



CITY FINANCES OF ULAANBAATAR MONGOLIA

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THE WORLD BANK

CITY FINANCES OF ULAANBAATAR

MONGOLIA

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Foreword

Today, 1.2 million people live in Ulaanbaatar, a city that was planned for half a million. This rapid urbanization is straining the city's ability to provide services, especially infrastructure. Nearly 60 percent of the population lives in unplanned settlements—or *ger* areas—that spread over 90 percent of the city's administrative area. Most lack access to basic services such as central heating, water supply, sewerage, and paved roads, and the low density and extremely cold climate make the provision of these services costly. As a result, the city must carefully aim to improve services within the affordability limits of public finance and people's own resources. In the difficult task of prioritizing services, the City intends to base its decisions on the transparent and effective management of its finances and preferences of its citizens.

Building on a strong democratic tradition, Mongolia is increasingly focusing on establishing systems for more active citizen participation, including participatory budgeting as presented in the 2011 Budget Law. Political leaders of Ulaanbaatar have voiced their commitment to involve their fellow citizens in the decision-making process more systematically. They also want to provide them with useful and reliable budget information on which they can base their views and hold the Municipality accountable.

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This study is a first step in contributing to this endeavor. Drawing on information reported in the city budget, the study describes how Ulaanbaatar's finance system works by assessing the current assignment of expenditure functions and revenue sources. It appears that Ulaanbaatar faces systemic challenges in its financial management and this may be compromising an efficient and equitable allocation of financial resources.

Despite the pressing need for services, the city has had annual budget surpluses. This suggests that a more sound investment planning system is needed for a more effective and efficient use of available fiscal resources. Moreover, the budget reporting system lacks clarity and specificity, making it difficult for citizens and the city council to have a clear understanding of how—and for what purpose—resources were invested or revenues generated.

This study is the first part of a program of research and technical support initiated at the request of Ulaanbaatar City to help it improve its finances.

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This study is the result of a scoping exercise that identifies a longer-term agenda for research and technical assistance for strengthening the city finance system for Ulaanbaatar. As such, it is based on a series of discussions with UB City and district leaders, especially representatives of the city parliament as well as Mongolia's Ministry of Finance. In particular, Mr. N. Bataa, Vice Mayor and Mrs. E. Gankhuu, Head of Finance and Treasury Division and her team (Mrs. S. Solongoo, Mr. J. Enkhtur, Mrs. J. Erdenechimeg and Mrs. B. Norjlkham) provided valuable guidance.

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Abbreviations and Acronyms

Bank	World Bank	MoF	Ministry of Finance
BL	Budget Law of December 2011	O&M	operations and maintenance
CCLSL	Capital City Legal Status Law	PIT	Personal income tax
CG	central government	PSMFL	Public Sector Management and Finance Law
GDP	gross domestic product	SDP	strategic development plan
GTC	General Tax Code	UB	Ulaanbaatar
LDF	local development fund	UB City	Ulaanbaatar City
LTAU	Law on Territorial and Administrative Units of Mongolia	VAT	value added tax

CURRENCY EQUIVALENTS

(As of June 2012)

Currency Unit = Mongolian Tugrik

MNT 1 = US\$0.00076

US\$1 = MNT 1318.4

Executive Summary

OBJECTIVE

Ulaanbaatar's (UB) population has swollen from half a million in 2001 to approximately 1.2 million in 2011, accounting for over 40 percent of the country's population. This trend is likely to continue as economic growth is increasingly concentrated in UB.¹ With its growing population and concerns with rising inequality, the city is facing increasing pressure to maintain and expand service provision (especially infrastructure). The local tax on wages² is expected to continue to provide substantial revenues to the UB government, which will assist the growing demand for services. Additionally, a new "capital city tax" is expected to come into effect in 2013. The decision of the central government (CG) to pursue further decentralization gives greater leadership to the UB government and its districts. It also provides local broader decision-making authority as well as opportunity for citizens' participation and for the improvement of governance and transparency. Therefore, a key challenge for UB and its districts is ensuring that the local fiscal system is sound and ready to handle a greater volume of revenues to achieve sustainable and inclusive growth. The city also needs to develop a robust and transparent fiscal management system if it is to make an effective use of new revenue sources.

The main objective of this study is to understand the inner workings of the city finance system in Ulaanbaatar and its districts. It empirically analyzes the city's revenue sources, expenditures in service provision, the legal framework governing them, and the budget reporting system. It identifies systemic issues that are compromising an efficient and equitable allocation of financial and fiscal resources for the provision of municipal services and urban infrastructure. Given the paucity of research

on UB's finances, it proposes a multiyear research agenda to guide the government in bringing about needed fiscal reforms. This note is intended to advise the incoming government following the elections of June 2012, especially the new UB leadership, in areas that need its attention and focus. It is meant to be used as a tool for launching a policy dialogue to develop more in-depth analysis and policy options as part of programmatic Economic and Sector Work beginning in fiscal year 2013.

KEY FINDINGS

This report consists of three main parts. Chapters 1 and 2 provide the background of the report, its scope and methodology, and a description of the prevailing budgetary norms and procedures. The main findings of the report are presented in chapter 3, which offers a detailed analysis of the revenue assignment, revenue sources, and revenue trend; and chapter 4, which examines expenditure functions and budget structures, and provides a comparison of revenue and expenditure trends. Finally, chapter 5 identifies gaps in current knowledge and proposes a prioritized agenda for technical assistance and research that will guide the next phase of the World Bank's engagement in this area. Below is a summary of the main findings with regard to revenues and expenditures and recommendations for future work.

Revenues

The UB government and its districts have several sources of revenue to finance their budgets, including own-sources, shared-revenues, and intergovernmental fiscal transfers.³ However, at present, UB has limited revenue authority primarily because Mongolia is a unitary state

1. The term UB City or UB refers to the UB government and its nine districts.

2. The wage tax was reassigned to the UB government and the aimags in 2009.

3. However, in practice, UB generates fiscal transfers to the CG, because UB (in contrast to most aimags) has relatively high revenues, and therefore MoF makes annual requests to UB for transfers to the CG. In this respect, some districts receive transfers from the CG and some of them also provide transfers to UB government.

where legislative and administrative authority (including taxes) are centrally established, approved, and overseen. First, UB does not have the authority to introduce new taxes, although it can set rates for a few taxes and user fees as determined by the parliament. However, many of these taxes are a small portion of its budget. For example, property and vehicle taxes only account for approximately 4 percent of total revenues, while other user fees generate less than 1 percent.⁴ Second, the UB government and its districts have little incentive to improve collection efficiency over its existing sources because the Ministry of Finance (MoF) ensures that any increase in revenues over the approved amount for each revenue source is equalized with one-to-one reductions in either tax-sharing or transfers. Thirdly, the MoF uses discretion in determining fiscal transfers from the UB government to the CG, and this vertical fiscal management creates uncertainty and unpredictability for UB and its districts. In sum, the current rules in revenue management and collection do not encourage the city of UB to generate additional own revenue.

With the passage of the Budget Law of 2011 (BL), this situation is poised to change because the law more clearly defines the criteria for revenue sharing and introduces new tax revenue sources, including the capital city tax and inheritance and gift taxes. *For the city to make use of these new sources, however, a regulatory framework must be put in place.*

The city's revenues are increasing significantly. Between 2009 and 2011, UB's total revenue more than doubled compared to the period between 2003 and 2008, when revenues were stagnant. In 2011, UB generated US\$164 million (216 billion Tugriks) in revenues, exceeding the approved budget by US\$14 million (18.7 billion Tugriks). This improvement was primarily due to an increase in revenues from the wage tax that was reassigned to UB City (and the aimags) in 2009.

4. The above percentages are averages for the last three years for the consolidated of UB City (see table A1.3). The figures for the UB government only are approximately 5 percent and less than 1 percent, respectively (see table A1.4).

Expenditures

In the last three years, expenditures for capital investments and current operations have rapidly increased, keeping up with revenue trends. Current expenditures more than doubled, between 2008 and 2011, increasing from 23.4 to 48.8 billion Tugriks (equivalent to US\$17.7–37 million), while capital expenditures increased sixfold, from nearly 17.8 billion to over 118.5 billion Tugriks (equivalent to US\$13.6–\$89.9 million). The typical services covered by these expenditures include street lighting, solid waste collection, social assistance, and prevention of infectious diseases. *However, there is little information on the quality and coverage of city services, an issue that merits further study in order to guide city leaders in decision making.*

As revenues increase, the city also needs to improve investment planning and absorptive capacity. Despite the city's significant need for infrastructure investment and services, 53.8 billion Tugriks (US\$40 million), amounting to 29 percent of planned expenditures, were unspent in 2011. There were surpluses in prior years as well. The empirical evidence suggests that these surpluses are not the result of fiscal discipline but instead the result of limitations in local investment planning and execution capacity. For example, expenditures for “environmental protection” and “services provided on behalf of the government” comprised only 46 percent and 59 percent of projected amounts, suggesting that planning for and delivery of services remains weak.⁵ *Limited absorption capacity would suggest that city leaders must study this issue more carefully before considering future borrowing that has recently been authorized under the Budget Law.*

An overlap in the assignment of expenditure responsibilities between the UB government and its districts—especially for capital investments and operations and maintenance (O&M), creates duplication. This overlap may compromise economic efficiency and inter-jurisdictional equity in service provision as well as

5. According to UB government's comments to this study, the revised executed expenditures for “environmental protection” (46%) and “works and services provided on behalf of the government” (59%) are: 77.6 and 64.7 percent, respectively; which suggests that expenditure performance for these expenditures, along with very few other items, was not as low (for fiscal 2011) as originally indicated.

accountability in general and financial accountability in particular. The UB government and its districts use an *ad hoc* and negotiated approach to address the lack of clarity in their functional responsibilities. *In order to address the current redundancies in the legal framework, these informal intergovernmental fiscal relationships could, among other things, be adequately regulated. Current measures to deepen decentralization should also clarify roles and responsibilities.*

The budget classification system and format of UB and its districts lack transparency, making it difficult for city leaders and taxpayers to understand the actual use of funds.

The UB government's main concern with regard to budget reporting is to show the use of funds from different sources rather than reporting on services provided with the funds. The actual use of significant portions of the operating and the capital budgets are not disclosed in the budget document. For example, in 2011, because almost 93 percent of the capital budget was labeled "Investments Financed by Own Revenue Budget," it is impossible to determine (from the executed budget) on what public works and services the funds were spent. Another significant expenditure item was labeled "Services Required under the Name of the Government," again making it impossible for decision makers and citizens to know what services were actually provided. Furthermore, the budget classifications and reporting of some specific⁶ current and capital revenue sources are not fully consistent with what has been established by law. A number of inconsistencies in budget classification distort the availability of funds in favor of UB's operating expenditure budget and against its capital budget. This situation may lead to a negative impact on capital investment planning and, ultimately, to lower coverage and quality of investments in services and infrastructure.

The city's budgetary operations are highly fragmented. The current budgeting system of UB and its districts does not report on the social services it provides on behalf of the central government because the law

6. While revenues from the vehicle tax and the road user fee are meant for the financing of the capital budget, in practice such revenue sources are reported as current revenue, not as capital revenue as it should be. Of course, this misclassification overestimates the current revenue budget and underestimates the capital revenue budget, providing (in today's numbers) a small distortion in UB's financial situation.

requires that these services be managed under a separate accounting, budgeting, and financial reporting system. Therefore, there is no consolidated budget report for the city as a whole that identifies operational budgets by departments or services. This makes it difficult for city leaders and the public to have an overall view and assessment of UB functions and service responsibilities. *Hence, the budgeting system needs to be made more transparent, classified in accordance with international best practices, and consolidated so that city leaders can make an accurate assessment of the city's financial situation and make informed decisions.*

NEXT STEPS

The last chapter of this report outlines a future agenda for research and technical assistance, which will inform the World Bank's engagement in the coming two years, during fiscal years 2013 and 2014, and will complement the preliminary findings of this report.

There are three key areas that need to be urgently addressed:

- Improving the current budgeting and accounting systems to enhance transparency in service provision through technical assistance;
- Analyzing in greater depth the system of intergovernmental fiscal relations between UB and its nine districts and determining how these relations can be improved to enhance economic efficiency, inter-jurisdictional equity, and financial performance; and
- Assessing the efficiency of UB and its districts in both revenue administration and collection performance as well as in expenditure execution.

In the medium term, four key research questions need to be addressed:

- How sustainable are the services⁷ provided by UB and its districts?
- Is the provision of any local service supplied by either the UB government or any of its districts substantially

7. This analysis would include both revenue-generating and nonrevenue-generating services.

more cost-effective to the extent that it could be used as a model or benchmark for service provision?

- What is the actual coverage in district service provision and how efficient is the current fiscal system in funding local public investment programs?
- How is the current budget process actually affecting local investment planning and execution in UB and its districts? For example, how much of the Strategic Business Plans and district's action plans are actually being implemented?

The World Bank will support the UB government through a programmatic research agenda to address the urgent priorities in fiscal 2013. It will especially focus on enhancing budget transparency. In fiscal 2014, it will focus on issues relating to quality and coverage of municipal services.

Chapter 1. Introduction

1.1. BACKGROUND

Over the past two decades, Mongolia has made good progress in navigating a simultaneous political and economic transition. Since the beginning of this transition in 1990, the government has undertaken fundamental economic reforms in the areas of price liberalization, privatization, trade, and foreign investment. Mongolia has also reformed its political system to a parliamentary democracy. With gross domestic product (GDP) growth at over 15 percent, it is one of East Asia's fastest growing economies. This rapid economic growth is expected to continue due to revenues generated by the mining industry, which now account for 20 percent of GDP (twice the rate of a decade ago). In recent years, the mining sector has contributed approximately one-third of total government receipts through royalty payments and direct and indirect taxes. By 2016, the mining sector is expected to contribute to over half of the GDP.

Economic growth has helped in almost halving the national poverty line between 2002 and 2008. Back in 2008, the poverty line stood at 35 percent. Despite the unprecedented growth of the past decade, job creation only increased by 11 percent, mainly because the mining industry is not labor-intensive. Inequality in both opportunities and outcomes will likely rise as the economy relies more and more on the mining sector. As measured by the Gini coefficient, inequality in household per capita consumption increased from 32.9 in 2003 to 35.8 in 2008.

Population and economic growth has become increasingly concentrated in Ulaanbaatar (UB), the capital city. Due to lack of employment opportunities and severe winters that have decimated livestock, people from rural areas continue to migrate to the capital at high rates. Ulaanbaatar's population has swollen from

approximately half a million in 2001 to approximately 1.2 million in 2011, accounting for over 40 percent of the country's population. UB is the political, industrial, and economic center of the country, generating 65 percent of the country's GDP, 85 percent of its power generation, and 50 percent of its investments. With a growing population and concerns about rising inequality, the city is facing increasing pressure to maintain and expand its provision of services (especially infrastructure). UB and district leadership anticipate that mining revenue will also translate into increased revenue for the city through intergovernmental fiscal transfers, which will enable it to meet the growing demand for services. The national decision to decentralize core services gives UB City leadership greater decision-making authority and creates an opportunity for citizen participation and the improvement of governance and transparency. Therefore, a key challenge for the country is ensuring that its intergovernmental fiscal systems are sound and ready to handle the greater volume needed to achieve sustainable and inclusive growth. Likewise, UB and the districts must develop robust and transparent fiscal management systems in order to effectively use anticipated revenues. At present, little is understood of how UB's overall municipal finance system works, especially with respect to expenditure and revenue management.

1.2. OBJECTIVES

The main objective of this study is to understand how the municipal finance system in UB works by empirically analyzing the expenditures in the provision of services as well as the city's revenue sources. The study identifies structural and systemic issues that could compromise the efficient and equitable allocation of financial and fiscal resources for the provision of municipal services and urban infrastructure. Following the elections of June 2012,

this study is also intended to advise the incoming government, especially the new UB leadership, on what areas need its attention and focus. Ideally, the study will be used to help launch a policy dialogue with more in-depth analysis to develop policy options as part of programmatic economic and sector work beginning in 2013.

1.3. RATIONALE

Over the past decade, the World Bank (Bank) has had several urban development operations in UB primarily focused on infrastructure service improvement; these projects have enabled the building of a strong partnership with the UB government. The city parliament requested the Bank's technical assistance to enable them to better understand the current municipal finance system in place so that they can carry out their oversight responsibilities more effectively. The city parliament has been significantly constrained by their limited authority under the current system, particularly in relation to UB City's investment decision-making and revenue management.

The Bank also needs to better understand the city's municipal finance system to ensure that the city has the ability to operate and maintain its infrastructure for the future sustainability of current investments. Furthermore, the Bank brings global knowledge with regard to best practices in municipal finance systems and has specific experience advising transition economies, such as those in Eastern Europe that share similar institutional challenges inherited from the Soviet system.

1.4. GOVERNMENT STRATEGY

The government strategy in transitioning to a market economy has been to increase the delegation of service delivery from the central to the local governments. Much of this effort can be characterized as deconcentrating central government functions rather than decentralizing authority to local governments. More recently, the government has been working toward more effective decentralization by clarifying functional responsibilities across different levels of government through legal measures. A number of laws have been passed, the most important of

which is the newly-approved budget law (BL); other laws remain under review. Some of the key provisions of the BL include clarification of the budget process, delegating key functions to local governments, giving them authority over revenue collection and borrowing, setting technical criteria for intergovernmental fiscal transfers, and establishing a formula-based local development fund. The BL also recognizes the importance of transparency and citizen participation. A new draft law on the legal status of UB as well as a draft law on UB taxation have recently been submitted to the parliament. Although it is not yet known when these laws will be passed, they are expected to promote transparency and minimize the political influence that comes with discretionary practices embedded in the current budget process. These laws are expected to free the UB government and its districts from the yearly political negotiations that limit effective and strategic decision making.

The UB government is making concerted efforts to improve its service delivery and planning systems by developing a new master plan. UB is making significant investments to upgrade infrastructure, especially its road network, using its own revenues, although these efforts are constrained by an inadequate capital investment budget. The BL authorizes local governments to borrow from the market and issue bonds—although rules and procedures are yet to be defined—that should provide additional resources in the future. In addition, to improve living conditions in the city's unplanned and poorest (*ger*) areas the government has adopted a policy of incrementally improving basic services—water supply, sewerage, drainage, roads, and solid waste management.

1.5. SCOPE OF THIS STUDY AND MAIN RESEARCH QUESTIONS

The focus of this study is to gain a greater understanding of how municipal finance works in Ulaanbaatar. Given this general objective, the scope of this study will cover the overall fiscal situation of UB and its districts and will examine in more detail their main revenue sources and expenditure responsibilities as well as the balance between revenues and expenditures, including an analysis

of their historical trends. As part of this effort, the study addresses the following main questions:

- What are *de facto* the main *revenue sources*⁸ for UB, including its nine districts, and how do they compare with those established by the current applicable laws?
- What are the main constraints preventing growth in UB government revenues, including those of its nine districts?
- What are *de facto* the major municipal *expenditure responsibilities* in the UB government, including its nine districts, and how do such responsibilities compare to those specified in the current legal framework?
- What are the main constraints obstructing the improvement of municipal expenditure efficiency for UB and its districts?
- What is the balance between revenues and expenditures? For what purpose are surpluses supposed to be allocated? In case of deficits, how are said deficits generally financed?
- Which areas of UB finances merit further research?

1.6. DATA SOURCES AND METHODOLOGY

The research focuses on three key areas to provide a clear understanding of the finances of UB and the districts: (1) the budgeting system; (2) expenditures; and (3) revenues. Subsequently, a comparison of revenues and expenditures must be carried out in order to provide: (1) information to UB's leadership on the main issues and constraints in the current system's operations; (2) relevant data enabling the city's administration to make informed decisions regarding the costs of service provision and the need for future revenue mobilization efforts; and (3) guidance on how to increase the transparency of budgeting and accounting systems.

An understanding of the current system will contribute to the development of regulations for the BL that establishes a local development fund for capital investments by local governments with the participation of communities in decision making.

For the purposes of this study, the data for analysis is primarily drawn from the approved and executed budgets obtained from the UB government and its nine districts. Data for UB cover the aggregated⁹ revenues and expenditures from 2003 through 2011 and the approved budget for 2012. Regarding disaggregated budgetary data for UB and its nine districts, the data covers revenues from 2003 through 2011, and expenditures from 2008 through 2011.

8. "Main revenue sources" refers to both local revenue collections and central government transfers from local taxes collected on their behalf as well as discretionary or emergency transfers and capital grants.

9. "Aggregated" data for revenue and expenditure is the sum of UB government's and its nine districts revenue and expenditure budgets.



Chapter 2. Budget Cycle and Budget Structure

2.1. LEGAL FRAMEWORK: RELEVANT LAWS

The responsibilities and powers regarding the finances and financial management of the UB government and its districts are governed through a gradually evolving legal framework resulting from Mongolia's transition out of a centrally-planned economy. Mongolia's constitution, adopted in 1992, provides the legal foundation for the current government structure, including basic principles on the role of local governments. The constitution divides the Mongolian government into aimags (further subdivided

into soums) and the capital city (subdivided into districts), and recognizes that these are economic, social, and jurisdictional subjects with their own functions and rights of self-governance. This evolution in the legal framework has successfully assigned typical municipal services to local governments and allows line ministries to delegate¹⁰ the provision of specific social¹¹ services to subnational levels of government at their own discretion. The laws most relevant to this study are summarized in table 2.1.

10. In the near future, current *delegation* could evolve toward actual devolution.

11. These services include, as examples, health and education.

Table 2.1. Summary of Main Legal Framework

LAWS	RELEVANT ASPECTS
Consolidated Budget Law Date: November 20, 2002	This law sets out the general budget composition, classification, and financing scope.
Public Sector Management and Finance Law (PSMFL) Date: January 1, 2003	This law establishes the authorities and responsibilities of the main actors in the budget cycle and budget process at all levels of government. It defines nine services as core local responsibilities.
Law on Territorial and Administrative Units of Mongolia (LTAU) Date: December 15, 2006	This law establishes the administrative system, structure, and authorities of different levels of assemblies and governors. Article 31 states that districts and soums have the authority to provide water supply, garbage collection, streetlights, and park maintenance.
Capital City Legal Status Law (CCLSL)—Old Law of 1994 Date: Revised draft was submitted to the parliament in 2010 but has not yet been approved.	The capital city must carry out those functions requested by the State Great Khural or the state general budget governors (i.e., the line ministries). CCLSL states (in Article 4.9.3) that UB shall “participate in establishing and developing integrated networks, including electricity distribution, roads/transportation, and communication and information technology networks.”
The Budget Law (BL) Date: December 23, 2011 Also known as the Integrated Budget Law	It establishes principles, systems, composition, and a classification of the budget, all used to implement special fiscal requirements. It also defines both the authority of the LGs and the responsibilities of budgetary bodies that participate in the budget process. In addition, it regulates relations that arise in connection with budget preparation, approval, spending, accounting, reporting, and auditing.
General Tax Code (GTC) Date: May 20, 2008	GTC defines the authorities of the central government (CG), UB City, and Aimag regarding the setting of tax rates. It also establishes tax administration responsibilities.

Overall, the net effect of the evolution in the legal framework has been a gradual strengthening of subnational levels of government. The current legal framework includes norms and procedures for the entire public sector. It covers the national and subnational levels of government, including UB and its nine districts.

It is important to acknowledge that the effort to decentralize roles and responsibilities across different levels of government is still incomplete and that additional regulations are needed to more efficiently implement these laws. This note addresses specific issues in the relevant chapters. For example, as will be discussed in chapter 4, the UB government and its districts have legal authority over the same set of services; therefore, their specific roles and responsibilities would benefit from further regulation. The next section will focus on the budget cycle. It highlights some of the cycle's main features and the roles and responsibilities of key actors in the budget process.

2.2. THE BUDGET CYCLE: AUTHORITIES AND RESPONSIBILITIES

The main phases of the budget cycle are consistent with international standards and are comprised of: (1) preparation; (2) submission and review; (3) approval; (4) execution and reporting; and (5) monitoring and assessment of performance agreements. Before describing the phases of the budget cycle (table 2.2), it is important to note the meaning of following four terms frequently used when referring to some of the main actors in the budget cycle.

- “*State*” refers to the central government (CG) and should not be confused with the same term used by some federal systems to refer to a subnational level of government;
- “*Local government*” refers to all types of subnational governments (i.e., Aimag, the capital city, soums, and district);
- “*Budgetary body*” refers to the national or local-level institution that manages a budget (e.g., the capital city, districts, or assemblies);

- “*Portfolio minister*” refers to the highest official with authority over the institution's budget (e.g., the capital city governor, district governor, or head of the presidium).

2.3. KEY BUDGETARY NORMS AND PROCEDURES

To guide budget preparation and implementation, several norms and procedures are in place, covering all levels of government. The key guidelines, as they apply to the capital city and its districts as well as to their actual implementation are summarized below:

Strategic development plans (SDPs). Public institutions are required to prepare SDPs covering three fiscal years; these plans are the basis upon which local budgets are prepared and approved. SDPs must include strategic objectives and outputs to be delivered during the next financial year, specifying category, quantity, quality (i.e., standards and specifications), and costs. The cost of outputs must be determined on the basis of a full accrual cost of production, including management, overhead, and capital charges. In UB City, this document is referred to as the “budget framework document.” It is prepared by the strategy and policy planning unit of the finance and treasury department, and it guides the annual budget proposal that is approved by the city council. Although the guidelines require the use of accrual cost accounting, budget reporting is done annually on a cash-flow basis. When works require more than one year to complete, unspent funds may be carried over and expenditures are reported in the year that they occurred.

