UNIT 3 MUNICIPAL FINANCE IN INDIA

Structure

3.1 INTRODUCTION

It should be explicitly recognised that urbanisation is a natural consequence of economic development and cities contribute far more to national economic growth than their share in total population. They contribute significantly to the country's national income and exchequer. Therefore, urban policy needs to enable cities to contribute to national development through the effective provision of infrastructure and services. This, however, cannot be viewed in isolation from broader economic and social policies. These policies lead to unintended spatial consequences, which may sometimes be far more profound than those intended or envisaged originally. In view of the above, the approach to urban development and management needs to take account of the likely impacts of multiple sectoral and spatial policies at Central, State and Local Government levels. Municipal finance reforms will have to be undertaken within the ambit of these policies and the structure of fiscal federalism in India. This unit deals in details the status of municipal finance in India. After reading this unit you would be able to:

- Explain the importance of Municipal Finance in Urban Development.
- Give an overview of the Municipal Finance in India.
- Describe the mechanisms to improve Municipal Revenue.

3.2 IMPORTANCE OF MUNICIPAL FINANCE IN URBAN DEVELOPMENT

Urban Local Bodies directly influence the welfare of the people by providing services and facilities in urban areas. Given their strategic position in delivering services in the hierarchy of Government set up, following the 74th Constitutional Amendment Act, more functions, powers and resources have been provided to them. However, this increase has happened without commensurate enhancement of their resource base.

Any analysis of finances of State and Central Governments in isolation (excluding that of the local bodies) will not provide a holistic picture of the public finances of the country. Recognising the fact that India is increasingly urbanising, and given the estimate that of more than 50 per cent of India's population will live in urban areas in another 3 to 4 decades, one cannot afford to ignore the fiscal situation of ULBs. Civic infrastructure and services in most cities and towns are in woefully dismal condition. They are grossly inadequate even for the existing population; leave alone the need for planned urbanisation and peripheral development to accommodate migrants and population growth. The floods in Mumbai, Chennai, Hyderabad and Bangalore in the recent past have exposed the vulnerability of cities, their fragile ecology, weak infrastructure systems, faulty planning, long records of under-investment and fiscal imbalances. With rising expectations from the public, the financing of civic infrastructure and services has assumed critical importance socially, economically and politically.

While the Twelfth Schedule of the 74th Constutional Amendment Act, 1992 demarcates the functional domain of municipal authorities, the Amendment Act has not provided for a corresponding 'municipal finance list' in the Constitution of India. The assignment of finances has been completely left to the discretion of the State Governments, excepting in that such assignment shall be 'by law'. This has resulted in patterns of municipal finances varying widely across States and in a gross mismatch between the functions assigned to the ULBs and the resources made available to them to discharge the mandated functions. The ULBs depend on the respective State Governments for assignment of revenue sources, provision of inter-governmental transfers and allocation for borrowing with or without State guarantees. Constitutionally, built-in imbalances in the functions and finances eventually reflect in the high dependency of urban local bodies on State governments and of the State Governments on the Central Government.

3.3 OVERVIEW OF MUNICIPAL FINANCE IN INDIA

Municipal finance can affect the nature and location of development. An overview of municipal finance includes the structure, composition, functions and finances of Urban Local Bodies (ULBs), examine the status of core municipal services and the financial needs for upgrading core infrastructure and services in India.

12th Finance Commission Report states that India has 3,723 ULBs, of which 109 are MCs, 1432 are municipalities and 2182 are Nagar *Panchayats*. The total revenue of the municipalities grew from Rs.11, 515crore in 1998-99 to Rs.15, 149 crore in 2001-02 The total expenditure increased from Rs 12,035 crore to Rs 15,914 crore during the same period. But total revenue of the municipal sector accounts for about 0.75 per cent of GDP of the country. Municipal revenue forms a little more than 2 per cent of combined revenue of State and Central Governments. In terms of total expenditure, the municipal sector accounts for about 0.79 per cent of the GDP of the country and a little over 2 per cent of the combined expenditure of State and Central Governments.

3.3.1 Municipal Revenues

Fiscal assessment of any entity is generally based on revenue and fiscal balance. Similarly, to assess qualitative aspects, the ratio of revenue expenditure to total expenditure is considered. Any entity generating surplus in revenue account (and if possible, in capital account) and maintaining low proportion of revenue expenditure to total expenditure, is considered to have sound financial health. However, this "standard approach" for making assessment may not hold for the ULBs. Municipal authorities are constrained by statutory mandates of balanced budgets and they are also not granted liberal permission by State Governments to incur debt. However, revenue expenditure is not undesirable, if a good proportion of this goes for operation and maintenance of civic amenities provided by the ULBs.

i) **Structure of Municipal Revenue**

The revenue base of MCs can be broadly categorized into:

a) Tax revenues ,

b) Non-tax revenues,

c) Assigned (shared) revenue,

d) Grants-in-aid,

e) Loans and

f) Other receipts.

While, property tax is the major revenue source, in most of the MCs, *octroi* is the major source in the MCs of Maharashtra and Gujarat. *Octroi* has been abolished in all other States excepting Maharashtra and Gujarat. An account of the various sources of revenue of the MCs is given in Table-1.

