



Technical Assistance Report

Project Number: 43214-01
Policy and Advisory Technical Assistance (PATA)
August 2009

India: India Municipal Finance Study
(Financed by the Republic of Korea e-Asia and Knowledge
Partnership Fund)

CURRENCY EQUIVALENTS

(as of 27 July 2009)

Currency Unit	--	Indian rupee/s (Re/Rs)
Re1.00	=	\$0.0207
\$1.00	=	Rs48.23

ABBREVIATIONS

ADB	–	Asian Development Bank
KIPF	–	Korean Institute of Public Finance
MOF	–	Ministry of Finance
NIPFP	–	National Institute of Public Finance and Policy
TA	–	technical assistance
ULB	–	urban local body
VAT	–	value-added tax

TECHNICAL ASSISTANCE CLASSIFICATION

Type	–	Policy and advisory technical assistance (PATA)
Targeting Classification	–	General intervention
Sector (subsector)	–	Public sector management (public expenditure and fiscal management)
Themes (subthemes)	–	Governance (economic and financial governance), capacity development (institutional development)
Location impact	–	Urban (medium)

NOTES

- (i) In this report, "\$" refers to US dollars.
- (ii) The fiscal year (FY) of the Government and its agencies ends on 31 March. FY before a calendar year denotes the year in which the fiscal year begins, e.g., FY2008 begins on 1 April 2008 and ends on 31 March 2009

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I. INTRODUCTION

1. Urban infrastructure constraints have become a bottleneck for India's rapid economic growth rate. When urbanizing is occurring rapidly without proper infrastructure, the urban environment rapidly deteriorates, risking the health of inhabitants. Most urban local bodies (ULBs) depend on intergovernmental fiscal transfers for their existence. This condition is not encouraging, as India has to accelerate urban infrastructure development on a sustainable and larger scale. Lack of periodic revision of municipal tax rates and user charges, and poor information systems and records management are some of the basic weaknesses in the present municipal administration. India's local governments are plagued by low municipal revenue compared with other emerging economies. This leads to the questions as to what afflicts the finances of municipalities in India, what options exist for strengthening their finances, and what the experiences are in other countries that can provide insights for local finance in India.

2. The midterm appraisal of the 10th Five-Year Plan¹ highlighted public finance issues requiring urgent attention, including extremely low revenues, poor service delivery, high level of deficit, and the need to upgrade infrastructure facilities. These issues continue to be included in the 11th Five-Year Plan (FY2007–FY2011). Closely aligned with the priorities of the 11th Five-Year Plan, the draft country partnership strategy (2009–2012) of the Asian Development Bank (ADB) emphasizes (i) supporting infrastructure development, (ii) catalyzing investment through public–private partnership or nonsovereign operations, and (iii) overall improvement of development effectiveness. ADB's long-term strategic framework 2008–2020 (Strategy 2020)² also indicates the urban sector as one of the key outcome areas for development effectiveness. Building the strength of urban local financing is a crucial factor for enhancing the effectiveness of infrastructure-led operations and outputs toward the Strategy 2020 results framework. The proposed technical assistance (TA) is closely linked to the Strategy 2020.

3. The Government of India has requested a TA from ADB for addressing the issues of municipal finance of Indian cities and municipalities to enhance their capacities in providing urban infrastructure and services. The TA³ is classified as category A. A fact-finding mission was carried out intermittently during 8–21 July 2009 to formulate the proposed TA. The mission met and consulted with government officials from the Ministry of Finance (MOF), municipal finance experts, academics, and knowledge partners for the TA. Discussing further details of the TA, the mission reached an understanding with the Government on the purpose, output, methodology, key activities, cost estimates and financing plan, and implementation arrangements. The design and monitoring framework is in Appendix 1.

II. ISSUES

4. The country is rapidly urbanizing (2.4% annual rate of increase in urban population while population grows at a rate of 1.5%) and at least 100 million people more are expected to be added to urban areas for the next decade. The estimates by the Government of India shows⁴ that nearly \$475 billion will be required for funding the required infrastructure development

¹ The 10th Five-Year Plan covers FY2002–FY2006. The essence of the plan is to change the role and improve the effectiveness of government, improve governance, reduce poverty, increase the economic growth rate, and improve the productive base and infrastructure. The increased growth rate required fiscal adjustment at both the central and state levels, as well as reform of the financial system.

² ADB. 2008. *Strategy 2020: The Long-Term Strategy of the Asian Development Bank 2008–2020*. Manila.

³ The TA first appeared in the business opportunities section of ADB's website on 2 July 2009.

⁴ ADB. 2007. *India: Country Operations Business Plan (2008–2010)*. Manila. The Government's estimation was for the total infrastructure investment needs, including urban sector.

programs just for the next 5 years. Given the large resource requirement for infrastructure investment, the Government will have to rely on the public–private partnership model for financing and operating infrastructure facilities.

