

## Section 3

# Expenditure assignments as the foundation for the system of financing local governments in Tanzania

The logical starting point for the exploration of any system of local government finances is to determine what functions and activities that should be funded at the local government level. With respect to expenditure assignments, the study's TORs request the current study to:

- Review any documentation of the functions and responsibilities of each level of government authority, including the lower-level local governments. (TOR 2.2 [iii] )
- quantify the total revenue required by each level of Local Government Authority in order to fulfill its obligations and perform its assigned functions. (TOR 2.2 [v(a)] ).

As already noted in Section 1 of the Final Report, we believe that a broad consideration of expenditure assignments in Tanzania should be an integral component of the study. In fact, expenditure assignments play a more important role in creating a sound framework for local government finance than made apparent by the TORs. Reflecting the importance that we attach to assuring that the expenditure assignments are right is that the first fundamental principle which we believe is needed as a foundation for a sound local government finance system is that expenditure assignments form the foundation for a framework for local government finances, and that “finance should follow function.” In other words: it would be impossible to get the system of local government finance “right” if the expenditure responsibilities that the system should be funding are improperly assigned. In fact, failing to consider the expenditure assignment question in a comprehensive manner as an integral part of the local government finance system would perpetuate numerous problems in the realm of local finance which cut across the various dimensions of the intergovernmental fiscal structure.<sup>1</sup>

In many developing countries –including those that are pursuing decentralization reforms-, local governments often have few *de facto* expenditure responsibilities. However, the evolution of decentralization reforms in Tanzania since 1982 has given local authorities a true role in the expenditure and delivery of key public services, in the

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<sup>1</sup> For instance, having an ineffective and incomplete assignment of expenditure responsibilities contribute to reduced revenue performance for local governments. Likewise, a comprehensive and clear assignment of expenditure responsibilities is needed as the basis for a sound system of intergovernmental fiscal transfers.

context of a relatively sound legal framework. Section 3.1 will review the local government structure and assess the appropriateness of expenditure assignments in Tanzania. Once the appropriateness of the expenditure assignments has been determined, Section 3.2 will consider in principle how different types of locally-provided government goods should be funded. Next, Section 3.3 explores the resource requirements for local governments in Tanzania. Section 3.4 contains concluding remarks and recommendations.

## **3.1 The local government structure and expenditure assignments in Tanzania**

### 3.1.1 Local government structure: the context for considering expenditure assignment

Before we can assess the appropriateness of expenditure assignments in Tanzania, we should consider Tanzania's current structure of subnational government, including the number of government levels, the size of subnational jurisdictions, and so on. Although we consider the local government structure as part of our broader evaluation (e.g., see the first row of Table 1.4), the subnational government structure was considered an exogenous factor during the formulation of the local government finance framework.

Nonetheless, we believe that the current local government structure in Tanzania provides an appropriate basis for moving forward. As the most important level for provision of local government services, district and urban councils are generally of an adequate size and have sufficient administrative capacity to operate as local government jurisdictions and to assure the delivery of the range of public services assigned to them. The facilitative role of the Regional Administrations (as opposed to their previous more hierarchical role) is appropriate and is seemingly allowing local governments greater control over their own affairs in recent years without regional interference.

Like many developing countries, Tanzania is facing tension between providing local government services by jurisdictions that are generally too large on one hand (thereby risking a lack of correspondence and local accountability) and providing local government services by jurisdictions that are generally too small (thereby risking inefficiencies due to scale economies and inadequate administrative capacity) on the other hand. Along this spectrum, Tanzania has made the prudent choice to assign the bulk of local responsibilities to the district level, while the village/mtaa level currently plays a minor role in the delivery of services and local infrastructure; the role of the village level is likely to increase in the future.<sup>2</sup>

### 3.1.2 Principles of a sound expenditure assignment

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<sup>2</sup> The Mtaa committee will become legal entity (body corporate) with the Budget Law for next year, allowing it to take on a stronger role within the overall local government system in urban areas.

The main principle of a sound expenditure assignment is the concept of “subsidiarity”, which requires that government services are provided at the lowest government level that is able to do so efficiently.<sup>3</sup> Although there is no single “best” manner in which to assign expenditure responsibilities across different local government levels, there are a number of steps that should be followed in the assignment of expenditure responsibilities (Martinez-Vazquez, 1998):

1. Determine the appropriate roles of the public and private sectors.
2. Establish a formal assignment of expenditure responsibilities - and do this before determining the other components of the system of intergovernmental fiscal relations. The lack of a clear, formal (legislated) expenditure assignment –or conflicts in the legislative framework- is a common shortcoming of fiscal decentralization reforms.
3. Follow the subsidiarity principle in assigning the allocation function:
  - Assign the responsibility to fund distributive programs to the central government.
  - Assign the responsibility to provide the stabilization function to the central government.
  - The subsidiarity principle and the nature of market failure should determine which level of government is best situated to ensure the efficient provision of other government services.
4. Assure that the expenditure assignment recognizes the multi-dimensional nature of expenditure responsibilities, including the responsibility to set policy norms and regulations; to finance; to provide; and to produce a certain government service.
5. Assure that the legislative framework is consistent and is clear in assigning the responsibilities of the various government levels, especially when different aspects of a functional responsibility are shared by different government levels. Then assure that the legislative framework is followed in practice.
6. Ensure that minimum standards of local service provision are assured via penalties and rewards, and make sure that local governments operate in a framework in which they are accountable.

### 3.1.3 Assessment of expenditure assignments in Tanzania

According to the legislative framework, local governments in Tanzania play an important role in the delivery of government services, as they are assigned the responsibility to deliver key public services such as primary education, basic health services, and other typical “local” public services. In addition, the *de facto* expenditure assignments closely match their legislated expenditure responsibilities. As a result, 20 percent of public expenditures are made at the local government level.

The responsibilities that are assigned to the local government level in Tanzania are typically “local” services, and the assignment of expenditure responsibilities generally

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<sup>3</sup> See Martinez-Vazquez (1998) for a discussion on the sound assignment of expenditure responsibilities.

follow the subsidiarity principle and broadly coincide with sound principles of expenditure assignment. Nonetheless, there are a number of shortcomings in the current assignment of expenditure responsibilities in Tanzania.