Table 1: Revenue Sources of Municipal Corporations in India 1998-2002

Revenue Head/ Category	**Sources of revenue**
Tax revenue	Property Tax, *Octroi*, Advertisement Tax, Tax on Animals, Vacant Land Tax, Taxes on Carriages and Carts
Non-Tax revenue	User Charges, Municipal Fees, Sale & Hire Charges, Lease amounts
Other receipts	Sundry receipts, Law charges costs recovered, Lapsed deposits, Fees, Fines & Forfeitures, Rent on Tools & Plants, Miscellaneous Sales *etc.*
Assigned (Shared) revenue	Entertainment Tax, Surcharge on Stamp duty, Profession Tax, Motor Vehicles Tax
Grants-in-aid	i) Plan Grants made available through planned transfers from upper tier of Government under various projects, programmes and schemes. ii) Non-Plan Grants made available to compensate against the loss of income and some specific transfers.
Loans	Loans borrowed by the local authorities for capital works *etc.* – HUDCO, LIC, State and Central Governments, Banks and Municipal Bonds.

Source: *Budgets of Municipal Corporations.*

Apart from their own revenue sources, i.e., tax and non-tax revenue sources, the MCs depend upon grants from State Governments. These grants are primarily intended to compensate for the mismatch of functions and finance. Most of the MCs receive financial support in the form of revenue grants from State Governments to meet current expenses. In addition to own revenues, shared revenues, user charges and fees and grants-in-aid, loans also constitute an important source of municipal revenues in some ULBs.

ii) Significance of Municipal Revenue

The revenue of the municipal government has significance to development of urban areas. Ironically, the percentage of municipal revenue is astoundingly low only 2.3 percent of total revenue of the centre and state combined during the year 2001-02. Research suggests that the urban local bodies need to have a good number of local taxes so as to become financially sound and match the number of functions assigned to municipalities successfully. The status of MCs revenue and its percentage to the GDP is given in Table-2.

Table 2: Significance of Municipal Revenue

Year	Municipal Revenue (Rs. Crore)	Percentage of GDP at Factor Cost	Relative share of Municipal Revenue (as percent of Total Revenue of)		
			State Govt.	Central Govt.	Combined State & Central Govt.
1998-99	11,515	0.72	4.4	4.1	2.5
1999-00	13,173	0.75	4.2	4.4	2.5
2000-01	14,581	0.77	4.2	4.5	2.4
2001-02	15,149	0.73	4.1	4.2	2.3

iii) Composition of Municipal Revenue and Trends

Between 1999-2000 to 2003-04, while the share of non-tax, assigned revenue, non-plan and plan grants improved, the share of tax revenue in total revenue receipts of MCs declined. Among the various revenue sources, tax revenue assumes greater importance in terms of both size and share. The composition of municipal revenue from various sources is given in Table-3.

Table 3: Composition of Municipal Revenue and Trends

(Rs. in Lakh)

Sl. No	Revenue component	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	Average %
1	Tax revenue	458509	554597	461895	573952	599387	8.23
2	Non-Tax revenue	238670	297890	296487	421422	434905	17.42
4	Assigned revenue	84557	115909	110146	132588	131076	11.66
5	Non-Plan grants	26667	34145	33341	54876	50161	20.42
6	Other revenue receipts	98600	86769	48024	64177	63271	-6.11
7	Revenue Receipts	910003	1089310	949893	1247015	1278800	10.18
8	Plan grants	16753	15665	31712	30027	49898	39.20
9	Loans	19917	47245	31805	28520	32835	27.33
10	Other capital receipts	11228	18101	18622	25785	33948	33.55
11	Capital Receipts	47898	81011	82139	84332	116681	27.89
12	Total Receipts	957901	1170321	1032032	1331347	1395481	11.04

Source: Based on the Budgets of Municipal Corporations

Table 4: Composition of Municipal Revenue and Trends

(Per Cent to Total)

Sl. No	Revenue component	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	Average %
1	Tax revenue	47.87	47.39	44.76	43.11	42.95	45.21
2	Non-Tax revenue	24.92	25.45	28.73	31.65	31.17	28.38
3	Assigned revenue	2.78	2.92	3.23	4.12	3.59	3.33
4	Non-Plan grants	9.14	9.90	10.67	9.96	9.39	9.87
5	Other revenue receipts	10.29	7.41	4.65	4.82	4.53	6.34
6	Revenue Receipts	95.00	93.08	92.04	93.67	91.64	93.08
7	Plan grants	1.75	1.35	3.07	2.26	3.58	2.40
8	Loans	2.08	4.04	3.08	2.14	2.35	2.74
9	Other capital receipts	1.17	1.55	1.80	1.94	2.43	1.78
10	Capital Receipts	5.00	6.92	7.96	6.33	8.36	8.36
11	Total Receipts	100.00	100.00	100.00	100.00	100.00	100.00

Source: Based on the Budgets of Municipal Corporations

3.3.2 Municipal Expenditure

Municipal governments in India are vested with a range of functions through the state legislature and other administrative orders. They are however, constrained in discharging their obligatory functions due to a limited resource base. The low per capita receipts of municipal governments do not enable them to meet the minimum standards of services. On the whole, the status of municipal finance in India suggests that the present revenues are insufficient to meet the growing expenditure needs of urban areas.

