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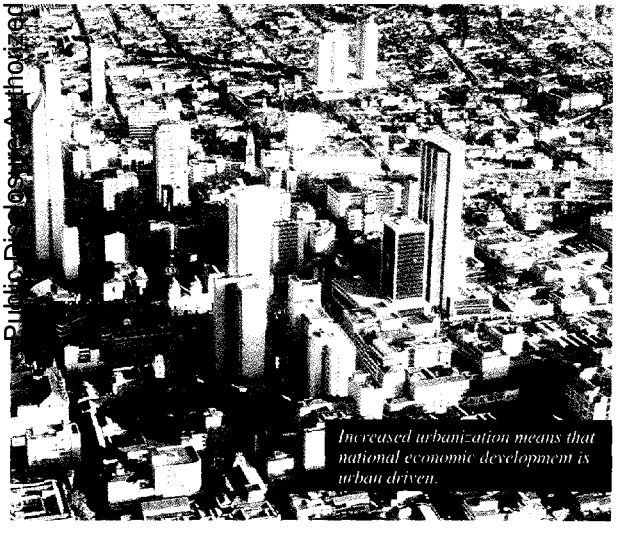
URBAN FINANCE ISSUE

Good Municipal Financing Practices in Latin America

by Monica Ramirez Londono

BOGOTA. Traditionally, local economic development in Latin America has been viewed as a consequence of national economic trends and policies introduced by central governments. Successful local economic development was considered to be simply the result of chance that a particular region or place ended up benefiting from a government investment, public infrastructure improvements, or better facilities.

However, as increased urbanization has taken hold on the continent, with more than 70 percent of the population now living in towns and cities, it is recognized that national economic development is increasingly urban-driven; it is also recognized that local authorities play a crucial role in removing inefficiencies in production that hinder the productivity of businesses, private enterprises, and family enterprises, which together account for nearly 80 percent of the gross national product (GNP) in developing countries.



Increased urbanization means that national economic development is urban driven.

Promoting local economic development

The importance of local government in local economic development is also underlined in the context of Latin America's recent economic crises and the macroeconomic or structural adjustment policies that were introduced in the region. Local governments were practically the only level of government during the 1980s where economic development and social policies were combined. Besides, local governments have certain clear advantages over national governments in promoting some kinds of local economic development. They have a better understanding of the dynamics of a local economy and are also better placed to mobilize community organizations.

Municipal governments in the region have tried to promote local economic development in various ways. Traditional approaches include establishing industrial parks, or places where enterprises can start up with the necessary infrastructure. Some of the most important new initiatives, however, are deregulating land markets, making investments in urban infrastructure, and making services run more efficiently. All three help stimulate economic productivity and private enterprise.

An interesting case is Tabio, a small town in Colombia, situated on the outskirts of Bogota. In the early days of Colombia's decentralization program, Tabio's mayor managed to get his local community to make a commitment to reduce the town's poverty and develop the town. He did this by motivating young people and helping create a sense of local pride and identity in the town. For instance, an inventory of the municipalities' botanical resources made the local community aware of the threats to the natural environment, and motivated them to work for the conservation of these resources. The community also became involved in local projects to pave streets and spruce up public places. These endeavors helped give Tabio the tourist appeal it had once had, and brought economic activity and dynamism back to the town.

In another initiative, IULA-CELCADEL in the Andean region has

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DEPARTMENTS

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This issue of *The Urban Age* is funded by the Danish Agency for International Development, the Federation of Canadian Municipalities (Canadian International Development Agency), the Fannie Mae Office of Housing Research, the Dutch Ministry of Foreign Affairs, and the World Bank. Developmental funding has been provided by the UNDP-UNCHS (Habitat)-World Bank Urban Management Programme and the World Bank.

LETTERS TO THE EDITOR

We welcome your comments, thoughts, and suggestions on The Urban Age.

Editor:
As the director of the French-Vietnamese Management Center in Ho Chi Minh City, I am very interested in your magazine *The Urban Age* and its coverage of issues such as urban infrastructure.

At present, Ho Chi Minh City is undergoing one of the most rapid and far-reaching social and economic revolutions found in the developing countries; therefore, its urban planners and managers should be aware in the coming years of the issues and solutions to infrastructure problems. A journal such as yours can certainly contribute to this aim.

Laurent Schwab
Centre Franco-Vietnamien de Formation à la Gestion
Ho Chi Minh City
Vietnam

Editor:
Your edition of *The Urban Age* on Information and Cities included a particularly informative piece on urban information systems. In terms of tecnological development, developed countries are better placed because these new technologies originate there before being exported to developing countries. Although new equipment such as satellites and cellular telephone technology now make communication possible among all people, these new technologies are often exported to developing countries that lack adequate infrastructural networks to support their use. Developing countries need to be better prepared in education and training before these technologies can be used to solve urban problems.

E.A. Arigbede
Lecturer in Urban Planning
Ondo State Polytechnic
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Editor:
In order to create an information database at the urban level, the availability of precise demographic data is an essential component for the efficient functioning of a city and its economic development. In the absence of reliable demographic data such as population statistics and migration and wealth levels, many mistakes in infrastructure planning and project design will occur. Sustainable urban development cannot be achieved without a reliable and accessible urban information database.

Dr. A.M. Thirumurthy
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Editor's Note

If recent global urbanization statistics mean anything (some studies claim that more than 60 percent of the world's population will live in cities by 2020) then, as Nasser Munjee writing from Bombay states, the efficiency of the city will increasingly determine the prosperity of the nation. This means that urban finance will play a key role as the engine of national economic growth.

In this issue we have focused on the ways that developing countries are experimenting with increasing municipal efficiency, particularly in the area of fiscal decentralization. Eduardo Wiesner from his long experience in Colombia maintains in his article that certain criteria must be met in order to sustain decentralization efforts. Most crucial for success is the sequencing aspect: governments should start with the functions to be transferred and then with the revenues—not the other way around.

Decentralization really underlines the question of how to improve the collection of local revenues and how cities should generate their own resources. One solution is offered by our guest editorialist, George Peterson of The Urban Institute: the recognition by local governments and by increasingly-active community groups, of the reality of budget constraints. This is a reality that is starkly underlined by Jonathan Foreman who writes about the Washington D.C. government's inability to keep within its budget and the subsequent formation of a financial control board by the U.S. federal government to enforce fiscal discipline.

Local governments are key to the thorny political question of how to share the burden of transition. Monica Ramirez Londono develops this theme in her lead: that decentralization is not sustainable without the corresponding transfer of responsibilities from central to local governments and proportional local fiscal effort. These should also be accompanied by strengthened local financial management.

In this issue, Cecilia Mou Charles from Ghana and Bob Vine from New Zealand, illustrate the constant dance between central and local governments over expenditure versus responsibility. Roberto Salinas from Paraguay describes the usefulness of a new urban cadastre to identify local government assets. Robert Kehew writes from the Philippines about the emergence of a fledgling bond market in Naga City and Mayor Hector Osuna Jaime tells us about Tijuana's betterment levy; both successful examples of how local government can independently generate its own resources.

During preparation of this issue, Mary McNeil has been seconded to the Bank's Environment Department to help prepare the Bank's annual report on the environment. In her absence, I have been the Acting Editor. As always, we welcome your comments, suggestions, and feedback on *The Urban Age*.

—Margaret Bergen

What Kind of Financing Systems Support Decentralization?

by George E. Peterson

George E. Peterson is senior fellow at the Urban Institute in Washington, D.C., and the author of several books on municipal finance and fiscal decentralization in the United States and the developing world.

A wave of decentralization is passing through developing nations, changing the expectations that citizens have of government. From Latin America to Asia, more responsibility has been turned over to local governments for basic service delivery. With this enhanced role has come increased citizen participation in decision-making, either in the form of direct elections of local officials or rules requiring that neighborhood organizations participate in setting priorities for local public works.

However, the type of financing systems that can best support decentralization are still being debated. In the theory of fiscal choice, local governments and citizens should pay for most local services from their own taxes or user fees. As long as local investments must be financed by the community itself, priority-setting becomes a matter of urgency; a community has to weigh better service quality and facilities against the costs of paying for them. When public works appear to be provided "free" by a higher level of government priority needs become endless, and communities must wait for central governments to decide which if any of their requests will be met.

Maybe the most direct way to finance decentralization would be to turn over both service responsibilities *and* revenue-raising capacity to local governments. In reality central governments and local authorities have resisted this solution: most central governments are reluctant to relinquish control over the principal national taxes, and most local authorities are not eager to assume more taxing authority.

The lack of appeal of tax decentralization is easy to understand. To central government, it suggests losing control of the revenue side of the national budget and having macroeconomic policy held hostage to local government budgetary policies. And local officials would rather have the right to designate investment priorities.

The most common solution to financing decentralization has been to increase local governments' share in nationally collected taxes through automatic revenue sharing. This approach allows central governments to retain control of tax rates and tax administration, while ensuring local authorities a higher flow of revenues. Revenue sharing arrangements of this kind have accompanied decentralization efforts in India, the Philippines, Central and Eastern Europe and many countries in Latin America.

Whether revenue sharing provides a stable basis for financing decentralization is open to debate. If central government retains the power to adjust annually the share of centrally collected revenues that go to local governments, then local authorities face a fundamental uncertainty about their revenues that make advance budgeting impossible.

Throughout Central and Eastern Europe, central governments have drastically reduced the share of personal income taxes allocated to local governments to relieve pressure on the central budget. These adjustments create a local dependence on central governments' annual revenue sharing decisions that is just as profound as the previous dependence on central government spending decisions. Brazil and Colombia for example have sought to remove the uncertainty surrounding revenue sharing by writing local authorities' entitlements to specific shares of nationally collected taxes into their constitutions. However, pressure has emerged to re-write the constitutions to reduce local authorities revenues. Brazil's central government for example has argued that its own budgetary management is crippled by the magnitude of revenues it must by law distribute to state and local authorities.

Behind the conflict over revenue sharing is the fact that most countries chose initially to transfer centrally collected tax revenues to the local level, without clarifying what service functions municipalities would have to provide from these resources. This of course made decentralization much more palatable to local authorities. But it has entangled the different levels of government in negotiations over just which service responsibilities should be transferred to local governments, whether the cost of these services fairly offsets the revenues that were transferred, and if the parties cannot agree on an equitable sharing of service expenditures, whether the central government can take back some of the revenues it originally allocated to the local level.

"The principal of moving budget choices "closer to the people" is an illusion unless local budgets are balanced and expenditure choices are defined."

There is no universal answer as to how decentralization should be financed. But experience does suggest that revenue and service transfers should be matched as closely as possible from the outset, so that decentralization involves a fiscally neutral devolution of responsibilities, not a disguised slashing of the national budget burden or a hidden windfall for municipalities. This requires careful estimates of the full costs of the services that are being turned over to lower levels of government and agreement on the service and revenue mix that ultimately will be transferred, before the transfers begin.

Local governments also need to acknowledge the reality of their budget constraints. Whether local spending decisions are made by mayors, by citizen voters at public meeting, or by neighborhood councils, the revenue side of the budget needs to be clearly defined and decision makers required to live with the resources available to them.

There are promising models of the constructive use of budget constraints in the developing world. The city of La Florida in Chile has developed a formal mechanism for making community groups the linchpin of the municipality's capital budgeting process. The community groups are given 60 days to consult with the citizenry on project priorities. A final assembly is organized in which all of the groups attend where a budget consensus is hammered out—their real power of course not just being the decision makers but recognizing and accepting the budget constraint.

Budget-balancing exercises of this kind are thus the key to decentralization. The worldwide momentum of decentralization can only be sustained if governments at all levels are able to agree on the financing rules that underpin the new decentralized system, and if local authorities commit themselves to incorporating the budget constraint into their daily operations.