Perhaps the most important shortcoming of expenditure assignments in Tanzania is that the current assignment of expenditure responsibilities in the Local Government Acts is one-dimensional. By failing to consider the multi-dimensional nature of expenditure assignments, the legislative framework does not distinguish between national functions for which the provision is devolved to the local government level; functions that are fully devolve to the local government level; and functions that are merely delegated to the local government level. In the absence of this distinction, it is unclear which level of government is responsible for funding the various responsibilities for which provision is assigned to the local government level (see Box 3.1).<sup>4</sup> As further discussed in Section 3.2, the exact nature of the expenditure assignment determines how a function or activity should be funded.

**Box 3.1**  
**Feedback from the Second Stakeholder Workshop (May 2005)**

The second stakeholder workshop on the development of a strategic framework for local government finances –held in Dar es Salaam in May 2005- was presented with the following statement for discussion and debate: “The assignment of expenditure responsibilities in Tanzania should be clarified. The legislative framework should clearly state for each local responsibility which level of government is responsible for (1) policy/regulation, (2) financing, (3) provision, and (4) production.”

Unanimous agreement and consensus exists with regard to this statement.

The discussion group that focused on this statement came up with a classification of expenditure responsibilities based on a number of key functions, such as primary education, basic health services, and so forth. It was noted that the assignment of functions requires a great deal of specificity, certainly beyond the main functional level. This study team believes that the legislative framework indeed should be clarified in this manner.

A point was also raised that there exists confusion surrounding the assignment of secondary schools, to the extent that currently LGAs are required to fund the development of secondary schools, while this is not currently a local government function.

The assignment of responsibilities in the DSM region requires greater attention in the expenditure assignment framework. While the DSM CC is intended to represent all constituent municipalities, in fact, it does not play this role. For instance, while the CC sits on the water board, the municipalities have significant issues.

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<sup>4</sup> In practice, there appears to be a relatively widespread degree of consensus about which local government activities are “truly local activities” (local markets, and so on), which functions are national functions where provision is devolved to LGAs (primary education, basic health, and other priority sectors) and functions that are delegated (e.g., contagious diseases).

A second important concern with the current expenditure assignments in Tanzania is the role of local government administration. In the current system, local government administration is a burden predominantly borne by LGAs themselves. At the same time, the Local Government Finance Act provides for a central government matching grant for local government administrative staff above a certain pay grade, although it appears in reality that the cost of personal emoluments for local administrative staff are in fact fully funded from central government resources. While there is no comprehensive picture of local government spending patterns, the available evidence from various selected LGAs suggests that local governments in Tanzania spend somewhere between 50-60% of their own source revenues on local administration. The fact that these own resources have to be generated locally for local administration without translating into services that directly benefit local residents has been identified as a major area of concern for local residents and taxpayers. In fact, based on survey evidence, certain studies have placed the blame for the low value-for-money at the local level from own resources on local officials; local officials are essentially accused of wasting local resources on administrative functions. However, it may simply be the case that in the absence of adequate funding for administrative tasks from alternative resources (e.g., intergovernmental transfers), local governments have no choice but to spend a large proportion of own revenues towards the cost of operating the local authority. If the latter is the case –and local communities are asked to bear a disproportionate share of the cost of local administration- then this would have significant negative reverberations throughout the system of local government finance that is beyond the fault of local governments themselves.<sup>5</sup>

Another set of concerns with the current expenditure assignments in Tanzania regard a number of secondary issues; although these problems in expenditure assignments may be serious in their own right, these problems are not likely to have system-wide effects on local government finances. Such concerns include the following:

- A real question should be raised whether the delivery of secondary education is appropriately assigned to the central government level. Given the prior failures of centralized primary education and the relative success of decentralized delivery of primary education, it is hard to justify the centralized provision of secondary education directly by the Ministry of Education and Culture. This debate should take on special prominence given the recent ramping up of funding for the Secondary Education Development Program. In fact, to the extent that as part of the budget formulation process for FY 2005/06 funding is actively being diverted away from primary education at the local level towards secondary education to be controlled by MOEC, one cannot help but wonder whether political motives have overtaken true policy objectives and concerns about service delivery.

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<sup>5</sup> To some extent, the introduction of the unconditional Compensation Grant / General Purpose Grant in the aftermath of the local revenue rationalizations of 2003 and 2004 should have offset this problem. This issue will be pursued further in Sections 4 and 5 of this report.

- Although the principle of decentralization by devolution is clearly articulated in the legislative framework and local governments receive a significant portion of their funding through the sectoral allocation mechanisms under the regional PO-RALG votes (Votes 70-95), this does not mean that there is universal acceptance of the role of local governments in the providing government services assigned to the local government level. Central government line ministries continue to assert a role for themselves within the responsibilities assigned by law to the local government level, often citing weak local government capacity as a reason for continued central government involvement. Within the health sector, the Ministry of Health continues to provide in-kind transfers of medicines to LGAs rather than devolving greater flexibility to local health authorities. The decentralization of local water services envisions the production of potable water by the private sector (water corporations, local water board, and/or local user groups), although the sector's *modus operandi* appears to be more one of deconcentration than devolution; for instance, the majority of local water board members are appointed by the sectoral minister as opposed to the relevant local council.<sup>6</sup> Likewise, the highly discretionary "hands-on" role played by PO-RALG in managing the local share of the Roads Board Fund also seems to contravene the assignment of the responsibility for maintaining local roads to the local level. The disbursement of the roads funds to PO-RALG rather than directly to the local governments clearly and unnecessarily diminishes local governments' role in exercising their functional responsibilities. The same concern (central micro-management of local government affairs) is raised by the earmarked provision of funding for urban fire-fighting services through the Administration Grant.
- A final issue of concern in expenditure assignments in Tanzania is the special role of the Dar es Salaam City Council vis-à-vis the three municipal councils in the DSM region. In order for "finance to follow function" it is imperative that the functions of the City Council relative to the municipalities are more clearly defined in the legislative framework.

#### 3.1.4 Achieving expenditure autonomy and accountability at the local government level

One of the biggest challenges in the realm of expenditure assignment has been the ongoing struggle to assure greater local government control over the actual delivery of services. Although local governments have been legally responsible for delivering key public services since the mid 1980s, until recently, the central government was able to micro-manage local government expenditure decisions through the highly discretionary transfer system. The center's control over local finances is now slowly being diminished as formula-based recurrent sectoral grants are being introduced. Instead, the center is improving its ability to properly exercise regulatory control over local budget decisions (i.e., in a less discretionary manner) through the local budget guidelines.