Budgetary savings. Savings from either the capital budget or operating budget of *state* and *local* budgetary bodies may be used for training and performance incentives or for strengthening operations.¹² These “savings” cannot be used as a basis for budget cuts during the appropriations process. This means that UB and its districts may use any *budgetary savings* for operating and/or capital expenditures during the following year.¹³

12. See Article 13.7 of the PSMFL—January 1, 2003.

13. See Article 45 of the BL (December 23, 2011) for a definition of “budget savings.”

**Table 2.2. Mongolia’s Budget Cycle Applicable to Ulaanbaatar
(Fiscal Year: January 1–December 31)**

SCHEDULE	ACTIVITY AND RESPONSIBLE INSTITUTION	LEGAL BASIS
	Budget Preparation	
January–June	Subnational levels of government (i.e., aimags and the capital city as well as districts and soums) under the leadership of their governors prepare strategic development plans (SDPs) and action plans prior to formulating their corresponding budgets.	PSMFL of January 1, 2003
By May 1	The central government’s Ministry of Finance (MoF) submits the fiscal framework statement for the following year to the State Great Hural.	PSMFL of January 1, 2003
By July 1	The state budgetary body submits a draft of the SDP to the portfolio minister, districts, UB government, and line ministries. Districts submit action plans to the UB government.	PSMFL of January 1, 2003
By August 15	A portfolio minister (such as the line minister) submits the SDP to the state central administrative body responsible for finance and budget. The UB government submits SDPs and district-level action plans to MoF.	PSMFL of January 1, 2003
	Budget Submission	
By December 1	The governor submits a budget proposal to the corresponding level assembly that includes: (1) short- and medium-term strategic objectives of the local government; (2) classes of outputs to be purchased, entities that will deliver outputs, and purchasing costs; (3) an investment plan; (4) a maintenance of physical assets plan; (5) an explanation of the consistency of the classes of outputs with strategic objectives; and (6) a comparison of budgeted, estimated, and actual figures for the previous period.	PSMFL of January 1, 2003
	Budget Debate and Approval	
By December 31	UB and district assemblies debate the budget proposals submitted by their governors.	PSMFL of January 1, 2003
	Budget Execution and Reporting	
Within one week after approval	UB and district budgets submitted to the state central administrative body responsible for finance and budget.	PSMFL of January 1, 2003
Semi-annual and annual reports	State budgetary bodies prepare financial statements and output delivery reports on a semi-annual and annual basis. Each category of outputs reflects quantity, quality, costs, and timeliness.	PSMFL of January 1, 2003
Within 20 days after end of fiscal year	(1) Governors report on the execution of local budgets; and (2) governors and chief accountants of local budgets sign financial statements and performance reports certifying their accuracy.	PSMFL of January 1, 2003
Within 1 week from audit opinion	The governor submits: (1) annual financial statements along with an audit opinion issued by local audit body to the relevant level assembly; and (2) financial statements submitted to the state central administrative body responsible for finance and budget.	PSMFL of January 1, 2003
	Budget Monitoring and Evaluation	
Ongoing activity during fiscal year of implementation	The capital city and district governors monitor the delivery of outputs and financial performance of local budgetary bodies based on: (1) budgets, action plans, and strategic development plans; and (2) agreements on delivery of outputs to be financed by the state budget, including quantity, costs, criteria, and procedures for the evaluation of the performance of these agreements.	PSMFL of January 1, 2003

Source: Elaborated for this report based on the relevant legislation.

UB City differentiates between *savings* and *surpluses*. A surplus occurs when the city spends less or raises higher revenues than planned. In some cases, it appears that revenue surpluses are transferred to the Ministry of Finance (MoF). How budget surpluses are treated in practice merits further research.

Budgetary outputs. The UB government and its districts are defined as local budgetary bodies when specific state functions are delegated to them and financed through the state. The UB government and the districts are responsible for the delivery of *core local outputs* that must be funded by *local budgets*.

Output purchase agreements and output performance. Capital city governors are authorized to sign agreements with line ministries for the delivery of outputs to be funded by the state budget. District governors have the responsibility to deliver outputs (i.e., education, health, and other services) on the basis of output purchase agreements made with the capital city governor.

Local and state budgets. When managing funds, *local* governments must differentiate between expenditures financed using their own revenues with those financed by the CG. UB City and its nine districts have their own treasury accounts¹⁴ that enable them to manage their revenues.

Fiscal transfers. *Local* expenditures financed by the *state budget* are funded by CG fiscal transfers from the corresponding line ministries. These types of CG transfers are generally earmarked for specific services, such as education, health, culture, and/or social welfare.

Separate accounts for state-financed works and services. All cash flows relating to revenues, expenses, assets, or liabilities incurred from works and services on behalf of the state are to be maintained in a separate subaccount managed by the state central administrative body

14. The roles of the treasury accounts of aimags, the capital city, soums, and the districts are properly established in Article 36 of the Budget Law (December 23, 2011). The treasury accounts of UB City and the districts are managed independently of the treasury single account administered by the MoF. UB and the districts treasury accounts are under the oversight of the elected city or district councils.

responsible for finance and budget or by the office of finance and treasury of the local government. Consistent with this norm, when UB City is contracted to provide a service for a line ministry, it maintains a subaccount to which expenses are charged, ensuring that funds are used for intended purposes.

The current practice in UB is to contract works through competitive bidding organized by its investment department that, in coordination with the relevant sectoral departments, is also responsible for monitoring performance. The UB treasury authorizes transfers based on performance evaluations as reported by the investment department. The same procedures apply to works financed with CG funds but implemented by the city.

Budgetary prohibitions. The Public Sector Management and Finance Law (PSMFL) prohibits the capital city and its districts from exceeding the limits of budget appropriations and from using revenues of asset sales to finance operating expenditures.

Assignment of local expenditure responsibilities. Although the assignment of expenditure responsibilities will be addressed in chapter 4, it is important to highlight that the PSMFL assigns the same responsibilities to the capital city governor and the district governors. These responsibilities are described in box 2.1.

2.4. BRIEF ASSESSMENT OF KEY BUDGETARY NORMS AND PROCEDURES

In principle, planning ahead for at least three years is a sound norm; however, its potential benefit depends on whether or not financial planning, particularly for investments, can be established with some certainty over the three-year planning period. The current capital financing system does not allow UB and its districts to forecast future capital resources because the system is primarily based on negotiations—as opposed to formula-based capital transfers. This will be further discussed in later chapters of this report. Due to this lack of predictability, the potential benefits of three-year plans are compromised.

Box 2.1. Local Responsibilities

Core local services: (1) public hygiene, waste removal, treatment, and disposal; (2) local environmental conservation and protection, gardening, renewal, and maintenance; (3) pest eradication and control; (4) local road maintenance; (5) provision of normal water operations, sewerage, and drainage systems; (6) flood prevention and soil protection; (7) fire prevention, protection, and mitigation; (8) outputs associated with local public infrastructure facilities; and (9) measures on fighting and prevention of infectious livestock and animal diseases including those transferable from livestock to humans. With the exception of waste collection and disposal, the remaining services must be financed through local taxes.

The capital city governor is responsible for: (1) delivering services financed through locally-mobilized taxes and nontax revenues as well as through transfers from the state budget; and (2) delivering key services to the central government delegated outputs to be financed from the central budget (such as education, health care, culture, labor, social welfare, and social security, among others) through a contractual agreement.

District governors are responsible for: (1) delivering services through locally-mobilized tax and nontax revenues as well as through *transfers* from the capital city; and (2) delivering services to be purchased by the central government (i.e., education and health) on the basis of output purchase agreements with the capital city governor.

Source: PSMFL, Articles 52 and 53.

There are several benefits associated with having separate accounts for state services financed by the state budget and implemented by UB and/or its districts. Separate accounts facilitate monitoring and evaluation by the corresponding line ministries and contributes to financial transparency of the services provided, enhancing state oversight in general. However, the proliferation of separate vertical financial and accounting systems without a horizontal consolidation of services provided by the city creates budgetary fragmentation, making it almost impossible to get a comprehensive view of all the services that UB delivers through contractual agreements and their associated budgetary costs.

In principle, the financing of selected social services through contractual agreements and other local services through locally-generated revenues is an economically sound approach. This occurs because the supply of social services tends to be more economically efficient when financed by the state budget instead of by local revenue sources alone. Public goods like social services that generate national benefits (i.e., through strong positive externalities) should be financed by the central government's budget. However, current output purchase agreements

between the UB government and the corresponding line ministry are based on negotiations, not on technical criteria. As such, the current allocation of state financial resources for the provision of social services (such as education and health) may be biased in favor of regions with greater negotiating power rather than being decided by objective criteria. Determining whether or not this is the outcome of current rules regarding the allocation of fiscal resources falls beyond the scope of this report. A next step to the current legal framework is to adopt a formula-based fiscal transfers system for basic social services.

The prohibitions against exceeding the limits of budget appropriations and using proceeds from the sales of fixed assets for current spending reflect sound rules for capital financing and are consistent with international standards of fiscal discipline. Similarly, the option to keep the surpluses¹⁵ and savings in operations may act as an incentive to revenue collection performance as well as expenditure efficiency. Conversely, if such savings are due to poor performance in budgetary execution, they

¹⁵ According to Article 56.2 of the BL, the "Portion of the basic budget surplus of lower level budgets equal to base expenditures shall be retained and the residual shall be mobilized to upper level budget."

may be an indicator of poor planning and service-delivery capacity.

Based on preliminary information, the overlap or duplication in functions between the capital city and the districts may only be a matter of appearance. Once an agreement has been reached between the city

governor and the district governor, district budgets can be approved only by their respective assemblies. The capital city governor has both ultimate authority and the majority of required fiscal resources to deliver the services. Therefore, the district budget formulation process may serve as a forum for clarifying the division of responsibilities between the districts and the UB government.

Chapter 3. Revenues

3.1. OVERVIEW OF ASSIGNMENT OF REVENUE SOURCES TO THE UB GOVERNMENT AND DISTRICTS

The UB government and its districts have several sources of revenue to finance its budget, including its own revenue, shared revenue with the central government (CG), and intergovernmental fiscal transfers. In addition, it benefits from financing from international organizations and donations from citizens and enterprises. However, these proceeds are not included in the budget because they are provided¹⁶ in kind, rather than in cash. Tax, non-tax, and capital revenues constitute its principal sources of own-revenue financing. Taxes are comprised of personal income taxes (PIT) that includes wage tax, unidentified income tax, self-employment tax, and livestock tax, and other taxes including property tax, vehicle tax, land payment, and fees.¹⁷ Nontax revenues include proceeds of dividends, rent, interest, and fines, and budget entities' own revenues. Capital revenues consist of proceeds from privatization and property sales taxes. Value added tax (VAT) royalties and license fees for mining and mineral prospecting are shared with the CG. Intergovernmental fiscal transfers are made on an *ad hoc* basis to fill vertical fiscal gaps; therefore, these amounts are largely determined by political considerations.

Given Mongolia's legacy of a centrally-planned economy, existing legislation assigns the most important sources of tax revenue to the central government, leaving relatively less significant taxes and fees to local governments. Even so, the 2002 Consolidated Budget Law granted local governments a share in the largest revenue sources: royalty on minerals and license fees for mining and mining exploration. VAT was shared among CG and the local government from 2000–09 only. From 2009–12

the VAT has been exclusively a CG revenue source. And until the BL of December 2011, 25 percent of domestic VAT was allocated to the local government through the local development fund (LDF). Furthermore, it should be noted that the royalty was shared at provisional rates among the CG and the provinces (including UB City), and license fees for mining and mining exploration were CG revenue until 2008. The minerals tax-sharing was formalized in 2006. Mineral royalty revenues are shared at a ratio of 70:20:10, and license fees for mining and mining exploration are shared at a ratio of 50:25:25 among the CG, the UB government, and the districts, respectively. However, the allocation principles for revenue-sharing among these three levels of government lacked transparency. The UB and districts have historically had limited revenue autonomy and have depended substantially on the CG for capital investment. With the formulation of new laws, especially the Budget Law of December 2011 (BL),¹⁸ this situation is poised to change because revenue sources for central and local governments are more clearly defined and transparent criteria are set for revenue-sharing (i.e., for the LDF, which is financed by the revenue-sharing system and will be allocated by formula). Table 3.1 indicates the revenue sources for each level of government (central, UB, and districts) per the new budget law of 2011.

The BL redefines the revenue assignment for shared taxes as well as state and subnational taxes. Under the new BL, the royalty on minerals is shared by a ratio of 95:5, and domestic VAT by a ratio of 75:25 between the central and local governments, respectively. Five percent of the mineral royalty revenues and 25 percent of domestic VAT will go into the general local development fund managed by the CG. Using a formula based on criteria like the local development index, population, population density, remoteness, territorial size, and local tax

16. Though these projects are financed by external sources, UB collaborates directly or indirectly in their implementation.

17. According to the budget Law of 2002 and PSMFL.

18. The government of Mongolia developed and passed a new Budget Law on 23 December 2011 by integrating the Budget Law of 2002 and PSMFL. The law will be fully enforced starting in 2013.

Table 3.1. Revenue Assignment According to the Budget Law of 2011^a

SHARED TAXES	CENTRAL GOVERNMENT TAXES	UB GOVERNMENT TAXES (AIMAGS)	DISTRICT TAXES (SOUMS)
Royalty on minerals (95:5) Domestic VAT (75:25)	<ul style="list-style-type: none"> • CIT • VAT of imported goods and services • Excise taxes • Custom duties • Gasoline tax • License fees for mining and exploration of mineral resources • Air pollution fee • Stamp duty (11.2 of the stamp duty law) 	<ul style="list-style-type: none"> • Capital city tax^a • Land payment • Immovable property tax • Vehicle tax • User fee for water on production • Wage tax^c (8.1.1 of PIT law) • Inheritance and gift tax^b • Stamp duties other than 11.2 of the stamp duty law 	<ul style="list-style-type: none"> • PIT other than 8.1.1 of the PIT law • Gun tax • Stamp duties other than 11.2 of the stamp duty law • User fee for hunting • User fee for natural resources other than minerals • User fee for herbs • User fee for timber • User fee for common minerals • User fee for drinking water and springs • Self-employment tax • Dog tax^b

Source: Budget Law of 2011.

a. The general tax code (GTC) and the tax laws establish the tax bases and defines central and local taxes, including ceilings for tax rates and regulations for tax administration. The parliament defines tax bases and rates for customs duties and for direct and indirect taxes.

b. These taxes are not yet regulated.

c. Article 8.1 of the PIT law defines all types of personal income on which taxes are levied, including wage income; operational income; property income; property sale income; income from book writing, innovation, sport activity, and concert organization; awards on sports and concerts; income from lottery and games; and indirect income.

incentive, a minimum of 60 percent of the general local development fund will go into the local development fund for expenditures at the district and Soum levels.

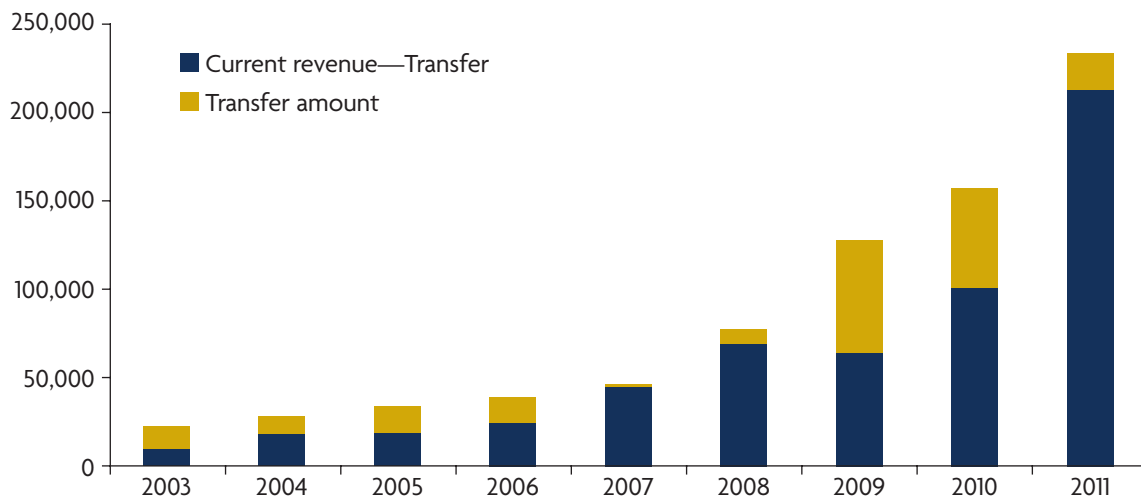
The new BL upholds taxes legislated under previous laws and practices, such as taxes on wages, property, and vehicles, as well as user fees for water production and land use, but also introduces new taxes like the capital city tax and inheritance and gift taxes. Likewise, districts may continue generating revenues from PIT, unidentified income taxes, gun taxes, license fees, and so on (see table 3.1), and may collect on the newly-created “dog tax.” However, the regulatory framework for implementing the new taxes (the capital city tax, the dog tax, and the inheritance and gift taxes) is not yet in place.

Although some taxes are assigned to local governments, collection is carried out by the Ministry of Finance (MoF) on their behalf through the local department of its national tax office because of Mongolia’s vertical fiscal

administration system. The employees of the national tax office at UB and the districts are under dual subordination, reporting to the locality’s governor and the MoF. These tax offices in UB and the districts collect all taxes and disburse/incorporate the corresponding revenue into UB and district budgets (i.e., through their treasury accounts) according to their monthly and quarterly revenue schedule approved by the MoF¹⁹. It should be noted that, as part of the overall fiscal system, annual transfers are made from the UB government to the CG on a discretionary basis in amounts determined by the MoF. There are, however, no clear criteria for determining the magnitude of these transfers. They are established, as noted above, at the discretion of the MoF and are based on the fiscal needs of the central government. Given its higher revenues, UB government transfers are relatively large compared to those of other jurisdictions. This is a disincentive for local revenue collection. The amount of

19. On the basis of the respective tax revenue proposals submitted to MoF by UB and the districts.

Figure 3.1. Transfer and Current Revenue of Ulaanbaatar and the Districts, Fiscal 2003–11 (in millions MNT)



Source: UB City Budget Book 2012, p. 22.

locally-collected revenue that is transferred to the central government varies annually, as illustrated in figure 3.1. For example, in 2003, UB City transferred 49.6 percent of its total current revenue. In 2007, it transferred 3.3 percent, and in 2011, 9 percent. The blue column represents the net current revenues of UB and the districts, not including funds transferred to the CG; the red column represents transfers made to the CG.

In a similarly *ad hoc* manner, the UB City government determines the amount of revenues that are to be transferred to and from districts, although the collection itself is done by the MoF as described above. For example, as reported in UB’s 2012 *Budget Book*, Baganuur, Bagakhangai, Nalaikh, and Songinokhairkhan districts received transfers from the UB government while Bayangol, Bayanzurkh, Khan-Uul, Sukhbaatra, and Chingeltei districts provided transfers to the UB government. The lack of revenue predictability makes any investment planning process a major challenge for UB and the districts. As a result, investment plans tend to be formulated by line ministries, approved by the parliament, and implemented by the UB City government.

The city and district councils “approve” the municipal budgets once they have the approval of the parliament

in the medium-term fiscal framework; although the law does not require the local council’s budget approval to be identical to it, this is what generally occurs as a result of the vertical planning and administrative systems. With regard to the budget process, the municipal council appears to be reduced to a rubber-stamping role. The city council also approves the three-year action plan and one-year socioeconomic guidelines upon which the budget is based.

3.2. BRIEF ASSESSMENT OF OWN REVENUE SOURCES

Own revenues play an important role in UB and the districts’ finances, accounting for 74 percent of the total municipal current revenues in the years 2009–11. UB and the districts have limited control over the taxes and fees it has the authority to levy, as illustrated in table 3.2.

Taxes. The UB government generates revenue from wage tax, property tax, and vehicle tax, while districts collect revenues from gun tax, taxes on property sales,²⁰

20. According to the budget format, UB City reports the property sale tax as capital revenue but, in practice, UB uses these proceeds for current expenditures.

Table 3.2. Legislative Controls over Subnational Own Revenues, 2011

TAXES	LEGISLATIVE LEVEL DETERMINING TAX BASE	LEGISLATIVE LEVEL DETERMINING TAX RATE	TAX REVENUE RECEIVING ENTITIES
Personal Income tax	Parliament	Parliament	
8.1.1 of PIT law (wage tax)			UB government
Other than 8.1.1 of PIT law			District
Unidentified income tax ^a	Parliament	Parliament	District
Immovable property tax	Parliament	UB government within limit	UB government
Gun tax	Parliament	Parliament	District
Vehicle tax	Parliament	UB government within limit	UB government
Capital city tax	Parliament	UB government within limit	UB government
Inheritance and gift tax	Parliament	Parliament	UB government
Dog tax	Parliament	Parliament	District
Stamp duties	Parliament		
For 6.2 of stamp duty law		CG within limit	CG
For 6.3 of stamp duty law		UB government within limit	UB government and districts
License fee for natural resources other than mineral	Parliament	Parliament	District
User fee for land	Parliament	Parliament	UB government
User fee for water ^b	Parliament	Central government within limit	
For production use			UB government
For household use			District
User fee for springs	Parliament	UB government within limit	District
User fee for timber	Parliament	Parliament	District
User fee for herb	Parliament	UB government within limit	District
User fee for common mineral	Parliament	Parliament	District
License fee for hunting	Parliament	Parliament	District

Source: Based on the GTC and Budget Law of 2011.

a. Unidentified income taxes are generated from the informal economy.

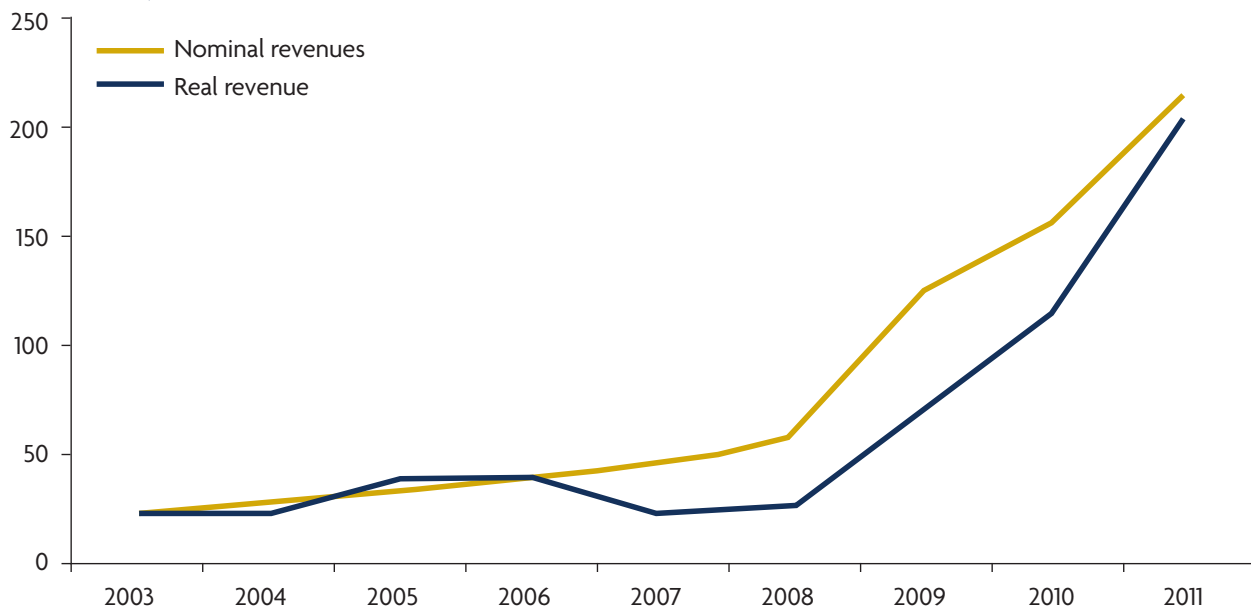
b. The UB government does not receive user fees for sewage, waste collection, or electricity because these services are provided by UB's independent companies.

and various PITs, including the unidentified income tax²¹ and the self-employment tax. The base and rates of personal income taxes (i.e., wage taxes, unidentified income taxes, self-employment taxes, and so on) are defined by

the parliament. The 2010 and 2011 amendments to the GTC authorize the city council to determine the rates for licenses, permits, user fees, and certain taxes—such

21. The “Unidentified Income Tax Law for Self Employment Activities” establishes lump-sum tax amounts by specific activity.

Figure 3.2. Trend of Current Revenue Budget of the UB Government and Districts in Nominal and Real Terms (in billions MNT)



Source: UB's executed revenue, as reported in table A1.1.

as property, vehicle, and capital city taxes.²² Districts do not have the authority to determine the rates of taxes, fees, and licenses.

Licenses and user fees. The UB government generates revenue from user fees on the productive utilization of land and water, while districts generate revenue from license fees for use of natural resources, with the exception of mineral licenses and hunting; household water consumption; and user fees for springs, timber, herbs, and common minerals.²³ User fees that generate higher revenues are assigned to the UB government; those that generate lower revenues are generally assigned to districts. Amendments to the GTC in 2010 and 2011 authorize UB

to determine rates for licenses and user fees, such as on tobacco sales, ground water extraction, and the keeping of wild animals. Districts do not have this same authority. Revenues of stamp duties are assigned to UB City government and district levels, although the law does not clearly differentiate the revenue assignment between the UB government and its districts.

User charges. User charges are meant for the payment of public services like electricity, water, heating, and garbage collection based on prices set by the central government. These services are provided by publicly-owned companies; therefore, the revenues generated from these services are not applied to the municipal budget.

Loans and credits. The BL allows the UB government, but not the districts, to borrow—upon the approval of the MoF—up to 15 percent of its base revenue for the previous fiscal year. UB may also borrow from the CG and incur debts for up to 4 years. The law also authorizes it to issue bonds.

22. Licenses and permits cover the following economic activities: manufacturing with emission, tobacco sale, digging or drilling groundwater, use of water in constructions, holding wild animal, use of extinct animal (species) for scientific purpose, sale of resources from herb and animals, hunting for manufacturing purpose, bringing stocks to the city for sale, use extinct herb species for scientific purpose, use of common herb in production, use of forest resources, veterinary services and medicines, use of springs and bottle water, sale and serve of alcoholic beverages, manufacturing of alcoholic beverages, and timber use.

23. It is important to note that the license fee set by law for mineral exploration is an absolute amount. Therefore, this fee is not buoyant, meaning that revenue from this fee does not increase with a boom in the mineral industry.

3.3. REVENUE TREND ANALYSIS: EMPIRICAL FINDINGS

Over the last three fiscal years (2009–11), the UB government's total *current* revenue has been growing, not only in nominal, but also in *real* terms. This is a sharp contrast to the period between 2003 and 2008; during that time revenues were stagnant (see figure 3.2). The *nominal* revenue growth rate of the last three years was substantially greater than the inflation rate (which actually declined), yielding a strong positive *real* growth rate in UB's revenue budget. This suggests that the UB government's financial situation has improved over the last few years, owing to an increase in revenues from the wage tax.