5. Municipalities of India are largely classified into three groups: (i) larger urban areas (populations of more than 1 million) governed by municipal corporations; (ii) medium-sized urban areas (population size of 200,000 but less than 1 million) governed by municipal councils; and (iii) smaller urban areas in transition from rural to urban areas (population size less than 200,000) governed by town councils. These categories are based on the types of governance organization permitted by laws and regulations. Municipal corporations usually exercise a good degree of fiscal autonomy and powers as they have a larger population and tax base, and deal with state governments directly. Municipalities with smaller jurisdictions have to deal with the state governments through the district collectors.⁵ As the revenue collection and sharing procedure differs by state government, exploring these intergovernmental fiscal relationships, procedures, and mechanisms may provide important insights into the limited access of ULBs to resources

6. Indian ULBs are third tier administrative divisions, responsible for providing basic infrastructure and services in cities and towns. In 2001, there were 5,161 cities and towns in the country. Under the 74th Constitutional Amendment Act of 1992, an initiative was launched to decentralize power and strengthen democracy at the local level. It provided ULBs with political, functional, and fiscal empowerment for good governance. Yet, more often than not, it is observed that current local government bodies—particularly small and medium-sized ULBs—have poor fiscal competencies and capacities to exercise devolved power. Mobilizing domestic resources or debt financing for urban infrastructure investments is difficult because, invariably, ULBs have very low credit ratings (if they can be considered for creditworthiness) due to fiscal weaknesses. The fiscal strength and sustainability of ULBs are at the core of financing the provision of sustainable urban infrastructure. It is important to review and analyze in-depth whether fiscal decentralization has been adequately placed to pursue effective urban development at the ULB level.

7. Meanwhile, state governments have made municipal laws grounded on the 74th Constitutional Amendment Act of 1992, and each state has varying degrees of conformity with the legislation in terms of what are obligatory or discretionary functions of municipal bodies within each state. These differences tend to create certain deviations from the principles of efficient allocation of resources across different levels of the governmental administration functions; i.e., under the theory of fiscal federalism, certain roles and functions are better placed in the lower tiers of government while some can be more efficiently delivered by higher levels of government. Thus, it is equally important to study whether (i) service provision and revenue generation and collection remain within the same jurisdiction, and (ii) efficient resources are allocated according to the economic principles of municipal financing.

8. Justification for the proposed TA stems from the fact that previous studies that have been conducted on this topic have been routine, comprising at most a bare analysis of municipal revenue and expenditure, with little insight into the underlying causes of stagnation in the finances of municipalities. Currently, no municipal fiscal policy exists in India. Due to the absence of a basic reference document, efforts to build capacities in the sphere of municipal finance have been ad hoc and perfunctory. ADB's assistance on public financing during the late 1980s and 1990s contributed to a major change in federal fiscal relations with regard to

⁵ District collectors (or magistrates) handle law and order, revenue collection, taxation, control of planning permission, and response to emergencies.

introducing state value-added tax (VAT). Recently, all the state governments have adopted VAT and there is a proposal to move towards a goods and services tax starting in April 2010. Some ULBs have taken steps to reform property tax issues.⁶ These initiatives have a multiplier effect in the improvement of taxes. However, issues of India's municipal financing have hardly been addressed in a holistic manner; they have been addressed in a fragmented way as the municipal capacity building component of urban infrastructure projects. A vast knowledge gap needs to be bridged.

9. Advanced decentralized Asian economies may provide insights into possible directions for further reforms in this sphere. Thus, promoting a partnership would be useful in filling the knowledge gap. A *Wall Street Journal* article⁷ summarized a recent study funded by the World Bank, *The Growth Report: Strategies for Sustained Growth and Inclusive Development*, wherein only six fast-growth countries were recognized as truly having become high-income industrialized economies: those are the four East Asian Tigers—Hong Kong, China; the Republic of Korea; Singapore; and Taipei, China. Among these emerging economies,⁸ the Republic of Korea is the only one that has a research institution dedicated to public finance (it is in conjunction with the Ministry of Strategy and Finance of the Republic of Korea). Knowledge partnership between such institutions in the Republic of Korea and in India would be conducive to networking and cross-learning.

10. A number of important initiatives have been taken in India to strengthen the finances of municipalities and to simultaneously identify areas needing attention: (i) the Jawaharlal Nehru National Urban Renewal Mission was launched, with one of the key aims being the fiscal empowerment of municipalities; (ii) the Reserve Bank of India has constituted a working group comprising the state finance secretaries and a few experts to consider additional reforms; and (iii) a high-powered expert committee⁹ was constituted to review the physical and financial norms of urban infrastructure services, and to suggest a model for financing such services. To support various initiatives by the Government of India in enhancing local public financing, the TA aims to review and analyze municipal financing in a holistic manner.