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launched a regional program aimed at strengthening municipal capacity to promote local development. The project's aim is to create conditions in five medium-sized towns in Venezuela, Colombia, Ecuador, Peru, and Bolivia conducive to attracting private companies that generate jobs and attract capital. Through training and technical assistance, the project hopes to increase the capacity of municipalities to market projects and form partnerships with private firms, other municipalities, other levels of government, nongovernmental organizations, and community organizations.

Another innovative approach to promoting local economic development is the case of Piedecuesta in Colombia. The city's growth quadrupled since the mid-1980s, and the administration was faced with the challenge of increased demand for urban services. It solved this problem in a creative manner. Through negotiations, local property developers took on responsibility for maintaining urban infrastructure, thus reducing responsibility on the fiscally strained municpality. Improvements in the housing stock were reflected in higher market prices and since 1989 the city has managed to increase its property tax collection by a factor of five.

As more systematic, institutionalized efforts emerge throughout Latin America—efforts that are aimed at developing local government capacity to promote economic development and that are supported by central government and/or international donor agencies—improved local financing should continue to occur with complementary improvements in urban infrastructure.

Interdependence between local economic development and municipal financing

Although systematic studies have not yet been done on the correlation between local economic development and municipal financing, from the examination of a few cases there seems to be a considerable interdependence between the two. For instance, the more wealth that is generated locally, the greater the potential for revenue collection, and the greater the demands made by the community for public investment in urban infrastructure. At the same time, the better the quality of public investment, the bigger the local economic development effects.

A study of the prospects of the capital district finances of Bogota carried out by Mision Bogota Siglo XXI, outlines what the long term revenues and expenditures may be with respect to the region's gross product. The study claims that between 1961 and 1990, the consolidated revenues in the district have been rising, in both constant and current value terms as well as in per capita terms. The fact that city revenues were increasing during the period at a faster rate than the gross regional product meant that such finances played an increasingly important role in regional growth, reflecting the considerable financial effort involved in capital investment in the city and increasing service coverage.

Most of the growth of such revenues was explained in the study by changes in the financial situation of the city's utilities, stemming from user charges and loans for capital investments. In fact, revenues derived

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Glossary of Terms

by Robert Varley

We present here an abridged glossary of terms that gives some of the more arcane terminology found in urban finance jargon a refreshing twist. Robert Varley is technical director for finance and private sector activity with USAID's Global Bureau's Environmental Health Project [EHP]. He has worked extensively in Indonesia in both the banking and irrigation sectors. He was an HIID advisor and consultant to the senior management of the Bank Rakyat Indonesia [BRI] from 1985 to 1993.

Ability to Pay—a concept that does not correspond in social science usage to what we would infer from common sense. Ability to pay is a subjective judgment predicated on some assumption as to what people ought to pay. Thus, the low-income clients are said to have a lower ability to pay than middle-income earners, irrespective of whether or not they buy the good/service.

Asset—something with market or exchange value that is part of the wealth or property of the owner.

Betterment Levy—a taxation device used to ensure that the beneficiaries of a government-financed project (usually infrastructure) pay for all or part of the costs.

Capitalization—it originally meant the aggregate value of a company, measured by the value of all outstanding equity as shown by stock prices. More recently it has been used to describe the process of providing money capital to start up a productive enterprise or financial institution.

Cashflow—yet another widely used term best understood in contrast to accounting terms such as sales and costs of production, which are often imputed values rather than actual sums of money that have changed hands.

Channeled Credit—credit made on the understanding that it be used for a specific purpose decided by the lender.

Collateral—an asset belonging to a customer that is held by the lender as security in the event of default.

Cost Recovery—a term emphasizing that all entities must pay their way or get someone else to do it for them. The degree of cost recovery is the percentage of full costs paid by the user or beneficiary of the goods or services supplied.

Cost of Funds (COF)—the cost a lender must pay on the funds lent out to borrowers.

Credit—allowing the use of goods and services without immediate payment. Credit may take the form of consumer credit, trade credit, or bank credit.

Debt—an amount of money or some other asset owed by one individual or organization to another. A debtor owes money, while a creditor is owed money.

Externality—also described variously as external effects, external economies/diseconomies, and spillover effects. If there were no externalities, competitive markets would ensure an allocation of resources wherein the price paid for each good or service was the same as the cost of the resources required to produce that good or service. Externalities arise because some byproducts of production and consumption are neither owned by nor the responsibility of any single party. Air pollution imposes costs on people (dirty lungs and washing) but will impose costs on the producer only if there are enforceable regulations that force that producer to pay compensation.

Finance—another word with many meanings; commonly taken to mean source of money to pay for something. More broadly, it is the provision of money when and where it is required. The financing question is usually posed as "who will pay for this?"

Funds—another fancy word for money, in this case, money available for a specific purpose.

Fungibility—the quality of money that makes one individual specimen indistinguishable from another. Anything used as money (gold, shell bank notes) must have this quality. The fungibility of money makes it

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from service delivery fluctuated much more in terms of income than other financial sources in the city. However, as income deriving from a demand for public goods and services also fluctuated considerably, public investment to expand city services had to rely on borrowing, and on the indexing of user charges, in order to recover the capital investment costs and service the debt. It has therefore become a matter of concern whether the city's finances in future will be able to support such a high level of debt and debt service charges, and whether user charges have been raised to the point where they cannot be increased.

Meanwhile, with respect to tax revenue sources, the Bogota city study noted that there was a constant, decreasing trend in tax revenues' participation in gross regional product in spite of a relative fluctuation in income derived from the urban taxes. The reasons for such constraint in tax collection are the political impossibility of raising taxes and the difficulties of keeping property censuses up to date. Consequently, tax collection in Bogota remains below its potential.

Regarding the expenditure side of the city's finances, the Bogota study established what it considers will be the most likely impact of the city's economy on the demand for goods and services. In view of the opening up of the national economy and the anticipated importance of Bogota, three major public investment priorities are clear. These are communications and city transport infrastructure, investments in health and education services, and investments in non-tradable local goods such as housing. It is anticipated that investments in these three areas will increase local productivity and competitiveness and help slow down inflation by increasing the supply of non-tradable local goods and services.

Habitat II Urban Finance Conference, September 10–13, 1995

As one of the events leading up to the City Summit of Habitat II that will take place in Turkey June 3–4, 1996, an Urban Finance Colloquium will be held September 10–13, 1995, at the World Bank. The colloquium is jointly sponsored by UNCHS (Habitat II), the World Bank, USAID, and the U.S. Department of Housing and Urban Development.

The colloquium will gather together 60 participants from developing countries including policymakers and finance experts as well as representatives from multilateral and bilateral organizations, non-government organizations, the private sector, and academia.

The focus of the colloquium will be a series of roundtable discussions developed along three themes: examining some of the emerging, innovative ways of accessing credit; clarifying the intergovernmental dimension of urban finance; and improving local accountability and resources.

Following the opening session, there will be three plenary sessions held on the first day. The first two will focus on the overall economic framework of urban finance, while the third will show the linkages between the themes to be discussed in the roundtable sessions and their broader economic implications. The third day's plenary sessions will synthesize the roundtable discussions into recommendations for future follow-up.

Overall, what this study of Bogota shows is how affected municipal revenues may be by a city's economic development. At the same time, the study also shows what type of public investment is needed to maintain and increase urban productivity and competitiveness when the economy is being deregulated and the demand for basic services increases.

How decentralization affects local finances

Another trend has been a vigorous decentralization movement in

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difficult for lenders to ensure that borrowers use the loan funds in the way lenders wish. One way they try to get around "misuse of funds" is to lend in kind. Often a person will borrow money for one stated purpose, but the effect of the loan is to finance another activity.

Hard Budget Constraint—a circumstance in which bills have to be paid. The classic example of the contrasting soft budget constraint occurs in nationalized industries and government-owned enterprises where deficits are financed by transfers from a central government that cannot afford politically to let these organizations be declared bankrupt.

Index-linked—a loan agreement that allows the value of loan repayments to be linked to an index of prices or a reference interest rate such as that on short-term government bills. In this way, short-term funds (such as liquid savings accounts) can finance long-term loans without the problem of liability mismatch (short-term liabilities and long-term assets).

Investments—in economic parlance, the amount by which the stock of capital goods of a firm or economy changes during a period of time. In everyday language, it is the purchase of an asset or undertaking of a commitment requiring an initial sacrifice followed by subsequent benefits.

Lumpy Expenditure—goods or services purchased requiring a large payment at one time, but whose benefits are enjoyed over a long period of time.

Minimalism—an approach to providing financial services to poor people that stresses efficiency and maximum outreach over other objectives stressed by the poverty-lending approach. Procedures are simple and costs of enforcing requirements for getting a loan (e.g., gender, income, place of residence) are minimized.

Principal—the initial amount lent. Loan repayments are accounted for in two components: a return of principal and interest. In calculating interest rates, an allowance should be made for expected inflation that will diminish the purchasing power of the amount of money represented by the principal.

Risk—when a range of uncertainty exists about possible outcomes. In modern corporate finance, risk is identified with measurable probabilities based on historic data. Keynes was among the first to distinguish between risk, which is measurable, and uncertainty, which is not.

Savings—in its fundamental economic sense, a use of income for other than current consumption. In primitive societies with poorly developed financial systems, savings may be made in the form of physical assets such as gold and cattle.

Solidarity Lending—an approach to lending with many variations. In its extreme form a loan is made to a group, with joint responsibility for repayment. If one member fails to pay, the others must make up the difference or the loan goes into arrears.

Subsidy—a payment made by someone other than the consumer of a good or service, which is supposed to reduce the price paid by the consumer.

Willingness to Pay—the amount a consumer will pay for a particular quantity of a good or service. In consumer demand theory, willingness to pay automatically implies ability to pay. In contemporary social science writing, "ability to pay" is sometimes contrasted with willingness to pay. The implicit assumption here is that even though people are willing to—and actually do—pay a certain amount, they lack the ability to pay because they should have spent this money on something else.

This glossary was excerpted from a paper titled "Applied Study 2: Financial Services Environmental Health," which is available from EHP, 1611 North Kent Street, Suite 300, Arlington, VA 22209. It is also available as a staff working paper, "Household Credit and Urban Environmental Health," from RTI, P.O. Box 12194, NC 27708.

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fiscal matters in most Latin American countries. As central government transfers of funds to local, municipal, and regional entities have increased significantly since the 1980s, municipal governments in the region have become more financially stable. Nonetheless, the decentralization movement may be at a turning point, and might even be reversed by central governments. A major problem is that if the devolution of responsibilities to local governments does not match the central government transfers, the advantages of decentralization—in terms of allocating and using funds more productively and efficiently—may simply be undermined.

By the year 2000, most Latin American countries will have introduced some form of decentralization as part of a series of reforms of the state sector to ensure sustainable economic growth. The process employs systems that are well designed for transferring revenues from central to local governments. However, local governments have not made many advances in terms of how to raise revenues locally or in terms of how to spend resources responsibly. As a result, questions have been raised about the underlying principles of accountability and efficiency in the Latin American fiscal choice model of decentralization.

According to the Urban Institute, a Washington D.C.- based think-tank, a constant feature of decentralization in Latin America has been the scale of the revenue sharing with local authorities and governments. Indeed, in some cases, central government transfers of funds have consistently exceeded the expenditure responsibilities devolved to local governments. As local financial management also increasingly relies on central government transfers to meet local demands, increasing inefficiency regarding both the allocation and the use of resources for local service delivery occurs.

When considering a decentralization model based on fiscal choice, improvements in efficiency and equity often depend on a local government's capacity to administer a variety of taxes and fiscal costs relative to a set of services that are aimed at satisfying local demand. But if local government budgeting relies on central government transfers and not on local revenue collection, the incentives for efficient funds allocation are weak. When looking at the expenditure side of local government finances, however, there is evidence that community participation, and changes in demand, can lead to greater efficiency when linked to local decision-making, local project design, and community project implementation.