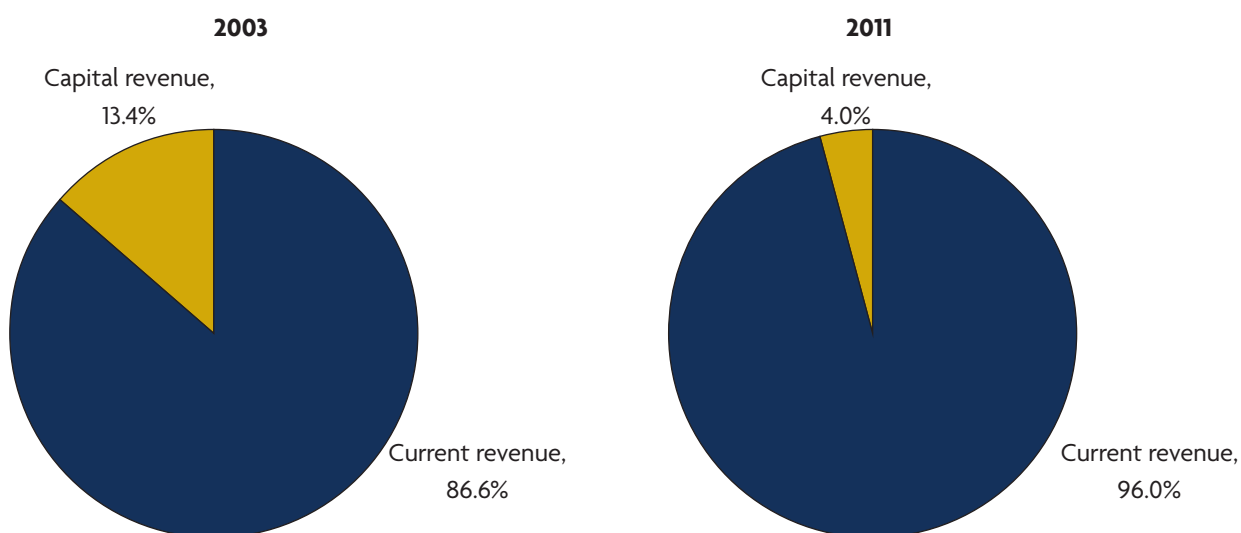
The revenue growth trend has contributed over time to an increase in the share of current revenues in total revenue, while the share in *own-source*²⁴ capital revenue

has been contracting. Nevertheless, the growth in revenues has increased the total amount of resources available to UB and the districts, allowing them to gradually address much-needed infrastructure and to improve municipal services. Specifically, while in 2003, current revenues accounted for 86.6 percent of the consolidated budgets (i.e., UB and districts combined), and capital revenues were only at 13.4 percent, in 2011, the current revenue share of the budget rose to 96 percent, and the capital revenue share decreased to 4 percent (figure 3.3).

With the growth of UB's population, per capita tax revenues have increased from approximately US\$4.2 in 2003 to US\$103.7 in 2011, based on a review of the consolidated budget of UB and its districts. (See figure 3.4 and table A1.7). This improvement is due to the increase in per capita tax revenues, especially wage taxes, the self-employment tax, and the property tax, particularly during the last three years; the improvement is also attributable to the improvement in *own-source capital revenues* (e.g., vehicle taxes, although the spike in 2011 is due to revenues generated from privatizing municipal assets). There were no significant changes demonstrated in other revenue sources.

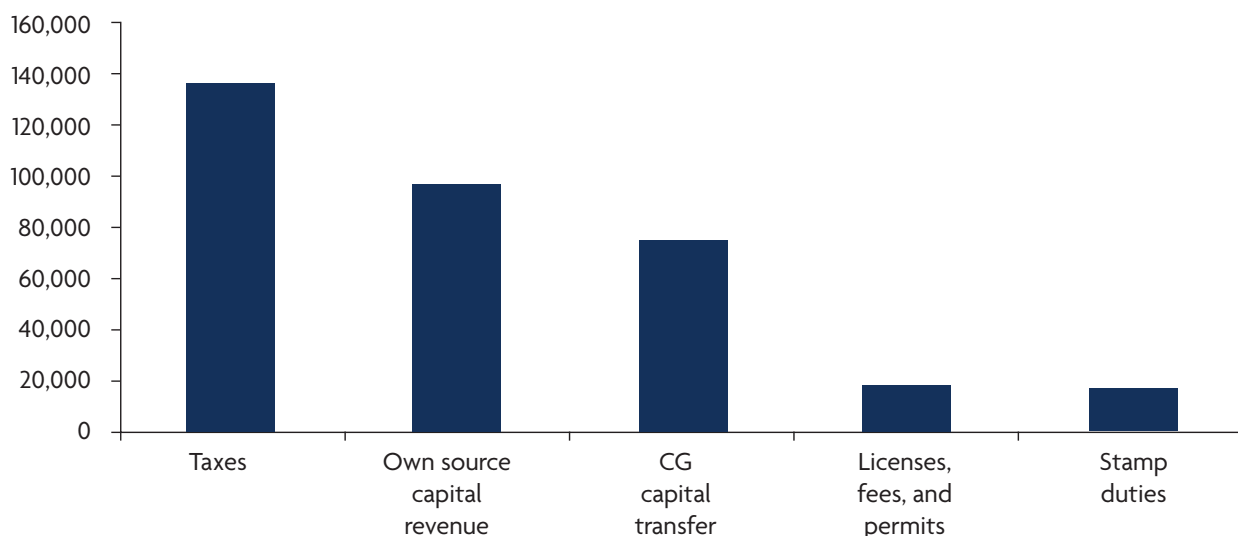
24. However, external sources of capital revenue from line ministries (which UB government reports in a separate budget) actually increased from 13 to 49 percent in the period 2003–11. This example, among others, suggests the importance of developing an integrated budget in order to have a comprehensive view of UB City finances.

Figure 3.3. Comparison of Current and Capital Revenue for the Consolidated Revenue of UB and Districts



Source: Data from UB treasury department (table A2.2).

Figure 3.4. UB and Districts Current and Capital Revenue Per Capita by Major Sources (in MNT for 2011)



Note: Own-source capital revenues consist of privatization revenues, vehicle taxes, and road fees.

Source: Elaborated for this study based on data from UB Treasury for 2011.

3.4. REVENUE SOURCES IN PRACTICE

There is a wider array of sources available for the current revenue budget than there is for the capital revenue budget (table 3.3), but the UB government has the discretionary powers to allocate resources between the two types of revenue sources.

Current revenues. The absolute amount of current revenues increased at an annual rate of 20 percent from 2004 to 2008, sharply rising by 120 percent in 2009, primarily due to the assignment of wage tax revenues to UB,²⁵ which accounted for approximately 37 percent

25. In this report the terms “UB” and “UB government” are used interchangeably.

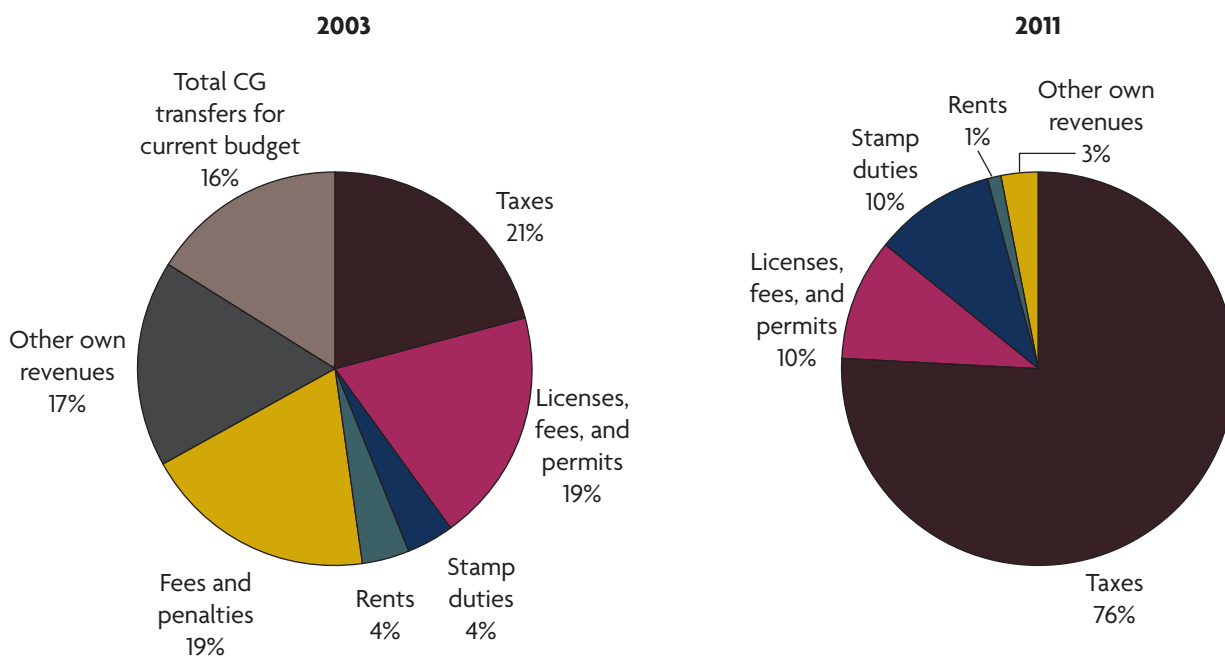
Table 3.3. Classification of Current and Capital Revenue Sources

CURRENT REVENUE SOURCES	CAPITAL REVENUE SOURCES
Licenses, fees, and permits	CG capital transfers
User charges	Capital transfers from development fund
Rents	Privatization revenues
Fines and penalties	Vehicle tax and road fees (i.e., Road Fund) ^a
Other (dividends of state-owned enterprises, own-revenues of municipal companies)	Property sale tax
Revenue-sharing in CG taxes	
VAT and CG grants	
Local Taxes	

a. According to UB government the proceeds from the Road Fund, along with other revenue sources are capital revenue—as illustrated in the “sources for investments” in page 26 of the Budget Book of 2012. The Road Fund is comprised by the vehicle tax and the road user fee. Therefore, these two taxes have been classified as capital revenue, even though in practice UB reports them as current revenue.

Source: Elaborated for this report based on current legislation.

Figure 3.5. UB and Districts: A comparison of Major Current Revenues



Source: Based on data from UB Treasury Department, 2003 and 2011.

of capital and current revenues combined. An increase in tax revenues is likely due to the country's improving economy, which in turn is contributing toward an increase in personal income. Due to the significantly higher rate of revenue flows resulting from the assignment of the wage tax to UB, the relative share of proceeds from licenses and fees declined from 19 percent in 2003 to 10.2 percent in 2011. Figure 3.5 illustrates the main changes in the revenue structure between fiscal 2003 and fiscal 2011. Taxes increased from 21 to 76 percent, primarily because of the new wage tax. Other revenue sources include stamp duties, which increased from 4 to 10 percent; other sources, such as fines and penalties and other, smaller own revenues have declined in importance.

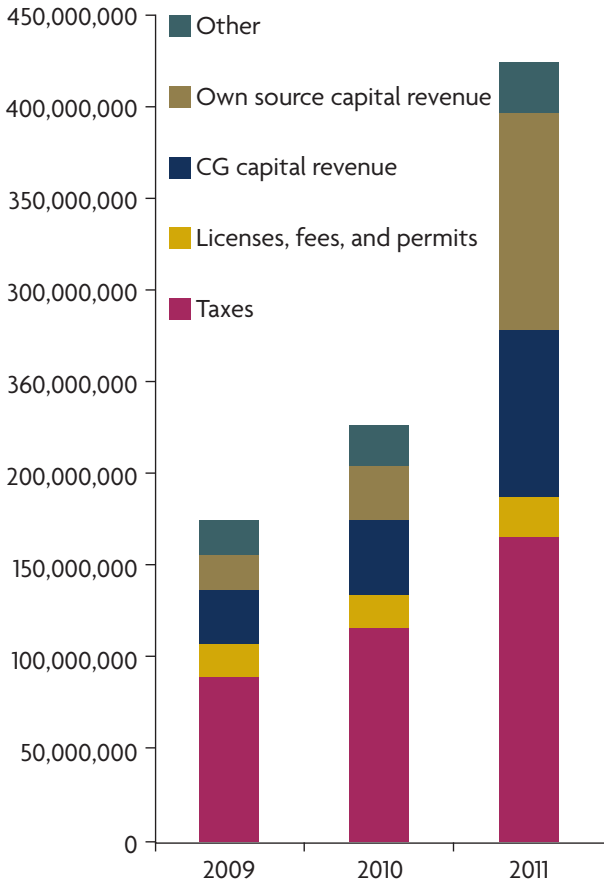
From 2009–11, the main sources of the current revenue were wage taxes—approximately 58 percent;²⁶ user fees for land—approximately 12 percent; and property tax—approximately 5 percent. Tax revenues, of which wage taxes are the largest source, collectively accounted for

approximately 73 percent of the current revenue between 2009–11, in contrast to 21 percent in 2003 (see table A1.1 for details). Furthermore, between 2009–11, the total amount of proceeds from taxes and capital revenues—especially *own-source capital revenue*—increased substantially compared to *licenses, fees, and permits* and *other revenues*, which have roughly stayed the same. The absolute amounts of these revenue sources are shown in figure 3.6.

The consolidated budget of UB and the districts are not that different from the UB government's budget alone, as illustrated in figures 3.7 and 3.8. In both cases, taxes account for the biggest share, followed by licenses and fees. This suggests that the current revenue structures of UB and the districts are rather similar, and that the impact of the districts on the structure as a whole is fairly marginal. The brief case study of two districts presented below (in Section 3.6) provides an example of district revenue structures.

26. These percentages are based on averages for the period 2009–11.

Figure 3.6. UB and Districts: Current and Capital Revenue by Composition, 2009–11 (in thousands MNT)

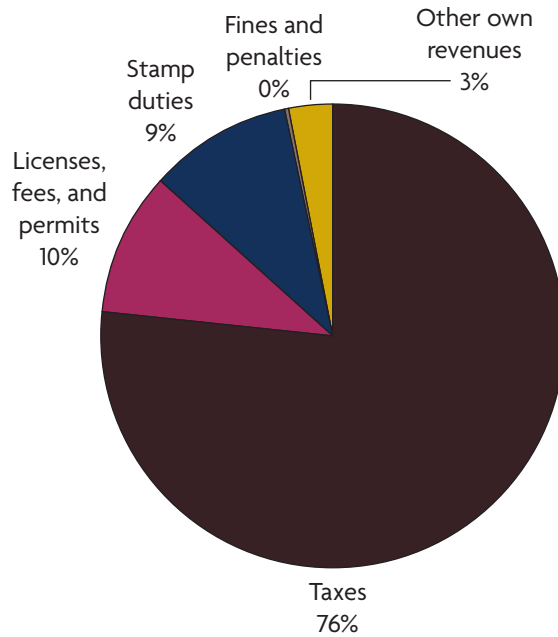


Source: Data from UB Treasury 2009–11. “Other” mainly includes user charges, rents, fines, and penalties.

3.5. CURRENT AND CAPITAL REVENUE BUDGETS

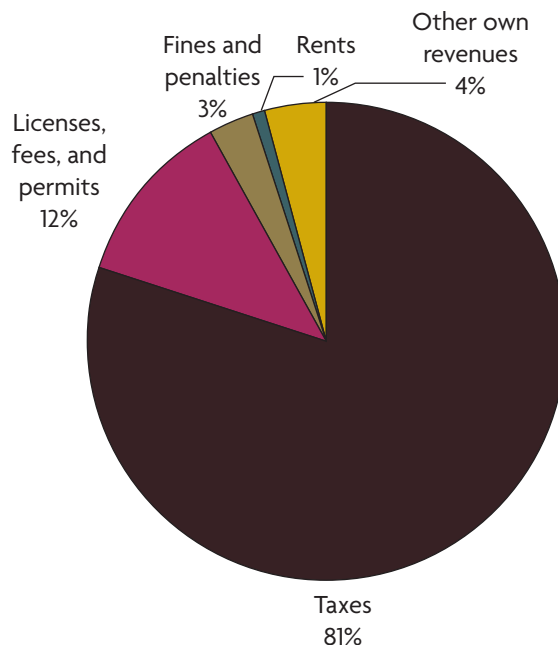
Capital Revenues. Following transfers from the central government, the development fund, and the surplus in current revenue from 2008 onward, the share of capital revenue to total revenue in UB and the districts has increased from an average of approximately 12 percent during 2003–07, to 43 percent in 2008 (see table A1.3). There is no substantial change in the amount of own-source capital revenue (e.g., vehicle tax, road fees, and privatization revenue) mobilized from 2003–10. However,

Figure 3.7. UB and Districts Current Revenue, Fiscal 2011



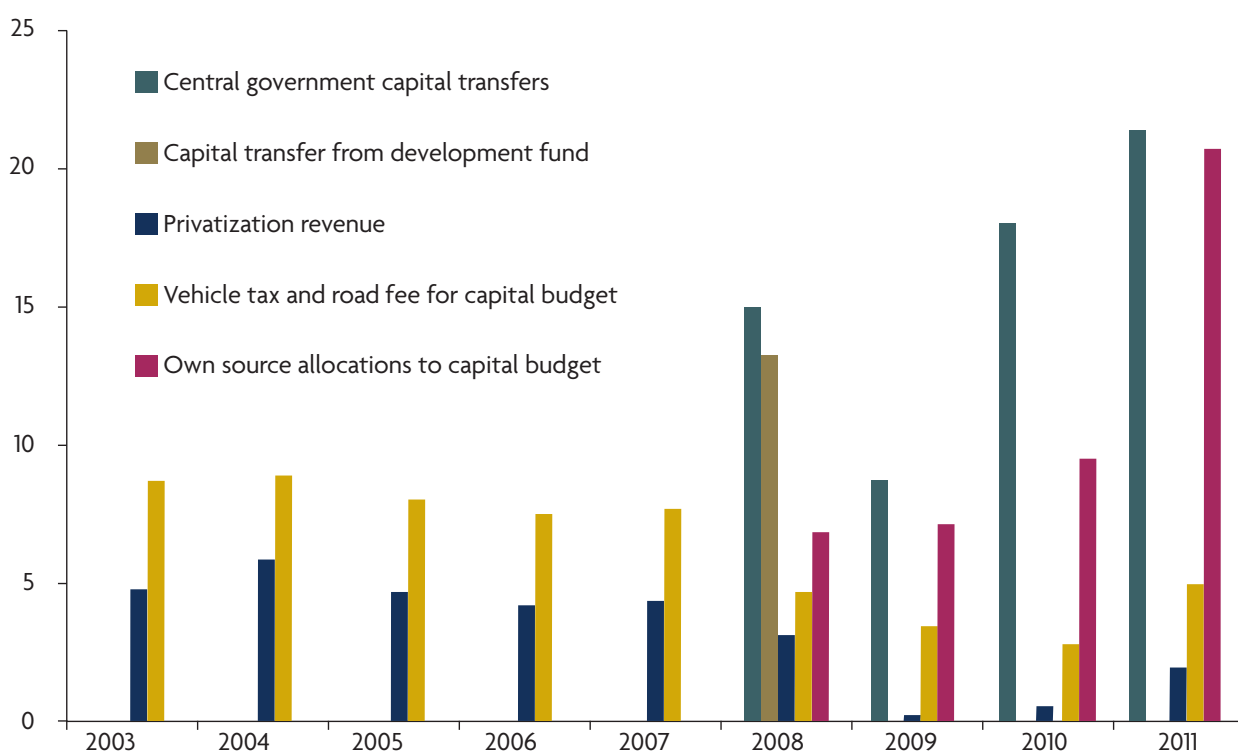
Source: Elaborated for this report based on UB treasury data.

Figure 3.8. The UB Government Current Revenue, Fiscal 2011



Source: Elaborated for this report based on UB treasury data.

Figure 3.9. Percentage of Revenue Sources in Total Capital Revenue in UB and its Nine Districts, 2003–11



Source: Executed data for 2003 through 2011. See table A1.1 for details.

in 2011, proceeds from privatization increased by 524 percent and proceeds from vehicle taxes and road fees increased by 229 percent compared to previous years. (See annual increases by revenue source in table A1.2 for details).

There is an increasing trend toward financing the capital budget using own-source allocations and CG capital grants, with a corresponding decrease in revenues from privatization and vehicle taxes. Between 2003–11, the relative weight of privatization and vehicle taxes both decreased—from approximately 5 to 2 percent, and 8 to 5 percent, respectively. By contrast, allocations to the capital budget from own-source revenue and CG capital transfers both rose—from approximately 7 to 21 percent, and from approximately 15 to 22 percent, respectively. These findings are illustrated in figure 3.9. It should be noted that in the past, the UB government only benefited twice from development fund resources—in 2008 and 2009 (figure 9).

It should be highlighted that the UB revenue budget format does not report the capital revenue from CG transfers from line ministries because they are reported in a separate budget. Considering that the actual budget format is not comprehensive, and lacks transparency this report has developed a broader classification of a revenue budget (included in table A1.1). For example, in fiscal 2011, under the actual revenue format, UB City reports 245.8 billions of MNT, while under a consolidated revenue budget report the total revenue of the city would be about 424.9 billion MNT. This comprehensive budget format shows that the revenues are 58 percent greater. In other words, UB’s “direct” revenue budget is equivalent to about 42 percent of the consolidated UB City revenue.

The road fund consists of proceeds from vehicle taxes and road fees for the financing of *capital* expenditures. However, UB and districts report these sources in the *current* revenue budget per the actual budget format. Moreover, according to the budget format, and the law,

revenues from privatization of municipal assets are to be included in the *capital* revenue accounts; and in practice, these are properly reported under the *capital* revenue budget. In order for UB finances to be consistent with the law and accurate, “*current* revenues” should be reported in the *current* revenue budget, and all “*capital* revenues” should be reported in the *capital* revenue budget. The lack of consistency in the budgeting of specific revenue sources distorts the actual availability of budget funds. Given the current magnitudes of these sources these distortions are relatively small, but it overestimates the revenues for operations and maintenance (O&M)—that is the *current* budget—and underestimates the availability of funds for *capital* investments (i.e., the *capital* budget). Therefore, planning with a smaller *capital* budget could potentially affect UB’s investment program for better local services. Finally, the budget surplus of the previous fiscal year is not reported in the revenue budget format of UB and the districts, but part of it is recorded in the expenditure budget as a financing source for capital investment. **The current budget formats, as they are, do not allow for a direct calculation of the balance between revenues and expenditures for the current and the capital budgets or for an accurate determination of surpluses or deficits.**

Finally, it is important to note that the city indirectly benefits from donor financing, grants, and loans. For example, the UB government has benefited from 43 investment projects, with a total value of US\$631.4 million, comprised of US\$176.6 million in grants and US\$454.7 million in loans from international organizations and foreign countries.²⁷ The proceeds of foreign aid, grants, and loans are decided and allocations are disbursed by the MoF. Because these investments benefit UB City, they should be reported as an annex to the budget.

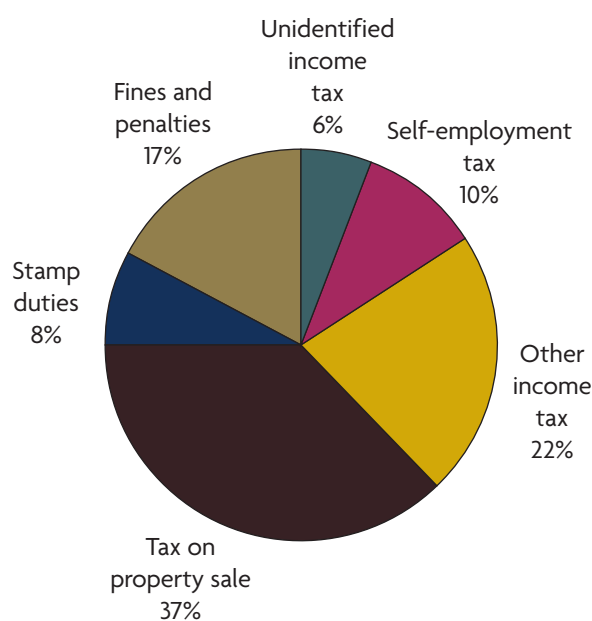
27. Data obtained from an interview with the head of foreign loan and donations unit with the development and planning department at the governor’s office in the UB government.

3.6. REVENUE MOBILIZATION AT THE DISTRICT LEVEL

UB City has six urban districts with populations ranging from 100,000–300,000: Bayangol, Sukhbaatar, Khan-Uul, Bayanzurkh, Chingeltei, and Songinokhairkhan (see maps in annex 3. UB City’s remaining three districts—Bagakhangai, Nalaikh, and Baganuur—are rural, with populations ranging from 3,000–35,000. A comparison of urban and rural districts illustrates the revenue generation capacity at the local level, using Bayangol (urban) and Nalaikh (rural) as case studies. Figures 3.10 and 3.11 illustrate the nominal revenue by source and share of the total revenue for 2011.

Like all remaining five urban districts, Bayangol only manages a current revenue budget and does not have capital revenues (see figure 3.10). Its main revenue sources are income taxes (38 percent), comprised of the unidentified income tax (6 percent), self-employment tax (10 percent) and other income taxes (22 percent). Taxes on property are 36.62 percent; fines and penalties, 16.6 percent; and stamp duties, 8 percent. Collectively, these sources accounted for 98 percent of total revenues in 2011.

Figure 3.10. Bayangol District Revenue, Fiscal 2011



Source: Elaborated for this report based on data from UB Treasury Department.

The remaining revenue sources were insignificant, generating less than 2 percent of the total revenue. Bayangol, much like the UB government, draws a significant share of its revenues from local taxes (e.g., 75 percent in 2011).

