

## **Chapter 5**

### **ASSESSMENT OF MUNICIPAL FINANCES**

#### **5.1 Approach to Study**

The macro overview of municipal finance in India, attempted in the preceding chapter, brought out the significance of municipal finance for the overall financial well-being of the economy and provided an insight into the sources, structure, composition and trends of aggregate revenue and expenditure of the MCs in metropolitan cities in India. It should be noted that many of the conclusions drawn at aggregate level above may not hold good for individual ULBs and may not throw enough light on the constraints faced by individual local bodies and the need for requisite policy initiatives to address them. Therefore, the present chapter examines the financial parameters of individual municipal bodies, to assess their ability to provide the required civic amenities and to identify the constraints faced by them.

#### **5.2 Analytical Framework**

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<sup>4</sup> and they are also not

---

<sup>4</sup> Statutorily, municipal bodies cannot run deficit and their revenue receipts must exceed revenue expenditure while presenting budgets. It is quite possible that MCs might be compressing its expenditure in order to meet the statutory requirement. Therefore, the surplus cannot be termed as a genuine surplus.

granted liberal permission by State Governments to incur debt [Mathur and Thakur (2004)]. However, revenue expenditure is not undesirable, if a good proportion of this goes for operation and maintenance of civic amenities provided by the ULBs.

With the above in the background, the assessment of ULBs needs to proceed on a different track, making use of an alternate set of parameters. These parameters are normative benchmarks which define the minimum level of expenditure that the ULBs are required to incur, in order to ensure a minimum standard of living to the inhabitants. A set of expenditure benchmarks, both for creating new assets, and for their maintenance were derived by the Zakaria Committee in 1964 for core urban services. These expenditure norms for service provision (capital) as well as operation & maintenance (O&M) are for the cities that are divided into categories AA, A, B, C, D and E, based on the population size. The expenditure norms for 5 core civic activities *viz.*, water supply, roads, storm water drainage, sewerage and street lighting for 3 major city classes covered by this study (at the 1996-97 prices) are shown in Table 25.

A comparison of municipal spending with these norms, after revising them to the current period, would reveal the level of under-spending by the ULBs. There are a host of factors which could be responsible for the level of under-spending, which can be divided into two broad categories. - *exogenous* and *endogenous*. As the terms

**Table 25: Zakaria Committee Norms of Expenditure on Services**

(Rupees per capita at 1996-97 prices)

City Class	Water Supply		Sewerage		Storm Drainage		Roads		Street Lights	
	Capital	O & M	Capital	O & M	Capital	O & M	Capital	O & M	Capital	O & M
AA	968	161	1117	182	611	-	1207	37	447	45
A	700	152	968	177	432	-	1043	33	372	42
B	699	146	819	161	387	-	611	27	328	37

AA - More than 20 Lakhs population; A - 5-20 Lakhs population; B - 1-5 Lakhs population

Source: Mathur and Singh (1998)

suggest, *exogenous factors* are those that are not within the control of concerned ULB whereas *endogenous factors* refer to those that have to do with the ULBs' own operations.

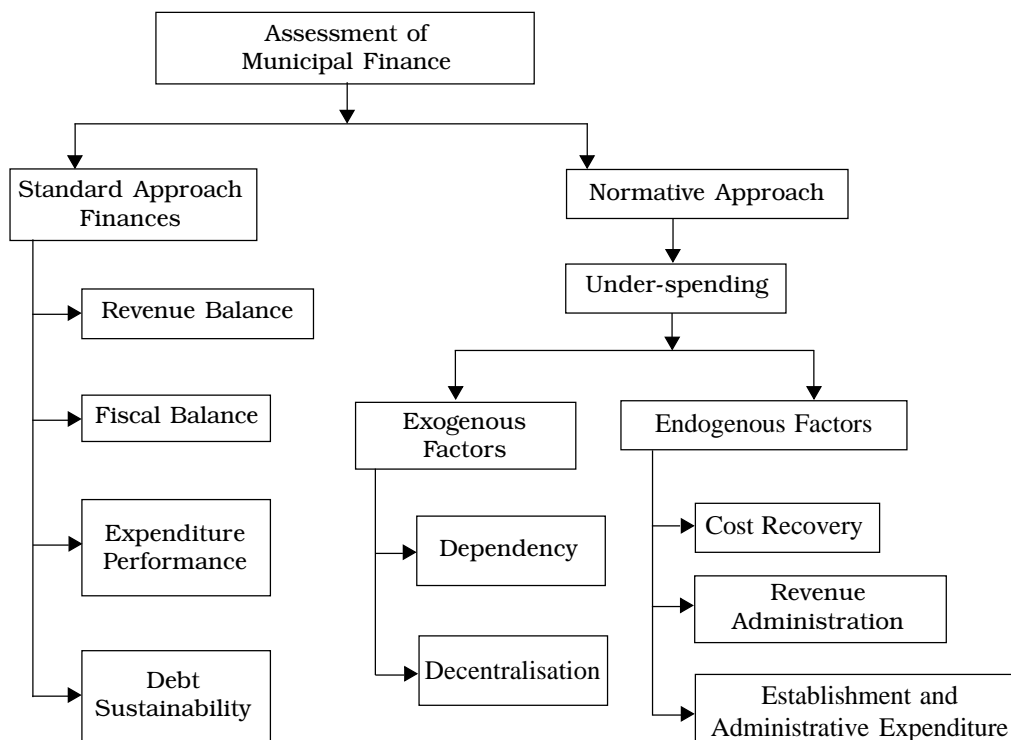
Exogenous factors include: delegation of revenue powers (decentralization) and dependency of ULB for resources on upper tier of government (dependency ratio). Endogenous factors include: revenue (tax) administration, cost recovery and quality of expenditure.

The framework of analysis proposed to be followed for assessment of ULB performance is set out in Figure 5.

Thus the assessment of finances of ULBs is proposed to proceed as follows:

- First, the ULBs have been assessed in terms of “standard approach” using revenue balance, fiscal balance and the ratio of revenue expenditure to total expenditure.

**Figure 5: Municipal Finance Assessment Framework**



- Secondly, ULBs were assessed in terms of “normative approach” by using Zakaria Committee norms. The Zakaria Committee norms for civic amenities are adjusted to the current prices of the period of 1999-2000 to 2003-2004, using an appropriate inflation index, *i.e.* WPI. The performance of individual MCs is compared against the respective norms, and, the level of under-spending is worked out. This is followed by the identification of the factors responsible for the level of under-spending.
- Next section, deals with ‘use of debt’ and ‘debt sustainability’ of the MCs and ascertain the capacity of the MCs to borrow for augmenting spending on provision of services.
- The subsequent section summarises the performance of individual MCs in terms of different parameters and attempts to rank them.
- In the last section, estimates of resource requirements of the urban sector and the potential of revenues of the ULBs in India have been attempted.

### **5.3 Major Inferences from Analysis**

#### **5.3.1 Standard Approach**

##### **i) Revenue Balance**

Revenue balance, measured as revenue receipts net of revenue or current expenditure, indicates whether a municipal corporation (MC) is able to meet its revenue expenditure from its own resources including grants from the upper tiers of Government. Table 26 reveals that all the MCs, barring Pune and Patna, were able to generate revenue surplus<sup>5</sup>.

---

<sup>5</sup> It has been pointed out that since a part of Municipal body expenditure is absorbed directly by the state government, particularly relating to deputed employees, expenditure shown by them (municipal bodies) is an underestimate. But this issue is not relevant for the bigger MCs considered in the study. For instance, proportion of deputed employees is miniscule in the case of Bangalore, Chennai and Hyderabad.