i) Expenditure Pattern

Municipal governments are legally required to have a balanced budget. The municipal expenditures are thus conditioned by the level of resources available. In the states, where the municipal receipts are very low, the municipal expenditures are also low. These low expenditures have a crucial impact on the quality and nature of services provided by the municipality. Often, the repairs and maintenance of services is poor and the expenditure on capital works is postponed

The expenditure incurred by the MCs can be broadly categorised into:

a) Revenue expenditure

b) Capital expenditure

Revenue expenditure broadly comprises:

i) establishment expenditure;

ii) administrative expenditure;

iii) operations and maintenance expenditure; and

iv) interest payments on loans.

Capital expenditure comprises:

i) expenditure on capital formation; and

ii) principal repayment.

Table 5: Categorization of Municipal Expenditures

Expenditure Category	Expenditure Items
Establishment expenditure	Staff salaries, Allowances, Wages, Pensions & Retirement benefits *etc.*
Administrative expenditure	Rents, Rates & Taxes, Office maintenance, Communications, Books & periodicals, Printing & Stationary, Travel Expenditure, Law Charges *etc.*
Operations & Maintenance	Power & Fuel, Bulk Purchases, Stores, Hire Charges, Repairs & Expenditure
	Maintenance and Interest payments made on loans
Capital expenditure	Buildings, Water Supply & Sewerage, Energy/ Lighting, Solid Waste Management, Roads, Bridges, Culverts, Causeways, Health & Sanitation, Parks and Recreation Spaces, Furniture & Fittings, Tools & Plant, Equipment *etc.*, Principal repayments of loans
Other expenditure	Miscellaneous expenses not accounted for in the above

ii) Significance of Municipal Expenditure

Municipal expenditure holds key to municipal development. However, due to abysmally low generation of resources, the municipal expenditure fall short of the required level in order to promote development of urban areas. The municipal expenditure, constitute less than one percent of GDP and less than three percent of total expenditure.

Table 6: Categorisation of Municipal Expenditures

Year	Municipal Expenditure (Rs. Crore)	Percentage of GDP at Factor Cost	Relative share of Municipal Expenditure (as percent of Total Revenue of)		
			State Govt.	Central Govt.	Combined State & Central Govt.
1998-99	12035	0.75	4.52	4.31	2.21
1999-00	14452	0.82	4.60	4.85	2.36
2000-01	15743	0.83	4.53	4.84	2.34
2001-02	15914	0.76	4.22	4.39	2.15

Source: (i) Report of Eleventh and Twelfth Finance Commission (ii) Handbook of Statistics on Indian Economy, RBI, 2005-06.

iii) Composition of Municipal Expenditure and Trends

The expenditure on operations and maintenances of municipal services accounts for only one fifth of the total expenditure. The level of spending on O & M of core services is important for maintaining a minimum standard of services in the urban settlements. Among all the components of municipal expenditure, the expenditures on capital works, establishment & administration, and operations & maintenance assume importance. The establishment & administrative expenditure constituted 36.25 per cent of the aggregate total expenditure, during 2000-2004. Capital expenditure, which is an important component, constituted less than 13 per cent of the total expenditure, during the same period.

Table 7: Composition and Trends of Municipal Expenditure

(Rs. in Lakh)

Sl. No	Expenditure component	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	Average %
1	Establishment and administration expenditure	279216	330414	329592	411432	402550	10.19
2	Operation and maintenance expenditure	107383	128165	142174	164406	154400	9.96
3	Other revenue expenditure	51830	56120	55954	58190	56265	2.17
4	Revenue Expenditure	438429	514699	527750	634028	613215	9.20
5	Capital Expenditure	96933	105942	119463	124817	150424	11.76
6	Other Expenditure (not classified)	209744	266611	210685	399205	470925	28.40
11	Total Expenditure	745106	887252	857868	1158050	1234564	14.34

Source: Budgets of Municipal Corporations

Table 8: Composition and Trends of Municipal Expenditure

(Rs. in Lakh)

Sl. No	Expenditure component	1999-2000	2000-2001	2001-2002	2002-2003	2003-2004	Average %
1	Establishment and administration expenditure	37.47	37.24	38.42	35.53	32.61	36.25
2	Operation & maintenance expenditure	14.41	14.45	16.57	14.20	12.51	14.43
3	Other revenue expenditure	6.96	6.33	6.52	5.02	4.56	5.88
4	Revenue Expenditure	58.85	58.01	61.52	54.75	49.67	56.56
5	Capital Expenditure	13.01	11.94	13.93	10.78	12.18	12.37
6	Other Expenditure (not classified)	28.15	30.05	24.56	34.47	38.15	31.07
7	**Total Expenditure**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

Source: Budgets of Municipal Corporations

In these sessions you read about the significance and various sources of municipal revenue and now answer the question given in *Check Your Progress-1.*

Check Your Progress 1

Note: a) Write your answer in about 50 words.

b) Check your progress with possible answers given at the end of the unit.

1) What is the main revenue base of municipality?

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2) Describe main expenditure pattern of municipality.