Consequently, decentralization in Latin America will not realise its potential if it continues to rely so much on central government transfers to increase local government spending. Without a corresponding transfer of responsibilities, and a proportional effort to raise income locally, a danger exists that governments may try and claw back some of the transfers that have already been agreed upon. Indeed there are now warning signs in both Colombia and Brazil, two of the Latin American countries that have made most progress in decentralization, that complementary strategies are increasingly necessary. In these circumstances, arguments are being made in favor of a strengthening of local financial management as a condition for fiscal decentralization, to ensure that the local allocation and use of resources will satisfy the efficiency and equity criteria for which they were intended.

Is the structure of local government financing viable?

Central governments are claiming that not enough effort is being made at a local level in fiscal matters and that this threatens Latin America's decentralization efforts. Local governments, for their part,

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NEWSLINE

Latin American Urban Agriculture Research Network—Agricultura Urbana Investigaciones LatinoAmerica [AGUILA] and La Paz seminar

The AGUILA network was created in La Paz in April 1995. It was the outcome of a 1994 Latin American seminar on urban agriculture in Bolivia sponsored by AIDE, IDRC, FAO and other entities. The seminar was conceived after an assessment was made of expertise, capacities, partnerships, support and interest in urban agriculture among nearly 50 institutions in nine Latin American countries.

AGUILA is composed of a variety of institutions and organizations, public and private, interested in promoting an economically viable, ecologically sustainable and socially equitable use of urban agriculture. AGUILA views urban agriculture as part of a broader approach to the development of cities that is both more economically viable and socially acceptable. It promotes policies, technologies and methods that improve the productivity, accessibility, and sustainability of urban production systems. Through its activities AGUILA seeks to improve several urban problems such as food security, income generation, sustainable use of resources, and community management.

These objectives will be realized through activities in the areas of information and publications; research into inter-institutional cooperation; training and education; institutional capacity strengthening; policy and strategy development; and interchanges with other related networks. Four working groups have been set up. They deal with popular hydroponics, the production of high value foodstuffs, animal husbandry, and organic solid and liquid waste reuse.

Papers commissioned for the seminar and debated in plenaries were a testimony to the wealth of current local experience in the region. Conclusions reached agreed there were several major stumbling blocks to progress on specific aspects of urban agriculture. For instance:

•Hydroponics should be aimed at communities with a minimum degree of organization, and only introduced once there is proven local commitment to ensure follow-up.

•Market feasibility needs to be stressed, as much as production technology itself.

•The benefits of having complementary production systems as part of community-scale development were also demonstrated. However, the links between urban agriculture and the rest of the urban economy need to be better documented.

•The efficiency and effectiveness of several ongoing public programs need to be evaluated to ensure financial viability beyond initial subsidies. Information training and municipal management are particularly needed to ensure the safe production of food from wastewater treatment plants.

As a follow-up to the April 1995 seminar, in June and July 1995 participants identified several matters to be negotiated over the next months for implementation in 1996-97. These are: research guiding the promotion and management of urban agriculture on communal land; training and pilot programs for commercial hydroponics as a source of income for low-income districts; technical training; information within the region on the treatment and reuse of municipal wastewaters for food production; and Internet-style regional courses on urban agriculture for selected audiences.

AGUILA members elected a Directive Council, composed of an executive secretary, Julio Prudencio, based in La Paz, (fax: 591-2-432-632), and three regional representatives for Central America and the Caribbean (Luis Carvajal, fax: 809-533-1106); the Andes (Albina Ruis, Internet: Albina@alter.org.pe); and the Southern Cone (Patricio Yanez, Internet: Cedal@rdc.cl). The Directive Council meets once a year, or when needed. Meanwhile, advisory institutions plan, evaluate, and monitor AGUILA's network activities.

Julio Prudencio (AGUILA), Luc Mougeot (IDRC), Juan Izquierdo (FAO) and Henk de Zeeu (ETC)

The Philippines: Financing Investment in Urban Infrastructure through Local Government Bonds

by Robert Kehew

Robert Kehew is an employee of PADCO, Inc., and has recently served as Chief-of-Party for the USAID-sponsored Decentralized Shelter and Urban Development Project in the Philippines.

MANILA. On August 6, 1993, an unusual event occurred in Naga City in the Philippines. On that day, citizens lined up to vote in a public referendum, one of the first of its kind ever held in the archipelago. By the time the votes were counted, it was clear that Nagenos had endorsed the construction by the city of a much-needed central bus terminal. What was unusual was not the project itself so much as how these citizens decided to pay for it. Taking advantage of new legislation, city residents endorsed financing the capital improvement through the flotation of local government bonds.

Bond flotation is alternative source of revenue

Most Naga City residents probably didn't realize it, but a successful bond flotation in their city could challenge prevailing notions about how to sustainably finance the work of cities in developing countries. The figure at right shows in a simplified manner the options that local governments around the world currently face when it comes to bankrolling capital investments. As the figure illustrates, these options generally change as countries strengthen their economies, develop their capital markets, and decentralize their governments. Brussels, located somewhere toward the top of the continuum, enjoys different financing options than, say, Bombay down toward the bottom. Two options prevail in developed countries. Richer European cities generally access funds from privately funded municipal credit institutions (MCIs), while American cities seek resources on the open market through floating bonds and other instruments [see top of diagram]. However, many cities in poorer countries try to obtain credit from publicly funded MCIs. Many other local governments in poorer countries finance projects on a case-by-case basis, if they succeed in finding any credit options at all (many only receive grant money).

International donors have helped shape the financial options open to local governments in developing countries. Recognizing the key role that finance plays in providing local services, donors have promoted the use of publicly funded MCIs in middle- to low-income countries. Called "organizational hybrids," these institutions typically attempt to combine the commercial incentives of private lenders with the financial backing of central governments and donors. However, in the search for viable financing alternatives for local governments, some economists are beginning to take a second look at options such as bond flotation. The question remains: How far down the development continuum can one successfully extend debt financing on the open market?

The Philippines offers a test case for a new development paradigm whereby local governments in countries of even lower- to middle-income status can compete for capital on the open market. The Philippines moved toward such a model in 1991 when it passed the Local Government Code (LGC). This groundbreaking legislation devolved major new resources and responsibilities to local governments, including enhanced abilities to float local government bonds. The LGC authorizes local councils to set the terms and conditions of bonds to finance "self-liquidating, income-producing" projects.

Preliminary signs suggest that, with time, local governments in the Philippines can come to rely on bonds as one source of revenue for sustainable development. To date, local governments have only used bonds to fund housing development. Local governments in the Philippines have thus not yet used this instrument for what is arguably its core mission—financing capital improvements related to the provision of basic urban services such as drinking water, sewage and sanitation, energy, and transport.

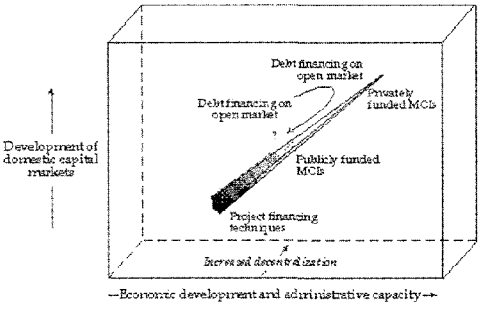
Introduction of "rainbow" bonds for Naga City

Impressed by Naga's successful referendum and seeking to encourage the use of bonds to finance local infrastructure investment, USAID recently organized a team to support bond flotation in Naga City. The group included a financial advisor, a feasibility analyst, and a policy analyst. It succeeded in winning passage by the Naga City Council of the terms and conditions for the bus terminal bonds. Some aspects of the process and the resulting bond features might raise the eyebrows of munibond experts in more developed economies. The range of coupon values planned diverges from common practice—from a maximum of the equivalent of US$40,000 down to a minute US$20 "minibond" targeted for local sale. This wide spectrum of coupon values prompted the city council to dub the issue the "rainbow" bonds.

City counselors also approved a five-year maturity period for the rainbow bonds—more than twice the period for other munibonds issued to date.

The USAID team did identify several constraints to expanding local government bond flotation in the Philippines, including the (apparently) taxable status of interest earned on the investment and the chronic shortage of independent financial advisors who have experience in Makati—Manila's Wall Street—and in the provinces. In a modest way, the Philippine experience does, however, suggest that expanded local government access to capital on the open market merits a place in a paradigm of sustainable development in developing countries.

Options Available to Local Governments for Financing Capital Investments



The diagram shows the changing financing options available to local governments worldwide.

Urban Development and Macroeconomic Reform in Africa: The Financial Link

by Cecilia Mou Charles

Cecilia Mou Charles is regional adviser to the Urban Management Programme in the regional office for Africa in Accra, Ghana.

ACCRA. Throughout Africa, towns and cities are burdened by inappropriate and outdated development policies. Most African cities are also insolvent, with unreliable sources of revenue and a management system that is embedded in a fragile institutional framework. Thus, common problems in urban development are inadequate and insufficient services for the local population; a lack of incentives to attract foreign investment in urban projects; and a reluctance by local investors to participate in local development because of the rising costs of investments, and because they generally have to provide a significant proportion of on- and off-site infrastructure themselves. To reverse this situation, urban development needs to be addressed in the context of current economic reforms.

Most of these economic reforms focus on large issues, such as improving the efficiencies of the marketplace, or rationalizing credit policies, or reducing the budget deficit. But whatever the policies, the way they are implemented will affect the performance of the urban economy. Thus far, the track record throughout Africa has been weak in national economic management, and worse in urban management practice.

Effects on urban finance

One of the most important ways in which the current macroeconomic reforms and urban development are linked is through policies that encourage a reallocation of resources. This applies to both public and private sector capital, as both are important for urban investments. At the urban level, one of the important changes that could be brought about by the economic reforms would be an improvement in the allocation of credit. (For example, the availability of credit is critical for housing, as well as for providing urban infrastructure and services. When interest rate policies change, there tends to be an immediate demand for housing loans; this in turn has an impact on the implementation of housing policies.) Such an improvement in credit allocation may occur as a consequence of reforms in the financial sector or as a result of a reduction in the national budget deficit.

Another important link between economic reforms and urban development is in the provision of infrastructure and related services. Most local governments in Africa are subsidized by central governments, so any advances made in reducing the central government's budget deficit have an impact on local governments. A key issue in this context is deciding how the budget deficits are going to be financed. More often than not, central governments in Africa tend to borrow from their countries' central banks. When this happens, the funds available to commercial banks for lending to local private investors are reduced. On the other hand, when deficits are financed by borrowing abroad, there is a likelihood that national debt servicing will become more onerous.

Local governments must establish priorities

However they do it, when central governments set out to reduce the budget deficit, central-local government relations are profoundly affected. Cuts in municipal spending can alter both the expenditure and revenue side of local budgets. Cities overburdened by a lack of resources, or lacking the autonomy to make their own decisions regarding investments, may be forced to establish new priorities for funding or endure new constraints. The capacity of cities to provide services and infrastructure may also be limited by the fact that central government deficit reductions tend to influence criteria for resource allocations. For example, road maintenance may not be considered as much of a priority as the provision of a sewage system. Aggravating the situation, African cities have no concept of revenue-sharing, so municipalities cannot offset cuts in their budgets by tapping into potential sources of income that will provide the bulk of central government receipts. Hardly surprisingly, many African cities are going through a period of economic belt-tightening, and are unable to maintain facilities or provide adequate services.

Improving municipal finance

Cities have not been able to function well in Africa because their roles have been marginalized for so long. The current economic reforms only make the situation worse. However, in the light of decentralization efforts now underway in Africa, there may be scope for mobilizing support to accelerate the pace of urban reform. Among the most important reforms on the table is the need to grant local governments financial autonomy. If towns became financially autonomous, they would be able to establish their financial independence and borrow directly from local commercial institutions. The availability of long-term loans for financing infrastructure and services would occur as soon as towns had the freedom to function with independence, and central governments would no longer need to be deeply involved in municipal finance. As a consequence, expenses incurred by borrowing to subsidize investments in municipal infrastructure could be reduced.