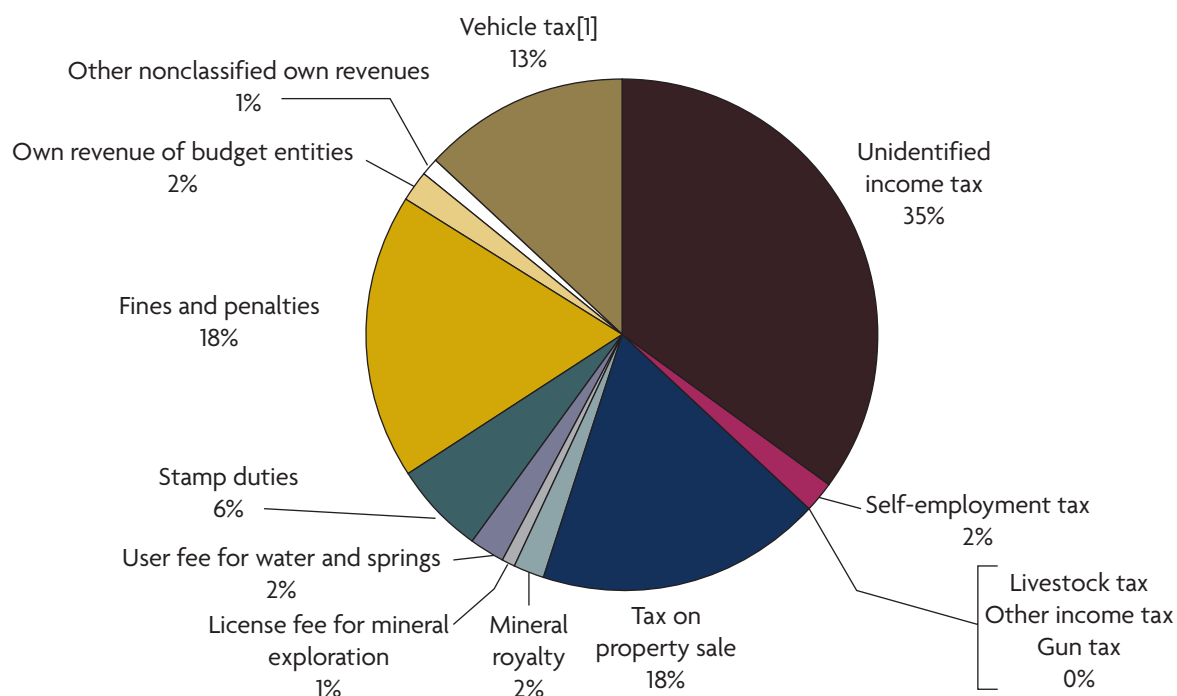
In contrast, in 2011, the rural Nalaikh district managed both a capital revenue budget (13 percent—derived from the vehicle tax) and current revenues (87 percent). Income taxes are the main source of current revenue, accounting for approximately 37 percent (consisting of the unidentified income tax and the self-employment tax); followed by property sales taxes, 18 percent; fines and penalties, 18 percent; stamp duties, 6 percent; and user fees, 2 percent (see figure 3.11).

In summary, the main revenue sources at the district level (urban and rural) are PIT and property sales taxes, followed by fines and penalties, which generate more than 70 percent of total revenue. The contribution of the remaining taxes and user fees is fairly small and has high administrative costs. Between 2003 and 2008, UB

shared VAT revenues with districts, although this was terminated by law in 2009. In practice, rural districts (Nalaikh, Baganuur, Bagakhangai) have one revenue source that urban districts do not, which is the vehicle taxes that is classified as current revenue but could be allocated to capital revenue for roads rehabilitation. In practice and according to the law, UB collects vehicle taxes in the urban districts and has the authority to spend the revenues generated.

A comparison of per capita revenues in these two districts illustrates the revenue efforts and fiscal capacity of one urban and one rural district (See figures 3.12 and 3.13). Between 2009 and 2011, per capita total revenues for Bayangol were almost twice as high as those of rural Nalaikh. The only exception is the gun tax, which was the same in both districts (approximately 30 Tugriks per gun). As expected, this finding confirms that an urban tax base usually has a greater revenue potential than a rural one. Future research will need to be conducted comparing all urban and rural districts in order to determine the

Figure 3.11. Nalaikh District Revenue, Fiscal 2011



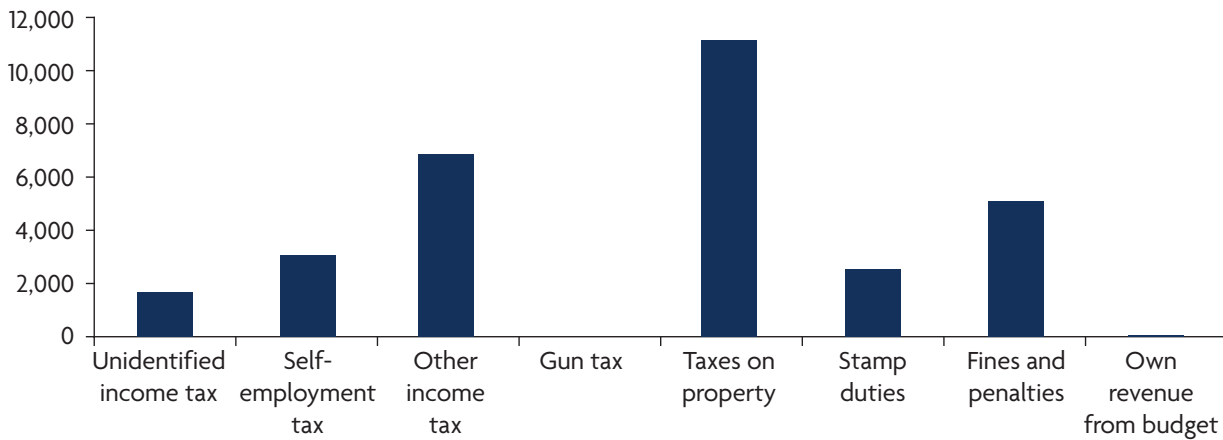
Source: Elaborated for this report based on data from UB treasury department.

differences in tax effort and to examine whether these differences are inversely related to the budget support they receive through fiscal transfers.

The revenue structure of rural districts seems to be more diverse than that of urban districts. Bayangol's per

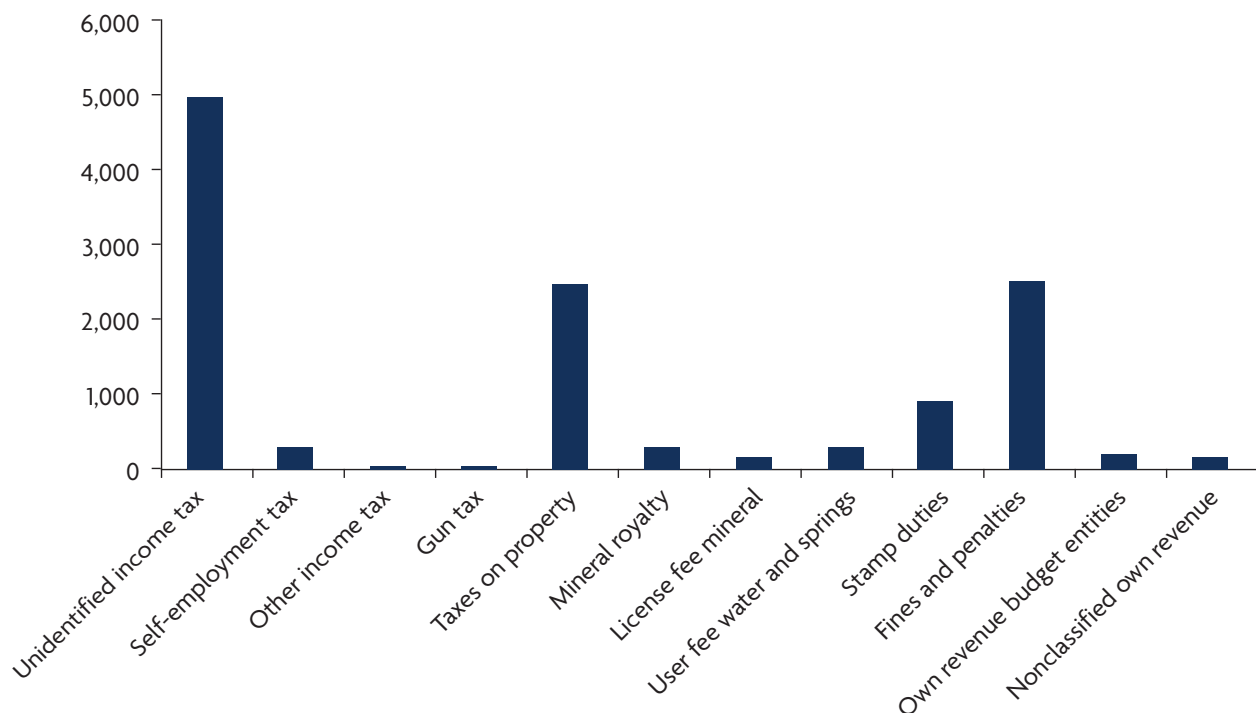
capita revenue sources have no user fees and consist primarily of taxes and stamp duties. In contrast, Nalaikh district collects revenue from user fees, such as mineral royalties, license fees for mineral exploration, and user fees for water supply and springs. Similar patterns can be observed in other urban and rural districts. This finding

Figure 3.12. Bayangol District Current and Capital Revenue per Capita, Fiscal 2011, in MNT



Source: Elaborated for this report based on data from UB Treasury Department.

Figure 3.13. Nalaikh District Current and Capital Revenue per Capita, Fiscal 2011, in MNT



Source: Elaborated for this report based on data from UB treasury department.

explains the limited fiscal potential of rural districts, which rely more on user fees that generate smaller revenues.

Empirical results reveal that per capita revenue only increased slightly in Nalaikh, the rural district with a population of 32,500; the per capita revenue of the urban district Bayangol grew significantly from 2009–11 (see table A1.8 for details). This sharp increase was due to a rise in taxes on property sales and may also be explained by Mongolia's robust economic growth since 2010 and its rapid urbanization since 2000. High economic growth and urbanization are characterized by greater urban productivity, which is reflected in high personal income or greater purchasing power for both private and public goods. The differences in per capita revenue among urban and rural districts may also lie in the economic abilities of their residents.

3.7. INTERNATIONAL COMPARISONS

When compared to international standards, the relative importance of the property tax in UB ranks among the lowest, especially considering that UB represents the largest and most valuable urban tax base in Mongolia. By contrast, local income taxes rank among the highest when compared with that of other nations. More than one third (36 percent) of UB's total revenue comes from income taxes, as illustrated in table 3.4. This makes the relative importance of local taxes in UB's revenue structure greater than it is in more advanced economies.

It is also worth noting that UB's own revenue sources represent close to 80 percent of UB's total revenue. Capital grants from the CG were equivalent to 21 percent. In contrast, among southeastern European countries, the average ratio of own-source revenue is approximately 34 percent,²⁸ illustrating that local governments in these countries are more dependent on CG transfers than on their own local tax sources.

It is important to highlight that business licenses and local business taxes on industrial and commercial

activities are fairly modest in UB (e.g., Stamp duties were equivalent to only 4.8 percent of total revenues in fiscal 2011). In contrast, the reason the property tax is negligible is due in part to the fact that formal housing is exempt from property taxes. The property tax in UB is levied only on businesses. In best international practices, local taxes on industrial and commercial activities are a fairly important revenue source, and so are property taxes on formal housing, which suggests a direction for future tax policy reforms in UB.

3.8. CONCLUSION

Because Mongolia is a unitary state where legislative and administrative authority are concentrated at the central level, authority is only partially delegated to UB City. Since almost all taxes are legislated by the central government, UB City has no authority to introduce new taxes. International experience suggests that subnational governments should have considerable power over their own revenues because they are best suited to understand their specific needs and make appropriate adjustments. According to current legislation, UB City can set the rates for a few taxes and for user fees within limits set by the parliament. However, some of these taxes generate comparatively low revenues. For example, property taxes and vehicle taxes only account for 4 percent of total revenues, and other user fees generate less than 1 percent.

Due to the centralized tax administration system, there is little incentive at the local level to generate revenues higher than the approved amounts because any increase is equalized by one-to-one reductions in tax-sharing or transfers. Vertical fiscal management creates uncertainty and unpredictability for the municipal government as the MoF determines fiscal transfers from the UB government to the CG in a discretionary manner. In addition, because of the cost of the administration of local taxes, collecting central taxes is in the best interest of the municipal government. The current rules in revenue collection do not encourage municipal governments to generate additional own revenue.

28. Network of Associations of Local Authorities of South East Europe (NALAS): Report on Fiscal Decentralization Indicators for South-East Europe. NALAS (March 2012); p. 24.

Table 3.4. Structures of Local Revenues for Selected Countries, 2006 (in percent)

	PROPERTY TAXES	INCOME TAXES	TOTAL TAXES	GRANTS	OTHER REVENUES	OWN REVENUES	TOTAL
Australia	39	31	43	14		83	100
Belgium		0.1	38	54		46	100
Botswana	8		10	83		17	100
Brazil	4		13	65		35	100
Canada	38	44	39	42		54	100
Denmark	3		47	39		57	100
Finland	2	7	39	29		72	100
France	34		46	29		65	100
Malaya				26		74	100
Thailand	8		55	31		69	100
Bulgaria	20		20	30	50	70	100
Croatia	3	46	61	12	27	88	100
Russia	8	0.1	31	58	11	89	100
Ukraine	2	23	42	48	10	90	100
China	38		39	42	19	81	100
Kenya	16		21	33	46	54	100
Mauritius	12		26	67	7	93	100
South Africa	17	7	20	25	55	45	100
Uganda	3	1	5	92	3		100
Bolivia	19	8	72	18	10		100
Cities:							100
Cape Town	25		25	25	9	25	100
Toronto	42		42	21	16	22	100
Madrid	12		31	39	14	16	100
Mumbai	19		65	4	8	23	100
Ulaanbaatar ^a	2.8	36	43.9	21.4	34.7	78.6	100

Source: E. Slack 2009—UNHABITAT.

a. Ulaanbaatar was added to this table by this study.

The analysis of the *current* and *capital* revenue structure shows that the budget format of UB and the districts is not in accordance with international best practices and some specific current and capital revenues are not reported in accordance with their intended purpose. For example, the vehicle tax, a source of capital revenue, is reported on the current revenue budget. Conversely,

the revenue from the property sales tax (apparently meant for the financing of the current revenue budget), is reported in the capital revenue budget. The UB government should consider improving the budget classification format for more clarity and transparency and greater accuracy in its financial situation. It would contribute towards the achievement of international standards.



Chapter 4. Expenditures

4.1. EXPENDITURE FUNCTIONS OF UB AND ITS DISTRICTS AND THE ADEQUACY OF REVENUE ASSIGNMENTS

Since transition, political and administrative reforms have made a gradual attempt to shift spending responsibilities and decision making from the central government (CG) to local governments, as summarized in table 4.1.

Despite the considerable legal efforts made to resolve ambiguities in functional responsibilities, there continues to be substantial overlap across different levels of the government. The Public Sector Management and Finance Law (PSMFL) attempted to clarify assignments of functions by distinguishing between those functions that are the sole responsibility of local governments and those that are delegated by the CG to local governments. The functions associated with local economic development and local infrastructure are the

Table 4.1. Summary of Legal Expenditure Functions

LAW	EXPENDITURE FUNCTIONS
Public Sector Financial Management Law (PSMFL) was approved by the parliament in 2002 and became effective on January 1, 2003. In Art. 52.2 it assigned nine core functions to subnational levels of government for the provision of basic local services	<ul style="list-style-type: none"> • Sanitation (Public hygiene; waste removal, treatment and disposal) • Environment protection and conservation; gardening renewal and maintenance • Pest eradication and control • Local road maintenance • Normal operations of water, sewerage, and drainage systems • Flood barriers and soil protection • Fire protection, prevention, and mitigation • Local public infrastructure facilities • Fight and prevention of infectious livestock and animal diseases
Law on Territorial and Administrative Units (LTAU of 2006) added three local responsibilities to aimags and the capital city (Article 29)	<ul style="list-style-type: none"> • Public safety • Disaster protection • Public order
LTAU (2006) assigns districts and soums four additional services (Article 31)	<ul style="list-style-type: none"> • Water supply • Garbage collection • Street lights • Park maintenance
LTAU (2006) expands local government functions (Article 31)	<ul style="list-style-type: none"> • Road planning • Communication lines • Land management
Capital City Legal Status Law (CCLSL), revised in 2010 and still subject to final approval, establishes special functions for the capital city and its districts. (Article 4.9.3)	<ul style="list-style-type: none"> • UB can “participate” in establishing and developing integrated networks • Power networks • Road networks • Transportation networks • Communication and information technology networks

(continued)

Table 4.1. Summary of Legal Expenditure Functions (continued)

<p>The budget law was approved by the parliament on December 23, 2011.</p> <p>It is also referred to as the Integrated Budget Law. It consolidates functions already established by previous laws (as listed above), makes explicit old expenditure responsibilities, and assigns new functions.</p> <p>Article 58.1 of the BL established seventeen expenditure functions for the capital city—as listed on the right hand side column of this table.</p>	<ul style="list-style-type: none"> • Capital city management • Urban planning, construction, and building new infrastructure • Maintenance of the capital city’s constructions and buildings, establishing new property, and making investments • Social care and welfare services • Implementing programs and measures to support employment and alleviate poverty • Development of small and medium-sized enterprises • Pasture management • Building water supply, sewerage, and drainage systems • Housing and public utility services • Flood protection • Public transportation services • Fight of infectious livestock and animal diseases; pest eradication and control • Disaster prevention • Environmental protection and rehabilitation • Building large-scale roads; bridges and their lighting; traffic lights and other related construction • Utility services for public areas, landscaping, public hygiene, street lighting, cleaning, and waste removal • Operations and maintenance (O&M) of high voltage and electricity lines and substations and other service-related activities • Other functions specified in law
<p>The BL establishes seven main functions for UB districts are listed in Article 58.3 of the BL.</p>	<ul style="list-style-type: none"> • District management • Social care and welfare services provided subsequent to the decision of district governors • Utility services for public areas, public hygiene, street lighting, cleaning, and waste removal • Promotion of intensified raising of livestock • Protection of nature and the environment • Recurrent maintenance of lighting of public areas • District landscaping, and development and maintenance of sidewalks, recreational areas, and children’s playgrounds • Other functions as defined in law

Source: Elaborated for this report based on respective legislation.

a. This function includes, among other responsibilities, land distribution and conflict resolution on land ownership issues.

mandate of local governments and must be financed through local revenue sources. Solid waste collection, water supply, and sewerage systems are typical household services generally financed with user fees. Services such as fire and flood protection, street lighting, and park maintenance are local services that should be financed through local taxes. The 2006 Law on Territorial and Administrative Units (LTAU)²⁹ established the autonomy

of local governments by emphasizing that upper levels of government are not to interfere in services that are the mandate of local governments. However, the division of responsibilities remains unclear. For example, in the Budget Law of 2011 (BL), most of the functions assigned to the nine UB districts are also assigned to the UB government as a whole, as illustrated in table 4.1.

29. As established in articles 29, 30, and 31.

Another key challenge for local governments—particularly the UB government—is to ensure that this gradual increase³⁰ in the assignment of expenditure responsibilities is supported by adequate revenue sources and institutional capacity to administer the effective implementation of these functions. **For the most part, the current expenditure assignment to subnational governments meets basic economic efficiency criteria and fundamental public finance principles.** Based on the *benefit* principle of public finance, residents of local jurisdictions, through their taxes and user fees, are generally financially responsible for the expenditures that primarily benefit them. Therefore, those who contribute to the financing of local services are primarily those who benefit from them. However, services intended primarily for income redistribution or one that are of a social nature, such as “social care and welfare services” or “employment and poverty alleviation,” would benefit from central-government financing to meet national goals, even though local governments might be better at the operation of such services. To a large extent, the local assignment of expenditure functions appears consistent with the *subsidiarity* principle—that is, a public service ought to be handled by the smallest, lowest, or least-centralized authority capable of effectively addressing the service.

The financing of other social services—those that may be characterized by their *spillover effects* (or positive *externalities*)—have been assigned to the central government. The PSMF in 2002 assigned the provision of key social services (education, health care, culture, labor, social welfare, and social security) to the CG but stressed that some of these could be delegated to local governments with financing from the state budget. These specific assignments of expenditure responsibilities enhance economic efficiency and interjurisdictional equity. These delegated responsibilities are implemented through contractual agreements between local governments and line ministries. Furthermore, the LTAU in 2006 explicitly states that local governments share authority with the CG in functions such as finance, planning, tax collection, local property administration, agriculture, mineral resource and land use, construction, parks, transportation, road building, communication, energy supply, education, health,

30. Such as those most recently assigned functions—as established in the BL of 2011.

culture and sports, social security, sanitation, and public order and safety.

Infrastructure that supports economic development (i.e., road networks, power distribution, transportation and communications, public safety) also benefits other jurisdictions and the country at large. Therefore, the financing of such services should not be the sole financial responsibility of the UB government and its districts. For a more economically-efficient provision of such services, financing should be a shared responsibility between central and local governments, subject to specific and objective indicators of *need* and local *fiscal capacity*. Therefore, UB City has proposed a revised Capital City Legal Status Law (CCLSL).³¹ This revision of the law was submitted to the parliament in 2011 and is pending approval. Its key feature, from a service provision and an expenditure point of view, is that it authorizes the UB government to participate in the establishment of network infrastructure (for power, roads, transportation, communication, and information and technology) and to generate revenues from new sources. The current and newly-proposed assignment of expenditures under the draft CCLSL is consistent with best international practices.

Most recently, as noted above, the BL of 2011 established the most comprehensive set of expenditure functions for the capital city and its districts—as well as for the aimags and the soums. However, there is still substantial duplication of functions between those assigned to UB City and the districts. **The BL still leaves part of the financing of several “local” government functions open to negotiations between the CG and the UB governor and the UB governor with district governors. This legal feature weakens the fiscal and political accountability of subnational governments with respect to adequate service provision.**

Table 4.2 summarizes core services provided by different levels of government, differentiating between assigning, financing, and service-delivery authorities. It also illustrates those functions for which there is an overlap in *financing* responsibility between the central and

31. The original law was approved by the parliament on July 5, 1994.

Table 4.2. Current Expenditure Assignment Functions for Local Governments in Mongolia

ROLE OF DIFFERENT GOVERNMENTAL LEVELS OF AUTHORITY			
EXPENDITURE FUNCTION	EXPENDITURE ASSIGNING AUTHORITY	FINANCING AUTHORITY	SERVICE-DELIVERY AUTHORITY ^a
Education			
Kindergarten	Central	Central	Local ^b
Primary School	Central	Central	Local
Secondary School	Central	Central	Local
Universities	Central	Central	Central/local
Health			
Hospitals	Central	Central	Local
Health Centers	Central	Central	Local
Epidemiology	Central	Central	Local
Social Welfare			
Social Protection	Central	Central	Central/local
Social Assistance	Central	Central	Central/local
Housing and Services			
Housing	Central/local	Central/local	Central/local
Sanitation and Disposal	Central	Local	Local
Water Supply	Central	Central/local	Central/local
Sewage	Central	Central/local	Central/local
Recreation and Culture			
Recreation	Central	Central	Local
Sports and Culture	Central	Central	Local
Economic Sectors			
Fuel and Energy	Central	Central	Central/local
Road Construction	Central	Central/local	Central/local
Transportation	Central	Central/local	Central/local
Environmental Protection	Central/local	Central/local	Central/local
Public Order and Safety	Central	Central	Local

Source: A comprehensive summary of functions may be seen in Ariunaa (2010).

a. As part of the CCLSL, UB may be required to deliver (subject to a contract) some of the social services currently provided by the CG through the line ministries.

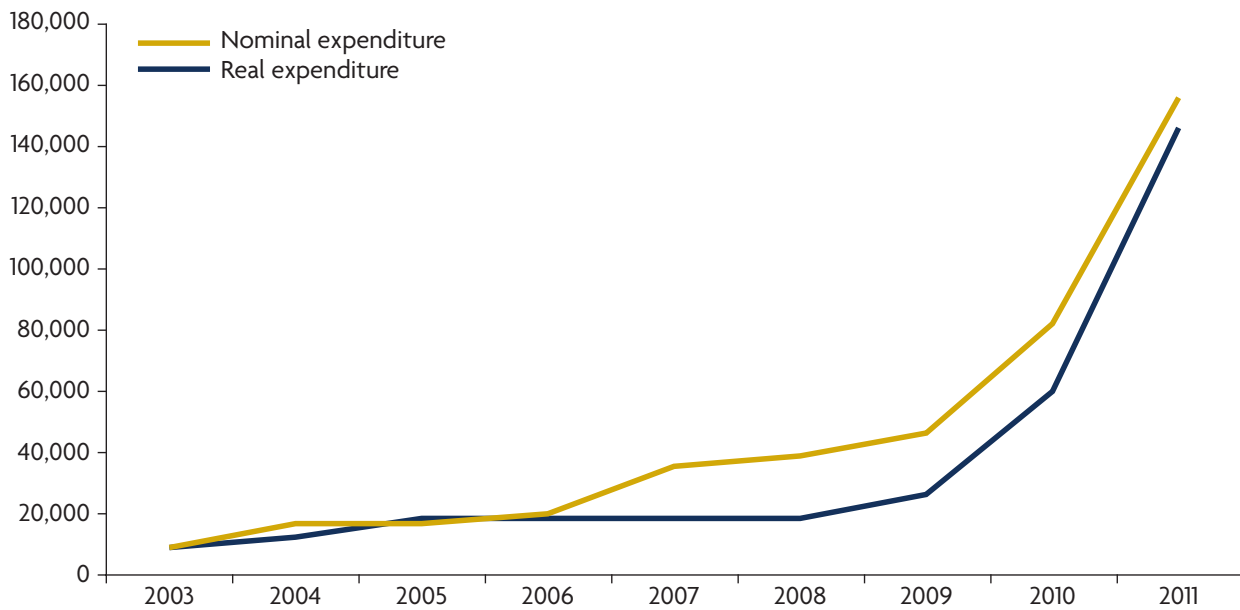
b. The legal term "local" is inclusive of UB and/or its districts.

local governments.³² For example, there is dual financing authority for public housing, water supply, road construction, transportation, and environmental protection. In contrast, there are some services for which the central

government has financing responsibility but, in practice, UB and its districts play an important role in service delivery (e.g., social assistance and protection, health, education, and public safety).

32. The law does not distinguish between the UB government and its districts.

Figure 4.1. Current Expenditure Trends in the UB Government in Nominal and Real Terms (in millions MNT)



Source: Elaborated for this report based on executed budgets 2003–11.

Because of the mobility of human resources, services such as education, health, social welfare, and recreation/sports and culture may be characterized by having benefits that spread over the nation as a whole. As such, in best international practices, these services are typically financed by the CG, as is the case in Mongolia. By contrast, most of the remaining services may be characterized as having benefits that are both local and national. Therefore, in principle, their financing should be shared.

