thousand), Ungheni (103.5 thousand), while the smallest districts have less or about 40 thousand residents (Basarabasca (26.9 thousand), Dubasari (33.9 thousand), Soldanesti (40.3 thousand)), which is closer to the population number of some town or rayon centers (Cahul, Ungheni, Soroca). Average area of district is 890 sq.km, the largest district (Cahul, 1545 sq.km) is 5.2 times larger as compared with smallest district (Basarabasca, 290 sq.km).⁵

The capital city, Chisinau, is both a second level and a municipality level administrative-territorial unit. The Chisinau city is divided in administrative-territorial subdivisions named sectors, while the municipality is comprised of towns and villages (communes) which are LPA level 1. There is no special Law on Capital City in Moldova, but the Law on Local Public Administration contains special chapter (VII) about public administration of Chisinau municipality. Not all provisions of the Capital City Law are fulfilled in fact.⁶

Besides the local government administrative territorial units there are six development regions in Moldova: North, Center, South, Chisinau, Gagauzia and Transnistria (based on Law on Regional Development No. 438-XVI of 28.12.2006).

In general, the administrative territorial division of Moldova could be considered as very fragmented and the average population size of local governments in Moldova is rather small. Territorial fragmentation is usually pointed out as one of the key barriers to a qualitative provision of the public service provision. The current small size of many villages (communes) is considered not economically viable in terms of self-governing units due to the narrow economic base and lack of economies of scale in terms of service production and provision. Furthermore, a large number of villages (communes) implies lower efficiency - high cost for administration, technical support, capacity building - as it promotes stronger supervision of local governments from the higher level of public administration and central government. The fragmentation of administrative territorial division of Moldova does not promote the decentralization and development of financial autonomy of local governments. While the decentralization reform has been adopted and implemented across the entire country as of 2015, a territorial-administrative reform of Moldova is a must for the authorities in the period to come.

1.3. Political structure

Moldova is a democratic and unitary republic. The political system is mixed parliamentary-presidential, with the Parliament (one hundred one representatives) and President. While the

³ Chapter III, Article 7 (3)

⁴ Osoian I., Sirodov I., Veverita E., Prohntichi V. Analytical Study on Optimal Administrative – Territorial Structure for Republic of Moldova. Chisinau, 2010.

⁵ Osoian I., Sirodov I., Veverita E., Prohntichi V. Analytical Study on Optimal Administrative – Territorial Structure for Republic of Moldova. Chisinau, 2010.

⁶ To be more precise, there law on the capital city dated on 1994 provides some baseline legislation for the capital city, but this law is not in accordance with the legislation of the Republic of Moldova.

Parliament is elected by population for a four year period, the president is elected by the Parliament for the same length of a mandate. The prime minister is appointed by the president only after the minister and his or her cabinet have received a vote of confidence from the parliamentary majority. The rights of the president to dissolve the parliament are very restricted. Some executive powers are vested in the president's hands: he or she can issue decrees and has special powers in defense and foreign policy. The delicate balance of power between parliament, government, and president is held to be responsible for the relatively high level of democracy as well as the blocking of important reform projects. Consequently, there have been discussions aimed at strengthening the powers of the president. Judicial powers are vested in the courts.

2. Local Government Competences

2.1. Local government functions, responsibilities, and rights

The Constitution (article 109, (1)) states that "... public administrations as manifested in the administrative/territorial units is based on the principles of local autonomy, of decentralization of public services, of the eligibility of local public administration authorities, and of consulting the citizenry on local problems of special interest." The responsibilities for providing local government services are stipulated in two laws: The Law on Administrative Decentralization and the Law on Local Public Administration."

The Law on Administrative Decentralization (article 3, a-e) defines the following principles that are connecting with the competence of local governments: (i) *principle of local self-government*, which implies the guaranteeing of the right and effective capacity of local public authorities to regulate and manage, under the law, on their own responsibility and in the interests of local population, an important part of public affairs; (ii) *principle of subsidiarity*, which implies the exercising of the public responsibilities by the lowest level authorities that are closest to the citizens, excepting the cases when the intervention of the high level authorities represents obvious benefits that proceed from the volume and nature of the responsibilities and the need to assure the efficiency of the public action; (iii) *principle of equity*, which implies the guaranteeing of some equal conditions and opportunities to all local public authorities with the aim to achieve their objectives in carrying out their duties; (iv) *principle of integrity of competences*, which supposes that any competence assigned to local public authorities shall be full and exclusive, and its exercising cannot be challenged or limited by another authority, with the exception of cases provided by law; and (v) *principle of correspondence of the resources with the competences*, which implies the correspondence of the financial and material resources allocated to the local public authorities with the volume and nature of the competencies that are assigned to them in order to assure their efficient fulfilment.

According the Law on Local Public Administration (article 10), local public authorities organize their activity in the fields established by the Law on Administrative Decentralization (see Appendix 8.1 for local government functions and Appendix 8.2 for local government domain of activity), being granted, for this purpose, full competences which shall not be undermined or limited by any public authority, unless the requirement of the law. The competences of the local public authorities are strictly defined, under this law, between the deliberative and executive public authorities of first and second levels. The central public administration authorities cannot assign or impose any competences to the local public authorities without a prior assessment of the financial impact that these competences may generate, without consulting the local authorities of the appropriate level, and without providing the local communities with the necessary financial resources.

The actual structure of local government functions is more or less a "classical" one for the transition countries, even the assignment of all the local functions is dissipated among a lot (too many) normative acts (laws, government decisions, or other regulations). A critical feature of the assignment process of functions to local government in Moldova stands out, namely the assignment is very

fragmented, a lot of sub-functions, arbitrary separated from the main functions, being transferred to local government units by a lot of normative acts in a very un-systemized way. The above classification is a strong rationalization and consolidation of the actual situation.

Some of the major problems in the assignment of functions to local governments are:

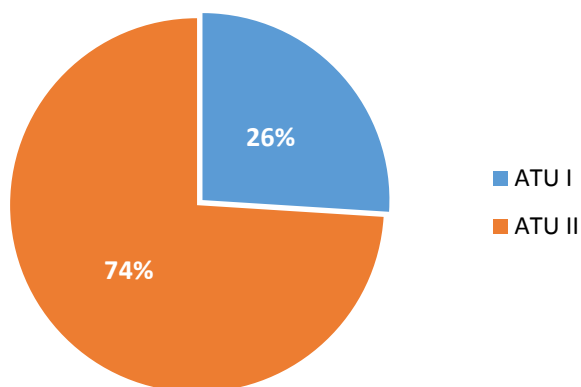
- a) Unclear assignment of functions among different administrative tiers: central, rayon and primaria, due to the high number of normative acts; a fragmented core responsibility in many sub-functions without any managerial or technical rationality; the lack of unique set of technical criteria to be used for any assignment of functions to local governments; as well as, a vague juridical language in the normative acts;
- b) The assignment of responsibilities is not coherent and uniform: many responsibilities are transferred through normative acts dealing with another subject, just like some auxiliary or connected provisions, with no details, without implementation and financial mechanisms, without respecting the general rules of decentralization;
- c) Generally the assignment is not correlated with the financial envelope – many reports and local authorities associations claim that the transfer of new responsibilities is done by the central administration without enough financial resources necessary to provide them. Moreover, the assignment of functions to one or other of local government tier ignores their fiscal and management capacity, jeopardizing the efficient and effective provision of public services;
- d) The assignment process is not correlated with the ownership of the infrastructure necessary to provide the transferred functions. Moreover, many decentralized responsibilities, the investment decision power remains at the central level, disconnected from the local authority which provide the service and decide on operational costs;
- e) Many local government units of the first level (primarias) complain against the permanent intervention (paternalism) of the central public administration or rayon (second level of the local government) on direct management of public service provision or in budgetary management. Partially, this paternalistic approach is justified by the lack of administrative and professional capacity at the level of primarias. It is expected that this issue will dissipate as the new law of fiscal decentralization is better understood by current public servants. Once fiscal decentralization is fully implemented, local public administrations will attain a greater financial autonomy. As such, their degree of responsibility will increase as well which will undoubtedly improve their professional and administrative capabilities.