**Table 26: Balance of Municipal Revenues and Expenditure  
(Average of 1999-2000 to 2003-2004)**

Sl. No.	Municipal Corporation	Revenue Income (Rs Crore)	Per capita Revenue Income (Rs)	Revenue Expenditure (Rs Crore) (Rs)	Per capita Revenue Expenditure Deficit	Total Revenue Surplus/ deficit (Rs Crore)	Per capita Revenue surplus/
1	Hyderabad	338.8	964.5	273.4	779.1	65.4	185.4
2	Visakhapatnam	110.1	1093.3	74.6	742.5	35.5	350.8
3	Vijayawada	61.7	705.6	44.5	509.8	17.2	195.7
4	Patna	21.8	150.4	29.6	205.1	-7.8	-54.7
5	Delhi	880.3	872.3	361.1	341.1	519.2	531.2
6	Ahmedabad	599.4	1668.5	556.7	1551.6	42.7	116.9
7	Surat	662.3	2577.0	208.7	816.5	453.5	1760.4
8	Vadodara	159.3	1233.4	141.8	1099.1	17.4	134.3
9	Rajkot	NA	NA	NA	NA	NA	NA
10	Jamshedpur	NA	NA	NA	NA	NA	NA
11	Dhanbad	NA	NA	NA	NA	NA	NA
12	Bangalore	369.5	810.4	296.4	643.5	73.2	166.8
13	Kochi	51.7	858.8	25.8	430.4	25.8	428.4
14	Indore	180.0	1029.6	81.4	464.9	98.6	564.7
15	Bhopal	80.4	545.4	27.8	189.2	52.5	356.2
16	Jabalpur	54.0	551.0	33.7	344.4	20.2	206.6
17	Greater Mumbai	4162.0	3417.1	1560.2	1283.8	2601.8	2133.3
18	Pune	507.2	1890.3	697.9	2582.0	-190.7	-691.7
19	Nagpur	249.6	1197.8	204.0	979.4	45.6	218.4
20	Nashik	268.3	2344.7	138.7	1221.2	129.6	1123.5
21	Amritsar	NA	NA	NA	NA	NA	NA
22	Ludhiana	194.7	1333.2	109.4	749.6	85.2	583.6
23	Jaipur	122.9	493.7	49.7	198.9	73.2	294.8
24	Chennai	591.0	1385.5	242.7	570.1	348.3	815.5
25	Coimbatore	72.1	763.0	47.1	498.7	25.0	264.3
26	Madurai	56.6	610.7	45.4	489.3	11.2	121.4
27	Lucknow	84.6	369.0	62.8	274.8	21.8	94.2
28	Kanpur	100.3	382.9	86.2	330.4	14.1	52.5
29	Allahabad	36.4	365.0	25.8	259.0	10.5	106.0
30	Agra	39.7	303.5	24.7	189.2	15.1	114.3
31	Varanasi	36.5	325.4	21.8	195.8	14.7	129.6
32	Meerut	40.9	365.3	31.6	283.0	9.4	82.3
33	Faridabad	78.1	697.4	75.1	671.3	3.0	26.1
34	Kolkata	542.4	1178.5	387.1	841.4	155.3	337.1
35	Asansol	11.1	218.2	7.4	145.8	3.7	72.4
	<b>Total for 35 MCs</b>	<b>10228</b>	<b>1271</b>	<b>5456</b>	<b>678</b>	<b>4772</b>	<b>593</b>

Source: Budgets of Municipal Corporations.

## **ii) Fiscal Balance**

This measure reveals the overall resource gap, after meeting both revenue and capital expenditure, that needs to be met through borrowings.

It can be observed from the above table that except 7 municipal corporations, *viz.* Mumbai, Chennai, Visakhapatnam, Surat, Delhi, Coimbatore and Faridabad, all other MCs had their revenue falling short of expenditure (having a negative surplus). This is significant in that for maintaining the present level of expenditure, revenues are inadequate and borrowed funds are used. Hence MCs are constrained to raise the expenditure to the desired level for ensuring minimum level of civic amenities. The level of shortfall ranges from Rs.3 per capita for Jabalpur MC to Rs.1,411 per capita for Pune MC. However, the 7 MCs which are enjoying surplus have the fiscal space and clear scope for improving the civic amenities in the immediate future. There was a surplus of more than Rs.750 and Rs.500 per capita in case of Surat and Mumbai, respectively<sup>6</sup> (Table 27).

## **iii) Expenditure Performance**

A proportion of revenue expenditure to total expenditure reveals the quantum of funds spent for maintaining the current assets and that available for creating new capital assets.

Table 28 shows categorisation of the MCs on this parameter. It indicates that many of them have very high proportion of revenue expenditure as compared to the group average of 56 per cent. Faridabad, Vishakhapatnam, Kolkata, Kanpur and Pune have shown revenue expenditure constituting more than 70 per cent of their total expenditure, while Kochi, Indore, Greater Mumbai, Jaipur and

---

<sup>6</sup> Budget documents for the year 2002-03 and 2004-05 of Brihat Mumbai MC state that surplus has resulted on account of efforts made by various economy measures to control the expenditure and augment the revenue.

**Table 27: Resource Gap of the Municipal Corporations**

Sl. No.	Municipal Corporation	Resource Gap in Rupees per-Capita (Average of 1999-2000 to 2003-2004)		
		Revenue Receipts	Total Expenditure	Resource Gap
1	Greater Mumbai	3417	2912	-505
2	Delhi	739	721	-18
3	Kolkata	1178	1224	46
4	Chennai	1386	1216	-170
5	Hyderabad	964	984	19
6	Ahmedabad	1668	2040	372
7	Kanpur	383	395	12
8	Pune	1890	3301	1411
9	Surat	2577	1818	-759
10	Jaipur	471	508	37
11	Lucknow	369	449	80
12	Vadodara	1434	1678	244
13	Agra	304	345	41
14	Nashik	2345	2711	366
15	Meerut	365	398	32
16	Faridabad	697	671	-26
17	Visakhapatnam	1093	941	-152
18	Allahabad	365	370	5
19	Rajkot	1020	1325	305
20	Jabalpur	551	554	3
21	Coimbatore	763	700	-63
22	Madurai	624	874	249
23	Vijayawada	706	772	66
24	Kochi	813	1133	320
25	Asansol	218	367	149
	<b>Total for 25 MCs</b>	<b>843</b>	<b>910</b>	<b>67</b>

\*: '-' indicates fiscal surplus.

**Source:** Budgets of Municipal Corporations.

Chennai have shown it at less than 40 per cent of total expenditure. The MCs with very a high proportion of revenue expenditure need to prioritise their expenditure in favour of capital expenditure.

### 5.3.2 Normative Approach

#### i) Availability of Civic Amenities

The Municipal Corporations are expected to provide certain minimum level of civic services to the citizens, in accordance with their obligatory functions and mandates. The availability of civic amenities in a MC could be approximated by the per capita

**Table 28: Categorization of Municipal Corporations as per Revenue Expenditure to Total Expenditure Ratio (2003-04)**

<b>Parameter</b>	<b>Municipalities</b>	<b>Top 5 Municipalities</b>
At or Above Average Vishakhapatnam Patna Ahmedabad Jabalpur Pune Ludhiana Coimbatore Lucknow Kanpur Allahabad Meerut Faridabad Kolkata	Hyderabad	Faridabad (100%) Vishakhapatnam (83.69%) Kolkata (73.36%) Kanpur (72.85%) Pune (72.65%)
		<b>Bottom 5 Municipalities</b>
<i>Below Average</i>	Asansol Agra Chennai Greater Mumbai Indore Jaipur Bhopal Madurai Nasik Kochi Bangalore Surat Vijayawada	Kochi (26.65%) Indore (37.68%) Greater Mumbai (38.03%) Jaipur (38.09%) Chennai (39.06%)

**Source:** Budgets of Municipal Corporations.

expenditure made by the MC on various services. The adequacy of services provided by the MCs is assessed by comparing the expenditure incurred by them on core services, namely, water supply, sewerage, roads and street lighting with Zakaria Committee expenditure norms<sup>7</sup>. Zakaria Committee norms were evolved in 1964. They were adjusted for inflation to arrive at norms for the period of 1999-2000 to 2003-2004. Since service-wise data for all the years have been available only for 11 MCs, average proportion of service-wise expenditure to total expenditure for these MCs was used to arrive at the expenditure incurred by remaining MCs on these services.

<sup>7</sup> Here, the expenditure norm for storm water drainage has not been included, which is not shown in the expenditure on services of the MCs.



The results shown in Table 29 indicate that spending on civic services of all the MCs has been lower than the Zakaria Committee norms. The extent of under-spending varied between 30.78 per cent in the case of Pune to 94.43 per cent in the case of Patna. The average level of under-spending for the 30 MCs under the study works out to 76 per cent.