In areas where there is an overlap in expenditure responsibilities across different levels of government, there is a corresponding lack of clarity on how to share financial responsibilities. This is most often done through a process of negotiations. For example, the central government may finance new investments, while local governments finance operations and maintenance (O&M). To ensure fiscal and political accountability, in best international practices, a clear distinction is made for financing O&M and capital costs. While investment costs—such as for roads—might usually be financed by CG grants, a functional distinction can be made regarding a typology of roads for the purposes of assigning expenditure responsibilities. The best intergovernmental fiscal designs

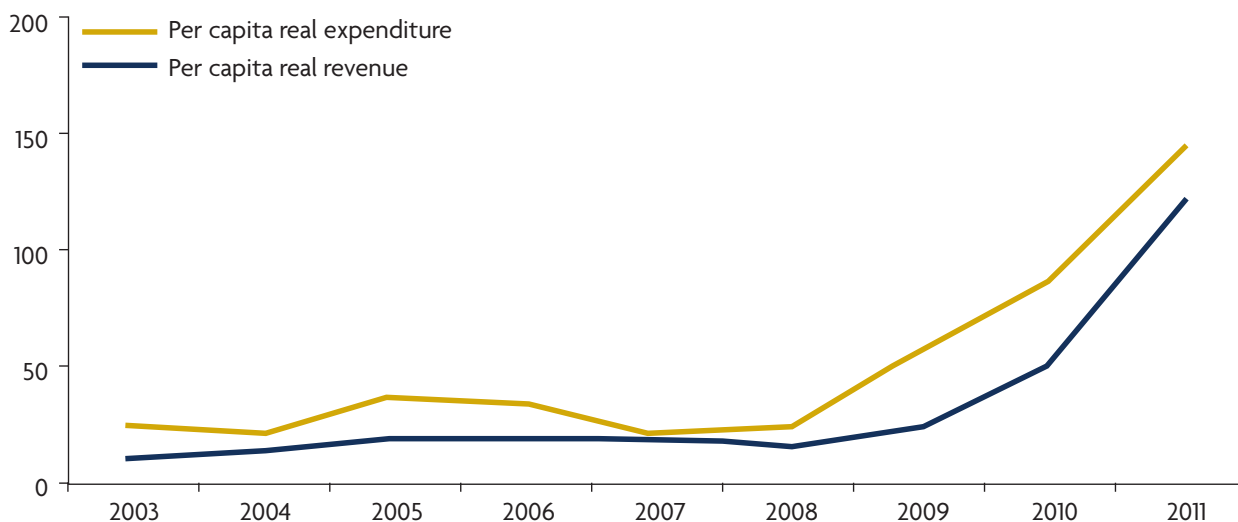
vary depending on the specific characteristics of each sector and revenue source but may include a range of formula-based grants comprised of *conditional*, *matching*, or *block grants*. The UB government would benefit from a technical assignment of alternative options for funding roads. UB City has been relatively neglected by state investments in favor of rural areas. This relative neglect is visible in increased traffic congestion. For example, it was determined that the “average recorded traffic speed in the city has declined from 25 km/h in 1998 to only 14 km/h in 2008.”³³

There is a corresponding lack of clarity in service provision functions between the UB government and its districts. For example, the PSMFL assigns nine functions on local service provision to the UB’s governor, while these same responsibilities are also assigned to the district governors (Article 53).³⁴ Current laws, including the BL would benefit from regulations that clarify these overlapping authorities and responsibilities.

33. World Bank; Mongolia: Improving Public Expenditures (2012); page 14.

34. See articles 52 and 53.

Figure 4.2. Trends in UB's Per Capita Revenues and Expenditures (in thousands MNT)



Source: Elaborated for this report based on executed budgets for fiscal 2003–11 and population data.

4.2. EXPENDITURE TREND ANALYSIS: EMPIRICAL FINDINGS

This section reviews trends in the UB government's current (operating) expenditure budget in order to identify functions where expenditure performance could be strengthened for more effective and efficient municipal service provision. *Nominal current* expenditure has generated annual savings, not deficits, in operations. In *real terms*, and consistent with the revenue trend presented in chapter 3, expenditures were stagnant between 2003–08. In the last three years, however, UB's nominal and real expenditures have rapidly increased, keeping up with revenue trends. This is illustrated in figure 4.1.

UB officials have expressed concern that the city may not be able to cope with the service provision needs of the growing population that has increased from approximately 890,000 in 2003 to approximately 1.2 million in 2011, despite growing revenues. **When measured in per capita terms, real revenues and expenditures have also been growing steadily during the last three years, as illustrated in figure 4.2.**

In short, empirical evidence suggests that population growth has not had a *net* negative effect on UB's financial

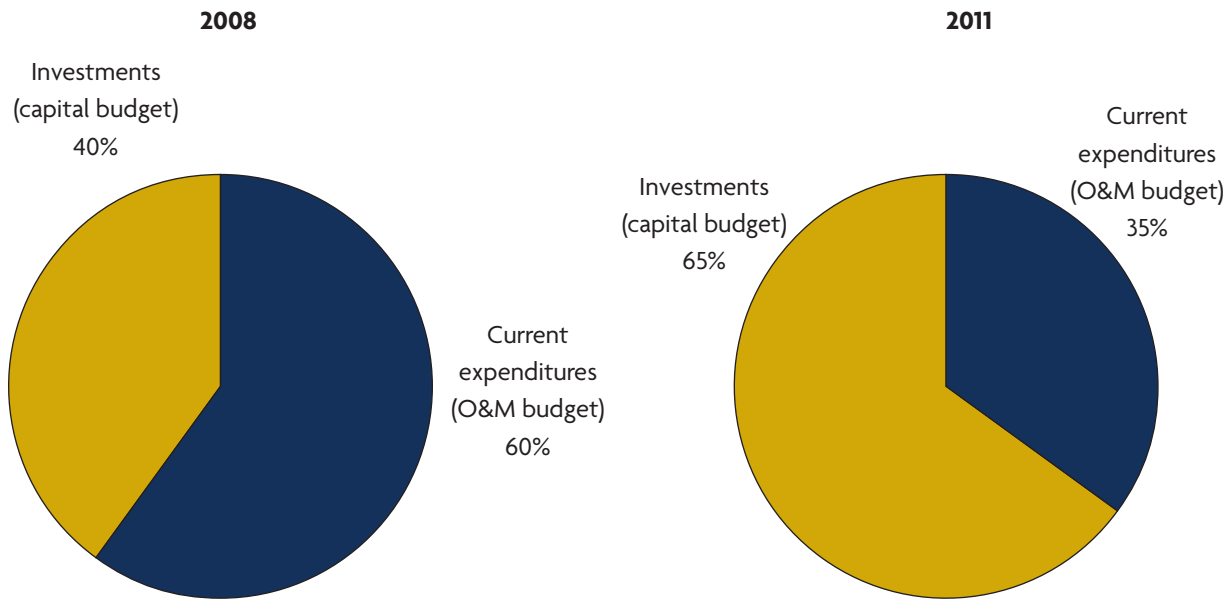
situation. However, further analysis is required to assess service coverage and quality standards associated with current expenditure levels.

4.3. CURRENT AND CAPITAL EXPENDITURE STRUCTURE

This section examines the UB government's expenditures, differentiating between *current* expenditures in O&M and capital investments for development. The empirical findings³⁵ indicate that UB is increasing its capital expenditures, expanding public services, and developing local economic infrastructure. UB's total expenditures for the current and capital budget increased from 39 billion Tugrik (US\$29 million) in 2008 to approximately 141 billion Tugrik (US\$107 million) in 2011. While in 2008, expenditures for capital investments accounted for 40 percent of the budget, by 2011, this figure had reached 65 percent. Similarly, the proportion of funds spent on O&M dropped from 60 percent in 2008 to 35 percent in 2011, as illustrated in figure 4.3. This trend in the relative weights of current

35. For comparison purposes, this section has specifically selected the data for the most recent executed fiscal year (2011) and compares those empirical results with the corresponding figures for fiscal 2008 because this is the earliest year for which there are disaggregated figures available. In this way, it is possible to see how the expenditure structure has evolved during the last four years.

Figure 4.3. The UB Government Current and Capital Expenditures, 2008–11



Source: Elaborated for this report based on UB’s executed budgets for fiscal 2008 and fiscal 2011.

and capital expenditures is consistent with the expected changes in the expenditure structure of rapidly-growing cities.

In absolute terms, current expenditures more than doubled between 2008–11, increasing from 23.4 to 48.8 billion Tugrik (equivalent to US\$17.7 million to US\$37 million), while capital expenditures increased sixfold, from nearly 17.8 billion to over 118.5 billion Tugrik (equivalent to US\$13.6 million to US\$89.9 million). UB investment is equivalent to 1 percent of gross domestic product (GDP), which ranks³⁶ on the low side when compared to south-eastern European nations, the highest being Slovenia (2.9 percent). This is, however, a rough indicator of performance because it only includes the UB government.

4.4. UB’S CURRENT EXPENDITURE BUDGET

In 2008 (the first year for which disaggregated numbers are available), the highest level of current expenditures (49 percent) was spent on subsidies to cover the cost of

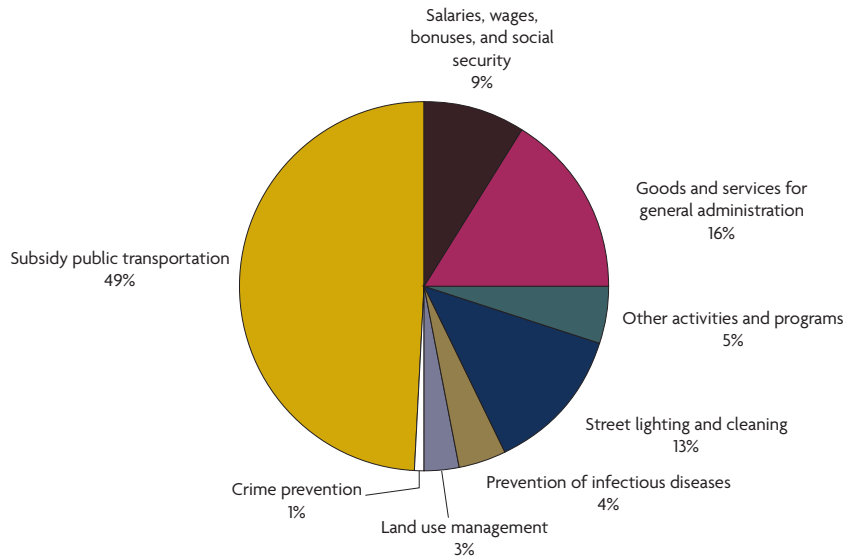
public transportation for students and the elderly (11.3 billion Tugriks, equivalent to US\$8.6 million). This level of subsidy is unusual by international standards but somewhat common in countries with a heritage of centrally-planned economies where public transportation is heavily subsidized.

The second most important expenditure (25 percent) relates to the UB government’s general administration (comprised of 9 percent in salaries and human resources payments and 16 percent in goods and services to support general administration and operations). The rest of UB’s current expenditures were allocated to five local services: street lighting and cleaning, the prevention of infectious diseases, land use management³⁷ (e.g., conversion of public lands to private use, land use zoning, conflict resolution associated with land, and so forth), and public safety. “Other activities and programs” (e.g., cultural activities) is equivalent to approximately 5 percent of the budget. A summary of the budget structures for 2008 and 2011 are illustrated in figures 4.4 and 4.5, respectively.

36. NALAS. 2012. Fiscal Decentralization Indicators for southeast Europe, p. 31, chart 14.

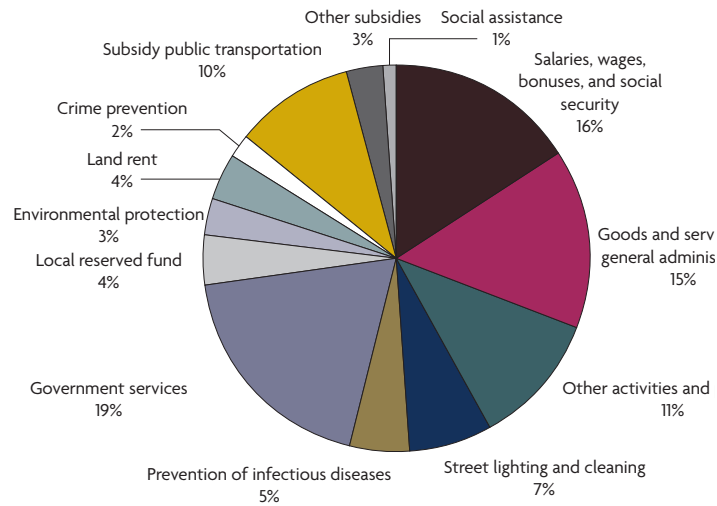
37. Expenditures on “land use management” should not be confused with rent payments on land (“land rent”).

Figure 4.4. The UB Government Current Expenditure, 2008



Source: Elaborated for this report using 2008 executed budget data.

Figure 4.5. The UB Government Current Expenditures, 2011



Source: Elaborated for this report using 2011 executed budget data.

Comparing spending in 2008 with spending in 2011, the main conclusions are as follows:

- On the whole, in 2011, the city maintained the services it provided in 2008; increased revenues enabled it to add some new ones, including environmental services and social protection.
- Following a policy decision to significantly curtail the public transportation subsidy, it dropped precipitously from 49 percent of the total *current* budget in 2008, to only 10 percent in 2011.
- The proportion of spending on salaries and general administration increased from 25 percent in 2008 to 31 percent in 2011.

The lack of transparency in some expenditure classifications significantly increased. The purpose of spending on over 30 percent of the *current* budget cannot be determined by reviewing the budget documents alone. For example, expenditures classified as “payments for services required by the government” (at 19 percent of the budget) or “other activities and programs” (at 11 percent) are unspecified, and as such are unknown. Equally obfuscating are expenditure entries that refer to financing sources (for example, “surplus from the previous fiscal year” or “local reserve fund”).

The UB government’s current expenditure format deviates from best practices in several ways, making it difficult to use the current budget as a tool for decision making. First, as already indicated, it is not always possible to determine the use of funds. Under best practices, expenditures in O&M associated with the provision of local public services are reported on separately from those related to the general administration; this clarifies the budgetary cost of providing specific services. The UB government’s primary role is to ensure the provision of services, either directly or indirectly, through local service companies (water supply, solid waste, and so on). When these services are provided by enterprises, the expenditures should be reported in an annex to the municipal budget to assist with decision making. City leaders need to know how much is being spent on a municipal service, regardless of who is delivering it. Second, no distinction is made between human resource-related expenditures made for those working in general administration and

those working in service provision, making it impossible to determine the budgetary cost of these services. Third, fiscal transfers to other levels of government (i.e., central government and districts) are not covered in the budget but they should be. Fourth, the budgeting system does not indicate which of the nine districts specifically benefit from expenditures in the services financed and/or provided by the UB government.

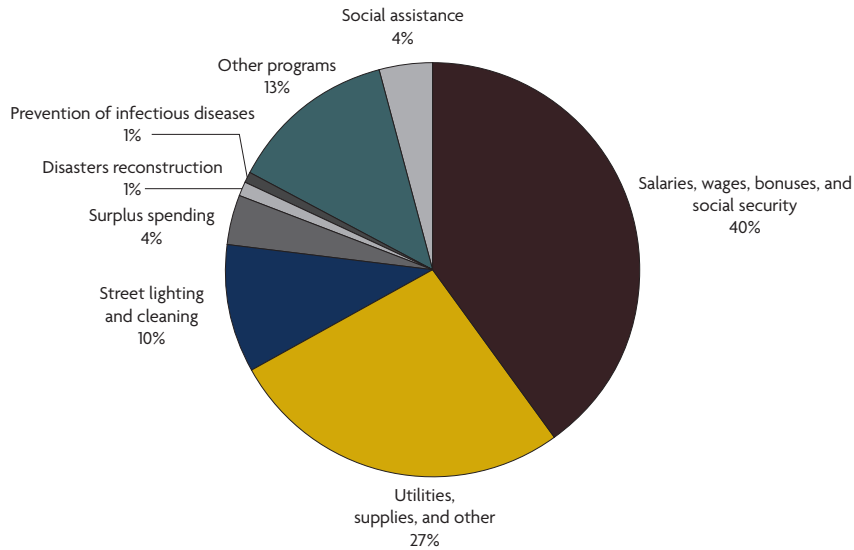
The Case of Bayanzurkh District

To better understand the functions of districts, compared below are the current expenditures of Bayanzurkh, an urban district with the largest budget for the period of 2008–11.

Bayanzurkh current expenditure budget. In 2008, Bayanzurkh allocated approximately two-thirds of its budget (67 percent) to general administration (staff costs), while only one-third was used for financing services (figure 4.6). The high level of spending on general administration is not surprising because international experience has shown that the smaller a local government, the larger the relative weight of these expenditures. The most important services provided by Bayanzurkh are street lighting and cleaning (10 percent) and social assistance (4 percent). As the budget format follows that of the UB government, all key challenges with regard to adequate reporting formats also apply to districts. For example, 13 percent of expenditures are only entered as a line item for “other programs,” like the UB government’s budget, there are also entries described solely based on the origin of sources (e.g., “surplus spending,” accounting for 4 percent of the budget and derived from unspent funds from the previous year’s budget).

In 2011, as in 2008, the lion’s share of expenditures in Bayanzurkh went to operations and general administration (72 percent). Services accounted for slightly less than one third of expenditures (approximately 27 percent) and explicitly included (1) street lighting and cleaning (13 percent) and (2) social assistance (2 percent). Presumably, expenditures for “other programs” (6 percent) and those made through the local reserve fund (6 percent) were also for service delivery, though the budget format does not indicate the purposes for which these funds were used (figure 4.7).

Figure 4.6. Current Expenditures Bayanzurkh, 2008

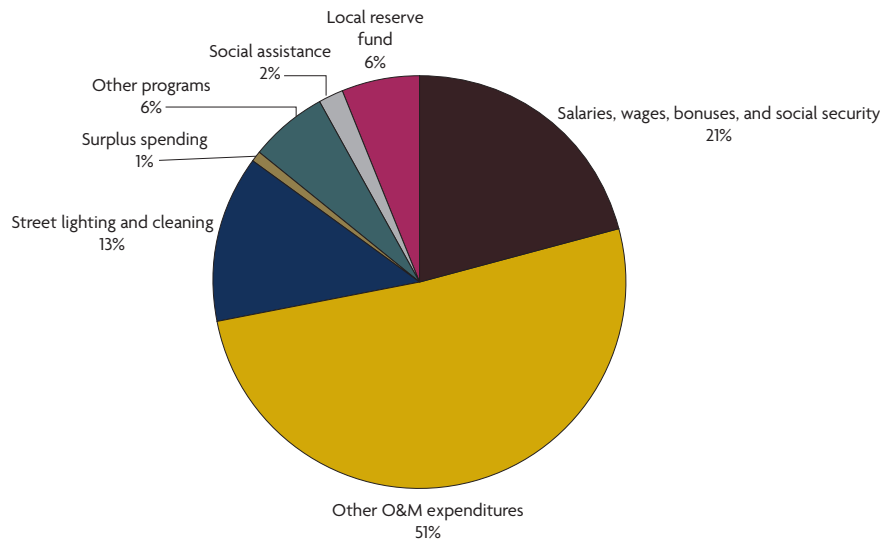


Source: Elaborated for this report based on data from Bayanzurkh's 2008 executed budget.

As can be seen in the expenditure budgets, **there is an overlap in the services provided by the UB government (i.e., “social assistance”) and services offered by districts.** It is not clear, however, which specific districts benefited from the UB government’s support. As previously discussed, the PSMF law creates an overlap in the

assignment of expenditure responsibilities between UB and its districts. There are no clear rules on how to address the apparent duplication in responsibilities across these two different levels of subnational governments. Additionally, it remains unclear how responsibilities are being shared or distributed in actual practice.

Figure 4.7. Current Expenditures Bayanzurkh, 2011



Source: Based on data from Bayanzurkh's 2011 executed budget.

4.5. CAPITAL BUDGET: EXPENDITURES

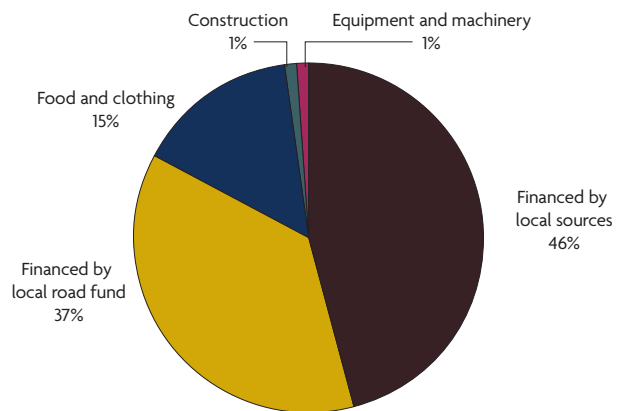
According to UB government's *executed budgets*³⁸ own capital expenditures increased sevenfold, from 17.8 billion Tugrik (US\$13.6 million) in 2008 to 118 billion (US\$89.9 million) in 2011. Because only the sources of capital financing are reported, by only reviewing the executed budget formats it is practically impossible to determine the spending purposes of over 80 percent of capital expenditures. About half (46 percent) of such expenditures were entered under the line item "financed by local sources," and more than one third (37 percent) were entered as "financed by the road fund" (see figure 4.8). **The main purpose of financial reporting is to show what investments in local services have been provided with the available funds from different financial sources.** Presumably, the reference to the road fund suggests that expenditures went toward road construction and rehabilitation, but this is not stated explicitly. The road fund consists of proceeds from the vehicle tax, and road fees collected by the UB government, which are intended for the financing of capital expenditures (i.e., for both new construction and rehabilitation).³⁹ As already discussed in chapter 3, however, the revenue from these sources is budgeted as current rather than as capital revenue. These inconsistencies are not easily detected because the budget does not adequately disaggregate between revenues from capital sources and revenues from current sources.

The third largest item under capital expenditures (15 percent) finances "food and clothing" (see figure 4.8). Because this expenditure item refers to consumption, it should have been included in the current expenditure budget, perhaps as part of a safety net program. Because this expenditure is not an investment, it should not be included under the capital budget. In other words, from an accounting perspective, "food and clothing" are

38. This report covers capital expenditures financed by UB's own revenue sources and by CG transfers through the local development fund only (referred as the "Direct" Budget). It does not include capital expenditures financed by the CG through its line ministries, or other CG sources; since these other capital revenue sources are not reported in UB's government budget and there is not a consolidated budget for UB City, as a whole, that illustrates on all other revenue sources and their actual use.

39. The purpose could be, for example, new construction for expansion of economic and social infrastructure or rehabilitations, equipment, and so forth.

Figure 4.8. The UB Government Capital Budget, Fiscal 2008



Source: Elaborated for this study based on data from UB's 2008 executed budget.

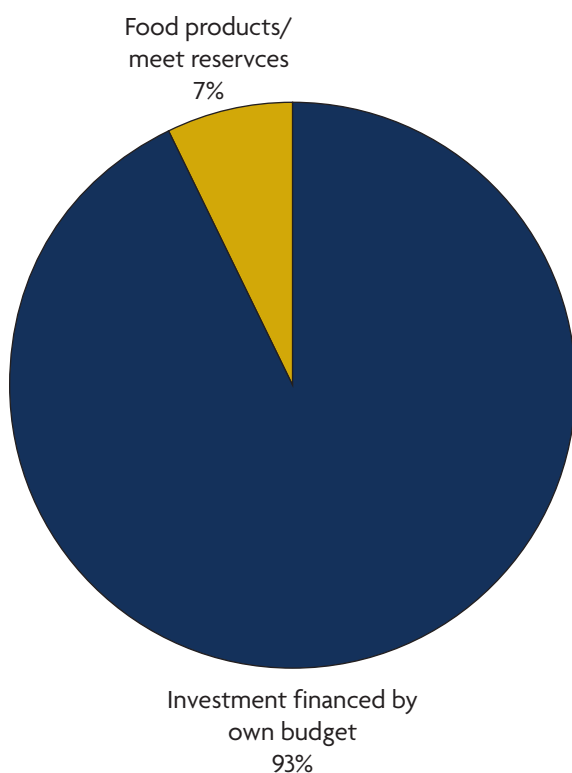
financed through a recurrent cash flow instead of as a one-time investment (as would be the case for a fixed asset).

A review of the UB government's reporting system indicates that its 2011 executed capital budget is even less transparent than that of 2008. About 93 percent (86 billion Tugrik or US\$65 million) of the investment is reported under the line item, "investments financed by own budget" (see figure 4.9). The rest of the "investment" was for purchase of "food products." Since this is a consumption item, not an investment, it should be reported under current expenditures.

Finally, the 2011 results suggest a degree of instability in the UB government's capital budget. Its revenue sources seem to vary from year to year. The 2008 budget reports funds from the "local road fund" and funds "financed by local sources." Neither of these funds appears in the 2011 budget report. In order to forecast capital revenues for effective investment planning, it is important to have stability in both the capital revenue sources and the reporting system.

UB's current budget practices stand in sharp contrast to current legislation, which places heavy emphasis on outputs over inputs. It is not possible to assess which of

Figure 4.9. The UB Government Capital Budget, Fiscal 2011



Source: Based on data from UB's fiscal 2011 executed budget.

the 20 services under UB's mandate have actually benefited from the 2011 investment budget. A more transparent budgeting system would facilitate the monitoring of these specific outputs. A budget classification based on those services and functions mandated by law would also facilitate the task of determining where and in what UB is investing its capital funds; this would substantially enhance the transparency, accountability, and accuracy of the budgeting system. These benefits could be achieved without compromising the current accounting system, in regard to keeping track of the origin and use of fund-sources for the financing of the different investments. Undoubtedly, the potential benefits to upgrading the budgeting reporting system to meet international standards are substantial.

In best international practices, a capital budget clearly illustrates all capital revenue sources (i.e., own revenue

sources, including tax and nontax sources), fiscal transfers from the central government (e.g., grants, national tax revenue-sharing, royalties), capital revenue from contributions (e.g., private sector and/or international donors), and capital revenue from loans and credits. Similarly, on the expenditure side, the city's capital budget would detail all the investments in every one of the services it is legally mandated to provide. Lastly, a capital budget format must illustrate the balance between capital revenues and expenditures (i.e., surplus or deficits). A comprehensive capital budget must be directly linked to a multiyear local development plan. UB and its districts must gradually move in this direction.