With respect to item (e) above, some clarifications are required. After approval of the Law on Local Public Finances dual subordination has been virtually ruled out. In fact until then double subordination was not legally stipulated. The law stipulated however that LPA were skewed to provide services to CPA without them covering with the required finances. Nevertheless, dual subordination has been manifested through:

- Budgeting: LPA II budgets have been formed in stipulation with the Ministry of Finance, which settled expenditure norms by domains, and then supplemented these with budgetary corrections in case of insufficiency of funds (ex. Ministry of Finance sent a letter of cost cutting by 20% to an LPA in 2008); LPA 1 budgets have been formed in concordance with LPA 2, which could redistribute transfers towards LPA 1 (more LPA 1 taxes would decrease general transfers by said amount);
- Investment planning: annual national budget contained an appendix that stipulated investments for LPAs; these were distributed according to political discretion after parliamentary approval;
- Personnel employment: central governments would establish the structure and employment limits; although these had a character of recommendation, these were still considered in budgetary planning.

Currently, the local public authorities of first and second levels, as well as the central ones, may cooperate, under the terms of the law, with the aim to assure the accomplishment of some projects or public services that require joint efforts of these authorities.⁷

Figure 1: Ratio of ATUI and ATU II budget



Source: Author calculations

2.2. Institutional structure of local governments

The Constitution (article 112) provides the following provisions on first level local government institutional structure:

- 1) At village and town level the public administration authorities through which local autonomy is executed are represented by the elected local councils and mayors.
- 2) The local councils and the mayors operate under the law as autonomous administrative authorities and are assigned the task of solving public affairs in villages and towns.
- 3) The ways of electing local councils and mayors, as well as their powers and competence's shall be established by law.

The Law on Local Public Administration determines the number of local council members, but the election process is set in a special law – the Elections Code. The number of councilors depends on the number of residents in municipality and it varies from 9 (in municipalities with less than 1,500 inhabitants) to 43 in municipalities with population over 200,000, but in Chisinau the council is composed of 51 councilors.⁸ Councils as representative authorities establish executive organs to fulfill local government's tasks. The mayor is the chief of the local public administration. The vice mayors are elected by the council upon the mayors proposal. The mayor proposes and the council approves under the law, the organizational and employees' chart, the salary plan.

The structure of Chisinau municipality differs from other local governments. The public administration of Chisinau municipality is implemented by the municipal council, town councils and village (commune) councils, as deliberative authorities, and by the general mayor of Chisinau municipality, and the mayors of the villages (communes) and towns, as executive authorities. The Law on Local Public Administration provides the requirement on position of secretary of local council and its duties, provisions on mayoralty.

The Constitution (article 113) provides the following provisions on districts:

- 1) The district council coordinates the activity of the village and town councils to achieve public service at district level.

⁷ Law on Administrative Decentralization, No.435.Article 5 (1).

⁸ Last local elections in Moldova were held in June 2011

- 2) The district council will be elected and will work in accordance with the law.
- 3) The interrelationships of public authorities are based on the principles of autonomy, legality and cooperation in solving common problems.

The rayon (district) council is the representative authority of the district's population. The district council is composed of councilors, elected according to the provisions of the Elections Code.⁹ Depending on the number of population the number of district councilors varies from 27 to 35. The district council elects the district president with the vote of the majority of councilors. The district president may be only the person that has access to the state secrets. The district president is assisted by the vice presidents. The staff of the district president's office is organized and functions based on a regulation approved by the district council. The secretaries of the district council, of the Chisinau municipal council and of the sector council of Chisinau municipality are considered civil servants.

To fulfill their functions local governments establishes administration and institutions and manage municipal enterprises (companies). According the Law the local councils are obligated to elaborate and approve the statute of the respective administrative-territorial unit, which contains specific data and elements that are designed to individualize them compared to other similar units. The Assessment Report on Administrative Capacity of Local Public Administration Authorities (2010) reflects that significant number of local governments (districts, cities, municipalities) does not have such document.¹⁰

Moldovan local public administration is influenced by both European models and principles and by Soviet vestiges, with the latter seemingly having a bigger influence on it.¹¹ Centralized model of administration was reinforced and replicated, especially in the period between 2003 and 2009, when the government took great efforts to strengthen the verticality of the power.¹²

The Law on Local Public Administration sets out the full right of the local and rayon councils to determine the necessary staff in institutions, but the Government decision nr. 688 (10.06.2003) "On structure and staff of local administration of cities and villages" and Government decision nr. 689 (10.06.2003) "On structure and staff of district administration" determines the necessary staff positions and the number of loads according the number of population in the administrative territorial unit. Those acts are obsolete because the structure and the staff shall be approved only by the Council (proposed by mayor or president), under the Law on Public Administration in force, from 2006.

Besides the Government decision No. 525 (16.05.2006) „On the remuneration of civil servants and persons performing technical service" determines local governments staff salaries.

According the Government Decision No.688 each first level local government administration has one chief accountant, local governments with population more than 6500 has deputy of chief accountant and tax specialist. Tax collection specialist load depends from the number of population – *minimal load* is 0.5, if population is less than 1,500, maximal load in rural municipalities is 3, if population is more than 10,500, in towns - 5, if population is more than 30,000.

However, regulation at issue provides special provisions for Balti and Chisinau municipalities. Thus, for these municipalities is established only the limited number of employees in the Finance Department, without specifying the number of tax collectors; their number may be assigned at the discretion of the respective public authorities.

⁹ Law No.436 on Local Public Administration, Article 41.

¹⁰ Assesment Report. Administrative Capacity of Local Public Authorities. Prepared by Popa V., Bulat V., Barbu D. for UNDP, Chisinau, 2010.

¹¹ Osoian I., Sirodov I., Veverita E., Prohntichi V. Analytical Study on Optimal Administrative – Territorial Structure for Republic of Moldova. Chisinau, 2010.

¹² Popa V., Bulat V., Barbu D. Administrative Capacity of Local Public Authorities. Assesment Report. UNDP, Chisinau, 2010.

According to the Government Decision No.689 each rayon council has Finance Department and the number of staff there depends from the number of administrative territorial units (first level local governments) in rayon. Minimal staff number is 11, if there are 6-14 administrative territorial units in rayon, maximal staff number is 17 in case of 35-40 administrative territorial units. Besides, there are accountants in the Chairman Office and in the Education Department.

In such way determined number of staff and financing does not promote local governments to think about administrative efficiency and also about amalgamation, in opposite those regulations could initiate the splitting of local governments. At the rayon level there is confusion between the missions and roles of deconcentrated institutions and decentralized institutions.

Although the Law on Local Public Administration sets out the full right of the local and district councils to determine the necessary staff in institutions, existence of above mentioned regulations indicate low level of local autonomy in expenditure side. International experience indicated opposite trend – local government finance autonomy since 1995 increased - spending has become more decentralized¹³. Only the economic crises in some countries set higher control over local spending. For instance, in Latvia within events to get out from economic crisis since 2010, when the country's GDP growth rate was negative, local government staff salaries were included in unified public sector salary system, but it is temporary solution.

2.3. Local governments supervision

Until 2006 there was establishment of prefects' system as state representatives in the territory of districts in Moldova. During the period 2006 - 2009 the LG supervision was ensured by the Ministry of Local Public Administration. It had 10 Territorial Administrative Control Subdivisions. In September 2009 the Ministry was abolished and its functions were transferred to the State Chancellery. The State Chancellery and the Ministry of Finance are the main organizations that define the local government's sector policy and ensure supervision of local governments.

In the State Chancellery for local governments responsible divisions are:

- Division (Department) of Decentralization Policy;
- Division of Local Public Administration.

In the Ministry of Finance the divisions that deal with local government issues are:

- Division on Budget of Administrative - Territorial Units;
- Service on Financial Control and Revision.

Also other ministries and state institutions have close relations and have shared public services with local governments, such as:

- Ministry of Regional Development and Construction;
- Ministry of Education;
- Ministry of Interior Affairs;
- Ministry of Agriculture and Food Industry;
- Agency for Land Relations and Cadastre, etc.

¹³ OECD COM/CTPA/ECO/GOV/WP(2009)7

The State Chancellery has competence and responsibility of the development and implementation of the administrative decentralization policy. The State Chancellery is responsible for organizing the administrative control of the local public authorities' activity (including legality control), implemented directly by the State Chancellery or by its territorial offices, ruled by the Government representatives in the territory.