III. THE TECHNICAL ASSISTANCE

A. Impact and Outcome

11. The long-term goal of this TA is to assist the Government in formulating a feasible direction for the fiscal reform program by assessing the fiscal decentralization and budget and revenue systems at the municipal level. The expected impact is improved fiscal and financial performance of ULBs, which can be monitored through the increased share of municipal expenditure as a percentage of total gross domestic product, combined with the increased ratio of own resources to municipal expenditure.

12. The immediate purposes of this proposal are to provide a holistic view of the issues of the municipal finance structure and/or system, and to identify key reform measures of municipal

⁶ An example of that is the Bangalore Municipal Corporation. In Gujarat, octroi has been abolished, and the state government now permits an additional 1% levy on the VAT to compensate the urban local bodies for the loss resulting from octroi abolition.

⁷ *Wall Street Journal*. 2008. How Nations Become Rich. 22 May.

⁸ Hong Kong, China and Singapore are city-states, and these two city-state countries have a governance structure that is relatively more simple than the others.

⁹ On 14 May 2008, the Government of India constituted a high-level policy advisory group called the High-Powered Expert Committee on Urban Infrastructure. It is also expected to review the experiences of "emerging market" countries to identify innovative ideas and solutions for the massive urban infrastructure challenges facing India.

finance in India's rapidly changing urban context. The expected outcomes of the proposed study are key reform measures and options that enable municipalities to function more effectively in the provision of urban infrastructure. Recommendations on short- and long-term institutional reform agendas and capacity development areas, together with a road map, can support some reform measures that would follow after the TA..

B. Methodology and Key Activities

13. In general, a study on municipal financing can be very broad, and requires extensive time and effort. Given the scale of challenges in India and the limited resources available under the TA, it is important to limit the scope of the TA to the most important issues. The study will focus on representative samples of 30 municipalities in 4–6 selected states with different levels of economic development and differing geography. Prevailing municipal acts will be considered when selecting sample ULBs. An eminent international expert on public finance will be engaged to guide the focus of the study. The TA will establish a knowledge-sharing platform with a prominent public finance research institution in the Republic of Korea, through which the Indian study team can access a broader knowledge-base of practices in Organisation for Economic Co-operation and Development countries. Further, resource persons will be invited at critical times to discuss policy measures and reform options, and join one of the national or subregional forums or international workshops. The expected outputs of the study and activities are as follows:

- (i) Component 1: Review overall issues and assess the sustainability of municipal finance in India, accompanied by recommendations for municipal fiscal policy and reform agendas.
- (ii) Component 2: Broaden the knowledge base regarding the municipal governments' fiscal and financial system through international good practices and knowledge partnership.
- (iii) Component 3: Increase awareness and build consensus in the political arena on the need for municipal finance reform.

14. The study will be implemented over 18 months starting on 1 September 2009 and ending by 28 February 2011. The TA will conduct the following activities: (i) literature survey; (ii) a macro analysis of municipal finances in India; (iii) detailed analysis in 4–6 states; (iv) case studies from three Asian countries and one developed country; (v) one international workshop, one national forum, one subregional forum, and a series of small local consultation meetings; and (vi) reports and publications.

C. Cost and Financing

15. The total cost of delivering the outputs of the proposed TA is \$670,000. The TA will be financed on a grant basis, in an amount equivalent to \$500,000, by the Republic of Korea e-Asia and Knowledge Partnership Fund, and will be administered by ADB. The Government of India will finance office space, miscellaneous administrative support, remuneration of government officials involved in the study, and other necessary facilities as in-kind expenses, equivalent to \$170,000. The detailed cost estimates and financing plan for the TA are in Appendix 2.

D. Implementation Arrangements

16. The Department of Economic Affairs of the MOF will be the executing agency for the TA. The TA underscores the importance of a potential policy reform agenda for which the TA has to consult closely with ministries and the Reserve Bank of India. In addition, the nature of the study

requires a highly regarded national institution that can access various levels of local data, for which international consultants will rely on adequately qualified domestic consultants. The National Institute of Public Finance and Policy (NIPFP)¹⁰ is such an institution; it is a center for applied research in public finance and public policy. As an apex institution to the MOF, the NIPFP's research has been influential in policy making on this subject in India. Therefore, the NIPFP is both strategically well-positioned and practically advantageous for the study. The TA will use the single source selection method for consultant selection, on a firm basis, to get the most qualified research institution in India in accordance with ADB's *Guidelines on the Use of Consultants* (2007, as amended from time to time). The proceeds of the TA will be disbursed in line with ADB's *Technical Assistance Disbursement Handbook*.¹¹

17. The TA requires 50 person-months of inputs. An additional 2 person-months input from an eminent international expert advisor on public finance will be required to work with the NIPFP at critical points, such as formulating the study direction, devising policy measures, and finalizing the report. The international expert advisor will be engaged intermittently on an individual basis in accordance with ADB's *Guidelines on the Use of Consultants*. ADB will also engage a maximum of three prominent global experts on public and municipal finance, in consultation with the India study team, as resource persons. These experts will advise on overall study, particularly policy measures and reform options that exist globally, by recommending effective actions for development of a reform agenda for India's municipal finance. ADB will engage these resource persons according to its guidelines. The NIPFP will provide the list of potential candidates for ADB's endorsement and recruitment. Appendix 3 includes the outline terms of reference.