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<sup>6</sup> The intrusion of central government in the management of residential water supplies in Dar es Salaam in May 2005 certainly seems to be inconsistent with a decentralized approach to service delivery in the water sector.

Possibly the last bastion of excessive central government control over local administration and delivery of services is through its control over the placement of local public servants. The fact that the center continues to exercise control over the placement of teachers and other local staff has major implications for the system of local government finance.<sup>7</sup> Despite the revision of the Public Service Act in 2004, PO-PSM continues to approve local staff positions without consideration as to whether local governments are able to afford the staff in the context of their formula-based grants. This is a major hindrance in fully implementing the formula-based transfer system. Therefore it is a key priority for the Ministry of Finance and PO-RALG to engage PO-PSM and bring local government staffing issues in compliance with the formula-based grant system.

Of course, in order to secure the benefits from local budget autonomy, local governments should operate in a transparent and accountable manner in a way that responds to local needs and preferences. Yet, many critics of decentralization have argued that local governments have insufficient capacity and lack accountability to ensure the sound delivery of public services. The available data do not support this conclusion; as a result, we strongly disagree with this contention. A series of recent opinion surveys suggests that there is a lack of public trust in local governments, which leads the author's to be highly critical of local governments' role in public finances (e.g., Fjeldstad 2004; REPOA/CMI, 2004). However, none of this work provides comparative data for the quality of services delivered by the central government, so we are simply not able to conclude whether the alleged poor performance of local governments is any different from the quality of central government services, or whether the shortcomings of local government services are simply caused by a broader lack of public resources (which potentially reduces the quality of services at both the central as well as the local government level). Nor do the studies isolate the negative impacts of shortcomings in the design of the overall local government finance system (for instance, the inadequate assignment of expenditure responsibilities for local administration as discussed above) which are simply beyond the control of the local government level. Although there is surely an ongoing need to build the capacity of local governments to be able to better plan and budget for the delivery of local government services, when properly financed, local authorities are clearly in a position to deliver services in a relatively effective manner. In fact, this assertion is supported by the survey data produced by the aforementioned studies. For instance, in a recent survey, an overwhelming majority of local residents (70.1%) expressed satisfaction with the local delivery of primary education services (Fjeldstad, 2004: Table 15). Although comparable data are not available for central government services, it is unlikely that citizens are equally satisfied with any public service provided by the central government. It is therefore simply untenable to suggest that local governments have insufficient capacity or are insufficiently accountable to effectively deliver key local government services. Institutional and administrative aspects of assuring a participatory

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<sup>7</sup> If local staff are placed without local consent, then local governments cannot necessarily be expected to pay for these staff from their formula-based sectoral grant. This issue is discussed by LGRP/GSU. 2003. Technical Notes on Local Government Finance Reform in Tanzania: The design of formula-based recurrent block grant system and the role of personal emoluments (Technical Note 2).

and accountable budget process at the local government level are further considered in Section 7 of this report.

### **3.2 How to fund different types of local government goods?**

When expenditure assignments are understood to form the foundation for a framework for local government finances, in order for “finance to follow function”, both intergovernmental transfers and own local revenues should play important but distinct roles in the system of local government finance. Thus, the first key question in designing a local government finance strategy should be: what determines how each local government activity should be funded?

According to a broad consensus among public finance experts and international best practices, the appropriate funding mechanism for any publicly provided good at the subnational level is determined by the subsidiarity principle, which states that government services should be provided (and financed) at the lowest level of government that can do so efficiently.<sup>8</sup> Following this principle, we can broadly classify four types of local government expenditures:

- Government services that are provided at the local government level but that are national policy priorities (or otherwise not exclusively local in nature).
- Government services that are provided at the local government level but that are exclusively local in nature.
- Expenditures on local government administration.
- Capital development that is provided at the local government level. Again we can distinguish between capital development spending that is exclusively local in nature, and projects that are not exclusively local in nature.

The appropriate funding mechanism for each of these four categories of local expenditures is determined by the reason why the public sector is providing the good in the first place.<sup>9</sup>

***National policy priorities.*** Local governments in Tanzania are responsible for delivering a number of services that, while they are provided (delivered) at the local government level, these activities are not exclusively local in nature. Examples of such activities include the provision of primary education, council health services, water, agricultural extension, and local road maintenance. Although it is appropriate for these services to be delivered by the local government level (because they are in a better position to deliver these services than the central bureaucracy), it would not be appropriate for these sectoral

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<sup>8</sup> See Martinez-Vazquez (1998) for a broader discussion on the subsidiarity principle and expenditure assignments.

<sup>9</sup> While conceptually it is appropriate to say that certain activities should be funded through different financing modalities, this does not mean that local governments should in fact funnel money through a system of different local government bank accounts. Local government financial management issues are discussed later in this section.



services to be funded at the local government level because these are national policy priorities. It is appropriate to fund these sectoral expenditures from central government resources (through some type of conditional transfers) because all these programs either involve (1) a significant element of poverty reduction which justifies central government funding, or (2) significant spillover effects to national policy objectives, such as national economic growth, or both.<sup>10</sup>

For instance, while providing a child with a primary education provides direct benefits to the child and his/her community, in many ways the benefits of primary education are felt nationwide through a better educated workforce and improved economic productivity and a more literate, healthier population, resulting in higher national tax collections, lower spending on poverty reduction programs and health care, and so forth. At the same time, central government funding of primary education assures equal access to primary education to all Tanzanians, an important element of the government poverty reduction strategy. Likewise, health services, water provision, agricultural extension, and local road maintenance can all be justified as having either positive spillover effects or significant redistributive impacts.

Indeed, the stakeholders' workshop held in January 2005 concluded that for the priority sectors, "decentralization by devolution" in Tanzania should be interpreted as devolution of provision, so that the central government will continue to have responsibility for determining sector policies, setting service delivery standards, and providing financing to fund the provision of services at the local government level (see Section 1.4 of this Final Report). As such, the provision in the Local Government Finance Act that provides central government funding for these activities through intergovernmental grants –and the actual provision of funding through formula-based sectoral block grants- is fully consistent with sound decentralization principles and practices. The provision of sectoral block grants is further discussed in greater details in Section 3.3.