The Ministry of Finance and/or Finance department is authorized to screen the budgets of administrative territorial units for accuracy of their preparation and execution. Revision to the execution of the budgets of administrative-territorial units is carried out by Financial Control and Revision Service under the Ministry of Finance, periodically, every two years.

In exercising its powers, the Court of Account audits the local authorities on formation and implementation of budget of administrative-territorial unit. In the Parliament the Public Administration and Regional Development Committee deals with the local governments issues. Above mentioned state institutions, local governments and their organizations form the range of main Moldova's stakeholders of decentralization and finance decentralization process. They have different interests and perceptions. Involvement of all of them in the process of finance decentralization planning and implementation is crucially important and must be done in the earliest possible stage.

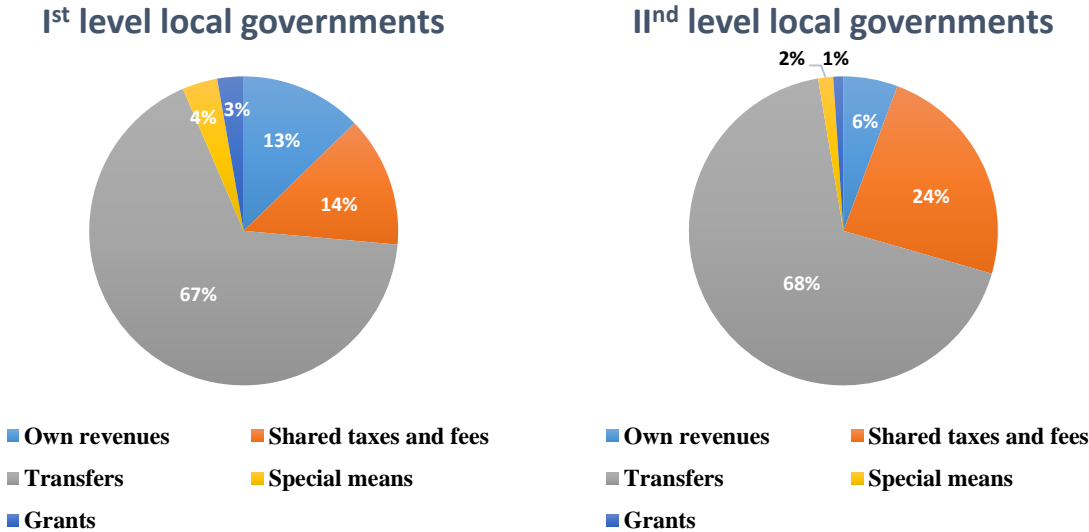
3. Local Government Own and Shared Revenues

According to the Law No. 397-XV on Local Public Finance, Article 4(1), the revenues of the administrative-territorial units' budget consist of:

- Own budget revenues that consist of local taxes and fees, property tax and other fiscal and non-fiscal revenues;
- Shared tax and fees;
- Special means/special funds
- Transfers from the state budget, rayon budgets;
- Grants/Borrowings.
- Revenues from property sale and privatization.

Figure 2 presents the share of revenues components in total revenues in year 2014 for I and II levels local governments.

Figure 2: The share of revenues components in total revenues, year 2014, %



Source: Elaborated by author according to the Ministry of Finance report on the execution of administrative-territorial units budgets year 2014. Note that the ATU I budget is calculated separately from the ATU II budgets.

As there are no preliminary data for 2015, a recent report which analyzed the effect of fiscal decentralization in the pilot regions shows that the new reform generated a number of interesting trends. As such, shared taxes decreased significantly while transfers increased significantly in the pilot regions. This tendency is primarily due to the modified inter-budgetary relations where income tax of legal entities is no longer shared. Public institutions are now financed via special transfers, which were introduced with the new law.

3.1. Own revenues

The budget classification does not contain such category as own revenues, and usually they are calculated as sum of local taxes and fees, property tax and other fiscal and non-fiscal revenues, and are transferred in whole and directly to the local governments budgets.

Local taxes and fees are stipulated in the Chapter VII of the Tax Code, and every year local government must establish these taxes/fees according between minimal and maximal levels from the Tax Code. This category of own revenues represents about 30-40% from amount of own revenues. The Chapter VII of Tax Code defines local fees as being “an obligatory payment made to ATU budget¹⁴. Article 288 states a number of definitions establishing the subjects and objects of local fees’ imposition. Till 13 January 2012 the Law determined 12 local fees categories, but with the amendments based on Law No 267 on December 23, 2011 five new categories of fees are introduced.

Thus till 2011 on the base of article 289 (2) the following 14 tax categories were in place:

- a) Fee for land management (territory accomplishment tax);
- b) Fee on auctions and lotteries organization on the territory of the administrative territorial unit;
- c) Advertisement fee (on placement of advertisement);
- d) Fee for application of local symbols;
- e) Fee for commercial and/or social services units;
- f) Market fee;
- g) Lodging fee;
- h) Resort fee;
- i) Fee on passenger auto-transport services on the territory of municipalities, cities and villages (communes);
- j) Parking lots’ fee (for physical or legal persons rendering such service);
- k) Dogs owners’ fee;
- l) Parking fee;
- m) Fee for solid waste removal;
- n) Fee on publicity devices.

While property tax (land and real estate tax) is also a local own source revenue, it is regulated in a different chapter of the Fiscal Cod (namely chapter VI, articles 276-287). Local taxes, on the other hand, are regulated in chapters VII of the Fiscal Code (art. 288-298). Figure 2 presents the share of revenue components in total own revenues.

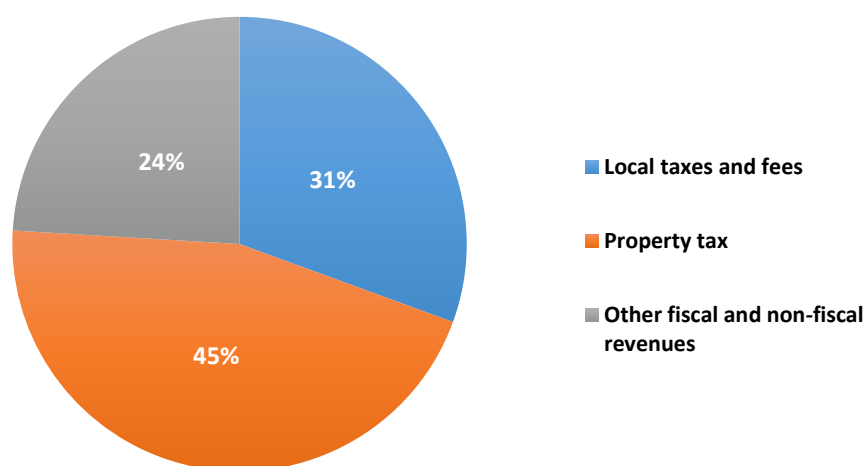
Figure 2 shows the structure of the total own revenues of the Ist level local government. Property tax is also regulated by the Chapter VI of the Tax Code. Property tax is divided in tax on lands and tax on real estate. First level local governments, Chisinau and Balti collect the property tax. According the Tax Code property tax represents “local tax which is an obligation towards budget deriving from the value of real estate goods.” The Tax Code sets the objects, subjects and tax rates for the purposes of property taxation. Real-estate tax objects are land, houses, buildings, apartments etc., including

¹⁴A.Secieriu, A.Casian, A.Petroia. Local public finance through the perpective of financial decentralization in Moldova. Chisinau, 2010. pp. 21

buildings, what construction is in process of finishing (50% and more) and is in construction more than 3 years. Subjects of real-estate taxation are both physical and legal persons.

Tax is calculated from estimated cadastral value of the property. Territorial cadastral administrations are responsible for property evaluation and re-evaluation according unified methodology. The Law stipulates that territorial cadastral administration every three years makes re-evaluation of property. In fact the situation is different. Actual evaluation of cadastral value of property is done mostly in the cities and rayon centers and did not cover most of the villages and individual housing (which includes expensive villas as well).