**Table 29: Zakaria Committee Norms and Under-spending of the Municipal Corporations (Averages of 1999-2000 to 2003-2004)**

Sl. No.	Municipal Corporation	Average Zakaria Norm (Rupees per capita)	Average Expenditure of the MC on Core Services capita)	Average Under Spending of the MC (As Percentage of Zakaria Norm)
1	Hyderabad	861.71	207.41	-76.01
2	Visakhapatnam	786.21	198.76	-74.73
3	Vijayawada	791.06	147.67	-81.40
4	Patna	856.56	47.56	-94.43
5	Delhi	920.78	137.35	-85.38
6	Surat	986.12	370.61	-62.24
7	Vadodara	804.18	384.21	-50.43
8	Bangalore	983.77	249.24	-74.92
9	Kochi	747.95	277.34	-63.65
10	Indore	843.88	210.63	-75.54
11	Bhopal	823.74	127.53	-84.50
12	Jabalpur	808.08	115.18	-85.79
13	Greater Mumbai	873.37	597.17	-31.64
14	Pune	985.55	684.89	-30.78
15	Nagpur	892.33	289.08	-67.50
16	Nashik	883.52	571.11	-35.52
17	Ludhiana	744.84	281.92	-62.77
18	Jaipur	979.17	114.32	-88.48
19	Chennai	839.69	250.84	-70.11
20	Coimbatore	771.71	146.19	-81.06
21	Madurai	726.77	187.30	-74.75
22	Lucknow	921.07	93.38	-89.88
23	Kanpur	917.65	82.45	-91.01
24	Allahabad	795.23	78.08	-90.17
25	Agra	837.94	72.70	-91.31
26	Varanasi	783.51	76.58	-90.17
27	Meerut	840.60	82.84	-90.15
28	Faridabad	896.00	141.14	-84.25
29	Kolkata	819.73	255.82	-68.75
30	Asansol	788.63	77.26	-90.21

## ii) **Factors influencing Under-spending**

There are a host of factors which influence the level of under-spending by local bodies. These could broadly be categorized as 'exogenous' or 'endogenous' in nature.

### **Exogenous Factors**

The exogenous factors are essentially those factors over which the MCs do not have any control. Since the level of spending depends upon the level of resources available with the MC, the delegation of revenue powers (fiscal decentralization) and grants (inter-governmental transfers), which determine the resources of the local bodies, would be the key exogenous factors influencing the ability of the MC to spend and provide these services. These factors could be captured in the form of 'dependency ratio' and 'decentralization ratio', defined as below:

- *Dependency ratio* refers to the share of grants a MC receives to its total expenditure.
- *Decentralisation ratio* refers to the delegation of autonomy in decision-making with respect to the finances of the MC. Revenue decentralization ratio is measured by ratio of MC's per capita revenue to State per capita revenue receipt.

### **(a) Dependency and Under-spending**

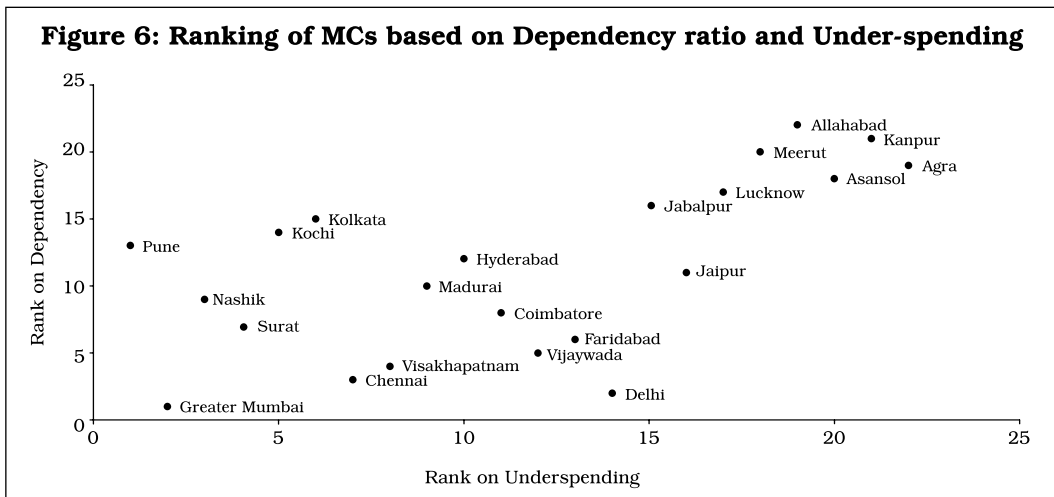
Table 30 juxtaposes the extent of under-spending with the dependency ratio of the MCs.

The rank correlation coefficient between these two series works out to 0.61. The coefficient is statistically significant at 1 per cent level of significance. Figure 6 presents the scatter diagram between under-spending and dependency on grants from higher level of governments. This indicates a significant positive

**Table 30: Dependency ratio and Under-spending of the Municipal Corporations**

Sl. No.	Municipal Corporation	Under Spending (%)	Dependency Ratio (%)
1	Greater Mumbai	31.64	0.69
2	Delhi	85.38	2.35
3	Kolkata	68.75	46.50
4	Chennai	70.11	3.97
5	Hyderabad	76.01	16.42
6	Kanpur	91.01	72.28
7	Pune	30.78	22.45
8	Surat	62.24	7.69
9	Jaipur	88.48	14.53
10	Lucknow	89.88	61.50
11	Agra	91.31	67.18
12	Nashik	35.52	8.98
13	Meerut	90.15	67.46
14	Faridabad	84.25	7.58
15	Visakhapatnam	74.73	4.03
16	Allahabad	90.17	72.67
17	Jabalpur	85.79	60.43
18	Coimbatore	81.06	8.01
19	Madurai	74.75	9.31
20	Vijayawada	81.40	4.80
21	Kochi	63.65	43.03
22	Asansol	90.21	62.07

relationship, implying that higher dependency would lead to higher under-spending.



**Table 31: Categorization of Municipal Corporations as per Dependency Ratio  
(Average of 1999-00 to 2003-04)**

<b>Parameter</b>	<b>Municipal Corporations</b>	<b>Top 5 Municipal Corporations</b>
At or Above Average (High dependency)	Kolkata Kanpur Pune Lucknow Agra Meerut Jabalpur Kochi Ahmedabad Allahabad Asansol	Kanpur (0.72) Allahabad (0.72) Agra (0.67) Meerut (0.67) Asansol (0.62)
		<b>Bottom 5 Municipal Corporations</b>
<i>Below Average</i> (Low dependency)	Greater Mumbai Delhi Chennai Hyderabad Surat Jaipur Vadodara Nashik Faridabad Vishakhapatnam Rajkot Coimbatore Madurai Vijayawada	Greater Mumbai (0.069) Delhi (0.023) Chennai (0.004) Vishakhapatnam (0.04) Vijayawada (0.05)

The MCs falling above and below the group average of the average dependency ratio (over the period 1999-2000 to 2003-2004) are shown in Table 31.

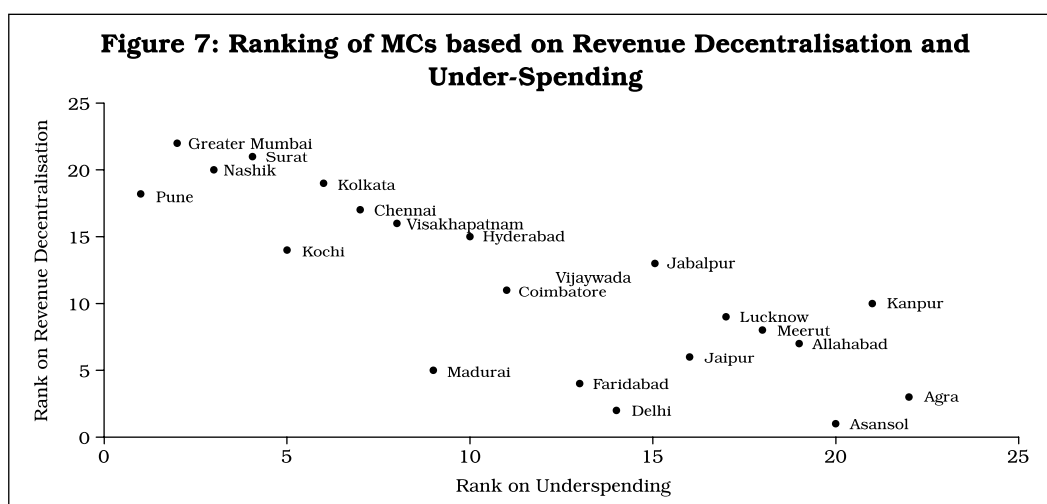
**(b) Decentralisation and Under-spending**

Table 32 compares the extent of under-spending and decentralization, a measure of delegation of tax powers to the MCs. Here, decentralization ratio has been measured as proportion of the MC's per capita revenue to State per capita revenue, over the time period of 1999-2000 to 2003-2004.