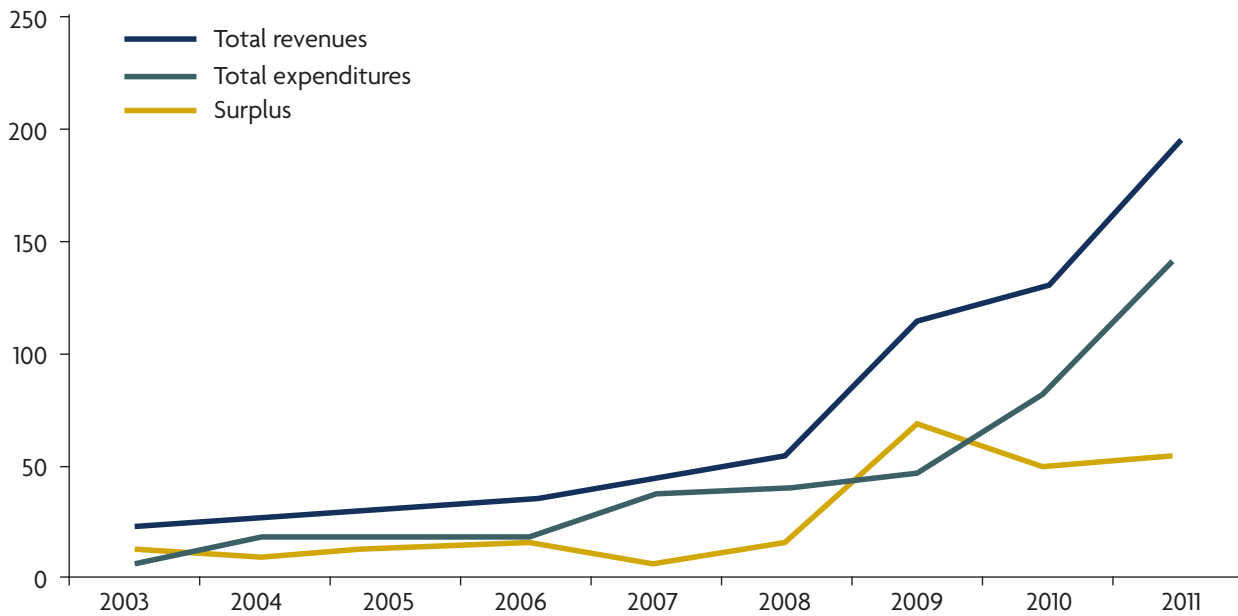
A clear and transparent budgeting system is a decision-making tool for city leaders and a way to report the management of resources to taxpayers, the central government, and other stakeholders. A current budget (operating revenues and expenditures) and a capital budget (revenues and investments in development) should be managed and reported in two different budget formats in order to determine the balance in the operating (current) budget and in the investments (capital) budget. In contrast, under the UB government's budgeting system, all revenues (current and capital) are reported in one budget, while all expenditures (current and capital) are reported in a separate document.

Consequently, the UB government is unable to report on the balance in its current and capital budgets, a critical piece of information reflected in best practices of comprehensive (integrated) budget reports. In other words, under the current budget format there is no budgetary line entry for reporting the corresponding surplus or deficit in operations and/or investments.

4.6. BALANCE BETWEEN TOTAL REVENUES AND EXPENDITURES

The objective of this section is to compare UB's total revenues and expenditures over time in order to determine what its financial situation has been in the past, how it has been in recent years, and how it is expected to be in the near future. A key indicator of UB's financial situation

Figure 4.10. The UB Government Trend in Revenues, Expenditures, and Total Surplus (in billions of Tugrik)



Source: Table 4.3.

is whether UB has been able to operate with an annually balanced budget.

Fiscal balance in the total budget over time. The budgetary data for the last nine years indicate fairly large surpluses in the operations of the UB government. Such surpluses have been as high as 59 percent in 2009 and as low as 13.39 percent in 2007, as illustrated in figure 4.10 and table 4.3.

These findings indicate that, for several years, the UB government has had a fairly solid financial situation in its operating budget; and this situation is expected to continue in the near future. The question then, is what UB should do with these fairly significant surpluses in operations. As has been shown in this study, part of the surpluses in operations has been allocated to the financing of the recurrent expenditures as well as to local investments. However, more research is needed in this area to ascertain a comprehensive view of the actual use of these resources. Nevertheless, the use of these funds seems to

be consistent with the PSMFL, which states that “budgetary bodies may deposit surplus of financial resources in the centralized cash management system.” “Any savings in the capital charge expense and operating expenses of the state budgetary body may be used for training, performance incentives, and providing secure operations. However, this shall not become a basis for cuts in approving the following year’s budget for the budgetary body concerned.”⁴⁰

It is no less important to determine the cause of these surpluses. First, it should be highlighted that the PSMFL of June 27/02 in Article 5.2.3 requires that “annual operating cash flow should be in surplus” (this applies to budgetary bodies such as UB and its districts), meaning that they should close their yearly operations with revenues exceeding expenditures. The purpose of this legal mandate is to avoid potential issues of deficit financing, which would ultimately need to be resolved by the Ministry of

40. As established in Article 13.7 of the PSMFL, and stipulated in Article 54.1 for the “Management of Local Budgets.”

Table 4.3. Yearly Surpluses in the UB Government’s Operations (in billions of Tugrik)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Total revenues	21.2	26.0	30.8	34.6	41.1	53.6	115.1	130.8	194.7
Total expenditures	8.4	16.2	16.1	19.0	35.6	39.3	46.7	81.6	140.8
Surplus	12.8	9.8	14.7	15.6	5.5	14.3	68.5	49.1	53.9
Surplus (%)	60.21	37.83	47.70	45.09	13.39	26.65	59.48	37.58	27.67
Consolidated Yearly Surpluses: The UB Government and the Districts (in billions of Tugrik)									
Total revenue	26.4	32.3	38.2	43.8	52.5	65.6	133.4	164.3	245.9
Total expenditure	12.5	21.8	22.0	27.5	47.2	53.6	61.3	103.5	180.9
Surplus	13.9	10.5	16.2	16.3	5.3	11.9	72.1	60.8	64.9
Surplus (%)	111.5	48.3	73.9	59.4	11.2	22.3	117.5	58.7	35.9

Source: Data provided by UB Treasury based on executed budgets for the corresponding years and calculations for this report.

Finance (MoF). As such, and in principle, this legal requirement seems sound from the perspective of *fiscal discipline*, specifically with respect to *no overspending*. However, in practice this principle cannot in and of itself justify all surpluses, irrespective of their magnitudes.

Given the magnitude of some of these yearly surpluses and the fact that approved budgets at the beginning of the fiscal year are balanced, it is logical to question how such large surpluses come about. This report has examined this question for the most recently-executed fiscal year (2011). The estimated surplus for fiscal 2011 was approximately 53.9 billion Tugriks, equivalent to more than one quarter (27.67 percent) of UB’s total revenue budget. Empirical findings indicate that, for fiscal 2011, execution in UB’s total expenditure budget was approximately 76.6 percent of the approved expenditures for the year. This suggests that a significant part of the surplus from the expenditure side of the budget was due to a low execution of approximately 23.4 percent below the budgeted expenditure target. In absolute terms, this is equivalent to approximately 32.9 billion Tugrik (or US\$25 million dollars). Subsequently, from the revenue side, the executed total revenue budget for this same year was 108.3 percent of the approved revenue budget. This unexpected increment amounts to 18.7 billion Tugrik (or US\$14 million dollars).

In short, the surplus is primarily due to a combination of low expenditure execution and unexpected higher revenues. However, it should be highlighted that the main determinant was poor performance on the expenditure side of the budget, which may be expected to negatively affect service delivery. In fact, it was found, for example, that in fiscal 2011, expenditure execution on “environmental protection” was only 46 percent of its target, and the execution of those “services required under the name of the government” was also quite low (58.9 percent). Therefore, even though the surplus in fiscal 2011 contributed to *fiscal discipline* (in terms of no overspending), it was of such magnitude on the expenditure side that it negatively impacted the delivery of specific services that the UB government is expected to provide.

Considering UB’s financial situation, particularly over the last three years, it may be argued that **the UB government has been and continues to be solvent in its annual operations**. This empirical evidence may also be an indicator of some level of *fiscal discipline*⁴¹ in UB’s financial management, as noted above, and to some extent of its potential creditworthiness. However, the magnitude of the surpluses also suggests that UB’s apparent weak

41. It should be noted that state budgetary bodies are legally prohibited from “spend[ing] above the appropriation limits” (PSMFL, Article 14.1.5). Also, Article 52.3 states that the “Capital City Governor is prohibited from exceeding budget and appropriation limits [through], allowing the bank account to be in overdraft.”

expenditure execution, which may be due in principle⁴² to limited revenue absorption capacity in both O&M as well as in capital investments, would need to be addressed before considering an additional revenue source from credit.

Therefore, given this relatively strong financial situation and low expenditure execution, it seems that UB should give some consideration to the option of whether part of these *surpluses* could be used to upgrade its execution capacity, to leverage capital for financing expansion of economic infrastructure, and to offer greater access to basic local services. At UB's discretion, some of these *surpluses* could potentially help increase UB's rating to creditworthiness within certain debt limits consistent with UB's current fiscal capacity.

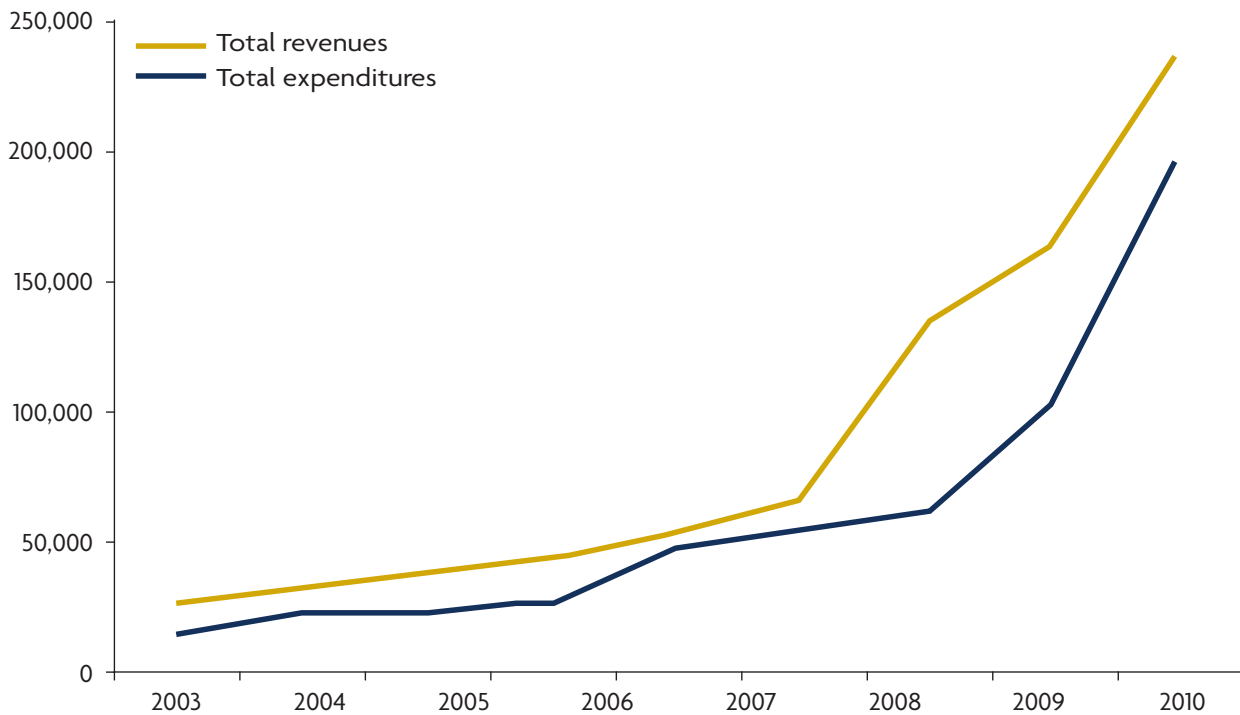
42. Another factor could be the discretionary inclusion of projects by the central government, which are not part of UB City's yearly investment plan and, therefore, the necessary project preparation for their implementation could not be ready in a timely manner.

The financial situation regarding *significant yearly surpluses* in operations remains fairly similar when the total budgets (for revenues and expenditures) of the nine districts and UB's are all consolidated, as illustrated in figure 4.11. This is particularly the case considering that the UB government's figures constitute the largest proportion in the consolidated of fiscal data. For example, the UB government's revenues for fiscal 2011 are equivalent to 79.2 percent of the total revenues of UB City as a whole; and similarly, UB's total expenditures are equivalent approximately 78.2 percent of the consolidated total expenditures of UB and its districts (table 4.3).

4.7. CONCLUSION

Legal framework and assignment of expenditure responsibilities. For the most part, the current expenditure assignment to subnational levels of government meets basic economic efficiency criteria and fundamental principles of public finance. However, there are

Figure 4.11. UB and Districts: Consolidated Yearly Surplus, Total Budgets (in millions MNT)



Source: Executed revenues and expenditures, as reported in table 4.3

redundancies in the assignment of responsibilities to UB and its districts. This overlap may compromise economic efficiency and interjurisdictional equity in service provision as well as accountability in general and financial accountability in particular.

Overlap in expenditure responsibilities. The PSMFL creates an overlap in the assignment of expenditure responsibilities between UB and its districts. Unfortunately, there are no clear rules on how to address this duplication. In practice, responsibilities seem to be shared and/or distributed on an *ad hoc* basis through a negotiated process supported by agreements between the capital city governor and the district governors. A next step for the current legal framework is to adequately regulate these informal intergovernmental fiscal relationships.

Actual practice in service provision. Meaningful spending in service provision by the UB government and districts is limited to a few legal responsibilities, although there is a gradual trend toward the provision of more services. About half of the 23 services established by law may have some meaningful level of spending. Typical services include street lighting, solid waste collection, social assistance, and prevention of infectious diseases. However, the quality and coverage of current services still needs to be examined.

Fragmentation of the budgeting system. The UB government's current budgeting system does not report on the social services it provides on behalf of the CG. This is because the law requires UB to manage these services under a separate accounting, budgeting, and financial

reporting system. This fragmentation through separate *vertical* financial and accounting systems, without a proper *horizontal* consolidation of these services, does not allow for a comprehensive view of all the services provided by the UB government and therefore makes UB's finances nontransparent.

The budgeting system. There is room to substantially upgrade the transparency in UB and district financial reports regarding the actual budgetary allocation to each of the services provided. This is the case for operating expenditures, including maintenance, as well as for specific investments in service expansions. The actual use of significant portions of the operating budget and the capital budget are not disclosed in the budget document. Considering that the budget classification for the nine districts is the same as that of the UB, districts face these same shortcomings in their budgeting systems. The UB government's main concern in budget reporting is to show the use of funds from the different revenue sources rather than reporting on the local services actually provided with the funds.

Trend in UB expenditures. Empirical results indicate that *real* expenditures, when measured in per capita terms, have also been growing steadily during the last three years. In other words, there is no evidence of a *net* negative effect of urban population growth on UB's financial situation; on the contrary, analysis has shown that increase in population size has expanded its revenue base. However, further analysis is required to determine service coverage and quality standards in municipal services.

Chapter 5. Recommendations for a Future Research Agenda

This study has identified key gaps in knowledge that need to be addressed in order to strengthen UB's finances, making it more transparent for more efficient service delivery. This chapter lays out an agenda for future research and technical assistance, building on the preliminary findings of this study. These topics have been grouped by research priority toward which the Bank will contribute in a programmatic manner over a span of two fiscal years: 2013 and 2014. However, this suggested priority, especially during the second year, could shift due to the dynamic development context, deepening dialogue, and emerging knowledge.

5.1. PRIORITY RESEARCH AGENDA AND TECHNICAL ASSISTANCE FOR THE SHORT TERM

The preceding chapters have highlighted the shortcomings in UB City's budgeting system. There are three key areas that need to be urgently addressed:

- (1) improving the current budgeting and accounting systems to enhance transparency in service provision through technical assistance;
- (2) analyzing in greater depth the system of intergovernmental fiscal relations between UB and its nine districts and determining how these relations can be improved to enhance economic efficiency, interjurisdictional equity, and financial performance; and
- (3) assessing the efficiency of UB and its districts in both revenue administration and collection performance as well as in expenditure execution.

Shortcomings in UB's Current Budgeting System

The current design of the budget formats and financial reporting system of UB and its districts must be substantially improved. The budget should more transparently identify the actual services provided. Appropriate improvements could significantly enhance accountability in the provision of municipal services. Also, the accounting and reporting of revenues and expenditures could be made more accurate and therefore more conducive to relevant economic and financial analysis of actual performance in operations, including local investments in socio-economic development. The numerous shortcomings and deficiencies that currently exist in the budgeting and accounting systems could be easily overcome through specific reforms in the budget and accounting formats and procedures, adequately supported by a technical assistance and training program designed for this specific purpose.

Intergovernmental Fiscal Relations

Intergovernmental fiscal relations between the UB government and its districts. Considering the overlap in expenditure responsibilities between the UB government and its districts, it is critical to determine how this overlap is being addressed in actual practice. The questions that need to be answered include: how is the current legal arrangement in assignment of functions affecting *efficiency* and *equity* in service provision across districts and what type of norms and regulations are needed to improve the current situation in both service provision and fiscal management in the UB government and its districts?

The UB government's allocation of surpluses and support to capital budgets of districts. As part of the intergovernmental fiscal relations, further research is needed on the role of the UB government in financing capital investments at the district level, particularly considering its surpluses in operations and the type of capital revenue sources currently assigned to the UB government (such as the vehicle tax). It is also important to address questions such as: What criteria does the UB government follow to decide the allocation of capital financial resources across districts? For example, which districts have benefited in recent years from UB's capital expenditures in local services and why? What alternative criteria could be used to improve the current allocation of UB's capital funds across districts? Could UB surpluses and better expenditure execution contribute to better service provision across all districts and if so, how?

It is important to determine how well the districts perform in terms of executing their own expenditure budgets. To this end, a detailed comparison of approved and executed revenues and expenditures for UB and its districts must be conducted. The results of this analysis would help determine some of the potential reasons behind the current pattern of systematic surpluses as well as what actions are necessary to improve budget execution. Performance in budget execution could ultimately contribute to the better provisioning of public goods and services.

The Financial Situation of UB's Districts

The analysis of the financial situation of UB's nine districts merits more in-depth research. A comprehensive analysis of their financial situation (in both the operating and capital budgets) must be carried out for each of the nine districts in order to determine the main factors affecting their performance in terms of financial management and services provided.

Revenue Administration and Collection Performance

Local revenue collection performance and transfers to the central government (CG). More research is needed on revenue administration in general and on UB's and district's performance in revenue collection efficiency.

Particular attention should be given to those revenue sources that constitute, in their entirety, local own revenue, and to those for which collections above specific levels (such as approved budget ceilings) are meant to be transferred to the CG. It is also important to determine how current annual revenue collection ceilings are established for local governments and how this policy affects the incentives for revenue collection efficiency and local tax effort. For example, do own revenues perform better than shared revenues? Do UB and the nine districts apply higher tax rates on nonshared taxes than on shared taxes? The answers to these questions would help policymakers identify revenue assignment issues and ways to encourage local revenue mobilization, both of which could result in better collection efficiency rates and greater local tax effort.

5.2. MEDIUM-TERM RESEARCH AGENDA

In the medium term, there are four key areas for research that need to be addressed.

- (1) How sustainable are the services⁴³ provided by UB and its districts?
- (2) Is the provision of any local service supplied by either the UB government or any of its districts substantially more cost efficient to the extent that it could be used as a model or benchmark for service provision?
- (3) What is the actual coverage in district service provision and how efficient is the current fiscal system in funding local public investment programs?
- (4) How is the current budget process actually affecting local investment planning and execution in UB and its districts? For example, how much of the strategic business plans and district's action plans actually gets implemented?

Efficiency in Service Provision

UB's constraints and opportunities in service expenditure efficiency. Considering that, as a whole, the city of UB includes nine districts, it should be possible to

43. This analysis would include both revenue-generating and nonrevenue-generating services.

develop unit cost⁴⁴ comparisons for main services. Does UB or any of its districts provide specific services in such a cost-efficient manner that it could be used as a model for other districts or for UB City as a whole? This analysis should cover both revenue- and nonrevenue-generating services. Ideally, a differentiation should be made between costs in operations and maintenance (O&M) by service and general administration costs. Furthermore, the analysis should identify the main constraints (e.g., lack of economies-of-scale due to fragmentation) and opportunities (e.g., economies-of-scale due to integration) in order to enhance expenditure efficiency across those services benefiting each district and the UB metropolitan area. The main challenge in this research would be determining estimates of O&M expenditures for selected services. At the very least, proxy indicators of such unit costs based on current expenditures could be used to determine optimal (i.e., the most cost-efficient) performance.

An analysis of fiscal relations between the service providers and the UB government and district administrations. Some of the main questions that should be considered include the following: What is the financial situation of the main companies providing municipal services? How does that situation affect the finances of UB and its districts? For example, are transportation and solid waste companies self-sustaining, or are they dependent on UB and district subsidies? Are there interjurisdictional fiscal imbalances due to greater expenditure responsibilities in some districts (e.g., due to traffic congestion and/or air-pollution) that, if corrected through a better assignment of revenue sources, could benefit the entire metropolitan area/region? What incentives, if any, are in place to encourage cost efficiency in service provision?

44. A distinction should be made between the “unit cost” of providing a service, subject to certain standards, and the “actual expenditures” in the provision of the corresponding service. The challenge is that many local governments and/or service providers generally have neither explicitly-established standards with corresponding unit costs for each particular service nor cost accounting systems to determine the actual costs of service provision. Therefore, this research must rely on the available budgetary and accounting data regarding the provision of each relevant service. At the very least, it is expected that the actual expenditures per unit of service being provided, at the ongoing standards of quality, would be possible to determine. This information could be used as a proxy for expenditure-efficiency analysis, subject to verification of the actual standards.

Sustainability in Revenue-Generating Services

The analysis would compare current O&M costs for selected services with the actual revenue collected to determine the collection efficiency of user charges and financial sustainability of the services provided. This analysis would also help determine whether or not service providers have adequate accounting records documenting the costs of service provision. It must be noted that the Public Sector Management and Finance Law (PSMFL) requires local governments to account for the costs of service provision. Article 26 states that the *cost of outputs shall be determined on the basis of full accrual cost of production, including management overheads and capital charges.*

Sustainability in Nonrevenue-Generating Services

Particular attention must be paid to those services that are nonrevenue-generating, especially because most services provided by UB and its districts could fall into this category. Analysis must be carried out comparing the current and O&M costs and their sources of financing. Determining the actual costs of provision, the current and potential sources of financing, and how to mobilize the needed revenue sources is challenging because these services are usually financed through a combination of local taxes and grants from central governments. For example, prevention of infectious diseases, public safety, environmental protection, and social assistance are services that are typically supported by both local taxes and CG sources through intergovernmental fiscal grants, tax revenue-sharing, and so forth. O&M costs of services, such as street lighting, could potentially be recovered through specific surcharges on the electricity bill. However, developing these types of inter-institutional arrangements could also be challenging. Overall, this analysis is expected to contribute to the identification of financial and administrative issues in the provision of nonrevenue-generating services along with the means and ways to enforce the financing of these services.

Actual Coverage of Municipal Services

Quality and coverage of municipal services. In order to determine the coverage and quality of the key municipal services, a representative survey must be carried out

on actual access needs. The survey would focus on both revenue-generating and nonrevenue-generating services, focusing on such questions as extent and quality of coverage by geographic area to determine equity in service delivery. The results of the survey would serve as a baseline for future improvements in services and enable UB City leaders make informed decisions in their investment planning and more equitable, efficient, and effective public investments. Likewise, the results of this survey would assist medium-term CG fiscal policy in the capital financing of local governments.

Local Investment Planning and the Capital Budget Process

Local investment planning and the budget cycle. It is important to examine how the investment planning of UB and the district is being affected by the current budget process. Some investments are financed by local sources, but the majority is financed by the state budget. However, greater clarity is needed on the type of investments supported by the state budget and their investment ceilings. As part of the local investment planning process, districts prepare annual action plans, while the UB government manages rolling three-year strategic development plans. Nevertheless, it appears that there is no certainty in the financing of such plans, nor is there an estimate in the minimum of future capital funds per district needed to support them. Capital budget financing must go through the budget cycle, which includes

revisions by line ministries, the Ministry of Finance, the cabinet, and the parliament. Considering the fact that the allocation of resources appears to be fairly discretionary, the uncertainty in annual financing is high. Empirical evidence on the local investments planned and their actual execution must be examined. It is worth reviewing different policy options in order to provide certainty on at least a minimum availability of capital funds for UB and its districts.

Considering the vertical (top-down) capital budget management and approval process under the current budget cycle, local governments have little control in capital budget planning and investment financing. How then does this budget process actually affect local investment planning and budget execution in UB and its districts? For example, how much of UB City's strategic business plans and district's action plans are actually implemented?

5.3. WORLD BANK SUPPORT TO THE UB CITY

World Bank support to the UB City during the Bank's fiscal 2013 will focus on the priority agenda of improving the current budgeting and accounting systems to enhance transparency in service provision through technical assistance. In fiscal 2014, work might focus on service coverage and quality, although this could change based on the UB government's request.

Annexes

This section includes two annexes: annex 1 presents a revised and reclassified budget format prepared for this study, using budget information already available. Annex 2 presents the actual budget format that UB City and its districts use to report their annual revenues and expenditures. A comparison of these two annexes illustrates that a more structured reclassification of the budget would provide greater and more transparent information for a more accurate analysis of UB City finances.

The main differences and the specific benefits of improving budget reporting in both revenues and expenditures are summarized below.

REVENUES

Actual reporting on the *revenue budget* does not always accurately differentiate between *current* and *capital* revenues. For example, while revenues from the real estate transfer tax and the vehicle tax should finance the capital budget, they are reported as current revenue. The *capital revenue* format (as can be seen in table A2.3) includes “sales of property” and “privatization revenue” as the only capital revenue sources. This classification overestimates UB’s current revenue budget and underestimates the actual availability of funds in its capital revenue budget, which together provide a somewhat distorted view of UB’s financial situation.

