

EVALUATING THE FINANCIAL HEALTH OF INDIAN CITIES: A DIAGNOSTIC REPORT

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Some “Myths” about Municipal Finance

- All municipalities are similar in terms of income and expenditure
- All municipalities are in a financial crunch
- Surpluses reflect good financial health
- Large cities can generate more finances
- High Incomes/expenditures indicate better financial health
- High operating costs indicate better level of services
- Cities with poor financial health follow cash based accounting system
- Loans deteriorate the financial health of a city
- Privatization can improve the financial health of a city

PURPOSE OF THE STUDY

- To examine the fiscal performance of the municipalities from different states and seeks explanation for their differential performance.
- To examine the fiscal performance of the municipalities from the same state and rank of these cities on the basis of their fiscal performance.

Questions that have Fundamental Importance

- What are the important indicators that explain the financial health of a municipality?
- What are the problems in inter and intra-state comparisons?
- What is the impact of population size on financial performance?
- Why have some ULBs (or municipalities) performed 'better' in terms of high per capita incomes and expenditures?
- Does high per capita expenditure indicate better financial health?
- Why do some municipalities have greater dependency on state transfers?
- Can municipalities be compared on the basis of their financial performances alone?

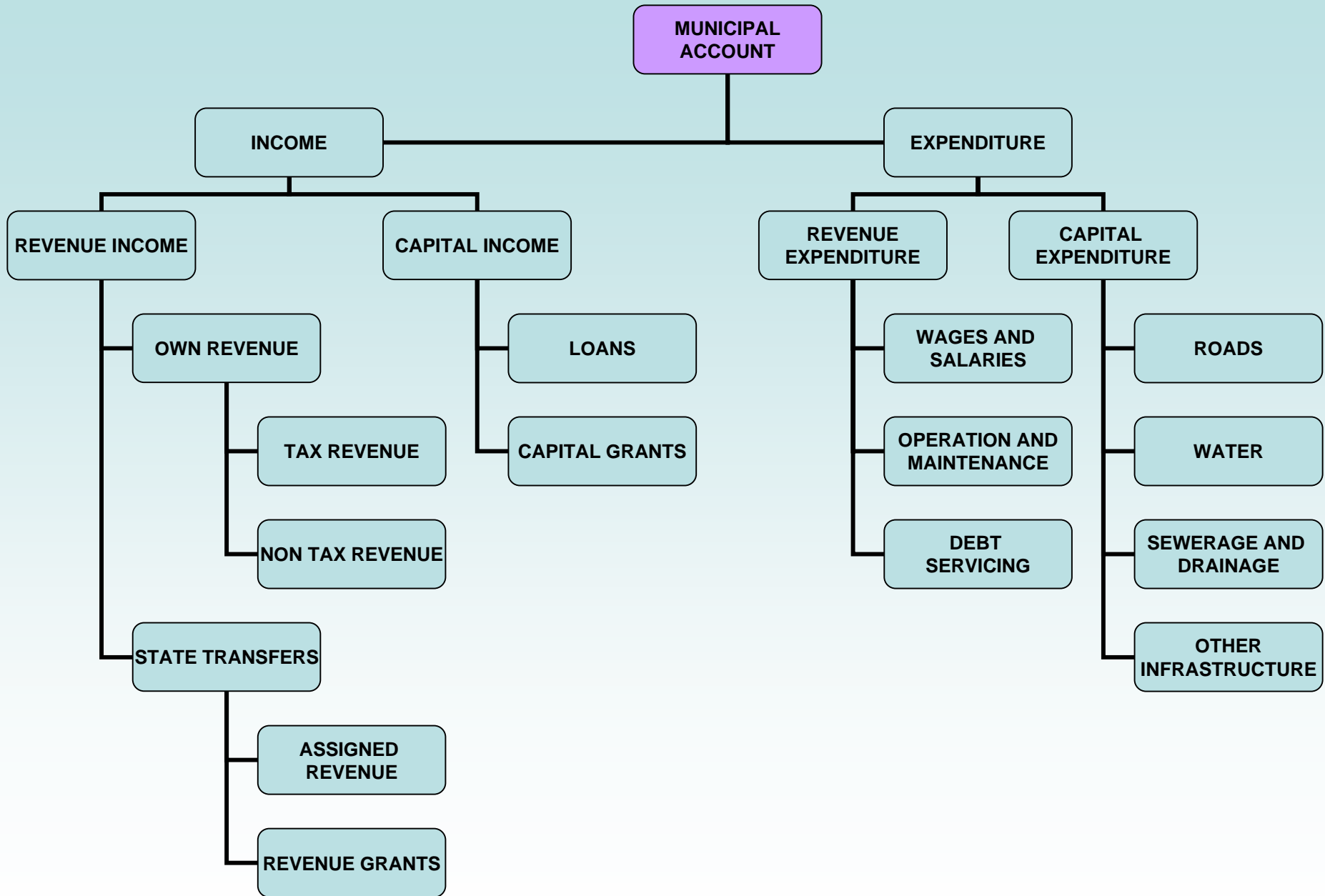
Database

- Thirteen out of sixty three cities which have been identified for JNNURM mission.
 - **Andhra Pradesh:** Hyderabad, Vijayawada, Vishakapatnam
 - **Gujarat:** Surat, Ahmedabad, Vadodra, Rajkot
 - **Tamilnadu:** Madurai, Coimbatore
 - **Rajasthan:** Jaipur
 - **Madhya Pradesh:** Indore
 - **Chattisgarh:** Raipur
 - **Assam:** Guwahati

Limitations of the Study

- Sectoral Financial Analysis could not be made at this stage (May be taken up in the next round, subject to availability of data)
- Department-wise financial analysis was not possible due to non-availability of data.
- Shortcomings of cash-based accounting system could not be overcome.
Only Income-Expenditure Statement are taken into account.
- Detailed analysis on Capital Account could not be made.

MUNICIPAL ACCOUNT AT A GLANCE



Own Revenue Receipts

	Amounts in Rs. Crore			Annual
	2001/02	2002/03	2003/04	Gr.Rate (%)
Ahmedabad	472.49	526.46	608.33	13.49
Surat			575.24	
Hyderabad	194.76	203.91	275.74	19.96
Vadodra	174.25	188.49	200.70	7.32
Rajkot	88.14	110.91	105.39	10.43
Vishakapatnam	93.34	85.14	94.85	1.31
Indore	56.76	66.20	81.19	19.63
Coimbatore	54.94	57.04	71.36	14.46
Vijayawada	30.20	50.00	64.54	47.32
Madurai	53.01	44.88	46.18	-6.21
Jaipur	35.77	37.92	22.89	-16.81
Raipur	15.91	19.64	16.18	2.94
Guwahati	25.23	26.79	15.66	-17.66

