

Assessment of Receipts and Expenditure of The Municipal Corporation of Delhi

In the Memorandum submitted to the Commission, MCD has indented for additional financial demand amounting to Rs 2,683.8 crore during 1996-2001 (Annexure 6.1). The demand comprises items of recurring nature, namely, Resource Gap estimated at Rs 262.2 crore, Impact of Fifth Pay Commission recommendations at an annual rate of Rs 215 crore (Rs 1,075 crore over the period), impact of two DA instalments at the rate of Rs 14 crore per instalment with multiplier effect (Rs 420 crore) and natural calamities relief (Rs 53.4 crore), together adding to Rs 1810.1 crore for the full five-year period. Demand for certain items on a one-time basis aggregated to Rs 873.2 crore, reflected in the year 1996-97, and included Operations and Maintenance (Rs 525 crore), Shortfall in sanitation (Rs 288 crore), delinking of sewers from storm water drains (Rs 25 crore), shortfall in expenditure on additional budgetary allocations for new works (Rs 22.3 crore) and expenditure on elections (Rs 13 crore).

Review of MCD's Approach

Based on the actual average annual growth rate, over past 12 years, of 14.43 per cent for receipts and 14.52 per cent for revenue expenditure, the Memorandum projected a resource gap of Rs 1.5 crore for the year 1996-97, increasing to Rs 6.2 crore in 2000-01, a total of Rs 18.17 crore for the reference period. However, MCD has argued that the resource gap so projected did not take into account the need for growth in expenditure in real terms (which had virtually remained stagnant at Rs 187 Rs 212 per capita between

1984-96); and that for making a positive impact on the level of services for the growing population as also for keeping the infrastructure in sound state, it would be essential to ensure that the expenditure was allowed to grow at the rate of 10 per cent per annum in real terms. Accordingly, assuming a rate of inflation of 10 per cent between 1996-2001 an annual increase of 20 per cent in nominal terms has been built into their projections of revenue expenditure. The resource gap, when reworked using this revised rate of projected growth for expenditure, but retaining the observed growth rate of receipts of 14.43 per cent, has been worked out to Rs 262.2 crore for the five-year period - as against of Rs 18.17 crore thrown up by projections made on the basis of the observed rates of growth of receipts and expenditure.

Commission's Reservations and Critical Evaluation of Additional Demands

(1) Estimation of Resource Gap: The Commission observed that for forecasting the resource gap, MCD has used the aggregate series of receipts and for expenditure, only Account I (A) has been taken into account. For projecting receipts and expenditure, MCD's Memorandum has adopted the arithmetic average growth rate. The aggregate series of total receipts included MCD's own taxes, non-tax receipts, grant-in-aid, share in assigned taxes as also, quite erroneously, the ways and means advances. Receipts from own taxes, in turn, represented the sum total of property tax, tax on vehicles and animals, theatre tax, tax on advertisement, duty on transfer of properties, tax on building applications, tax on consumption and sale of electricity and education cess.

The Commission have basic reservations about the methodology used by MCD and have, therefore, not found it possible to accept the projections and the resultant resource gap. A major lapse has been MCD's failure and/ or reluctance to estimate the revenue gap for the reference period although the relevant data required for this purpose is available in the Memorandum. The revenue gap, as is known, is met through external sources (grants, share in assigned taxes and borrowings) but with the added responsibility of accommodating therein capital expenditure. No doubt, much of the capital expenditure is and can perhaps continue to be met from Plan resources. Since those funds are external to the own kitty of the Corporation, over which it has no control, its requirements for

meeting the gaping shortfall in infrastructure by marshalling requisite investment must be specifically assessed and provided for. In the absence of the estimates for revenue gap during 1996-2001 designing a policy framework for subvention by the Government on the basis of resource gap alone would be a rather inaccurate, rough and ready exercise. The Commission have, therefore, decided to follow a more rigorous and sound analytical approach.

The choice of the growth rates for receipts and expenditure used by MCD in projecting receipts and expenditure is faulty *ab initio*, there being no logic behind leaving certain accounts out of the picture. This matter was specifically discussed with Chief Accountant of the Corporation. Further, these growth rates representing the average percentage changes recorded over the preceding years are prone to an in-built bias caused by any wide fluctuations during the period and are therefore technically incorrect to be used for making projections into the future. The technically sound and widely accepted method would be to adopt growth rates derived from regression analysis, as these eliminate/ minimise the effect of abnormal fluctuations.

Further, in projecting expenditure, instead of using the observed growth rate of 14.52 per cent per annum (assuming for the sake of argument that their methodology was correct), as already noted, MCD has applied an arbitrarily inflated rate of 20 per cent, composed of an assumed rate of inflation of 10 per cent; and another 10 per cent for real rate of growth. No rationale was forthcoming for assuming a 10 per cent rate of inflation, which by all accounts was unjustifiably high. In all their exercises the Tenth Finance Commission, the Planning Commission and the Planning Board for NCT of Delhi assume a much lower rate of inflation of 7.5 per cent (which happens to be higher than the current rate of inflation). Incidentally, the rate of 14.52 per cent would have ensured a 10 per cent growth in expenditure in real terms after taking care of the current rate of inflation. The implicit assumption of MCD that inflation rate had no nexus with growth rate of receipts but impinged only on the expenditure side was lacking in logic. Again, MCD erred in adopting separate but single growth rate for aggregate receipts and expenditure which failed to capture the varying inter-temporal behaviour of their different components. As different components grow at different rates, more appropriate would have been to adopt

a differential regime of observed growth rates for each of the major components. Failure to do so vitiated the projections both for receipts and expenditure as the weightage and rates of growth for different component showed wide variations, e.g., own taxes - 17.89 per cent, shared taxes - 9.18 per cent, education - 11.57 per cent and conservancy - 19.01 per cent under non-Plan, etc.

For some inexplicable reasons, all non-Plan transactions were not taken into account by MCD in its projections. It restricted itself to Account I(A) omitting the transactions in Accounts III, IV and V and also without measuring the impact of Plan on non-Plan budget. In other words 5 per cent to 10 per cent of non-Plan transactions with compounding effect were not factored into their analysis. Simultaneously, MCD included the non-Plan loans secured on three occasions during the period in projecting the receipts, thereby over-stating growth rates and projected receipts with consequential effect on estimated gaps for the future as well as for each of the years over the reference period.

(2) *Shortfall in Expenditure on Operations and Maintenance (O&M)*: Amongst the one-time items, MCD projected a demand of Rs 525 crore - at the rate of 15 per cent of the capital cost - on account of shortfall in O&M of municipal assets, composed of Rs 225 crore for assets created before 1985-86; and Rs 300 crore for assets created thereafter. Application of a unified rate across the board by MCD is contrary to the accepted practice that the provision for operation and maintenance should not only be asset specific but wherever possible should also take into account the age of the asset. The demand was also not projected on annual basis but was for past arrears representing the accumulated shortfalls between money required and that actually spent on O&M, the latter stated to be only 10 per cent of the requirement. While the Commission felt greatly concerned about the poor maintenance of capital assets - an obligatory function of MCD - and about the need to provide adequate funds for this purpose, nevertheless the methodology employed by MCD for estimating legitimate requirement on this account was lacking in sound basis, both on facts and on logic.

(3) *Shortfall in Budgetary Allocation of New Works:* The Commission also failed to appreciate the circumstances wherein after seeking allocation for Rs 22.28 crore in 1996-97 for new works, no gaps were identified for subsequent years.

(4) *Funds for Natural Calamities:* The projected demand of Rs 53.43 crore for extending relief from natural calamities was derived by applying the observed growth rate of 14.52 per cent on expenditure at Rs 7 crore incurred in 1995-96. The Commission are of the view that expenditure on natural calamity relief is not susceptible to projections by applying a pre-determined rate of growth as the requirement was contingent to the happening of certain adverse natural events. The matter, therefore, called for separate and different treatment. This notwithstanding the expenditure incurred in 1995-96 has already been factored into the projections by MCD while estimating the gaps. Clearly, therefore, a separate demand tantamount to a double count.

(5) *Savings on Account of Handing Over of Hospitals:* There are also other minor infirmities in the projections, e.g., the saving as a result of State Government's decision, in 1996, to take over the colony hospitals under Medical Relief was not taken into consideration by MCD. The Memorandum mentioned the expenditure on total medical relief in 1995-96 at Rs 57.47 crore. Likewise, the aggregate rate of growth used for projections included the expenditure on fire service although this activity stood transferred to the State Government since 1995-96.

(6) *Impact of Fifth Pay Commission:* The Memorandum was also silent on the basis of arriving at the projected requirement on account of implementation of recommendations of Fifth Pay Commission and DA instalments. All subsequent queries to ascertain the basis/ rationale for the projected demands failed to reveal the arithmetic employed by MCD in reaching the stated figures.

Commission's *de novo* Assessment of Financial Needs

In the above background, the Commission had no option but to make *de novo* projections on transparent and technically sound basis and to estimate the gaps between

MCD's receipts and expenditure in the years to come upto 2000-01 for purposes of recommending appropriate regime of fiscal devolution.

(1) Assessment of Revenue and Resource Gaps: Commission's re-assessment of the forecast and the consequential determination of gaps, the revenue gap is taken as the difference between MCD's receipts from internal sources and its total non-Plan revenue expenditure; and the resource gap or the budgetary gap as the difference between its total receipts and total non-Plan expenditure. Revenue gap has been estimated on the basis of revenue transactions in Account I(A), committed Plan revenue expenditure of Account II; and Account III; and the resource gap by additionally including the revenue transactions in Account IV and V also. For quantifying these gaps budgetary data of the time series from 1984-85 to 1995-96 have been used to determine the income-buoyancy and income-elasticity of receipts and expenditure respectively; and based on these coefficients, their respective growth rates have been arrived at, which in turn have been used to extrapolate the series for the period of award, 1996-97 to 2000-2001 with 1995-96 as the base year. Use of separate buoyancy coefficients, for receipts became unavoidable as it was not feasible to segregate from the data received from MCD - the effect of additional resource mobilisation in the time series for receipts and to determine its elasticity coefficient. Simultaneously, projections were also carried out by applying the trend growth rate estimated by adopting the regression method. The results were found to be strikingly similar.

In generating the aggregate series for revenue expenditure, expenditure of capital nature was first netted out from the total expenditure. Further, adjustments were made by netting out the expenditure incurred on fire services, colony hospitals and terminal tax agency as these functions are no longer required to be performed by MCD. The debt charges, being a function of repayment schedule and the rate of interest are not generally susceptible to forecasting by trend behaviour and have, therefore, been estimated by independently projecting liabilities on each debt on the basis of an analysis of the terms of individual loans contracted upto 1995-96.

In reassessing the receipts and expenditure, Plan receipts and Plan capital expenditure have not been included in the time-series data. MCD's Plan expenditure is entirely financed by grants/ loans by the Government/ Planning Commission released through the State Government and the budgets are generally balanced, so much so that if in any particular year, the loans/ grants are not fully utilised the balance is netted out from subsequent years' grants/ loans; and any excess in Plan expenditure over and above loans/ grants has to be met by MCD from its own resources. Apropos, Commission's projections exclude the Plan receipts and Plan capital expenditure. However, the impact of Plan expenditure on non-Plan expenditure due to committed liabilities at the end of each Plan have been fully provided for in estimating the non-Plan revenue expenditure.

DERIVED VARIABLES

Data series on non-Plan budgetary transactions have been adjusted for estimating gaps and resulting identities are as follows:

1. Total Exp = {Rev Exp + Cap Exp}
2. Rev Exp = [(A/c I (A) - (Fire Service+ Exp on TTA + Colony Hospitals + Debt Charges)) + A/c III]
3. Cap Exp = {A/c I (A) + A/c IV + A/c V}
4. Debt Charges = {Interest + Instalments}
5. Receipts = {Internal + Grants + Revenue-sharing}
6. Grants = {A/c I (A) + A/c III + A/c V}
7. Revenue Sharing = {Terminal Tax + Motor Vehicle Tax + Entertainment Tax}
8. Grants for Education (Current) = {Exp on Education * 0.5}
9. Grants for Education (Proposed) = {Exp on Education * 0.6}
10. Rev Gap = {Internal Receipts - Rev Exp}
11. Resource Gap = {Total Receipts - Total Exp}

CLASSIFICATION OF RECEIPTS

Receipts have disaggregated source-wise as follows;

1. Internal Receipts

- a. Domestic Taxes (i). Property Taxes and (ii). Other Taxes
- b. Non-tax receipts

2. External Receipts

- a. Share in Assigned Taxes in

- i. Terminal Tax (Compensation in lieu of abolition of Terminal Tax since 1993-94),
- ii. Entertainment Tax, and
- iii. Tax on Motor Vehicles.

- b. Grants-in-Aid for education and maintenance of Resettlement Colonies.

On the receipts side no adjustment has been considered necessary in case of 'internal source'. In case of receipts on account of 'external source'; loans have been excluded for reasons already stated. Receipts on account of terminal tax and grants for education have been substituted by independent forecasts. The grants for education have also been treated differently. These are specific purpose matching grants, based on net non-Plan revenue expenditure incurred by MCD on certain approved items of expenditure on education. To project this grant the observed series of expenditure on education was first adjusted by netting out non-eligible expenditure items and receipts (e.g., fines and fees) from gross expenditure as reflected in the budget. "The Grants-in-aid to Local Bodies in Union Territory of Delhi Rule, 1990" stipulate the quantum of grants at 60 per cent of the expenditure incurred on eligible items in the preceding year. The receipts on account of education grants were, therefore, projected on this basis. Similarly, this component was segregated from committed Plan expenditure on education. The Commission note that notwithstanding the provisions contained in the Grants-in-aid Rule, 1990, MCD was being provided only 50 per cent of the eligible expenditure on education as grant and inquiries made failed to uncover the reasons for the discrepancy; nobody seemed to know or care. MCD deserves to be duly compensated for this deficiency.

Classification of Expenditure

Non-Plan expenditure has been classified as follows:

- i. General Administration
- ii. Education
- iii. Libraries
- iv. Public health
- v. Medical relief net of five hospitals
- vi. Conservancy and street cleansing
- vii. Scavenging, drains and sewers
- viii. Roads and public streets
- ix. Buildings, land acquisition and management
- x. Licensing, removal of encroachment etc.
- xi. Gardens and open spaces
- xii. Markets and slaughter houses
- xiii. Miscellaneous, net of debt charges and expenditure on Terminal Tax Authority
- xiv. Developmental charges
- xv. Grants to institutions, Stipends and Cultural activities
- xvi. Reserve for unseen charges
- xvii. Special Funds
- xviii. Pension Funds
- xix. Salary Equalisation Fund, and
- xx. Transfer to Plan deficit.

In January, 1993, the Government of India abolished the terminal tax but decided to compensate the loss of revenue of the local bodies by giving them 'grants' calculated at 10 per cent compound increase each year on the base of the proceeds during 1992-93. For Account III grants have been retained as equivalent to projected expenditure as it is on cent per cent re-imbursement basis.

Receipts were projected on the basis of sub-aggregates and the revenue expenditure on the basis of its functional classification and each was then aggregated. The disaggregated approach was preferred as it enabled capturing separate trend behaviour of various components, each comprising items with more or less homogenous characteristic; and simultaneously took care of variations in their individual coefficients and relative weights. In case of a few minor items with negative coefficients, the observed value for 1995-96 was retained for all the years of extrapolation.

The projections for the period 1996-2001 were made by adopting elasticity/buoyancy-based growth rates assuming that receipts and expenditure were effected linearly by movements of State Income (State Domestic Product). The strength of this assumption is borne out by the values of R^2 shown in each case.

On the above basis, the Commission reassessed the resource surplus at Rs 253.64 crore and the revenue deficit at Rs 996.58 crore, compared to a resource gap of Rs 262.12 crore projected by MCD for the reference period. (As already noted, no projections have been made by MCD for revenue gap).

Estimated Revenue / Resource Gap (Aggregate of 1996-97 to 2000-01) (Rs in crores)	
Projected Revenue gap	(-) 996.58
Add:	
a. Share in assigned taxes	589.36
b. Grants	886.20
Balance	(+) 478.98
Less:	
i. Capital expenditure	91.90
ii. Repayments of loan instalments	133.45
Resource surplus	(+) 253.64

The Commission has reassessed the requirement of Rs 1,075 crore for all the other items aggregating to Rs 2,421.71 crore as projected by MCD.

(2) *Impact of Fifth Pay Commission:* MCD have estimated, although no basis has been provided, the impact of implementation of the Recommendations of Fifth Pay Commission at the rate of Rs 215 crore per annum aggregating to Rs 1,075 crore during 1996-2001. *Prima facie*, this appears to be on the higher side. The Commission, therefore, decided to re-assess its impact. However, in the absence of any supporting data furnished by MCD, the only basis available to the Commission was the Report of the Fifth Pay Commission, 1997 which estimated the cost of their recommendations as:

"the amount received by a government employee/ pensioner comes to around Rs 10,547 per year or Rs 879 per month."

Subsequently, the Government modified the recommendations of the Pay Commission with regard to pay fixation and decided to add an amount representing 40 per cent of the basic pay in the pre-revised scale to the emoluments as on 1.1.1996, (as against 20 per cent recommended by the Pay Commission). Accordingly, the Commission's projections are based on this enhanced rate and cover total number of employees whether or not paid from non-Plan account. Based on the total number of employees with MCD and its composition between serving employees and pensioners the Commission worked out the average amount for the two categories separately at Rs 17,833 and Rs 4,697 respectively and used this to project the additional burden of MCD on this count. The underlying assumption being that the average burden per employee in the case of MCD would not be materially different than that in case of Central Government employees/ pensioners. For Account III, this impact was arrived at on proportionate basis. The total net impact on account of the implementation of the recommendations of the Pay Commission including arrears, taken together for the serving employees and the pensioners, is net estimated at Rs 623.19 crore (as against Rs 1,075 crore sought by MCD). The Commission are conscious that this may not an entirely satisfactory method of estimating the additional burden on account of pay revision but it is nevertheless confident, that this will not be an under-estimate considering that the

proportion lower end employees (safai-karmcharis, manual workers etc) is much higher in MCD than in Government of India. The estimates of the Commission have been scaled down to provide for 60 per cent of the share of expenditure on establishment in education received by MCD as grants approximately Rs 145.21 crore in 1996-2001.

(3) *Impact of DA Instalments:* The impact of two DA instalments at the rate of Rs 14 crore each, increasing in arithmetic progression by Rs 28 crore each year, has been projected by MCD at Rs 420 crore. The Commission are of the view that as the total expenditure has been projected on the basis of income-elasticity which *ipso facto* has taken care of the inflationary impact in the forecast period, there was no justification for a separate additional provision. In this connection, the observations of the Tenth Central Finance Commission (p.15) are very instructive and bear reproduction here:

"3.66. We have noticed that almost all State Governments are following the same pattern in payment of dearness allowance as the Central Government. The sanction of dearness allowance instalments by the Central Government is followed sooner or later by the States. Since we have taken note of the expenditure figures of 1992-93 in our estimates for arriving at the base year estimates, we are of the view that the expenditure on dearness allowance instalments sanctioned upto that year are adequately provided for. The trend growth rates of expenditure adopted for arriving at the base year also take into account the expenditure liabilities which have arisen on account of payments of dearness allowance during 1993-95. In our forecast, we have already provided adequately for the effect of such price increase on non-Plan expenditure through the price elasticity of such expenditure".

(4) *Provision for Natural Calamities:* On the demand of Rs 53.43 crore for natural calamities, the Commission are of the view that while it will not be either feasible or appropriate to quantify the provision for natural calamities in advance, it needs nevertheless to be recognised that there is a need for prompt release of funds, when required. For this purpose, funds should be placed, without loss of time, at the disposal of the agency responsible for executing the work. Experience shows that if the funding body is different from the implementing body, valuable time was lost in seeking authorisation from the competent authority in times of crises. In these circumstances, the Commission opt for a separate treatment for it.

In this context, the Commission note that a Natural Calamity Fund is presently maintained by the State Government. In order to bring transparency and instil confidence in implementing agencies, it would be desirable in Commission's view, that the Fund should be managed by a Committee comprising the Lt. Governor, the Chief Minister, the Chief Secretary, the Mayor, the Commissioner, MCD and the Administrator of NDMC, with the Finance/ Planning Secretary as Secretary of the Fund. While it should be left to the State Government to decide the size of the corpus, this Committee should be charged with the specific responsibility of carrying out the assessment of requirement of funds on each occasion and to arrange for its expeditious release.