The actual classification of *current revenues* does not adequately differentiate between “own revenue sources” and “external revenue sources.” For example, revenues from CG fiscal transfers, such as “revenue sharing,” for transparency reasons, should not be combined with “own revenues” so that budget reporting could offer a more accurate view of UB City finances (as illustrated in table A1.1).

The actual classification of *capital revenues* does not report on all of UB’s *capital revenue* sources and it does not differentiate between “own” and “external” capital revenue sources. For example, the *capital revenue* budget (table A.2.3) does not report sources such as: “CG capital transfers” and “CG capital transfers from the development fund” and “own source capital revenues,” such as the vehicle tax and the road fee. table A1.1 (in contrast to table A2.3) reports all these revenue sources under the capital budget so as to determine the real financial situation of UB City in capital financing.

The above arguments also apply to budget reporting done by UB districts. Additionally, districts do not differentiate between tax and nontax revenues sources. This makes district’s budget reporting even less transparent—as illustrated in table A1.5.

EXPENDITURES

Based on the budget format currently applied by UB City (included in table A2.2), it is evident that some efforts have been made over the years to gradually improve financial reporting. However, there are still substantial improvements that could be made to UB’s current expenditure budget reporting format, as illustrated below.

UB’s budget reporting is done on *cash-flow* basis; however, part of the current efforts to improve financial reporting in the *expenditure budget* includes some basic elements of a balance sheet (i.e., assets and liabilities). For example, table A2.2 illustrates how assets (such as cash and receivables) and liabilities (such as payables) are reported together with the fiscal 2011 expenditure budget that, in principle, should only refer to cash flows.

Present reporting on *current expenditures* is a list of insufficiently-structured expenditure items with limited classification. For example, no reporting is done on total expenditures on general administration and for services provided by UB City to its residents. The *current budget* is a mix of a list of purchases of inputs together with a list of several expenses for the delivery of specific *outputs/* services. Furthermore, some categories are too general. For example, expenditures classified as “payments for services required by the government” or “other activities and programs” simply do not report what the budget was spent on. Equally inadequate are the expenditure entries that refer to the financing sources rather than to the specific services provided with such funds (for example, “surplus from the previous fiscal year” or “local reserve fund”). These budgetary entries may be seen in table A2.2.

Furthermore, as shown in annex 2, the budget format of *current expenditures* does not identify how much was spent on operations and maintenance (O&M) for each of the main services provided by UB City. Furthermore, the budget makes no distinction between expenditures in

human resources in general administration and expenditures in service provision, making it impossible to determine the budgetary cost of these services. Consequently, the expenditure budget, as it is, cannot be used as a decision-making tool to decide, monitor, or control cost-efficiency and effectiveness.

Fiscal transfers across levels of government (i.e., CG, UB City, and districts) are not always explicitly covered in the budget as they should be. For example, the budgeting system neither reports UB transfers to the CG nor any explicit transfers from UB to any of its nine districts.

The budget format on *capital expenditures* is even more limited in transparency than the *operating* budget (table A2.2). It reports very little on what services or sectors benefited from the public investment executed and/or funded by UB City. For example, the *capital* budget in fiscal 2011 simply reports the total amount of investments made by UB City that were “funded by its own budget.” It does not specify what local services or local public infrastructure benefited from such investments.

Annex 1. Revenue and Expenditure Budgets Reclassified for this Study

Table A1.1. UB and Districts Revenue, 2003–11 (in millions MNT)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Own revenue sources									
1. Taxes									
1.1 Wage tax							68,844.3	90,084.7	135,527.8
1.2 Unidentified income tax	705.8	1,395.7	1,625.5	829.5	798.7	952.1	1,038.3	1,226.1	1,616.1
1.3 Self-employment tax	931.2	1,453.6	1,503.2	1,583.7	3,636.6	3,745.6	4,189.7	5,437.7	7,340.2
1.4 Livestock tax	4.9	7.7	8.9	9.8	14.8	24.0	14.2	1.5	0.244
1.5 Other income tax		1,790.5	3,236.6	6,378.0	1,443.2	3,117.5	6,029.0	5,343.8	8,784.7
1.6 Property tax	2,818.3	3,343.8	3,864.9	4,088.2	4,912.4	5,710.8	6,733.5	8,653.2	10,371.5
1.7 Gun tax	16.2	16.5	17.0	19.6	22.3	25.7	30.5	28.7	33.8
1.8 Tax on property sale	334.6	359.2	655.8	892.7	1,491.5	1,741.4	1,281.8	3,862.3	1,570.7
Subtotal taxes	4,811.2	8,367.2	10,912.1	13,801.8	12,320.0	15,317.5	88,161.6	114,638.4	165,245.4
2. Licenses, fees and permits									
2.1 License fee for mineral exploration						22.0	28.8	37.3	31.6
2.2 Mineral royalty	739.7	579.4	843.0	874.4	335.8	359.8	424.0	628.5	624.8
2.3 User fee for common minerals	50.0	27.6	37.2	47.1	73.8	83.7	50.0	60.6	68.5
2.4 User fee for land	3,509.9	3,729.4	5,705.3	6,904.5	11,290.8	15,847.8	17,742.8	18,348.7	20,580.0
2.5 User fee for water and springs	31.2	29.2	187.9	217.0	213.3	266.4	252.6	577.8	721.3
2.6 User fee for timber	13.5	10.8	13.5	18.5	18.4	18.1	12.1	39.7	74.9
Subtotal licenses, fees, and permits	4,344.4	4,376.6	6,787.0	8,061.7	11,932.2	16,598.0	18,510.6	19,692.9	22,101.3
3. User charges									
3.1 Stamp duties	871.4	3,339.8	4,018.1	3,902.2	5,232.9	6,537.7	6,685.3	6,654.0	20,496.8
Subtotal user charges	871.4	3,339.8	4,018.1	3,902.2	5,232.9	6,537.7	6,685.3	6,654.0	20,496.8
4. Rents	1,020.0	703.1	522.0	682.0	752.0	811.3	759.3	772.1	1,034.7
5. Fines and penalties	4,243.9	4,395.8	4,966.9	4,856.7	8,722.9	4,511.0	6,910.6	8,625.8	527.1
6. Other own revenue									

(continued)

Table A1.1. UB and Districts Revenue, 2003–11 (in millions MNT) (continued)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
6.1 Dividend of state-owned enterprises	95.4	67.4	51.7	81.8	132.0	145.1	166.8	111.6	112.9
6.2 Own revenue of budget entities	1,376.3	1,634.5	1,443.3	1,098.5	1,540.0	1,628.9	4,898.1	5,337.2	5,997.5
6.3 other non classified own revenues	2,481.7	1,284.0	360.7	181.7	399.0	711.6	856.4	651.3	761.6
Subtotal other own revenues	3,953.6	2,986.0	1,855.7	1,362.1	2,071.1	2,485.7	5,921.4	6,100.1	6,872.0
7.1 Revenue sharing CG taxes	3,594.5	3,366.0	4,253.2	5,996.2	5,103.3	11,389.9	0.00	0.00	0.00
7.2 Grants from CG for current budget									
Subtotal CG transfers current budget	3,594.5	3,366.0	4,253.2	5,996.2	5,103.3	11,389.9	0.00	0.00	0.00
Total current revenue	22,839.2	27,534.8	33,315.3	38,662.9	46,134.7	57,651.2	126,948.9	156,483.6	216,277.6
8. Central government (CG) capital transfers						15,093.2	15,446.7	41,140.6	90,820.0
9. Capital transfer from development fund						13,325.2	14,461.0		
Subtotal CG capital revenue	0.00	0.00	0.00	0.00	0.00	28,418.4	29,907.7	41,140.6	90,820.0
10. Own source revenue for capital budget									
10.1 Privatization revenue	1,260.0	1,901.4	1,807.0	1,851.0	2,274.0	3,172.0	375.1	1,332.8	8,316.5
10.2 Vehicle tax and road fee	2,285.7	2,873.5	3,073.4	3,251.4	4,051.0	4,744.7	6,056.9	6,458.0	21,261.2
10.3 Other own revenue source(s) for capital budget (from UB budget)						6,852.4	12,449.2	21,525.9	88,229.4
Subtotal own source capital revenue	3,545.7	4,774.9	4,880.4	5,102.4	6,325.0	14,769.1	18,881.2	29,316.7	117,807.2
Total capital revenue	3,545.7	4,774.9	4,880.4	5,102.4	6,325.0	43,187.5	48,788.9	70,457.3	208,627.2
Total revenue	26,385.0	32,309.7	38,195.7	43,765.4	52,459.8	100,838.8	175,737.9	226,940.9	424,904.9

Source: Calculated for this report based on the UB Treasury Department Data (2003–11).

Table A1.2. Percentage Change in the UB and Districts Revenue, 2003–11

Revenue	2004	2005	2006	2007	2008	2009	2010	2011
Own revenue sources								
1. Taxes								
1.1 Wage tax	0.0	0.0	0.0	0.0	0.0	0.0	30.9	50.4
1.2 Unidentified income tax	97.8	16.5	-49.0	-3.7	19.2	9.1	18.1	31.8
1.3 Self-employment tax	56.1	3.4	5.4	129.6	3.0	11.9	29.8	35.0
1.4 Livestock tax	54.8	15.5	10.3	51.7	61.6	-40.7	-88.9	-84.5
1.5 Other income tax	0.0	80.8	97.1	-77.4	116.0	93.4	-11.4	64.4
1.6 Property tax	18.6	15.6	5.8	20.2	16.3	17.9	28.5	19.9
1.7 Gun tax	1.7	2.7	15.4	14.0	15.1	18.7	-5.9	17.7
1.8 Tax on property sale	7.3	82.6	36.1	67.1	16.8	-26.4	201.3	-59.3
Subtotal taxes	73.9	30.4	26.5	-10.7	24.3	475.6	30.0	44.1
2. Licenses, fees, and permits								
2.1 License fee for mineral exploration	0.0	0.0	0.0	0.0	0.0	30.9	29.5	-15.4
2.2 Mineral royalty	-21.7	45.5	3.7	-61.6	7.1	17.9	48.2	-0.6
2.3 User fee for common minerals	-44.8	34.8	26.6	56.7	13.4	-40.3	21.3	13.1
2.4 User fee for land	6.3	53.0	21.0	63.5	40.4	12.0	3.4	12.2
2.5 User fee for water and springs	-6.2	542.0	15.5	-1.7	24.9	-5.2	128.8	24.8
2.6 User fee for timber	-20.0	24.1	37.6	-0.7	-1.8	-32.7	226.2	88.5
Subtotal licenses, fees, and permits	0.7	55.1	18.8	48.0	39.1	11.5	6.4	12.2
3. User charges								
3.1 Stamp duties	283.2	20.3	-2.9	34.1	24.9	2.3	-0.5	208.0
Subtotal user charges	283.2	20.3	-2.9	34.1	24.9	2.3	-0.5	208.0
4. Rents	-31.1	-25.8	30.7	10.3	7.9	-6.4	1.7	34.0
5. Fines and penalties	3.6	13.0	-2.2	79.6	-48.3	53.2	24.8	-93.9

(continued)

Table A1.2. Percentage Change in the UB and Districts Revenue, 2003–11 (continued)

	2004	2005	2006	2007	2008	2009	2010	2011
6. Other own revenue								
6.1 Dividend of state-owned enterprises	-29.4	-23.3	58.3	61.3	9.9	15.0	-33.1	1.2
6.2 Own revenue of budget entities	18.8	-11.7	-23.9	40.2	5.8	200.7	9.0	12.4
6.3 Other nonclassified own revenues	-48.3	-71.9	-49.6	119.5	78.3	20.4	-23.9	16.9
Subtotal other own revenues	-24.5	-37.9	-26.6	52.0	20.0	138.2	3.0	12.7
7.1 revenue sharing in CG taxes for current budget	-6.4	26.4	41.0	-14.9	123.2	-100.0	0.0	0.0
7.2 Grants from CG for current budget	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Subtotal CG transfers for current budget	-6.4	26.4	41.0	-14.9	123.2	-100.0	0.0	0.0
Total current revenue	20.6	21.0	16.1	19.3	25.0	120.2	23.3	38.2
8. CG capital transfers	0.0	0.0	0.0	0.0	0.0	2.3	166.3	120.8
9. Capital transfer from development fund	0.0	0.0	0.0	0.0	0.0	8.5	-100.0	0
Subtotal CG capital revenue	0.0	0.0	0.0	0.0	0.0	5.2	37.6	120.8
10. Own source revenue for capital budget								
10.1 Privatization revenue	50.9	-5.0	2.4	22.9	39.5	-88.2	255.3	524.0
10.2 Vehicle tax and road fee for capital budget	25.7	7.0	5.8	24.6	17.1	27.7	6.6	229.2
10.3 Other own revenue source(s) for capital budget (from UB budget)	0.0	0.0	0.0	0.0	0.0	81.7	72.9	309.9
Subtotal own source capital revenue	34.7	2.2	4.6	24.0	133.5	27.8	55.3	301.8
Total capital revenue	34.7	2.2	4.6	24.0	582.8	13.0	44.4	196.1
Total revenue	22.5	18.2	14.6	19.9	92.2	74.3	29.1	87.2

Source: Table A1.1.

Table A1.3. Composition of Total Revenue for UB and Districts, 2003–11 (percentage)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Own revenue sources									
1. Taxes									
1.1 Wage tax	0.00	0.00	0.00	0.00	0.00	0.00	39.17	39.70	31.90
1.2 Unidentified income tax	2.68	4.32	4.26	1.90	1.52	0.94	0.59	0.54	0.38
1.3 Self-employment tax	3.53	4.50	3.94	3.62	6.93	3.71	2.38	2.40	1.73
1.4 Livestock tax	0.02	0.02	0.02	0.02	0.03	0.02	0.01	0.00	0.00
1.5 Other income tax	0.00	5.54	8.47	14.57	2.75	3.09	3.43	2.35	2.07
1.6 Property tax	10.68	10.35	10.12	9.34	9.36	5.66	3.83	3.81	2.44
1.7 Gun tax	0.06	0.05	0.04	0.04	0.04	0.03	0.02	0.01	0.01
1.8 Tax on property sale	1.27	1.11	1.72	2.04	2.84	1.73	0.73	1.70	0.37
Subtotal taxes	18.23	25.90	28.57	31.54	23.48	15.19	50.17	50.51	38.89
2. Licenses, fees, and permits									
2.1 License fee for mineral exploration	0.00	0.00	0.00	0.00	0.00	0.02	0.02	0.02	0.01
2.2 Mineral royalty	2.80	1.79	2.21	2.00	0.64	0.36	0.24	0.28	0.15
2.3 User fee for common minerals	0.19	0.09	0.10	0.11	0.14	0.08	0.03	0.03	0.02
2.4 User fee for land	13.30	11.54	14.94	15.78	21.52	15.72	10.10	8.09	4.84
2.5 User fee for water and springs	0.12	0.09	0.49	0.50	0.41	0.26	0.14	0.25	0.17
2.6 User fee for timber	0.05	0.03	0.04	0.04	0.04	0.02	0.01	0.02	0.02
Subtotal licenses, fees, and permits	16.47	13.55	17.77	18.42	22.75	16.46	10.53	8.68	5.20
3.1 Stamp duties	3.30	10.34	10.52	8.92	9.98	6.48	3.80	2.93	4.82
4. Rents	3.87	2.18	1.37	1.56	1.43	0.80	0.43	0.34	0.24
5. Fines and penalties	16.08	13.61	13.00	11.10	16.63	4.47	3.93	3.80	0.12

(continued)

Table A1.1. UB and Districts Revenue, 2003–11 (in millions MNT) (continued)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
6. Other own revenue									
6.1 Dividend of state-owned enterprises	0.36	0.21	0.14	0.19	0.25	0.14	0.09	0.05	0.03
6.2 Own revenue of budget entities	5.22	5.06	3.78	2.51	2.94	1.62	2.79	2.35	1.41
6.3 Other nonclassified own revenues	9.41	3.97	0.94	0.42	0.76	0.71	0.49	0.29	0.18
Subtotal other own revenues	14.98	9.24	4.86	3.11	3.95	2.47	3.37	2.69	1.62
7.1 Revenue sharing in CG taxes for current budget	13.62	10.42	11.14	13.70	9.73	11.30	0.00	0.00	0.00
7.2 Grants from CG for current budget	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Subtotal CG transfers for current budget	13.62	10.42	11.14	13.70	9.73	11.30	0.00	0.00	0.00
Total current revenue	86.56	85.22	87.22	88.34	87.94	57.17	72.24	68.95	50.90
8. CG capital transfers	0.00	0.00	0.00	0.00	0.00	14.97	8.79	18.13	21.37
9. Capital transfer from development fund	0.00	0.00	0.00	0.00	0.00	13.21	8.23	0.00	0.00
Subtotal CG capital transfer	0.00	0.00	0.00	0.00	0.00	28.18	17.02	18.13	21.37
10. Own source revenue for capital budget									
10.1 Privatization revenue	4.78	5.88	4.73	4.23	4.33	3.15	0.21	0.59	1.96
10.2 Vehicle tax and road fee for capital budget	8.66	8.89	8.05	7.43	7.72	4.71	3.45	2.85	5.00
10.3 Other own revenue source(s) for capital budget (from UB budget)	0.00	0.00	0.00	0.00	0.00	6.80	7.08	9.49	20.76
Subtotal own source capital revenue	13.44	14.78	12.78	11.66	12.06	14.65	10.74	12.92	27.73
Total capital revenue	13.44	14.78	12.78	11.66	12.06	42.83	27.76	31.05	49.10
Total revenue	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Source: Table A1.1.

Table A1.4. Composition of Total Revenue for UB Government, 2009–11

REVENUE SOURCE	2009 (thousands MNT)	2010 (thousands MNT)	2011 (thousands MNT)	2009 (%)	2010 (%)	2011 (%)
Own revenue sources						
1. Taxes						
1.1 Wage tax	70,273,109.80	92,717,446.10	140,410,685.70	61.04	66.84	72.12
1.2 Deductions	-1,428,763.20	-2,632,686.90	-4,882,818.40			
1.3 Other income tax	743,493.30	830,553.90	1,441,056.10	0.65	0.60	0.74
1.4 Property tax	6,733,511.00	8,653,207.70	10,371,518.20	5.85	6.24	5.33
1.5 Gun tax	1,204.10					
Subtotal taxes	76,322,555.00	99,568,520.80	147,340,441.60	66.29	71.78	75.68
2. Licenses, fees, and permits						
2.1 License fee for mineral exploration	7,906.70	18,679.20	16,244.10	0.01	0.01	0.01
2.2 Mineral royalty	266,936.80	381,924.10	390,059.20	0.23	0.28	0.20
2.3 User fee for common minerals	50,000.00	60,650.00	64,000.00	0.04	0.04	0.03
2.4 User fee for land	17,742,885.80	18,348,734.60	20,580,066.50	15.41	13.23	10.57
2.5 User fee for water and springs	227,030.10	458,425.30	540,922.30	0.20	0.33	0.28
2.6 User fee for timber	12,189.10	39,759.10	74,937.50	0.01	0.03	0.04
Subtotal licenses, fees, and permits	18,306,948.50	19,308,172.30	21,666,229.60	15.90	13.92	11.13
3. User charges						
3.1 Stamp duties	3,935,678.50	1,399,631.30	47,909.60	3.42	1.01	0.02
Subtotal user charges	3,935,678.50	1,399,631.30	47,909.60	3.42	1.01	0.02
4. Rents	759,300.00	772,169.30	1,034,781.90	0.66	0.56	0.53
5. Fines and penalties	3,931,815.20	4,304,946.90	5,209,421.20	3.42	3.10	2.68
6. Other own revenue						
6.1 Dividend of state-owned enterprises	166,862.40	111,613.70	112,911.50	0.14	0.08	0.06
6.2 Own revenue of budget entities	4,705,249.90	5,109,231.20	5,798,818.60	4.09	3.68	2.98
6.3 Other nonclassified own revenues	724,695.00	518,429.40	626,963.10	0.63	0.37	0.32
Subtotal other own revenues	5,596,807.30	5,739,274.30	6,538,693.20	4.86	4.14	3.36
Subtotal current revenue	108,853,104.50	131,092,714.90	181,837,477.10	94.55	94.51	93.40
Own source revenue for capital budget						
Privatization revenue	375,100.00	1,332,803.60	1,570,768.90	0.33	0.96	0.81
10.1 Vehicle tax for capital budget	5,408,098.10	5,771,665.90	10,751,335.80	4.70	4.16	5.52
10.1 Road fee for capital budget	496,892.90	510,572.20	527,132.00	0.43	0.37	0.27
Subtotal own source revenue for capital	6,280,091.00	7,615,041.70	12,849,236.70	5.45	5.49	6.60
Subtotal capital revenue	6,280,091.00	7,615,041.70	12,849,236.70	5.45	5.49	6.60

Source: Elaborated for this report based on data from UB Treasury Department (2009–11).

Table A1.5. Composition of Total Revenue for Two Selected Districts, 2009–11

REVENUE SOURCE	2009 (thousands MNT)	2010 (thousands MNT)	2011 (thousands MNT)	2009 (%)	2010 (%)	2011 (%)
Bayangol District						
Taxes	1,701,852.00	2,480,222.70	4,394,630.80	60.40	70.69	74.83
Unidentified income tax	197,992.80	181,890.20	325,042.90	7.03	5.18	5.53
Self-employment tax	462,857.90	652,065.20	594,948.30	16.43	18.58	10.13
Other income tax	723,710.30	685,501.40	1,316,971.40	25.69	19.54	22.43
Gun tax	5,782.20	6,085.00	7,168.90	0.21	0.17	0.12
Tax on property sale	311,508.80	954,680.90	2,150,499.30	11.06	27.21	36.62
Stamp duties	659,540.60	347,580.60	490,752.20	23.41	9.91	8.36
Fines and penalties	419,958.90	671,801.20	979,490.90	14.91	19.15	16.68
Own revenue of budget entities	7,257.40	7,174.40	7,773.80	0.26	0.20	0.13
Other non classified own revenues	28,868.70	1,884.60		1.02	0.05	0.00
Subtotal current revenue	2,817,477.60	3,508,663.50	5,872,647.70	100.00	100.00	100.00
Capital revenue	0	0	0	0.00	0.00	0.00
Total Revenue	2,817,477.60	3,508,663.50	5,872,647.70	100.00	100.00	100.00
Nalaikh District						
Taxes	154,420.00	192,081.80	255,461.40	47.74	48.72	55.31
Unidentified income tax	12,316.10		162,859.90	3.81	0.00	35.26
Self-employment tax	18,906.50	164,184.30	9,736.10	5.84	41.65	2.11
Livestock tax	6,634.50	737.70	31.20	2.05	0.19	0.01
Other income tax	107,204.60	1,461.30	510.40	33.14	0.37	0.11
Gun tax	918.00	1,011.00	1,044.40	0.28	0.26	0.23
Tax on property sale	8,440.30	24,687.50	81,279.40	2.61	6.26	17.60
Mineral royalty	11,053.50	8,653.00	10,160.60	3.42	2.19	2.20
License fee for mineral exploration	4,000.00	2,900.90	5,225.00	1.24	0.74	1.13
User fee for water and springs	10,283.70	9,982.70	10,437.10	3.18	2.53	2.26
Stamp duties	11,784.50	11,660.00	29,686.10	3.64	2.96	6.43
Fines and penalties	51,327.00	56,399.10	81,942.50	15.87	14.31	17.74
Own revenue of budget entities	2,285.60	26,766.10	6,603.00	0.71	6.79	1.43
Other non classified own revenues	3,269.90	1,118.30	4,796.30	1.01	0.28	1.04
Subtotal current revenue	248,424.20	309,561.90	404,312.00	76.80	78.52	87.54
Capital revenue						
Vehicle tax ^a	75,048.70	84,667.10	57,540.20	23.20	21.48	12.46
Subtotal capital revenue	75,048.70	84,667.10	57,540.20	23.20	21.48	12.46
Total revenue	323,472.90	394,229.00	461,852.20	100.00	100.00	100.00

a. According to 2009–11 budget data, there is no capital revenue for all six urban districts.
Source: Elaborated for this report based on data from UB Treasury Department (2009–11).

Table A1.6. Transfer from the UB Government to the Central Government, 2003–11 (in millions MNT)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Transfer amount	11,259.1	9,963.3	14,803.8	14,177.0	1,539.9	9,132.2	62,751.2	56,159.0	20,898.1
Total current revenue of UB	22,839.3	27,534.9	33,315.3	38,663.0	46,134.7	77,063.9	126,949.0	156,483.7	232,948.8
Share of transfer in total current revenue (%)	49.6	36.4	44.4	36.7	3.3	11.8	49.4	35.9	9.0

Source: UB City Budget Book 2012: 22.

