Sub-national Finances and Fiscal Sustainability

Workshop IDB
21 and 22 January, 2010
Washington DC
I. Clue:
- Globalization and localization effecting growing LG 20/25 year
- Financial crises
- Sustainability
  - Position revenue LG
  - Dependent of transfers – 60%
  - Ec crisis, fiscal crisis
  - Reduction of tax

II. National Level:
- Ec. Crises, fiscal pressure to increase tax
- Increasing needs of SNG

III. Public Services
- Devolve services
- Share lesson Learned
Mexico

Frame Work:
• Fiscal Dec increasing: 1995-2005 > 8-20%
• Sub-national exp high and low, assume more services within autonomy
• Fiscal Dec > efficiency, accountability, competition, local preferences
• Fiscal rules effective for key issues: fiscal autonomy, wealth matters, revenue collaboration, fiscal preferences

• Inter-gvt fiscal relation
• Growing concentration of power for tax collection
• Dec of public expenditures at local level
  - participation : %
  - own revenue : %
  - Special decentralization arrangements/agreements
Mexico

- Federal transfers: increased in Mexico
- Incentives
- 11.5% own rev = low
- Federal transfer = high
- Prop Tax Mexico = low (below it’s potential), cannot finance basic services (US$ 175 = US$ 3 p.p./p-yr.)

- Challenge = increase sub-nat revenues
- Incentive based on agreements SNG and CG to collect taxes
- Deal with bigger budgets as education (agreements)
- Formulate new district formula
- CG has to concentrate on
  - > role of SNG in fiscal dec
  - > Challenge to devolve to SNG rev and resp to spend
- Fisc sustainability: only in relation to whole Gvt.
- CG has to push more problems to LG
- Promotions to change attitude of CG and SNG
QUESTION OF SMALL LOCAL GVT’s

Question from Suriname:
• Questions of small governments
• Low Tax Collection
• Low transfers
• Role of CG
• Capacity to manage self financial management, capital works

HOW T TO FINANCE LOCAL GVT’s?
• Summary Rafael: Increase local revenue
• Create rules for intergov relations
• Transfers CG through debts

Reaction:
• Capacity SNG = there is not one size SNG’s
• Incentive 10-12%
• Automatic transfers from Central to local (don’t cause delays in spending at local level)
• Strengthen capacity to raise revenue
• Create fiscal rules
• Create stabilization funds (DEF)
COLUMBIA

- No relation to own rev
- Tax base rev is not necessary
- That is Model for poor/small countries
- Manage small SNG based on ‘private financial systems of a ‘warehouse’. See Study wrld bank
- Trend for strong countries is high level of fiscalization.
- Make Loans for economic activities
- Transfer system for SNG:
  - > population, health, fiscal behavior, etc
  - >increasing of global transfer
  - >borrowing allowed (debt)
- Method: policy, fiscal rules in place, time effort (don’t delay spending activities)

- Look at capital income. Tax collection based on income:
- Poor countries: rev based on property tax= main source (poor areas/rich areas)
- Developed countries: rev based on income tax
- >Rev based on raw material export (not all of export)
- >Face the shocks (ups/downs of world market); create equalization Fund for bad times
- =high level of external revenues
- >Fiscal behavior
Bolivia

- 20% of all revenues = local
- Dec = highly political criteria; per capita
- Responsibilities: public services
- Oversight committees, demand driven
- Municipalizasation / creating of new municipalities
- Cooperative sharing of responsibilities in: industry, communication, water, environment, health, transport (clear view)

- Democracy and Decentralization are each complementary
- Simplicity and transparency
- Enhances accountability level
- Clear division of authority
- Devolve significant tax raising process to each level
- Scale back central Gvt
- Decentralization is a policy proces, not a measure
- All LG’s – integrated Mgt systems
- Improve peoples quality of live through: health, sanitation, water, electricity,
BRASIL

- Rev grew: federal transfer as fiscal
- Fiscal target: keep ‘n eye on it
- Royalties: some % as extra to SNG-funds
- Fiscal transfers: extra to SNG-funds> who will pay for it; strategy focused on the suppliers, industry, whole sale, retail (increase taxes not at the level of retail); tax the other levels.

- Go after the taxpayers
- Credit cards companies
- Millions of cell phones in Rio. Tax $ 1, and see the grew of income.
Bogota

- 35% households financing 60%
- Property tax = $ 4000 per year per household
- **Decentralization in Bogota = success via incentives given to SNG**
- Finance some of the areas and declare transfer from CG
- For instance: building of schools in coop between CG and LG

**Summarizing:**
- **Strengthen own rev cap of the SNG**
- **Mix: transfer and own rev**
  Region in general diff consequences:
  - **Fiscalization: problems**  
    (Bogota, Mexico, Spain)
    - Lack of taxation power
    - Lack of unavailable taxes
    - Rich and poor areas
    - GPD’s difference
  - Decentralized countries:
    - Rich dec countries
    - Poor dec countries (poor and rich areas)
    - Bureaucracy in SNG’
Fiscalization: problem

- Tax Collection: problems:
  - Lack of coordination SNG/CG
  - Main: property taxes
  - Lack of accountability
  - Decentralize cadastre: no capacity to do this
- So, many challenges

Opportunities:

- Coordinate better tax collection
- Re: solitary authority: which taxes to dec > property tax (see also ethnical property
- Cloning of tax systems?
• Tax Income activity
  > info, info, info
  > use of IT to reduce costs
  > work together: national and local gvt
  > transparancy

• Tax Sharing
  > Through notary
  > Partnership

• Taxes in Brazil:
  > environment (oil) 4/5%
  > VAT 25%
  > royalties NG, SNG (2 bil $)
While Columbia struggles with:
  1% RVT, No cadastre/no info

• Power to collect:
  • > local taxes/prop tax
  • > municipality taxes:
    telecommunication, transport, interstate

• Why so many efforts? No explanation; lack of capacity, poor entities (no ec. Act)
RIO

- Simple transfers:
  - Transfer real estate tax via notary
  - Transfer income tax
  - Fee/charge of police
  - Inter-gvt transfer: tax and revenue sharing
  - Transfer by state

- Difficult to collect taxes:
  > small entities
  > simplify systems
  > no one sole system in so many differences
  - Area’s with high income and area’s with low income
  - We have to create other type of systems
  - Prop tax is not popular
  - Work out other formula’s
  - > request of fiscal invoice
  - Brazil: the option is: simple management
ARGENTINA

• Clear tax rules
• Budget municipalities of 400 million $
• 40% is shared revenue
• Prop tax 3 or 4 % a month some cat.
• And 8% other cat.
• Land use with houses is 1\textsuperscript{st} cat.

• The more transfer from CG the less effort of collecting local revenues
• Relation Mayor and citizen: elected mayors are closer to the voters/citizen
CENTRAL AMERICA

• Collection negative
• Costs are higher
• Collection positive when strengthening the capacity
• NEED TO HAVE PROGRAMS TO STRENGTHEN LOCAL REVENUE CAPACITY