



JANAAGRAHA CENTRE FOR CITIZENSHIP & DEMOCRACY

# Municipal Finance Reforms in India's Municipalities

A closed-door consultation, Bengaluru,  
Tuesday, 30 October 2018

Supported By



## BACKGROUND

Janaagraha Centre for Citizenship and Democracy, supported by Omidyar Network, Shakti Foundation and Dasra hosted a closed – door consultation on **Municipal Finance Reforms in India's Municipalities**. The workshop, held on 30th October in Bengaluru, brought together a select group of over 30 participants as domain experts from government and civil society to draw out and synthesize hands-on experiences to identify pathways to fast-track solutions in this sector. Our focus in this consultation was to quickly cover the diagnosis (“what’s the problem”), spend little more time on the technocratic solutions (“what to do about them”) and the most time on pathways to the solution (“how to get them implemented”).

This was envisaged as a full day convening, covering two sessions, Session 1 on **“Fast-tracking reforms in financial management of municipalities”** and Session 2 on **“Making municipal borrowings work in India”**. **The detailed background note, agenda and full list of participants is given in the annexure.**

# SUMMARY OF DISCUSSIONS

We have captured below a crisp action-oriented summary of discussions covering the opening plenary and both sessions. The purpose of this summary is to serve as the starting point for next steps and not as a comprehensive record of all conversations at the convening, which were extremely rich and perceptive and which we have separately recorded for reference and use. We would be happy to share those notes on specific request.

## 1. We must boost demand-side accountability

We need to undertake concerted efforts to boost demand for financial and operational information among citizens and civil society. Unless citizens demand for better services that meet benchmark standards and seek information on financial management, political and administrative leaders may not have adequate incentive to focus on and fast-track reforms to financial management. This requires significant investments to be made in communication and engagement with citizens on budgets, works, user charges etc. and also civil society consolidation.

## 2. We need to create demonstration effect of reforms in a geographic area; civil society needs to coordinate and confederate

There is a predominance of projects over reforms in public discourse on cities. In order to prioritise reforms, civil society organisations may need to close ranks, pick a specific geographic area (state, city), implement reforms over the medium-term and showcase the same. This “demonstration effect” will get political and administrative leaders to stand up and take note of the significance and impact of reforms. Both to create demonstration effect and to boost demand side accountability, we need to invest in regional or national platforms or networks that enable confederation of civil society to exert greater influence to fast-track reform agendas, and also as means to scale reform initiatives.

## 3. We need to engage elected representatives and political parties on city agendas and reforms

Elected councilors of city councils in their capacity as policy makers are largely left out of popular discourse on urban governance, financial management of cities and reform agendas. Civil society organisations need to undertake systematic efforts to develop simple and easy to understand learning modules with multiple language options for large scale and deep engagement of councilors on urban governance reforms, particularly on budgets, civic works and finances. We also need to engage with political parties particularly on their election manifestos and other agenda-setting processes.

## 4. We need to fix the basics, strengthen absorptive capacities of municipalities

Municipal finance reforms are fundamentally about getting the basics right, about ensuring that the daily, ostensibly small and routine activities are done well. Therefore, there needs to be a sharper focus in governments on these aspects. Civil society can contribute by getting engaged formally with governments and partnering with them in systematically strengthening financial management systems and processes. Secondly, even as we focus on enhancing revenue base and financial sustainability of municipalities, we need to concurrently enhance the absorptive capacities of municipalities. Some of the gaps/needs are

- a “blue book” which clearly delineates roles and responsibilities of municipal commissioners and their teams,
- fully integrated IT systems (rather than stand-alone applications), proper application of technology and process workflows to side-step the capacities challenge in respect of double entry accounting,
- specific ways to demonstrate utility of double entry accounting through revenue enhancement, improved asset management etc.,
- shorter cycle times for tendering and procurement to ensure timely utilization of funds.
- range of municipal staffing reforms
- financial management processes that are linked to outputs and outcomes (rather than just metrics on budget utilization)

## 5. We need to create an enabling ecosystem for ULBs to better understand the market, to diversify their financing options, including but not limited to municipal bonds

Engaging with markets judiciously can potentially drive greater accountability and financial sustainability in municipalities. Markets particularly bond markets over a period of time differentiate between good performers and bad performers. To begin with we need to create an enabling ecosystem for municipalities to understand and engage with markets. We need to systematically work on estimating capital needs of municipalities over the medium and long term, work towards improving % of municipal budgets to a predefined % of GDP, provide predictable fiscal transfers, provide support to understand financing options and evaluate them etc.