***Truly "local" government services.*** In addition to providing a number of national services at the local level, local governments in Tanzania are responsible for delivering a number of services that are not only delivered at the local government level, but are in fact exclusively local in nature. Examples of such local activities include local refuse collection, street cleaning, parks and recreation activities, community activities, and so forth. Such services are provided by the public sector either because they are local public goods (the enjoyment of a local park is neither rival nor excludable) or because they are what economists refer to as club goods.<sup>11</sup>

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<sup>10</sup> The expenditure assignment literature is clear that under the subsidiarity principle, the financing of income redistribution (including poverty reduction activities) generally cannot be achieved in an efficient manner with funding from own local revenue sources. Likewise, to the extent that the benefits from a locally-delivered service are felt outside the local jurisdiction or nationwide, these activities should (partially or wholly) be funded from higher government levels.

<sup>11</sup> A public good is a good or service that is non-rival and non-excludable. Non-rival means that one person can enjoy the benefits of a good without reducing the benefit received by others; non-excludable means that a person cannot be excluded (or it is prohibitively expensive to exclude him/her) from enjoying the benefits of the good. Club goods are private (i.e., rival and excludable) goods and services that are provided by local

Since the benefits of these activities exclusively befall the local community, it would therefore be appropriate for the local community to pay for these activities from its general budgetary resources, which include its own source revenues supplemented by unconditional transfers received from the center. While conceptually it would be best to pay for such local activities through local benefit taxes, there are two reasons why own source revenues may have to be supplemented with unconditional grants. First, the revenue sources assigned to the local level may not yield adequate revenues to fund the “truly local” expenditure responsibilities assigned to local governments; as such, unconditional grants can be used to assure vertical fiscal balance. Second, if exclusively local government services would be exclusively funded from own source revenues, this could lead to horizontal fiscal imbalances.

The issue of horizontal fiscal balance is a valid concern when considering whether local government activities should be funded from general budgetary resources at the local level (which currently consists mostly of own source revenues). There are three arguments that could be made that might mitigate this concern. First, as the local services in question are non-priority in nature (especially when compared to primary education or basic health services), it is in fact not inappropriate to allow variations in service delivery across local government jurisdictions with wealthier local jurisdictions being able to provide somewhat better services than poorer local governments. After all, allowing variations in the mix of local services offered among jurisdictions is required in order to achieve the efficiency benefit of a decentralized system. Second, it is worthwhile to note that the demand for many of the local services under consideration is more closely connected to the economic base of a jurisdiction rather than to the population of the locality. For instance, the need for street cleaning and public refuse collection tends to increase proportionally with the level of economic activity (especially around markets), so that funding these activities from own source revenues assures that there is a correspondence between the demand for this local service and the resources provided by the funding mechanism. A third factor mitigating the equity concern of locally-funded activities is that, as we discuss further in Section 5 of this report, we recommend transforming the General Purpose Grant into a genuine equalizing, unconditional grant scheme. Introduction of an equalizing GPG would assure greater horizontal fiscal balance while ensuring revenue autonomy for local governments that are able to raise adequate own source revenues from local sources.<sup>12</sup>

***Local administration expenditures.*** Another question that has been the source of some concern in Tanzania’s current system of local government is whether local administration is in fact a local government affair -and thus should be funded from own local sources-, or whether the cost of local government administration should be considered as part of the national realm of expenditure responsibilities. As noted in Section 3.1, the Local

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governments because they can be provided more cost-effectively when produced for a group of residents instead of a single household.

<sup>12</sup> Note that the current General Purpose Grant is currently (notionally) distributed in accordance with the revenues lost due to the revenue rationalizations of 2003 and 2004. As such, the GPG is currently likely counter-equalizing.

Government Acts determine that local government administration is a local government function, although part of local administrative costs are defrayed by the central funding of local administrative salaries.

There are three problems with the current legislated funding mechanisms used to finance local government administration, concerning both the efficiency and equity of the system. First, since local taxpayers are interested in paying for local services that provide a direct benefit to the local community, their incentive to pay for administrative overhead is extremely low. Thus requiring local governments to self-fund a significant part of their administrative cost reduces local taxpayer compliance, which will ultimately result in suboptimal funding for local government administration and for other local services.<sup>13</sup> Second, the current approach to funding local government administration is potentially inequitable, since matching grants will favor wealthier districts in setting up better (or at least, better funded) local government administration. Additionally, the horizontal allocation of administrative personnel has historically taken place in an extremely discretionary manner, which has resulted in large variations in administrative grants between LGAs. Third, and perhaps most importantly, it would be fair to consider local government administration as an integral part of the national administrative infrastructure, as an important part of its functions is to oversee and provide national public services. In this context, it should be noted that a large majority of expenditures at the local government level (ranging from 80-90 percent in most councils) is spent on national priority programs. Therefore, although local administration is clearly a local government function, there is a strong case for local administration to be financed (in large part or wholly) with central government funds. However, this should be done without rigid earmarked financing tied to existing personnel posts in local administrations.

Since assuring devolved local provision and production of local administration is the best way to safeguard local autonomy, we recommend that local administrative activities should be viewed as local in nature and should be funded from general local resources. However, to prevent local governments from spending an excessively large share of local own source revenues on local administration, and in order to recognize the important role that local government administration plays in the infrastructure of the national public sector, it would be appropriate to assure that unconditional transfers are provided to LGAs in order to cover the cost of local administrative expenditures. By providing local governments with unconditional transfers to cover the basic cost of local government administration, LGAs should be able to provide their residents with much better “value for money” for programs funded from locally raised sources.<sup>14</sup>

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<sup>13</sup> Conversely, local government officials have a bureaucratic tendency to consider administration as a first charge. As a result, a majority of locally collected revenues are absorbed by local administration: for instance, see the studies on local public finances in Mbeya, Mtwara and Singinda (UUAP, 2001).

<sup>14</sup> To some extent, the current provision of GPG transfers already allows local governments to cover most or all local administrative expenditures from this unconditional grant. However, since the local revenue trend has been toward less rather than more revenue autonomy, fewer LGAs have been able to capitalize on the revenue reforms to increase local fiscal compliance.

***Local capital development projects.*** At the present time, there is no systematic financing system for the financing of local capital development expenditures, and only 4 percent of the Development Budget is passed more or less directly through to the local government level. Local capital development is funded through a number of –predominantly donor-driven- sources, including centrally earmarked transfers from the development budget for local projects, sectoral capital development programs (including classroom construction, health facility rehabilitation, and agricultural development programs) and area-based local development programs (ABPs). Many of these funding mechanisms require some co-funding (generally 10-20 percent) by local governments from own sources.<sup>15</sup> Some capital development funding is provided through the Local Government Loans Board (see Chapter 5 of the Local Government Fiscal Review).