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3.4 ESTIMATED INVESTMENT REQUIREMENTS, NORMS AND STANDARDS

Accurate estimates of financial resource requirements for urban infrastructure are difficult to arrive at. The costs of desired service levels are dependent on a number of factors including as the technology used, topography and geology of the urban area, past investments in a particular service, the size of population, economic profile of the urban area and the geographical area to be covered. Despite these difficulties, various efforts have been made in India to evolve norms and standards of urban infrastructure and services and compute average per capita costs. For computing the financial needs of urban infrastructure, the physical norms have to be converted into financial norms. The Zakaria Committee on Augmentation of Financial Resources of urban local bodies had attempted to evolve per capita investment norms for various urban services in early sixties; The Task Force on Housing and Urban Development, Planning Commission worked out these norms in 1983.

Table 9: Physical Standards of Services for Human Settlements

Service	Sector	Minimum levels of services required to be obtained		Remarks
		Population/ Area target	Service level target	
I. Water Supply	Urban	100% population to be covered	Piped water supply with sewerage: 150* lpcd Piped water supply without sewerage: 70* lpcd 40 lpcd with spot sources/ standposts (* Including wastage of water – roughly 20%)	Public stand posts in the low income settlements One source for 20 families within a walking distance of 100 metres.
II. anitation / Sewerage	Urban	100% city area to be covered by sewerage system with treatment facilities in large urban centres Low cost sanitation methods for other urban areas.	Large city: Full coverage by sewerage with treatment. Medium town: Public sewers with partial coverage by septic tanks. Small town: Low cost sanitation methods.	In low income areas of large cities, community latrines may be provided
III.Solid waste collection and disposal	Urban	All the solid waste generated should be collected and disposed.	100% collection of generated waste, with its proper disposal. Hazardous wastes such as hospital wastes must be incinerated in all cases. Whereas mechanized composting and incineration is recommended for large urban centres, sanitary land fill method of disposal may be used in small and medium towns.	Keeping in view the refuse generation level and its composition, each local body should determine the requirements of collection bins/ collection centres, kind of transport vehicle to be used , staff deployment for various activities, type of treatment to be given to the collected wastes, etc.
IV. Primary Education	Urban & Rural Both	Fulfilment of national goal of universalisation of elementary education for children up to 14 years of age.	Provision of primary school in all areas of the country as per the following guidelines: At least three reasonably large all weather rooms with teaching material At least one teacher per class room/section One primary school for every 3000-4000 population, Area: 3 acres; seats/school: 300-400	In order to improve enrolments at the upper primary stage specially for girls, the walking distance of school should normally be 2 kms In case of primary schools, this standard is 1 km.
V. Primary health care	Urban & Rural Both	Fulfilment of national goal of health for all by 2000AD.	One PHC for 20,000 – 30,000 population. One-sub centre for 3000-5000 population. One community health centre for one lakh population.	Primary health care has been accepted as the main instrument for achieving the goal of 'Health for All'.

Source: NIUA (1995), Working Group report on Norms and Expenditure for Infrastructure, prepared for the Fourth National Seminar of State Finance Commissions, New Delhi, November, 1995.

Table 10: Suggested Financial Norms for Provision of Core Civic Services at 1988-99 prices

(Rs. /capita)

Core Services	Planning Commission		Zakaria Committee (Wt.Avg.)
	Low	High	
Water Supply	980.00	1470.00	706.69
Sewerage	980.00	1102.50	961.26
Solid Waste Disposal	122.50	196.00	n.a.
Storm Water Drains	367.50	490.00	483.72
Roads	980.00	1470.00	828.02
Street Lighting	294.00	294.00	410.66
All services	3724.00	5022.50	3390.36

n.a. Comparative norms (per capita) are not available/not provided.

Note: Planning Commission have suggested two levels of norms – one at low level and another at high level of service standards.

Source:

i) *Zakaria Committee, Augmentation of Financial Resources of Urban Local Bodies, Report of Committee of Ministers, Constituted by the Central Council of Local Self Government, 1963 (weight age averages worked out as per class wise norms).*

ii) *Planning Commission; Task Force on Housing and Urban Development, - Financing Urban Development, 1983.*

Table 11 gives the estimated additional investment needs for provision of core services in the urban areas of the country for the years 2000 to 2020. The range of required investments by 2005 works out to be approximately Rs. 55 thousand cores to 74 thousand crores.

Table 11: Estimated Additional Investment Needs for Provision of Core Urban Services as per Planning Commission Norms and Standards, at 1998-99 prices.