Giving towns financial autonomy will not only reduce the central government's presence in the marketplace; it will also provide towns with an opportunity to try out new entrepreneurial management techniques that may succeed in increasing productivity in various ways. For example, many large towns and cities have been trying out various public and private sector partnerships, and this trend may well spread in future. In addition, as towns become more independent and accountable, efforts to improve the mobilization of local funds will be strengthened.

If cities are to provide the services needed to sustain agriculture and the rest of the economy, economic reforms must be accompanied by urban policy reforms. Economic management is not only a national concern—it should also be intrinsic to urban organization and management. The success of economic reforms can be measured at the level of urban development. Current structural adjustment programs need to be backed by policies that improve the contribution of cities to national development. UA

Fiscal Decentralization in Colombia: Advantages and Pitfalls

by Eduardo Wiesner

Eduardo Wiesner is the former minister of finance and director of Colombia's National Planning Department. He has also served as executive director of the World Bank and as director of the Western Hemisphere Department of the International Monetary Fund. He teaches economics and writes extensively about public economics and international issues.

BOGOTA. After many years of successful macroeconomic management, Colombia's policymakers have decided that the next challenge to the country's long-term development is a reform of the public sector in local government. To implement such a reform and respond to the challenge, the government has started a process of decentralization in both the political and the fiscal spheres. (Colombia actually started decentralizing in the late 1970s and mid-1980s, but the recent deepening of the reform process is the result of a new constitution passed in 1991 and legislation passed in 1993.) The new policy can bring benefits, but it also poses problems. If it is successful, it could improve the quality of life of most Colombians. If it is a failure, it could jeopardize the country's traditional economic stability and weaken local government.

On the positive side, the reform could increase the efficiency and political advantages of providing local public goods and services and improve the efficiency of spending on social services (e.g., health and education). Against this, risks have cropped up in the area of local tax collection and with respect to certain monopolistic practices in the provision of primary and secondary education.

Opportunities

The advantages of decentralization are well known: in principle, it can make local authorities more accountable to the needs and demands of local inhabitants. Establishing closer links between the authorities and taxpayers can increase economic efficiency and political participation, and more democratic local government and accountability are, in turn, nurtured by fiscal decentralization.

A basic purpose of decentralization is to find efficient ways of allocating resources. Fiscal decentralization and the decentralization of the public sector may therefore be the answer to how to provide local inhabitants with certain public goods in an efficient way when demand and supply are largely determined by local circumstances. Decentralization is thus a search for efficiency in both the provision and financing of local and national public goods; it means striking a balance between the levels of taxation, expenditure, transfers from central government, and regulations imposed on a particular local government.

Most spending on social services in Colombia is done at a local level. And Colombia's new development plan for 1994 to 1998 gives priority to social sector spending and makes decentralization an integral part of this social strategy. If the policy framework for the decentralization is well designed, decentralization can improve effectiveness in spending on social services. Furthermore, if as a result of a well-designed system of central-to-local government transfers, local spending on social services helps relieve the poverty of the poorest members of the population, that alone justifies a decentralization policy.

Challenges and risks

While the theoretical arguments in favor of decentralization are strong, converting them into reality can be very complicated. In Colombia's case, in the light of the model finally adopted, it seems the country's enthusiasm for decentralization exceeded the realities of putting it into practice. It is noteworthy that the original policy expressed in the 1990-94 development plan, *La Revolucion Pacifica,* was well conceived and consistent. However, for reasons of political economy, this policy framework was distorted by restrictions and became a highly questionable constitutional and legal mandate when implemented.

Specifically, two problems exist in connection with Colombia's decentralization policies. First, national transfers from central to local governments are structured to meet revenue targets. Second, decentralization in the area of spending on social services has not led to competition—for example, in the provision of primary and secondary education. Rather, it is reinforcing monopolistic practices.

Sequencing crucial for success

The proper sequencing of fiscal decentralization is a key condition for its success. It is important to try and ensure that revenue transfers from the central government do not exceed or outpace the expenditure responsibilities at a local level. The right sequence is to start with the *functions* that are to be transferred, and with the local government's institutional capacity to absorb them, not with the *revenues* that are to be transferred. Colombia's policy framework, however, does not follow this sequencing. Revenue transfers, rather than being decided by the process, are mandated as a target to be met. One of the most expensive consequences of this approach is that local governments are guaranteed revenues almost unconditionally. As a result, local governments tend to make little effort to tax their constituency, especially when the local jurisdiction is small or medium-sized.

Not everything is a source of concern in Colombia's decentralization drive. Now that mayors are elected and more accountable to their citizens, some big cities are setting an example in fiscal reform. During the last few years, in Bogota, Baranquilla, and Medellín, mayors have been able to convince their electorate to pay more in local taxes, and local tax income has increased. In these cases, transfers of funds from the central government do not seem to have discouraged local fiscal efforts. It is a development that is most encouraging.

Colombia's National Transfers as a Percentage of Current Revenues

	1990 %	1995 %	2002 %
Main National	12.2	16.0	22.0
Transfers	13.8	23.5	24.0
Total	**26.0**	**39.5**	**46.0**

Source: Eduardo Wiesner, La Decentralization, el Gesto Social y la Gobernabilidad en Colombia, *forthcoming publication by the Colombian National Planning Department.*

Bombay: Institutional Governance and Urban Finance

by Nasser Munjee

Nasser Munjee is executive director of the Housing Development Finance Corporation in Bombay, India.

BOMBAY. A casual visitor to Bangkok, Manila, Jakarta, or Bombay cannot fail to notice the impact of unbridled growth on city infrastructure, which is manifested most visibly by traffic congestion, insufficient drainage, inadequate health and education facilities, and water shortages. Worse still, with higher rates of economic growth fueled by economic reform, cities are likely to face many pressures for expansion, all of which make major demands on city infrastructure. Therefore, if insufficient attention is paid to city planning and urban development, stimulating economic growth by means of economic liberalization measures may have only short-term advantages.

Financing infrastructure

Investments in infrastructure by local governments have been woefully insufficient to meet the growth of developing city economies. Much of this deficiency reflects the dearth of financial arrangements that exist for investments in the renewal and expansion of infrastructure. How to finance urban development is therefore a key issue. With economic liberalization proceeding rapidly, the decentralization of powers to local authorities for the provision of infrastructure has not been met by a similar devolution regarding revenue-raising powers.

The reluctance of central governments to grant local government authorities access to established sources of funds often stems from a fear that too many resources may be accessed at the central government level by local authorities. Central government fears that this could affect its budgeting process and make economic management more complex.

In the World Bank's 1994 Development Report, *Infrastructure for Development,* it is emphasized that there is a need for increased efficiency in infrastructure delivery that responds to effective demand and simultaneously addresses the issues of poverty alleviation and environmental sustainability. Most developing countries have suffered from a supply-driven economic orientation, undertaken by bureaucracies, rather than emphasizing service delivery and the development of industry. This lack of commercial sense has often led to a situation where objectives are confused, customer satisfaction is ignored, and the quality and quantity of services provided are determined by the supplier. The report (not surprisingly) recommends a different type of commercialization using competitive suppliers. This should create a situation where consumers have a direct impact on the type, quality, and quantity of services to be provided; and where the private sector competes for or joins as a partner in the process of delivery.

Whatever one may say about the theoretical issues of commercialization and competition, in the final analysis, the institutional setting will be the critical factor in terms of increasing efficiency. Thus, the future of our cities depends on making institutions efficient. But how is this to be achieved?

While the issues posed by the relationship of urban governance and urban finance for institutional structuring are profound and complex, a second major factor connected with macroeconomic adjustment will perhaps be the major force for change. This factor is the fairly rapid dismemberment of the state-directed credit system in developing countries.

The dismantling of the directed credit system

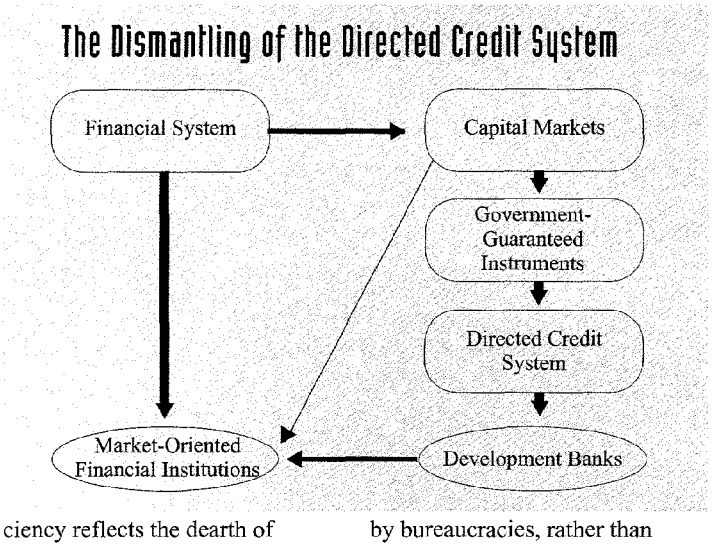
In a state-directed credit system, major development banks and financial institutions—including parastatals involved in housing and urban finance—have functioned in a protected environment, with government-guaranteed funding channeled through the directed credit system constituting a major resource base. Liberalization and the demise of a planned economic system imply the end of this directed flow of credit. This could well lead to crisis in institutions that have for decades depended on the system.

Problems arise for institutions that have been dependent on state finance. They are being forced to move to the left in the diagram and re-establish their "connectedness" to the overall financial environment with only one parameter finally determining whether they succeed or fail: performance. The economics and the technology of the changes are also gradually undermining the advantages of specialist knowledge and capability. Institutions can no longer anchor themselves to particular markets, but have to redefine their comparative advantages in a more holistic manner. Customers are also more fickle and may pick and choose in an open market. So how will the transition be managed?

Bombay First

Bombay has begun an initiative to create a nongovernment institution to focus attention on city issues. "Bombay First," as it is called, will create a core competency to assess the strategic needs of the city. Bombay First, it is hoped, will become a magnet for many interested groups and create a constituency for change. If the experiment is a success, many other cities may follow suit, thus bringing about a major drive for urban development and city planning throughout India.

The question of how to govern is truly a study in political economy: a study of the political forces present and the formal and informal mechanisms at play in re-engineering institutional processes that presently have a major impact on the urban economy. Ultimately, the efficiency of the city will increasingly determine the prosperity of the nation and the individuals within it.



FEATURED COLUMNIST

Financing Decentralized Government: Indonesia, Hungary, and China—A Status Report

by Nick Devas

Nick Devas is senior lecturer at the School of Public Policy at the University of Birmingham, England, and has most recently been a contributor to A. Coulson (ed.) Local Government in Eastern Europe: Establishing Democracy at the Grassroots, *published by Edward Elgar, Aldershot.*

BIRMINGHAM. Decentralization is high on the political agenda in many developing countries. Problems arise, though, because local government revenue sources are often inadequate. At the same time, central governments face increasing pressures on their national budgets, obliging them to economize on transfers to local governments. In this article, I look at the case of Indonesia, and contrast it with the cases of Hungary and China where—despite very different contexts—there are many parallels.

Indonesia

Local governments in Indonesia receive around three-quarters of their budgets from central government. Local taxes contribute less than 10 percent of local budgets on average, and there is a constant search for new local revenue sources. This search has been given added impetus by the government-sponsored Integrated Urban Infrastructure Development Programme that gives Indonesian cities a greater role in planning and financing their urban infrastructure.