Figure 2: The share of revenues components in total own revenues, year 2014, %



Source: Elaborated by author according to the report on the execution of administrative-territorial units budgets year 2014

The Law establishes a minimum and a maximum tax rate. At the same time local public administration authorities can establish their property tax rate within the limits set by the Tax Code. It is custom to set property tax rates at the minimum in villages and communes, while in cities these are slightly higher but not at the maximum. The Law envisages tax exemptions. At the same time the Law regulates tax exemptions awarded by LPA authorities.¹⁵

Article 280 of the Chapter VI of the Tax Code sets the following minimum and maximum tax rates:

- In municipalities and town: min 0.05% - max 0.3% from the taxable value of the real estate;
- For the agricultural land with constructions on it – min 0.1%– max 0.3% from the taxable value;
- For other real-estate objects – 0.1% from the taxable value.

Under category of *non-fiscal own revenues* (about 20-30% from amount of own revenues) related to local budgets are assigned:

- other income from entrepreneurial activity and property (such as: payments for rent of natural resources, for agricultural land and land for a purpose other than the agricultural, rent of public assets, other property income etc.);

¹⁵A.Secrieru, A.Casian, A.Petroia. Local public finance through the perspective of financial decentralization in Moldova. Chisinau, 2010. pp. 20

- administrative taxes and payments (includes revenues received from collection of the state fee, local fees and other charges and administrative payments);
- fines and administrative sanctions (this chapter includes income received as fines, penalties and administrative remedies imposed by the court institutions and other competent bodies in supervision and regulations. Fines and penalties related to the calculation of certain tax or fee is included in the record together with the tax or fee to imposing the fine);
- other unidentified receipts.

Capital revenues are predominantly used by LPA to cover their budget deficits when necessary. Revenues from sale and privatization of public property take 90% of the capital revenues structure and have accounted for over 236 mln MDL which is by far the largest share. Over 62.7% have been collected by LPA I while the rest by LPA II. Revenues from public property rent are part of the own revenues.

Revenues from local property management are relatively evenly distributed throughout the country. While in rural areas, revenues from land taxes are dominant, in urban areas building taxation is the main revenues driver. Unlike many other European countries, Moldova does not face the problem of the concentration of property tax revenues in urban regions. With the increase in revenues from real estate tax, there is an increased risk of territorial concentration of such income in urban areas where property value is greater. However, special equalization transfers, which are already part of the Moldovan system of local finances, should offset this development.

3.2. Shared taxes and fees

The system of shared general state taxes (duties) and fees to the local government budgets, includes: income tax and fees to the Road Fund.

Until 2014, the income taxes (personal and corporate taxes) were shared in the local budgets in a different proportions established by Ministry of Finance. In 2013 were operated some changes in the Law on local public finance no.397/2003. The operated changes determine that the corporate income tax will be transferred in whole and directly to the state budget, but personal income tax will be transferred in a proportion of 75% to first level local governments and 25% to the second level of local government from the total amount of income tax collected on the territory of the administrative territorial unit. For Chisinau and Balti municipalities was established a proportion of 50% and respectively 45%, and for residence towns (the towns where the rayon council is located) a proportion of 20% from total amount of personal income tax collected on their territories. Therefore, clear proportions were established in legislation for tax breakdown of individuals. As of 2015 breakdown of taxes to businesses flows 100% towards the state budget, while until 2014 these were transferred only partly (shares set by Ministry of Finance). These were replaced by special transfers to finance preschool, primary, secondary, special, and complementary education, as well as other delegated powers.

According to Law nr. 435 on administrative decentralization and local autonomy, local authorities are entitled to manage and regulate under their own responsibility and in the interest of the local population, an important part of public affairs. Financial and budgetary autonomy is the right of local authorities to have sufficient own financial resources and use them freely, under the law, by adopting their own local budgets and setting taxes, tariffs and user charges.

It is important to note that local tariffs and user charges are set based on political, rather than economic, principles. These, in most cases, do not cover expenses and as such most of the service

provision enterprises risk bankruptcy. For the Chisinau Municipality, local tariffs and user charges are set by the National Agency of Energy Regulation of the Republic of Moldova.

Most municipalities registered a satisfactory level of collection of taxes in the local budget, however, these do face some difficulties in forecasting and collection of taxes. Some APL recorded a collection level higher than planned while others - lower than planned in the initial budget as approved. In recent years, there was a tendency for collection rate of taxes to reach 100%. Weaknesses are caused in particular by the lack or poor quality databases of individual taxpayers and businesses, which would allow better forecasting of income taxes. At the same time mayors do not use sufficient means of disseminating information on tax liabilities which would contribute to an effective local budget collection.

Management of public property is characterized by a medium level of inventory and registration of public property. In most municipalities there is a specialist or service responsible for managing public property and records. In about half of the APLs there is compliance with a set of procedures for recording public property and a local register of public property has been developed. The registry contains annual reports, collected until April 15, on public property under the administration of the Public Property Agency. Most public land and real estate are inventoried by municipalities at a rate of 60-80%, but their body cadastral registration records a much smaller proportion. The entire public patrimony is managed by City Hall and its subordinate institutions. Public tenders are organized for sale of municipal heritage. The resources obtained from auctions are usually used to cover the budget deficit. Records show low recovery of public assets through investment projects.

Following our analysis above, we present the areas of local own source and shared revenues benchmarking at international and local level in Appendix.

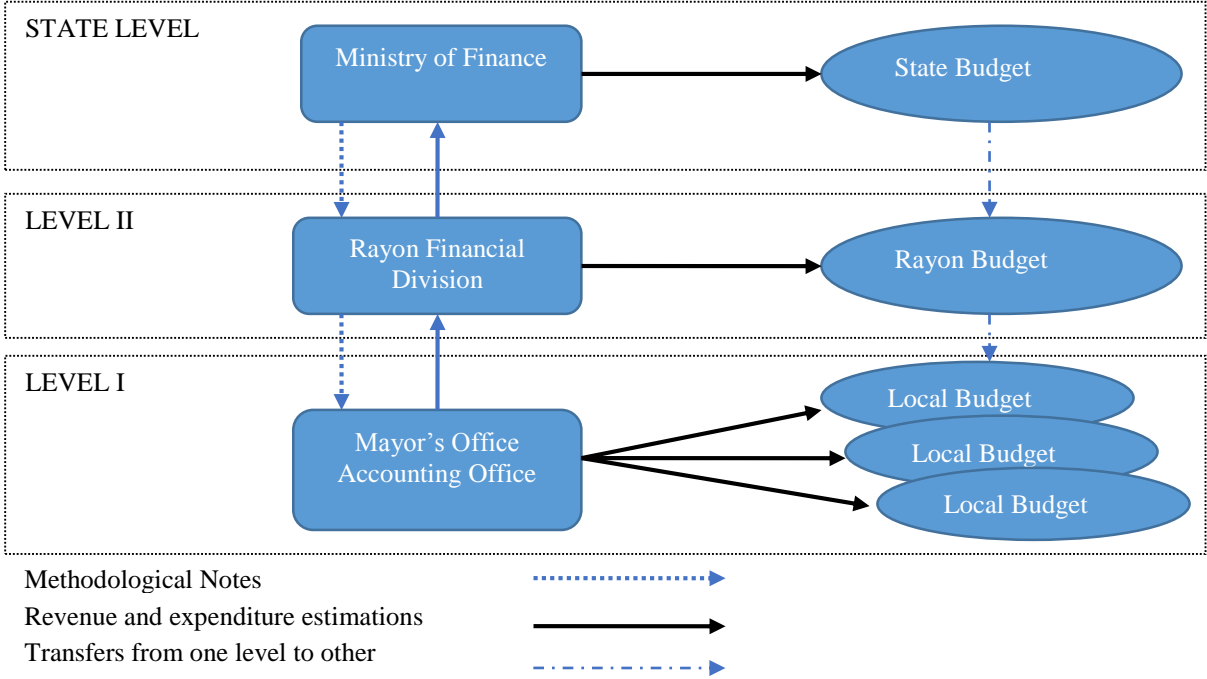
4. Intergovernmental Transfers, Fiscal Equalization

Central government transfers are the main source of revenue for local government. The analysis of the current system of local finances proved that the financing of local public tasks is dependent on major transfers from the state budget (in 2014 - 64% of total local revenues, including Chisinau and Balti, and 68%, excluding these two municipalities), making them financially weak in performing their responsibilities.