(5) Shortfall in Expenditure on Sanitation and De-linking of Sewer Lines: A one-time demand for shortfall in sanitation amounting to Rs 288 crore has been raised by MCD which, in fact, is a repetition of the demand made in the Interim Memorandum submitted to the Commission regarding improvement of sanitation services in Delhi. Commission's views in this regard have already been documented in its Interim Report on the subject. The Commission had recommended a devolution of Rs 18.5 crore as revenue expenditure (including Rs 10 crore for the purchase of poly-packs) and Rs 75 crore as capital expenditure (for the purchase of equipment and construction of *dalaos* etc.) for the year 1996-97. For the following year, the Commission had recommended the devolution of Rs 20.1 crore as revenue expenditure. Since revenue expenditure is recurring in nature, it has been estimated, for the rest of the period, on the basis of annual growth rate on the assumption that purchase of poly-packs would continue. The Commission reiterate the same.

Similarly, the Memorandum has reflected a demand of Rs 25 crore on account of delinking of sewer from storm water drains. This has already been considered, accepted and recommended for devolution, by the Commission in its Interim Report.

(6) Shortfall in Provision of Expenditure on Operations and Maintenance: In case of expenditure on O&M, MCD's demand of Rs 525 crore represents the cumulative shortfall, upto 1995-96, in money that was needed for proper maintainannce and actually spent. It is composed of Rs 75 crore for assets created before 1986-87 in roads and

buildings, education and medical sectors; and Rs 150 crore for assets in other sectors. The corresponding demand for maintenance of assets created after 1986-87 is Rs 100 crore and Rs 200 crore respectively. As already stated, the requirement of funds has been estimated in an entirely unsatisfactory manner, without sound basis in facts and logic. The Commission have, therefore, reassessed the requirements themselves. It may, however, be conceded straightaway that in doing so the Commission were severely handicapped for want of requisite data which MCD remained unable to furnish.

The Commission aggregated the total capital expenditure over the reference period under both Plan and non-Plan accounts to arrive at the investment in new assets in all sectors. A like amount was added as the proxy value for the assets created prior to 1984-85. A rate of 5 per cent of capital value per annum was adopted as amount needed for maintenance. Thus, O& M requirement in the base year was arrived at. This was then projected for the award period following the same methodology. To eliminate the possibility of double count this was then netted by the projected expenditure on operation and maintenance during the award period. The resultant figure worked out to Rs 588.41 crore.

(7) *Committed Expenditure of Plan Projects:* MCD in its Memorandum have pointed out that an amount of Rs 141.29 crore was transferred from Plan to non-Plan budget in the year 1989-90 and Rs 171.83 crore, 187.69 crore and 201.92 crore in the succeeding years. However, no amount has been included in their projected demand of Rs 2,683.83 crore during the award period. Besides the expenditure on maintenance of completed Plan schemes/ projects, the expenditure on establishment and contingency of these schemes/ projects also convert to non-Plan revenue expenditure at the expiry of the Plan. In assessing the total non-Plan revenue expenditure of MCD for the award period, the Plan revenue expenditure on the establishment and contingency on schemes/ projects completed during the Eighth Plan period for the year 1995-96 has been transferred as non-Plan revenue expenditure and from 1996-97 onwards has been projected at the assumed rate of inflation of 7.5 per cent (compound) with 1995-96 as the base. It has been possible to do so as separate data of expenditure on establishment and contingencies for the Plan schemes/ projects was available in MCD. In the case of GNCTD, as separate

information for these components was not available, 35 per cent of the total Plan revenue expenditure in the base year 1995-96 has been treated as non-Plan revenue expenditure for maintenance, establishment and contingencies taken together and has been projected at the assumed rate of inflation, i.e. 7.5 per cent. It may be of interest to note that the Tenth Finance Commission assumed 30 per cent of the total Plan revenue expenditure as the share of these items in the case of States other than special category states and 40 per cent in the case of the latter and applied buoyancy rates thereon to arrive at the base year figure which was then adjusted for the assumed rate of inflation ranging between 7.5 per cent to 5 per cent.

While examining the question of maintenance of capital assets, the Tenth Central Finance Commission (p. 14) observed that this was a neglected area in most of the States *"in view of the paucity of resources"* and expressed the hope that the possibility of maintenance *"being done by groups of beneficiaries or non-governmental organisations or even though private parties could be explored by the States if they happen to be cost-effective options"*. Further, noting that the most of the money provided for maintenance was diverted to payments of salaries and wages rather than to material and equipment necessary for maintenance work, the Tenth Finance Commission expected that *"... not more than 20 per cent of provision would be spent on establishment"* As the problems for maintenance whether of municipal or of State/ Centre Government assets cannot be strikingly dissimilar, the Commission commend the above suggestion of the Tenth Central Finance Commission as worthy of adoption by the municipalities.

(8) *Expenditure for Conducting Elections*: MCD has also claimed an amount of Rs 13 crore on account of election expenses. Commission note that whereas the elections of the State Assembly are conducted by the State Governments, when elections to the Parliament and State Legislature are held simultaneously the expenditure is shared by the two in a predetermined manner. Thus, the basic principle in this regard is that election for a particular level of government are to be financed by that level of government. There is no justification to deviate from this principle. Moreover, the Commission also understood that the expenditure on municipal elections in Delhi was only Rs 6 to 7 crore and not Rs 13 crore as demanded by MCD. The Commission, therefore, decided to take into

consideration the actual expenditure incurred in holding the municipal election in 1996-97 of Rs 8 crore as one-time non-Plan liability while ascertaining the gaps.

(9) *Loan Liabilities:* MCD has projected, without furnishing any data, a loan liability amounting to Rs 388.5 crore and have sought either its write-off or conversion into grants. As against this, the Commission have reassessed the loan liability taking into account the repayment schedule valid for the reference period and the rate of interest separately for each loan contracted upto 1995-96. Interest has been provided on diminishing balances on the basis that there should be no default in repayment of instalments.

(10) *Adverse Fiscal Impact of Expenditure on Rural Areas:* MCD have argued that it is the only municipal authority in the country which has been called up on to provide civic services in its rural areas concentrated in Nazafgarh and Narela zones. As per 1991 census, the rural population of MCD was 9.49 lakh. The provision of these services entails an additional financial burden on MCD as the resource base of rural areas was found to be too weak to sustain even a moderate dose of resource mobilisation. For example in 1995-96 the total expenditure incurred in Nazafgarh and Narela Zones was Rs.62.44 crore (Rs.42.56 crore in Nazafgarh and Rs.19.88 crores in Narela). The accounts of rural areas within rural zones form an integral part of zones' accounts and are not separately maintained. However, compared to the expenditure incurred the total receipts of rural areas would not be significant. Following the recommendations of the Morarka Commission (1968) regarding payment of special grants to MCD to cover its entire net deficit in respect to rural areas provide a separate account of income and expenditure was made. MCD maintained a separate account during 1969 to 1974-75. During this period expenditure was in excess of receipts by 19.77 crores and quoting the National Institute of Urban Affairs' report that - Municipal Corporation of Delhi - A Study on its Finances (June, 1989) "During 1977-81 this increased to Rs.2581.05 lakhs." The Government, however, did not implement this recommendation of the Morarka Commission with the result that MCD continues to bear the additional financial burden on this account. MCD, inter alia, sought that and the Commission fully endorse that special grants for provision and maintenance of services in the rural areas to cover the net

deficit in respect of rural areas. As an alternative NIUA's recommendation that "Since there already exists Panchayati Raj Institutions (PRI) as also the field administration of Delhi Administration, the local function may be financed out of PR funds or the allocations of the Delhi Administration for rural development. If at all the MCD has to provide services in rural areas, the MCD should be given a rural development grant" are worth considering."

In the light of the foregoing, the Commission reassessed the Corporation's receipts, non-Plan revenue expenditure and the resultant revenue/ resource gap of MCD. The detailed exercise is presented in Annexures 8.2 to 8.4 along with necessary elaborations showing disaggregated trend rate and buoyancy/ elasticity trend rates applied, the non-Plan grants for education and for Resettlement Colonies, re-assessment of additional demands indented by MCD including impact of Pay Commission, expenditure on operation and maintenance and debt repayment liability. With regard to grants for education and Resettlement Colonies, the implicit assumption is that those would continue to flow to MCD on the same basis as at present. The comparative picture that emerges is:

Estimated Revenue / Resource Gap of MCD and DFC
(1996-97 to 2000-01)
(Rs in crores)

	MCD	DFC
A. Total Expenditure (A.I + A.II)	4,695.64	4,731.09
A.I. Total revenue expenditure	4,695.64	4,505.74
A.II. Total capital expenditure	Included in A.I	225.35
B. Total Receipts (B.I + B.II)	4,433.52	4,984.73
B.I. From Internal Sources	Separate	3,509.16
B.I.a. Tax receipts	projections	3,119.94
B.I.b. Non-tax receipts	have not been	389.22
B.II. From External Sources (As per existing fiscal transfers policy)	done.	1,475.56
B.II.a. Share in assigned taxes	Included in B	589.36
B.II.b. Grants-in-aid		886.20
C Revenue gap - {Surplus (+) / Deficit(-)} [B.I - A.I]		-996.58
D Resource gap - {Surplus (+) / Deficit(-)} [A - B]	-262.12	253.64
E. Additional Financial Requirements as per Memorandum's	-2,421.71	-1,429.88
E.I. Revenue account	-2,174.43	-1,404.88
(1). Impact of Fifth Pay Commission	-1,075.00	-623.19
(2). Natural Calamities	-53.43	0.00
(3). Impact of 2 DA Instalments Annual @ Rs 14 cr.	-420.00	0.00
(4). Shortfall in Sanitation	-288.00	-185.28
(5). Elections	-13.00	-8.00

(6). Expenditure on O&M	-525.00	-588.11
<i>E.II. Capital account</i>	-47.28	-25.00
(8). Delinking of Sewers from Storm Water Drains	-25.00	-25.00
(9). Shortfall in Budgetary for New Works	-22.28	0.00
F. Aggregate Revenue Surplus (+) / Deficit (-) [B.I - (A.I + E.I)]		-2,401.46
G. Financed through Receipts from external sources		-1,475.56
H. Balance after financing through external sources		-925.90
I. Add: Expenditure on capital account		-250.35
J. Aggregate Resource Surplus (+) / Deficit (-) [B - (A + E)]	-2,683.83	-1,176.24

- Notes: 1. Projections of receipts by MCD includes the effect of share in assigned taxes, grants and loans in Account I(A).
2. Projections of expenditure by MCD includes the effect of, among others, loan repayment (instalments and interest) and capital expenditure.
3. Separately revenue gaps were not estimated.
4. Under expenditure on O&M, MCD's figure is on account of shortfall upto 1995-96 and no account for future made made. But on the contrary, DFC's estimates are on annual basis for the period of award.

In nutshell, for the reference period, the Commission have projected a revenue deficit of Rs 996.58 crore (as has been mentioned earlier no projections for this have been made by MCD); and against the projected resource deficit of Rs 262.12 crore by MCD, Commission's estimate is a surplus of Rs.253.64 crore. The Commission's estimate for additional financial requirements on account of impact of Pay Commission etc. is Rs 1,429.88 crore against Rs 2,421.71 crore projected by MCD. The aggregate resource gap after taking into account the impact of these items as estimated by the Commission is Rs.1,176.24 crore against Rs 2,683.83 crore estimated by MCD.

Estimated Revenue / Resource Gap of MCD: (Aggregate of 1996-2001)	
	Rs in crores
1. Internal Receipts	3,509.16
2. Revenue Expenditure	4,505.74
3. Revenue Gap (1-2)	(-) 996.58
4. Grants	886.20
5. Revenue Gap after adjusting for grants (3-4)	(-) 110.38
6. Non-Plan Capital Expenditure	(-) 225.35
7. Resource Gap to be met through tax-sharing (5+6)	(-) 335.73
8. Estimated Share in Assigned Taxes on present basis	589.36
9. Resource Gap (7-8)	(+) 253.64

The Commission's projections and the consequential gap did not take into account the incidence of what is generally designated as the committed liabilities created as a result of transfer of revenue components of the Plan budget to the non-Plan budget after

Assessment of Receipts and Expenditure of New Delhi Municipal Council

In its Memorandum submitted to the Commission, NDMC has made projections of its receipts and expenditure and determined the resultant surplus/deficit for the period 1997-98 through 2000-2001, i.e. for four years only against the award period of five years of 1996-97 through 2000-01.

In doing so, internal receipts have been projected by NDMC on simple trend line of average increase since 1992-93 at the rate of 12 per cent; assigned taxes at the rate of 13 per cent; and non-Plan grants at the rate of 16 per cent per annum. On the expenditure side, salary and pensionary benefits have been first stepped up by 30 per cent in 1997-98 over 1996-97 to provide for the incidence of the Fifth Pay Commission; and thereafter at a trend rate of 15 per cent. Maintenance expenditure is projected to increase at 7 per cent to meet normal escalation in cost (implying a 7 per cent rate of inflation). Capital expenditure on non-Plan side has been estimated as per "*likely cost of projects in progress decided to be taken up to 200 per cent*", without any explanation as to how this has jumped from Rs 13.75 crore in 1995-96 to Rs 51.20 crore in 1997-98.

On this basis, NDMC has projected its gross receipts (including supply of electricity and water) to grow from Rs 515.12 crore in 1997-98 to Rs 719.82 crore in

2000-2001. Similarly, its gross expenditure has been estimated to rise from Rs 527.19 crore to Rs 731.72 crore over the same period. These have resulted in a revenue surplus of Rs 92.51 crore but a resource deficit of Rs 43.21 crore during 1997-98 to 2000-2001 - a four-year period, implying that NDMC will need funds over and above its revenue surplus, grants and share in assigned taxes for meeting its projected non-Plan capital requirements.

Unlike MCD, NDMC has not made any specific demand for additional funds either for items of recurring nature or otherwise. In very general terms, the Memorandum seeks higher allocations for 'massive investment' required for infrastructure sectors. This has been justified in view of the need for large-scale augmentation in existing infrastructure which was set up about half a century back. The Memorandum does not suggest even vaguely the amount likely to be required for this purpose or the basis arriving at that. Likewise, though the Memorandum speaks of NDMC's compost plant which has been a loss-making unit and is projected to be so in future also, no estimate of the compensation asked for has been provided. Merely asking 50 per cent of the expenditure incurred on certain activities as grants, without either quantifying or providing any basis for the same cannot, in itself, be a justification for additional funds.

The Commission note that by and large NDMC's projections suffer from the same infirmities as in the case of MCD such as use of aggregate series and simple averages as trends for projections. Additionally, even at aggregate level, at least in some cases - the most important of them being internal receipts - the growth rates have been derived by NDMC on the basis of average increase since 1992-93, i.e. for only a period 3 to 4 years. Strangely, in the instant case, the projected period is longer than the observed period. Be that as it may, the Commission consider it appropriate that the projections and the requirement of funds for the two local bodies should be assessed on a uniform basis and period and accordingly decided to replicate the methodology and classification used in the case of MCD.

Apropos, the time-series from 1984-85 to 1995-96 has been used to determine the income-buoyancy and income-elasticity coefficients of receipts and expenditure

respectively and based on these coefficients the respective growth rates have been determined which in turn have been used to extrapolate the series for five years of 1996-2001, with 1995-96 as the base year. The year-wise estimates and detailed exercise along with necessary elaboration, disaggregated trend rates and buoyancy/ elasticity trend rate applied, the non-Plan grants for education, impact of the Fifth Pay Commission, separately with and without taking into reckoning supply of electricity and water, is presented at Annexures 9.1 to 9.3.

Presented below are, first, the estimates of revenue and resource gaps estimated by NDMC in their Memorandum, followed by Commission's own assessment of the same.

Estimated Revenue/Resource Gap of NDMC as per Memorandum (1997-98 to 2000-01) (Rs in crores)					
Detail	1997- 98	1998- 99	1999- 00	2000- 01	Total
NON-PLAN EXPENDITURE					
1. Salary	122.20	140.53	161.60	185.85	610.18
2. Pensionary benefits	16.30	18.77	21.59	24.81	81.47
3. O & M	250.35	267.87	286.62	306.68	1111.52
4. Sub-Total	388.85	427.17	469.81	517.34	1803.17
5. Capital	51.20	58.58	60.96	63.34	234.08
6. TOTAL	440.05	485.75	530.77	580.68	2037.25
RECEIPTS					
7. Internal	407.24	451.84	496.27	540.33	1895.68
8. Assigned	12.90	14.39	15.87	17.36	60.52
9. Grants	7.84	8.92	16.00	11.08	43.84
10. Total	427.98	475.15	528.14	568.77	2000.04
ESTIMATED GAP (SURPLUS + / DEFICIT -)					
11. Revenue gap (7-4)	18.39	24.67	26.46	22.99	92.51
12. Resource gap (10-6)	-12.07	-10.60	-2.63	-11.91	-37.21

Estimated Revenue and Resource Gap of NDMC by DFC (Aggregate of 1996-97 to 2000-2001) (Rs in crores)	
1. Internal receipts	3,089.69
2. Revenue expenditure	3,268.15
3. Revenue Gap	(-) 178.46
4. Education Grants	58.81

5. Revenue Gap with adjustment of Grants	(-)119.65
6. Share in assigned taxes	91.75
7. Revenue Gap with adjustment of share in assigned taxes	(-)27.90
8. Non-Plan Capital Expenditure	68.77
9. Uncovered Resource Gap	(-) 96.68

The resulting findings of the projections of receipts and expenditure are summarised below:

- ⇒ The NDMC is projected to have an aggregate revenue deficit of Rs 178.46 crore during 1996-2001.
- ⇒ After including non-Plan education grants of Rs 58.81 crore, the revenue deficit is reduced to Rs 119.65 crore.
- ⇒ After taking into account its estimated share, on the existing basis, in assigned taxes of Rs 91.75 crore, the balance show a deficit of Rs 27.9 crore on aggregate basis
- ⇒ On aggregate basis, after adjusting for non-Plan capital requirements of NDMC of Rs 68.77 crore, there will be deficit of Rs 96.68 crore.

Assessment of Receipts and Expenditure of Government of National Capital Territory of Delhi

The Commission is required as per its TOR, to have regard, among other considerations, to the overall resource position of Government of National Capital Territory of Delhi (GNCTD). In this context, the Commission requested GNCTD to furnish their forecast of receipt and expenditure on revenue and capital account for the period 1996-97 to 2000-01. GNCTD furnished their forecast piecemeal. Forecast relating to the revenue receipts was received in September 1996 and that relating to non-plan expenditure in December 1996. The final revised forecast alongwith the memorandum was received as late as in June 1997 i.e. two years and three months after the appointment of the Commission. Assessment of resource position of GNCTD have been carried out by the Commission on the basis of analysis of the revised forecast of GNCTD and the past trends (for eleven- year period, 1985-86 to 1995-96).

Forecast Made by GNCTD

GNCTD have mentioned in their memorandum that while making recommendations on devolution of funds to the municipalities for the period 1996-2001 the forecast in respect of entire receipts and expenditure/disbursements of GNCTD (before transfers to local bodies) are required to be looked into. Their forecast is related to the Consolidated Fund of GNCTD only, since the Public Account has not yet been transferred to GNCTD. The forecast has been furnished separately for non-Plan and plan

accounts. This has further been segregated into revenue and capital accounts. It is based on time series data of income and expenditure from 1985-86 to 1995-96, for which actuals are available. Data relating to non-Plan revenue account is given in Annexures 10.1, and 10.2.

The forecast furnished by Government of NCT of Delhi is summarized below. To provide a benchmark for comparison, figures for the base year 1995-96 have also been indicated. (It may be noted that receipts and expenditure on police have been separately shown).

(Rs crore)

	1995-96 Actual	1996-2001 Forecast
I. Non Plan Account		
A. Revenue		
a. Receipts	2150.84	17546.01
b. Expenditure	787.57	9892.39
c. Surplus/Deficit	1363.27	7653.62
B. Capital		
a. Receipts	29.00	160.00
b. Expenditure	308.28	165.25
c. Surplus/Deficit	-279.28	-5.25
C. Total Surplus/Deficit (Non-Plan)	1083.99	7648.37
II. Plan Account		
A. Revenue		
a. Receipts	122.32	785.75
b. Expenditure	199.50	2004.32
c. Surplus/Deficit	-77.18	-1218.57
B. Capital		
a. Receipts	796.38	4430.84
b. Expenditure	256.05	3819.49
c. Surplus/Deficit	540.33	611.35
C. Total Surplus/Deficit (Plan)	463.15	-607.22
III. Total Surplus/Deficit (Plan + Non Plan)	1547.14	7041.15
IV. Police		
a. Expenditure	328.71	112.12
b. Receipts	23.35	10.31
c. Net (a-b)	305.36	101.81
V. D.V.B. (DESU)		
Plan - Grants	0.02	0.25
- Loans	298.20	2473.39
Non-Plan Assistance	225.70	2285.74
Interest Payments	0	-523.03

Total - D.V.B.	523.92	4236.35
VI. D.T.C.		
Non-Plan Loans	0	333.99
Equity/Loans	0	355.00
Repayment of Loans	0	-26.00
Interest Payments	0	-33.34
Total - D.T.C.	0	629.65
VII. Total Net Surplus/Deficit	717.86	2073.34

GNCTD have thus indicated a surplus of Rs 2073 crore which can be considered as the resource pool available for devolution to bridge the fiscal gaps of the local bodies both under non-Plan and Plan accounts (revenue as well as capital), after providing for their own expenditure in full as well as on account of financial support for capital expenditure to Delhi Vidyut Board and Delhi Transport Corporation.