The only substantial local tax source is that on motor vehicles, which belongs to the province level. In addition, there is a property tax, *Pajak Bumi dan Bangunan*, which is technically a national tax but the revenue is distributed to local government mainly according to origin. Reforms to the property tax during the 1980s have increased the yields substantially, but it still contributes only a relatively small fraction of local expenditure needs (around 7 percent).

There is, of course, plenty of room for improving the collection of local revenues and for better cost recovery from beneficiaries on projects such as water supplies through improved pricing policies.

So what can be done? Apart from increasing the effective rate of the property tax, three other avenues could be considered. First, implement some sort of tax or license on businesses. The second is some form of local tax or charge on land development. This would be levied mainly in the larger urban areas, but could generate substantial resources from landowners and developers to finance the essential infrastructure to cope with urban growth. The third possibility is to generate more from automobile taxation, both by increasing tax rates on vehicles and by introducing a local tax on motor fuel.

The other element of the jigsaw is the grant system. Three-quarters of local expenditure comes from grants, but this is fragmented into a large number of components. These grants have evolved over time, each one having its own allocation criteria. These issues are coming into focus with a new government initiative to hand over some of the line responsibilities of central ministries to local governments in some areas. This may be seen as the beginning of a necessary process of simplifying and clarifying responsibilities for particular functions. But it also necessitates a clearer system of funding that matches responsibilities with financial resources, and a grant system that takes due account of relative expenditure needs and local revenue capacities in each region.

Hungary

In contrast to Indonesia, the demand for local autonomy in Hungary sprang from the grassroots as part of the post-Communist reform process. As a result, the 1990 Law on Local Governments recognized a large number of local governments and gave them a high degree of local autonomy. But this decentralization was not matched by local revenue sources. Currently, local taxes generate only 2 to 3 percent of local government budgets. The main local taxes are a property tax or a communal tax on residential buildings, a tax on businesses based on the number of employees, and a tax on businesses based on turnover. The last of these accounts for 70 percent of aggregate local tax revenue.

As in Indonesia, it is often suggested that local governments should become more self-sufficient. There certainly is some scope within the existing laws to increase local tax revenues, but a significant increase could only come by the adoption of a value-based system of property taxation. This is already permitted by law but has not been widely adopted because of the undeveloped nature of property valuation in Hungary. However, newly elected mayors and local assemblies have been understandably reluctant to increase local taxes.

China

The pattern of decentralization in China has occurred largely as a byproduct of the economic reform process started in the early 1980s. The failures of the centrally planned system and the ensuing marketization of the economy transferred many responsibilities to the managers of enterprises, and thereby to the local governments that owned them.

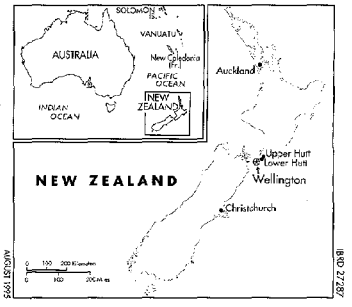
Paradoxically in such a centralized state, economic management has become quite decentralized in practice. Even though local governments cannot levy significant taxes of their own, they seem to have considerable scope in administering national taxes locally, in ways that benefit their local enterprises and hence their own budgets.

The tax system, both national and local, has undergone a series of reforms over the last 15 years, aimed mainly at making the economy more efficient. At the same time, there have been many changes in the revenue-sharing arrangements between levels of government. One consequence of the changes has been that an increasing proportion of local resources have taken the form of "extra-budgetary" revenues, from which it is more difficult for central government to obtain a share. This has squeezed the resources available to central government, resulting in serious budgetary deficits. Consequently, the central government has started to centralize certain taxing functions.

Another consequence of the decentralization process is that rich regions have benefited disproportionately from economic liberalization. But in an increasingly fragmented situation, it becomes difficult to devise a system of resource transfers between levels of government to restore inter-regional equity, or even to know accurately the relative financial position of each local government.

UA

New Zealand: Reforming Municipal Financial Management



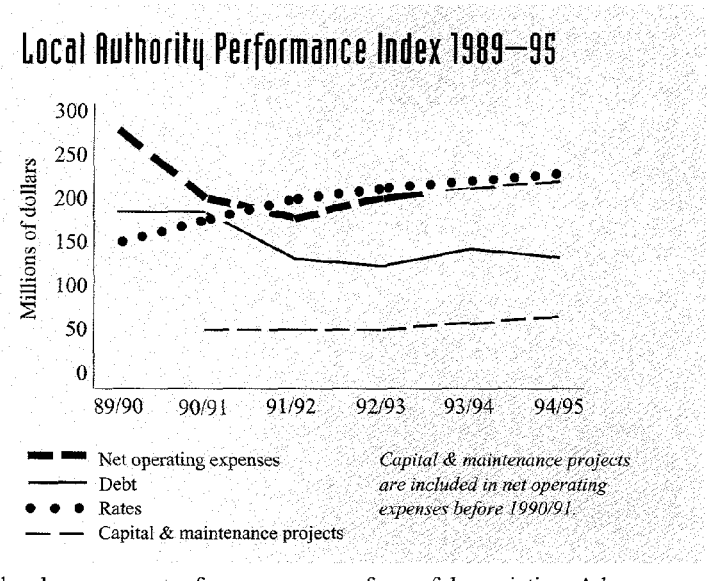
By R.J. Vine

Bob Vine is executive director of Interlog (New Zealand) Limited, a consulting group that provides information and advisory services on New Zealand local government principles. Mr. Vine was chief executive of the Upper Hutt City Council (1976-85) and the Lower Hutt City Council (1985-89), and following reorganization became chief executive of the Hutt City Council until retiring in 1993.

LOWER HUTT. Over the last decade, New Zealand has been a laboratory for radical economic and public management reforms that are presently being admired worldwide, and that are under active consideration in countries where reinventing government is a priority.

In 1984, the New Zealand government deregulated financial markets, slashed import tariffs, and began to reshape the way the public sector was managed.

The national government believed local government was also in urgent need of reform, and much the same principles that had been used since 1984 in the rest of the economy began to be used in local government. The three underlying principles to these local government reforms are: accountability, transparency, and contestability.



Change in local government accounting methods

Changes in the area of city, district, and regional council financial management required the introduction of accrual-based accounting as opposed to cash accounting. Accrual-based accounting measures the full cost of producing goods and services, and accurately accounts for assets and liabilities regardless of timing issues. It leaves no room for the kind of creative accounting used in the past by local governments, which made their results look more impressive on their balance sheets.

Accrual accounting methods

In terms of local government, accrual accounting means that infrastructure assets are valued with provision made for some form of depreciation. A key benefit of the valuation process is the identification of the assets: most councils in New Zealand had very little knowledge of the standard of their utilities' infrastructure, and this ignorance has been largely overcome as a result of the accrual-based accounting system.

With the new financial reforms, most New Zealand local authorities now have, or are devising, long-term plans to satisfy the infrastructure needs of their communities.

Increase in allocation of resources for urban investments

As a result of the new system, many local governments are now able to allocate more resources for capital investments from revenue surpluses that are planned, and so reduce their borrowing requirements. This is sound financial management, and it gives local authorities the choice to decide which projects to fund with credit after considering criteria such as intergenerational benefits.

Meanwhile, the New Zealand parliament is considering introducing new legislation that will encourage local authorities to link expenditure to where the benefit lies: the exacerbator (e.g., the extent to which individuals or groups contribute to the need for the expenditure) and the time at which the benefits are received (e.g., the intergenerational argument).

Performance targets required for local governments

In addition to requiring a customer-driven focus with a new and more rigid system of accounting, New Zealand's local government reforms are uncompromising in their requirements for work and output based on performance.

Forward thinking, combined with a need for local authorities and their communities to address the question, "What business should we be in?" has resulted in a release of funds for core business—for instance, for infrastructure. By dismantling local government ownership of services using the principle of contestability, it has been possible for local governments to reduce debt and reinvest funds. The funds have been obtained by selling off activities that are better carried out by the private sector. Following the reforms, divestments have included the sale of electricity and gas distribution, public passenger transport operations, infrastructure construction and maintenance operations, and port operations.

Thus, New Zealand local governments have eliminated operating deficits by making financial management more focused; reduced debt levels by selling non-core business activities; reduced property tax increases in line with the nation's reduced level of inflation; and have been able to maintain capital expenditure levels and infrastructural assets at a reduced cost, under a contestable system.

Improved financial management has been an essential ingredient in the restructuring of the national economy in New Zealand. Local government is accordingly far better placed to meet the infrastructure demands of developing cities and regions in the long term. Furthermore, stakeholders have a much better idea of the health of their city and its finances now that accountability, transparency, and contestability are guiding principles. UA

Urban Cadastres: The Paraguayan Experience in Small and Medium-sized Municipalities

by Roberto Salinas

Roberto Salinas is an expert in urban and community development working for Deutsche Gesellschaft fur Technische Zusammenarbeit (GTZ). He is currently the coordinator of the IDM-GTZ Development Project in Paraguay.

ASCUNSION. A distinctive feature of Paraguay's municipal governments is that they are self-financing and receive almost no transfers from the state: income is generated almost exclusively from taxes and local contributions, and only to a small degree by public sector credits. This financial independence makes it expedient for municipalities to find ways to increase revenue collection in the community, as well as ways of reinvesting such revenues so that community needs are met.

Debate about decentralization initiatives

Following the establishment of a new national constitution in 1992 and the subsequent emergence of various decentralization initiatives, a debate was started about the adequacy of local government budgets, both at a department (regional) and a municipal level, and about the balance between the responsibilities transferred by the central government. Issues such as the degree of preparedness and qualifications of local government personnel, and whether local resources were sufficient for such responsibilities, were also raised.

At this time the central government introduced another change: all the real estate taxes levied by local governments were to be kept by them and not transferred to the central government. So, property taxes became an important part of municipal income.

However, an early difficulty encountered by municipalities in implementing the new reform was a lack of up-to-date information on both urban and rural cadastres (property censuses). Often, municipalities were simply not aware of what property or land fell within their jurisdiction.

The main features of the new cadastre

To overcome these problems, municipalities developed an all-purpose cadastre based on simple, clear criteria and information. All that is required is a chart with an index, which is based on national maps and divides an urban area into blocks and includes data on property owners. A card containing basic information on each property can then be attached to each block. The drafting of the index charts generally needs to be done by professional land surveyors. However, the sketches of the blocks, the location of the building, and their approximate measurements and data can be done by municipal personnel.

With this new system, it should be possible to find out how urban land is really being used and to start planning how property taxes should be devised and implemented. The system is meant to be all-purpose in the sense that it will help shape urban administrative, fiscal, and planning decisions.

Cadastre system encourages transparency

The system, designed for small and medium-sized municipalities, cross references owners and properties. The cadastre system in Paraguayan municipalities that has been introduced works with computers. This ensures that data are collected in a speedy and reliable way. In addition, the transparency of the system is guaranteed. Making tax collection an impersonal function is something that the vast majority of Paraguayans now expect. The days when people were excused from paying taxes as a political favor are now considered over.

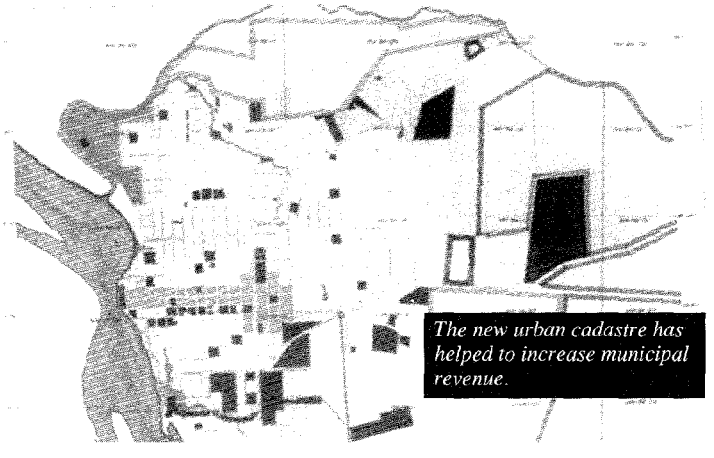
Implementing a cadastre: its effects on municipal finances

In many municipalities, the mere fact that enquiries into property ownership were started was an incentive to many owners to bring their property taxes up to date. As a result, municipalities became aware of the full extent of the properties in their area, and of the owners, so tax collection could begin. Specific taxes were also introduced for instance, on urban land that was lying idle, on offices, on land that was divided between owners, and to maintain sidewalks and pay for garbage collection. As a result of these changes, tax revenues are increasing.