The Law on Local Public Finance (article 1) defines that transfers is financial resources allocated, with final claim and absolute amount, as provided by law, from the state budget to the administrative territorial unit budgets, for leveling the financial possibilities of administrative-territorial units for the purpose of performing the established public functions, financing of the activities performed by local public authorities, or for other special purposes.

Until 2014, the transfers were shared in the II level local government budgets in a different proportions by established Ministry of Finance. The amount of funds received by first level local governments from intergovernmental transfers and shared revenues was solely determined by second level local governments. It was a process of negotiations between 1st and 2nd local governments, before the transfers were made and it was highly dependent on political colour of the mayor of I level local government and unclear rules rather than on objective criteria.

Figure 3. Transfers system before changes in Law on local public finance

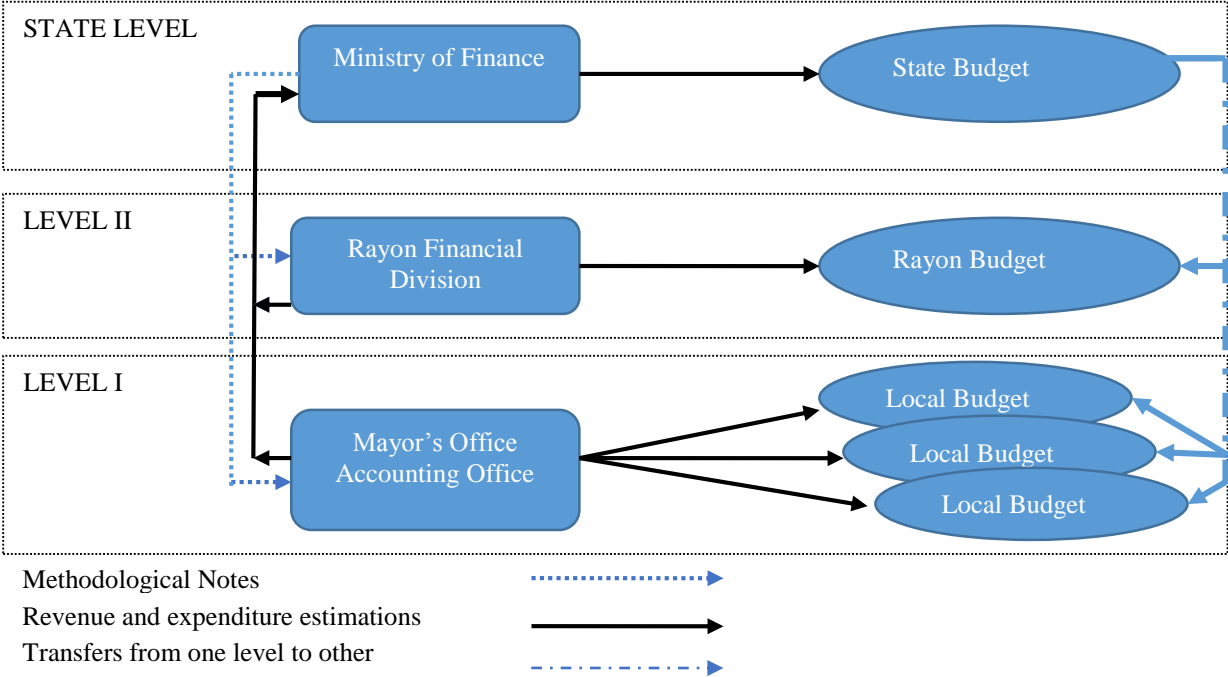


Source: Intermediary progress report on Moldova Intergovernmental Fiscal System, page.40

In 2013 were operated some changes in the Law on local public finance no.397/2003. In 2014, the UATs from 4 rayons (about 78 LPAs) had implemented the new system of local public finance. From 2015, the system is implemented across all LPAs from the Republic of Moldova. The operated changes established a new formula for calculation of general transfers, which represents the financial resources allocated with final claim and absolute amount from the state budget to the rayon's budgets, to finance their own spheres of activities.¹⁶ Therefore the Ist level local governments can easily calculate the amount of transfers they must receive. In addition, the new Law on local public finance define a new category of transfers – special transfers. Special transfers represents transfers is financial resources allocated, with final claim and conditioned amount, as provided by law, from the state budget to the administrative territorial unit budgets, to ensure the exercise of public functions or for other special purposes delegated by the state.

¹⁶ To be more precise, until 2014, transfers were calculated not only based on the local taxes (listed above) on which the LPA has decision powers. Any increase in property or other fiscal and non-fiscal revenues would diminish the transfer flows. As such, LPAs had no incentives to facilitate own revenue increases. The new law, on the other hand, creates incentives to LPAs to identify new revenues sources as the more revenues are collected the more LPAs can spend on service provision and infrastructure improvements. The transfers are stipulated by law and are unaffected by collected revenues. These changes have increased the fiscal autonomy of an LPA by 6-8 times due to increased flexibility in setting rates and fees on income and property taxes for individuals.

Figure 4. Transfers system *after changes in Law on local public finance*



Source: Intermediary progress report on Moldova Intergovernmental Fiscal System, page 40

To be more precise, general transfers (equalization) for the LPAs of level I are based on three indicators, namely: (i) fiscal capacity per capita (measured as revenue collected from tax deductions on personal income per capita), (ii) area of the LPA, and (iii) population. Moreover, the new equalization formula also relies on a number of relative indicators. These are presented along the corresponding formulae in Appendix 7.3.

4.1. Special means

Special means represent revenues obtained by public institutions, under conditions approved by the regulatory acts, from the work undertaken and services delivered, as well as donations, sponsorships and other funds properly come into possession the public institution. These financial means represents up to 5% in total revenues of local governments.

The Appendix summarizes the main benchmarking areas in fiscal equalization and grant allocation.

4.2. Local Borrowing

4.2.1. Grants

Grants are financial flows that are allocated to local governments, most often by the central governments. They can also come from federated states in federally-structured countries, from other local governments or from foreign or international sources. Several types of grants exist however which have a more or less limiting effect on local autonomy. Grants are currently distributed through the so called Extra-budgetary Fund, which comprises funds from various international donnors into, for example, Regional Development Fund, National Environment Fund, Energetic Efficiency Fund, etc.

Financing through grants is generally considered as being unfavorable to local autonomy in that local governments remain dependent upon the authority allocating these grants. However, transfers from the central state form the largest share of grants received by local governments. So not the mere size of central budget grants, but more the methods of allocation define the local fiscal autonomy. Interestingly, even under the new fiscal decentralization law, the rules of grant allocation are not clear, as a straightforward formula is yet inexistent.

4.2.2. Borrowings

Loans are one of sources for local government capital investments. However, access to the borrowing by the local governments has not yet evolved very much in Moldova. Table 2 summarizes the borrowing levels across UATs of level 1 and 2.

Table 2: Borrowing for Local Public Administrations in Moldova (2014, in thousand MDL)

	Total TAU level 1	Total TAU level 2	TOTAL
Internal Financing Sources (Internal Borrowing)	-7,325.04	-1,435.48	218.0453
External Financing Sources (External Borrowing)	-	3,072.517	3,072.517
Public Property Sale and Privatization Proceeds	148,000	88,252.58	23,6252.6
Account Balancing	45,880.92	-65,458.6	-19,577.7
Temporary Financing from the Budget	673.6465	742.1528	1,415.799
TOTAL	26,0536.7	156,090.4	95,467.71

Source: Elaborated by author according to the report on the execution of administrative-territorial units budgets year 2014

The Law on Local Public Finance (2003) determines the rights of local governments to take long-term or short term loans or float bonds for capital expenditures upon the decision of the corresponding representative and deliberative authorities. This applies to loans from domestic or foreign financial institutions. The law specifies that within the loan agreement revenues to repay the interest and principal must be identified from the jurisdiction's own fiscal revenues. The law is also clear that the central government may not act as a guarantor of loan repayment. Article 14 specifies that the loan may not exceed 20 per cent of the total annual own revenues, what is often recognized requirement in other countries, too. Contrary, for current expenditures, LPAs can borrow up to 5% of the approved revenues for the given year. The maturity of these loans is by law within the same year of the said budget.