**Table 32: Decentralisation and Under-Spending of the Municipal Corporations  
(Average of 1999-2000 to 2003-2004)**

Sl. No.	Municipal Corporation	Under Spending (%)	Revenue Decentralisation Ratio (%)
1	Greater Mumbai	31.64	110.61
2	Delhi	85.38	18.03
3	Kolkata	68.75	67.65
4	Chennai	70.11	45.07
5	Hyderabad	76.01	34.43
6	Kanpur	91.01	24.67
7	Pune	30.78	61.19
8	Surat	62.24	79.92
9	Jaipur	88.48	21.69
10	Lucknow	89.88	23.77
11	Agra	91.31	19.55
12	Nashik	35.52	75.90
13	Meerut	90.15	23.53
14	Faridabad	84.25	19.82
15	Visakhapatnam	74.73	39.02
16	Allahabad	90.17	23.52
17	Jabalpur	85.79	25.67
18	Coimbatore	81.06	24.82
19	Madurai	74.75	20.31
20	Vijayawada	81.40	25.18
21	Kochi	63.65	26.76
22	Asansol	90.21	12.53

The results shown in Table 31 and the scatter diagram in Figure 7 confirm our *a priori* view that higher the revenue



**Table 33: Categorization of Municipal Corporations as per Revenue Decentralisation Ratio (Average of 1999-00 to 2003-04)**

<b>Parameter</b>	<b>Municipal Corporations</b>	<b>Top 5 Municipal Corporations</b>
At or Above Average (Highly decentralized)	Greater Mumbai Surat Nashik Pune Kolkata Chennai Visakhapatnam	Greater Mumbai (110.61%) Surat (79.92%) Nashik (75.9%) Kolkata (67.65 %) Pune (61.19%) Surat (38.99%)
		<b>Bottom 5 Municipal Corporations</b>
<i>Below Average</i> (Lowly decentralized)	Hyderabad Kanpur Jaipur Lucknow Agra Delhi Kochi Madurai Vijayawada Jabalpur Meerut Coimbatore Faridabad Allahabad Asansol	Asansol (12.53%) Delhi (18.03%) Agra (19.55%) Faridabad (19.82%) Madurai (20.31%)

decentralization, lower the level of under-spending. The rank correlation computed as per Spearman's rank correlation works out to be - 0.81 and has a desired negative sign. It is highly significant at 1 per cent level of significance.

Table 33 provides the list of MCs that fall above or below the group average decentralization ratio.

### **Endogenous Factors**

#### **(a) Revenue Administration**

This parameter refers to local body's efficiency in levying and collecting revenues which falls in its jurisdiction i.e, own sources of revenue of the MC. Although not a very accurate measure, it aims at measuring MC's performance with regard to own revenue.

The ratio of per capita own revenue of MC to State GDP (GSDP) per capita could be taken as a close approximation of the efficiency of revenue administration<sup>8</sup>. Table 34 provides a comparative scenario of under-spending and efficiency of revenue administration.

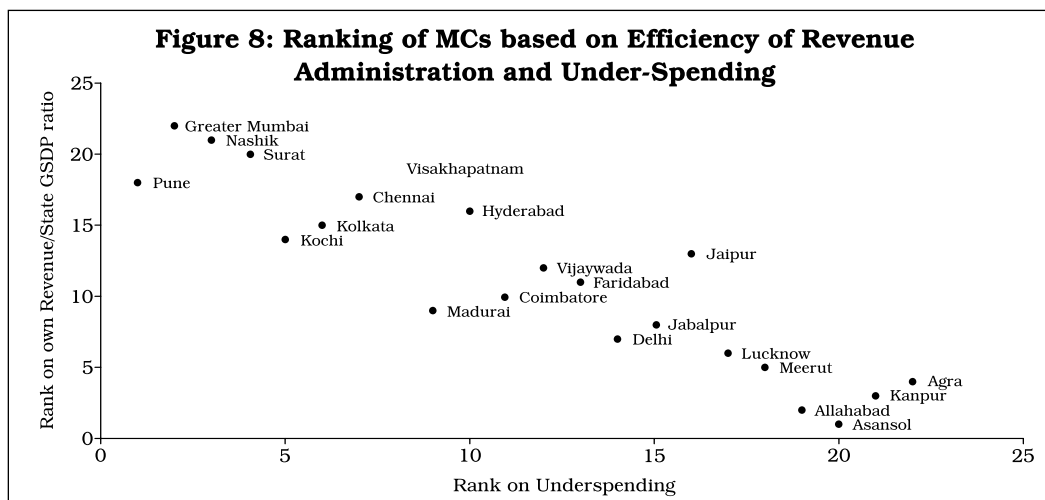
With efficient revenue administration reflected by own revenue as a proportion to GSDP, the availability of resources with the MC improves and level of under-spending is accordingly lower. Rank correlation among the two parameters works out to -0.913, which is statistically significant at 1 per cent level.

The scatter diagram in Figure 8 clearly reveals a negative relationship between efficiency of revenue administration and level of under-spending.

**Table 34: Efficiency of Revenue Administration and Under-Spending of the Municipal Corporations**

Sl. No.	Name of the Municipal Corporation	Under Spending (%)	Ratio of Per capita Own Revenue to GSDP per capita (%)
1	Greater Mumbai	31.64	18.45
2	Delhi	85.38	2.30
3	Kolkata	68.75	5.36
4	Chennai	70.11	6.61
5	Hyderabad	76.01	5.75
6	Kanpur	91.01	1.44
7	Pune	30.78	6.66
8	Surat	62.24	9.69
9	Jaipur	88.48	4.43
10	Lucknow	89.88	1.90
11	Agra	91.31	1.50
12	Nashik	35.52	12.26
13	Meerut	90.15	1.55
14	Faridabad	84.25	3.82
15	Visakhapatnam	74.73	7.25
16	Allahabad	90.17	1.27
17	Jabalpur	85.79	2.50
18	Coimbatore	81.06	3.80
19	Madurai	74.75	3.19
20	Vijayawada	81.40	3.91
21	Kochi	63.65	4.81
22	Asansol	90.21	0.73

<sup>8</sup> The ability of the local body to collect taxes also depends upon delegation of revenue powers.



A comparison of the own revenue with performance on individual taxes that are levied and collected by the Municipal Corporations would provide further insight into tax efficiency of the urban local bodies. Table 35 provides a comparative position of

**Table 35: Own Revenue-GSDP Ratio and Performance on Individual Taxes**

Sl. No.	Municipal Corporation	Own Revenue to GSDP	Property tax	Profession tax	Advertisement tax	Octroi Ratio
<b>High Own Tax</b>						
1	Greater Mumbai	8.63	×		×	√
2	Surat	9.93	√			√
3	Chennai	3.41	√	√	×	
4	Visakhapatnam	8.24	√	√	×	
5	Vijayawada	4.45	√	√		
6	Hyderabad	6.53	√	√	√	
<b>Lower Own Tax</b>						
7	Kochi	1.55	√	√		
8	Jabalpur	1.02	×	×		×
9	Nashik	1.30	×			√
10	Coimbatore	1.38	×	×		
11	Jaipur	.50	×		√	×
12	Madurai	.93	×			
13	Faridabad	1.11	×		×	

**Notes :**

√ : represents equal or above average performance,

×



different tax sources in order to identify the corporations with potential for improving tax administration

It is pertinent to note that all MCs, barring Mumbai, with above average own tax revenue have performed well in case of property tax and/or profession tax. In case of Mumbai, it has done well in case of Octroi. On the other hand, except Kochi, all MCs falling in the below average category have not done well in either of the major taxes.

**(b) Recovery of Cost**

Cost recovery of services is an important measure, which is used to assess the health of municipal finances. It can be broadly measured as a ratio of municipal fees and user charges to revenue expenditure incurred by an MC for the provision of respective services *viz.*, water supply, sanitation, health services, education and street lighting. As detailed data on service-wise user charges and fees are not available, the broad indicator of ratio of municipal fees and user charges to aggregate revenue expenditure has been used as a proxy. Table 36 makes a comparison of under-spending and cost recovery of the MCs. None of the MCs, barring Delhi, Visakhapatnam and Bhopal show a high proportion of cost recovery. It is less than 10 per cent in the MCs of Kerala and Tamil Nadu. Cost recovery has to be an integral part of service provision, especially when services can be measured and beneficiaries identified, as in case of water supply, education and health.