There is consensus among economists that financing capital infrastructure from recurrent resources generally results in an under-provision of investment in public infrastructure. Instead, borrowing is an appropriate mechanism to pay for capital expenditures, as it allows the (local) government to restore the match, over time, between the costs and benefits of capital infrastructure (see Section 3.4). Yet, in the absence of well-developed capital markets and a sound framework for local government accounts, private financial institutions such as banks are often unwilling to lend to local governments as the risk of local government authorities defaulting on repayment is often considered high. Thus, in the absence of a well-functioning capital market, alternative mechanisms are needed to finance the capital development needs of subnational governments.

As such, in order to resolve the market-failure in capital markets for local government borrowing, we recommend that local capital development expenditures in Tanzania are funded from two sources. First, we should expect that a majority of LGAs in Tanzania are not in a sufficiently sound fiscal position to borrow and repay money for virtually any of their capital development needs any time in the near future: for these councils, an expanded system of capital development grants will need to be the predominant source of capital funding. Second, to the extent that councils in Tanzania are able to responsibly borrow resources –either through the LGLB or directly from the capital market- the framework for local government borrowing should be expanded appropriately to accommodate for this. To the extent that borrowing might be a feasible option for LGAs in Tanzania, the proposed framework for local government borrowing is discussed in greater detail in Section 3.4.

The first step towards a comprehensive, formula-based Local Government Capital Development Grant (CDG) system was made as part of the preparation for the World Bank credit under the Local Government Support Project (LGSP). It is expected that the CDG system will soon start providing essentially unconditional capital development grants to the local government level. Consistent with PO-RALG’s current Letter of Sector Policy -which clearly states that the CDG is to be the main mechanism for funding local capital development infrastructure- the CDG mechanism will be financed from government’s “own” resources, contributions from bilateral and multi-lateral donors, as

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<sup>15</sup> LGSP/PWC. 2004. Background Paper: Development Funding To Regions and Local Government Authorities.

well as loan proceeds from international financial institutions. The *Local Capital Development Grant System: Manual for the Assessment of Councils Against Minimum Conditions and Performance Measurement Criteria* (PORALG, 2004) provides a comprehensive description of the CDG. Section 3.3 (below) discusses the evolving role of capital grant funding in Tanzania's local government finance system.

### **3.3 The resource requirement for subnational governments**

The TORs (Section 2.2 (v)(a)) request the current study to quantify the amount of resources required by each subnational government level in order to fulfill its obligations and perform its assigned functions in terms of the Constitution, legislation, and national policies, particularly the poverty reduction strategy. Such a costing of each level's expenditure needs is useful to assure vertical fiscal balance in the system of intergovernmental fiscal relations.<sup>16</sup> However, before we proceed to quantify the expenditure needs of each government level for specific activities, it is important to consider the relative nature of public expenditure needs.

*The nature of public expenditure needs.* Determining the expenditure needs of different government levels in the public sector begins with the explicit recognition that public resources –and by extension, public resources available to the local government level- are always scarce. While it is tempting to believe that the expenditure needs of governments can be quantified in an objective manner, we need to recognize upfront that expenditure needs are, by their very nature, always relative to the resources available and never absolute. Even though a sector ministry may quantify its fiscal needs in terms of the cost of achieving certain desirable sectoral service delivery norms, this does not necessarily mean that the service norms are achievable within the resource constraint within which the government must operate. For instance, despite the desire of the Ministry of education to achieve a 40 to one student-teacher ratio, this does not necessarily mean that this norm is affordable given the other demands on the national budget. As such, any successful public expenditure management process needs to determine expenditure needs on a relative basis, which allows for the prioritization of budgetary resources among competing uses. As part of any budget process that recognizes the relative nature of expenditure needs, the central government will have to decide the most efficient use of any additional budgetary resources given the government strategic priorities.

In a sound budget process, the central government decides the overall size of the public sector through its macroeconomic (taxation and borrowing) policy decisions. As part of the government's broader fiscal policy strategy (which incorporates decisions on the tax system as well as the annual budget processes), the relative expenditure requirements of the local government level are implicitly determined by the revenue sources assigned to

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<sup>16</sup> Vertical fiscal balance is said to exist when there is a broad correspondence between the aggregate financial resources assigned to each level of government and relative expenditure responsibilities of each government level. Vertical fiscal imbbalance results when one government level receives a disproportionate amount of revenue sources compared to its expenditure responsibilities, and this imbalance is not corrected through the transfer system.

the local level, the vertical allocation of grant resources through the regional votes, and possibly, by the level of transfers from sector ministries and the development budget to local governments.

**Box 3.2**  
**Risks associated with absolute expenditure requirements**

Not only is a budget process that is anchored on the concept of absolute public expenditure requirements unlikely to produce a balanced budget, but more importantly, a decentralization strategy based on this principle raises the possibility of actually derailing the decentralization process.

When the national budget process quantifies the expenditure requirements of local governments in an absolute manner, this raises the expectations by local residents that these local services will be fully funded (one way or another) by the public sector. While disappointment with the decentralization process will ensue when subsequently the requisite resources for local government services turn out not to be available, it won't be necessarily clear who is at fault and who should be held accountable for this failure. Local government officials will, of course, blame the central government for inadequate funding. At the same time, opponents of decentralization at the central government level can exploit the failure of local governments to deliver public services as an argument to recentralize sectoral activities. As such, a decentralization approach that quantifies expenditure requirements based on absolute norms is unlikely to produce a sound and consistent basis for decentralization reform.

*The previous National Minimum Standards approach.* The National Minimum Standards approach to financing local governments previously used in Tanzania failed to recognize that local expenditure needs are never absolute. Under the NMS approach, the resource needs of each local government sector were determined based on “national minimum standards” (NMS) for local service-delivery.<sup>17</sup> These NMS generally reflected a desired level of service delivery (for instance, a desired student-teacher ratio of 45:1), without considering whether the service level was actually fiscally affordable from a budgetary viewpoint.<sup>18</sup> Since under the previous NMS system the quantification of expenditure needs was developed outside the context of the regular budget process, the formulation of the standards did not consider the overall affordability of the service delivery standards. As such, the NMS reflected policy goals that were not necessarily obtainable by local governments, rather than budget norms for which local governments could be held accountable.

