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Intergovernmental Fiscal Relations and Local Financial Management

In co-operation with the Local Government and Public Service Reform Initiative of the Open Society Institute, Budapest and the World Bank Institute, Washington

July 12-23, 2004

Course directors: **Adrian Ionescu**, Local Government and Public Service Reform Initiative of the Open Society Institute, Budapest
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Serdar Yilmaz is a Public Sector Specialist at the World Bank Institute (WBI). He coordinates curriculum development activities of the WBI's Intergovernmental Fiscal Relations and Local Financial Management Program. In addition to his managerial assignments, he does research and scholarly work on issues related to public finance and intergovernmental fiscal design in developing countries. His research interest areas are analysis of decision making in the public sector, analysis of intergovernmental policies in developing countries, and the role infrastructure service provision in regional development patterns. He has participated in many learning activities of the WBI and his research has appeared in academic journals and books edited by leading academics in the field. He holds a Ph.D. degree in Public Policy from George Mason University.

József Hegedüs is Head of the Metropolitan Research Institute. He was trained as an economist and holds a Ph.D. in sociology. He has ten years experience in Hungarian local government reforms, especially financial issues such as grant allocation, budgeting process, designing equalisation grants, analysing effects of local tax, local government capital budgeting, etc. As a project manager he has been lately involved in research on local government finance in Budapest, and in the preparation of the Budapest Program for 1996-2000. He led a team at MRI in co-operation with the Urban Institute, Washington to develop a training course for local government financial experts on program budgeting and related financial issues, and took part in the SNDP (Sub-National Development Program of World Bank, USAID and Know How Fund in Hungary). He was co-author of the study "Local Management in Hungary: Fiscal and Structural Adjustment at the Local Level in the Context of Economic Transition."

Adrian Ionescu is the Program Director for the Local Government and Public Service Reform Initiative (LGI) at the Open Society Institute in Budapest, Hungary. In addition to managing LGI, he is responsible for the "Subnational Governmental Finance, Fiscal Decentralization and Budgeting" program to generate and disseminate knowledge and best practices in CEE and fSU. Before joining the program in Budapest, Adrian worked as Project Manager for the Soros Foundation, and previously as a Research Officer for the Ministry of Public Works and Regional Planning in Romania. He holds a certificate from Harvard University, a MBA from Université du Québec à Montréal and a M.Sc. in Engineering from the Polytechnic University of Bucharest.

Course objectives

The objectives of the course are to (i) provide participants with the analytical framework for understanding intergovernmental fiscal economics and various modules of the central-subnational (e.g., local) relationship, (ii) enhance participants' capacity for successful implementation of public sector resource management reform by analysing mechanisms for the transfer of resources among governments and identifying ways to address the issue of regional disparities and local resource mobilisation, (iii) and increase participants' understanding in the issues of fast restructuring public economy in countries of transition, (iv) enhance participants' capacity to understand and use the practical simulation methods on public finance issues (transfers, local taxes).

Course level, target audience

The course has been designed for the practitioners, researchers/academics and trainers in the area of public finance related to local government issues and intergovernmental fiscal relations. Applicants are expected to have a basic knowledge of computer and software usage, e.g. Ms Excel. During the course one day will be dedicated to simple simulations using Ms Excel.

Syllabus

I. Fiscal decentralization

Overview of the fiscal decentralization problem. Key questions in decentralization. Another distinction: unitary versus federal states. Fiscal and other forms of decentralization. Critical question of decentralization. Musgrave's definition of state functions. Traditional approach of decentralization. Why or why not decentralize. Benefits and risks of decentralization. Does decentralization destabilise? A new approach of decentralization in a transitional economy.

II. European Charter of Local Self-Government

Application of the decentralization theorem of Oates. Goals and structure of ECLSG. The subsidiary principle. Autonomy in expenditure decisions. Legal independence and protection. Financial autonomy according to ECLSG. Minimal requirements. Draft European Charter of Regional Self-Government.

III. The assignment of expenditure responsibilities

Fiscal roles and responsibilities and the operations of a multi-tier government. Finance follows function, an axiom. The assignment of expenditures--the theory and practice. First division: Public versus private goods. Second division: principles to guide expenditure assignment. Externalities of local expenditures: the spill-over effects. The capacity of local governments. Economies of scale problem. Invention at local level. Operating vs. capital spending. An appropriate regulatory framework of local expenditures. The role of privatization of public services.

IV. The tax assignment problem: conceptual and administrative considerations in achieving subnational fiscal autonomy

Narrowing the scope of inquiry: Musgrave's three-functions framework. Realizing the political benefits of tax assignment. Constraints on tax assignment. Conceptual arguments. Alternative methods of revenue assignment. Administrative considerations. Vertical imbalance and horizontal disparities. Concluding remarks: tax competition revisited.