The scattered diagram in Figure 9 indicates a negative but relatively weak relationship between under-spending and cost recovery. In case of MCs such as Kanpur, Allahabad and Lucknow, despite higher cost recovery, under-spending has not been lower. Rank correlation for these two series is -0.39, which is significant at 10 per cent level.

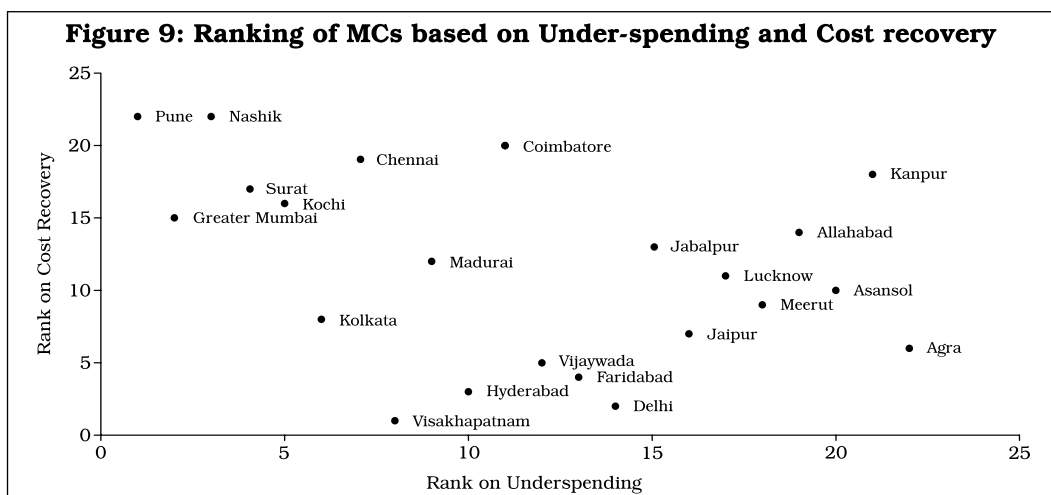
**(c) Quality of Expenditure**

The expenditure structure of Municipal Corporations throws some light on the relative importance assigned to each component in

**Table 36: Under-spending and Cost recovery of the Municipal Corporations**

Sl. No.	Municipal Corporation	Under Spending of the MC (%)	Average Cost recovery (%)
1	Hyderabad	76.01	38.88
2	Visakhapatnam	74.73	81.91
3	Vijayawada	81.40	37.48
4	Delhi	85.38	94.13
5	Surat	62.24	11.11
6	Bangalore	74.92	14.41
7	Kochi	63.65	7.76
8	Indore	75.54	31.83
9	Bhopal	84.50	62.85
10	Jabalpur	85.79	7.20
11	Greater Mumbai	31.64	11.16
12	Ludhiana	62.77	9.18
13	Jaipur	88.48	33.61
14	Chennai	70.11	7.74
15	Coimbatore	81.06	4.47
16	Madurai	74.75	4.79
17	Lucknow	89.88	9.82
18	Kanpur	91.01	3.90
19	Allahabad	90.17	6.06
20	Agra	91.31	23.25
21	Varanasi	90.17	9.34
22	Meerut	90.15	12.39
23	Faridabad	84.25	28.15
24	Kolkata	68.75	15.17
25	Asansol	90.21	13.08

the total expenditure and it also has a bearing on the financial position and service delivery.



### ***Relative shares of Capital, Maintenance and Establishment Expenditures***

While a low proportion of spending on establishment is desirable, too low a proportion may hamper the capacity for service delivery. Likewise, expenditure on capital works is important as it provides future sources of revenue; but very high proportion on it would have a bearing on the finances available for provision of services and even necessitate external support, in the form of either grants or borrowings. Table 37 presents the relative shares of various expenditure components of the MCs. It indicates that some of the MCs have an unsustainably high proportion of (more than 50 per cent) total expenditure on establishment and administration, which affects the future of their finance and their service delivery capacity. Likewise, some MCs have an abysmally low capital expenditure (less than 10 per cent to almost zero), which is equally detrimental to the health of civic finance and its long-term sustainability. It is, therefore, desirable to develop certain guidelines/norms for the municipal corporations towards spending on capital and its maintenance works, as well for rationalizing the staffing pattern so as to ensure that excessive amounts are not spent on staff.

### ***Establishment & Administration Expenditure and Under-spending***

The revenue expenditure, which comprises expenditures on (i) establishment and administration and (ii) operations and maintenance, assumes critical importance, as it relates to the provision of civic services to the people and their maintenance. However, a very high proportion of expenditure on establishment and administration can be detrimental to both the expansion of capital assets and maintenance of existing facilities. Thus, with a relatively lower proportion of expenditure devoted to establishment and administration, the MCs would be better equipped to provide

**Table 37: Relative Share of Expenditure Components of the MCs  
(Average of the Shares during 1999-2003)**

Sl. No.	Municipal Corporation	Share of Establishment & Administration Expenditure in Total Expenditure (%)	Share of Operations & Maintenance Expenditure in Total Expenditure (%)	Share of Capital Expenditure in Total Expenditure (%)
1	Hyderabad	56.95	22.19	19.82
2	Visakhapatnam	46.55	32.38	18.74
3	Vijaywada	46.55	32.38	18.74
4	Patna	53.09	26.46	N.A.
5	Delhi	43.71	2.18	6.08
6	Ahmedabad	0.00	0.00	23.82
7	Surat	37.61	8.01	39.47
8	Vadodara	41.53	20.03	13.48
9	Bangalore	49.00	4.72	N.A.
10	Kochi	16.01	32.94	1.25
11	Indore	28.61	12.15	25.96
12	Bhopal	20.64	11.06	2.85
13	Jabalpur	55.34	7.52	N.A.
14	Greater Mumbai	36.79	8.30	0.06
15	Pune	20.06	58.62	21.32
16	Nagpur	37.98	36.72	25.30
17	Nashik	25.03	20.56	42.29
18	Ludhiana	42.75	13.19	1.37
19	Jaipur	31.53	5.17	36.03
20	Chennai	42.77	4.76	21.61
21	Coimbatore	55.91	15.53	28.56
22	Madurai	53.21	2.34	29.98
23	Lucknow	48.83	14.12	23.96
24	Kanpur	66.89	17.15	1.50
25	Allahabad	51.03	18.89	0.24
26	Agra	50.72	4.16	12.41
27	Varanasi	50.93	6.05	0.11
28	Meerut	58.45	13.03	21.34
29	Faridabad	46.84	53.16	N.A.
30	Kolkata	61.30	7.39	8.72
31	Asansol	32.07	7.92	40.12
	<b>Total</b>	<b>36.25</b>	<b>14.43</b>	<b>12.37</b>

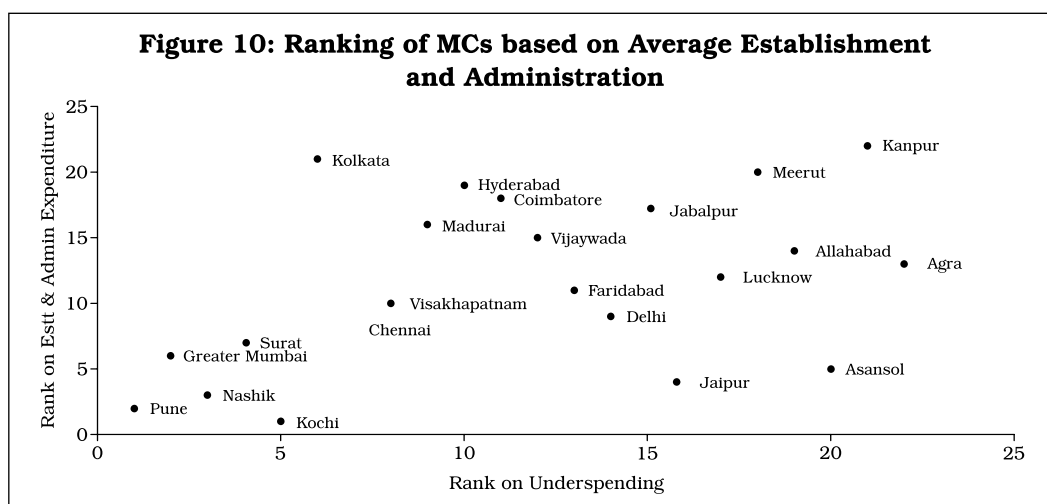
**Source:** Budgets of Municipal Corporations.

civic amenities. Table 38 compares the establishment and administration expenditure and under-spending of the MCs. The relationship of under-spending with the proportion of expenditure on establishment and administration is shown in the scatter diagram in Figure 10. It indicates a positive relationship conforming to a priori expectations. Rank correlation for these two series is 0.44 which is significant at 5 per cent level.