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<sup>17</sup> See PWC. 2000. *Local Government Finance Reform: A System for the Financing of Local Government* for a description of the NMS approach. See LGRP Technical Note 2003-03 (“*Introducing formula-based block grants as an alternative to national minimum service standards*”) for a critique of the NMS approach.

<sup>18</sup> To further compound the problem, some standards may not even be objectively quantifiable in terms of expenditure needs.

While the use of budget norms or minimum standards is not uncommon, an ill-conceived NMS approach can be seriously detrimental to the decentralization process. On one hand, if the minimum standards are set too low, local services received by residents end up being poor and the nation will fail to achieve its national policy priority objectives. On the other hand, if the minimum standards set by the central government are in fact set too high and become unaffordable to local governments, this would set local governments up for failure. Excessively high NMS would also allow local government officials to pass the blame for inadequate local service delivery to the central government's inability to pass down adequate resources.

***The current national budget process and local resource needs.*** As part of the current system of formula-based sectoral block grants in Tanzania, the relative policy importance of the six main recurrent local government functions -and the associated level of funding made available to each local government function through the transfer mechanism- is determined at the Cabinet level as part of the annual Budget Frame based on the government's national policy priorities. By determining the sectoral budget envelopes for local government sectors up-front in the budget process, the process assures that local governments are able to develop realistic budget plans that fall within the resources available to the local government sector. As noted elsewhere in this report, sectoral allocations for local governments have grown over the past years in proportion to the rest of the national budget.

In practice, the budget formulation processes in Tanzania combine the realization that expenditure requirements are relative with the desire to achieve a well-defined absolute minimum level of public services. The relative prioritization of budget resources is achieved in the context of a cross-sectoral medium-term expenditure framework (MTEF) by first computing the absolute cost requirements for achieving desirable standards of service delivery across all sectors. As the next step in the budget formulation process, the Ministry of Finance determines how much of each sectoral expenditure requirement can be funded within the public resources available. Aggregate local government allocations (sectoral transfers) for primary education and other local government sectors are treated in a similar fashion. This allows policy makers to establish budget priorities based on how much of each sector's requirement is being funded. Although such comparisons may be helpful in identifying budget priorities between central government agencies as well as between central and local government programs, one has to interpret such analyses with extreme caution since the absolute expenditure requirements are determined in a very subjective manner. For instance, based on expenditure norm for primary education based on a student-teacher ratio of 45 students to 1 teacher (and other similar norms), one could conclude that Tanzania is currently fully funding its primary education requirement. However, if the Ministry of Education would redefine the expenditure norm for the student-teacher ratio to 30:1 or even 20:1, the very same analysis would show that the sector is grossly under-funded.

In addition to the analysis of expenditure requirements in the cross-sectoral MTEF, the Ministry of Finance rolled out a budget planning software in late 2004 that integrated a performance-based dimension into the central budget formulation process in the context

of the new poverty reduction strategy (PRS II/NSGRP). Whereas the previous poverty reduction strategy exclusively focused on poverty priority sectors, PRS II moves away from the sectoral approach by recognizing that not all expenditures within the priority sectors necessarily contribute to poverty reduction. Instead, the new PRS focuses on a cluster strategy approach. The major clusters of poverty reduction include (i) Improvement of quality of life and social well being; (ii) growth and reduction of income poverty; and (iii) governance and accountability. The new cluster-based approach does not mean that the sectoral nature of expenditures becomes irrelevant altogether, but it does mean that spending within sectors is further scrutinized to identify whether the resources are used to fund pro-poor activities. As part of the performance-based budget approach, line ministries need to indicate in the budget planning software to which extent specific budget items address pro-poor priority cluster activities. This will then assist the Ministry of Finance and Cabinet in prioritizing proposed sectoral expenditure programs. See Section 5 for a further discussion of the inclusion of intergovernmental transfers in the central government's budget formulation process.

In contrast to expenditures in the national priority sectors, which are predominantly funded from intergovernmental transfers, local non-priority budget expenditures are almost exclusively funded from own local revenue sources. As such, in practice the fiscal priority of these expenditure responsibilities is implicitly determined by the yield of the local revenue instruments that are made available to the local level, plus the amount of unconditional grants which are provided to the local government level. In this regard we should note that a substantial share (about 50-60%) of own local revenues are needed to cover local administrative expenses, thereby greatly limiting the amount of resources available for “truly local” expenditure activities. However, the under-funding of local expenditure programs does not necessarily give rise to unfunded mandates as local governments are able to respond by reducing the quality and level of local government services. (see Box 3.3)

**Box 3.3**  
**Alternative approaches to addressing the vertical resource needs of subnational governments**

Reaching vertical balance in a decentralized system is always a challenge, as international experience indicates; functions and revenues are provided to local governments in different combinations and with varying relationships between these two building blocks of local fiscal autonomy. Some countries address this challenge of achieving vertical fiscal balance by providing local governments with autonomous revenue sources and some clarity on expenditure functions. Local governments can then, for example, increase or decrease the tax rates of some significant taxes to raise adequate revenues for their stipulated expenditure responsibilities. Such a “revenue first” approach, with little follow-up on expenditure assignment, avoids vertical imbalances by definition, but this construction potentially can make it difficult for the national government to realize national interests and priorities through local government service delivery.

Other countries choose not to provide local revenue autonomy, and rely on alternative mechanisms to reach vertical balance at the local level. For instance, vertical fiscal imbalances



could be avoided by not defining in any concrete way the expenditure responsibilities of local governments or leaving quite open, that is subject to the availability of resources, the level at which concrete physical expenditure norms could be fulfilled. In essence, these approaches mean that local expenditure choices are made at the level and quality that available local resources allow in accordance with local priorities. This has been largely the experience of most transition countries in Central Europe and the former Soviet Union and it is also a common practice in Latin America.

*Source: Jorge Martinez-Vazquez, Jamie Boex and Gabe Ferrazzi. 2004. Linking expenditure assignments and intergovernmental grants in Indonesia. ISP Working Paper Number 04-05 (September).*

***Absolute resource requirements based on current national standards.*** There are two sources that provide guidance on the budgetary implications of an absolute approach to budget requirements. The first source is the report produced by PWC (2000) on a system for the financing of local governments based on the national minimum standards approach; the second source is the cross-sectoral MTEF produced by the Ministry of Finance for 2002.