# AGENDA

Time	Agenda
10.30-10.45	Introductions
10.45-11.00	Context setting presentation by Janaagraha
11.00-11.30	Opening Plenary
11.30-13.00	<b>Track 1: Fast-tracking reforms in financial management of municipalities (Open Moderated Conversations)</b>
13.00-14.00	Lunch
14.00-16.00	<b>Track 2: Making municipal borrowings work in India (context setting presentation by The Bridgespan Group followed by open moderated conversations)</b>
16.00-16.30	Action agenda

## LIST OF PARTICIPANTS

Name	Designation	Organisation
Dr R. Vishal, IAS	Commissioner, RDWSS; Former DMA	Government of Karnataka
Nivedita Raju	Principal Accountant General	Government of Karnataka
Rajamani Muthuchamy, IAS (rtd)	Former Joint Secretary	Ministry of Urban Development
Dr Alby John Varghese, IAS	Commissioner	Thoothukudi City Municipal Corporation
Dr V.N. Alok	Associate Professor of Public Finance	IIPA, New Delhi
Chetan Vaidya	Former Director	School of Planning & Architecture, Delhi
Karanraj Chaudri	Advisor, Social Impact Investments	UNDP SDG Impact Finance (UNSIF)
Mohan Nagarajan	Senior Economist	The World Bank
Alok Shiromany	Senior Financial Management Specialist	Indo- USAID FIRE-D Project
Harsh Kothari	Senior Manager	Deloitte Touche Tohmatsu India LLP
Ravi Ratanpal	Fund Manager (Debt)	SBI Mutual Fund
RS Murali	Managing Director	MaGC, Bengaluru
Ashok Rao	Executive Director	MaGC, Bengaluru
Alok Prasanna	Senior Resident Fellow and Head	Vidhi Centre for Legal Policy, Bengaluru
Apoorva Goyal	Associate, Investments	Omidyar Network
Vivek Chandran	Programme Manager	Shakti Sustainable Energy Foundation, Delhi
Subalakshmi Krishnamurthi	Public Finance Consultant and Founder	Public Finance India
Ronak Sutaria	Founder	Urban Sciences
Anoop Nautiyal	Founder	Gati Foundation, Dehradun
Vivek Singhal	President	Meerut Citizens Forum
Antaraa Vasudev	Founder	Civis Vote
Milind Mhaske	Director	Praja Foundation, Mumbai
Kashyap Shah	Manager	The Bridgespan Group
Pritha Venkatachalam	Partner	The Bridgespan Group
Monami Chakraborty	Associate	Dasra
Deepak Batra	Partner	Batra Deepak and Associates, New Delhi
Sheetal N Singh	Coordinator	City Manager's Association, Karnataka
Swastik Harish	Head, Urban Practitioners' Programme	IIHS, Bengaluru
Jigisha Jaiswal	Research Associate	CEPT, Ahmedabad

## 1 Our analysis shows weak governance is the root cause of poor service delivery

The Annual Survey of India's City-Systems uses the City-Systems framework to diagnose the systemic ills that ail our cities and act as barriers to them achieving their true potential. ASICS looks at 83 parameters across City-Systems to present a picture of the readiness of 23 of India's largest cities in delivering high quality of life to their citizens. The findings are as follows:

1. Municipal Corporations are glorified service providers, not the 3rd tier of government as envisaged by the Constitution. Cities are tightly controlled by States, constitute neither a whole unit of Governance nor of the Economy.
2. Cities do not have a cogent definition in India; metropolitan areas not recognized; legitimate political leadership at a city-level is absent
3. Spatial Planning, including land management, and urban design in cities are characterised by poor technical capacities, outdated policy framework and tepid implementation; downstream impact on land-based revenues
4. Municipalities in India are weak institutions
  - Restricted powers
  - Handle only few functions, with the State covering several critical functions, services
  - Staffing is a critical and weak link; both quantity and quality
  - **Finances are scarce, most MCs are not financially self-sufficient; exacerbated by absence of robust performance measurement and audit/accountability mechanisms**
  - **Opacity in finances and operations, and lack of accountability for performance and service levels; absence of citizen participation**

## 2 Challenges specific to Municipal Finance can be categorized under 6 key heads

These 15 challenges, specific to Municipal Finance, listed under 6 categories are based on our findings from ASICS survey of 23 cities over 5 editions.