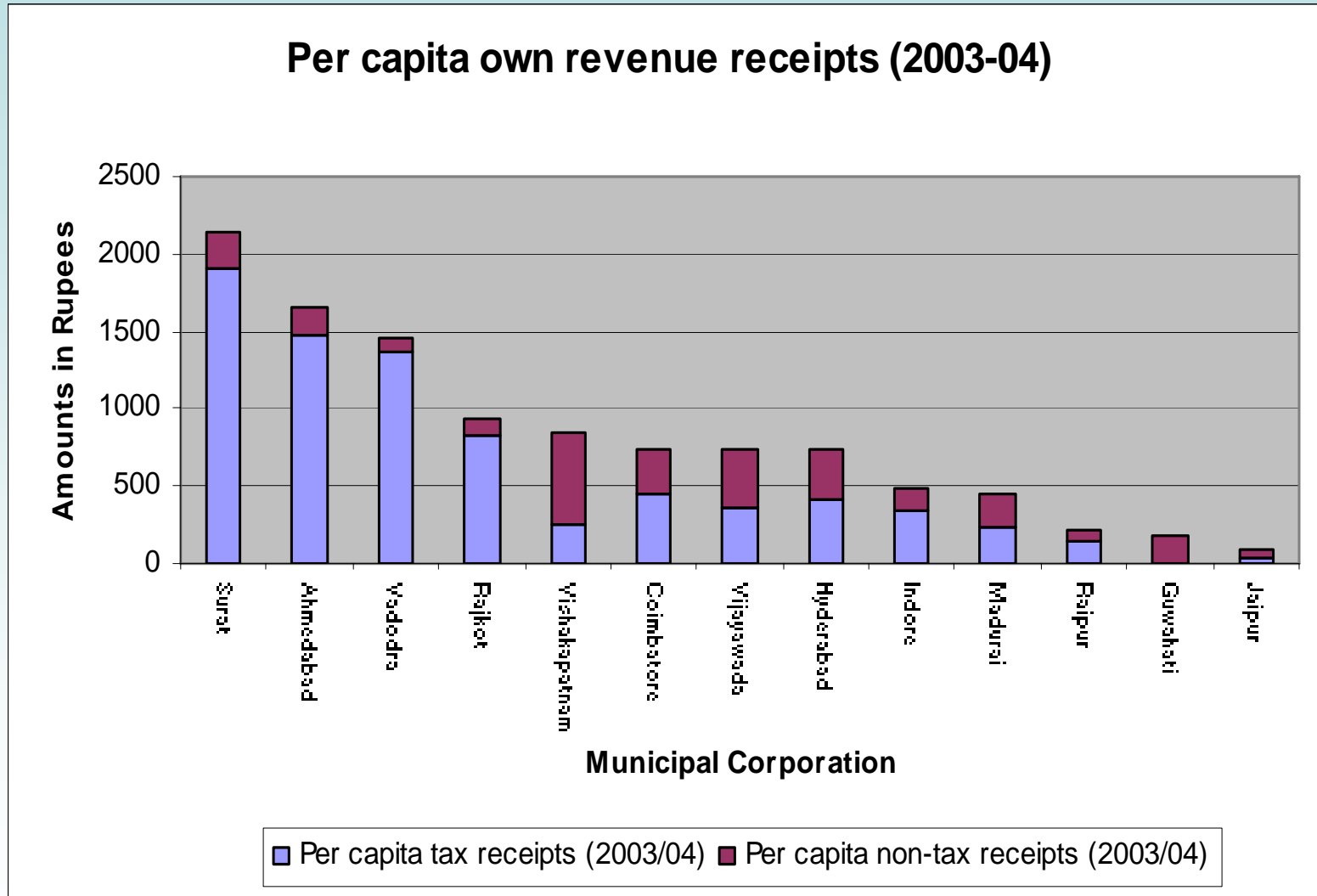
Population as per Census, 1991, 2001

	Population in Lakhs		Annual Exp. Gr.Rate (%)
	1991	2001	
Hyderabad	30.50	36.30	1.74
Ahmedabad	28.77	35.20	2.02
Surat	14.99	24.33	4.84
Jaipur	15.20	23.20	4.23
Indore	11.04	15.43	3.35
Vadodra	10.31	13.06	2.36
Rajkot	5.59	10.02	5.84
Vishakapatnam		9.60	8.25
Coimbatore	8.06	9.31	1.44
Madurai		9.29	5.87
Vijayawada	7.02	8.45	1.85
Guwahati	5.84	8.10	3.27
Raipur	4.61	6.70	3.74

Population Growth of Municipalities 1991 to 2001

Population size (2001) and Annual growth rate (%)	High growth rate (AAGR $\geq 3.5\%$)	Medium growth rate (2.5% to 3.5%)	Low growth rate ($\leq 2.5\%$)
More than 3 million			Hyderabad, Ahmedabad
1 to 3 million	Jaipur, Surat, Rajkot	Indore	Vadodra
Less than 1 million	Vishakapatnam, Madurai, Raipur	Guwahati	Vijayawada, Coimbatore

Per capita Own Revenue Receipts – A Comparison



OWN RESOURCE GENERATING CAPACITY OF MUNICIPALITIES

Own resource generation capacity	Municipal Corporations
High	Surat, Ahmedabad, Vadodra, Rajkot,
Medium	Vijayawada, Coimbatore, Vishakapatnam, Hyderabad, Indore, Madurai,
Low	Raipur, Jaipur, Guwahati