Year	2010		2015		2020	
Projected Population	391,567,855		458,052,907		535,826,583	
Services	Low	High	Low	High	Low	High
Water Supply	19937	29906	26453	39680	34075	51112
Sewerage	19937	22430	26453	29760	34075	38334
Solid Waste Disposal	2492	3987	3307	5291	4259	6815
Storm Water Drains	7477	9969	9920	13227	12778	17037
Roads	19937	29906	26453	39680	34075	51112
Street Lighting	5981	5981	7936	7936	10222	10222
All services	75762	102180	100521	135572	129484	174634

Method to Compute the Requirement:

Requirement 2020 = (norm × (pop2020 – pop1998) + ((pop1998.30)*norm))/10000000*

Where: Population 98 = 268,748,694

Table 12: Estimates of Urban Infrastructure Investment Requirements

Agency	Services covered	Period of Recommen-dation	Resource Requirements (Rs. In crore)
NIUA (Planning Commission Norms updated to 1998-99 prices)	Water Supply, Sewerage, Solid Waste Disposal, Storm Water Drains, Roads, Street Lights	2000-2020	129484-174634
Zakaria Committee Norms (updated to 1998-99 prices)	Water Supply, Sewerage, Drainage, Roads and Street Lights	2000-2020	113754
India Infrastructure Report (Rakesh Mohan Committee)	Water Supply, Sanitation and Roads	1996-2001	41636-43573
Ninth Plan Document	Water Supply and Sanitation	1997-2002	50000

The Indian Infrastructure Report (Rakesh Mohan Committee) estimated a fresh funds required to augment the core services of water supply, sanitation and roads to clear the backlog provision, new investments and operation and maintenance of the services provided. The committee had estimated that a total of Rs. 42 thousand crores to 44 thousand crores for the period 1996-2001 are needed for augmentation of these services. This includes backlog provisions as also the new investment needed for the purpose.

It is significant to note that the Zakaria Committee's financial norms adjusted for inflation are still widely used as benchmarks for assessing infrastructure needs in urban areas, even though they are outdated and cannot match with the changing life style of the people, technological advances and growth in the economy. Considering this, the Ministry of Urban Development, Government of India has prescribed service level benchmarks for a number of urban services, and has published a hand book on service level benchmarking in 2008. The 13th Central Finance Commission has endorsed these benchmarks and has made compliance with them a necessary condition for urban local bodies to obtain performance-linked grants.

3.5 MECHANISMS TO IMPROVE MUNICIPAL REVENUE

Faced with growing demand for urban services, urban local bodies (ULBs) in India are challenged to generate more revenue. The devolved sources of revenue do not match a wide range of functions required to be performed by them. This has led to increasing dependence of ULBs on higher levels of government. Broadly, they can increase revenues from their own internal sources, seek external funding from outside agencies, and reduce expenses. An increasing demand on local services, abolition of *Octroi*, loss of buoyancy and elasticity of annual rental value (ARV) based Property Tax(PT) and the consequent fiscal stress of ULBs in India have become compelling reasons to innovate new sources of revenue. Some of the mechanisms, the ULBs can develop for enhancing their credit worthiness are follows. To mobilize resources on their own, ULBs can impose new taxes, increase tax or fee rates, or introduce management innovations within the existing revenue structures. Imposing new sources or increasing tax or user fee rates require approval of the elected municipal council and/or state government, a cumbersome and time-consuming process.

i) Refurbishing Major Taxes

Octroi and PT (Property Tax) have traditionally constituted the mainstay of municipal finance in India. In India, it is abolished in all states except in the states of Punjab, Orissa and the municipal corporations in Maharashtra and Gujarat. Analysis of data on revenue from PT reveals that share of PT in the total tax revenue is declining. In the state of Rajasthan, the share of PT in total revenue is only about 2 percent.

Decline in fiscal role of PT in India is due to a host of administrative and legal reasons. Revenue generation from PT depends on an updating of the base according to the prevailing rental values. This is hardly done despite a legal provision for this in municipal laws. Other administrative reasons pertain to lack of transparency in determination of the base and rationalisation of rate structure.

ii) Property Tax Innovations

Property taxes are the major source of revenue of ULBs in India. However, in most cities, not all properties are assessed, records are not updated regularly, and tax collection is far from satisfactory. ULBs can increase revenue by improving property inventories, record management, public awareness and participation, and tax collection. Collections from property tax can be enhanced substantially by maintaining the tax base through indexing and regular valuation, supported by legal safeguards. Some critical observations in the context of property tax administration in the country in the past include the following:

The area-based property tax systems introduced by Andhra Pradesh and Patna in the recent past is simple and innovative. When introduced in Patna, despite a reduction in the rate from 69 per cent to 9 per cent, the revenue increased substantially. These positive attributes of the system have led to its snowballing effect in other states. The system first introduced in Andhra Pradesh, has now travelled to Gujarat, Rajasthan, Uttar Pradesh, Madhya Pradesh, Tamil Nadu and Delhi. Besides, adopting a Unit Value system of Property Tax, the State Government of Uttar Pradesh has also amended Municipal Laws for de-linking the standard rent concept of the Rent Control Law from valuation of Property Tax base.

The agenda for property tax reforms may cover: simplification of tax assessment and collection, introduction of area-based methods that link property tax to location, type of building and type of use parameters based on some rational criteria, bringing government properties and unauthorised constructions into tax net, elimination of discretion on the part of assessors, self-assessment of tax and payment through banks, rationalisation of exemptions, computerisation of accounts and speedy procedures for dispute resolution.

Transparency, objectivity and simplicity of the unit value system not withstanding the system is unlikely to enjoy buoyancy and elasticity as the unit values are frozen. In order to address this problem the unit values would need to be reviewed periodically and indexed with inflation. In any scheme of refurbishment of PT, what is important is that it has to be conceived within the existing legal framework in each country so that it could be sustainable in law. Also intervention is required on all the four important organs of PT, are as follows:

a) Nature of base,

b) Valuation and assessment practices,

c) Rate structure, and

d) Collection efficiency.