The PWC report costs out, at a very high level of detail, the exact resource requirements for the delivery of local government services. For instance for the delivery of primary education, the proposed NMS approach costs out the fixed costs of running a District Education Office as well as the variable costs of primary education based on projected teacher costs (salaries and benefits) and the normative student-teacher ratio of 45 to one; their projected cost of material and equipment (including slates, books, and science kits); as well as the projected cost of in-service training of teachers (at local Teacher Resource Centers). Likewise, the report produced NSM estimates for the administrative cost of non-priority sectors based on national input requirements. Based on the computations by PWC (2000), local governments faced a substantial budget shortfall (of almost 50%) based on an absolute costing of their expenditure requirements, as shown in Table 3.1.

<b>Table 3.1</b>				
<b>Local expenditure requirements based on national minimum standards for service delivery</b>				
<b>(Tsh millions, 1998/99)</b>				
<b>Grant</b>	<b>Funding Required</b>	<b>Budget amount</b>	<b>Shortfall</b>	<b>Shortfall as % of Budget</b>
Education	126,240	81,910	44,330	54.1
Health	58,506	32,470	26,036	80.2
Roads	63,445	15,314	48,131	314.2
Water	2,030	1,755	275	15.7
Agriculture	6,111	4,200	1,911	45.5
<b>Total Conditional</b>	<b>256,332</b>	<b>135,649</b>	<b>120,683</b>	<b>89.0</b>

Unconditional	5,414	4,596	818	17.8
Total Grant Costs	261,746	140,245	121,501	86.6

Source: PWC (2000): Page A6.

A more optimistic picture is shown by the cross-sectoral MTEF for 2002. The MTEF summarizes the expenditure requirements for activities in the priority sectors in the public sector (for both the central and local government level), indicating that the expenditure norms for almost all sectors were fully funded. For instance, the budget plan suggests that the budget allocations made in the national budget for primary education cover 99% of the sector's expenditure needs, while the resources set aside for local health-care cover 96% of expenditure requirements. The fulfillment rates for the other local government sectors (including agriculture and livestock, water and local roads) are only slightly lower (Table 3.2). This means that unless the minimum standards are modified, in principle, local governments are currently receiving adequate amount of resources. If this were truly the case, the only adjustment that would have to be made from year-to-year would be to increase the transfer pool for local governments at the annual rate of inflation.

**Table 3.2**  
**Summary Of Funds Requirement And Proposed Allocation**  
**For Priority Activities In Priority Sectors**  
**(TSh millions, FY 2002/03)**

	<b>Funding Requirement</b>	<b>Proposed Allocation</b>	<b>Proposed Allocation as Percent of Requirements</b>
Education	403,979	396,067	98%
<i>o/w Basic Education</i>	<i>203,560</i>	<i>202,515</i>	<i>99%</i>
Health	192,226	171,848	89%
<i>o/w Primary Health</i>	<i>160,232</i>	<i>154,263</i>	<i>96%</i>
Water	100,228	93,978	94%
Law and Order	182,715	106,948	59%
Agriculture	85,512	71,548	84%
Roads	286,806	250,744	87%
<i>o/w Rural Roads</i>	<i>185,018</i>	<i>161,754</i>	<i>87%</i>
Other Sectors	246,340	201,383	82%
<b>TOTAL</b>	<b>1,497,806</b>	<b>1,292,516</b>	<b>86%</b>

Source: MOF. 2002. Cross-Sectoral MTEF 2002 (Table 5).

**Local resource requirements based on revealed policy preferences.** Although estimates of absolute expenditure requirements are helpful in determining local resource

requirements, their use is limited, as they fail to take into account the availability of resources for the public sector. Instead, a more practical approach considers that the policy decisions that are made as part of the central government budget process implicitly reveal how policy makers consider the priorities and needs of central government ministries, as well as local government authorities. Under this assumption, historical expenditure levels provide a useful guide in determining the relative resource requirements of the central government versus the local government level for the various expenditure responsibilities.

- *Expenditure requirements for priority sectors.* As discussed earlier in this section, sectoral block grants should provide the mainstay of funding for the delivery of local public services in the priority sectors in order to assure an “adequate” level of service delivery. In fact, no local contributions should be expected from own sources in order for local governments to achieve the desired “minimum service level”. If the local government financing framework would allow central government ministries to claim any part of a local governments own resources for sectoral purposes, this would quickly result in different sectoral ministries, laying competing claims over a local governments resource base, without any safeguards to the local authorities that anything will be left for their own purposes. Although at times, attempts are made by sector ministries to lay claim to local resources, in fact the Local Government Finance Act is clear that local services delivered within the priority sectors should be fully funded through the recurrent transfer system.<sup>19</sup> As such, the level of funding provided to the priority sectors in the national budget (as detailed in Section 2.2) gives an indication of the relative expenditure requirements for the local priority sectors (including primary education, health, agriculture and livestock, water, and roads). Survey evidence suggests that over two out of every three residents are satisfied with the quality of primary education services provided by their local authorities, whereas satisfaction with the other priority sectors is substantially less (Fjeldstad, 2004: Table 15). The government’s success in improving the quality of services for primary education is, no doubt, in large part due to the additional resources made available under the Primary Education Development program (PEDP). This success notwithstanding, the relatively low levels of satisfaction with other priority sectors may signal that future marginal resources should be shifted more towards the other priority sectors.<sup>20</sup>

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<sup>19</sup> For instance, some stakeholders in the roads sector recently suggested that district and village governments should contribute to the maintenance of local roads from their own resources. Others have proposed that perhaps intergovernmental transfers should be limited only to the PE portion of local government spending, and local governments should bear the cost of Other Charges. Another common opinion is that wealthier, local governments (for instance, the municipalities in Dar es Salaam) should receive fewer transfers for the priority sectors because they can contribute more from own resources. None of the suggestions would be consistent with the view that own resources should be used for general purpose local government activities outside the priority sectors.

<sup>20</sup> In addition, public expenditure tracking surveys have suggested that some of the resources earmarked for primary education and local health services are in fact being diverted for other purposes. To the extent that these resources are being used for legitimate local government expenditures, this would indicate that local governments believe that other priority sectors are being underfunded.

- *Expenditure requirements of local government activities outside the priority sectors.* Local governments have numerous expenditure responsibilities that fall outside the central government's priority sectors, which have to be funded from general purpose resources. These activities include the cost of local government administration; the cost of delivering “truly local” government services (such as refuse collection, community development activities, and so on); as well as the (co-)funding of local capital development projects. In the emerging framework for local government finance, local general purpose activities would be funded from two sources: unconditional grants, as well as own revenue sources. If we were to combine the general purpose resources currently available to the local government level, they would add up to approximately TSh 85 billion for FY 2004/05 (namely about TSh 45 billion in administration and general purpose grants combined, and approximately TSh 40 billion in own source revenues).