Access to the borrowing by the local governments has not yet evolved very much in Moldova. Considering the large number of the village (commune) local governments in the rural areas, their low revenue potential for some time in future, lack of administrative capacity and mere absence of financial and capital market, it appears that the borrowing option is far from reality for the local governments. As a result, they may have to continue depending on central transfers to bridge the fiscal gap. The situation with municipalities (in particular in Chisinau) where the residents' awareness and the ability to pay for the service is relatively high might be different.

Article 13 of the Local Public Finance Law nr.397 stipulates that executive authorities on the basis of the representative and deliberative decisions have the right: to borrow loans for current expenses with maturity in the same budgetary year, from financial institutions and other creditors both in country and abroad, and the total volume of loans for current expenses due on the same budget year should not exceed 5% of total revenues approved (corrected) of the administrative-territorial unit budget, which is a prerequisite. However, Article 14 of the same law states that executive authorities under the representative and deliberative decisions have the right to borrow short-term and long-term capital expenditure from financial institutions and other creditors both from our country and abroad, may contract by issuing bonds, short-term loans and long-term capital expenditures if the total amount of annual payments (repayment of principal, interest and other payments related payment) related to debt

servicing unit budgets territorial administration to contracted or guaranteed loans and/or to be contracted or guaranteed shall not exceed 20% of total annual revenue of the respective budgets.

5. Local Financial Management

Presently in Moldova the practice of negotiations is not an established element in relations between central government and LPAs. Such practice could be introduced in the course decentralization reform process. At the same time practice of consultations is rather common and has different informal forms.

Subjects of consultation and agenda of those consultations depend on existing legislation and existing budget creation practice.

5.1. Budgetary consultations

In annual budgetary consultations in central level local governments are represented by rayons, but each rayon organizes consultations with the first level local government representatives. Budget consultations undergo the same stages as budget preparation and approval.

Total necessity of financing corresponds to the sum of necessities for particular LPA of second level, which is an object of central budgeting. Total necessity corresponds also to the particular LPA of the first level, which is object of rayons' budgeting.

Consultations started by technical meetings (and gathering data) between financiers from LPA of the first level with financiers from rayons. They prepare data for calculation of budgetary needs of consolidated rayons' budget.

After calculations of rayon's needs technical meetings (and gathering data) between financiers from second level LPA and corresponding officials from the Ministry of Finance take place. After gathering data about situation it is possible to calculate total needs for the centrally planned revenues of consolidated local government's budget.

Total calculated necessity must be balanced with budget feasibility. On the basis of that feasibility system of normative could be corrected each year. Discussion in the technical level is about local government needs to increase staff or to introduce new activities in its territory.

Fundamental feature of Moldova system is the principle of multi-level budget. If budget is multi-level, then central government attempts to ensure necessary expenditures for all local governments and proposes total budget to the parliament, which consists of central government budget and rayons budgets plus budgets of Chisinau and Balti.

When new set of normative is prepared (the set of previous years can be preserved), then central government has the proposal for 35 second level LPAs. Ministry of Finance organize consultations with rayons' presidents. Each head of second level LPA can express his position and ministry can agree or not about needed changes.

Better form for building common position is consensus. That is not always possible, because usually economic interests are different for variety of local governments of different types, different size and different financial capacity. Experience of the LALRG show, that achievement of common opinion sometimes takes large efforts from all sides. Preferable is also to achieve common opinion with central government, at least partly.

Broader involvement of associations will be logical, if decentralization of local budgets will be implemented. That will be also one of the goals for a new equalization system.

There were several LG associations during the period from 1990-s in Moldova. Until creation of CALM different types of local officials joined in their associations in the capacity of physical persons. Several associations of such kind are also represented as collective members of present CALM. Organizational form of CALM - association of public legal entities is much better form to negotiate on behalf of all local governments.

Until 2013, APL had discretion over spending the income from local taxes only. Therefore local autonomy in public spending was limited. In 2014, after the implementation of a new fiscal system in 78 pilot APL's, this autonomy has increased. As the law has been implemented as of 2015 throughout the entire country, it is expected a similar trend nationwide. In the new system, the local autonomy increased significantly. APL now have decision-making power over collected revenues from: property taxes, income from lease of public property, deductions from citizen's income tax and on transfers of general purpose, which can be calculated unaided by LPA according to formula specified in the legislation. The LPA have greater resources to fulfill their competencies and establish priorities for independent choices over the use of public funds. Control and monitoring of budgets is carried out by preparing and submitting quarterly reports of the budgets and annual presentation of reports on budget implementation.

Municipal enterprises providing public services, recorded a low level as organizational and financial management. The delegation of powers of public services is carried out by signing a contract of delegation of powers between APL and municipal enterprises. Usually businesses are not generating profits and APLs do not have sufficient human resources to monitor their activity. Currently in Moldova, there are inter-municipal cooperation initiatives between several locations, which improve public services (utilities) to citizens and provide economies of scale.

Information on tax liabilities is not sufficiently disseminated to ensure an adequate level of information for citizens on tax obligations. The most used methods of disseminating this information are: Mayoralty panels, City Hall's website (if any), TV, newspaper or local radio. Most municipalities use all budgetary classification (functional, economic and organizational) required by law in the budgetary process. But not all APL take into account all budget documentation (macroeconomic indicators, inflation, currency, economic development and social assumptions, previous budget, the amount of debts, estimating the impact) in the drafting, approval and execution of the budget. The transparency of the budget process record is low. The budget documents required by law to be presented to the public include: the village budget, the annual report on budget execution quarterly reports on budget implementation reports and external audit reports on public procurement. The most frequently presented documents to the public are: the village budget and annual report on budget implementation. The remaining documents should be available to the public. The methods of presenting such information are panels in the City Hall, City Hall's website (if any) public debate. According to a previous survey, 5% of citizens know which village budget and how public money is spent.

In most LPAs, the budget is running at a rate higher than that originally approved. Municipalities record deficiencies in budgetary expenditure control and budgetary planning and execution. Municipalities allow offsetting main categories of expenditure at the expense of others and allow arrears for goods and services. The Auditor's Court is the only authorized public institution that controls the formation, administration and use of public funds and public property management by providing external audit in the public sector as a supreme audit institution. The Auditor's Court work program is planned independently by it for a period of 1 and/or 3 years.

Resolving conflicts of interest is a huge issue for local governments in Moldova. Conflicts of interest and incompatibility are regulated by the Law on Conflict of Interest No. 16 of 15.02.2008. According to the General Investigations Division of the Prosecutor General of the Republic of Moldova, during the checks it was brought to light an enormous number of cases of incompatibilities for public office, when the leaders of local government occupied also other functions and carry out other activities, including holding positions in management bodies of commercial structures. In the old system of formation of local budgets, budgets of LPAs of level I were dependent enormously on the second level budgets. Given that the share of transfers in the budget of LPA level I is an average 60% of own resources, independent decisions could not be exercised. Therefore, this has created a huge dependency towards level II TAU's. Thus to obtain benefits and advantages, not the personal need for the community were relevant, but the strong connections within the party or special personal relations with people with political decision makers. So getting these benefits was depending on political affiliation and relationships with party leaders. The new fiscal system of local budgets, LPA's can obtain general transfers calculated by the formula stipulated in the law and the subordination to LPA's of level II disappear. Thus transparency in the allocation of transfers has increased considerably compared to the old system.

Most LPAs have a very low financial management capacity, particularly towns/villages. Towns recorded a higher capacity compared to towns / villages in 2014. Most municipalities in cities have a person/department responsible for writing and project management with internal and external financing. In the mayoralties of villages the situation is worse, but there are a few exceptions as some villages record high skill levels of financial management. Major issues recorded in writing and project management are the lack of trained personnel in the field, lack of knowledge, lack of partners, the language barrier, too large proportion of co-financing. Most villages do not have sufficient investment opportunities. As such, they start cooperation initiatives and public-private partnerships, creating new services for localities.