The projections of GNCTD are not based on any uniform trend. For 1996-97 they have adopted Revised Estimates (RE) and for 1997-98 they have adopted the modified figures of Budget Estimates (BE) by excluding resource augmentation of that year. Taking modified figures for 1997-98 as base, the projections for rest of the forecast period have been done by GNCTD on the basis of past trend in some of the cases. In other cases the projections are based on the assessment of the concerned department. It has not been explained as to how the concerned departments arrived at the projected figures. It has been mentioned that these projections are supposed to encompass growth of income and prices as also the effect of discretionary measures. There is no mention of any specific rate of inflation assumed nor any comparison between tax/GSDP ratio of the forecast period (1996-2001) and actual period (1985-96). There is also no indication as to at what rate the GSDP is expected to grow during the forecast period, which would be a major factor influencing growth in revenues.

The approach adopted by GNCTD for projections as explained above cannot, therefore, be accepted by the Commission as technically sound. In fact, the base year should have been 1995-96 and projections for the forecast period based on the observed past trend. The Commission, therefore, decided to reassess the forecast of GNCTD on transparent and technically sound basis.

Reassessment of Receipt and Expenditure

While reassessing receipts and expenditure of GNCTD the Commission have confined its exercise to the non-Plan revenue account only. This is because major part of the Plan expenditure is financed mainly from grants and loans from the Central Government and loans raised under small savings & market borrowings. So far as transfers on Plan account are concerned, these will be in accordance with the size of the Five Year and Annual Plans of GNCTD and the pattern of assistance under different schemes as determined by the Planning Commission for each 5- year or annual plan.

The Commission have used the time series of budgetary data of GNCTD for the period from 1985-86 to 1995-96 (last year for which actuals were available) to determine the buoyancy coefficients. Thereafter, buoyancy-based growth rates were applied to the actuals for 1995-96 (base year) and the figures for the forecast period from 1996-2001 were projected, the projection methodology remaining the same as in case of MCD and NDMC.

Revenue Receipt

Total revenue receipt for the forecast period as projected by the Commission comes to Rs17630 crore against Rs17546 crore projected by GNCTD. Notwithstanding GNCTD's figures for 1996-97 being higher by Rs22 crore in comparison to the projections made by the Commission, they have projected total receipts less by Rs 84 crore. As already mentioned GNCTD have adopted three different ways for projections. On the other hand, the Commission have applied buoyancy coefficients uniformly for projecting tax and non-tax revenue. Be that as it may, there is remarkable convergence of the results of two approaches - a rare coincidence !

Tax Revenue

In tax revenue, there is an overall difference of Rs 36 crore in projections made by GNCTD and the Commission. The total tax revenue projected by the Commission comes to Rs 17331 crore against Rs 17295 crore by GNCTD. Going by individual items of tax receipts, it has been observed that in case of Sales Tax the difference in the projections of the Commission in comparison to that of GNCTD is on lower side and very significant. In other cases the projections of the Commission are on the higher side.

(i) *Sales Tax*: In this case no trend rate has been applied by GNCTD whereas the Commission have worked out the projections on the basis of buoyancy. Not only this, the growth over previous year during the forecast period is not uniform but erratic in the projections of GNCTD. An amount of Rs 12898 crore has been projected to be collected by GNCTD against the Commission's projections of Rs 12324 crore during the forecast period. This difference of Rs 574 crore is significant for the purpose of working out the overall surplus. However, in the absence of any explanation for higher projections by GNCTD the Commission adopted their own projections.

(ii) *State Excise*: As in case of Sales Tax, GNCTD have not adopted any trend in case of excise revenues as well. The Commission have, however, worked out the projections based on buoyancy coefficient of 0.85. GNCTD estimated the projections of Rs 2320 crore against Commission's estimates of Rs 2504 crore.

(iii) *Stamps And Registration*: Projections of GNCTD have come down from a growth of 25.56 per cent in 1996-97 to 20.04 per cent in 2000-01 with a major decline of (-)14.04 per cent in 1997-98 resulting in an overall average growth rate of 14.31 per cent for the forecast period. This is against the trend growth rate of 21.22 per cent for the period 1985-86 to 1995-96. The projections of GNCTD have been reassessed on the basis of buoyancy coefficient of 1.28 and work out to Rs1157 crore against GNCTD's forecast of Rs898 crore.

(iv) *Taxes On Vehicles*: On the basis of buoyancy coefficient of 1.13 the projections for the forecast period works out to Rs598 crore against GNCTD's forecast

of Rs474 crore at an average growth rate of 10.09 per cent against the observed trend rate of 18.45 per cent.

(v) *Other Taxes & Duties:* Receipts on account of Betting tax, Entertainment tax and newly introduced Luxury Tax are included in this head. The projections have been made on the basis of buoyancy in this case also. However, as assessed by GNCTD, receipts in respect of the newly introduced Luxury Tax have been added to the figures for 1996-97 and 1997-98 to the tune of Rs 30 crore and Rs 100 crore respectively. Our projections in this case work out to Rs749 crore against forecast of GNCTD at Rs 704 crore.

Non-tax Revenue

Since non tax revenue constitute only about 3 per cent of total revenue receipts in 1995-96 and does not contain any major item of receipts, it has been projected as a single item unlike tax revenue. The police receipts have been excluded while interest receipts and dividends have been included during the actual period while projecting the figures for the forecast period on the basis of buoyancy. GNCTD have projected each item separately. In some cases trend growth rate has been adopted and in other cases where the growth rate was negative or negligible 5 per cent rate has been adopted. There is significant difference in the projections of Rs 299 crore made by the Commission and Rs251 crore by GNCTD.

It would be worth mentioning that most of the local bodies/plan implementing agencies, to whom loan is provided whether under plan or non-Plan, are default in payment of interest due. Similar is case of dividend receipt from State Corporations and Cooperatives. Otherwise, there is enough scope to increase the interest receipt.

Non-Plan Revenue Expenditure

(Before transfer of assigned taxes to Local Bodies)

Total of our projections for the forecast period from 1996 - 2001 worked out on the basis of buoyancy of major items of expenditure comes to Rs 8792 crore against

GNCTD's projections of Rs 10004 crore. The major items of expenditure (95-96) projected individually constitute about 87 per cent of total expenditure and are - interest payment, public works, education, medical and public health, housing, social security & welfare, roads and bridges and non-plan grants to local bodies. Rest of the items constituting about 13 per cent have been clubbed together for the purpose of projections. While calculating projections on trend basis GNCTD applied minimum and maximum limits of 10 per cent and 20 per cent respectively. No such ceiling has been applied by the Commission. Important items of expenditure which need special mention are given below:

(i) *Pensions*: GNCTD have included expenditure on Pensions in their forecast whereas the Commission have not included any expenditure on this item in the projections for the reasons explained in chapter 7.

(ii) *Interest Payments* : GNCTD have given year-wise figures of loans likely to be received during the forecast period along with interest accruing during this period. The Commission have also adopted their estimates of receipts on account of likely loans. GNCTD have calculated the interest on outstanding loan on small saving and Central assistance taken together at interest rate of 14 per cent in 96-97 and 15 per cent in rest of the years. However, since interest rates on small saving loans and central assistance loans are different, the Commission have calculated interest on the basis of current rate of interest which is 14.5 per cent for small saving loans and 13 per cent for central assistance loan. In the Commission's projections the interest payments work out to Rs 2080 crore against GNCTD's projections of Rs 2202 crore.

(iii) *Non-plan Grants*: The Commission have assumed that non-plan grants to the local bodies would continue to flow on the same basis as at present. These grants are meant to cover special expenditure liabilities entrusted to the local bodies. These grants have been provided to grow on the same basis as other expenditure i.e. on the basis of buoyancy coefficients. GNCTD have, however, excluded these grants from their projections.

(iv) *Fresh Liabilities*: The Government of NCT submitted that subsequent to the presentation of budget for the year 1997-98 some fresh liabilities had arisen. These are - committed liability on account of Plan schemes completed by 1996-97 and impact of Fifth Pay Commission. Expenditures on these items have also been included as under:

(a) *Committed Liabilities*: GNCTD have taken Revenue Plan expenditure of Rs281.74 crore for Annual Plan 1996-97(RE) without excluding expenditure on Centrally Sponsored Schemes (CSS). This expenditure does not include the Plan revenue expenditure provided to the municipalities. They have adopted a norm of 60 per cent of the Revenue Plan expenditure for 1996-97 to arrive at the committed liability for the year 1997-98 and then applied a growth rate of 15 per cent for the remaining period.

The Commission have not accepted their estimates as the norms are too high and GNCTD have not excluded expenditure on Centrally Sponsored Schemes. The Commission have adopted a norm of 35 per cent (Tenth Finance Commission adopted a norm of 30 per cent) for committed expenditure in 1997-98 in respect of Plan schemes completed by 31st March, 1997. The 5 per cent additionality has been allowed to compensate the impact of Pay Commission recommendations. The expenditure of Rs50 crore in respect of CSS has also been excluded. The estimates of committed liability for 1997-98 thus arrived at have been protected for the remaining period of the forecast against inflation taken @ 7.5 per cent as estimated by the Planning Commission in their guidelines for the Ninth Plan. An amount of Rs 363 crore has thus been calculated for the forecast period by the Commission against GNCTD's projections of Rs 844 crore.

(b) *Impact of Pay Commission*: The impact of Pay Commission in the forecast period has been calculated by the Commission on the basis of the financial implications estimated by the Pay Commission and subsequent decisions taken by the Government for its implementation including mode of payment of the arrears from 1-1-96 to 30-9-97. Accordingly, total impact during the forecast period work out to Rs 530 crore against the estimates of Rs758 crore

of GNCTD. While calculating impact of the Pay Commission GNCTD have included impact of pensioners and committed liability as well.

Surplus / Deficit On Non Plan Revenue Account

The following table gives the surplus/deficit on non plan revenue account for the forecast period 1996-97 to 2000-01 before transfer of assigned taxes to local bodies worked out on the basis of the foregoing assessment. For comparison the forecast furnished by GNCTD is also given alongside.

Surplus of GNCTD over Award Period

	GNCTD's Forecast		DFC's Forecast	
	Absolute (Rs crore)	% of GDP	Absolute (Rs crore)	% of GDP
I. Revenue Receipts	17546	9.31	17630	9.36
a. Tax Revenue	17295	9.18	17331	9.20
i) Stamps & Registration Fee	898		1157	
ii) State Excise	2320		2504	
iii) Sales Tax	12898		12324	
iv) Taxes on Vehicles	474		598	
v) Other Taxes & Duties etc.	704		748	
vi) Others	1		neg.	
b. Non-Tax Revenue	251	0.13	299	0.16
II. Non Plan Revenue Expenditure	10004	5.26	8792	4.66
i) Normal	8402		7330	
ii) Non-plan Grants to local bodies	--		569	
iii) Committed liability	844		363	
iv) Impact of 5th Pay Commission	758		530	
III. Surplus (+) / Deficit (-) on Non Plan Revenue account	7541	4.05	8838	4.71

As indicated above the surplus, on non-plan revenue account, over the award period, as worked out by the Commission comes to Rs 8838 crore. Details of projections relating to revenue receipts and non-Plan revenue expenditure are at Annexures 10.3 and 10.4 respectively.



Scope for Economy in Municipal Administration

Economy in Administration is not exactly a popular subject in any quarter. The reasons are not far to seek. The rising tide of job-seekers entering the market in unstoppable waves have their own urge to get employment and what can be better than a Government or quasi-Government job with all its 'perks' and little accountability. The political executive with its inescapable need to win the favour of its voters' constituency find it difficult to ignore demands for jobs from them. In the bureaucracy as well, a big vested interest has taken deep roots in filling every vacancy, right from the employment exchanges to the dealing hands and their supervisors in the recruiting establishments. At the higher levels in the bureaucracy, the most readily available shield against criticism for low level of services rendered is 'lack of resources' which invariably implies employing more and more manpower.

There is thus hardly any segment constituency in the Government or quasi-Government bodies which feels an urge to seek out the scope for economy in carrying out its activities and discharging its responsibilities. In effect, there is little effort at focusing

the mind and effort on raising productivity of the resources already harnessed to the tasks at hand.

Yet, however the rising cost and declining quality of services rendered to the citizens has, quite legitimately, raised serious questions about the sustainability of continuing to transact 'business as usual'. The whole issue of providing governance at acceptable cost and quality has assumed central importance in the field of public administration theory and practice. The search for more efficient and effective modes of delivering public services has engendered fresh thinking of a fundamental nature in regard to the working of government at all levels, involving *"major and visible management innovations in the organisational structures and systems of government aimed at delivering greater efficiency, and more responsive and flexible public services"*. Reforms of far reaching significance have been brought about with the objective *"to shift emphasis from developing plans to developing key strategic areas; to shift emphasis from inward-looking systems to developing partnerships; to shift emphasis from inputs and processes to outputs and outcomes; and to shift emphasis towards managing diversity within a unified civil service. Finally, managerial pragmatism and political conviction are highlighted as essential to motivating management innovation in government"*. (The New Public Administration: management innovations in government by Mohan Kaul, Public Administration and Development Vol. 17 No. 1 Page 13).

The need for bringing in fundamental reforms in the functioning of municipal government in Delhi can hardly be over-emphasised. That there has been a decline of municipal services across the board despite the escalating municipal budgets and bloating municipal staff is a crying reality which comes alive dramatically with every outbreak of diseases, but has to be endured day in and day out in the form of rising toxicity in air and water, overflowing 'nalis' and drains, choked sewers, littered garbage and other solid waste, low availability of essentials like water supply and electricity, and so on.

The sad state of civic life in the Capital comes out in its stark reality in the recent assessment of five leading cities of the country reported by the 'Times of India' (June 1,

1997; p.19) under the title 'Best and worst of Indian cities'. In an evaluation, based on 15 selected parameters of city life, made by a panel of three eminent citizens of the respective cities, Delhi managed to collect a mere 55 points as against 69 for Mumbai, 81 for Bangalore, 85 for Chennai and 92 for Calcutta. The panellists for Delhi were Shri Jag Pravesh Chandra, former Chief Executive Councillor (1983-90), Mr. Bhaskar Ghosh, former Secretary, Information & Broadcasting, Government of India and Smt. Maneka Gandhi, former Minister for Environment, Government of India. Among the parameters on the state of which the assessment was based included power, water, public health, pollution, traffic, and 'slummification'. It is worth pondering that if Lutyen's Delhi which, by and large, forms the jurisdiction of NDMC was excluded, how low would have gone down the rating of the remaining city falling under MCD.

MCD's Perception

Despite near unanimity on the poor performance of MCD in discharging its basic obligation towards the citizens of Delhi, the authorities in the Corporation do not seem to entertain the possibility of improving performance by raising productivity of their operations. To quote from the Memorandum submitted by MCD to the Commission "*the nature of municipal functions does not permit the use of sophisticated cost saving devices through innovative technology. There cannot be any substitute for band of teachers, doctors, health workers, sanitation staff etc. so that cost could be reduced on these and economy in expenditure achieved. MCD has to pay wages and salaries to its more than one lakh employees and workers who cannot be sacked. In the wake of controversy on deficiencies in sanitation services, an attempt was made to reduce expenditure through privatisation and contracting out of sanitation services. This, however, led to intense agitation by the employees and the workers in the relevant department. MCD had, therefore, to postpone such an innovation for promoting economy. The workers, in any case, cannot be dismissed from the job at least in the short-run. Likewise, materials and equipments are becoming costlier day by day and there appears to be no scope for substituting these materials or for getting them at a lower price*" (p.29).

It is not clear as to how the nature of municipal functions prevents the use of innovative technology. Expert opinion as well as real life experience of municipalities with a yen for modernising their operations do not support such helplessness or pessimism. For instance, the Indian Infrastructure Report, drawn up by a Committee headed by Dr. Rakesh Mohan, Director, National Council of Applied Economic Research had recently recommended use of technology and prudent practices for reducing the cost of collection, treatment, and disposal of solid waste (ET, Jan. 9, '97, p.12).

It needs to be realised, sooner the better, that privatisation of certain municipal services in order to reduce costs cannot be ruled out. Municipalities alone cannot handle huge infrastructural projects like water supply, sewage disposal, and urban transport. Involvement of private sector is required to meet the scale of investment in these areas.

Public disenchantment with services provided by MCD is not conceptual but borne out of its inefficient and sometimes corrupt management. The merits of privatisation are seen in terms of improvement in efficiency and reduction in budgetary burden. To draw upon the Rakesh Mohan Committee again, Public-Private-Partnerships (P-P-P) is recommended as the appropriate strategy to be adopted for the present. Specifically, it is suggested that, *"In water supply projects, it is possible to privatise sourcing, treatment, and bulk supply. The retail distribution and pricing may remain with the public sector. Solid waste disposal can be privatised fully. Low-cost sanitation may be privatised fully on the model of Sulabh Shauchalaya. Maintenance of roads can be entrusted to the private sector subject to quality control"* (The Indian Infrastructure Report, Volume II, p.30).

There is no question about MCD looking for any robotic substitutes for teachers, doctors, safai karmicharis, etc. in the name of adopting innovative technologies. What has been suggested time and again is that there is considerable scope for getting much greater and higher quality output from them. Resorting to privatisation, contracting out of

services and adopting similar other strategies which have been implemented elsewhere with impressive results cannot be avoided on the facetious plea of *"intense agitation by the employees and workers"*. No doubt, this would require the political leadership to exercise the requisite will and the managerial cadres to assist the former in the task of reforming the administrative system of MCD in step with the spirit and the imperatives of the times. What other local governments within and without the country can adopt successfully, MCD should also be able to emulate.

Public Perception

It would be pertinent to take note of the perception of eminent public men in this regard. In response to the Commission's questionnaire, the respondents not only expressed their disappointment but went to the extent of saying that there was need for the citizens to assert *"that services exist for the people and not the people for the services"* and that there was *"need to prescribe standards of quality of performance in the matter of provision of services to the people"*. A former Chairman, Standing Committee, MCD and a former Commissioner have suggested that privatisation/contracting out of services in respect of some functions like sanitation, distribution of electricity is a must and a beginning is very much required. Yet another eminent respondent suggested that privatisation and resorting to contracting out of specific jobs to NGOs would be a welcome measure aimed at improving the standard of delivery of services to the citizens and that the interests of existing employees could always be protected through mutual consultations in a democratic manner. Likewise, an NGO has suggested the involvement of a wide array of business and voluntary organisations in providing civic services and strongly recommended reduction of MCD/ NDMC staff. It has, however, expressed the view that *"outright privatisation is considered to be the last resort"*. The head of a national institute had advocated an important role for the NGOs. Not surprisingly, the chief executive of a business chamber has suggested the handing over of provision of sanitation facilities and infrastructure services like water, power,

roads, bridges etc. to the private sector. In the Chamber's view, "*privatisation should be done with strong determination*".

The above represents a sample of the strength of views seeking alternative strategies to the delivery of civic services instead of relying on business-as-usual approach adopted by MCD/ NDMC.

The Commission are, however, in no way equipped to embark upon a systematic inquiry into the level of efficiency being achieved by the two municipalities, or wastage or misapplication of resources prevalent, in the discharge of their functions and responsibility of rendering various civic services to the citizenry. Efforts made to enlist the assistance of consultants to undertake studies of productivity/ scope for economy in administration in municipal functions did not bear fruit. It seems that this is an arena of activity which is not in the mainstream of productivity analysis by professional consultants who are geared to examine and report on the industrial production and the commercial services sectors. The Commission have, all the same, examined this important aspect in some depth and presents its findings and suggestions hereafter.