18. The TA will form an experts advisory group, composed of 5–6 experts selected from the members of the working group of the Reserve Bank of India, members of the high-powered expert committee, a globally eminent international expert advisor in public finance, an expert from the Korean Institute of Public Finance, and the director of the NIPFP as well as the principal team leader of NIPFP. ADB's principal task manager will participate in key meetings from time to time, upon request by the experts advisory group. Also, a knowledge-sharing platform will be arranged through a prominent public finance research institution in the Republic of Korea, through which the Indian study team can access broader knowledge. The Republic of Korea's experience in devolved municipal financing can facilitate NIPFP learning practices relevant to India's context. A workshop will be conducted in the Republic of Korea, which will be attended by an Indian delegation of a maximum of 20 persons, including the experts advisory group, senior policy makers on municipal finance, and core members of the NIPFP study team.

IV. THE PRESIDENT'S DECISION

19. The President, acting under the authority delegated by the Board, has approved ADB administering technical assistance not exceeding the equivalent of \$500,000 to the Government of India to be financed on a grant basis by the Republic of Korea e-Asia and Knowledge Partnership Fund for the India Municipal Finance Study, and hereby reports this action to the Board.

¹⁰ The NIPFP maintains its independence in its research activities, and raises funds for its research activities from the central and state governments, as well as from international and bilateral organizations. The main aim of the NIPFP is to contribute to policy making relating to public economics. The NIPFP has made important contributions to reforming the tax system and in designing the VAT. It is one of the three nodal agencies responsible for appraising the Jawaharlal Nehru National Urban Renewal Mission agenda. It is involved in a number of studies for the 13th Finance Commission, including one on property taxation (<http://www.saneinetwork.net/directory/Institutes/aspgenerator.asp?FI=MI&directory=43>).

¹¹ ADB. 2008. *Technical Assistance Disbursement Handbook*. Manila.

DESIGN AND MONITORING FRAMEWORK

Design Summary	Performance Targets/Indicators	Data Sources/ Reporting Mechanisms	Assumptions and Risks
<p>Impact Improved fiscal and financial performance of ULBs</p>	<p>Increased share of municipal expenditure as percentage of total GDP, combined with increased ratio of own resources to municipal expenditure</p>	<p>Government reports Reserve Bank of India reports CPS update</p>	<p>Assumption Government of India is keen to improve local municipal financing in pursuing inclusive growth</p>
<p>Outcome Identification of key reform measures and options for ULBs effective functioning to provide urban services and infrastructure</p>	<p>Reform recommendations submitted to MOF/MOUD Study results disseminated to ULBs as a reference document Better understanding and knowledge of urban finance via 3–4 publications</p>	<p>TA final reports Findings of review missions</p>	<p>Assumptions Stakeholders are committed to improving institutional fiscal capacities State governments are interested in strengthening municipal local financing</p>
<p>Outputs 1. Component 1: Review overall issues and assess the sustainability of municipal finance in India, accompanied by suggestions for a municipal fiscal policy and reform agenda (within India) 2. Component 2: Broaden knowledge-base regarding the municipal governments' fiscal and financial system through international good practices and knowledge partnership 3. Component 3: Reports documenting cases of increased awareness and consensus built on the need for municipal finance reform</p>	<p>Mapping of existing municipal financing arrangements for all three categories of ULBs from 4-6 sample states Knowledge partnership signed with an expert institution in Asia on municipal financing Assessment of existing municipal finance system against international best practices Workshop report Proceedings of final forum recording the discussions and consultations on the key reform agenda and ways to move forward based on recommendations</p>	<p>Workshop report Proceedings of forum Minutes of meetings from the local government consultations Field survey data report</p>	<p>Assumptions Good cooperation between the consultant and counterpart staff Series of discussions provide a good venue for government officials to discuss openly and to increase awareness on municipal finance issues Consultation with sufficiently high-level policy makers Risks Government officials are too busy to join consultation Unwillingness of municipal governments to share information and data</p>

Activities with Milestones	Inputs
Literature survey (September–November 2009)	Republic of Korea e-Asia and Knowledge
A macro analysis of municipal finances in India (December 2009–April 2010)	Partnership Fund:
Detailed work in states and series of small local consultation meetings for survey (April–October 2010)	\$500,000
Case studies from three Asian countries and one developed country (April–October 2010)	Government: \$170,000
International workshop (April 2010)	Korean Institute of Public Finance's in-kind inputs under a partnership agreement
Workshop proceedings (October 2010)	National consultants: 50 person-months of inputs
Two national forums (June 2010, and February 2011); the second forum is a subregional forum for advocacy and wider dissemination of the outputs:	International consultant: 2 person-months of inputs
(i) Inception report (October 2009),	Resource persons: 30 person-days
(ii) Interim report (April 2010),	
(iii) Workshop proceedings (October 2010),	
(iv) Two national forums (June 2010 and February 2011),	
(v) Draft final report (November 2010), and	
(vi) Final report (February 2011).	