Obligatory and Discretionary Tax powers

Tax Domain of Municipal Corporations

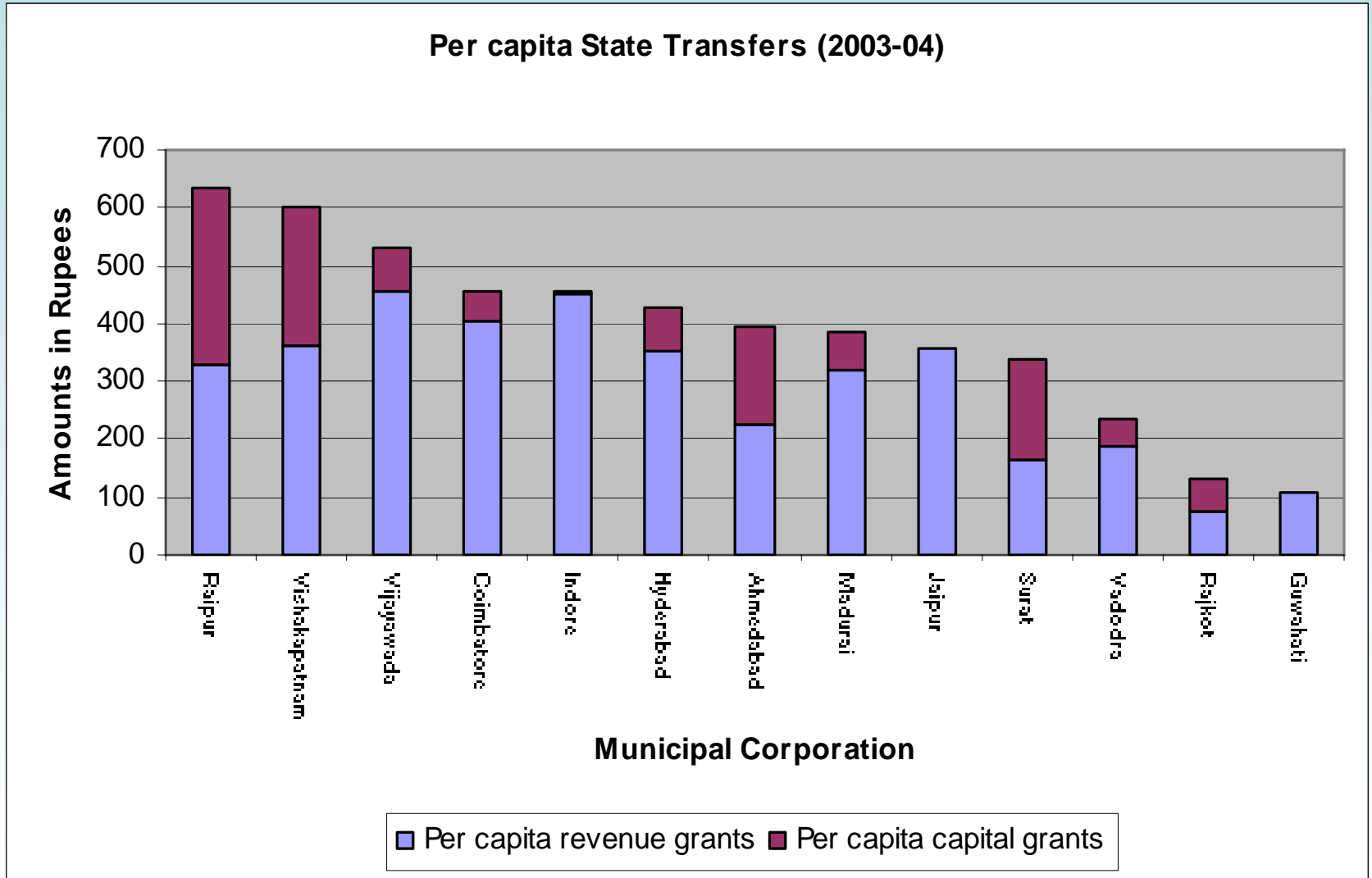
Tax Domain	Municipal Corporations
With Octroi and with composite property tax	Ahmedabad, Surat, Rajkot, Vadodra
Without Octroi and with composite property tax	Hyderabad, Vishakapatnam, Vijayawada, Madurai, Coimbatore
Without Octroi and with general property tax and water tax	Indore, Raipur
Without Octroi and with general property tax only	Jaipur, Guwahati

Note: In addition to these taxes Municipal Corporations levy other taxes also but collections from other taxes are not significantly high.

State Transfers in Rs.Crore

	Revenue and Capital Grants		
	2001 /02	2002/03	2003/04
Hyderabad	165.71	227.72	161.27
Ahmedabad	130.59	126.44	145.36
Surat			91.16
Jaipur	79.37	82.65	89.93
Indore	97.93	74.37	75.20
Vishakapatnam	29.36	59.40	67.88
Vijayawada	28.34	31.27	46.51
Raipur	44.51	55.22	45.65
Coimbatore	31.84	52.88	43.70
Madurai	38.16	42.38	40.31
Vadodra	29.73	38.18	32.44
Rajkot	7.58	17.03	14.60
Guwahati	6.72	11.11	9.16

Per capita State Transfers – A Comparison



Level of State Dependency (2003-04)

(Revenue transfers as % of revenue receipts)

Level of state dependency	Municipal Corporations
High dependency (>40%)	Jaipur , Raipur, Madurai, Indore
Medium dependency (20-40%)	Hyderabad, Vishakapatnam, Vijaywada , Coimbatore, Guwahati
Low dependency (<20%)	Ahmedabad, Vadodra, Surat and Rajkot

Structure of State Transfers

Category	Municipal Corporations
With octroi compensation and With assigned revenue	Hyderabad, Vijayawada, Vishakapatnam, Coimbatore and Madurai
With octroi compensation and Without assigned revenue	Raipur, Jaipur, Indore, Guwahati