Isolated intervention on any one of these organs is unlikely to enhance revenue productivity of this tax.

All these organs would need to be addressed at the same time.

iii) Effective Tax Administration

Maladies in tax administration relate to:

i) Lack of effective and objective valuation of tax base; and

ii) Deficiencies in assessment of demand, billing and collection.

Widening of tax-net, addressing the question of under assessment, review of exemptions of lands and buildings from Property Tax are required to be objectively addressed. Some of the cities have now gone for tax mapping for widening the tax-net.

Physical surveys of lands and buildings by using GIS base maps tried in the cities of Ludhiana, Indore, Mirzapur, Ghaziabad, Agra, Lucknow, Kanpur and other cities have dramatically widened the local tax-net and enhanced revenue. It has also helped in imparting objectivity and transparency in valuation and assessment of Property Tax.

Tax collection and generation of additional revenue could be ensured through (i) a scheme of incentives and penalties for municipal staff and the taxpayers and (ii) by profitably adopting the ABC Analysis, which is usually applied in management of inventory in an organisation or a project. Some of the tax administration measures taken by various state governments are narrated behalf.

a) **Self-Assessment System (SAS):** Several ULBs introduced SAS to make property tax assessments simpler and more transparent. This method helps taxpayers to understand the assessment process and removes the discretion of the assessors to assess the properties in an arbitrary manner. It increases taxpayers' involvement by allowing them to calculate their own assessment within pre-established guidelines.

The Municipal Corporation of Hyderabad (MCH) introduced SAS for property taxes in 1999-2000. MCH computerized all property records and gave each unit a unique identification number. The corporation involved the public in determining the revised tax rates by consulting resident welfare associations. Tax education and publicity campaigns, including newspaper advertisements, helped the corporation introduce the reforms. Consequently, the city increased its property tax revenue from Rs. 569 million in 1998-99 to Rs. 1008 million in 2000-01.

b) **Improved Information Base:** In 1997-98, the Chennai Corporation introduced a computerized information system that enables better linkages between property taxes and facilitates close monitoring of collections. This helped the corporation to increase its property tax revenue by 50 percent. The Indore Municipal Corporation (IMC) computerised existing property tax records and conducted a physical survey of all wards to identify properties not on record. It increased number of properties identified from 1.55 to 2.67 lakh. Some city governments have put in place friendly payment gateways like collection through banks and web-based tax collection. Indore Municipal Corporation has introduced a system of group health insurance of senior citizens. This enables the senior citizens to avail of free hospitalisation up to Rs. 20,000 provided they have paid Property Tax. A few cities have put in place a tax collection system by involving banks and on-line payment of PT.

c) **Collection Drives:** Ahmedabad conducted a special campaign to increase property tax revenue by forming special collection teams. The corporation gave the teams power to disconnect water supply or drainage lines, attach the property of defaulters, and issue arrest warrants for non-payment of property taxes. The result: in two years, 1993-94 to 1995-96, Ahmedabad nearly doubled its property tax collection, which rose from Rs. 47 crore to Rs. 92 crore.

d) **Outsourcing Bill Distribution:** Tax administration systems are labour intensive and sometimes the cost of collection exceeds the revenue collected. Some ULBs have begun to outsource sub-processes. The Municipal Corporation of Ludhiana (MCL), introduced a courier system for bill distribution. MCL had 28 bill distributors to serve property tax and water charge bills and issue overdue notices at an annual salary expense of Rs. 3.5 million. It reassigned these employees to other positions as they became vacant and gave their work to three private couriers. The couriers completed the task for Rs. 1.1 million, saving nearly Rs. 2.5 million per year.

e) **Tax Collection Centres:** ULBs in Tamil Nadu organised special tax collection camps in a group of wards. The councillors took a keen interest in organising these camps and carried out door-to-door campaigns to inform people about them, urging them to utilise the facilities and pay their taxes. The Tirunelveli Municipal Corporation opened 17 unit offices in the city to improve its property tax collection. They publicized this through all available media and fitted corporation vehicles with audio announcements and banners. Due to this publicity, 65 percent of taxpayers paid their dues before the due date and the collection were Rs. 185 lakh within six months compared to Rs. 200 lakh collected in 12 months during the previous year. In Andhra Pradesh, the Guntur Municipal Corporation also increased the number of collection centres and opened these centres on every second Saturday or Sunday. The Vishakhapatnam Municipal Corporation opened city civic centres so citizens can easily visit them to make payments.

f) **Tax "*Adalats*"(Tax courts):** Often property tax is vexatious and disputes end up in courts. Delays in solving such cases result in loss of revenues for ULBs. To avoid delays in settling property tax matters some ULBs have established special tax "*adalats*" to resolve tax disputes quickly.

3.6 NEW AREAS FOR IMPROVING MUNICIPAL RESOURCES

Some of the new suggested areas needed for the improvement of municipal revenue are described below.