1. **Institutional Design**
  - a. No integrated view of city's finances; no integrated treasury management
2. **Fiscal decentralization**
  - a. Few eligible revenue streams; unpredictable transfers, SFCs largely dysfunctional
  - b. No control over tax rates and capital/base values
  - c. Low threshold for expenditure limits
  - d. Limited powers over debt and investments
3. **Revenue Optimisation**
  - e. Poorly designed tax and fee structures, weak collection efficiencies and low return on assets
4. **Fiscal Responsibility and Budget Management**
  - f. No Medium-Term Fiscal Plans
  - g. Poor quality of budgeting, sometimes not presented on time
  - h. Absence of citizen participation in budgeting
  - i. Backlog in audit/preparation of annual accounts, no uniform accounting standards
  - j. Weak internal control environment, no robust internal audit function
5. **Transparency and Accountability**
  - k. Poorly drafted laws and policies,
  - l. No penalties for non-compliance; no redressal mechanism
6. **Institutional Capacities**
  - m. Inadequate staffing, both quality and quantity
  - n. Non-existent or weak Information systems

### 3 Long history of reform initiatives, weak accomplishment overall

#	Key development	Year
1	<b>Eleventh Finance Commission</b> recommends CAG's oversight over accounts and audit of all Local Bodies (LBs) including ULBs.	2000-2005
2	<b>ICAI</b> publishes Technical Guide on Accounting and Financial Reporting by Urban Local Bodies (ULBs)	Sep 2000
3	Local Bodies department established in the <b>CAG</b>	Dec 2001
4	<b>Ministry of Finance</b> guidelines recommend "Database on Finances of Local Bodies" to be developed/ collated by the MoUD based on formats to be prescribed by the CAG	2003
5	Report on Accounting and Budget Formats for ULBs by <b>CAG Task Force</b>	
6	Model Municipal Law issued by the <b>MoUD</b>	Oct 2003
7	<b>National Municipal Accounts Manual (NMAM) drawn up by Task Force chaired by a Dy CAG</b> and membership from MoUD, State Municipal Departments, ULBs and select Department of Local Fund Audit representatives.	Dec 2004
8	<b>Twelfth Finance Commission</b>	2005-2010
9	<b>ICAI</b> constitutes a full-fledged Committee on Accounting Standards for Local Bodies (CASLB)	Mar 2005
10	<b>Public Disclosure Law</b> , a mandatory reform under the JNNURM	2005
11	Accounting Reforms part of <b>JNNURM</b>	2005
12	<b>Service Level Benchmarks (SLBs)</b> for key urban services adopted by the MoUD	2006
13	<b>Technical Committee on Budget and Accounting Standards for ULBs</b> formed	Oct 2006
14	Report of the <b>Second Administrative Reforms Commission</b>	Oct 2007
15	<b>Thirteenth Finance Commission</b> recommendations on audit and accounting	2010
16	<b>Report of the HPEC</b> on Indian Urban Infrastructure and Services	Mar 2011
17	<b>Modified Database on Finances of Local Bodies</b> issued by the <b>MoUD</b> in consultation with the <b>CAG</b>	2011
18	<b>Seminar on Performance Reporting for ULBs</b> hosted by the <b>CAG</b>	Sep 2012
19	<b>SEBI guidelines</b> on <b>municipal bond</b> issuances	2015
20	<b>Fourteenth Finance Commission</b> devolves Rs 87,000 crores to ULBs, mandates audited annual accounts, recommends fiscal decentralization to ULBs	2015
21	<b>AMRUT</b> mandates audited annual accounts as grant condition	2015
22	<b>Smart Cities Mission</b> lists audited annual accounts as a pre-condition	2015
23	<b>NITI Aayog</b> workshop on Municipal Finance	2018

#### Highlights:

- Focus on double entry accrual based accounting system (DEABS), no sharp focus on municipal balance sheets
- Implementation of DEABS appalling
- Improvements to procurement systems and processes incl laws, to a lesser extent to IT systems
- Driven mainly by central government, no conceptual buy-in from states, municipalities
- Pushed as reform conditions, mixed results
- Several missing pieces in the puzzle primarily because contemporary, institutional approach to financial management not adopted

#### Bottomline:

Cities continue to suffer from lack of financial sustainability and financial accountability. This is widening the infrastructure and service delivery gap in cities and worsening quality of life for citizens. In turn 1) competitiveness, economic growth and productivity, job creation 2) equitable access to opportunities and services for all citizens 3) environmental sustainability, climate change and disaster management are all getting directly impacted. We need to break the status quo!