Scope for Economy in Conservancy and Sanitation Services

The Commission got the singular opportunity, created as a result of a peculiar set of circumstances, arising out of the public interest litigation (PIL) in the Hon'ble Supreme Court of India for issuing directive to MCD to effectively perform its sanitation functions, of studying the resource use efficiency in such a large sector of municipal functioning as conservancy and sanitation. The results of the study are contained in Appendix titled 'Detailed Analysis of Demands for Additional Resources for Conservancy & Sanitation Services by MCD & NDMC' attached to the Commission's Interim Report (September 1996). The major findings of this study need to be recalled here (para nos. in parenthesis refer to those in the Appendix cited above):

- 1) the current manpower availability in MCD area compared with the average Indian values, as determined by the Sivaraman Committee through a survey conducted in 1974, was as follows:

		MCD	Average Indian Value
(i)	Cleaning -	3.15	2.3
(ii)	Transportation -	0.19	0.3
(iii)	Dumping -	0.12	0.2
	Total	3.46	2.8

The lower figures under transportation and dumping reflect the impact of mechanisation of these operations since 1974. The 37% higher figure under 'cleaning', despite the large scale provision of sewerage thereby dispensing with the physical collection and disposal of human waste and the provision of wheel barrows (in place of head loads), endorses the popular perception of low productivity of safai karamcharis (vide para 5.17)

- 2) Applying the average Indian values, noted above, MCD has an excess manpower of 9730 (27%) out of 35910 Skes engaged in cleaning and of 7645 (19%) out of 39517 Skes engaged in all sanitation chores (vide para 5.18)
- 3) The excess manpower in NDMC on the same basis is, proportionately, far higher, at 1243 (64%) out of 1948 Skes engaged in sweeping and 1264 (60%) out of 2122 Skes engaged in various sanitation duties; this is partly explained by the low density of population in NDMC area (vide para 5.19).
- 4) MCD has prescribed its own norms for providing Skes for sweeping areas varying from type of colony/ roads ranging from 30,000 sq. ft. in walled city/ congested

areas to 75,000 sq. ft. in rural areas. Adopting an average of 40,000 sq. ft. per Sk, only 21504 Sks can be justified for an established sweeping area of 79.91 sq. kms. Even if their unproven claim of a much higher sweeping area of 90.73 sq. kms. is taken as the base, only 24416 Sks can be justified on the basis of their own norms as against as high a number as 35910 Sks engaged on sweeping duties in 1996. From this point of view as well, the surplus manpower with MCD runs into five figures.

- 5) All this boils down to the startling result that the average sweeping area per Sk works out to a mere 2225 sq. mtrs. or 47 mtr x 47 mtr *which is just about one-third of a hockey field* (100 x 80 sq. yards). In terms of an 18 mtr wide road, one Sk is required to *sweep a mere 123 mtr length of road in 8 hours!* Almost identical situation prevails in NDMC where the per Sk sweeping area works out to a mere 2259 sq. mtrs (vide paras 5.12 and 5.20).
- 6) *Zone wise analysis* of Sks per 1000 population and solid waste clearance per Sk carried out for 12 MCD zones shows that there is no discernible pattern in the deployment of Sks either in terms of population to be served or in relation to garbage cleared (vide para 5.21).
- 7) A 1995 study by Department of Administrative Reforms found that the state of cleanliness was extremely poor, largely due to problems in effective deployment of staff and in supervision. The respondents reported that, *"they hardly ever see a sweeper around"* and that, *"they disappear after marking their attendance on the duty site"* (vide para 5.22).
- 8) The truancy, shirking and other malpractices of sanitation staff are also highlighted in an investigative report published in the Indian Express of July 26, 1996 titled *"SAFAI SHIRKERS, OBLIGING SUPERIORS - Bogus muster rolls, absenteeism stink of malpractice."* It reports that while an elaborate hierarchy,

comprising 1,400 Sanitary Inspectors supervising 38,311 Safai Karamcharis, is engaged in keeping Delhi clean, only about "40 per cent turn up for duty. The rest also turn up but only on paper... about 15 per cent are absent. Of the rest 60% absentees, about 45 fall into two very interesting categories. They are nicknamed 'the Lahories and the Peshawaris'. The first are a lot who come only for attendance but get their pay, nevertheless. They have to pay relatively a small amount of Rs.300 to Rs.400 to their superiors. The second neither turn up nor do their work but get paid for a consideration of Rs.700." Again, "a handful have sublet their job for Rs.500... The time, meanwhile, is spent in more profitable ventures, some as private sweepers that every colony employs" (vide para 5.23).

The scope for economy in municipal administration, as seen from the above statistical analysis which corroborates the widespread public perception in this regard, is, without doubt, immense. Conservancy and sanitation services represent an activity the results of which are literally out in the open, for everyone to see and suffer or enjoy, as the case may be. That is why this is a civic function the efficiency or inefficiency of which is readily perceived. A situation of sub-optimal efficiency may well prevail, even though not so tangibly, in other activities which are widely dispersed, almost at the level of individual workers deployed on streets, roads, pavements, 'nalis', drains and other open spaces, such as parks and gardens.

Efficiency and Economy in School Administration

Insofar as another very major area of civic activity namely providing primary education is concerned, although a number of teachers work in a comparatively small building, supervised by a head from close quarters, yet it is no secret that given the level of motivation on the part of the staff and the will to enforce discipline on the part of the authorities, the situation is not vastly different. The availability of teachers to match the number of students to be catered to in different schools often becomes a serious problem particularly in schools situated in rural areas or localities inhabited by the poor such as

Jhuggi-Jhopri clusters, resettlement colonies, slums etc. The likely result is that the very children who need the maximum attention from educational authorities and teachers of the municipalities are the ones who are left largely to fend for themselves. What is even more worrisome is the fact that whereas the results of malfeasance, neglect and default in the case of a service like conservancy and sanitation, the result of neglect and default are readily and palpably visible, those in the field of education remain hidden until it is too late to do much to repair the damage. It all shows up in terms of large numbers of school drop-outs and illiterates of which India easily has the largest numbers as well as the highest rates in the world, excepting perhaps, the strife-torn countries of sub-Saharan Africa. The need for making an all-out effort to reform the school system so that it can serve the basic purpose of laying secure foundations for future can scarcely be over-emphasised. This important subject will be reverted to, later, while taking note of outstanding success stories of public management in USA.

Scope for Economy in Discharge of Discretionary Functions

Another avenue holding out scope for economy is to be found in the realm of the functional domain which the municipalities have chosen to adopt. As noted earlier, the functions which MCD and NDMC are required to perform are split into obligatory and discretionary. As the nomenclature itself indicates, there is no choice Government discharging obligatory functions are concerned. The municipalities are, by law, enjoined upon to undertake and discharge the functions that are classified as obligatory to a satisfactory level. This is their inescapable primary responsibility. By definition, therefore, until such time as they are able to do so, there is, by implication, a legal obligation on them not to dabble into other activities. Or, to put it differently, the first charge on the available resources of the municipalities is the discharge of their obligatory functions to a satisfactory level. This issue was posed squarely to the eminent citizens for their views and the position outlined above has been endorsed by most of the respondents. A senior leader, however, pointed out that it was not pragmatic to place a strict prohibition on the municipalities in regard to undertaking discretionary functions

until they were able to discharge properly their obligatory functions, and in this context he cited the example of the civic body being called upon to hold civic receptions to honour the visiting foreign dignitaries. The point is certainly well taken. Barring the municipalities from performing any of the functions whether obligatory or discretionary which the Parliament in its wisdom has placed in their jurisdiction is, of course, ruled out. But the frittering away of scarce resources on discretionary functions which can be easily avoided and are perhaps taken up voluntarily at the expense of the due performance of obligatory functions, can hardly be justified. Besides, in respect of discretionary functions, such as holding civic receptions which are undertaken in the interest of national and other larger considerations, there should be adequate provision for the municipalities to be reimbursed by the Government of NCT or the Union Government as may be appropriate. The bottom-line in such matters is that the dichotomy established in the governing Act of the municipalities must be duly respected in the interest of the citizens' receiving due satisfaction in respect of the services which are regarded as being of fundamental importance to civic life and have, therefore been categorised as obligatory functions of the civic bodies. The Memorandum of MCD concedes that *"there could be some scope for economy here. But the General Wing spends hardly 6 to 7% of the total budget on such functions which are discretionary but not non-essential. The city fathers have retained them for a long time and the same deserve to be continued"* (p.29-30).

Though, in percentage terms, the expenditure of MCD on non-obligatory functions stood at around 6.5% in 1994-95 and 1995-96 and rose to 7.2% in 1996-97 (table 22, p.82 of the Memorandum), the amounts in absolute terms are not insignificant, ranging, as they do, from Rs.31 crores to Rs.42 crores. To the extent that the involvement of MCD in performing these functions can be minimised, much needed resources can become available for diversion to the performance of its obligatory functions.

In this context, one activity of MCD deserves particular attention. This relates to maintenance of hospitals including the expansion and upgradation of facilities, which is a functions included in the list of obligatory functions of MCD purely for historical

reasons. This is clear from the very wording of the entry which restricts this function explicitly to those "existing on the date of commencement of the DMIC (Amendment) Act, 1993". This shows that MCD is precluded from opening new hospitals. The expansion of curative medical facilities has been permitted only at the hospitals which were existing on that date, evidently in order that the growth of those hospitals was not stunted thereby depriving the beneficiaries served by them of the latest developments in medicine and surgery. As the Memorandum of MCD itself notes "*Medical Relief (curative health) consisting of a chain of hospitals, dispensaries, maternity homes etc. (discussed in para 2.5) is not strictly in the nature of local functions. There does not appear to be any justification for a municipal authority to maintain huge hospitals containing beds and specialities. This pertains to the state functional domain and there is every justification for withdrawing of this function from MCD and its transfer to the Government of NCT. Presently, MCD spends (as of 1995-96) Rs. 5747.37 lakhs. If this transferred from the MCD, it will result in a saving of about Rs.58 crores in a year to be used in augmenting the much needed other obligatory local functions. Hence, the Commission may consider to rationalise the functional domain of the MCD so that it could be enabled to generate additional financial resources through savings on the transferred functions*" (p.40).

Apart from making savings for MCD, this suggestion has the merit not only of relieving the civic body of the administrative burden of maintaining, expanding and upgrading these hospitals but also of bringing hospital care under one umbrella with its attendant advantages of networking of physical facilities, managerial resources and advanced expertise.

Exemplary Achievements of Some Municipalities

It is not as if in the current stage and time, seeking a higher level of performance from the local bodies is asking for the impossible. There are inspiring examples of what can be achieved, regardless of the seemingly daunting and insuperable obstacles posed by powerful unions, tolerant citizens or entrenched vested interests. The example of what has

been achieved in the city of Calcutta under the bureaucratic leadership of Ashim Barman, the intrepid and imaginative Municipal Commissioner under the aegis of the Basu Government of West Bengal has already caught not only the nation's but the world's attention.

The *NEWSWEEK*, March 31, 1997 has made Calcutta's turned-around its cover story, emblazoning the title page with "INDIA THE NEW CALCUTTA --- Surprise! The World's Worst City Has Cleaned Up Its Act". Inside, the story, titled "Calcutta's Glow" has the following to say:

"The real revolution came to Calcutta with a simple idea: to clean things up a bit for foreign investors. The city built a four-lane express way to the airport, put in new entrances to train stations and - in a mid-night raid called Operation Sunshine - sent bulldozers to raze side-walk shacks and food-stalls along major thoroughfares If there is a spark plug of Calcutta's reforms, it is Ashim Barman, the city's intrepid municipal commissioner. Barman brings back ideas for change for visits to cities like London, Chicago and New York (where he has studied mayor Rudolph Giuliani's effective crackdown on petty crime). Among other things, he has formed unblushing alliances with private business. After turning over the city's erratic electric supply, the private management, Calcutta now produces surplus power. The government has attracted private investors to build office towers and shopping malls, and it has leased out public parks for private businesses to run. Barman also has signed an agreement with a US company to burn some of Calcutta's 2,200 daily tonnes of refuse to generate electricity. Another company will pay the city for garbage that it can process into fertiliser..... Citizens group seen to be springing up daily - this one to help keep parks clean, that one help to garbage collection. Examined coldly, the Renaissance of Calcutta has been purchased with pretty small change."

The success story of Calcutta has been juxtaposed in the same issue with the lost case of Delhi in the story titled "Paradise Lost: The Decline of Delhi - A capital defeated by traffic, disease and pollution".

Other success stories within the country are those of Ahmedabad and Baroda and the latest of Vijayawada where the municipalities have achieved credit ratings that would be the envy of many a business-house.

Success Stories from Abroad

The above sample of exemplary achievements by local bodies within the country may, with advantage, be supplemented by those from the cities abroad. Among the most analysed and documented examples of vastly improved public management in the domain of civic services are those from the United States of America. Following the 'revolt' by the tax-payers, city governments all over the US were compelled to look for and adopt new strategies and methods for delivering basic municipal services to their citizens. A large number of success stories have been presented by David Osborne and Ted Gaebler in their epoch making work "*REINVENTING GOVERNMENT*" (1992). As we have given particular attention to two areas of civic functions under the municipalities in Delhi viz. sanitation and education, it would be pertinent to cite a few outstanding examples in these areas.

(a) Sanitation

To take sanitation first, the case of New York City's Sanitation Department is illuminatingly illustrative. To quote from Osborne and Gaebler:

"What Gets Measured Gets Done"

.....
.....
.....
During New York City's fiscal crisis in the 1970s, an independent foundation developed a method to measure the cleanliness of streets, called Scorecard. It then sent out volunteers every month to rate each of 6,000 streets. The sanitation department had always focused on inputs: How many trucks were assigned to each district? How many men were needed on each truck? Now it began to look at the Scorecard information, which rated outcomes: How clean was each street? Using this information, it reassigned its street cleaners and began to reward crews that made the greatest improvements. By 1986, the percentage of streets rated "filthy" had declined from 43 to 4 percent. Nearly 75 percent were rated "acceptably clean."

The foundation, called the Fund for the City of New York, went on to develop outcome measures for parks maintenance, job training and placement, foster care, home care services, school maintenance, and other programs. "In large institutions, public and private, things are counted, and whatever is counted, counts," said then Executive Director Greg Farrell. "What is counted shapes and influences the behaviour of the organisation. It helps make public policy practicable, gets it out in the field, on the ground. And it leaves a trail."

Another example having direct bearing on the efficiency and effectiveness of sanitation services provided by the municipalities in Delhi pertains to the achievements of Ronald Contino in NY City's Sanitation Department's Bureau of Motor Equipment -

"Consider the New York City Sanitation Department, a huge, sprawling organisation that collects the garbage and sweeps in a city of 7 million. In 1978, when Ronald Contino was hired to manage the department's Bureau of Motor Equipment, it was a shambles. With more than 1,300 mechanics, welders, electricians, blacksmiths, and machinists, it was responsible for maintaining all Sanitation Department vehicles. Yet on any given day, it could keep only half of the city's 6,500 garbage trucks and street sweepers in operation.

Contino tapped the ideas of his employees through a top level labor committee and a series of labor-management committees. Within three years, 85 percent of the garbage trucks were back in operation, and departmental innovations had saved more than \$ 16 million. "This was possible because an environment had been created where each individual knew that he was being represented in the decision-making process, and that he had a direct 'pipeline to the top' to voice his very own concerns and desires," Contino says. "Changes in procedures were no longer viewed as orders generated by a distant elite, but rather as a product of teamwork and a universal desire to see the job improve".

Once the department was back on solid footing, Contino began handing day-to-day control over operations to line employees. He put a machinist in charge of his new Special Projects Division, which handled all new equipment orders. He had auto mechanics help write all specifications for new orders, test all new equipment when it first arrived, and staff the unit that negotiated and enforced warranties. He created a Research and Development Group, composed entirely of auto mechanics, which has implemented at least 50 design improvements and licensed several to private companies, earning royalties for the city. An employee team even developed a new refuse wagon, a construes vehicle used to carry garbage from a wharf to a landfill. They call it 'Our Baby'."

This is not by any means an isolated example. A similar achievement is recorded by the Motor Equipment Division of Madison, Wisconsin, USA, which

"saved \$700,000 a year by creating a preventive maintenance program and reducing average vehicle downtime from nine days to three. Another employee group studied problem in solid waste, where waiting time at the Energy Recovery Plant was delaying drivers every afternoon. Management was planning to spend \$1 million to double the size of the tipping floor, where the trucks unloaded. But by charting the traffic flow, the employees figured out that if drivers on the East Side simply started an hour earlier, the early afternoon traffic jam would disappear."

(b) Education

Likewise, remarkable improvements in the quality of output of the schools system have been achieved by bringing about the requisite changes in the public management of school education in different cities of USA. The most important element of the strategy for achieving enhanced level of performance from existing schools was to allow the parents real control over the management of the school in which their children receive education. Osborne and Gaebler quote John Chubb, coauthor of *Politics, Markets and America's Schools*:

"The largest estimated influence on the effectiveness of school organisation is the role of parents in the school. All other things being equal, schools in which parents are highly involved, cooperative, and well-informed are more likely to develop effective organizations than are schools in which parents do not possess these qualities."

The change was not easy to make. There were the inevitable prophets of doom. Osborne and Gaebler quote Don Moore, whose advocacy organisation, *Designs for Change*, spearheaded the reform effort:-

"Lots of people told us we were making a terrific mistake, because we were turning power over to illiterate, underclass people, taking it away from those who had the professional knowledge. They said we wouldn't get people to run for

the councils. But 17,000 people ran, and we had a higher turnout than they get in suburban school board elections. We see the councils as a new democratic unit in the community. We expect that the people who serve on councils will probably get involved in other issues, like housing, economic development, and adult education. These are real seedbeds for leadership development."

The extent of parental control and the mechanism of exercising it can be seen from the system as it operates in Chicago -

"In Chicago, every public school is now run by a council of six parents, elected by parents; two community members, elected by community residents; two teachers, elected by the school staff; and the principal. This council acts as the board of directors; it hires the principal (on a four-year performance-based contract), prepares a school improvement plan, and prepares the school budget, in accordance with its improvement plan. Principals are now hired and fired based on merit rather than seniority. After the first year, 81 percent of parents and 62 percent of teachers said their schools were operating "better" than before the reform. Seventy-eight percent of parents reported improvements in safety and discipline, 61 percent saw improvements in the physical plant, and 83 percent reported progress in educational programs. (Ibid)

Similar success was achieved in New Haven, Connecticut which tried innovative experiments way back in 1968.⁴ "At two failing inner-city schools, it set up Governance Management Teams made up of parents, teachers, other staff members, and the principal. By 1978, students at the two experimental schools had caught up to grade level. By 1984, they scored third and fourth highest in the system and had the best attendance records. By 1990, the specific model, called the School Development Program, was used in all 42 New Haven schools-and in more than 60 other schools in eight states."

Apart from creating parental 'ownership' of schools, another important measure of reform is to allow principals and teachers to exercise adequate authority over the management of their school. To quote from the same source again -

"Traditionally, public school systems have been horribly centralised. (Before its recent decentralisation, Chicago had 500,000 public school students and 3,000 administrators; Chicago's Catholic school system, with 250,000 students, had 36 administrators.) Yet study after study has proven that schools in which principals and teachers have significant authority are more successful than those in which the important decisions are made by a central administration. So hundreds of

school districts have begun to practice what educators call site management—pushing “decision-making authority down as much as possible to the school level,” as Arkansas Governor Bill Clinton describes it, to “give the principals more authority (and) give the teachers more authority.

Dade County, Florida, which encompasses Miami, has given authority over most of its schools to teams of principals, teachers, and, sometimes, parents. In Dade County and in Rochester, New York, each school now has a mission-driven budget. In Chicago’s first year of reform, it shifted \$40 million from central administration to the schools, cut 640 administration positions, and turned each school over to an elected council of parents, teachers, and community members.”

Chicago’s recent-most success in achieving reform of the school system in the face of the might of the teachers’ union has been impressive enough to have caught the attention of *The Economist* (July 26th, 1997, page 30-31) which carries a full length report under the eye catching title ‘*Reforming the Schools—The difference a mayor makes*’.

“It is hard to sack a public-school teacher in America.....

So how is it that Paul Vallas, chief over-seer of Chicago’s schools, could lay off nearly 1,100 employees at the city’s worst-performing high schools and draw only mild protest from the historically militant Chicago teachers’ union? The answer is Mayor Richard Daley.....

.....The system was long governed by a semi-independent school board and its appointed superintendent. When the system faced financial collapse in 1995, those officials went looking to the state legislature for money.....

.....It passed legislation making it easier to sack teachers, giving principals more control over their schools, and consolidating 27 sources of state finance into two block grants. Then it gave the whole system over to Mr Daley, sacking the superintendent and school board and replacing them with a five-person school reform board of trustees appointed directly by the mayor....

The reform team had a simple technique: demand that children learn the basics..... The reform board opened alternative schools for disruptive young people, required daily home work, added more maths, science and foreign languages to the curriculum, expanded early childhood programmes and kept many schools open longer.....