ADB = Asian Development Bank, CPS = country partnership strategy, GDP = gross domestic product, MOF = Ministry of Finance, MOUD = Ministry of Urban Development, TA = technical assistance, ULB = urban local body.

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Total Cost
A. Republic of Korea e-Asia and Knowledge Partnership Fund^a	
1. Consultants (NIPFP)	
a. Remuneration and Per Diem (NIPFP consultants)	165.0
b. International and Domestic Travel	20.0
c. Reports and Communications	4.0
2. International Consultant and Resource Speakers	
a. Remuneration and Per Diem (international expert advisor)	48.0
b. Honorarium and Per Diem (international resource persons)	27.0
c. International and Domestic Travel	24.0
d. Reports and Communications	2.0
3. Surveys and Consultation Roundtables (data collection and consultations)	32.0
4. Seminars, Forum, and Workshop	
a. India-based forum for the midterm and final results (30 officials and costs of venue/equipment)	20.0
b. International workshop for knowledge sharing (travel and accommodations for the Government delegation)	80.0
c. Publications and Disseminations	10.0
5. Innovative Knowledge Partnerships	30.0
6. Miscellaneous Administration and Support Costs	6.6
7. Equipment	0.0
8. Contingencies (6.3%) ^b	31.4
Subtotal (A)	500.0
B. Government Financing	
1. Office, Forum Venues, Accommodation Facilities, and Local Transport	60.0
2. Remuneration for the Counterpart Staff	60.0
3. Miscellaneous Administration and Support Costs	18.0
4. Contingencies (10%)	32.0
Subtotal (B)	170.0
Total (A+B)	670.0

NIPFP = National Institute of Public Finance and Policy.

^a Administered by the Asian Development Bank.

^b Contingencies for activity items 2, 4, 5, and 6 only. Activity item 1 for NIPFP's contingency is budgeted under the Government financing.

Source: Asian Development Bank estimates.

OUTLINE TERMS OF REFERENCE FOR CONSULTANTS

1. The technical assistance (TA) aims to holistically review and analyze India's municipal financing, including (i) overall fiscal sustainability, (ii) local revenue sources and financial management of urban local bodies (ULBs), (iii) financing local expenditure, (iv) intergovernmental fiscal relations, and (v) local tax or other instruments to finance the provision of urban services and maintenance. Crucial issues pertaining to the finances that derived from the country's federalism need to be considered systematically and professionally.

A. International Expert Advisor (public finance expert; 2 person-months)

2. **Key Responsibility.** The international expert advisor will work with the principal team leader and National Institute of Public Finance and Policy (NIPFP) study team to support and advise on the initial preparation of the study structure and to assist in final report preparation, ensuring the technical quality of outputs. The advisor will also provide advice (from the home office via the internet) to the NIPFP and the experts advisory group on the overall approach of the study, and participate in national forums as a facilitator.

3. **Qualifications.** Over 20 years of experience is expected in public finance, government fiscal relationships, and associated topics. At least 10 years of working experience is expected in developed as well as developing countries in municipal finance. The international expert advisor is expected to have gained practical knowledge on public finance or municipal financing through international consultancy work or as an employee or an advisor in government or in the public sector for a minimum of 5 years. It is required that the international expert advisor should have a post-graduate degree in public finance, public administration, economic development, or relevant fields, with expertise demonstrated through research articles or publications.

4. **Detailed Tasks.** While closely coordinating with the Asian Development Bank (ADB) task manager and the principal team leader of the NIPFP, the international expert advisor will undertake tasks which include, but are not limited to, the following:

- (i) Work with the experts advisory group to set up an appropriate study framework, including samples and categories of ULBs and states to analyze current problems and bottlenecks in India's local financing, where the results and findings can be generalized;
- (ii) Advise the NIPFP study team on determining detailed activities of the study, literature reviews, methodology, subtopics to be addressed, types of analytical methodology, and data collection requirements, to produce an implementation working plan (technical substance as well as time bound action plan) for the study;
- (iii) Review, revise, and comment on the study reports, technical quality of the assessment, and the results;
- (iv) Participate in one of the national forums as a facilitator;
- (v) Join the meetings of experts advisory group through teleconference or internet; and
- (vi) Communicate and discuss with the principal team leader of the NIPFP study team, on a constant basis through the internet.

5. **Key Deliverables.** An advisory note regarding an initial framework for the study direction, and a high-quality draft final report in coordination with the NIPFP study team.