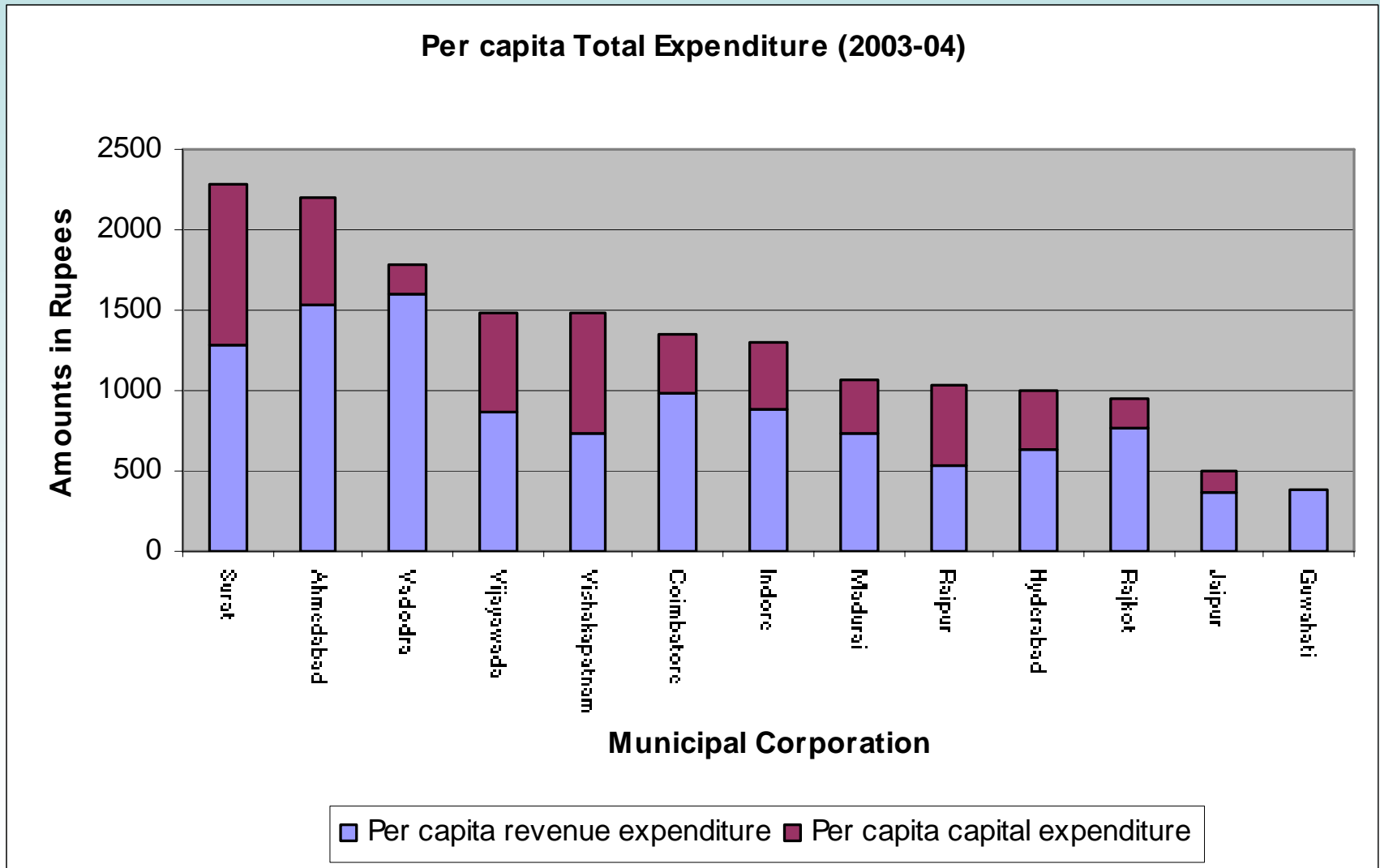
Devolution Package (First and Second State Finance Commission)

State	Recommended shares (first state finance commission)	Recommended shares (second state finance commission)
Andhra Pradesh	39.24% of state tax and non-tax revenue to all local bodies.	40.92% of state tax and non-tax revenue to all bodies, both rural and urban bodies, 9.67% is allocated to municipalities.
Madhya Pradesh	8.67% of the tax and non-tax revenues of state government.	1.07% of divisible pool of state own tax revenue.

State	Recommended shares (first state finance commission)	Recommended shares (second state finance commission)
Rajasthan	2.18% the net proceeds of state taxes should be devolved on the local bodies; the division of these proceeds between rural and urban should be in the ratio of 3.4:1.	Total devolution of Rs.794.43 crore consisting of 2.25% share in states net own tax revenue (excluding entertainment tax); 15% share in entertainment tax for ULBs for the award period 2000-05 and 1% share in royalty receipts from minerals to Gram Panchayats.
Tamil Nadu	8% of the state's net tax revenue should be devolved on the local bodies in 1997/98; this should gradually increase in successive years to 9%, 10%, 11% and reaching 12% in 2001/02. The division of this amount between rural and urban should be on the basis of population as in the last Census.	8% of state's own tax revenue, after excluding entertainment tax to local bodies for each year from 2002/03 to 2006/07; shares of PRIs and ULBs in the recommended devolution will be in the ratio 58:42.

Source: Reports of the Finance Commission of States.