**Table 38: Average Establishment and Administration Expenditure of the Municipal Corporations (1999-2000 to 2003-2004)**

Sl. No.	Municipal Corporation	Under Spending (%)	Expenditure on Establishment and Administration to Total Expenditure (%)
1	Greater Mumbai	31.64	36.79
2	Delhi	85.38	43.71
3	Kolkata	68.75	61.30
4	Chennai	70.11	42.77
5	Hyderabad	76.01	56.95
6	Kanpur	91.01	66.89
7	Pune	30.78	20.06
8	Surat	62.24	37.61
9	Jaipur	88.48	31.53
10	Lucknow	89.88	48.83
11	Agra	91.31	50.71
12	Nashik	35.52	25.03
13	Meerut	90.15	58.45
14	Faridabad	84.25	46.84
15	Visakhapatnam	74.73	46.55
16	Allahabad	90.17	51.03
17	Jabalpur	85.79	55.34
18	Coimbatore	81.06	55.91
19	Madurai	74.75	53.21
20	Vijayawada	81.40	51.03
21	Kochi	63.65	16.01
22	Asansol	90.21	32.05

Table 39 provides a summary position on relationship of under-spending with other major variables as discussed above. Under-



**Table 39: Summary of the Assessment of Finances of Municipal Corporations**

Sl. No.	Municipal Corporation	Under-spending %	Dependency	Decentralisation	Revenue (Tax) Administration	Quality of Expenditure	Cost Recovery
1	Pune	30.78	√	√	√	√	
2	Greater Mumbai	31.64	√	√	√	√	×
3	Nazi	35.52	√	√	√	√	
4	Vadodara	50.43	√	√			
5	Surat	62.24	√	√	√	√	×
6	Ludhiana	62.77					×
7	Kochi	63.65	×	×	×		×
8	Nagpur	67.50					
9	Kolkata	68.75	×	√	√	×	×
10	Chennai	70.11	√	√	√	√	×
11	Visakhapatnam	74.73	√	×	√	√	√
12	Madurai	74.75	√	×	×		×
13	Bangalore	74.92					×
14	Indore	75.54					√
15	Hyderabad	76.01	√	×	√	×	√
16	Coimbatore	81.06	√	×	×	×	×
17	Vijayawada	81.40	√	×	×	×	√
18	Faridabad	84.25	√	×	×	×	√
19	Bhopal	84.50					√
20	Jabalpur	85.79	×	×	×	×	×
21	Jaipur	88.48	√	×	×		√
22	Lucknow	89.88	×	×	×	×	×
23	Meerut	90.15	×	×	×	×	×
24	Allahabad	90.17		×	×	×	×
25	Varanasi	90.17					×
26	Asansol	90.21	×	×	×	√	×
27	Kanpur	91.01	×	×	×	×	×
28	Agra	91.31	×	×	×	×	√
29	Patna	94.43					

√ : Above average performance.

× : Below average performance.

spending has been shown in the ascending order with the MC on the top being the best performer (with highest per capita spending on core services). Subsequent columns indicate status of individual MCs against various parameters that are expected to influence the level of under-spending. With a majority of the tick marks being concentrated towards the top, the influence of various factors on the level of under-spending is quite apparent.

#### (d) Debt Position

The debt position of MCs can be assessed in terms of the followings: a) use of debt and b) debt sustainability. The former has been examined by computing debt to capital expenditure ratio and the latter has been ascertained by computing interest coverage and debt coverage ratios.

#### *Use of Debt*

Borrowed funds are intended for creation/development of infrastructure by a MC, resulting in asset creation so that the returns generated from the assets can be utilized for servicing the debt (here, it is implicitly assumed that either returns are designed to be adequate or facilities are subsidized by upper tiers). The ratio of borrowings to capital expenditure of the municipalities provides an indication of the extent to which borrowed funds are spent on capital formation. A value of the ratio above one (a proportion greater than 100 per cent) will indicate that a portion of the borrowed funds is utilized for current consumption.

Table 40 indicates that except three MCs belonging to Kochi, Ludhiana & Allahabad no other MC have a borrowing to capital

**Table 40: Borrowings to Capital Expenditure Ratio of the MCs  
(Average of 1999-2003)**

Municipal Corporation	Loans (Rs. Lakhs)	Capital Expenditure (Rs. Lakhs)	Borrowings/Capital Expenditure ratio' (%)
Vijaywada	520	1495	34.74
Delhi	1253	4807	26.06
Ahmedabad	12205	17564	69.49
Surat	5653	18169	31.11
Kochi	1562	148	1053.03
Indore	1643	5323	30.86
Bhopal	16	283	5.66
Nagpur	2737	5620	48.69
Ludhiana	715	268	266.92
Jaipur	375	4875	7.69
Chennai	4244	11314	37.51
Coimbatore	763	1898	40.18
Madurai	1118	2666	41.92
Lucknow	2026	2595	78.09
Allahabad	124	37	333.78
Meerut	405	924	43.85
Asansol	26	755	3.38

**Source:** Budget documents of Municipal Corporations.

expenditure ratio of more than one, suggesting that the borrowed funds have been utilized for capital expenditure only.

### **Debt Sustainability**

Apart from the use of borrowings, debt sustainability of the MCs needs to be assessed, and this can be done in terms of two indicators: ratio of outstanding debt to total revenues and ratio of debt servicing to revenue receipts. As the outstanding debt details of the MCs are not available in the budget documents, the second measure is used in the study. It may be noted that debt repayments include both principal and interest components.

Table 41 sets out the information relating to debt repayment to revenue receipt ratio of the MCs. It reflects that the debt repayment of 18 MCs has not been very high. Excepting the cases of MCs of Chennai, Madurai and Vijayawada, wherein the debt repayment is over and above 10 per cent of their revenue receipts, there is a potential for using debt wisely, by the MCs for capital formation.

**Table 41: Debt Repayment to Revenue receipts ratio of the MCs  
(Average of 1999-2003)**

<b>Municipal Corporation</b>	<b>Debt Repayment (Rs. Lakhs)</b>	<b>Revenue Receipts (Rs. Lakhs)</b>	<b>Debt Repayment to Revenue receipts (%)</b>
Hyderabad	307	33882	0.91
Visakhapatnam	217	11007	1.97
Vijaywada	935	6165	15.17
Delhi	309	88030	0.35
Bangalore	2805	36954	7.59
Kochi	60	5168	1.16
Indore	304	17997	1.69
Greater Mumbai	29549	416203	7.10
Pune	216	50716	0.43
Nagpur	1574	24961	6.31
Nashik	2231	26830	8.32
Ludhiana	328	19467	1.68
Jaipur	301	12286	2.45
Chennai	6762	59103	11.44
Coimbatore	124	7210	1.72
Madurai	962	5660	17.00
Kanpur	68	10033	0.68
Kolkata	655	54239	1.21

**Source:** Budget documents of Municipal Corporations.



However, apart from the measure of debt service in relation to the revenue receipts, debt sustainability should be examined from the point of view of an MC's capacity to service debt. The capacity to service the debt refers to how easily and readily the MC will be able to meet its commitment in respect of the contractual interest payment and the repayment of debt. The MC's ability to service the liabilities can be measured with the help of coverage ratios. The coverage ratios establish relationship between committed liabilities, and the MC's surplus out of which these claims are to be paid. These measures try to relate the MC's surplus to the level of debt repayments with a view to assessing the degree of comfort with which the MC can meet these repayments. The following coverage ratios may be used to analyze a MC's ability to service committed liabilities.

### ***Interest Coverage Ratio***

This ratio is also called the "times interest earned" ratio and it measures the ability of an MC to pay the interest liability on debts. This is calculated as the ratio of operating surplus to interest payment\*. The Interest Coverage (IC) Ratio, therefore, measures how many times the interest liability of the MC is covered with the MC's operating surplus. The ratio gives an idea of how much fall in surplus the MC can sustain, before it defaults or borrows to meet the interest liability. Table 42 shows the performance of the MCs on this measure.

For the MCs whose interest payment details exist, the measure shows that they are on the higher side. The higher the IC ratio, the better it is both for the MC and for the lenders. For the MC, the probability of committing default is reduced and for the lenders, the

---

\* Operating surplus is defined as current revenue - operating expenditure (operation & maintenance including material as well as staff salaries). Given that the accounts are not segregated in a manner required to measure operating surplus, current expenditure net of interest payments has been used as operating expenditure for computation.