But the new board went far beyond that. ended social promotions; students in the 3rd, 6th, 8th and 9th grades (that is, at the ages of around nine, 12, 14 and 15) who lack the required academic skills must either raise their performance in summer school or repeat the same grade the next year...

Next, the board went after schools with a pattern of failure. Some 109 schools were put on probation... seven high schools showed no improvement or got worse. These schools were "reconstituted". Every employee, from custodian to principal, was removed. Some were rehired by the schools new management; the rest were placed in a reserve pool for 20 months (reduced to 10 months this week). If they are not hired somewhere else in the system by the end of that time, their contracts will end..

"I've not made a secret of it. I like the mayor," says Mr Reece (president of the teachers union). "He really loves the town, and I think he really cares about the public school system." Strange world's from the head of a union that has gone on strike nine times since 1972.

Best of all, the reforms are working. For the first time in many years, teachers are excited to be in the classroom. The new reform board has put the fiscal house in order, closing a projected four-year \$1.3-billion deficit without increasing the size of classes. In 1996, the bond-rating agencies raised the Board of Education's debt to investment grade for the first time since 1979, enabling the board to launch a five-year \$850m capital improvement plan.

Students are doing better, too. Of 71 elementary schools put on probation, 54 showed improvements in reading and 69 in maths. Reading test scores went up in 52 and maths scores in 61 of 74 high schools. With the end of social promotions, teachers will spend less time dealing with students who have fallen years behind."

These success stories hold out tremendous hope for bringing about a sea change in the realm of public management in all areas of civic services in order to vastly improve the delivery system. The path-breaking contribution of the work 'Reinventing Government' by Osborne and Gaebler lies not merely in making the term literally a household one but in drawing significant conclusions to provide what they call the 'road map' for the reformers of public management world-wide. Likewise, mayors like Richard Daley of Chicago could serve as role models for our own municipal leaders - both political and bureaucratic - getting them fired with the obsession to make the cities under their care good places for the citizens to live in.

The phenomenon of lack of discipline, motivation, application and conscientiousness of doing one's duty is not peculiar to the municipalities. Nor are the reasons and causes therefor any different from those in other parts of government and quasi-government institutions. Among others, resistance from organised trade unions has specifically been stated as a major factor blocking any reform of the system. No doubt, ground realities will have to be reckoned with. At the same time, it would not also do to give up the cause of effecting economy in administration as lost without the concerned political and bureaucratic executive making a determined, well-planned and sustained effort to re-order their operations on scientific lines, with the help of latest available technologies and by making an all-out effort to enlist the support of the unions as well as the citizens.

Scope for Augmentation of Resources

Article 243-Y of the Constitution specifically requires the State Finance Commission to make recommendations as to the measures needed to improve the financial position of the municipalities. Following therefrom, the TOR of the Commission also list 'the scope for improvements in resource mobilisation by the municipalities and the tax efforts made by the municipalities' as considerations which the Commission shall, inter alia, take into account in making its recommendations.

It may be recalled that both MCD and NDMC are precluded from having deficit budgets. The clear and explicit intent of such provisions is that municipalities must live within their own means. As has been noted, if they borrow to cover any gap between income and expenditure or for capital expenditure, the payment of instalments and interest due thereon is the first charge on their revenues. Consequently, these municipalities must raise their resources in order to meet the expenditure for meeting the civic requirements of the population they serve.

No doubt, the Constitutional Amendments have opened up an important revenue for buttressing the finances of the municipalities. Yet, in doing so, particular care has been taken, as is clear from the provisions quoted above, to ensure that the municipalities do their best to augment their own resources. In principle, they are expected to exhaust the potential of the resource bases provided to them before they become entitled to

assistance from the higher level of government. It is in this context that the question of scope for mobilisation of additional resources assumes singular importance.

An examination of this resource base of municipalities is the first step towards judging the potential for resource augmentation. The Commission note that while the tax base of MCD and NDMC is identical, there is a great deal of difference between the non-tax bases of the two bodies, with NDMC obtaining a large share of its own financial resources from non-tax resources as against the low of 13.5 percent in case of MCD.

Tax-based Resources

(1) *Property-tax:* As already noted, property tax constitutes the mainstay of the own resource-base of the municipalities. In the case of MCD, it accounted for as much as nearly two-thirds of its own revenue in 1995-96. In the case of NDMC, if the income and expenditure from water supply and electricity distribution are excluded, property tax accounted for 27 per cent percent of its own revenue. In rest of the country as well, property tax is a major source of finance for the municipalities with its share ranging from 40 percent to 80 percent of their own income. It is only in the 6 states which levy octroi that property tax does not have such a dominant role but ranks at second place making a sizeable contribution to the kitty. Realising the importance of property tax in the existing scheme of municipal finance in Delhi, the Commission decided to have an in-depth study of all aspects of property tax levy and collection made through Human Settle Management Institute (HSMI), a wing of Housing Urban Development Corporation (HUDCO) of Government of India.⁷ This study bears out the common knowledge that the municipalities have been able to collect only a fraction of the potential revehues from this source due to sheer management inadequacies. The HSMI study also goes on to identify the legal hurdles and anomalies that stand in the way of the municipalities tapping this source fully.

PROPERTY TAX

Property tax (also called house tax or building tax) is the most universal and stable of local government taxes. In large and metropolitan cities, land values have gone up precipitously. Sections of society related to trade, industry and professions who are the beneficiaries of urban development. These groups ought to contribute the maximum to provide solvency to municipal bodies. Using urban land should be the chief source of financing urban development.

Property Tax (PT) may be based on the capital value of property (land and building) or Annual Rateable Value (ARV) of the property. In India it is the second alternative which has been used for levying property tax. The rateable value of any land and building assessable to property tax is the annual rent at which such land or building might reasonably be expected to let from year to year minus a certain sum allowable for repairs, insurance and other expenses necessary to maintain the land or building in a state to command that rent. Actually, it is a hypothetical value which can be interpreted as the market rent of the property concerned. Ideally, the base of property tax should respond to the value of properties.

In India, many local governments use the base of property tax for levying various types of service taxes for water, sewerage, street lighting, etc. Tax rates and charges for various services are normally specifically identified.

The practice to levy service tax along with general tax is not always desirable. There is perhaps a need to decompose property tax into service taxes so that a transparent framework as to how the service is financed is known to one and all.

In most metropolitan cities of India the revenue from property tax has not increased commensurately with skyrocketing real estate prices. The slow growth of property tax is attributed to exogenous factors as well as factors internal to the system. Exogenous constraints pertain to the impact of rent control legislations on property valuation. Assessed rateable values are income inelastic mainly due to judicial pronouncements regarding standard rent, fair rent etc. Internal factors include methods of assessment, coverage, rate structure, and collection efficiency. There is generally poor maintenance of record keeping, slack administration and enforcement.

The HSMI Study Report was drawn up by the Consultants after exposing the draft report to both experts and practitioners including those from MCD and NDMC. Consequently, the Commission consider that the analysis and conclusions of the Report are not disputed in their essentials by the two local bodies, apart from the fact that they are duly informed of the valuable contribution made by eminent and knowledgeable participants in the Seminar on the Report held in May 1997 as part of the terms of reference given to them by the Commission.

The Commission commend the report for an in-depth study and implementation by the concerned authorities in Government of NCTD, MCD and NDMC. For the purpose at hand, it would suffice to place its Executive Summary alongwith Revenue Enhancing Action Plan (REAP) at Annexure 12.1.

A major finding of the report that needs to be emphasised is that the current performance of collection of property tax is far from satisfactory. In MCD only 1 out of 4 properties assessed actually ends up contributing to the Corporation kitty some amount as property tax. As a percentage of total demand including arrears the recovery percentage is a mere 11.42 percent as per Audit Report (1993-94, p.11). In NDMC the situation is equally bad with only one-ninth of the current demand of property tax actually being captured into the tax net. Further, it is a startling fact that the five-star hotels in NDMC area yielded only 3 percent of the demand billed against them. Large amounts, as much as two-thirds of the civic body's total current demand on account of property tax are thus blocked in arrears with them. It is not surprising therefore that with such low performance in collecting property tax revenues, the municipalities should have huge arrears of un-realised property tax - Rs. 2037 crore and Rs. 367 crore respectively in MCD and NDMC.

Another outstanding feature of property tax management is its narrow base and heavy under assessment. According to the findings of the study, if the assessable properties are brought into the tax net, the demand would go up by 50 percent even at current level of assessment efficiency. If however the under-assessment is also taken care of, the demand may go up by 300 percent. In monetary terms, it is estimated that for the year 1995-96, the demand in case of MCD would have gone up from Rs. 367 crores to Rs. 540 crores to Rs. 1632 crores, with corresponding figures for NDMC being Rs. 47 crores, Rs. 62 crores and Rs. 186 crores.

As regards arrears, the study had estimated that an amount of Rs. 1396 crore is 'collectible' as against the outstanding arrears of Rs. 2405 crores in 1996-97 (vide Table

6.8 and 6.12 of the HSMI Report). An estimate of how much MCD should be able to collect over the five year period is projected to rise from Rs. 275 crores to Rs. 866 crores, totalling Rs. 2780 crores giving an average of Rs. 572 crores per year (p.77 Table 6.12A, *ibid*). The latter estimates are based on the assumption that legal changes suggested by the Study would be implemented. These are mainly:- (a) Deletion of the term 'reasonably' from Section 116 of DMC Act, and Section 63 of NDMC Act, and introduction of the concept of market/ actual rent; (b) Exemption of all non-residential properties from Delhi Rent Control Act; (c) Amendment of Section 126 (4B) of DMC Act and Section 72 of NDMC Act to reduce 'ex-parte' timing from 3 years to 3 months.

ECONOMIC ASPECTS OF PROPERTY TAX

As put succinctly by Dr. Raja J. Chelliah property tax "can be looked upon partly as a user charge for many of the services rendered. However, following the Anglo-Saxon tradition, the levy has been treated as a pure tax to be determined on the basis of the ability to pay The income from rented properties is of course also subject to income tax. Thus income from real estate gets subjected to two progressive taxes levied by two different authorities".

Further, "Now that rent control is being relaxed, rents are rising and the 30 percent marginal rate becomes applicable in a large number of cases. Also, as regards newly constructed owner-occupied houses, since the annual value is estimated on the basis of costs of land and construction, which have sky-rocketed, if the true cost is revealed the rateable value becomes inordinately high. Hence, the true cost of property is rarely shown. We have thus got into a vicious circle.

I believe that the solution to the property tax problem lies in bringing about three changes:

i). The present property tax should be split into two parts: (a) user charge; and (b) tax based on ability to pay. The former should be related to the cost of providing services, on the one hand, and the area of the property, on the other. The rate of user charge will be lower for unbuilt land, but there should be a separate vacant land tax on such land. The rate of user charge could also be fixed at a lower level for jhuggi-jhonpris.

ii). Property tax should be levied at a flat rate of 5 percent of rateable value.

iii). The rebate for owner-occupied properties constructed after 1970 or so should be 50 percent, so long as the present owner is alive, and should be reduced to the usual 25 percent when the next generation inherits it." (Towards Sustainable Growth - Essays in Fiscal and Financial Sector Reforms in India, Oxford University Press, 1996, p. 155).

Of course, the extent to which property tax can yield additional revenues without any amendments in the law is a matter of great interest as tapping it, without loss of time, is entirely within the reach of the municipalities to achieve. Therefore, the Consultant was asked to estimate separately the achievable additional resource mobilisation *within the existing framework*. Drawing upon the extensive data contained in the report, the estimates of additional resource mobilisation for MCD and NDMC consequent to the implementation of REAP (without changes in law but with administrative measures alone) are given in the following table:

Potential and Estimated Collections of Property Tax by MCD
(1998-99 to 2000-2001)

(Rs.Crore)

Description/Year		1998-1999	1999-2000	2000-2001
Collectable Arrears upto 1996-97	Demand	280	280	280
	Collection	280	280	280
Current Year	Demand	530	598	665
	Collection	212 (40%)	268 (45%)	333 (50%)
Current Arrears	Demand	281	486	546
	Collection	112 (40%)	219 (45%)	273 (50%)
Base-Widening & Logical Assess	Demand	226	226	226
	Collection	56 (25%)	79 (35%)	113 (50%)
Total	Demand	1317	1590	1717
	Collection	660	846	999

Notes:

1. Rs.226 crore increase in CD as part of widening of base and logical assessment is onetime growth and further changes in such properties will be covered under normal growth.

2. Figures in brackets indicate proposed ratio of collection against demand

In making the above estimates, the Consultants have made the following assumptions:

- (a) Entire amount of accumulated collectable arrears will be collected within five years @ Rs. 280 crore per annum.
- (b) Collection efficiency which is as low as 31% in 1996-97 can be increased only gradually to the level of 40% in 1998-99, 45% in 1999-2000 and 50% in 2000-2001. Subsequently it should be taken to a level of 70%.
- (c) The current arrears (i.e. arrears from 1996-97 onwards) will be collected in the same ratio as per (b) above.
- (d) One time increase due to widening of base and logical assessment will also be converted into revenue in a gradual process. Although MCD has already taken up widening of base and is likely to rationalise discretionary assessment in 1998-99, we take only 25% of such increase as PT revenue for 1998-99 followed by 40% in 1999-2000 and 50% in 2000-2001.

The Study has also suggested the adoption of unit area method (UAM) as an alternative to 'reasonable' annual rent (actual or assessed) for computing the annual rateable value (ARV). This system has already been adopted in Patna, and Hyderabad. It is based on rental data developed from a reasonable sample of properties taking into account size, use, structure, and location. To begin with UAM may be applied in low income areas such as LIG flats and resettlement colonies. The existing bye-laws of MCD of 24.10.94 already provide for applications of UAM. This exercise in real life would provide valuable feedback for application of UAM to other areas of Delhi.

PROPERTY TAX REFORMS IN ACTION

Despite the exogenous and internal constraints, some States/cities in India have recently introduced improvements in property tax policies and administration.

Patna. In 1993, Patna Municipal Corporation introduced area based property tax assessment. This was made possible after the State issued revised Assessment Rules in 1993 to spare the house owners from constant harassment and threats of arbitrary revision of tax rates. These rules laid down certain definite criteria for assessment of property tax which included location of the property, use, area, and type of construction. The rate of taxation was also reduced from 43.75 per cent to 9 per cent.

This method was challenged in the State High Court. Subsequently, upon appeal, the Supreme Court upheld this system. It ruled that the new system had been designed "with good intentions" and should be allowed to be implemented.

Tamil Nadu. In 1993, the Government of Tamil Nadu issued guidelines for quinquennial revision of ARV for Municipal Councils and Townships to ensure objectivity in the levy of PT. The basic value was fixed for different zones of all the centres. It was based on the probable rental yield per unit area for residential use of a reinforced cement concrete (RCC) building. A clear demarcation of the zones was made on a map and it was displayed in the concerned municipal office. Street and house numbers covered in different zones were also displayed. A discount of 10 to 20 per cent was given according to the age of buildings. In addition, owner occupied houses were given a discount of 30 per cent. Non-residential buildings were assessed 2 to 3 times the residential rates.

Ahmedabad. Recently, Ahmedabad Municipal Corporation has taken drastic steps to increase PT recovery through improved administration. The Municipal Commissioner who took charge in 1994 thoroughly reviewed the financial health of the Corporation and took drastic measures to check PT evasion. These included disconnection of water supply and drainage lines as well as issuance of warrants to raid premises upon non-payment of property tax. The result was a huge increase in PT collections from Rs.47 crores to Rs.92 crore between 1993-94 and 1995-96. As a consequence, the Corporation was transformed from a financially crippled institution to a stable and self-sustaining one.

Hyderabad. Beginning 1993, the Municipal Corporation of Hyderabad had undertaken several steps to increase revenue from its own sources. The whole exercise was focused on PT recovery through collection of arrears, bringing previously unassessed properties within the tax net, and revaluing under-assessed properties. Arrears collections gained momentum through strict enforcement measures such as issuance of warrants for non-payment of taxes.

Revenue targets were fixed for each of the seven circles into which the Corporation is divided and a system of weekly reviews of collections was introduced to meet the targets. Another important step taken was the computerisation of records and issuance of computerised bills to house owners in the city. Tax collection through bank branches was also introduced. Following these measures, PT collections in Hyderabad increased from Rs.27 crore in 1992-93 to almost Rs.50 crore in 1995-96.

It is now apt to quantify the additional revenue that MCD should be able to generate from 1997-98 to 2000-01. The figure for actual realisation during 1996-97 from this source, available since, is Rs.341.74 crore (plus Rs.62.04 crore from Transfer Duty Tax), showing a growth of 28 per cent over the collection of Rs.267.23 crore in the previous year, standing out in sharp relief from the low growth of 14 per cent in two previous years. Note must also be taken of the sudden jump of 50 per cent in 1993-94, to Rs.206 crore from Rs.137 crore in previous year, which must have been due to concerted action under dynamic leadership.

The Commission note that MCD was under considerable pressure following the two meetings it held with Commissioner, MCD and Officers of Assessment & Collection Department (vide Minutes of Meetings held on 10.4.96 and 1.8.96 placed at Annexures 12.2 and 12.3 respectively) and from the inter-action that HSMI had with them, to tap more effectively the vast potential of this source, specially the huge pool available in accumulated arrears. Consequently, with greater effort, they were able to double the rate of growth of property tax revenue to 28 per cent. Now that the HSMI study report has been available to concerned MCD officials and they must be making concerted and well-directed efforts towards stepping up collection both from current as also from the huge arrears demand, a rate of growth of 30 per cent should be maintained and collections, rising from Rs.342 crore in 1996-97 should go up to Rs.444, 577, 750, 975 crore in the four years 1997-98 to 2000-01. These estimates compare with the HSMI projections of Rs.660, 846 and 999 crore for the last three years given earlier (p.6). The former estimates being on the lower side by Rs.203 crore in respect of the years 1998-99 to 2000-01 for which HSMI's estimates have been made, the Commission adopt the same for quantifying additional revenue that MCD should reap from property tax over and above the amounts projected from past trend i.e. without taking into account the concerted administrative effort for resource augmentation. The respective figures are given below:

Estimates of PT Revenue	Years of Award Period					Total 1996-2001
	1996-97	1997-98	1998-99	1999-2000	2000-01	
A. Commission's Estimate of P.T. Tax Collections in MCD	342	444	577	750	975	3088
B. Projected P.T. Revenue on 12 year Trend	313	369	434	511	601	2228
C. Difference (A)-(B)	29	75	143	239	374	860

As for NDMC, the performance in collection of property tax has been higher, than that of MCD, the respective trend growth rates being 23.9 and 17.6 per cent per annum. However, the arrears at Rs.367 crore are equal to 15 times the actual collections in 1996-97 as against the same ratio of 9 times in case of MCD which underscores the point that

the scope of resource augmentation in NDMC is no less than that in MCD. Inquires from NDMC to ascertain their actual collections from property tax in 1996-97 revealed that for reasons beyond their control, they could not compile the recovery accounts for the year with the result that the requisite figure was not available. Therefore, estimating the revenue that NDMC can realise from this source on the same basis as in case of MCD i.e. 28 percent rise in 1996-97 and 30 percent in the remaining three years, amounts of Rs.31, 40, 52, 68 and 88 crores should be well within the reach of the municipality. This adds up to Rs.279 crore for the five-year period as against an amount of Rs.236 crore projected from past trend. Thus, in case of NDMC the additional resource generation would be Rs.43 crore.

Contribution of other taxes to the internal revenue of MCD has been, on an average, 19 per cent but it has been steadily rising in the nineties from 15.3 in 1990-91 to 24.2 per cent in 1995-96. Among these, mention must be made of taxes/duties on (a) stamp duty, (b) advertisements and (c) sale and consumption of electricity.

(2) *Duty on Transfer of Properties:* This tax has been the most important one among "other taxes", with a contribution of Rs.59 crore, accounting for 13.7 per cent (out of 24.2 per cent) of MCD's internal revenue. Rising by a mere 5 per cent, it came to Rs.62 crore in 1996-97. Apparently therefore this source is not an exciting one from the point of view of resource augmentation if the levy of stamp duty by GNCTD continues without a major change. It is gathered by the Commission that a proposal to levy stamp duty at enhanced rates/on power of attorney transactions, etc. is under advanced stage of consideration. Should the proposal materialise, it may bring in its train a bonanza for MCD. As things stand, the Commission is not in a position to take into account any amount by way of additional revenue tapped from this source. Suffice it to say, however, that if GNCTD implemented any changes as envisaged, the additional resource generation to MCD from duty on transfer of properties attributable to these measures would reduce the requirement of devolution correspondingly. The Commission,

therefore, do not take into account the additional resource from this source and leave it as a custodian for MCD.