Per capita Total Expenditure – A Comparison

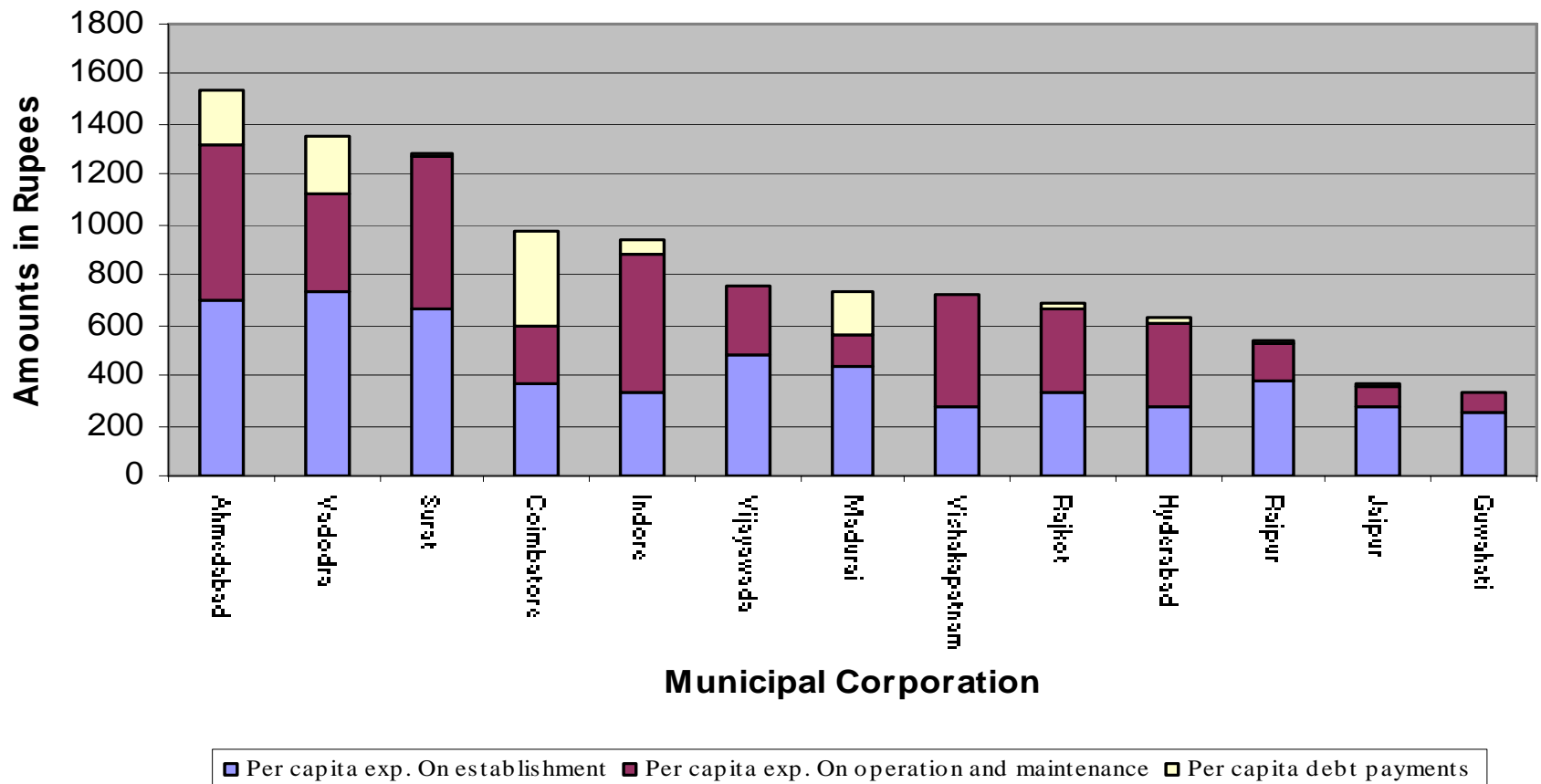


Functional Domain of Municipal Corporations

Categories of Tax/Functional domain	Municipal Corporations
Large functional domain	Surat, Ahmedabad, Rajkot, Vadodra, Vijayawada, Vishakapatnam, Madurai, Coimbatore
Low functional domain (excluding water/drainage)	Raipur, Indore, Hyderabad , Jaipur, Guwahati

Per capita Revenue Expenditure – A Comparison

Per capita Revenue Expenditure (2003-04)