B. International Resource Persons (three public finance experts; total 30 person-days)

6. **Key Responsibilities.** The main purpose of engaging international public finance experts as resource persons for the TA are to provide: (i) the Indian study team with a broader exposure to relevant international experience as well as in-depth analytical guidelines for the study, and (ii) expert opinions and advice to the experts advisory group on alternative policy measures and reform options that exist globally to improve India's municipal finances. In this regard, the subject research materials are less on academic or purely theoretical research and more on (i) practical experiences or applied research demonstrating successful or failed cases, identifying the best solutions or criteria in a given context; (ii) examples of fiscal federalism; and (iii) decentralized fiscal relationships in different countries.

7. **Key Qualifications.** More than 20 years of professional experience and post-graduate degrees in public administration, municipal financing, public finance, public economics, and/or related fields are expected, as is having held senior positions in highly regarded research institutions in countries with advanced economies. Demonstration of applied research on subjects covering both developed and developing countries is preferable.

8. **Detailed Tasks.** The resource persons will undertake the following tasks while closely coordinating with the experts advisory group and the principal team leader of the NIPFP study team:

- (i) Upon invitation, provide an abstract of the appropriate cases or key studies and findings as a sign of confirming acceptance to participate;
- (ii) Advise the team leader of the NIPFP team and experts advisory group on overall directions and key issues, including weaknesses, key bottlenecks to be eliminated, and support in mapping out a potential reform agenda in a structured way with a time-bound action plan;
- (iii) Participate in one of the national forums or international workshop as resource speakers;
- (iv) Actively participate in experts advisory group meetings as appropriate and as requested to provide expert opinions and interpretation for policy and system improvements, through information technology connections; and
- (v) Upon the conclusion of the final forum, provide a report of expert opinions, relevant to improving India's municipal financing system.

9. The key deliverables are:

- (i) a draft working paper and presentation materials for the final forum; and
- (ii) a final briefing paper on the critical bottlenecks of India municipal financing, time-bound action plans at the macro level, and policy advice to the Government of India.

C. Korean Institute of Public Finance

10. **Qualification.** The Korean Institute of Public Finance (KIPF) was established in 1992 for the purpose of policy-oriented research and analysis on all aspects of taxation and public finance. Since its inception, the institute has played a critical role in developing tax and budget policies, improving tax administration, and recommending policy alternatives. The KIPF recognizes the importance of in-depth research and the impact of various policy alternatives or tax and/or fiscal tools for a sound economic environment in a globalized and open economy. Although the Government of the Republic of Korea is not based on federalism, it introduced local autonomy in the late 1980s. Progress and lessons learned over the last two decades can provide valuable insights into India's current problems in improving municipal financing

conditions. Further, the KIPF covers everything about public finance, with highly competent researchers (about 30 professional staff with doctorates in relevant fields) who have international exposure. The KIPF's various research areas on Organisation for Economic Co-operation and Development countries' municipal financing can facilitate the NIPFP's access to globally available knowledge and practices relevant to India's context. Therefore, the TA proposes a knowledge partnership with the KIPF to conduct a workshop in the Republic of Korea. The key research areas of the KIPF include:

- (i) tax system and tax administration,
- (ii) international taxation,
- (iii) tax systems in the era of local autonomy,
- (iv) fiscal policy and government expenditure,
- (v) consultation,
- (vi) contract research, and
- (vii) others (such as conducting special long-term projects such as a history of Korean tax policy, which reflects 50 years of tax policies of the Republic of Korea and the productivity of the public sector).

11. **Key Responsibilities.** The KIPF, as a highly specialized research institution on public finance, will conduct a workshop in the Republic of Korea for Indian delegates, in coordination with, and sponsored by, the Asian Development Bank (ADB). ADB will support the logistics required for inviting Indian government officials, in coordination with the NIPFP, while the KIPF is expected to focus on developing the substantive contents of the workshop program and venue arrangement in the Republic of Korea. The KIPF's key responsibilities are to

- (i) mutually share interesting and relevant knowledge products with the NIPFP, on a constant basis, as a knowledge platform on the subject of municipal finance;
- (ii) undertake a high-quality workshop on municipal financing issues;
- (iii) provide KIPF's staff as resource speakers who can share the experiences of challenges faced in the introduction of local autonomy in the early 1990s; and
- (iv) provide a summary report of the workshops, focusing on lessons learned from the Republic of Korea's municipal financing systems, and discuss recommendations.