**Table 42: Interest Coverage Ratio of the Municipal Corporations  
(Average of 1999 – 2003)**

Sl. No.	Municipal Corporation	Interest repayment (Rs Lakhs)	Operating Surplus (Rs Lakhs)	Times Interest Earned Ratio (%)
1.	Hyderabad	307	6852	22.32
2.	Kochi	20	2604	130.18
3.	Indore	202	10064	49.82
4.	Nagpur	593	5155	8.69
5.	Nashik	1607	14565	9.06
6.	Jaipur	172	7489	43.54
7.	Chennai	1798	36629	20.37

**Source :** Budgets of Municipal Corporations.

MC is considered to be less risky. A lower IC ratio indicates a low surplus or a deficit of the MC in relation to its interest payment commitments.

Mathur and Ray (2003) provide criteria based on IC ratio as follows: a ratio less than 1.5 is poor, 1.5 to 3 is moderate, 3 to 6 is good and greater than 6 is favourable. Therefore, all the above MCs are on a favourable side of the measure.

### ***Debt Coverage Ratio***

The debt coverage ratio shows the relationship between the operating surplus of the MCs and the committed liability in respect of interest and principal. It is calculated as the ratio of operating surplus and debt repayment (interest and principal repayments). Table 43 provides the performance of the MCs on this measure.

A high debt coverage ratio is indicative of the MC's ability to meet its committed payment obligations easily, while a low ratio indicates its difficulty to meet the obligations.

According to Mathur and Ray (2003), the criteria laid down for this measure are as follows: a ratio less than 1 is poor, 1 to 2 is moderate, 2 to 4 is good and greater than 4 is favourable. For the MCs under study whose debt repayment details exist, the measure shows that all MCs except 4 fall in category of 'favourable'. Vijaywada and Madurai fall in 'moderate' category whereas Bangalore and Nagpur could be termed as 'good'.

**Table 43: Debt Coverage Ratio to Operating Surplus of the MCs  
(Average of 1999-2003)**

Sl. No.	Municipal Corporation	Debt Payment (Rs Lakhs)	Operating Surplus (Rs Lakhs)	Times Debt Covered (Operating surplus/ Debt payment)
1.	Hyderabad	307	6852	22.3
2.	Visakhapatnam	217	3551	16.4
3.	Vijaywada	935	1715	1.8
4.	Delhi	309	51917	168
5.	Bangalore	2805	7317	2.6
6.	Kochi	60	2604	43.4
7.	Indore	304	10064	33.1
8.	Greater Mumbai	29549	260181	8.8
9.	Pune	216	-19072	Negative
10.	Nagpur	1574	5155	3.3
11.	Nashik	2231	14565	6.5
12.	Ludhiana	328	8524	26
13.	Jaipur	301	7489	24.9
14.	Chennai	6762	36629	5.4
15.	Coimbatore	124	2500	20.2
16.	Madurai	962	1125	1.2
17.	Kanpur	68	1408	20.7
18.	Kolkata	655	15531	23.7

Source : Budgets of Municipal Corporations.

## 5.4 Projection of Investment Requirement in Urban Areas

This section attempts to project resource requirement for basic civic amenities via, water supply, sewerage, roads, solid waste management and street lighting and for the provision of mass urban transport systems as well as road infrastructure. For making these projections, various norms have been used: Zakaria Committee Norms (Basic amenities), Service cost Norms (Rail/ Road based mass transport) and the Expected Service cost (Inner and Outer ring roads). The details of methodology used for projections are provided below.

### 5.4.1 Basic Amenities

There would be need for resources for creating new infrastructure for the growing population (including backlog) and for maintenance of current and future assets. Thus, funds would be needed for: i) New infrastructure for backlog, ii) New infrastructure for incremental population and iii) Operation and Maintenance expenditure.

- (i) The investment needs for creating new assets for civic amenities *viz.*, water supply, sewerage, roads and street lighting were worked out using Zakaria Committee norms. In the case of solid waste management, the norms were worked out from the estimates made in Arabi (2006). These norms were adjusted for inflation assuming head line inflation of 5 per cent per annum during the projection period.
- (ii) It was assumed that there was a service backlog of 33 per cent *i.e.* one third of the population did not have service coverage<sup>9</sup>.
- (iii) Zakaria Committee norms were used for working out the operation and maintenance expenditure requirement for all the services mentioned at (i) except solid waste management<sup>10</sup>.

Thus, the resource requirement for incremental investment and O&M worked out for each year as:

*Incremental Investment Need = Zakaria Norm (adj)\* Incremental Population*

*O&M expenditure Needs = Zakaria Norm (adj) \* Population*

Resource requirement for backlog population worked out as:

*Backlog Investment Needs = Zakaria Norm (adj)\* Backlog Population*

The total resource needs for the provision of major civic services can be estimated by adding up:

*Incremental Investment Needs + O&M Investment Needs + Backlog Investment Needs*

Using the above estimates of total investment needs for the 35 MCs, the corresponding figure for the entire urban population is estimated.

---

<sup>9</sup> NIUA study (1998) states a 30 per cent backlog in the year 1997-98. Given that the availability of civic amenities has not improved since then and backlog would have increased, a conservative estimate of 33 per cent backlog has been assumed.

<sup>10</sup> Norms were worked out from Arabi (2006).

### 5.4.2 Urban Mass Transport Systems

Urban areas require not only the basic civic amenities but also other services like urban transport and similar public goods and services. An attempt is made to estimate the investment needs of providing (i) mass urban transport systems and (ii) major road infrastructure in the form of inner and outer ring roads for providing faster movement of vehicles. As these services are meant to be provided in metropolitan cities/agglomerations, the 35 MCs with urban agglomeration population more than one million population are considered and categorized into Class AA, A and B based on the prevalent city (MC) population as on 2001.

- (i) The mass urban transport systems considered include: elevated metro system for class AA and A cities (with service length of 100 and 50 km respectively) and bus rapid transit system for Class B cities (with a service length of 100 km). Therefore, for all the cities, according to their city class, the mass urban transport investment needs are estimated using the capital investment norms provided in Bandai and Coppice (2004) together with the assumed service length.

*Mass Rapid Transport System Investment Needs = Norm \* Service length*

- (ii) The major road infrastructure needs include: Outer and Inner ring roads for all class AA cities (with a service length of 100 km), Inner ring roads for class A cities (with a service length of 100 km) and Inner ring roads for class B cities (with service length of 50 km). The norms for Outer and Inner investment needs of the roads / expressways per km length in urban areas are formed using the actual cost estimates of their provision in Hyderabad<sup>11</sup>. Using these norms and coverage length, the investment needs of the cities for the provision of road infrastructure/ expressways is estimated.

---

<sup>11</sup> The Hyderabad Urban Development Authority (HUDA) has undertaken this major project in Hyderabad city and it shared the unit costs information, which form the norms used here.

**Table 44: Projection of Investment Requirement in Urban Areas**

Sl. No.	Infrastructure Component	Investment Need for Ten Years (2004-05 to 2013-14) (Rs Crore)*
1	Urban basic services	Rs 3,25,010
2	Mass urban transport services	Rs 2,53,700
3	Road infrastructure services	Rs 49,500
4	Total urban services	Rs 6,28,210

\*: At 2004-05 prices.

*Road infrastructure Investment Needs = Norm \* Service length*

Therefore, the total investment needs of providing urban infrastructure services can be expressed as:

*Total Urban Investment Needs = Basic Amenities Investment Needs + Mass Rapid Transport System Investment Needs + Major Road Infrastructure Investment Needs*

The estimate given in Table 44 shows that on an average investment requirement is around Rs 62,821 crore per annum at constant prices of 2004-05, which comes to 2.2 per cent of GDP in year 2004-05. Here, it may be noted that total revenues of ULBs remained stable at around 0.75 per cent of GDP, which is much less than the requirement.

### **5.5 Estimate of Potential for Revenue Mobilisation by ULBs**

As mentioned earlier, shortfall in resources is on account of the vertical imbalance as well as the nature of ULBs' own operations. The present section attempts to estimate the potential growth in ULB revenues assuming a status quo in fiscal federal relationship. Thus, it would indicate the size of revenue gap which would necessarily have to be met through major structural reforms in the nature of altering fiscal federal relationship.