However, the degree of public satisfaction with truly local services (such as garbage collection or local markets) is among the lowest for all local delivered services, suggesting that the services are proportionally under-funded by the current system. Data from sample local governments indicate that local governments currently use approximately 60% of own resources for local administration alone (including staff salaries, sitting allowances for councilors, as well as other overhead costs), therefore leaving extremely few resources for the delivery of local services or for the funding of local capital development. Based on local collections for 2002, this would indicate that local governments spend approximately TSh 30 billion of their own resources on administrative costs.

Since in the absence of adequate untied grants local governments are forced to use most own local resources for local administration. The poor “value-for-money” received by local residents for their local taxes has contributed to extremely high rates of local tax evasion. This problem could be mitigated in the future by providing additional general purpose resources through the transfer mechanism, which would allow local authorities to use a higher proportion of own source revenues directly for services and infrastructure projects that benefit the local community.

- *Expenditure requirements for local capital development.* As noted in Section 1 of this report, local governments in Tanzania receive only extremely limited direct resources from the Development Budget for the purpose of local capital development. Similarly, local governments have been unable to rely on borrowing for the purpose of funding local capital development. As such, the historical spending levels for local capital development would provide limited guidance on the relative expenditure needs for local capital development spending.
- *Village-level expenditure responsibilities.* Likewise, very little is known about historical spending patterns at the village level. In fact, before we can truly engage in an informed discussion regarding the expenditure requirements for village level activities, we would have to clarify the expenditure responsibilities that are in fact assigned to the village level. However, based on the apparent practical division of

responsibilities between the districts and the lower-level local governments, and based on previous resource sharing arrangements between the two local government levels, one could infer that the aggregate expenditure requirements of the village level broadly fall in the range between 20-50 percent of all general-purpose local spending.

### **3.4 Recommendations**

Assuring that the assignment of expenditure responsibilities to LGAs in Tanzania follows sound principles and international best practices is a critical first step in a sound system of local government finance. A sound expenditure assignment is also needed to prevent a variety of cross-cutting problems in the system of intergovernmental fiscal relations. As part of the “next steps” in transforming the system of local government finance in Tanzania, a number of expenditure assignment issues should be addressed:<sup>21</sup>

#### Overall policy stance and policy effectiveness.

Generally, Tanzania’s policy stance of “decentralization by devolution” is the appropriate basis for expenditure assignments. Although there is an increasingly broad acceptance of devolved delivery of service through LGAs, not all sectoral policy programs are consistent with this government policy stance. On a sector-by-sector basis, PO-RALG, MOF, and the relevant sector ministries should review the *de facto* expenditure assignments (especially within the priority sectors) to make sure that the expenditure assignments are consistent with the policy paper on local government reform and the subsidiarity principle (see Section 3.1.3). Part of this review should consider whether the provision of secondary education should in fact be devolved to the local government level. On a sector-by-sector basis, recommendations should be made on how to move forward by transforming improper expenditure assignments in accordance with the principle of “decentralization by devolution.”

#### Constitutional and legal framework.

The legislative framework needs to be reviewed and revised as needed to assure that the legislative framework for local government (finance) recognize the multi-dimensional nature of expenditure assignments, since “decentralization by devolution” means different things for different locally-provided services. For every expenditure function assigned (in part) to the local government level, the legislative framework should indicate which level of government is responsible for policy and regulation; finance; provision;

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<sup>21</sup> These “next steps” are organized in accordance with the categories used in Table 1.4.

and production.<sup>22</sup> Whenever the central government is responsible for the financing of government services provided at the local government level, the Local Government Finance Act should also clarify which mechanism ought to be used to provide the local government level with the necessary resources.

#### Central government institutional and regulatory framework.

Next, the regulatory framework and central government's budgetary practices should make sure that "finance follows function". This means that:

- a. To the extent that the provision of national (priority sector) functions is devolved to the local level, these sectoral activities should be funded through sectoral block grants, and not through earmarked parallel funding mechanisms in ministerial budgets. Unfunded mandates should not be created by establishing "minimum required services standards" which are unaffordable based on the total level of funding provided through the sectoral block grants.
- b. The responsibility for local government administration should be assigned to the local government level, and should be fully funded from unconditional grants.
- c. Functions that are fully devolved to the local government level should be funded from general local budgetary resources, which include locally generated revenues (own source revenues) plus unconditional grants provided by the central government. Since these functions are assigned fully to the local government level, such local services should not be subject to mandatory minimum service standards by the central government.
- d. Functions that are delegated to the local level (i.e., that are explicitly not devolved to the local government level) should be funded through earmarked ministerial subventions.

In order to assure that the regulatory framework and central government's budgetary practices assure that "finance follows function", two concrete actions need to be taken.

First, PO-RALG, MOF, and the relevant sector ministries should produce a comprehensive mapping of finances that flow to the local government level. This mapping should identify every funding stream (including in-kind transfers) that flows to the local government level, as well as the purpose of each funding mechanism. Such an

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<sup>22</sup> Alternatively, the legislation may classify which functions are delegated to the local government level; for which functions only provision is devolved; and which functions are fully devolved to the LGA level (as classified in Table 1.3).

inventory of local financing instruments is needed to verify that local government expenditure assignments are funded through the correct funding modality.

Second, it is essential that the regulatory framework and administrative arrangements at the central government level assure that LGAs have adequate administrative control over the functions assigned to the local government level. In practice, the largest obstacle to local administrative control over the delivery of local services is the excessive control by central government ministries over local staffing decisions. While legislative steps have been taken to revise the Public Service Act in line with a decentralized framework, proactive coordination is needed between PO-RALG, PO-PSM and Ministry of Finance to assure that in practice local governments are indeed able to make local staffing decisions within the context of the resources available to them (see Section 5).

Local government institutional and regulatory framework; participation by civil society and private sector

In order to realize the benefits from decentralization, a sound (transparent and accountable) local expenditure management is needed. Improvements are needed in the local budget processes and the monitoring and reporting of local government finances to assure greater transparency and accountability. The institutional and administrative dimensions of local government finance –including the need for participatory and accountable local government budget processes- are further addressed in Section 7 of this report.