12. **Detailed Tasks.** The KIPF will designate a qualified professional researcher and supporting staff as a focal point to closely coordinate the following tasks with the ADB task manager and the NIPFP:

- (i) Provide existing literature available on, and follow-up with, the ongoing assessment of India's municipal financing study, conducted by the NIPFP under the TA, to understand the status of India's municipal financing conditions;
- (ii) Identify the objectives and issues to be addressed during the ADB-sponsored workshop for a maximum of 20 Indian delegates involved in the TA study;
- (iii) Formulate the most optimal workshop program, structure, format, and appropriate time, considering a maximum program of 4 days including field visits, based on the issues identified in items (i) and (ii); draft and finalize the program in consultation with the ADB task manager and the NIPFP;
- (iv) Provide additional qualified staff to take notes in English from discussions during the conference, and help draft a summary report by professional experts of the KIPF for all the sessions of the workshop, focusing on key discussions, challenges, and recommendations;

- (v) Assist the ADB task manager in producing workshop proceedings (in English) by compiling the presentation materials and papers, reflecting the recommendations and conclusions of the workshop;
- (vi) The director of fiscal research at the KIPF will serve as a member of the experts advisory group, in an advisory role through internet and telephone calls, as needed;
- (vii) The KIPF provides advisory functions to the study team from time to time through the internet, supplementing global knowledge and Organisation for Economic Co-operation and Development experience; and
- (viii) The KIPF and NIPFP will seek a potential knowledge partnership during the TA implementation to make this engagement sustainable in the longer term.

13. The key deliverables (all in English) are as follows:

- (i) A preliminary draft report identifying key issues to be addressed during the 4-day workshop, and associated program, detailing workshop format, field visits, and time-bound preparation action plan;
- (ii) Draft summary notes of the discussion held during the workshop; and
- (iii) Adequate contribution (as a co-author) in supporting the ADB task manager to convert the workshop proceedings into a publication.

D. National Institute of Public Finance and Policy

14. **Key Responsibility.** The NIPFP will be: (i) the primary investigator and researcher for the proposed TA (the India Municipal Finance Study); (ii) advised by the international expert advisor to undertake the subject matter holistically; (iii) responsible for coordinating, informing, and consulting with relevant parties involved throughout the study, such as the executing agency, government officials, local governments of study areas, the experts advisory group, international expert advisor, and the ADB task manager; (iv) responsible for providing relevant data, draft report, review materials as necessary in obtaining appropriate advice from the international expert advisor and the KIPF; and (v) the leader in undertaking a series of consultations, experts advisory group meetings, and the planned national forum.

15. **Qualifications.** The proposed research institution should be able to demonstrate its history of close relationship with the relevant ministries and the Reserve Bank of India for the study. The main aim of the NIPFP is to contribute to policy making related to public economics. The nature of the study requires a highly regarded national institution which can access various levels of policy makers, and state and local data (for which the international consultants will rely on adequately qualified national consultants). In addition, as an institution responsible for monitoring the Jawaharlal Nehru National Urban Renewal Mission reform for the Ministry of Finance, the NIPFP's research has been influential for policy makers in India. Therefore, the NIPFP is strategically well-positioned as well as practically advantageous; its qualifications are unique. The TA will use the single source selection method for consultant selection to get the most qualified research institution in India. The NIPFP is already identified as the most suitable candidate for applied research in public finance and public policy.

16. **The Key Roles of the Experts Advisory Group.** In consultation with ADB, NIPFP will form an experts advisory group to: (i) lead the overall progress of the study; (ii) direct the study approach and the methodology; (iii) establish the framework and selection criteria for states and cities, and case studies in the Asian context; (iv) lead policy dialogue between or across intergovernmental and/or ULBs as needed to enhance the relevance of the study at the policy level; (v) be responsible for integrating appropriate theoretical ground, advanced knowledge, and international experiences throughout the study; and (vi) guide the study team to formulate

recommendations on municipal financing policy and reform options to be presented at the final forum in Delhi.

17. **Detailed Tasks.** The NIPFP will undertake the following activities:

- (i) Review municipal financing theories, international practices, and India's current practices of municipal finance;
- (ii) Review literature on fiscal decentralization to pursue effective urban development at the ULB level;
- (iii) Work with the international expert advisor and experts advisory group in determining detailed activities of the study, methodology, subtopics to be addressed, types of analytical methodology, and data collection requirements, to produce an implementation working plan (technical substance as well as time-bound action plan), and prepare the reports of the study;
- (iv) Prepare study reports, and feasible options to be considered by the Government of India;
- (v) Consult with government agencies, coordinate experts advisory group meetings for guidance, and disseminate the findings to the public and stakeholders for consensus building throughout the study;
- (vi) Conduct local consultation and data collection as required for the study.
- (vii) Prepare and conduct two forums (one national and one subregional) at appropriate times to inform, consult, and build consensus on study findings and municipal reform issues;
- (viii) Actively pursue advice and share knowledge with the international resource persons or the KIPF;
- (ix) Organize local meetings, national forums, and the international workshop in the Republic of Korea in coordination with the KIPF and ADB; and
- (x) Analyze and assess the areas and topics suggested below, while seeking advice from the international expert advisor, international resource persons, and the knowledge shared with the KIPF, to strengthen the outcomes of the study:
 - (a) A literature survey to become familiar with the role of municipal finance in developing and developed countries; policies governing municipal finances; the importance of municipal finance; and municipal tax jurisdiction. Provide ideas on the precise nature of questions that the study needs to probe, and generate ideas on the analytical architecture of the study.
 - (b) A macro analysis of municipal finances in India, focusing on (i) policy with regard to the finances of municipalities; (ii) typologies of their functions, i.e., regulatory, enforcement, service provision, etc.; and (iii) nature and dimension of municipal finances, i.e., tax, nontax, transfers, and grants on the revenue side; and capital versus recurrent expenditure, wages and establishment, service provision on the expenditure side. A macro analysis may also look at the market or creditworthiness. It will be a data-based component.
 - (c) Detailed work in 4–6 states. Guided by the expert advisory group, the NIPFP will develop criteria for the selection of states. It will be a detailed study and probe where the weakness and strengths of the current systems lie and look at the impact of parastatal agencies on the functioning and finances of municipalities.
 - (d) Case studies from three Asian countries and one non-Asian developed country which is a member country of ADB. These case studies are seen