1) Municipal Asset Management

Municipal Corporations usually have limited sources of revenue generation, moreover, most of the sources remain unexplored or under explored. Just for instance, not all the properties are assessed for property tax. There is undervaluation of properties and there are many trades which are not assessed for trade tax, license fees and municipal properties encroached etc. At the same time they lack proper mechanisms for expenditure management and linking of budgets and accounting systems. These two together lower creditworthiness of the Corporation as they first limit the Corporation's capacity for efficient service delivery and second limits its capability to raise funds from capital market, pooled funds, and special schemes like JNNURM etc. ULBs generally hold a significant amount of fixed assets in real estate. But very few local bodies have exploited the commercial potential of these properties to generate non-tax revenues. Most ULBs do not have a proper inventory of assets nor do they update them regularly. Often villages on the periphery are brought into municipal limits as the city expands. *Panchayat* land then comes under municipal ownership.

The Guntur Municipal Corporation regularised all the subleased municipal shops by collecting 30 percent of land and shop construction value. The Vishakhpatnam Municipal Corporation leased out the aquarium and marriage halls by fixing daily rents for them. Through this measure, corporation collected Rs. 80 lakh and was free from the related liability and expense of maintaining these properties.

2) User Fees and Charges

This is an area which needs to be focused for greater resource mobilisation and linkage between tax payment and service delivery. User charges promote efficiency by providing information on demand to the public service providers and ensure that what the public sector supplies are valued (at the margin) by citizens. They have the advantage of tying the mobilised revenues to the costs of services being provided. Institutional financing of projects becomes feasible if loans raised by ULBs are paid back through project revenues. User charges may be designed based on the users pay/beneficiaries pay principle. Services provided by a public organisation are grouped as

i) Public-goods and

ii) Merit goods or non-public goods, or private goods.

The latter is fit for application of principle of exclusion. The consumers are identifiable and the quantum of services consumed is possible to be measured. In case the consumers do not pay for the services consumed, the service can be disconnected.

User fees can also increase municipal revenues. User charges levied by ULBs include fees for water, sewerage, solid waste management, parks, parking, birth and death certificates, business licenses, streetlights, ad space, and cable TV.

a) **Sewerage Charges:** Most cities in India do not levy fees for sewerage and also are unable to provide the service. Several small ULBs in Tamil Nadu structured an innovative mechanism to finance construction of underground drainage systems. Beneficiaries contribute connection fees that share in the capital costs, reducing the debt required. The Alandur Municipality built 120 kilometres of underground drainage and a 24 million-litre per day sewage treatment plan using these deposits. The municipality charged a one-time deposit of Rs. 5000 or Rs. 10000 per connection for domestic and non-domestic users respectively. The municipality also fixed monthly sewerage maintenance charges of Rs. 150 per household connection, Rs. 450 per commercial connection and Rs. 750 per industrial connection. The ULBs conducted awareness campaigns to obtain people's support. These programmes were supported by the ULB's elected and administrative officials, as well as by state officials. The Amravati Municipal Corporation in Maharashtra built a sewerage scheme by levying sewerage charges of Rs. 2019 per year per household. They also used the revenue for debt servicing and operation and maintenance of the scheme.

b) **State Guidelines for Setting Water Charges:** Municipal water charges are generally very low and not revised for very long periods. The Government of Karnataka issued a government order for ULBs to set water charges in line with actual costs. It requires them to levy minimum water charges that would cover expenditures for operation and maintenance and debt servicing.

c) **Parking Fees:** The BMP implemented a *pay and park* scheme in the central business district. Parking fees are based on the duration of parking.

d) **Eco Fee:** The BMP council resolved to levy an "eco fee" on the persons using the municipal garden. The city collects this fee at the entrance of the garden but regulars can obtain a monthly pass. Children and senior citizens are exempted.

e) **Charges for Collecting Solid Waste:** Various ULBs levy solid waste charges for the use of public places based on the amount of waste generated. The ULBs decided that organizers of private functions in the city's marriage halls should pay a fee for waste collection. Similarly, some ULBs levy lifting charges to remove debris from construction sites.

f) **Fees for "Tatkal" (Hindi for "Quick") Delivery of Services:** Issuing birth and death certificates and building permits are ULB responsibilities. To simplify the process some ULBs in Tamil Nadu decided to mail birth certificates to applicants. These ULBs levy a service charge of Rs. 5 per certificate for postal expenses. Some municipalities in Tamil Nadu and West Bengal charge extra for the delivery of this certificate on a priority basis.

The Guntur Municipal Corporation streamlined issuance of building plans by providing that any applicant paying a 25 percent additional fee with an affidavit from a licensed surveyor gets approval across the counter. Many appreciate these convenient procedures and choose the quick delivery of service.

g) **Advertisement Tax:** BMP's revenue from the advertisement tax rose from Rs. 2.43 crore in 1999-2000 to Rs. 4.01 crore in 2000-01 due to increased space available from construction of bus shelters and public toilets and other administrative measures. The MCH's advertisement income increased with its aggressive auctioning of space on billboards, bus shelters, road arches, and footpath railings.

h) **Cable Charges:** The Government of Tamil Nadu allowed ULBs to charge cable TV operators for the use of public property. Gobichettipalayam, the first to implement this order, charges cable operators Rs.5.5 per year per kilometre of cable. In addition, the council collects from the cable operators a monthly fee of Rs. 15 per connection. The total revenue generated from these measures was about Rs.4.19 lakh in 2000-01.

i) **Street Tax:** The Pune Municipal Corporation in Maharashtra levies a street tax to help finance a plan to improve traffic and public transportation. The fee is collected with the property tax and is five percent of annual rateable value.