Table A1.7. UB and Districts per Capita Revenue by Sources, 2003–11 (in thousands MNT)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
1. Taxes									
1.1 Wage tax	0.000	0.000	0.000	0.000	0.000	0.000	62.093	77.406	112.134
1.2 Unidentified income tax	0.811	1.525	1.707	0.840	0.779	0.890	0.937	1.054	1.337
1.3 Self-employment tax	1.070	1.588	1.578	1.603	3.547	3.502	3.779	4.672	6.073
1.4 Livestock tax	0.006	0.008	0.009	0.010	0.015	0.023	0.013	0.001	0.000
1.5 Other income tax	0.000	1.956	3.398	6.457	1.408	2.915	5.438	4.592	7.268
1.6 Property tax	3.240	3.652	4.058	4.139	4.792	5.340	6.073	7.435	8.581
1.7 Gun tax	0.019	0.018	0.018	0.020	0.022	0.024	0.028	0.025	0.028
1.8 Tax on property sale	0.385	0.392	0.689	0.904	1.455	1.628	1.156	3.319	1.300
Subtotal taxes	5.531	9.140	11.458	13.972	12.018	14.322	79.516	98.504	136.722
2. Licenses, fees, and permits									
2.1 License fee for mineral exploration	0.000	0.000	0.000	0.000	0.000	0.021	0.026	0.032	0.026
2.2 Mineral royalty	0.850	0.633	0.885	0.885	0.328	0.336	0.382	0.540	0.517
2.3 User fee for common minerals	0.057	0.030	0.039	0.048	0.072	0.078	0.045	0.052	0.057
2.4 User fee for land	4.035	4.074	5.990	6.990	11.014	14.818	16.003	15.766	17.028
2.5 User fee for water and springs	0.036	0.032	0.197	0.220	0.208	0.249	0.228	0.497	0.597
2.6 User fee for timber	0.016	0.012	0.014	0.019	0.018	0.017	0.011	0.034	0.062
Subtotal licenses, fees, and permits	4.994	4.781	7.126	8.161	11.639	15.520	16.695	16.921	18.286

(continued)

Table A1.7. UB and Districts per Capita Revenue by Sources, 2003–11 (in thousands MNT) (continued)

3. User charges																			
3.1 Stamp duties	1.002	3.648	4.219	4.219	3.950	5.104	6.113	6.030	5.718	16.959									
Subtotal user charges	1.002	3.648	4.219	4.219	3.950	5.104	6.113	6.030	5.718	16.959									
4. Rents	1.173	0.768	0.548	0.548	0.690	0.734	0.759	0.685	0.663	0.856									
5. Fines and penalties	4.879	4.802	5.215	5.215	4.917	8.509	4.218	6.233	7.412	0.436									
6. Other own revenue	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000									
6.1 Dividend of state-owned enterprises	0.110	0.074	0.054	0.054	0.083	0.129	0.136	0.150	0.096	0.093									
6.2 Own revenue of budget entities	1.582	1.785	1.515	1.515	1.112	1.502	1.523	4.418	4.586	4.962									
6.3 Other nonclassified own revenues	2.853	1.403	0.379	0.379	0.184	0.389	0.665	0.772	0.560	0.630									
Subtotal other own revenues	4.545	3.262	1.949	1.949	1.379	2.020	2.324	5.341	5.242	5.686									
7.1 Revenue sharing in CG taxes for current budget	4.132	3.677	4.466	4.466	6.070	4.978	10.650	0.000	0.000	0.000									
7.2 Grants from CG for current budget	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000									
Subtotal CG transfers for current budget	4.132	3.677	4.466	4.466	6.070	4.978	10.650	0.000	0.000	0.000									
Total current revenue	26.255	30.076	34.980	34.980	39.139	45.002	53.906	114.500	134.460	178.946									
8. CG capital transfers	0.000	0.000	0.000	0.000	0.000	0.000	14.113	13.932	35.350	75.143									
9. Capital transfer from development fund	0.000	0.000	0.000	0.000	0.000	0.000	12.460	13.043	0.000	0.000									
Subtotal CG capital transfer	0.000	0.000	0.000	0.000	0.000	0.000	26.572	26.975	35.350	75.143									
10. Own source revenue for capital budget	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000									
10.1 Privatization revenue	1.448	2.077	1.897	1.897	1.874	2.218	2.966	0.338	1.145	6.881									
10.2 Vehicle tax and road fee for capital budget	2.628	3.139	3.227	3.227	3.292	3.952	4.437	5.463	5.549	17.591									
10.3 Other own revenue source(s) for capital budget (from UB budget)	0.000	0.000	0.000	0.000	0.000	0.000	6.407	11.228	18.496	73.000									
Subtotal own source capital revenue	4.076	5.216	5.124	5.124	5.165	6.170	13.810	17.030	25.191	97.472									
Total capital revenue	4.076	5.216	5.124	5.124	5.165	6.170	40.382	44.004	60.541	172.616									
Total revenue	30.331	35.292	40.105	40.105	44.305	51.172	94.288	158.504	195.001	351.562									

Source: Elaborated for this report based on data from UB Treasury Department (2003–11).

Table A1.8. Comparison of Per Capita Revenue across Districts

REVENUE SOURCES	2009	2010	2011
Bayangol District			
Taxes	9.733	13.399	22.875
Unidentified income tax	1.132	0.983	1.692
Self-employment tax	2.647	3.523	3.097
Other income tax	4.139	3.703	6.855
Gun tax	0.033	0.033	0.037
Tax on property sale	1.782	5.158	11.194
Stamp duties	3.772	1.878	2.555
Fines and penalties	2.402	3.629	5.099
Own revenue of budget entities	0.042	0.039	0.040
Other non classified own revenues	0.165	0.010	0.000
Subtotal current revenue	16.114	18.955	30.569
Capital revenue	0.000	0.000	0.000
Total Revenue	16.114	18.955	30.569
Nalaikh District			
Taxes	5.1107	6.1060	7.8572
Unidentified income tax	0.4076	0.0000	5.0091
Self-employment tax	0.6257	5.2192	0.2995
Livestock tax	0.2196	0.0235	0.0010
Other income tax	3.5481	0.0465	0.0157
Gun tax	0.0304	0.0321	0.0321
Tax on property sale	0.2793	0.7848	2.4999
Mineral royalty	0.3658	0.2751	0.3125
License fee for mineral exploration	0.1324	0.0922	0.1607
User fee for water and springs	0.3404	0.3173	0.3210
Stamp duties	0.3900	0.3707	0.9131
Fines and penalties	1.6987	1.7928	2.5203
Own revenue of budget entities	0.0756	0.8509	0.2031
Other non classified own revenues	0.1082	0.0355	0.1475
Subtotal current revenue	8.2219	9.8405	12.4354
Capital revenue	0.0000	0.0000	0.0000
Vehicle tax	2.4838	2.6914	1.7698
Subtotal capital revenue	2.4838	2.6914	1.7698
Total revenue	10.7057	12.5319	14.2052

Source: Elaborated for this report based on data from UB Treasury Department (2009–11).

Annex 2. Actual Budget Formats of UB and District Revenue and Expenditures

Table A2.1. Actual Format of UB and District Revenue and Expenditure Budgets (in millions MNT)

ITEMS	2003	2004	2005	2006	2007	2008	2009	2010	2011
Total budget revenue	26,385.0	32,309.8	38,195.8	43,765.5	52,459.8	65,568.0	13,3381.0	164,274.5	245,855.6
Tax revenue collected by districts and UB City	0.0	0.0	23,073.0	27,850.3	26,933.2	38,292.6	10,1112.5	128,483.8	0.0
Tax revenue	15,572.9	21,964.1	28,173.2	33,927.8	36,824.7	52,500.8	11,7635.8	143,070.5	153,269.3
Personal income tax (PIT)	1,642.0	4,647.6	6,374.3	8,801.2	5,893.6	7,839.4	80,115.7	102,094.1	153,269.3
Wage tax	0.0	0.0	0.0	0.0	0.0	0.0	70,273.1	92,717.4	140,410.7
Deduction from wage tax	0.0	0.0	0.0	0.0	0.0	0.0	-1,428.8	-2,632.7	-4,882.8
Unidentified income tax	705.8	1,395.7	1,625.5	829.6	798.8	952.1	1,038.3	1,226.1	1,616.2
Self-employment tax	931.2	1,453.6	1,503.2	1,583.8	3,636.7	3,745.7	4,189.8	5,437.8	7,340.3
Livestock tax	5.0	7.7	8.9	9.8	14.9	24.1	14.3	1.6	0.2
Other PIT	0.0	1,790.6	3,236.6	6,378.0	1,443.3	3,117.6	6,029.0	5,343.9	8,784.8
Property tax	2,834.6	3,360.4	3,882.0	4,107.8	4,934.9	5,736.6	6,764.1	8,682.0	10,405.4
Immovable property tax	2,818.3	3,343.8	3,865.0	4,088.2	4,912.5	5,710.9	6,733.5	8,653.2	10,371.5
Gun tax	16.3	16.6	17.0	19.6	22.4	25.8	30.6	28.8	33.9
Consumption tax	5,880.3	6,239.6	7,111.7	9,054.7	8,831.0	15,789.0	5,560.1	5,947.4	10,808.9
Value added tax	3,594.5	3,366.1	4,253.2	5,996.2	5,103.4	11,389.9	0.0	0.0	0.0
Excise tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Vehicle tax	2,285.8	2,873.6	2,858.4	3,058.5	3,727.6	4,399.1	5,560.1	5,947.4	10,808.9
Other taxes	5,216.0	7,716.4	10,805.2	11,964.0	17,165.2	23,135.7	25,195.9	26,347.0	42,598.2
Stamp duties	871.5	3,339.8	4,018.2	3,902.3	5,232.9	6,537.7	6,685.3	6,654.1	20,496.9
License fee for mineral exploration	0.0	0.0	0.0	0.0	0.0	22.0	28.8	37.4	31.6
Land payment	3,509.9	3,729.4	5,705.3	6,904.6	11,290.8	15,847.9	17,742.9	18,348.7	20,580.1
User fee for water	31.2	29.3	188.0	217.1	213.4	266.5	252.6	577.9	721.4
User fee for timber	13.6	10.9	13.5	18.6	18.4	18.1	12.2	39.8	74.9
Mineral royalty	739.7	579.4	843.0	874.4	335.8	359.8	424.1	628.6	624.8
User fee for common minerals	50.0	27.6	37.2	47.1	73.8	83.7	50.0	60.7	68.6

(continued)

Table A2.1. Actual Format of UB and District Revenue and Expenditure Budgets (in millions MNT) (continued)

ITEMS	2003	2004	2005	2006	2007	2008	2009	2010	2011
Nontax revenue	9,217.5	8,085.1	7,559.7	7,093.9	11,869.6	8,153.7	14,088.3	16,008.7	18,886.4
Dividends of state-owned enterprises	95.5	67.4	51.7	81.9	132.1	145.2	166.9	111.6	112.9
Rent of state assets	1,020.0	703.2	522.0	682.0	752.0	811.3	759.3	772.2	1,034.8
Own revenue of budget entities (schools, universities, hospitals)	1,376.4	1,634.6	1,443.3	1,098.5	1,540.0	1,629.0	4,898.1	5,337.2	5,997.5
Interest and fines (penalties)	4,243.9	4,395.9	4,966.9	4,856.7	8,723.0	4,511.0	6,910.7	8,625.8	527.1
User fees for roads (entrance tolls)	0.0	0.0	215.0	193.0	323.5	345.7	496.9	510.6	10,452.4
Other unclassified revenues	2,481.8	1,284.1	360.7	181.8	399.0	711.6	856.5	651.4	761.6
Capital revenue	1,594.6	2,260.6	2,462.8	2,743.8	3,765.6	4,913.5	1,656.9	5,195.2	9,887.4
Privatization revenue	1,260.0	1,901.4	1,807.0	1,851.0	2,274.0	3,172.0	375.1	1,332.8	8,316.6
Tax of property sale	334.6	359.2	655.8	892.8	1,491.6	1,741.5	1,281.8	3,862.4	1,570.8

Source: UB Treasury Department. Data for 2003–11.

Table A2.2. UB Government Budget Expenditure Format and Percent Execution (in thousands)

DESCRIPTION	PLANNED 2011	EXECUTED 2011	EXECUTION (%)	EXECUTED RELATIVE WEIGHT
UB	183,816,195.40	140,833,637.00	77	
Cash beginning balance	-	1,127,287.00		
Bank beginning balance	-	1,127,275.60		
Beginning balance of receivables from other organizations and persons	-	64,252.50		
Beginning balance of payables to other organizations and persons	-	41,376.10		
Total income	183,816,195.40	142,479,196.10	78	
Investment financed by state budget	107,957,000.00	71,413,331.80	66	
Financed by road fund	11,255,000.00	20,489,686.60	182	
Financed by own revenue from basic activities	3,020,895.00	4,256,057.70	141	
Financed by additional/supplementary activities	1,024,513.20	1,542,760.90	151	
Financed by beginning balance	8,996,649.60	-		
Financed by state budget	51,562,137.60	43,804,088.70	85	
Other income	-	973,270.40		
Total expenditure and net borrowing	183,816,195.40	140,833,637.00	77	100.00
Recurrent or current expenditures	58,382,995.40	48,817,639.40	84	34.66
Expenditure in goods and services	51,687,585.10	42,150,381.00	82	29.93
Basic salary and bonuses	7,095,323.10	6,863,636.30	97	4.87
Basic salary	5,321,047.30	5,233,399.70	98	3.72
Bonuses	838,141.60	770,073.60	92	0.55
Contract worker's salary	223,189.90	213,482.00	96	0.15
Allowances: transportation and food	712,944.30	646,681.00	91	0.46
Social insurance fees paid by employer	801,301.10	737,920.20	92	0.52
Pension and assistance insurance fees	659,751.30	606,187.80	92	0.43
Pension insurance fees	509,895.00	456,831.00	90	0.32
Assistance insurance fees	35,390.00	52,508.40	148	0.04
Insurance fee: Sickness and accidents in the job	79,079.50	64,593.60	82	0.05
Unemployment insurance fee	35,386.80	32,254.80	91	0.02
Health insurance fee	141,549.80	131,732.40	93	0.09
Health insurance fee paid by employer	141,549.80	131,732.40	93	0.09
Expenditure on other goods and services	43,790,960.90	34,548,824.50	79	24.53
Stationary	207,439.60	193,515.30	93	0.14
Electricity	861,848.40	742,682.40	86	0.53
Heating	552,355.30	417,960.50	76	0.30
Transportation and gasoline	519,851.70	507,669.00	98	0.36
Communication and postage	258,317.40	242,119.40	94	0.17

(continued)

**Table A2.2. UB Government Budget Expenditure Format and Percent Execution (in thousands)
(continued)**

DESCRIPTION	PLANNED 2011	EXECUTED 2011	EXECUTION (%)	EXECUTED RELATIVE WEIGHT
Drinking and service water	139,823.90	96,831.90	69	0.07
Domestic subsistence expenditure	33,150.00	29,889.20	90	0.02
Foreign subsistence expenditure	1,000,000.00	847,205.20	85	0.60
Books, newspapers, journals	19,000.00	18,303.00	96	0.01
Training and internships	72,460.00	59,697.40	82	0.04
Purchase of small items	357,099.50	431,288.10	121	0.31
Equipment purchase	70,000.00	62,327.60	89	0.04
Furniture cost	234,591.00	320,164.60	136	0.23
Less priced, fast depreciated items	52,508.50	48,795.90	93	0.03
Soft items and uniforms	62,850.00	59,507.50	95	0.04
Food	117,720.00	117,694.40	100	0.08
Drugs	2,962.00	2,962.00	100	0.00
Routine maintenance	239,050.00	223,069.40	93	0.16
Expenditure on art work	21,018.80	19,934.90	95	0.01
Small taxes, user fees and other expenditure	1,606,391.20	1,524,939.80	95	1.08
Expenditure on foreign guests	300,000.00	331,895.80	111	0.24
Organizing sports activities	49,856.30	49,856.30	100	0.04
Rent	232,795.20	229,517.60	99	0.16
Not allocated local expenditure	581,394.80	555,796.80	96	0.39
Printing matter	256,395.00	225,078.20	88	0.16
Festival expenditure	300,000.00	305,823.50	102	0.22
Unallocated spending	24,999.80	24,895.10	100	0.02
Current spending on activities and programs	64,000.00	18,946.40	30	0.01
Activities related to crime prevention	850,000.00	846,974.20	100	0.60
Environmental protection and recovery	2,680,450.10	1,235,827.40	46	0.88
Street lighting and cleaning	3,336,931.70	3,461,208.90	104	2.46
Site security cost	60,939.80	59,640.00	98	0.04
Local reserve fund	2,632,000.00	2,038,471.60	77	1.45
Financial support to the parties in the parliament	45,000.00	45,000.00	100	0.03
Veterinary medicine cost	170,293.00	170,293.00	100	0.12
Services received from others	15,614,302.60	9,203,989.60	59	6.54
Payments for services provided on behalf of the CG government	15,614,302.60	9,203,989.60	59	6.54
Advertisement and information cost	49,300.10	38,520.90	78	0.03
Land rent	2,142,441.40	1,809,082.30	84	1.28

(continued)

**Table A2.2. UB Government Budget Expenditure Format and Percent Execution (in thousands)
(continued)**

DESCRIPTION	PLANNED 2011	EXECUTED 2011	EXECUTION (%)	EXECUTED RELATIVE WEIGHT
Surplus from previous year	8,909,918.10	8,918,534.30	100	6.33
Subsidies and recurrent transfer	6,695,410.30	6,667,258.40	100	4.73
Subsidies	6,195,454.30	6,194,767.60	100	4.40
To electricity producer/electricity and heating loss	260,000.00	260,000.00	100	0.18
To public transportation	4,990,454.30	4,990,454.30	100	3.54
Other subsidies and transfer	295,000.00	295,000.00	100	0.21
International organization member tax	650,000.00	649,313.30	100	0.46
Transfer to families	499,956.00	472,490.80	95	0.34
One time assistance and reward	488,956.00	461,490.80	94	0.33
Compensation	11,000.00	11,000.00	100	0.01
Capital expenditures	125,433,200.00	92,015,997.60	73	65.34
Investment financed own revenue budget	119,433,200.00	86,016,239.60	72	61.08
Food products/meat reserves	6,000,000.00	5,999,758.00	100	4.26
Cash ending balance	-	2,772,846.10		
Bank ending balance	-	2,772,845.40		
Ending balance of receivables from other organizations and persons	-	61,455.70		
Ending balance of payables to other organizations and persons	-	39,748.00		

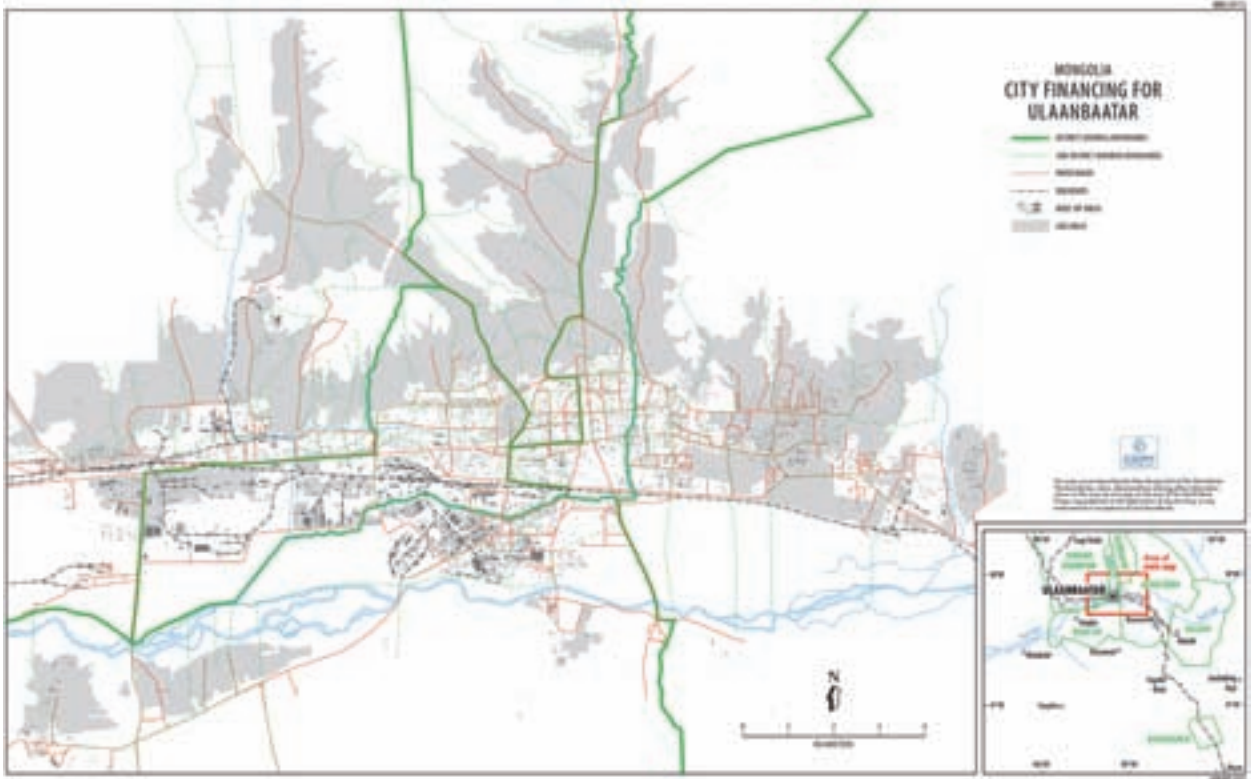
Source: UB Treasury Department. Computations of percentages for fiscal 2011 were done for this report.

Table A2.3. UB Government's Actual Budget Revenue Format (in millions MNT)

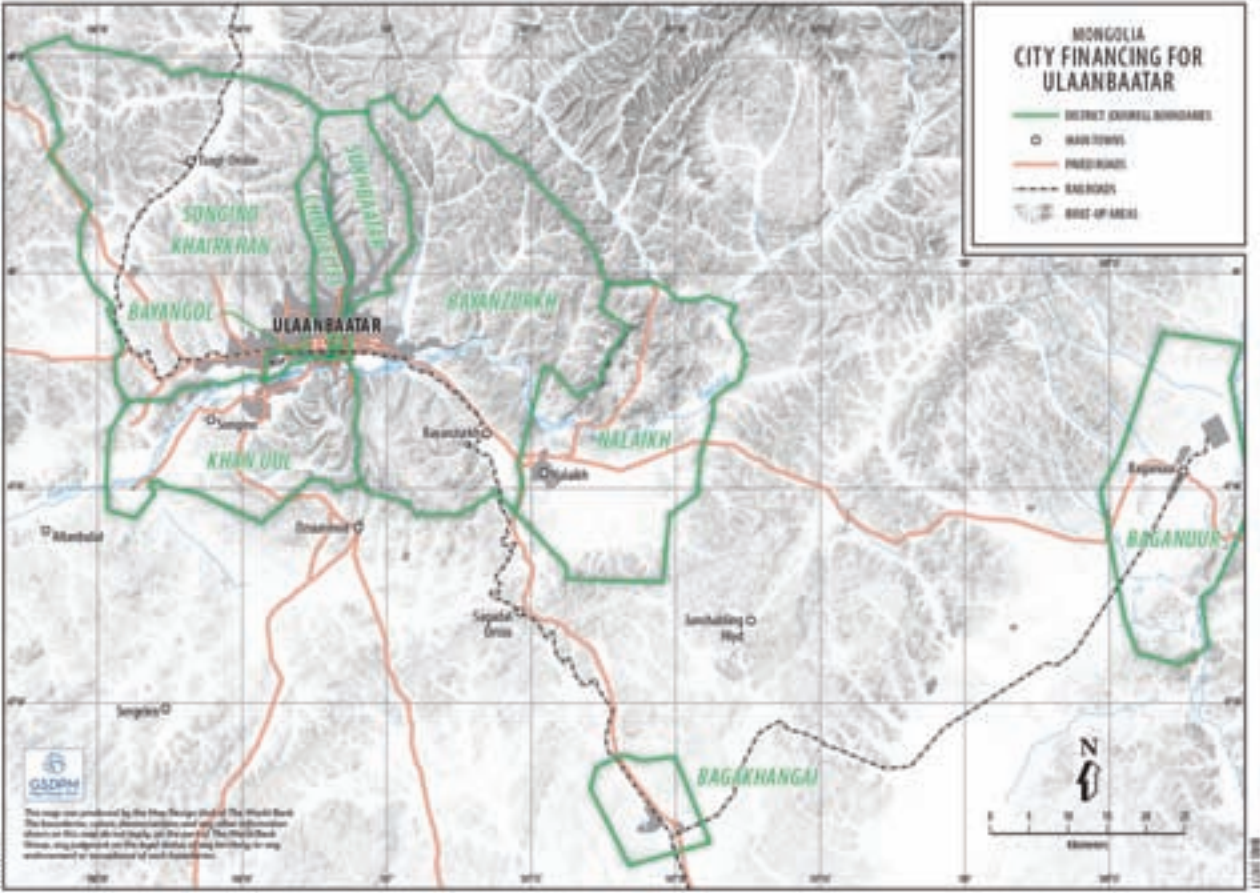
NO	REVENUE SOURCES	2009	2010	2011
	Total revenue and transfers	115,133.2	138,707.8	194,686.7
A	Current revenue	114,758.1	137,375.0	193,115.9
I	Tax revenue	103,973.3	126,048.0	179,805.9
1	Income tax	69,587.8	90,915.3	136,968.9
1.1	Personal income tax (PIT)	69,587.8	90,915.3	136,968.9
1.1.1	Wage tax	70,273.1	92,717.4	140,410.7
1.1.2	Deduction of PIT	-1,428.8	-2,632.7	-4,882.8
1.1.3	Unidentified income tax		0.0	0.0
1.1.4	Self-employment tax		0.0	0.0
1.1.5	Livestock tax		0.0	0.0
1.1.6	Other income taxes	743.5	830.6	1,441.1
2	Property tax	6,734.7	8,653.2	10,371.5
2.1	Immovable property tax	6,733.5	8,653.2	10,371.5
2.2	Gun tax	1.2	0.0	0.0
3	Tax on goods and services	5,725.0	6,214.2	11,205.4
3.1	Tax related to license fee on special purpose manufacturing	5,408.1	5,771.7	10,751.3
3.1.1	Vehicle tax	5,408.1	5,771.7	10,751.3
3.1.2	License fee for the exploration of resources other than minerals		0.0	0.0
3.2	Other taxes and fees on goods and services	316.9	442.6	454.1
3.2.1	Royalty on mining	266.9	381.9	390.1
3.2.2	User fee for common mineral resources	50.0	60.7	64.0
4	Other taxes	21,925.7	20,265.2	21,260.1
4.1	Stamp duties	3,935.7	1,399.6	47.9
4.2	License user fee for mineral resources	7.9	18.7	16.2
4.3	Land payment	17,742.9	18,348.7	20,580.1
4.4	User fee for water and springs	227.0	458.4	540.9
4.5	User fee for timber	12.2	39.8	74.9
4.6	Other taxes and fees		0.0	0.0
II	Nontax revenue	10,784.8	11,327.0	13,310.0
1	Dividends	166.9	111.6	112.9
2	Revenue from state property renting	759.3	772.2	1,034.8
3	Own revenue of budget entities	4,705.2	5,109.2	5,798.8
4	User fee for roads	496.9	510.6	527.1
5	Revenue from fines and interests	3,931.8	4,304.9	5,209.4
6	Other revenues	724.7	518.4	627.0
B	Capital revenue	375.1	1,332.8	1,570.8
1	Revenue from property sale		0.0	0.0
2	Privatization revenue	375.1	1,332.8	1,570.8

Source: UB Treasury Department. Computations of percentages for fiscal 2011 were done for this report.

City of Ulaanbaatar



City of Ulaanbaatar Reflecting District Boundaries



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