6. Implementation of LFB

Local Finance Benchmarking is designed to facilitate comparison between decentralized local governments. By definition, the more decentralized an LPA is, the easier the implementation of LFB and the more benefits it could potentially have on national and local governments activities. To better understand the process of LFB implementation in Moldova we summarize below the main issues related to data sources, potential problems and obstacles at national and local levels

6.1. Information, datasets for comparison

A summary of information and datasets for analysis and comparison of local authorities' activities is presented in a report on the Assessment of the available municipal level data and information sources by Gabor Peteri and Ana Popa. Appendix 7.9 summarizes the available data sources with appropriate additions where necessary.

6.2. Problems and obstacles in LFB implementation

While the benefits of LFB implementation are straightforward for a decentralized government, there are still obstacles that might minimize the expected effect of such a policy design. In Moldova, the main obstacles are related to: (i) lack of incentives, (ii) lack of competence, and (iii) lack of public interest.

While fiscal decentralization is now fully functioning in Moldova (as of 2015), the full potential of this reform is yet widely misunderstood by many local civil servants. A recent study of the pilot regions shows that although local budgets face some improvements, the benefits of fiscal decentralization have not been fully taken advantage of by the local governments. This leaves two potential issues that might be related to LFB implementation as well.

On one hand, local civil servants might have *insufficient competences and skill* to fully understand the complexity of LFB implementation and as such the benefits it might bring to local and national development. On the other hand, not being fully aware of the benefits and the essence of LFB implementation might minimize the incentives local governments have to fully adhere to an objective local, national, but also international comparison.

These problems could be overcome either by organizing special training programs that would develop the required skills and understanding related to the benefits of local finance benchmarking or by creating incentives for civil servants via increasing the public awareness of the population about the LPA's activities. However, as a recent UNDP survey shows, while a vast majority of population (around 70%) knows their rights to be informed about the LPA's activities, only about 10% of the population actually does so. Thus, more intense policy initiatives are required to facilitate citizen's involvement in the local government's activities.

7. Appendix

7.1. Local Government Functions

According to the Law on Administrative Decentralization (article 4) the first level local governments are responsible for:

- a) urban planning and management of green spaces of local interest;
- b) household waste collection and management, including the sanitation and maintenance of lands for its storage;
- c) distribution of drinking water, construction and maintenance of the sewerage systems and of used water and rainwater treatment systems;
- d) construction, maintenance and lighting of streets and of local public roads;
- e) local public transport;
- f) planning and maintenance of the cemeteries,
- g) administration of local public and private assets;
- h) building, management, maintenance and equipping of preschool and extra-scholastic institutions (crèches, kindergartens, art schools, music schools);
- i) development and management of the urban networks for gas and heat distribution;
- j) cultural, sports, recreation and youth activities, as well as planning, development and management of the infrastructures needed for these types of activities;
- k) planning of the agricultural markets, of the trading spaces, accomplishment of any other measures necessary for the economic development of the administrative-territorial unit;
- l) setting up and management of the municipal enterprises and organization of any other activity necessary for the economic development of the administrative-territorial unit;
- m) building of houses and providing of other types of facilities for the socially vulnerable people, as well as for other categories of people;
- n) organization of the fire services.

The Law also determines that second level local governments are responsible for:

- a) administration of the public and private assets of the district;
- b) planning and administration of the construction, maintenance and management works of some public units of local interest;
- c) construction, management and repair of the roads of district interest, as well as of the road infrastructure;
- d) organization of the passenger road transport, management of the bus stations and stops of district interest;
- e) establishment of the general framework for the territory development at district level and protection of forests of district interest;
- f) support and stimulation of the initiatives referring to the economic development of the administrative-territorial unit;
- g) development and implementation of projects for the construction of interurban gas pipelines (including the gas pipelines of medium pressure), of other thermal power units of local destination;
- h) administration of cultural, tourism and sports institutions of district interest, of other activities with educational, cultural and sports character of district interest;
- i) administration of the municipal enterprises of district interest;
- j) administration of the social assistance units of district interest;
- k) development and management of the community social services for socially vulnerable people, monitoring of the quality of social services.

7.2. Domains of Local Government Functions

The main domains of local government functions are summarized below:

Communal Services:

- 1) Producing, transport and distribution of drinking water; management of sewage systems, including water treatment plants;
- 2) Collection, transport and disposal of garbage, including the management of landfills;
- 3) Management and maintenance of public parks, green areas and cemeteries;
- 4) Public lighting.

Public Transport and local/rayonal Roads:

- 1) Management of the public transport system within locality and/or rayon;
- 2) Maintenance of locality and rayon roads (streets).

Territorial and Urban Planning:

- 1) Designing, up-dating, implementation, monitoring urban plans;
- 2) Territorial planning;
- 3) Public constructions/social houses.

Local Economic Development and Management of the Public Property:

- 1) Designing and implementation of local economic development strategies;
- 2) Organizing and managing local public enterprises;
- 3) Management of the public property in the ownership of local government units, including renting and concession.

Public Utilities:

- 1) Management, maintenance and development of heating systems;
- 2) Participation to the development of gas network;
- 3) Participation to the development of electricity network.

Pre-university Education:

- 1) Maintenance of the buildings and facilities of pre-school education;
- 2) Maintenance of the buildings and facilities for extra-school activities;
- 3) Delegated function from the state to finance pre-university education.

Social Services:

- 1) Planning, financing and providing community social assistance services at primaria level;
- 2) Planning, financing and providing specialized social assistance services at rayon level.

Public Health Services:

- 1) Public health education;
- 2) Participation to the development of public health network;
- 3) Designing and implementing local strategies in the domain of public health.

Human Rights, Gender Equality and Social Inclusion of Vulnerable Groups:

- 1) Implementing at local level the national policies regarding human rights, gender equality and vulnerable groups protection.

Marital Status Services:

- 4) Issuing, recording, modifying, annulation of marital status documents;
- 5) Managing the data basis and the archives of marital status documents.

Civil Defense and Emergency Situation Services:

- 1) Implementing the national policies referring to civil defense and emergency situation;
- 2) Public information activities in this field.

Environment Protection:

- 1) Implementing the national standards of environment protection referring to drinking water supply and sewage, garbage collection and disposal, landfill management;
- 2) Ecological re-construction of damaged areas under local government ownership;
- 3) Implementing the national policies referring to protected areas.

Public Order:

- 1) Cooperation with the national police – establishing an administrative commission in this domain.

Agriculture and Veterinary Consultancy Services:

- 1) Cooperation with deconcentrated services in the field of food safety activities and epizootics.

Culture, Youth, Sport and Leisure Services:

- 1) Management and financing the local/rayonal cultural institutions: libraries, museums, theatres;

- 2) Building and maintenance of sport and leisure facilities/infrastructure;
- 3) Planning and financing the sport and youth activities.

National Defense:

- 1) Responsibilities in preparing the territory for defense;
- 2) Financing the recruitment centre

7.3. General Transfers (Equalization)

In Moldova, the amendments to the Law no. 397-IV of October 16, 2003 on Local Public Finance and Tax Code 1163-XIII of April 24, 1997, there have been significant changes in the way of budgeting administrative units both income formation ATU budgets and the expenses. Completely new is the method of calculating equalization transfers and transfers to special purpose. The new vision creates real opportunities for strengthening the financial autonomy and fiscal decentralization.

The transition to the new formula of budgeting administrative units has started drafting ATU budgets for fiscal year 2014. For this purpose, all administrative - territorial units of Republic of Moldova received indication from the Ministry of Finance to prepare draft budgets for fiscal year 2014 in two variants: Variant I - the existing formula and variant II - after the new funding formula. Distinct budgeting for administrative territorial units highlights new conditions determined by the new method of calculating general transfers (equalization) and special transfers for both: level I and level II.

- Talking about calculating the general transfers (equalization) for administrative territorial units (ATU) of first level is noted that for the calculation of equalization transfers are counted three financial indicators, such as: Fiscal capacity per capita (measured as revenue collected from income tax deductions of individuals and number of inhabitants of ATU);
- Concrete land area;
- Number of population of a specific territory.

These indicators find expression in the new formula for calculating general transfers (equalization) In addition to these indicators "local" in the formula are found weighted indicators specified as:

- PS_{CFL}^1 : specific weight indicator per capita of fiscal capacity;
- PS_p^1 : specific weight of the population indicator;
- PS_s^1 : specific weight of the area indicator;
- P_e : supraunitar parameter.

where $PS_{CFL}^1=60\%$, $PS_p^1=30\%$, $PS_s^1=10\%$, and $P_e=1.3$.