(3) *Tax on Advertisements:* Though revenue from this source grew fast in the nineties - from Rs.3.6 crore in 1990-91 to Rs.11.7 crore in 1995-96, yet in immediate future the restrictions on erection of hoardings may come in the way of relying on this source for additional resource generation. The share of this tax in internal revenues of MCD is a mere 2.7 per cent and is, therefore, being left out of reckoning.

(4) *Tax on Sale and Consumption of Electricity:* This tax had a sizeable contribution of Rs.32.45 crore equivalent to 7.6 per cent of internal revenue of MCD in 1995-96. Since price of electricity has been going up alongwith its consumption, the proceeds from this tax have grown faster in the nineties than those from property related taxes, the corresponding ratios being 2.7 and 2.3 over 1990-91 to 1995-96. This trend is in reversal of the 12 year picture which throws up the respective ratio as 4.4 and 7.7. This aspect of analysis is significant in the context of the recent escalation in the price of electricity by Delhi Vidyut Board as a result of which MCD would reap substantial additional revenue. The Commission gather from DVB that an increase of around 25 per cent in revenue is expected on the basis of projected increase in its revenue. The Commission, however, leave this out of their reckoning, by way of a resource-custodian for MCD.

Apart from the taxes discussed above, the municipalities have been assigned certain tax sources which they can tap in their discretion. Of these taxes, the tax on professions, trades, callings and employments is an important potential source of revenue for the municipalities. Another tax which can be levied on increase in urban land values caused by the execution of any development or improvement work has considerable potential and a great deal of appeal on grounds of equity but is fraught with a maze of complications in actual implementation. The Corporation has proposed to utilise the former source for additional resource mobilisation.

(5) *Tax on Professions, Callings etc.*: Without disclosing the basis on which the tax would be levied or the methodology employed for estimating its yield, MCD has indicated an annual additional resource mobilisation of Rs. 20 crore. Considering that (a) Delhi has the highest per capita income in the country, (b) it also has a very large salaried class, both in the public and private sectors, as well as trading and professional classes, and (c) the area of collection is very compact, the potential revenue from this source should be much higher. The Commission, therefore, looked at the realisation from this tax in comparatively prosperous State of Maharashtra where as much as 2.7 percent of state's total tax revenue comes from this source (vide table in Annex.12.4). In West Bengal the percentage is even higher, at 3.1 percent. In terms of the percentage of SDP that Maharashtra (and Karnataka) collect from this source, the figures work out to .30 (and .34 percent). Applying the rate of .3 percent to the SDP of Delhi of Rs.18231 crore in 1994-95 (Economic Survey 1996-97 p S-ii), which would in fact be under-estimate as the share of urban population is far lower in that state, the professions tax collection should easily be around Rs.55 crore in a year.

Professions Tax

A tax on professions is levied as a fixed amount per person per year on professions, trades, callings and employments. It is a kind of licence fee to practise a profession. The tax is levied irrespective of the income derived by a person from the profession practised by him.

Entry 60 of List II (State List) in the Seventh Schedule of the Constitution authorises State Governments to levy a tax on professions, trades, callings or employment. However, the total amount payable in respect of any one person to the State or to any one authority (such as a municipality, panchayat etc.) in the State by way of such tax is not to exceed Rs.2,500 per annum [Article 276(2)]. Using this constitutional power, many State Governments levy tax on professions.

In 1996-97 (budget estimates), tax on professions constituted 1.15 per cent of total revenue from States' taxes : Rs 830 crore out of Rs.72,416 crore (Table 1). Smaller States collect a sizeable portion of their total tax revenue through professions tax. In 1996-97 (B.E.), the relative share of professions tax in the total tax revenue of these States was as follows : Mizoram (22.41 per cent), Manipur (15.06 per cent), Nagaland (11.61 per cent), and Tripura (9.73 per cent). West Bengal, Maharashtra and Karnataka collect 3.07 per cent, 2.71 per cent, and 2.09 per cent of their tax revenue through professions tax respectively (Table 2). There is no tax on professions in Delhi.

Tamil Nadu Tax on Professions, Trades, Callings and Employments Act, 1992, authorises the State Government or any local authority to levy and collect tax on professions etc. at rates specified in the schedule.

The Act prescribes 21 categories of persons who are liable to pay the tax. Self-employed practitioners are taxed according to their standing in the profession.

The Act provides for penalty in case of non-registration, non-filing of returns, and non-payment of tax assessed.

The Act exempts, *inter alia*, the following categories of persons from the payment of tax:

persons employed on casual basis, pensioners, members of the armed forces, and physically disabled persons.

Andhra Pradesh Tax on Professions, Trades, Callings, and Employment Act, 1987, empowers the State Government or any local authority to levy and collect tax on professions etc. at rates specified in the Schedule. The provisions of the Act are more or less analogous to the provisions of the Tamil Nadu Act.

Under Section 113(2)(c) of Delhi Municipal Corporation Act, 1957, MCD has the power to levy and collect tax on professions, trade, callings and employment in accordance with the provisions of this Act and the bye-laws made thereunder. Presently, the tax is not being levied.

Memorandum received from MCD by the Commission speaks of a proposal under consideration of the Government of Delhi regarding the levy of professions tax. According to the Memorandum, the tax will yield an additional revenue of Rs.20 crore per annum.

Assuming the tax is levied at the maximum permissible rate of Rs.2,500 per person per annum, it would mean in terms of MCD's estimation that there are 80,000 potential taxpayers for the proposed tax. The number constitutes less than one per cent of Delhi's population, or about 2.5 per cent of its working population. Considering Delhi's position as a leading centre of industry, trade and commerce, and the services rendered/provided by traders, doctors, engineers, advocates, architects, bankers, etc., the derived figure of potential taxpayers and the estimated figure of tax revenue (Rs.20 crore) seems to be on the lower side.

Though it is difficult to give a precise figure of potential taxpayers, it can safely be assumed that four lakh persons can be brought within the purview of the proposed tax. This figure constitutes 4 to 5 per cent of Delhi's population and 10 to 12 per cent of Delhi's working population. By this reckoning, MCD can collect an amount of Rs.100 crore from the proposed tax on profession.

As the revenues from an entirely new tax may take time to pick-up on account of gradual gearing up of tax-administration machinery, the Commission consider it reasonable for the figure of Rs. 55 crore being attained in the final year 2000-01 starting

at Rs. 30 crore in 1998-99 and rising to Rs. 40 crore in the penultimate year. Thus, the additional resource generation from this source would come to Rs. 125 crore.

It would be fair to take note of the economic aspect of levying professions tax as brought out by Dr. Raja J. Chelliah (*Ibid.*, p. 153). To quote -

"Though legally professions tax may not be construed as an income tax, nevertheless it is a tax on income to be paid only by particular groups of income earners. The imposition of this tax therefore violates the rule of horizontal equity. If the States are not willing to abolish this tax, the Central government should agree to give full credit for profession tax paid against the income tax payable. The divisible pool of income tax would have to be reduced accordingly".

It is not easy for MCD or NDMC or GNCTD to get the suggested dispensation from Government of India. Nor can they go without tapping a source which is within easy reach and will yield substantial revenue almost painlessly because of its low incidence. Further all professionals and other employed people must contribute to the municipal kitty in consideration of enjoying, without direct quid pro quo, a number of civic services. Besides, the three major advantages inherent in the nature of this tax, given the specific endowment of NCT of Delhi mentioned above, make this tax a very appealing instrument of raising revenue for the municipalities. The Commission, therefore, fully endorse the proposal of MCD for the levy of this tax and observes that since it would gather revenue from those living in the areas of NDMC and DCB also, the proceeds from it should be equitably shared with them. On rough and ready basis, a division of Rs.100, 20 and 5 crore respectively is being taken for the purposes of this exercise.

(6) *Entry Tax:* Another tax that the Municipal Corporation has proposed to levy is entry tax. This is to be collected from persons coming to Delhi from outside by rail and air. The proposal which was at initial stages of consideration was expected to yield Rs. 20 crore in a year. In the absence of relevant information being available to the Commission, this figure is being accepted on faith. The collection over the remaining three years is being taken at Rs. 50 crore allowing for a gradual build-up of yield; as the

people entering Delhi would also be coming to their areas, this amount may, on a rough and ready basis, be shared between MCD, NDMC and DCB as Rs. 40, 8 and 2 crore respectively.

Non-tax Sources

The current income of MCD from non-tax sources constitutes 13.45 percent of its revenue from internal sources. This is far below the average figure of over 19 percent over the twelve year period during which the contribution from this source has been in excess of 20 percent in as many as 5 years. Not long back, of the six years in the nineties, the share was 21, 18 and 15 percent respectively in 1990-91, 1992-93 and 1994-95 respectively. The data suggests that a share of 20% represents a reasonable bottom-line which MCD should be able to maintain with due effort. The Commission are, therefore, of the view that MCD must take pragmatic and determined action to ensure that the contribution of non-tax sources to its kitty rises by 2 percent per year in the remaining three years so as to attain a share of 19 to 20 percent from non-tax sources in internal revenues. On this basis, the additional resource generation by MCD, over and above the amounts already projected, would be around Rs.50 crore.

One index of the potential of this source lies in the well-known extent of corruption prevailing in the grant of various permissions and approvals by the municipalities. Clearly, there are huge 'rents' to be earned by way of tapping the 'surplus value' in monetary terms in giving and receiving these services. A very large section of citizenry not only resents being forced to pay under the table, they also feel humiliated and diminished. The municipalities must introduce 'fast-track, high-level', service channels for which this section of citizens would be only too willing to pay comparatively a high price - even five to ten times the current official charges - for preservation of their self-esteem and saving of valuable time and effort.

In case of NDMC, thanks to the contribution of surplus from distribution of electricity, the share of non-tax sources in its internal revenue has been steadily rising from around 70 percent in mid-eighties to 85% in 1995-96. A disturbing development, however, is the deficit lately being incurred by it in supplying water, a function which yielded it a small surplus continuously till 1990-91. But then, in 1991-92, there is a sudden massive deficit of Rs. 15 crore. This would need to be corrected if the surplus available from the other activity viz., electricity distribution, is not to be eaten into by the loss on water supply. There is no reason why NDMC should not step up its revenue from this source, by achieving higher collection efficiency and, if necessary, by raising water charges, so as to ensure that the activity is not a loser for it.

Yet another area with great potential for enhancement of non-tax revenue is that of commercial exploitation, selectively, of lands/ buildings owned by them in an innovative and imaginative manner. Given the scarcity of office and trading spaces in the city and sky-rocketing prices of urban land, the Commission consider this avenue akin to the proverbial hen that can lay golden eggs for MCD and NDMC (and by analogy, for GNCTD). By way of an example, a number of school buildings, presently in ill state of repair or in tubular-truss structures or even in tents could be entirely redesigned and rebuilt, with a part of their lands being used for shops and offices, while segregating and insulating the school proper from any disturbance arising out of commercial use of the earmarked portion. In most cases, the project would not only be self-financing but the premium could finance the reconstruction of the project plus give a periodic (say quarterly) return to the owner-government by way of handsome rent. On exploring this line of thinking, it was found that the main hurdle in reaping the hidden harvest from urban land has been the land-use policy of Government. The Commission, therefore, content themselves with recommending that GNCTD, MCD and NDMC may take a co-operative initiative to persuade Government of India in the Ministry of Urban Development (Land and Development Office and Delhi Development Authority) to draw up sound guidelines for exploitation of government land and buildings in the manner suggested above so as to permit socially beneficial exploitation of this source of great

potential for revenue generation. The target should be to initiate such redevelopment projects on ground at least in 1999-2000, the last but one year of the period covered by the Commission's recommendations.

On its own, MCD has in its Memorandum proposed levy of night-parking charges for augmenting its revenues. The Memorandum states "*that the proposal under consideration for levy of Night Parking charges is under consideration which is expected to yield an additional revenue of Rs. 53 crores.*". Again, no basis has been disclosed for arriving at the estimated annual yield from this source. Consequently, the Commission have made a broad estimate on the basis of assuming a fraction of the total four-wheel motor vehicle population in Delhi. This number according to "Delhi Statistical Handbook - 1996" was around 8 lakhs at the end of December 1995. Taking the current figure at 10 lakhs and a percentage of 10 of these vehicles being parked on public streets, the number of tax-paying vehicles works out to 1 lakh. On the basis of an average realisation of Rs. 2500 per annum from each vehicle, an amount of 25 crore may be estimated as being realisable by introduction of this non-tax levy. Since the collection of a tax of this nature from literally the doorsteps of vehicle owners would involve considerable administrative effort, the profile of yield from this source is expected to be Rs. 15, 20 and 25 crore in the remaining three years, yielding a total of Rs. 60 crore.

In sum, the Commission arrive at the following estimates of additional resources that MCD and NDMC must raise during the award period, most of them during the three full financial years available to them until the year 2000-01:

**Additional Resource Generation by MCD & NDMC upto 2000-01
(Taken Into Consideration by DFC)**

Source	Rs. in crores	
	MCD	NDMC
Tax Sources :		
(1) Property Tax	860	43
(2) Duty on Transfer of Properties*	Nil	Nil
(3) Tax on Advertisements	Nil	Nil
(4) Duty on Sale and Consumption of Electricity*	Nil	Nil
(5) Professions Tax	100	20
(6) Entry Tax	40	8
Non-tax Sources		
(7) Increase from Fees, Charges etc	50	
(8) Night-parking charges	60	Nil
Total	1,110	71

* Likely additional revenue from these source not taken into reckoning; left as a resource-cushion for MCD.

Borrowing and Debt Management

The Commission are called upon to take into account 'the scope for improvements in resource mobilisation by the Municipalities' and to recommend 'the measures needed to improve the financial position of the municipalities.' The Commission have separately considered various aspects of resource mobilisation through tax and non-tax means. One important source, over and above these, is resort to borrowings, specially for projects which can be made self-financing, largely, even if not wholly.

Importance of Borrowing as a Source of Finance

Borrowing is an important source of finance for local bodies in advanced countries with developed capital markets, all over the world. In the United States of America, which represents an outstanding example of debt-financed municipal infrastructure build-up, the municipal debt issued over the 15-year period from 1970 to 1985 was twice the value of corporate debt. The total municipal debt currently outstanding is a colossal sum of US Dollars One trillion, equivalent to Rs. 40 lakh crore (about Rs. 40 trillion), as per information provided by Indo-U.S. Financial Institutions Reforms and Expansion (FIRE) Programme, (Debt Market/Infrastructure Component) Consultants. The FIRE Programme, it must be noted, has been playing a catalytic role in

motivating and enabling municipal authorities in tapping the capital market for financing their ever-rising investment requirement to provide basic civic services to people, with other sources, notably government grants, falling way behind their pressing needs. (A copy of the presentation to the Commission, "MUNICIPAL BONDS - Potential and Relevance for India", made jointly by the National Institute of Urban Affairs and FIRE Consultants, bears close study and is placed at Annexure 13.1).

Given the woeful state of urban infrastructure, verging on breakdown of such basic services as power, water, sewage disposal, sanitation and so on, and the likely resource flow to municipalities estimated at a mere one-fifth or less of the required investment, the huge resource shortfall can be met only through market borrowings.

Even otherwise, it is only meet and proper, from the point of view of inter-temporal equity, that the current set of tax-payers are not made to finance the infrastructure build-up whose benefits would be reaped by subsequent generations. Infrastructure investments financed from long term borrowings, with repayment extending over 30 to 40 years or longer, spreads the burden equitably over time.

This is not all. The requirements of securing loans and of managing the debt on a credible basis impose the much needed fiscal discipline. As Lane points out --

"Effective market discipline requires that capital markets be open, that information on the borrower's existing liabilities be readily available, that no bailout be anticipated, and that the borrower respond to market signals".
(Lane, Timothy D (1993): *Market Discipline. IMF Staff Papers*, 40(1), March)

The transparency and discipline, arising out of the necessity to meet the criteria of credit worthiness and the demands of sound debt management, of municipal fiscal affairs is, in itself, a highly desirable outcome. The burden of debt fund should also lead to improved project formulation and tighter implementation as also for higher cost recovery through adequate user charges.

Control by Higher - Level Government

Borrowings by local government is almost always controlled by higher level governments, though there are variations as to the extent of such control, note *Bahl and Linn (1992): Urban Public Finance in Developing Countries: Oxford Univ. Press, Washington*). They further note that in many countries local authorities may borrow only from higher level governments. Such restriction on borrowing by local governments is not surprising in countries where capital markets are in undeveloped state and where national governments consider themselves obliged to play an active role in nation-wide allocation of public and private savings.

"Countries generally adopt", observes Teresa Ter-Minassian, Deputy Director, International Monetary Fund, "one of four approaches to controlling sub-national borrowing (1) sole or primary reliance on market discipline, (2) co-operation by different levels of government in the design and implementation of debt controls, (3) rules-based controls, and (4) administrative controls. Examples of the first model can be found in Brazil (until recently) and in Canada. Notable examples of the second model are Australia, Germany and the Scandinavian countries, although in Germany sub-national governments must also follow the "golden rule," which prohibits borrowing to finance current expenditure. Other types of rules, prevailing in different countries, stipulate limits to the absolute level of sub-national governments' indebtedness; allow new borrowing up to a level of debt, consistent with a maximum debt-service ratio; and/or ban or restrict certain types of borrowing that involve greater macro-economic risks, such as borrowing from the central bank or from abroad. Examples of a rules-based approach can be found in, among other countries, Spain, Switzerland and the United States". (*Finance & Development, September 1997, Pp 38 -39*)

Direct controls by Central or State Governments over local government borrowing, though not uncommon, represent an inferior form of intervention as compared

to rules-based approach. As Ter-Minassian points out, "the current decentralisation trend seems likely to be in conflict with systems of administrative controls imposed by the central government on sub-national borrowing. Rules-based approaches to debt control would appear preferable to administrative controls in terms of transparency and certainty and are also preferable to statutory limits defined in the context of the annual budget process which may be unduly influenced by short-term political bargaining. There is, in any case a clear macro-economic rationale for barring all levels of government from borrowing from the central bank (or, at a minimum, severely restricting their ability to do this). Borrowing abroad by sub-national governments should also be strictly limited, in accordance not only with their debt-servicing capacity but also with macro-economic (specially monetary and balance of payments) considerations" (Ibid. p. 39)

While, in general, it may be best to leave the discretion as to the purposes for which local authorities may incur debt obligation, yet the "golden rule" forbidding borrowings to finance current expenditure - a rule that binds the sub-national governments in Germany - has a great deal of justification, specially in developing countries having weak institutional controls and traditions. To quote Ter-Minassian again, "In principle, a good case can be made for limiting all borrowing to investment purposes. However, the so-called 'golden rule' may not be sufficiently restrictive in countries that need to generate government savings to finance at least a part of public investment. Moreover it may not be difficult to prevent governments from getting around the golden rule by labelling certain current expenditures as investments." (Ibid p. 39)

Borrowing by local bodies from abroad has, however, been tried successfully in some countries, notably Argentina, England and Brazil. In Argentina, all levels of government can borrow domestically as well as abroad. In 1994, the provinces in Argentina were able to finance a deficit of about 0.7 percent of GDP from borrowings. In Brazil, Sao Paulo alone is reported to have accumulated a debt of some \$ 40 billion (Financial Times, March 25, 1995, p. 4). In England, the local councils under the 1972 Act of Parliament can borrow abroad. In fact, Central Government in 1973 encouraged

bigger councils to seek foreign loans. (*Redcliffe and Wood, 1974: English Local Government Reformed, Oxford University Press, Washington*)

Controls over Municipal Borrowings in India

Following the advent of municipal government in India, the British government brought in the requisite laws to control municipal borrowings. A series of enactments - Local Authorities Loan Acts were passed in 1871, 1879 and 1914. Broadly, as Rao has summarised, the Acts mainly provided:

- (i) the period of borrowings not to exceed thirty years;
- (ii) the rate of interest on local borrowing not to be unduly high as to adversely affect the interest of government security holders;
- (iii) that there was an adequate repayment provisions of both the principal and interest; and
- (iv) that all public loans of municipal bodies have the necessary legal approval of their Governments.

[*Rao, NR (1986) Municipal Finance in India, New Delhi, Inter-India publications*]

The Constitution of India did not alter the status of local borrowing. The States adopted the Local Authorities Loan Act of 1914 with little modifications. Local bodies were permitted to borrow money either from State government or from the market with the prior approval of State government subject to the following conditions:

- (i) The loan is for municipal development and is exclusively used for the purpose sought;
- (ii) It is for the acquisition of land or providing relief and establishment and maintenance of relief works in famine and scarcity conditions;
- (iii) It is meant to pay off debts due to the government; and
- (iv) It is to repay a loan raised earlier under Municipal Act.