- i) For working out potential revenue, separate estimates were made for tax and non-tax revenues and grants were assumed

to grow at historical growth rate. For working out tax revenue, estimates were made for major taxes *viz.*, property, advertisement and professional tax. For each tax, best performer among the 35 MCs was taken as the benchmark<sup>12</sup> and potential revenue was worked out assuming all ULBs are able to catch up with the benchmark<sup>13,14</sup>.

- ii) For working non-tax revenue, the optimal performer in terms of proportion of cost recovery was chosen as benchmark<sup>15</sup>. In the previous chapter, cost recovery has been defined as the ratio of user charges to revenue expenditure. Thus, to work out the potential non-tax collections, the proportion of cost recovery of the optimal performer was applied to aggregate revenue expenditures of ULBs in the country.

The sum of all above estimates provides the potential resource mobilization. However, the entire resources cannot be assumed exclusively available for the provision of core urban services or basic infrastructure services. Therefore, we use the proportion of these resources that would reach to these services<sup>16</sup> that give us utilisable

---

<sup>12</sup> The average of top performer MCs of class AA and A cities has been taken as benchmark.

<sup>13</sup> Computation of potential revenue would, however, be quite an involved exercise which needs to take into account myriad number of factors such as tax rate, tax base and tax exemption. Ignoring the tax rate factor, there could be many ways to enhance the tax base and reduce the exemptions granted. There are possibilities such as changing the base of the property tax, trade licensing fee, advertisement fee *etc.*, imposing vacant land tax, premium on Floor Space Index (FSI), rationalization of user charges, formulae for inter-governmental transfers *etc.* Exploring those is beyond the scope of the present study.

<sup>14</sup> In an emerging global scenario, sunrise industries such as IT are contributing towards employment and income generation in cities. While income, turnover and services generated through these activities do not fall within the revenue powers of the municipal bodies, there could be some indirect positive contributions in terms of profession and property tax. But these aspects could not be quantified in this study due to lack of detailed data.

<sup>15</sup> It may be noted that cost recovery to the tune of 90 per cent of revenue expenditure, as is found in the case of best performer MC (Vijayawada) is ridden with difficulties as it leaves little room for revenue expenditure on establishment and administration for service provision. An optimal performer MC (Bhopal) with a cost recovery of 60 per cent of revenue expenditure is, therefore, taken as an appropriate benchmark.

<sup>16</sup> Here, the average proportions of spending on core urban services to total expenditure of average and best performer MC (Kolkata) of the 11 MCs, for which continuous data were available, stood at 35% and 65% respectively. These have been used as proxies.

**Table 45: Projection of Potential Revenues of ULBs (2004-05)**

Sl. No.	Revenue Source	Projected Revenues (Rs Crores)
1	Property Tax	10,577
2	Profession Tax	2,389
3	Advertisement Tax	510
4	All Major Taxes (1+2+3)	13,476
5	Non Tax (User charges & fees)	9,746
6	Grants in Aid	4,064
7	Total Potential Revenue (4+5+6)	27,285
8	Total Utilisable revenue for Core Service provision (best case – 65%)	17,736
9	Total Utilisable revenue for Core Service provision (conservative case – 35%)	9,550

resources for service provision in the best case and in the average case scenarios. The estimates that have been made as per the procedures delineated above for the year 2004-05 are set out in Table 45.

The above Table shows that if current status in fiscal federal relationship continues, ULBs in India together have the potential to raise revenues only up to Rs.27,285 crore in 2004-05. This amounts to about 1.0 per cent of the GDP. Of these funds, in a best case scenario, only 2/3rd would be available for asset creation after meeting the current expenditure. Thus, the utilizable resources of the ULBs only for core service provision even after attaining the benchmark figures of resource mobilization fall short of investment needs (Rs.28,000 crore) to the tune of Rs.10,000 crore in the best scenario and Rs.18,000 crore in the conservative (average) scenario for the year 2004-05, which are substantial amounts that cannot be raised by ULBs assuming status quo in all respects. There is, therefore, urgent need for reforms to mobilize the funds needed for investment in urban infrastructure as estimated in the previous section. Given the magnitude of the problem, it is necessary to have a Centre-State-Local-Private Partnership (CSLPP) for development of urban infrastructure.

## **5.6 Some Observations**

The key conclusions that emerge from the foregoing aggregative and Municipal Corporation-wise analysis of municipal finances are:



- Analysis of the revenue and expenditure of the MCs reveals that most of them are generating revenue surplus and overall resource gaps are not very large. At the same time, assessment of municipal finance reveals that spending by all the municipal bodies is lower than that required for providing a minimum level of civic amenities. The study observes that this apparent contradiction of sound fiscal health and high level of under-spending is due to statutory obligations, whereby ULBs are generally bound to restrict their expenditure to the resources available to them and also are not granted liberal permission by State Governments to incur debt [Mathur and Thakur (2004)].
- In view of the above observation, the study has undertaken an assessment of municipal finance in “normative terms”, besides the “standard approach” of revenue or fiscal balance.
- A comparison of per capita spending on core services by MCs in terms of the Zakaria Committee norms indicates that the level of under-spending on an average works out to be about 76 percent. Significantly, MCs belonging to Bihar and Uttar Pradesh are the ones that have highest level of under-spending whereas those belonging to Maharashtra, Gujarat are among the best performers.
- Reasons for under-spending could be traced to MCs’ own operations (endogenous) as well as to policy issues related to the upper tiers of Governments (exogenous). Exogenous factors include dependency for resources on upper tiers of the Government and inadequate delegation of revenue powers. Endogenous factors include inefficient revenue (tax) administration, low cost recovery and poor quality of expenditure.
- MCs which have lower level of under-spending levels or better performance have fared well on 4 out of 5 criteria *viz.*,

dependency, decentralization, tax administration and expenditure quality. On the other hand, MCs with ranking “below average” on these 4 parameters are also the ones which have been spending less on core civic amenities. Thus, the analysis suggests that restructuring of revenue powers may be given top priority by State Governments if urban amenities are to be improved.

- Though delegation of revenue powers is a key factor, need for efficient revenue (tax) administration cannot be underplayed. Examination of various taxes across the local bodies reveals that property and profession taxes are important sources. (Octroi is the most important source of revenue in municipal corporations belonging to Maharashtra and Gujarat). The local bodies need to adequately tap the existing avenues. Unit area system of computation, based on self-assessment principle, with respect to property tax needs to be extended to all MCs and in the case of MCs where Octroi has been a major source they should be adequately compensated when Octroi is abolished. Other sources like entertainment tax, development charges, betterment levies *etc.* need to be tapped.
- Quality of expenditure, measured as establishment and administrative expenditure as a proportion of total expenditure also turns out to be a major factor in determining the ability of MCs to provide core services. Lower spending on administrative purposes would leave more resources with the MCs to provide for civic amenities. This calls for rationalization of the work force and reduction in spending on establishment and administration.
- There is a very weak link between under-spending and cost recovery. Interestingly, MCs such as Mumbai, Surat and Pune which are among the best performers in terms of other financial parameters, have below average user charges. This is because

the municipalities are resorting to lower use of user charges than would be desirable. In fact, on an average the cost recovery is below 1/4<sup>th</sup> of the expenditure incurred by the MCs. Considering the benefit principle<sup>17</sup>, there is a large scope for improvement in levying User Charges.

- It is apparent from the analysis that there is a need to substantially increase the spending by local bodies. Given the constraints faced by State Governments, it is essential that the MCs be granted access to borrowed funds. At least there are two convincing arguments in favour of MCs going for borrowed funds. First, there is a scope for MCs to go in for borrowed funds as their current level of indebtedness is not very large. Secondly, there is a scope to raise the user charges which are abysmally low across the States. Enhancement of user charges would make the new projects undertaken with borrowed funds economically viable and ensure that MCs are debt-sustainable.
- Investment requirement for urban infrastructure has been estimated at about Rs.63,000 crore per annum for the next ten year period (2004-05 to 2013-14), which forms about 2.2 per cent of GDP. Assuming the current status quo in fiscal federal relationship, the study has projected that ULBs together have the potential to raise revenues only up to about 1.0 per cent of the GDP.
- Given the magnitude of the resource gap of the municipal sector as a whole, it is necessary to have a Centre-State-Local-Private Partnership (CSLPP) for development of urban infrastructure. Revisiting revenue assignment is the first task of a partnership.

---

<sup>17</sup> Benefit principle imply that services that local governments provide should be paid for by those who benefit from them (Bird, 1976).