as city-specific and may focus on how the finances of municipalities are attended to—such as administrative procedures, capacities, internal communication, management and governance—as well as the financial strengths and weakness, sources of revenues, and the allocation of revenues for different services (i.e., budgeting), among other things. Clearly, the messages of such cases will be on the changes that can be brought about in the Indian system. Each case study will take 6 weeks, and will be conducted by local national consultants.

18. The key deliverables are as follows:

- (i) inception report (October 2009),
- (ii) interim report (April 2010),
- (iii) workshop proceedings (October 2010),
- (iv) two national forums (June 2010, and February 2011),
- (v) draft final report (November 2010), and
- (vi) final report (February 2011).

19. **Suggested Assessment Subtopics.** The proposal aims to assess the status, issues, challenges, and opportunities for improvement in municipal finance in a holistic way. It is suggested that the NIPFP considers the study framework for sustainable urban financing and the associated reform agenda to be structured systematically by, but not restricted to, addressing the following review areas:

- (i) **Budget management to enhance fiduciary control.** Municipal laws prescribe the resource-raising powers and budgeting, accounting, and auditing procedures to be followed by ULBs. These procedures do not meet modern standards for fiduciary control and also differ considerably across states. Preferably, the budgetary process, accounting and auditing standards, procedures, and codes should be set nationally, as in the case of the accounts of the central and state governments. Budget and financial control reforms should aim for segregation of revenue and capital budgets, adoption of accrual-based accounts, cash planning and budgeting, centralized financial control, development of core investment plans to ensure adequate allocation of resources for priority projects, development of a project cost system, financial forecasting models, and a reliable financial management information system.
- (ii) **Tax and nontax revenue reforms to strengthen financing resources.** Property tax and octroi tax reforms are an immediate imperative. The scope to introduce new taxes, such as the vacant land tax, and development fees could be explored. The TA could also look at the scope for assignment of taxes from the state governments. Nontax revenues, which are a form of benefit taxes, are the most efficient ways to raise revenues at ULBs. But reforms are difficult; particularly because the existing cost recovery rates are low. The feasibility of various options could be assessed, i.e., a tiered tariff structure, the gradual increase in tariffs by fully passing on incremental costs, constitution of regulatory authorities to depoliticize tariff setting, linking resource flows from the state governments to performance in cost recovery, and making tariff reforms mandatory for accessing loans from domestic and international financial institutions.

- (iii) **Fiscal sustainability and prioritizing expenditures.** Assessment of financial resources should cover whether government expenditure is used, or whether it is being used for its intended purposes. Inefficiencies regarding spending allocations across sectors, weaknesses in procurement, and the accountability framework are also identified. What are the main drivers of ULBs public expenditures? Accordingly, some financing options can be considered for medium- and longer-term frameworks. As the immediate need for public spending in most ULBs is immense, an analysis of expenditure patterns and trends precedes an option on how to determine priority expenditure across and within sectors. Often forgotten questions for fiscal sustainability assessment are: (a) What is the right sequencing between competing priorities?; and (b) What are the most effective interventions?
- (iv) **Political, legal, and institutional matters.** A rational realignment of the resources and responsibilities of ULBs would be needed for them to properly deliver public services mandated under the 74th Constitutional Amendment Act of 1992 on a sustainable basis. This requires an in-depth study and suggestions on some feasible options for the state governments to rationalize location and distribution of resources, policy making, and executive powers to enhance the delivery of public services. The reform options could seek to achieve, through a national consensus, a degree of uniformity in the basic framework for (a) division of responsibilities and resources between the state governments and ULBs, (b) institutional arrangements for setting service delivery standards and addressing vertical and horizontal fiscal imbalances, and (c) measures to improve the political accountability of ULBs as mandated under the Constitution. Typically these reforms are time consuming and need considerable intergovernmental consensus, agreement, and coordination. The NIPFP could suggest (a) the ground to be covered; (b) how to proceed; (c) sequencing of steps; and (d) a feasible timetable in consultation with the experts advisory group, the international expert advisor, and the KIPF.