V. User fees at local level

Concept of user fee finance. Application of benefit principle at local level. The nature of local public goods. Residual or essential revenue. 'Price' or 'charge'. User charges in theory and in practice. A Public Finance vs. Public Choice. Determination techniques of user charges. Charging in relation to costs, marginal cost pricing. Charging in relation to benefits. Charges and collective provision of Services. Charging the poor. User fees in CEE countries.

VI. The intergovernmental systems and grant structure

Questions of macroeconomic control by central government. The objectives of an intergovernmental grant system. Correcting or adjusting for vertical imbalance. The

determination of transfer pool. Internalize spillovers. Correcting inequalities among local governments: horizontal equity. Coordinating central and subnational spending. Central goals and local incentives (tax effort, inter-governmental cooperation, structure of government).

VII. Framework for enhancing local government creditworthiness, municipal credit markets

Framework for International Local Creditworthiness; General Features, and Issues Underlying the Development, of Municipal Credit Markets; "Structured" Financing in Municipal Credit Markets; Legal and Regulatory Framework; Local Government Institutional Capacity; Infrastructure Financing and Access to Private Capital Markets; Municipal Bond Markets Prospects for Developing Countries

VIII. Property Tax, an appropriate option for local tax

Increased importance of the property tax in the OECD countries; Advantages of a property tax; The property tax as a local tax; Basing the property tax on market values; Taxing both land and buildings or taxing land alone; Administration of the property tax; **Exercise:** designing property tax (simulation). Implementation: metering, collection, enforcement, billing; Case study.

IX. Local Government Budgets and Financial Management

Budget purpose; Types of budgets; Budgeting and Accounting; Stages of the budget process; Capital Budgeting; Evaluation of performance. Adjustment techniques in changing environment. Off-budget services. Privatization of local public services. Regulation of local market.

X. Sector approach: housing

Role of the state in housing in the pre-transition and after the transition; Different privatization strategies: alternative service delivery (municipal, non-profit and private); Central and local housing programs: structure of grants and subsidies (housing allowances, vouchers, construction subsidies, etc.), combining central and local programs; Private and public partnership in housing development at local level; Local Housing Funds: revenues and expenditures, operational issues; Issues of regulation: rent control (central and local solution), building regulations, land development, arrears; Issues of externalities: grant "leakage"; Local housing indicators; **Exercise:** designing a housing program grant (simulation)

XI. Sector approach: water and sewage

Structure of the sector in pre-transition period, Fragmentation or decentralization: institutional restructuring, Alternative service delivery: one-purpose districts, Privatization of water services: advantages and possible dangers, Role of the user charge in public services: Water price structure, willingness to pay, and arrears issues, Environment regulation: role of supervisory agencies, EU accession: investments needs, Investment grants, **Exercise:** case study of privatization

Distance Learning

The course organisers will send out distance learning materials at the beginning of April and will involve participants in a pre-course distance learning project. These materials will cover an overview of issues of financial decentralisation as well as those of revenue and expenditure assignments. Course tutors will keep contact with participants sending out and discussing assignments via email. They will also establish email discussion forums among prospective participants so that they can exchange information and views prior to course start.

Assignments and assessment

Each participant is expected to prepare a presentation on the fiscal decentralization issues of her/his country and on the issues of one public sector. These papers will be presented during the course.

Submission of five assignments related to the Distance Learning Modules is mandatory for participation in the SUN course in July.

The participants will be evaluated according to their attendance and contribution to class discussions and workshop exercises.

Teaching methods

The course aims to achieve the right mix of exercises, lectures, and interactive learning methods. This includes the dissemination of materials prior to the course presentation (paper and/or electronically) and supplementing the content with simulations, case studies and interactive discussions. Preceding the course participants will receive a distance learning package containing six modules of the course (see syllabus). Teaching of the DL stage will be conducted via email discussion, guided reading, and a series of exercises via email. It is expected that students will continue to receive support after the course using Internet and Email.

Travel grants

Through the generous funding of the course received from the World Bank Institute and the Local Government and Public Service Reform Initiative of the Open Society Institute applicants from all countries of Central and Eastern Europe, the former Soviet Union and Mongolia, as well as from countries of emerging democracies worldwide are eligible for travel grants.

For more detailed biographies, updated course description, syllabus, reading lists please check <http://www.ceu.hu/sun/index.html>

Non-discrimination policy statement

Central European University does not discriminate on the basis of--including, but not limited to--race, color, national and ethnic origin, religion, gender or sexual orientation in administering its educational policies, admissions policies, scholarship and loan programs, and athletic and other school-administered programs.