Tax collection in municipalities that use cadastres now constitutes an important source of municipal income. Such revenue in some cases represents 15 percent of the total municipal budget.

A great deal still has to be done. The information obtained in the cadastre is now being used to develop other areas of urban planning. Experience has shown that there is no need to have completed the property census or cadastre before starting this work. The two endeavors—compiling the property census, and compiling data for other areas of urban planning—can be done simultaneously. The system is proving so successful that even small municipalities now want to have a cadastre because of the simplicity of the system and its usefulness.

Any type of urban planning that is aimed at regulating land use, or that involves planning investments, should be based on cadastre information, and this information ought to be integrated in municipal management. By means of such a cadastre system it is possible for municipal governments to draw up realistic investment budgets based on accurate estimates of income from property and related taxes. Finally, a *sine qua non* of such cadastres is that although municipalities may differ between countries, the design of the system everywhere must have one thing in common: it must guarantee that the cadastres will be used in a fair and objective way.



The new urban cadastre has helped to increase municipal revenue.

Washington, D.C.: Federal Control Reasserted through Creation of the Financial Control Board

4 *by Jonathan Foreman*

Jonathan Foreman is a lawyer and freelance writer living in New York City.

WASHINGTON, D.C. In most countries, urban finances tend to be artificially boosted by national government contributions. This is particularly true of capital cities. Sometimes it is a question of image: governments are keen to give visitors a favorable impression. Elsewhere, it may be a matter of security. In famine-plagued Ethiopia, food aid was reportedly diverted away from its intended beneficiaries in the countryside, and used instead to keep food prices down in Addis Abbaba, the country's capital, allegedly to reduce urban discontent.

Decline in the quality of urban life

But in the United States, the reverse is happening. There has been a gradual shift in the population and in electoral power away from cities. And this has been accompanied by declining federal government transfer payments and by a decline in the quality of American urban life: taxes are high, services are bad, and infrastructure is in a state of disrepair. Much to the federal government's embarrassment, Washington, D.C., is a particularly bad case.

Washington, D.C., has one of the highest murder rates of any American city. Some of its schools have the reputation of being among the most run-down in the country. And earlier this year, even before a federal financial control board was created to oversee and supervise the city government, the virtual collapse of Washington's city services forced the federal government to intervene in the city's management. Public housing was apparently so badly managed that the courts appointed a receiver to administer it. A federal judge was appointed to take over the city's foster care services. And conditions in the city's jails were considered so bad that the federal government is now managing these as well.

Declining tax base

Washington's problems are similar to those of Chicago and Boston. The first problem is that city tax bases are declining. American cities generally finance themselves with local tax revenues and bond issues. But during the last 30 years, their tax bases have declined as more and more inhabitants have moved to the suburbs. Many of the new suburbs that have developed lie outside the political and fiscal jurisdiction of the cities where their inhabitants are employed. Under state laws, municipal governments can sometimes annex incorporated suburbs, and claw back money from wealthy taxpayers. But some cities, such as New York and Philadelphia, both of which are bordered on one side by the state of New Jersey, can do nothing about the flight of wealthier citizens into a lower tax commuter belt in a neighboring state. Washington, D.C., is in the worst position of all, because all of its suburbs lie outside the city's reach in Virginia and Maryland.

A second problem appears to be the increased unionization of municipal workers that has accompanied the expansion in urban welfare programs after the 1950s. In a style that some say is reminiscent of New York's notorious Tammany Hall tactics in the last century, jobs have allegedly been allocated in D.C. along ethnic lines in a bid to cultivate loyal voters. Sustaining such a group of voters in the face of, first, the departure of wealthy taxpayers to the suburbs and, then, an exodus of middle-class taxpayers, has—according to this argument—led big city governments to postpone the business of maintaining urban infrastructure and increased their borrowing requirements. It was this type of mismanagement that allegedly caused New York's financial collapse in 1973.

Washington's turn came this year, when re-elected mayor Marion Barry announced a projected US$722 million budget shortfall. Unlike New York, D.C. has always been supported by the federal government and has almost no experience in self-government. Indeed, from 1874 to 1972 it was run by three commissioners appointed by the President. This was followed by years of partial autonomy. The district was run by a mayor and a council, who presented Congress with a budget. However, the citizens of the district remained largely disenfranchised in national political terms, and even now their only voice in Congress is a nonvoting representative.

Creation of the financial control board

Each year the budget expanded until it resembled that of a small nation, but Congress tended to give Barry and other mayors what they requested. This situation no longer applies. In spring 1995, Congress created a financial control board to take over many of the functions of D.C.'s municipal government. The board holds in trust all funds from the annual federal payment, as well as all funds borrowed from the United States Treasury, and allocates them as it sees fit. It will remain in power until city officials succeed in balancing the budget for four consecutive years. The board also has the power to review major labor contracts with the city and all city legislation.

The chairman of the financial control board is Arthur F. Brimmer, the first black to have served as governor on the Federal Reserve Board, America's central banking and monetary authority. Like the Federal Reserve, the financial control board is a professional institution that is deliberately non-partisan in the interests of financial stability.

Control board will create fiscal discipline

The board offers Washington some hope of competent, responsible financial policymaking. However, opposition to the board remains high among the city's residents. Even those who are weary of the poor services and inadequate schools resent the re-imposition of federal authority. Suspecting, as they apparently do, that congressional Republicans and Southern Democrats have long resisted giving Washington the representatives and senators that could more closely represent the interests of the city's inhabitants, the board looks to them like another ploy aimed at depriving them of a political voice. The fact that the board has so far refused to consider a tax on commuters, who enjoy the city's benefits without paying for them, only fuels these suspicions. So, while the board may bring D.C.'s financial crisis under control, it remains an open question whether it will win the hearts and minds of D.C.'s residents. UA

ROUNDTABLE

In the "Roundtable," we present several questions to prominent people on the topic being discussed in each issue. The purpose is to create a forum for interchange and debate among people with opposing points of view. Our hope is that readers will find it a starting point for generating their own discussions, both within their cities and in response to The Urban Age.

Marlene Fernandes is an architect and urban planner. She is currently technical assistant to the executive director of the Brazilian Institute of Municipal Administration (IBAM), and is coordinator of the Mega Cities Project in Rio de Janiero. Ms. Fernandes is also the coordinator of the Habitat II regional seminar on urban financial strategies for Latin America and the Caribbean.

Roy Bahl is professor of economics and director of the Policy Research Center at Georgia State University. His book with Johannes Linn,* Urban Public Finance in Developing Countries, *is one of the few comprehensive analyses of this subject. Recently, Professor Bahl has been working on fiscal decentralization in Russia and China.

UA: ***Urban finance involves the provision of important goods and services; improvements in the provision and funding of these activities require what kind of changes in the political incentive structure?***

FERNANDES: The improvement in the provision and funding for housing, infrastructure, and urban services requires government incentives that reduce risks, increase competitiveness and enable markets, formal and informal, to work. Some of these incentives are: keeping a stable regulatory framework, such as tariff structures to sustain long term capital investment recovery; providing subsidies to supply those who cannot afford to pay full service costs; and using bidding or contracting-out procedures that reward the suppliers' competitiveness, productivity, and efficiency.

BAHL: Local government officials must be accountable to those who consume urban services if the efficiency of delivering these services is to improve. This requires that local councils be popularly elected and that local chief officers be appointed by these councils. It is also important that budgets be formulated by local councils so that citizen preference for various government services can be reflected.

UA: ***What kind of intergovernmental revenue arrangements should accompany fiscal decentralization?***

FERNANDES: It is necessary to adopt a fiscal structure that would reduce the need for intergovernmental transfers, giving each level of government the autonomy to collect and allocate the fiscal resources necessary to exercise their specific functions.

Ideally, intergovernmental transfers should be used only as a compensatory mechanism between regions, municipalities, or cities with different economic capacities. Part of the transfers could be used to stimulate local governments to improve their fiscal capacity and increase their revenues.

BAHL: Three characteristics of the intergovernmental fiscal system must hold if true decentralization is to be achieved. First, there must be some assignment of revenues and rate-setting power to the local government; the sharing of central government taxes on a derivation basis is not decentralization. Second, grants must be distributed in a transparent way so that local governments can plan their fiscal affairs with a reasonable degree of certainty. Third, there must be correspondence between the expenditure responsibility and the fiscal resources that are assigned to local governments.

UA: ***What risks do intergovernmental financing arrangements create for national macroeconomic management?***

FERNANDES: Subnational governments may force upwards interest rates in the financial markets. They may also increase living costs, affecting inflation through their pricing policies that could increase public deficit and external debt - risks usually associated with national governments.

BAHL: If the intergovernmental system assigns significant taxing and spending powers to local governments, the ability of the central government to use fiscal measures in its macroeconomic stabilization program will be limited. As fiscal decentralization shifts the determination of investment priorities to local governments, higher income local governments will have a greater taxing capacity. On the other hand, decentralization should lead to a greater willingness to pay for services and therefore to an increase in the rate of revenue mobilization.

UA: ***How does one encourage cities to become creditworthy while giving them a reasonable but binding constraint to encourage efficient use of revenue sources and service provision?***

FERNANDES: There are three ways to do this. First, by adopting criteria to distribute fiscal resources that would reward efficiency and effectiveness of service provision. Second, by reinforcing local social controls to improve accountability, efficiency, and transparency in the use of resources. Third, by adopting enabling strategies such as capacity-building and institutional development, to improve planning, budgeting and management activities.

BAHL: Local governments will never have an incentive to be creditworthy unless they have some autonomy in determining their budgets, real access to credit financing and a hard budget constraint that limits their liability to run up deficits. A key to encouraging strong and responsive local government is to allow the imposition of a wide range of user charges, limited only by the acceptance of these by local voters. There is no inherent inconsistency between fiscal responsibility and budget constraints; legal limits on borrowing and tax rates can still leave room for discretionary fiscal actions and for budget planning to meet local demands.

The Urban Activation Plan: Tijuana's Betterment Levy

By Hector Osuna Jaime

Hector Osuna Jaime was elected president of the municipality of Tijuana for the first time in December 1992 as a member of the Partido Accion Nacional (P.A.N.). *He is a former elected state assemblyman for the Eleventh District of Tijuana in the Baja California State Legislature.*

The municipality of Tijuana has above average annual population growth of 4.2 percent, (reflecting the high rate of migration by Mexican nationals from the center and south of the country), and the urban perimeter is spreading by an average of two hectares per day, which has resulted in increasing pressure on local government and infrastructure and led to gaps in urban services.

There is no doubt then that urban conditions in the municipality of Tijuana have been a serious limitation to the city's growth, and that Tijuana's infrastructure needs have exceeded its long term investment capability. The budgets available from all three levels of government in Tijuana have not been sufficient to alleviate or reduce the municipality's gaps in urban services. And for the long term, Tijuana's finances will not be solved by the public sector.

So, in 1994, in order to address this situation, the municipality of Tijuana developed an urban development plan known as the Urban Activation Plan. It is an urban infrastructure macroproject that aims to lay the foundations for the integrated development of the municipality. Based on a series of priority public works, the plan is having a significant impact on Tijuana's economic growth and general standard of living. It is the largest investment project ever proposed by a municipal government in Baja California.