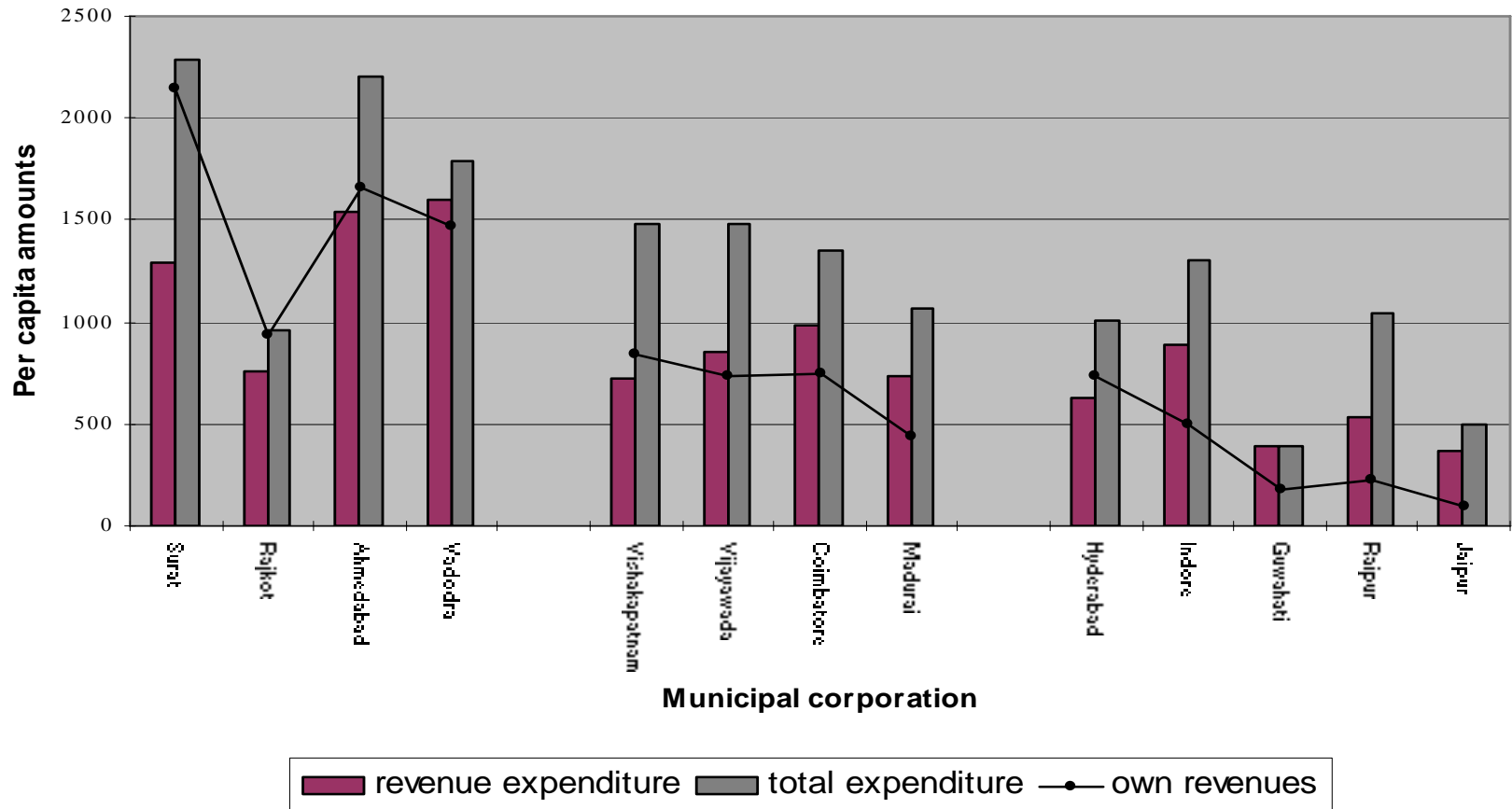


Fiscal and Functional Domain of Municipal Corporations

Categories of Tax/Functional domain	Municipal Corporations
Large functional domain and Large tax domain (octroi, composite property tax)	Surat, Ahmedabad, Rajkot, Vadodra
Large functional domain and Medium tax domain (without octroi but with composite property tax)	Vijayawada, Vishakapatnam, Madurai, Coimbatore
Low functional domain (excluding water/drainage) and Low and Medium tax domain (includes water/drainage tax)	Raipur, Indore, Hyderabad , Jaipur, Guwahati

A Comparison of Municipal Corporations having a similar kind of Fiscal and Functional Domain

Own revenue receipts vs total/revenue expenditure (2003-04)