Below we present the method of calculating equalization transfers for ATU level I (A); level II (B) and special purpose transfers (C).

A. Calculation of general purpose transfers (equalization) for ATU first level:

$$TE_i = FEB_1 + \left[\left(PS_{CFL}^1 + \frac{P_e \times CFL_n - CFL_i}{\sum_i P_e \times CFL_n - CFL_i} \right) + \left(PS_p^1 \times \frac{P_i}{P_n} \right) + \left(PS_s^1 \times \frac{S_i}{S_n} \right) \right],$$

where

- TE_i - balancing transfer for some ATU of first level;
- FEB_1 - ATU budget fund balance of the first level;
- CFL_i - per capita fiscal capacity of some ATU first level;
- CFL_n - the national average per capita of fiscal capacity;
- P_i - population of a certain ATU of first level;
- P_n - total population of administrative-territorial units of the first level;
- S_i - particular area of the first level ATU;
- S_n - total area of the administrative units of the first level;
- PS_{CFL}^1 - specific weight of indicator per capita of fiscal capacity;
- PS_p^1 - specific weight of the indicator population;
- PS_s^1 - specific weight of the indicator area, and
- P_e is the supraunitar parameter.

B. Transfers of budget balancing for ATU of second level

FEB_2 is intended to balance budgets of ATU of second level and is distributed according to the following indicators:

- population;
- the area ATU, according to the formula:

$$TE_j = FEB_2 \times \left(\frac{PS_p^2 \times P_j}{P_n} + \frac{PS_s^2 \times S_j}{S_n} \right)$$

where

TE_j - balancing transfer for some ATU of second level;

FEB_2 - ATU budget fund balance of the second level;

P_j - population of a certain ATU of second level;

P_n - total population of the second qualifying assignment;

S_j - particular area of the second level ATU;

S_n - total area of the second qualifying assignment;

PS_{CFL}^1 - specific weight of indicator per capita of fiscal capacity;

PS_p^1 - specific weight of the indicator population;

PS_s^1 - specific weight of the indicator area.

Calculation of general purpose transfers (equalization) for ATU of second level is directly proportional to the population and ATU area, balancing local budgets being qualified to the second level, with the exception of municipal budgets Chisinau, Balti and autonomous territorial unit budget (ATU) with special legal status.

C. Special purpose transfers

Special purpose transfers from the state budget is allocated to ATU budgets for funding:

- a) primary, secondary, general, special and (extracurricular) education;
- b) the power delegated to APL by the Parliament on the Government's proposal.

Information on special purpose transfers from the state budget to local budgets for financing primary, secondary, general, special and (extracurricular) education for 2014 and estimates for the years 2015 to 2016 are presented in Appendix. 2.2. to notes about the development projects of ATU budgets for 2014 and estimates for 2015 and 2016.

At present, establishing relations between the state budget and local budgets, transfers to finance powers delegated to APL are considered:

- a) social transfer payments;
- b) transfers to compensate for the difference in tariffs for electricity and natural gas (used by residents of localities Dubasari and Căușeni and Varna village from Anenii Noi district);
- c) transfers to compensate for lost revenues of ATU budget (... compensation of local budget income, budget of state social insurance and mandatory health insurance funds, missed about exempting landowners located on route Râbnița - Tiraspol.);
- d) transfers from the republican fund of social support of the population.

7.4. Summary of the proposed benchmarking areas: local own source and shared revenues

<i>Scope of fiscal decentralization: national systems</i>	<i>Local government financial resources, financial management</i>
Fiscal equivalence: scope of own revenues; diversity of tax base	Local taxes: significant, stable, simple
Tax decentralization: autonomy in rate setting and defining tax reliefs	
Autonomy in own revenue raising: regulatory methods, stability of national tax policies	Tax system audited: collection rate, coverage of taxpayers
Procedures of national tax policy design: openness, consultation	Local tax policy design, sound, open, legal (approved by elected bodies)
Economic impact: neutral, limited distortions	Capital revenues: separated, used for capital investments
User charges: scope, limits on access to services, local autonomy in charge setting	User charges are comparable to costs, support to disadvantaged users
Tax administration: local vs. central, administrative capacities, standard litigation procedures	Local tax administration: collection is effective, costs of tax administration
	Local records on assets and liabilities
	Organizational forms and management of local property
Tax sharing is origin based, supporting local tax efforts to increase the tax base	
Transparent sharing rules are set by law for a longer period	
Shared taxes are not earmarked	

7.5. Summary of the proposed benchmarking areas: equalization, grant allocation and local borrowing

<i>Scope of fiscal decentralization: national systems</i>	<i>Local government financial resources, financial management</i>
Complexity of intergovernmental transfer: expenditure and revenue based equalization	
Characteristics of grant allocation:	
<ul style="list-style-type: none"> • rule based or arbitrary; • transparent, understandable or too complex and managed internally by the administration, 	
stable, predictable for the local governments or often changing	
General grants vs. specific, earmarked grants	
Objective measures are used for calculating expenditures needs and local fiscal capacity	
Incentives created by the intergovernmental transfers: economizing on expenditures, increasing revenues	
Loans are used for capital investments	Loans are used for financing capital investments
Loans are repaid by local revenues, user charges generated by the project	Short term borrowing for cash flow management only
No national government guarantees	Compliance with the national borrowing limits
Regulations on local borrowing limits are set	

7.6. Summary of the proposed benchmarking areas: local financial and budgetary management

<i>Scope of fiscal decentralization: national systems</i>	<i>Local government financial resources, financial management</i>
Budgeting process, budget approval and implementation is regulated by law	Local strategies, multi-annual budget plans exist
Basic budget requirements are set and they operate effectively: balanced budget, separate current and capital budget	Budgeting methods support council decisions by providing analytical sheets, service performance information, consolidated reports on satellite organizations
Commercial activities of local governments are limited	Budgeting process is opened and participatory, allowing sufficient time for review
National government intervention in local budget planning and implementation is indirect, proportional and not excessive	Budget implementation is monitored and regularly evaluated.
Rules and procedures of financial recovery are in place and operate effectively	Budget report is independently audited.
Reliable budgetary information is available for the local administration and the general public	Internal audit system is in place and used.
Monitoring system of local finances is in place.	Relationship with the service organizations, commercial entities
Human capacity development needs are identified continuously	

7.7. Summary of available data sources and information available

<i>Information</i>	<i>Size, number</i>	<i>Level of disaggregation</i>	<i>Source</i>
1. Revenues			
local taxes	60	rayon, primaria	The rate of local taxes is available at http://www.fisc.md/CodulfiscalalRM.aspx
shared revenues	4	rayon, primaria	Ministry of Finance (MoF)
transfers, grants	app. 20	rayon, primaria	MoF
2. Expenditures			
administrative categories	4 levels, 475 entries	rayon, primaria	http://minfin.md/ro/BOOST/
functional classification	Main groups: 42 entries Level 2.: 232 items		
economic classification	Main groups: 52 items Level 2: 311 items		
programs	Level 1: 109 Level 2, sub-programmes: 243		
3. Balance sheet	assets: 91 liabilities: 65 extra balance: 23	Rayon, primaria	For rayons available at MoF, for primaria available at rayon level
4. ATU budget execution reports		rayon, villages city,	Form No. 524 Available at MoF
5. Special reports		Rayon, primaria	For rayons available at MoF, for primaria available at rayon level
staff			
use of special funds			
external funds for projects			
use of assets			
6. Utility companies		41 water companies MSW Public cleansing	Asociatia Moldova Apa-Canal (AMAC), Min. of Environment, Min. of Construction NBS
7. Housing stock		Primaria	NBS
8. Area		rayon, primaria	Cadastral Agency, 2009
9. Urbanization level (share of urban population,		Rayon, primaria	NBS, also can be calculated based on NBS and Cadastral Agency data

**population
density)**

**10. Length of
roads**

Rayon, primaria

NBS

Ministry of Economy

Source: Peteri and Popa, Assessment of the available municipal level data and information resources