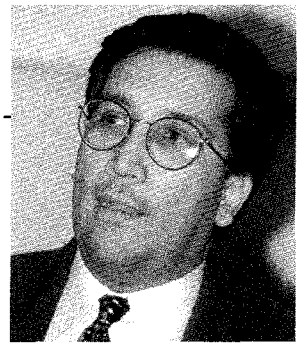
One of the responsibilities of local governments is to work for the steady improvement in the quality of life in their communities so in addition to the urban transformation it will bring about, the plan is also a social and political project that will give the municipality greater autonomy and create improved mechanisms for community participation.

Although the Urban Development Act of the State of Baja California allows governments to carry out civil works on their own, it was decided to put the Activation Plan up for public debate, consultation, and approval; a principle of the plan is that participation of society is essential if adequate private and public resources are to be raised to finance urban civil works, and that consultation with the public should be a permanent tool of the municipality.

The plan calls for a total investment of MexN$500 million, with the central government providing 25 percent, the "productive" sector (industry, commerce, tourism, and transport) 15 percent, direct beneficiaries 20 percent, and the community at large the remaining 40 percent. The *Consulta Publica* or referendum which took place in March 1994 was held to decide whether the plan should proceed and whether the community would pay its share to support the plan; it was passed by a 66 percent vote.

The plan will create additional revenue for Tijuana. Additional tax revenues are estimated at MexN$100 million; the value added tax should also generate MexN$50 million. For the municipal government the plan offers an opportunity to participate in solving real problems for the inhabitants of Tijuana. For the community, it means an opportunity to achieve a better quality of life through participation in municipal decision-making and responsibility for putting the plan into effect.

An Interview with Hector Osuna Jaime, President of the Municipality of Tijuana



UA: What event occurred that persuaded you to raise a betterment levy?

Osuna Jaime: There was no one specific event. The circumstances of the Mexican political system are such that the municipal government of Tijuana has very limited possibilities to build new infrastructure even though there is access to financing programs. So, the alternative was to turn to the citizens of Tijuana and ask them to pay a special one time tax, in this case a betterment levy, where the beneficiaries help fund part of the cost of the plan.

UA: Can you explain how the betterment levy works and how successful it has been?

Osuna Jaime: It is a very simple scheme. You fund your infrastructure project, in this case the Urban Activation Project, with the lowest interest rate credit that you can find and assess the cost to the beneficiary. For instance, 40 percent is covered by the community at large, 20 percent by direct beneficiaries, 15 percent by the industrial/commercial sector and 25 percent by the municipal government. In the case of specific sub-projects like building roadways, where the general impact of public works schemes benefits everybody, we tax people based on the square meters of their property and proximity to the road.

UA: Was the raising of the betterment levy a unique or unusual taxation device for the municipality of Tijuana?

Osuna Jaime: It definitely was. For the first time in Tijuana we managed to organize a more democratic, community participation in keeping with the principles of the Urban Activation Plan. In March 1994, we organized a four day referendum or *Consulta Publica* on the plan and it was passed by a 66 percent vote.

UA: What other interesting taxation devices have been used recently in Tijuana?

Osuna Jaime: This is not exactly a tax but we have a citizen participation program we call *Manos a la Obra* or Hands-on Work where we subsidize 40 to 60 percent of the cost to pave residential streets with concrete. The communities pay for the rest and either hire a contractor or do the work themselves. This has resulted in 800,000 square meters of paving this year alone through this mix of resources. The streets were built much more inexpensively than if they were paid for by the government and this initiative has created a great sense of community pride. UA

We actively seek our developing country readers' input for this section. Our intention is to facilitate networking among developing country city managers and their constituents.

INSTITUTE OF SMALL ENTERPRISES & DEVELOPMENT

Contact: Dr. P.M. Matew, Director, ISED, Vennala, Cohin 682 028, India; Tel: 347884, fax: 345163.

The Institute of Small Enterprises and Development promotes the development of small and medium-sized enterprises through research, training, and consulting services. Development of urban microenterprises is a priority for the institute, which regularly organizes entrepreneurship development programs for micro-enterpreneurs and carries out studies on urban microenterprise development. The findings of these studies have been translated into training and consulting activities. The director of the institute received the Asian Productivity Award in 1994, given by the Asian Productivity Organization of Tokyo.

USC'S SCHOOL OF URBAN AND REGIONAL PLANNING

Contact: University of Southern California, School of Urban and Regional Planning, 351 Von KleinSmid Center, Los Angeles, CA 90089, USA. Tel: 213-740-2264; Fax: 213-740-1160.

The University of Southern California's School of Urban and Regional Planning announces a new degree, the Master of Planning and Development Studies, designed for those who expect to succeed in the new global environment. Whether located in a small city in rural America or an urban metropolis in a nation on the other side of the world, planners and developers today work in an international arena. Accordingly, this program will be offered in a variety of venues, including Los Angeles, Washington, D.C., Hong Kong, and Australia.

The Master of Planning and Development Studies is designed to educate mid-career professionals who are ready to be 21st century leaders. The curriculum includes core courses covering urban planning analysis, research and analytical methods, as well as methods and problems of the planning and development process.

THE CITIES NETWORK

Contact: Michel Ligthart, bothends@gn.apc.org@INTERNET

The Cities Network is a network of grassroots organizations formed to support and stimulate efforts to achieve the creation of sustainable urban environments. In working toward this end, the network recognizes the need to understand the diverse and complex set of social, ecological, political, and economic relations promoting or impeding this goal. In seeking to improve the urban situation, the network stresses the importance of local solutions to specific challenges.

The aims of the Cities Network include the facilitation of the flow of information and the sharing of experiences between diverse urban-based grassroots-oriented organizations working in the field of social and ecological transformation, as well as building alliances and cooperation between these organizations. The network also seeks to organize city or regional and global workshops facilitating communication on common agendas, strategies, and the implementation of programs.

The network is worldwide, with partners in Africa, Asia, North and South America, and Europe.

WORLD BANK UPDATE

Better Urban Services: Finding the Right Incentives

The International Bank for Reconstruction and Development/ The World Bank, 1818 H Street, NW, Washington, DC, 20433, USA. First Printing July 1995. ISBN 0-8213 3232-5.

One of the reasons the World Bank decided to revise and publish this book (it was originally an internal sector review) was to stimulate debate on a key issue in urban reform policy—namely, the growing decentralization of responsibilities and resources between central and local, or municipal, governments. Just how significant a phenomenon this has become at the end of the 1990s is demonstrated, the book says, by the fact that out of 75 developing and former Eastern European Communist countries with populations exceeding 5 million, all but 12 have started some sort of devolution of power to local governments.

The development is too big for multilateral and bilateral institutions, or the countries they lend to, to ignore. Moreover, decentralization does not just have implications for programs in developing countries that aim to improve key urban services such as clean water, sanitation, waste collection, and transport. It also impinges on other vital public services such as primary education, health, and environmental protection, which in turn affect programs to reduce poverty and to stop environmental degradation—both pressing issues in urban areas.

Indeed, another reason why the trend toward decentralization is currently so crucial is because it is taking place against a background of massive migration from rural areas to towns and rapid urbanization in most developing countries. The United Nations predicts that by 2020 more than half of the population of the developing world will be living in towns.

In one respect this urban tide indicates success: despite the deepening pockets of urban poverty practically everywhere, the incomes of town dwellers are higher than those of rural dwellers. Equally, worldwide growth rates in manufacturing and services—both urban-based economic activities—have also been consistently higher than growth rates in agriculture for the last decade.

But the downside is that the quality of basic services in most towns is poor. In developing countries the deficiencies have particularly dire effects as failures in urban service delivery disproportionately affect the poor. In the absence of piped water systems, for example, households invariably have to purchase water from vendors, paying several times more than the cost of the piped water system.

Key urban services such as clean water, waste collection, sanitation, and transport will have to be expanded very rapidly in future if urban environmental problems in developing countries are to be tackled, or controlled at all. This expansion, however, will depend on urban institutions functioning well.

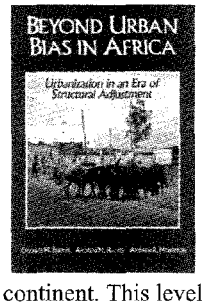
But this, in turn, will depend on a change of emphasis in urban institutional reform programs, the authors say. Traditional institutional reforms at this level focused on providing technical assistance and on efforts to improve the internal administration of local government. However, the book says, urban service delivery questions now need to be viewed from a broader perspective that takes the structure of the entire public sector into account, and especially central-local government relations. For instance, it is important to find out what the constraints are that local governments face when trying to deliver services, and what incentives are inappropriate, as both are obstacles to efficient local service delivery and often reflect problems in central-local government relations.

In these circumstances, the book says, three elements are crucial to reforms. First, the functional responsibilities of different levels of government must be clearly defined so that consumers, private contractors, and the public in general can identify a particular urban service with a particular government office. Related to this, the sources of revenue that correspond to the functional responsibilities of services also need to be made explicit. And in this context, one improvement could be reducing the uncertainty and bargaining that now often accompanies intergovernmental financial flows. Finally, there needs to be accountability in urban service delivery that makes allowances for both regulations made at a central government level and incentives devised for local constituents.

Beyond Urban Bias in Africa: Urbanization in an Era of Structural Adjustment

by Charles M. Becker, Andrew M. Hamer, and Andrew R. Morrison. Heineman, a division of Reed Elsevier, Inc., 361 Hanover Street, Portsmouth, NH 03801-9912. ISBN 0-435-08091-1.

The urbanization of Africa is increasing at an alarming pace. It



is a development that is aggravating macroeconomic problems all over the continent. This level of urbanization has increased the demand for imported goods, added to budget and balance of payments deficits, and coincided with a decline in agricultural production and a disastrous export performance.

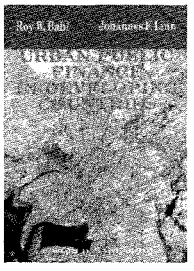
But there is a way out of the mess. Greater emphasis needs to be placed on the productivity of food production for urban as well as for national development reasons. There also has to be a greater focus on raising national savings rates. Industrial policies also need to be reorganized with more attention paid to the creation of labor-intensive industries to relieve urban unemployment.

Structural adjustment in Africa must also develop local administrative capacity and local fiscal authority, and create ground rules for the participation of the private sector in local development and urgently needed urban infrastructure.

Urban Public Finance in Developing Countries

by Roy W. Bahl and Johannes F. Linn. Oxford University Press, Inc., 200 Madison Avenue, New York, NY 10016, April 1992. ISBN 0-19-520805-6.

There is often a mismatch between a city government's



responsibilities for providing public services and its revenue-raising authority. Furthermore, experience shows that city governments do a better job of urban management when they have greater authority over their own affairs than when they must continually coordinate their actions with national or other local entities.

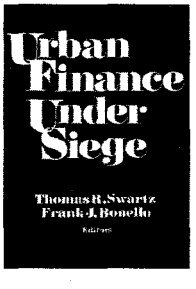
One area where urban governments in some developing countries have been found to be exceeding themselves, is when they try to provide services for all levels of the population that are not affordable.

Among the local sources of revenue available for financing public services, the authors recommend property taxes, taxes on business licenses, user charges, and taxes on automobile and vehicle use and ownership. The latter type of taxes, the authors say, have been neglected by urban governments in developing countries up to now. However, the revenue potential of such taxes can no longer be ignored.

Urban Finance Under Siege

by Thomas R. Swartz and Frank J. Bonello (eds.). M. E. Sharpe, Inc.,80 Business Park Drive, Armonk, NY 10504, 1993. ISBN 1-56324-224-9 (cloth). ISBN 1-56324-225-7 (pbk).