Provisions Governing Borrowing by Municipalities in Delhi

(a) *Power to Borrow:* DMC Act 1957 and NDMC Act 1994 make identical provisions to empower Municipal Corporation of Delhi and New Delhi Municipal Council to borrow, under sections 185 and 126 respectively. S.185 of DMC Act provides—

"185. Powers of Corporation to borrow -(1) The Corporation may, in pursuance of any resolution passed by it, borrow by way of debenture or otherwise on the security of all or any of the taxes, rates, cess, fees and charges authorised by or under the Act any sums of money which may be required:

- (a) for acquiring any land which it has power to acquire;*
- (b) for erecting any building which it has power to erect;*
- (c) for execution of any permanent work, the provision of any plant, or the doing of any other thing which has power to execute, provide or do, if the cost of carrying out the purpose in question ought to be spread over a term of years;*
- (d) to pay off any debt due to the Government;*
- (e) to repay a loan previously raised under this Act or any other Act previously in force, or*
- (f) for any other purpose for which the Corporation is, by virtue of this Act or any other law for the time being in force, authorised to borrow.*

Provided that -

- (i) no loan shall be raised without the previous sanction of the Central Government or without previous publication of the application for sanction under the Local Authorities Loan Act, 1914 (9 of 1914), and the rules made thereunder; and*
- (ii) the amount of loan, the rate of interest and the terms including the date of floatation, the time and method of the repayment and the like shall be subject to the approval of the Central Government.*

(2) When any sum of money has been borrowed under sub-section (1), no portion of any sum of money borrowed for any of the purposes referred to in clause (c) of sub-section (1) shall be applied to the payment of salaries and allowances to any municipal officers or other municipal employees other than those exclusively employed in connection with the carrying out of that purpose."

Section 186 of DMC Act stipulates that time for repayment of such loans should, in no case, exceed 60 years and the time for repayment of any money borrowed for the

purpose of discharging any previous loans shall not, except with express sanction of Central Government, extend beyond the unexpired portion of the period for which such previous loan was sanctioned (corresponds to S.127 of NDMC Act 1994).

These restrictive conditions on local loans appear to be inoffensive and even desirable. Yet, within the ambit of statutory control the local bodies need generous accommodation for local capital build-up. The municipalities in general are stagnating for want of adequate loanable funds to make provision for civic necessities. Municipal capital formation has been one of the most neglected sectors in our scheme of public finance. Liberal loan-financing is vital in supplementing municipal resources.

(b) Repayment Modalities/ Sources: Provisions for redemption of municipal debt may take any of the following three forms, viz., (i) Sinking fund system, (ii) Annuity system, and (iii) Instalment system. DMC Act provides u/s 190 (NDMC Act u/s 131) the maintenance and investment of sinking funds for the purpose of repayment of debts. It cannot be applied to any other purpose until whole loan is discharged. Section 194 of the DMC Act and S.135 of NDMC Act also provide that *all repayments due from the Corporation for interest on and repayment of loans shall be made in priority to all other payments due from the Corporation*. In addition, failing this commitment, section 195 of DMC Act and S.135(2) of NDMC Act provide that if any money borrowed or deemed to have been borrowed by Corporation from Central Government or any interest or costs due in respect thereof be not repaid according to the conditions of the loans, *the Central Government may attach the Municipal Fund or any part thereof*. And Central Government will appoint an officer to look after this Fund in the same manner as the competent Municipal Officer would have been doing.

Whether the municipal loan should be repaid from general tax revenue or from surpluses which the service-rendering agency must generate, is a controversial issue. In terms of business economics, it is undeniable proposition that loans should be productive and self-liquidating. But in the case of public borrowing, especially of local bodies, it is

accepted that this principle cannot always be adhered to. The nature and purposes of municipal projects are such that they cannot be treated or managed on solely commercial basis. The municipal public sector providing public goods and services cannot, in several cases go for fully remunerative pricing in order to ensure sufficient surpluses. It seems inevitable, therefore, that a part of the loan may be a charge to current revenues of the municipal body in exceptional cases where a section of the service recipients deserve subsidy the burden of which cannot be met fully by over-charging the more affluent ones, i.e. by way of cross-subsidy.

Recommendations of Relevant Committees

The Local Finance Enquiry Committee had proposed that it was desirable to have a co-ordinated loan policy in which the interests of Union Government, the State Governments and the local bodies should be duly harmonised. It did not favour State governments' guaranteeing the principal and interest of loans raised by local bodies. But on the question whether Section 20 of the Indian Trusts Act may be amended to include local bodies of bigger cities to enable funds of registered trusts to be invested in municipal bonds, it suggested that the Government may consider it favourably. The Committee viewed that there should be no curtailment of local borrowings so long as they are intended for productive schemes.

The Augmentation of Resources Committee, 1963 expressed the view that, "*The debt of remunerative enterprises should be a charge on the revenue derived from these enterprises. There should, however, be staggering of dates for paying instalments for the repayment of loans at least for such period till the enterprise really becomes remunerative. Local bodies should not in any case be allowed to borrow indiscriminately from the open market but borrow their entire loan requirements either from the State government or from a central loans institution like the Urban Development Board to be created for the purpose*".

The Committee went on to make the following recommendations —

- (a) A Statutory Urban Development Board should be set up in each State which should be empowered to acquire lands and properties wherever necessary and undertake most aspects of town development. The Board may also statutorily undertake water supply and sewerage schemes in respect of specified regions. It can also function as Central Loans Institution which would supply long-term as well as short-term credit to local bodies. The initial capital for the Development Boards should come out of the total provisions made in the plan for urban development. The Board should also be empowered to raise resources of its own and should also explore the possibilities of financial assistance from various international aid agencies.
- (b) A standard percentage of collections should be prescribed and any municipality which fails to achieve this percentage without adequate reasons should be disqualified from receiving any government grant or loans.
- (c) Urban local bodies should be encouraged to take up remunerative activities which would create permanent assets yielding perennial non-tax income. As far as possible these remunerative activities should be financed out of a revenue fund.

The Rural-Urban Relationship Committee (1966) made some more elaborate recommendations. The appropriate solution to the problem of financing capital works of local bodies lies in preparing city development plans and incorporating them in the State Five-Year Plans. The State Governments should include the requirements of urban local bodies in deciding the quantum of loans to be raised from the open market. With a view to meeting the capital requirements of municipal enterprises, including city transport, milk supply, electricity, markets, cinemas, hotels and the like, a Municipal Finance Corporation should be set up to advance loans to local bodies. It should have an authorised initial capital of Rs 10 crore to be subscribed by Government of India, Reserve Bank of India, State Bank of India, Life Insurance Corporation, commercial banks and other financial institutions and also the local bodies. It should be run on commercial lines

and should have the power to issue debentures and raise market loans under the guarantee of Union Government.

Present Status of Borrowings by MCD and NDMC

Loans to MCD come from the Government, broadly in two forms - one for meeting its non-Plan requirements and the other for creation of capital assets, as also for the development of various localities in urban and rural areas, under Plan projects. For non-Plan purposes, petty loans are received for capital works as reflected in A/c IV of the budget of General Wing of MCD. To correct the revenue account deficits in certain years, it requests the government for and receives Ways and Means Advances as loans. For Plan schemes, the Corporation prepares its five-year development Plan to be considered by the Government for Plan assistance by way of a combination of loans and grants, tagged with various terms and conditions.

NDMC too has been receiving Plan assistance largely by way of loans from GNCTD for different sectors viz., (i) Power, (ii) Housing, (iii) Water Supply & Sewage Disposal, and (iv) Agriculture and Allied Services (Compost Plant)

Debt Profile of MCD

Neither the Memorandum of MCD nor the budget papers throw any light on the outstanding amount of principal and interest payable annually. However, the Commission have drawn up MCD's loan profile since 1958-59 and of erstwhile local bodies before that which were merged with MCD and were with repayment arrears by eliciting information on instalments and interest due on year-wise basis which the Corporation confirmed subsequently, vide letter No.CA/B&A/97/28 dated 25.4.1997, with minor modifications for certain years leaving the unreconciled difference of a mere Rs 3.70 lakhs.

The loans received by MCD are shown in table at Annexure 13.2. Total amount of loans received from 1958-59 to 1995-96 was Rs 438.8 crore, in addition, at the time of re-organisation of municipal bodies on April 7, 1958, the newly created MCD had owned the loan outstandings of erstwhile local bodies amalgamated with the Corporation. This balance amounted to Rs.1.81 crore out of a total loan of Rs.2.86 crore that the erstwhile municipalities had borrowed from Government during 1949-50 to 1957-58. Annual instalments liability of these loans works out to Rs.5.53 lakh and interest liability on outstandings at Rs.7.40 lakhs. As per the agreed terms and conditions, the redemption of this old loan should have been over by the year 1987-88. Likewise, the entire loan obtained from 1949-50 to 1995-96 is due to be redeemed by the year 2010-11.

It may be noticed that in five of the years viz., 1960-61, 1966-67, 1969-70 to 1973-74 and 1974-75; MCD did not receive any loans but from 1976-77 continuously, it has been obtaining loans, and from 1984-85 the amounts have become larger.

The loans to MCD may be broadly classified as non-Plan and Plan loans and also on purpose-wise basis. Another basis of categorisation may be as those for remunerative schemes and for non-remunerative (welfare) activities.

As noted above, for non-Plan purposes, MCD has depended on higher-level government for correcting its revenue account fiscal imbalances through Ways and Means Advances. On six occasions, a total sum of Rs 48.94 crore was received during this period (1958-59 to 1995-96). These loans were to be repaid over 5-15 years at the interest rates ranging from 9 to 12.5 percent. Normally, such advances are of one or two year duration as the same are granted merely as stop-gap assistance to meet the short-term deficits on revenue account. Seeking such advances frequently with repayment spread over longer period is a sign of unhealthy financial management.

Under Plan heads, MCD obtains large amounts of loan for undertaking projects for development of civic infrastructure for a wide array of activities as will be seen below.

Purpose-wise loans obtained by MCD since its inception have been shown in (Annexure, 13.3), detailed into outstandings as on April 1. During the entire period from 1958-59 to 1995-96 total loans received were Rs 438.35 crore out of which Rs 50.68 crore may be categorised as being for non-remunerative purposes. These account for 80 per cent of the entire loans. They were raised for development of regularised unauthorised colonies (37.8 percent), ways and means advances (11.2), development of rural villages (19.9), for the construction of office building and civic centres (7.6 percent) and the rest 3.5 percent was for other activities such as development of urban villages, sanitation and conservancy, flood relief, general purposes and other miscellaneous activities. All these loans may not be purely non-remunerative as a part of it may be recovered in the form of development charges from the property owners themselves of whose property goes up due to these developments.

Loans classified as being for remunerative purposes accounted for 20 percent of the total, at Rs 87.67 crore. Among them, loans for construction of quarters for *Safai Karmacharis* and other staff together account for 18.4 percent and the rest 1.6 percent was procured for construction of shopping complex, land development, compost plant, slaughter house, development of *dhobi ghats*, low income housing schemes, dairy colonies and tourist spot facilities. Strictly speaking, these remunerative schemes do not pay back the cost, therefore, the major burden is borne by the Corporation itself. It may be argued that the Corporation has not been able to recover its cost. Only a few capital assets like shopping complex, slaughter houses and housing schemes qualify for total cost recovery as the services provided therefrom are commercial in nature.

The loans received by the Corporation range from those at a low rate of interest of 3.5 percent per annum to those at the high 12.5 percent per annum and the period of

repayment also ranges from 2 years to 30 years as shown in table at Annexure 13.4. All the loans were received from the Central Government. The cost of loans as defined by ratios of total interest accrued and principal amount, or, alternatively total interest accrued and total debt repayments, show that for the entire period from 1949-50 to 1995-96 (47 years) the average cost comes out to 75.6 percent and 43 percent respectively, by the two ratios. The rate of interest and the length of repayment decides the magnitude of the cost. Recently, these ratios have been as high as 87.5 percent and 46.7 percent which implies that nearly half of the total debt charges is towards payment of its interest. Judged from the loan financing structure by financial sector for priority and non-priority projects, these loans may be termed as soft loans.

As already noted, Section 195 of the DMC Act stipulates that the debt servicing is the first charge on the revenues of the Corporation in priority to all other payments. The Memorandum mentions vide para 4.4 the ever-increasing loan liabilities bearing on the local body. It argues that lack of financial resources has been compelling the MCD to postpone the repayment of loans. As a consequence, its loan liabilities have been increasing over the years. Repayment data on loan liabilities of MCD are presented in table, Annexure 13.2. It is evident therefrom that against the loan liability payable during the year, MCD has been repaying insufficient amounts only about a quarter. In 1994-95, for example, against a liability to pay Rs 56.5 crore (29.1 crore of instalment due and Rs.27.4 crore as interest), MCD could repay only Rs 7.43 crore i.e. 13.2 per cent of due for the year. Loan liability excluding interest payment, has increased from Rs 196.48 crore in 1990-91 to Rs 336.01 crore in 1994-95 and Rs 373.37 crore in 1995-96. According to the Memorandum, *"the loan amount is thrust on the MCD by the Government of NCT under the Five-Year Plans of the NCT without getting its consent and without an assessment of prospects for repayment of outstanding loans due to the very nature of expenditure financed out of loan which are not remunerative in nature so that cost recovery for loan repayment could be easier. This has exacerbated the fiscal stress which became acute and critical. As discussed, subsequently in this Memorandum, the Delhi Finance Commission needs to give serious thought to this kind of funding where*

non-repayment of loan is built into the pattern of funding. The Commission fail to appreciate how loans can be 'thrust' on anyone. MCD could easily excuse itself from accepting the offer of loans unless the terms and conditions for them were changed by GNCTD to meet its particular requirements. The logic given above is an after-thought which can hardly justify MCD's persistent violation of mandatory provisions of law and has been clearly brought forth for the sake of making out some kind of a case for debt-forgiveness, in one form or another. In the context of MCD's argument, it is pertinent to note that MCD does not observe budgetary distinction between revenue and capital account, the provision of repayment of loan instalments and interest thereon is made in the main account of General Wing i.e. Account 1(A).

Debt Profile of NDMC

NDMC has been receiving loans only for development projects under Plan except for once, in 1991-92, when it took a small loan of Rs.6.40 lakh under non-Plan schemes. At the beginning and end of the twelve year reference period, it received loans of Rs.2.36 crore in 1984-85 and Rs.8.54 crore in 1995-96, vide table, Annexure 13.5, showing a growth rate at 14.01 percent per annum. Highest growth rate was for loans received for electricity supply - Rs 0.26 crore in 1984-85 and Rs 5.70 crore in 1995-96. For construction of staff quarters, it received Rs.0.18 crore in 1984-85 and Rs.2.30 crore in 1995-96, showing a growth rate of 14.99 percent. For water supply and sewage disposal, it obtained Rs.1.72 crore in 1984-85 and Rs.2.30 crore in 1995-96 at a rate of growth of 9.04 percent over the period. For compost plant and public works, the Council has been receiving loans inconsistently over the period.

On an average, the highest share of the loans, 56 percent, went for electricity supply - the share in 1984-85 was only 10.98 and jumped to 66.74 percent in 1995-96. Next in priority was for water supply with an average share of 28.21 percent, going down over the period from 73.07 percent in 1984-85 to 26.93 percent in 1995-96. The third largest amount was for housing with an average share of 13.60 percent. It would thus be

noted that NDMC has been incurring loan liability for activities which are remunerative, with over four-fifth of the debt having been employed for profit-generating activities of supply of electricity and water.

NDMC has argued that net flow of funds as receipts net of repayments is not in their favour. With time, the repayments have been nearly matching the plan assistance. If current loans are to be repaid, there is an outflow rather than inflow, in net terms. The total loans and grants on plan side as a percentage of receipts is 4.6 percent while principal and interest payment amount to 4.2 percent of expenditure. Since the surplus is marginal there is hardly any net inflow. The grants portion on Plan side is only 2.8 percent of receipts against the outflow on account of principal and interest repayment at 4.2 percent of total expenditure. The actual flow of assistance on the Plan and non-Plan side having gone down in real terms over the years, NDMC's internal resources have come under an ever-increasing pressure. This analysis by NDMC is based on the data for the five year period 1989-90 to 1993-94. An analysis based on the data for the entire reference period 1984-85 to 1995-96 has revealed that on exclusively netting out the loan components, the Council is not running in a state as stated *supra*. The loans are given by Govt. of NCTD at interest rates between 10 and 12.5 percent and it is presumed that the return will be more than compensate for the interest outgo. It means the benefits will over weigh the costs of the projects and the project is, thus, economically viable. Only loans given for compost plants do not come true on this test but this project has some other social benefits, which have not been estimated in monetary terms and are of indirect nature also, related to environmental and ecological bearing.

Unlike MCD, NDMC has been repaying the due instalments of both principal and interest. Balances of current receipts of Plan loans and current repayment show that lately there has been a net outflow rather than inflow though over the twelve year reference period as a whole, the net inflow was Rs.32.41 crore, the Council having received loans worth Rs.119.42 crore and having repaid Rs. 87.01 crore inclusive of Rs.1.94 crore deposited in sinking funds.

It will thus be seen that of the two municipalities, the problem of non-payment of instalments of principal and interest due, in violation of the mandatory provisions of law of 'unviable loans' by government as extenuating circumstances and have requested the Commission to consider debt-forgiveness in one way or another. This aspect will be considered later.

Recent successes in floating bonds by some municipalities

As already noted, the Indo-US FIRE Project has successfully brought the municipal bond concept to municipality in our country. Already Ahmedabad, Mumbai, Pune, and Vijayavada have achieved credit ratings for floating municipal bonds from nationally recognised credit rating agencies. The position, as set out in the presentation made to the Commission by FIRE consultants placed in full at Annexure 13.1, is given below:

Credit Rating of Municipal Bonds				
- All Three Indian Rating Agencies Have Been Involved in Rating of Municipal Bonds in India				
Declared Ratings				
City	Agency	Rating	Date	Amount
- Ahmedabad	CRISIL	A+	Feb 96	Rs. 100 crores
- Mumbai	CRISIL	AA-(SO)	Jan 97	Rs. 25 crores
- Pune	CARE	AA-	Feb 97	Rs. 200 crores
- Vijayavada	CRISIL	A-(SO)	Nov 97	Rs. 30 crores
- On Going Ratings				
Municipal Authorities: Calcutta, Coimbatore, Surat, Madurai, Sholapur, Bangalore, Baroda, Ludhiana, Utility Boards: Madras Metro, Bangalore Metro, Punjab Water, Kerala Water.				

Ahmedabad Municipal Corporation is all set to issue its municipal bond in December 1997. The success of this experiment which appears to be beyond doubt would be a historic milestone in the evolution of municipal finance in India. Pune, Vijayavada and others should follow soon. The Commission hope fervently that the municipalities in Delhi will not lag behind but would soon tread the path of financial self-reliance for raising the level of civic services from the current far from satisfactory state to a much higher level of which the Capital can justifiably be proud.

Road Map for Raising Resources from Market

There appears to be an unstated assumption at the back of people's minds that municipalities in general and MCD in particular are in such poor financial straits that it is a pipe dream to think that they could raise resources from the market for civic infrastructure build up from the market. As a result of a series of interactions with credit rating agencies, the Commission have been confirmed in their tentative thinking that local bodies serving comparatively affluent population and having access to taxation powers over a booming resource like urban land and buildings, should, ipso facto, be capable of tapping the capital market. Considering that, there may not be any other option available to MCD and NDMC to raise finance for providing essential civic services, the Commission have taken particular pains to draw up a road map which our municipalities can and must follow in order to be able to float their own municipal bonds. Apart from what the municipalities should do, the Commission have also some suggestions to make for the consideration of higher level governments for actively encouraging local bodies and utilities in the country to access long term finance from the market by providing a policy regime aimed at promoting bond floatation by them. These would be set out later; it would be appropriate here to present details about the kinds and nature of municipal bonds and the procedure for raising resources through them based on Commission's elaborate discussions with, and inputs from, the credit rating agencies.

Municipal Bonds may broadly be classified as (1) Tax-backed or General Obligation (GO) bonds and (2) Revenue-backed bonds.

(1) *Tax-backed or GO bonds* are secured by the full faith and credit of the issuer, which, in turn, is derived from the taxing powers and revenue-generating capabilities of the issuing authority (local government). These are, thus, in the nature of general obligation bonds. These bonds can be structured with certain credit enhancement mechanisms. The structuring of the municipal bonds could be done using an escrow mechanism which involves creating a special account in which the revenue streams for debt servicing are collected and which is supervised by an independent trustee. The borrower-municipality gets a lien on the account only after debt servicing requirements have been fulfilled. The trustee is armed with the authority to direct the municipality to meet any shortfalls in the account by diverting funds from a cash collateral account or any other specified source.