3) Using Land as Resource

The installation of infrastructure (e.g., roads, water, sewer, and electricity) increases the value of the land in the vicinity of the infrastructure investment. Unused land owned by local governments or state government has a market value that can be put to use to accomplish development objectives highlighted in a city development plan (CDP). Converting land values into resources needed to pay for infrastructure is an important alternative to using debt financing and is being used in rapidly growing cities like Bangalore, Mumbai, and Pune.

4) Internal and External Development Charges:

These charges include costs of off-site and on-site infrastructure such as water source development, laying of water, sewer and power lines, development of freeways/roads, parks, etc. The development charges could be collected at the time of giving approvals to layouts and buildings. These charges, which cover costs towards the following range of infrastructure amenities, provide an excellent example of cost recovery:

1) Water supply;

2) Sewerage;

3) Storm water drainage;

4) Roads;

5) Electrification including 26.5 per cent operation and maintenance and supervision charges;

6) Street lighting;

7) Community buildings;
8) Diversion of high tension (HT) lines;
9) Horticulture including first five years maintenance;
10) Conservancy;
11) Nominal maintenance of roads
12) Resurfacing of roads;
13) Maintenance of Public Health Services for first five years
14) Maintenance of street lights for first five years;
15) Maintenance of street lights beyond five years and up to 10 years;
16) Horticulture after 5 to 10 years;
17) Beautification of entry points, junction improvements and levelling;
18) Development of recreational and communication zones; and
19) Protection works, etc.

In these sessions you read about various mechanisms to improve the sources of revenue for the municipal government. Now answer the question given in Check Your Progress-2.

Check Your Progress 2

Note: a) Write your answer in about 50 words.

b) Check your progress with possible answers given at the end of the unit.

1) Describe one of the mechanisms to enhance the municipal revenue.

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2) What are the internal and external charges for raising municipal revenue?

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3.7 LET US SUM UP

Municipal Finance is critical to municipal development. It can affect the nature and location of development. Government of India from time to time has introduced various reforms in order to enhance the revenue base of municipal government.

As a part of municipal tax reforms, it is necessary to broaden the existing tax base of the Municipalities and to improve collection from other important municipal taxes such as Profession Tax, Entertainment Tax, Advertisement Tax, Motor Vehicles Tax and Business Licensing Fees. Many developed countries authorise the levy of local option income, sales and excise taxes by the local authorities. The possibility of levying a local surcharge on sales and excise taxes (on petrol, diesel, etc.) may need to be explored.

Increasing municipal revenue is a major challenge for ULBs. Some have implemented management innovations resulting in significantly increased revenues. Improved information systems simplified billing and collection, better enforcement, and public communication are key elements of success. The most important lesson learned is that the reform process requires the strong commitment and unwavering support of elected leaders as well as of administrators.

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3.9 CHECK YOUR PROGRESS: POSSIBLE ANSWERS

Check Your Progress 1

1) **What is the main revenue base of municipality?**

   The important revenue base of the MCs can be broadly categorized into:

   d) tax revenues ,

   e) non-tax revenues,

   f) assigned (shared) revenue,

   d) grants-in-aid,

   e) loans and

   e) other receipts.

2) **Describe main expenditure pattern of municipality?**

   Revenue expenditure pattern of the MCs can broadly comprise:

   i) establishment expenditure,

   ii) administrative expenditure,

   iii) operations and maintenance expenditure, and

   iv) interest payments on loans;

   Capital expenditure comprises

   i) expenditure on capital formation and

   ii) principal repayment.

Check Your Progress 2

1) **Describe one of the mechanisms to enhance the municipal revenue.**

   User charges promote efficiency by providing information on demand to the public service providers and ensure that what the public sector supplies are valued (at the margin) by citizens. They have the advantage of tying the mobilised revenues to the costs of services being provided. Institutional financing of projects becomes feasible if loans raised by ULBs are paid back through project revenues. User charges may be designed based on the users pay/beneficiaries pay principle. Services provided by a public organisation are grouped as

   i) Public-goods and

   ii) Merit goods or non-public goods, or private goods.

2) **What are the internal and external charges for raising municipal revenue?**

   The internal and external charges include costs of off-site and on-site infrastructure such as water source development, laying of water, sewer and power lines, development of freeways/roads, parks, etc. The development charges could be collected at the time of giving approvals to layouts and buildings. These charges, which cover costs towards the following range of infrastructure amenities, provide an excellent example of cost recovery:

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- Resurfacing of roads;
- Maintenance of Public Health Services for first five years
- Maintenance of street lights for first five years;
- Maintenance of street lights beyond five years and up to 10 years;
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- Beautification of entry points, junction improvements and levelling;
- Development of recreational and communication zones
- Protection works, etc.