In this book, experts in the field of urban finance examine the root



causes of the fiscal problems now experienced by many major U.S. cities. One reason for the financial difficulties, the experts say, is that ever since the 1950s wealthy Americans have been moving out of cities to suburbs, because they were no longer finding high-quality services, good schools, and safe streets in cities. As a result, the tax base of city governments was eroded—a development that was compounded by the collapse of property values in many cities.

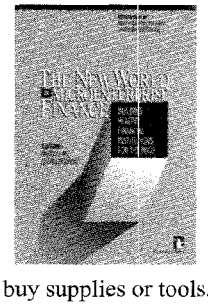
According to the authors, the best thing that could happen would be reversing the policies of the 1980s: restoring progressivity in the tax system, reinstating federal revenue sharing, and having the national government once again assume responsibility for social and economic problems that are national in scope and that cannot be adequately addressed locally.

The New World of Microenterprise Finance: Building Healthy Financial Institutions for the Poor

by Maria Otero and Elisabeth Rhyne (eds.). Kumarian Press, Inc., 630 Oakwood Avenue, Suite 119, West Hartford, CT 06110, 1994. ISBN 1-56549-031-2.

For increasing numbers of poor people, small businesses and informal economic activities constitute the only form of income and employment.

The owners of such enterprises are often seriously hampered by a



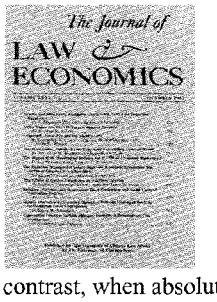
lack of working capital and because they cannot make the appropriate investments to buy supplies or tools, or make the needed improvements on their premises. Furthermore, lacking access to formal financial and credit services, many informal sector workers seek help from relatives or resort to costly, often extortionist, money-lenders.

However, viable self-sustaining financial intermediaries like the Grameen Bank in Bangladesh and the Unit Desa credit system of Bank Rakyat of Indonesia can be created to service low-income microenterprise clientele. These programs succeeded because they overcame the problem of the financial risk to mainstream credit and financial institutions by lending to microenterprises.

Princes and Merchants: European City Growth Before the Industrial Revolution

by J. Bradford de Long and Andrei Shleifer. Journal of Law and Economics, Vol. XXXVI, The University of Chicago Press, October 1993. ISBN 0022-2186/93/3602-0001.

The authors of this book contend that for 800 years before the Industrial Revolution, despotic



and autocratic rule is associated with periods of slow economic growth. By contrast, when absolutist rule was held in check, and merchants or landed magnates were given a voice through a constitutional veto, economies and commerce flourished.

The reasons for the contrast are that during autocratic rule governments tended to be centralized, individual rights to own property were precarious, and a rule of fear and insecurity made people who owned (capital) stock, hide it. On top of this, absolutist princes tended to tax towns and cities to increase the power of the state or the splendor of the court, or to finance wars. On the other hand, when princes' powers were limited, ordinary people were taxed less, cities had more autonomy, and prospered.

Below is a selection of urban events and training courses culled from The Urban Age*'s current files. We are not always able to list events more than once, given space limitations. Please refer to past issues of* The Urban Age *for additional events scheduled in 1995. Send your announcements to: The Editor,* The Urban Age, *Room S6-065, The World Bank, 1818 H Street, NW, Washington, DC 20433, USA. Fax: 202-522-3232, Internet: mmcneil@worldbank.org*

Conferences

Brisbane, Australia—September 18–20, 1995. **Australian Tropical Health & Nutrition Conference.** Contact: ATHN Conference Coordinator, Wendy Gardiner, Tropical Health Program, ACITHN, The University of Queensland Medical School, Herston Road, Herston, Queensland 4006, Australia. Tel: 61-7-365-5408; Fax: 61-7-365-5599.

Arlington, Virginia—October 1–3, 1995. **Urban Economic Development Summit.** Contact: Chris Mead, Conference Director, National Council for Urban Economic Development, 1730 K Street, NW, Suite 915, Washington, DC 20006, USA. Tel: 202-223-4735; Fax: 202-223-4745.

Rio de Janeiro and São Paolo—October 2–12, 1995. **EDIEN Regional Seminar on Management of the Urban Environment.** Contact: Ephim Shluger, EDIEN, The World Bank, 1818 H Street, NW, Room M-5066, Washington, DC, 20433, USA. Tel: 202-473-6428; Fax: 202-676-0978/7.

Vancouver, British Columbia—October 26–27, 1995. **Linking Transportation and Land Use Planning.** Contact: Ann Long, Registrar, Lincoln Institute of Land Policy, 113 Brattle Street, Cambridge, MA 02138, USA. Tel: 617-661-3016.

Auckland, New Zealand—November 16–18, 1995. **The New Local Government Conference—An International Perspective.** Contact: Massey University, P.O. Box 11, 222 Palmerston North, New Zealand. Tel: 64-6-350-4352; Fax: 64-6-350-5689; Internet: V.E.Forgie@massey.ac.nz

Dubai, United Arab Emirates—November 19–22, 1995. **Best Practices International Conference for Habitat II.** Contact: Christina Engfeldt, Chief of Information and External Relations, Habitat II Secretariat, P.O. Box 30030, Nairobi, Kenya. Tel: 254-2-623033; Fax: 254-2-623080.

Third Annual Conference on Environmentally Sustainable Development, October 4–6, 1995, Washington, D.C.

At a time when most countries face significant resource constraints, this conference will address the crucial question of how new and innovative financial instruments can be developed and used to meet the financial requirements of advancing environmentally sustainable development. The application of existing financial resources, fiscal and monetary policies, innovative partnerships for long-term financing, and the creative application of technologies will be examined.

This multidisciplinary conference—which will emphasize cross-cutting issues and sectors, as well as regional differences—will include a distinguished group of international authorities, including national and local government officials, private sector leaders, scientists and other scholars, and practitioners from both industrialized and developing countries.

Contact: Aïssatou Seck, The World Bank, Room S4-061, 1818 H Street, NW, Washington, DC 20433. Tel: 202-473-5546; Fax: 202-522-3244; Internet: ASECK2@Worldbank.org

Education Programs and Courses

Istanbul, Turkey—The Med-Campus Housing Network, in conjunction with Istanbul Technical University, is currently accepting applications from graduate students of architecture and urban planning, and professionals of public or private institutions for its second training course, **Housing for Low-Income Groups**. The course, to be offered October 2–20, 1995, will integrate theory with practice through lectures, case studies, individual studies, and discussions drawn from the global housing environment for low-income groups. The course aims to enable people to understand and solve housing problems, to train people with different backgrounds in the housing sectors and in the construction industry, and to equip individuals with different skills to set up groups that contain members with diverse expertise for solving a problem. Contact: Prof. Dr. G. Saglamer, Istanbul Technical University, Faculty of Architecture, Med-Campus Network C078, Taskisla Rektorluk Ofisi, Taksim, Istanbul 80191, Turkey. Tel: 0-212-243-1111; Fax: 0-212-251-4895.

Boston, Massachusetts—Boston University's School of Public Health will sponsor the eighth annual **Management Methods for International Health** program, to be held February 8–May 3, 1996. The intensive 12-week course addresses the practical application of management principles in the public and private health sectors of developing countries. All health personnel who have, or expect to have, managerial or supervisory responsibilities are welcome to apply. The course, which includes site visits to US health care facilities and a two-day academic retreat, offers participants a rigorous and timely educational experience. Contact: William J. Bicknell, Center for International Health, 53 Bay State Road, Boston, MA 02215, USA. Tel: 617-353-4524; Fax: 617-353-6330.

Birmingham, England The University of Birmingham's School of Public Policy is holding its third International Seminar of Senior Government Policy Makers, **Improving Performance in the Public Service**, October 30–November 25, 1995. The seminar is concerned with administrative reform and is organized to allow both individual and group exploration of the participant's key issues. Contact: Yvonne Swain, Course Administrator, Development Administration Group, School of Public Policy, University of Birmingham, Edgbaston, Birmingham B15 2TT, England. Tel: 44-121-414-4969; Fax: 44-121-414-4989.

Birmingham, England—Improving Financial Performance in Local Government is a three-month program being offered by the University of Birmingham beginning in February 1996. The intensive program—designed for senior officials from local and central government who are concerned with local government finance, as well as those from training institutions—looks at current practices in Britain and internationally, and is designed to address the practical needs for wider knowledge and improved skills of the participants, related to their own work situations. Contact: Yvonne Swain, Course Administrator, Development Administration Group, School of Public Policy, University of Birmingham, Edgbaston, Birmingham B15 2TT, England. Tel: 44-121-414-4967, Fax: 44-121-414-7164.

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also have their criticisms. Mayors who attended the Inter-American Conference of Mayors, "Pathways of Development for Municipal Governance" in Washington, D.C., in November 1994, said any reliance on central government transfers involves a risk as such transfers can always be withdrawn or altered. As a result, the control of local governments over the revenue side of their budgets is strictly limited.

Latin America's mayors realize it is important to improve local revenue collection. However, they often feel constrained by the strict rules imposed by their central governments regarding local taxation and the application of local user fees or charges. Indeed, it turned out that most mayors would rather have the right to levy a variety of taxes and user fees locally at preferred rates, so they could at least have some control over their revenues.

Still, it is generally understood by local governments that a lot can be done to improve the efficient use and flows of local government financing, that it is important to raise revenues locally, and to link sources of revenue with allocations of expenditure to increase accountability. However, this balance has not yet been struck by local governments because of a variety of constraints. For instance:

- At the same time, local governments have tried to increase their share of national revenue transfers by negotiating with the central governments. They have opted to do this rather than try to negotiate higher local taxes or user fees with their constituents.
- Local revenues have traditionally been raised by local taxes and user fees or charges for services. Attempts to increase the revenues from these sources are generally related to improvements in their management and collection, and fee limits are usually legally and/or politically restricted.
- Even though decentralization has helped bring the state closer to ordinary people, there are no signs yet that ordinary people trust the authorities, even when they are elected.

However, user charges for service delivery are increasingly being used to generate income to pay for the operational and maintenance costs of services. Such income has only a limited use when it comes to financing capital investments to expand a city's infrastructure, because of the increase in marginal costs when such services are expanded, and the increased costs involved in servicing public debt.

New approaches to local finance management: public-private partnerships

Some innovative financial strategies that could improve local governance and financing have already been introduced and developed by municipalities in Latin America, while others have been tested in other developing countries. Most of these strategies involve the private sector and community participation in the operation and management of projects.

Among the alternatives, there are three main areas where the public and private sectors complement each other.

- From an economic point of view, public investment in social (i.e., health and education), and urban infrastructure helps boost private sector productivity. The more the public investment is targeted, the bigger the impact it has in terms of economic growth.
- Public and private sector financing is also complementary when it pays for a project that is a joint venture, or helps to match funds, or is involved in privatization programs. In cases like these, public resources use private capital as leverage and, as a result, often improve the efficiency and targeting of such investment.
- Latin American communities often participate in small municipal projects. The community designs and plans the project, and provides the labor and/or oversees the use of the public funds. Although the impact of the public funding on the local economy is small, there is considerable accountability in the use of such public funds as the community is directly involved in, and committed to, the success of the project and also controls how the money is used.

It seems then that a pattern is emerging that promises a new approach to municipal financial management in Latin America.

Monica Ramirez Londono is a Colombian economist. She has worked in Colombia in several national institutions in charge of policy design for decentralization, financing and providing technical assistance to municipalities. She is currently a specialist in municipal financing with IULA/CELCADEL with repsonsibility for the municipal training program for Bolivia, Colombia, Costa Rica, Ecuador, Peru, and Venezuela.

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Next Issue

The fall 1995 issue of *The Urban Age* will be on Best Practices in Urban Management. In the winter issue, the focus will be on the New Urban Poor. We look forward to receiving your comments and thoughts on these upcoming issues.

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