Important Indicators of Municipal Financial Health

2003-04	Surat	Rajkot	Ahmedabad	Vadodra
Own revenue receipts as % of total revenue receipts	92.80	92.71	88.08	88.65
Own revenue (w/o octroi) as % of total revenue receipts	35.66	41.45	30.03	27.91
State transfers as a % of total revenue receipts	7.20	7.29	11.92	11.35
Octroi as a % of own revenue receipts	61.57	53.99	65.91	68.51
Property tax as a % of own revenue receipts	26.10	0.00	21.52	24.75
Non-tax as a % of own revenue receipts	11.37	10.89	11.60	6.74
Revenue expenditure as a % of total expenditure	56.43	79.52	69.80	89.29
Capital expenditure as a % of total expenditure	43.57	20.48	30.20	10.71
establishment expenditure as a % of revenue expenditure	51.28	44.10	45.57	46.20
O&M expenditure as a % of revenue expenditure	47.17	43.55	40.26	24.19
Debt servicing as a % of revenue expenditure	1.55	2.26	14.17	14.42
Own revenue receipts as a % of revenue expenditure	166.64	123.27	108.12	91.84
Own revenue (w/o octroi) as a % of revenue expenditure	64.04	53.24	36.86	28.92
capital grants as % of capital expenditure	18.17	30.38	27.45	27.04
transfers (revenue+capital) as % of total expenditure	15.50	14.39	19.12	13.92

Important Indicators of Municipal Financial Health

2003-04	Vishakapatnam	Vijayawada	Coimbatore	Madurai
Own revenue receipts as % of total revenue receipts	70.23	61.70	64.92	57.99
State transfers as a % of total revenue receipts	29.77	38.30	35.08	42.01
Property tax as a % of own revenue receipts	21.00	46.97	56.44	49.78
Non-tax as a % of own revenue receipts	69.21	50.45	40.03	47.22
Revenue expenditure as a % of total expenditure	49.13	57.89	72.39	68.72
Capital expenditure as a % of total expenditure	50.87	42.11	27.61	31.28
establishment expenditure as a % of revenue expenditure	37.12	56.35	37.90	59.23
O&M expenditure as a % of revenue expenditure	62.13	31.38	22.62	16.86
Debt servicing as a % of revenue expenditure	0.75	0.37	38.54	23.91
Own revenue receipts as a % of revenue expenditure	115.20	85.71	75.90	60.41
Own revenue (w/o octroi) as a % of revenue expenditure	115.20	85.71	75.90	60.41
capital grants as % of capital expenditure	31.67	11.99	15.64	21.69
transfers (revenue+capital) as % of total expenditure	40.91	36.47	36.67	39.85

Important Indicators of Municipal Financial Health

2003-04	Hyderabad	Indore	Guwahati	Raipur	Jaipur
Own revenue receipts as % of total revenue receipts	67.50	52.19	63.09	40.47	20.29
State transfers as a % of total revenue receipts	32.50	47.81	36.91	59.53	79.71
Property tax as a % of own revenue receipts	42.76	51.28	0.00	40.44	30.06
Non-tax as a % of own revenue receipts	43.52	30.51	0.00	33.71	69.94
Revenue expenditure as a % of total expenditure	62.57	67.83	100.00	51.61	74.98
Capital expenditure as a % of total expenditure	37.43	32.17	0.00	48.39	25.02
establishment expenditure as a % of revenue expenditure	44.63	36.96	63.03	70.05	72.87
O&M expenditure as a % of revenue expenditure	51.49	63.04	21.93	28.58	23.74
Debt servicing as a % of revenue expenditure	3.87	5.67	0.00	1.37	3.40
Own revenue receipts as a % of revenue expenditure	116.77	55.47	46.29	41.79	24.34
Own revenue (w/o octroi) as a % of revenue expenditure	116.77	55.47	46.29	41.79	24.34
capital grants as % of capital expenditure	20.20	1.29	#DIV/0!	67.37	0.00
transfers (revenue+capital) as % of total expenditure	42.73	37.63	30.05	68.14	76.73

CONCLUSIONS-GENERAL

- Municipalities can not be compared merely on the basis of per capita incomes and expenditures.
- Municipalities differ because of their Fiscal and Functional Domain.
- Across States and within States bigger municipalities have larger functional domain and larger control over their tax and non-tax administration.
- State Municipal Acts also differ in allotting tax powers and functions between Municipal Corporations and Municipalities.
- Reforms initiated in developed states have started giving positive results.
- Reforms-Tax reforms, Cost cutting exercises, Involvement of Private sector in technological innovations

CONCLUSIONS-City Based

- Self sufficiency is indicated by the lower state dependency and higher coverage of expenditure from own resources.
- To improve the financial health of a city:
 - Increase Revenue base, Competitive Revenue structure, Time based Rate revisions
 - Introduction of user charges.
 - Using all its statutory powers to impose taxes, charges, fees and fines etc.
 - Bridging the gap between service costs and service pricing.
 - Reduce establishment costs which leads to improved operation and maintenance and developmental activities.
 - Community participation should be encouraged in staff oriented services.
 - Debt servicing ratio should be low.
 - Involve private sector participation to instill competition and to bring about technological innovations.