The credit quality of general obligation bonds can be enhanced by providing (a) collateral of streams of tax/non-tax collections; (b) state government guarantee; (c) cash collateral/marketable securities.

(a) *Collateral of streams of tax/non-tax collections*: Identified streams of revenues of a municipal body can be captured in an escrow account with a bank, to act as collateral for bond servicing. The funds in escrow account could also meet the debt obligation directly at the discretion of the trustee of the bonds. The relevant revenue stream of the municipal corporation could be transferred into an escrow account upto the predetermined level of debt servicing (principal and interest of existing debt and interest of proposed debt) every quarter. This would be supervised by a trustee. The balance amount of the relevant revenue stream collections would be available for the current expenditure of the corporation alongwith revenues from other sources.

(b) *State government guarantee*: The state government can provide security to the bond issue by pledging to meet the debt obligation in case of the inability of the municipal body to meet them. The state government would be required to make a budgetary allocation for servicing municipal bonds.

Alternatives to a unilateral state guarantee could be -

i. An agreement with the state government where the grants to the municipal body could be captured in an escrow account and act as collateral to the municipal bond issue.

ii. Rather than a complete guarantee on the bonds, the state government could guarantee to meet a fixed number of interest payments in case of inability of the municipal corporation to meet them.

(c) *Cash collateral/ marketable securities*: A portion of the funds raised through the bond issue can be kept in an escrow account or invested in marketable securities like Unit 64 of UTI and provide credit cum liquidity support to the instrument.

(2) *A revenue bond* is project-specific and is secured by the revenue streams (user-fees or the service charges paid by the users) of the urban infrastructure facility it finances. A bond secured by the tolls collected from a highway or by the charges levied on users of a drinking water facility are typical examples of revenue bonds. The revenue streams standing security for the bonds can be routed through the following structures:

(a) *Pass-through structure*: The cash flows from the assets are 'passed-through' without reconfiguration as and when they are received. The revenues would be captured in an escrow account and periodic payments (usually on monthly basis) would be made to investors, based on the amounts collected.

(b) *Pay-through structure*: The cash flows are reconfigured before payments are made to the investors. The revenue streams would be collected in the escrow account as in case of pass through structure; however, only a

predetermined amount would be passed on to the investors and the balance would be invested in liquid securities.

Credit enhancement could be provided with a combination of the following:

- (a) *Over-collateralisation*: The credit quality of revenue bonds can be enhanced by securitising only a portion of stream of receivables, the balance revenues would also be captured in escrow account and form over-collateralisation. In case of decrease in level of revenues the cushion of over-collateralisation would take care of meeting the debt obligation.

- (b) *Cash collateral*: Cash collateral can be provided (in escrow account as in case of CO bonds), which would be drawn down to suffice the payment obligations on the bond in case the revenues are not sufficient to meet these.

- (c) *State government guarantee*: State guarantees could provide additional comfort to the credit quality of the bond. The payment structure with well defined triggers would be essential for providing state guarantee to revenue bonds.

- (d) *LOC/ Bank Guarantee*: Letter of credit from banks can substitute/ complement the cash collateral to the bond issue.

Securitisation of the revenue streams in a classic revenue bond presupposes that only the revenues from the proposed project are utilised for the debt servicing. This may not be a feasible option for Municipal Corporations as the revenue stream may not be adequate and the costs of additional collateral will have to be incurred specifically in the construction phase.

Raising of Indian Municipals

In general, municipal bodies in India suffer from a poor image. In order to increase the confidence of investors and to make it easier for municipal bodies to raise

funds for infrastructure projects, a credit rating from an independent body becomes imperative. A methodology for rating of General Obligation bonds of municipal bodies was prepared by CRISIL in November 1995 after an in-depth theoretical study. The methodology took into account various credit assessment factors required for the rating of municipal bodies. It was tested on the Ahmedabad Municipal Corporation (AMC) in March 1996 and an A+ rating assigned to the Corporation for a Rs.1000 mn debt issue. After completing the rating assignment, the methodology was reviewed and necessary changes incorporated in it. In its discussions with CRISIL (Ms Sujata Srikumar, Mr. Shogun Banerjee and Mr. Rohit Jha), the Commission underscored the need to make municipalities in Delhi duly aware of the criteria by which credit rating assessment is carried out. The same, as gathered from them, is presented here.

The credit rating exercise can be broken down into the following three principal segments:

- (1) Overall Profile of Municipal Body
- (2) Details of Municipal Finances
- (3) Managerial Assessment of the Municipal Body

(1) *Overall Profile of Municipal Body*: The overall profile is divided into two categories: (a) Legal & Administrative Framework and (b) Economic Base of the Service Area.

(a) The analysis of the *Legal & Administrative Framework* is based on the relevant enactments, which define all the legal, structural and administrative elements of a municipal body. From the perspective of credit-assessment, the following areas are of concern.

- (i) Municipal Functional Domain (Obligatory and Discretionary functions)
- (ii) Grants from the State: Manner of transfer, formula linked or otherwise
- (iii) Tax Powers Allocated to Municipal Body

- (iv) **Tax Rates and Basis of Assessment:** rationalisation of tax-rates, and revision in tax rates and user charges
- (v) **Borrowing Powers of the Municipal Body:** Method of operation of the sinking fund
- (vi) **Organisation of Accounts:** The Act Rules and Regulations specify the organisation of accounts, head-wise and activity-wise, the presentation of budget and the adjustments of deficits in the Municipal Accounts.

(b) The *Economic Base of the Service Area* is analysed with the objective of assessing the revenue-generating potential of the Municipal body. Most proactive municipal bodies have initiated measures to enhance the contribution of tax and non-tax revenues. The extent to which such measures would yield the desired result would depend considerably on the level of economic activity in the service area. This is of specific consideration in cases where the municipal body intends to harness revenue-generating activities like commercial property development.

(2) *Details of Municipal Finances:* The municipal finances are considered in detail in the conventional frame-work of Revenue Account and Capital Account. The receipts and expenditures for the past 5 years are assessed separately. In addition, specific attention is paid to the debt-profile of the municipal body.

(a) *Trends in Revenue Receipts:* Revenue-receipts are broadly classified into tax and non-tax revenues. The contribution of each of these revenue-streams in the aggregate receipts of the municipal body is analysed. In general, increased dependence on tax-based revenues is considered a favourable trend, as a greater degree of fiscal autonomy and control can be associated with such revenues.

- (i) *Property Tax:* Specific attention is given to property-tax assessment and collection mechanisms adopted by the municipal body. The rise in property-tax collections on account of increase in assessed rental value of the properties leading to higher demand raised by the

municipality and increase in the collection efficiency is considered a favourable aspect.

- (ii) *Non-tax revenues*, which are largely in the form of user charges, grants from the state government and income from municipal properties, are analysed as a distinct component of revenue receipts. As far as user charges are concerned the following issues are addressed: (i) extent of cost coverage, (ii) extent of cross-subsidisation, (iii) track record of tariff revisions, and (iv) collection efficiency for user charges and settlement of arrears.

- (iii) The *specific grants* from the state government and their contribution in the total revenue receipts of the municipal body is analysed. A trend which reflects that the dependence on grants is stable or decreasing and that no additional municipal functions are being placed under grant support is viewed favourably. The likelihood of any reduction in the grant support extended by the state government and the extent of stability and transparency in the transfer mechanism is also assessed.

(b) *Trends in Revenue Expenditures* of the municipal body are assessed with reference to activity and head-wise classifications. The *activity-wise analysis* considers the proportionate allocations made for provision of core services (water supply & sewerage, primary education, public health & medical relief, public safety, public works and solid waste management). The emphasis here is on the stability and consistency in expenditure allocations for provision of core services.

- (i) The *head-wise analysis* of revenue expenditures considers the allocations made under various functions like wages & salaries, operating expenses, repairs and maintenance and debt-servicing. The head-wise analyses indicates the main cause of increase in expenditure levels and the extent of flexibility and expenditure control that can be exercised by the municipal body. In cases where the wages & salaries and debt-servicing costs have increased

significantly, the extent of flexibility and the potential for expenditure control is limited.

- (ii) The *debt profile* of the municipal body is analysed with reference to the source, tenure, interest-rates and repayment arrangements for all major loans raised by the municipal body. The loan retirement schedule and the average interest costs are considered in detail.

(3) *Managerial Assessment of a municipal body* is made on the basis of an in-depth study of its (a) *structural strengths* as judged from the organisational structure, division of responsibilities, systems and procedures, level of computerisation etc., (b) *managerial capabilities*, comprising calibre of key personnel, collection efficiency for taxes, level of control exercised on expenditures, project-management capabilities, track record in managing external environment, including political forces, resource mobilisation abilities, responsiveness to emerging opportunities, level of private sector involvement, etc., and (c) political risks, taking into consideration political will to undertake reforms, conflict of interest between municipal executive & elected council, council's support to municipal executive, differences in tax-rates, tariffs: Commissioner's budget vs. council's approval, elections, frequency, council under suspension, relationship with state government, exposure to changes in state-level political scenario.

Municipal Bonds for Civic Infrastructure

Financial requirement for building up urban infrastructure have very recently been estimated by the Expert Group on the Commercialisation of Infrastructure Projects headed by Dr. Rakesh Mohan, Director General, National Council of Applied Economic Research. The Report of the Expert Group titled "*THE INDIA INFRASTRUCTURE REPORT - Policy Imperatives for Growth and Welfare*" notes the unsatisfactory state of current urban infrastructure, and 'colossal' requirements of investment to bring it to a satisfactory level. It goes on to state that the urban local bodies who provide infrastructure services in cities and towns have lacked resources "even to meet the O & M

requirements of these services" and that "the government does not have the financial capacity to continue to subsidise the beneficiaries" in the circumstances it concludes that, "It is high time that a commercial approach is adopted." (Ibid, Vol. I, Executive Summary, p. 27).

It will be seen that a progressively larger share of outlays on urban infrastructure build-up would have to come from the capital market. Given the fiscal constraints under which the Union and State Governments have to function under the new policy-frame of the Central Government, flow of funds from Plan resources has been dwindling and will continue to go down in foreseeable future. The Commission would therefore stress upon both MCD and NDMC to prepare themselves in all respects for securing high credit ratings by adopting the approach outlined above and to go for bond floatation to raise the necessary resources for meeting growing civic needs of their increasing populations.

The Commission also take note of the fact that the huge success of municipal bond market in USA which is bigger than the corporate equity market is, in no small measure, due to the grant by the federal and state governments of (income) tax-free status to them. It appears necessary that some similar policy of fiscal incentives is adopted by the Government in order to promote the concept of municipal bonds and to build up investor incentive and confidence in such new financial instruments.

Debt Relief to MCD

In its Memorandum, MCD have stated that the total loan liability excluding interest payment stood at Rs.388.55 crore in 1995-96 (incidentally Annexure 13.6 shows the total loan liability at the end of 1995-96 at Rs.366.46 crore). Citing the Morarka Commission recommendation to give assistance as grant-in-aid on hundred per cent basis "in respect of non-remunerative capital projects which are undertaken by the Corporation....." MCD have argued that the "financial assistance which is being presently given in the form of loan may, therefore, be given as Plan grants and further in

order to give relief to MCD, outstanding loan of Rs.388.55 crore as on April 1, 1996 may be converted in grants or may be written off" (Commission's assessment, however, shows that the total outstanding loans as on April 1, 1996 were Rs.373.37 crore and interest due but not paid was Rs.143.16 crore).

The Commission do not view with favour the above suggestions of MCD. The two alternatives suggested by them, in a sense are one and the same thing viz. the lender relinquishing his claims over the principal and interest thereon permanently. The Commission consider that any debt relief in the form of write offs, partially or fully, will lead to fiscal profligacy and may even provide an inbuilt disincentive for prudent use of borrowed funds in future. Such write offs, as a rule, undermine the sanctity of contracts. In the instant case it also tantamounts to an *ex post facto* condonation of the violation of the mandatory provisions of the DMC Act. Further, the Commission are unable to overlook the current stress on the overall fiscal system of the country which also acts as a constraint on the extent of the debt relief that can be allowed during the award period.

The Commission, however, have been concerned with the state of indebtedness of MCD and felt that some relief in debt servicing was unavoidable. While it would have been ideal to device an arrangement in which debt relief was linked to the fiscal performance of MCD, it may not be possible to do so immediately till the necessary resource augmentation measures are implemented in right earnest. To provide relief to MCD, the Commission have, therefore, evolved a package comprising consolidation of past loans, reduction in rate of interest and partial rescheduling of loans with a cap on annual burden, but simultaneously ensuring repayments of the rescheduled instalments and interest due. In doing so, the Commission have been guided by the twin objectives that loans once contracted must be repaid in full (a) to protect the interest of the lender and (b) to enhance the credit-worthiness of the borrower. The Commission accordingly recommend that the loans outstanding as on April 1, 1996 be consolidated into a single loan at a fresh rate of interest 2 per cent lower than the weighted average interest rate of the loans so consolidated (which ranged between 3.5 per cent to 12.5 per cent). This

amount, according to the Commission's calculations, stands at Rs. 373.37 crore. The period of the loan so consolidated be raised to 20 years i.e. 5 years more than that of the last loan taken upto March 31, 1996. The interest due upto March 31, 1996 but not paid, aggregating to Rs.143.07 crore, should also be recovered in 20 equal instalments alongwith the interest and instalment of the consolidated loan. The annual burden of interest and repayment instalment, however, should not exceed 10 per cent of the internal receipts of MCD plus its share in the assigned taxes or in the global tax revenue of GNCTD in any year. The Commission are of the view that this dispensation would ease the burden of debt-servicing on MCD and bring it within manageable limits. These payments should be made unfailingly by MCD being the first charge on the Municipal Fund as is provided in Section 194 of DMC Act, failing which they should be deducted by the State Government from instalments of non-Plan grants or from other fiscal transfers of the respective year. The loans contracted after April 1, 1996 are not to be included in the package. It should be for MCD to deploy them, to the maximum extent possible, in such a manner that the return on borrowed funds will at the least not be less than the rate of interest at which these are held so as to enable MCD to service them in full in accordance with the contract.

According to the reassessment made by the Commission taking into account the repayment schedule, the current rate of interest separately for each loan contracted upto 1995-96 and providing interest on the diminishing balances, the total projected liability on account of debt charges during the award period is estimated at Rs.254 crore comprising Rs.133 crore on account of repayment of instalments and Rs.121 crore on account of interest excluding payments of arrears of interest. As a result of Commission's recommendation, in the award period MCD is estimated to save Rs.34 crore on account of interest payment. The outgo on account of repayment of instalments is estimated to come down from Rs.133 crore to Rs.93 crore i.e. by Rs.40 crore during the award period. The two together are estimated to result in a relief of Rs.75 crore per annum. As against this MCD will be required to pay Rs.36 crore towards payment of arrears of interest on loans upto March 31, 1996, still leaving them with an estimated

relief of Rs.39 crore during the award period, besides other benefits which cannot be quantified, specially reduction in the annual repayment burden. Annexure 13.6 details the rescheduled amount of repayment liabilities with dues computed as per agreed terms and conditions of loans. Total relief at the rate of 2 per cent at total outstanding of Rs.373.37 as on April 1, 1996 at reduced balance would amount to Rs.78.4 crore with soft-phasing of repayment of annual instalments at Rs.18.67 crore till 2016-17 as against Rs.29.14 crore in the absence of the proposed relief.

As has been noted earlier in Chapter 8, MCD deserves to be recompensed for the deficiency in grant-in-aid on account of expenditure on education incurred by it during the first two years of the award period i.e. 1996-97 and 1997-98. These deficiencies worked out to Rs.13.68 crore and Rs. 15.43 crore as against the repayment instalments of Rs. 18.67 crore each for the two years respectively. The former amounts should be adjusted against the latter thereby providing MCD relief to the extent of Rs.29.11 crore and reducing the instalments due against it in the two years to Rs. 4.99 crore and Rs. 3.24 crore respectively. This would be a measure of further relief to the civic body.

Scheme of Devolution

The "revenue gap" of MCD i.e. the deficit prior to fiscal transfers, for the award period, has been estimated by the Commission at Rs. 2401 crore. If the present system of fiscal transfers is projected into the future, MCD would receive, over the award period, Rs. 886 crore by way of grants-in-aid and Rs. 589 crore on account of share in the proceeds of assigned taxes - a total of Rs. 1475 crore, leaving a "resource gap" of Rs. 1176 crore. The corresponding figures for NDMC are Rs. 178 crore, Rs. 59 crore, Rs. 92 crore and Rs. 97 crore respectively. These are the gaps which the Commission must keep in view in making their recommendations.

Before proceeding to undertake this exercise, it would be appropriate for the Commission to give an overall assessment of the financial situation of the municipalities in Delhi. The Commission find that popular fears about MCD's "distressful", "poor", "critical" financial condition are not entirely well-founded. First, even as things stand, if MCD were to collect even a part of the huge amounts owed to it by others, it could achieve a comfortable financial position. The law places coercive process to make recoveries at its disposal but it has failed to employ them effectively. Even the alternative administrative methods of negotiating, providing incentives, adopting quick and impartial review/ arbitration settlement mechanisms, etc. have not been resorted to. Secondly, MCD has tremendous potential for resource raising which has not been duly tapped.

Thirdly, there is immense scope for raising productivity of its operations in order to save expenditure on manpower and improve quality of service.

Principles and Modalities Governing Devolution

In light of the above, the Commission would like to suggest certain principles/ guidelines that should inform the conduct of state-municipal fiscal relations in light of the spirit of the Constitutional Amendments. The starting point of this exercise is to keep in view the ultimate objective of making the local self-governing institutions financially self-reliant so as to equip them with real autonomy. This involves making such fiscal arrangements as would bring access to financial resources in balance with the relative weight of responsibilities to be discharged by the state government and the municipalities.

In this context, it is important to stress that the 73rd and 74th Constitutional Amendments have accorded to the fiscal needs of the local bodies the status of a prior charge on the resources of the state government, excepting, of course, any other Constitution-determined charges. These must be met in priority to those of the other institutions/ bodies which are created by the government either by an executive fiat or under a statutory provision. Happily, GNCTD's finances when looked at closely by the Commission, have been found to be in good enough shape to allow it to recommend the needed devolution without having to confront difficult dilemmas or painful choices.

The access to financial resources should not only be commensurate with functional responsibilities to be discharged but should be definite in terms of availability, non-discretionary in nature, predictable in a budgetary sense and income buoyant. The fiscal arrangement should be so designed as to take care of the usual aspects of equity, efficiency and growth. It should come to the aid of the weak, should promote productivity and economy, and provide incentives for investment into the future.

Yet another guiding principle which the Commission have adhered to is that of honouring the sanctity of inter-governmental contracts, specifically in the matter of municipal borrowing. The Commission have favoured measures to strengthen the finances of municipalities in order to enable them to honour their debt obligations instead of conceding the suggestion/ request for debt-forgiveness. Re-scheduling of debt in order to ease the annual repayment burden coupled with increasing the rightful flow of funds to the civic bodies is, as a matter of sound fiscal principle, a higher and better option than loan-forgiveness of one kind or another. What is more, there is a pressing need for municipalities to acquire an image of trustworthy borrowers. For, it is clear beyond doubt that they will have to tap the market in a big way in future to supplement the resources for infrastructure build-up, over and above the progressively dwindling share of their essential requirements that might be expected to be met from Plan resources.

Considering that civic infrastructure in the metropolis is in pretty bad shape, there is an urgent need to provide for (a) adequate resources for operations and maintenance (O&M) of existing capital assets, and (b) stepped up flow of funds for capital projects by generating adequate surplus in the revenue accounts to supplement the flow of funds from Plan resources. This would be possible only if potent incentives are built into the scheme of devolution with the objective of motivating the municipalities to mount the requisite effort to (a) tap their revenue potential optionally and (b) realise the vast scope for economy in municipal administration by raising the current low levels of productivity of its staff and operations, plugging leakages and wastages, and adopting new methods, techniques and technologies of functioning.

The need to recover costs of municipal resources by levying appropriate user charges is another matter of basic importance that needs to be kept constantly in view. This neglected principle of public finance has brought the nation's infrastructure to a critical state of disrepair and its essential civic and other services to a sorry pass. While cross-subsidies in favour of the weak and poor at the expense of the well-off are inescapable in a caring society, cost recovery is equally important. It is obviously not

possible to build up impressive cities on the shaky foundations of municipal deficits. The crucial importance of non-tax sources of revenue follows from these vital considerations.

Within the broad frame-work of the aforesaid guide-posts, the Commission have put to test the extant system of fiscal transfers by way of statutory grants-in-aid and assigned taxes. It is not hard to come to a quick finding that the system fails on all counts but one. There is no doubt that it is not discretionary and that the revenues are predictable for budgetary and planning purposes. Equally straightforward is the conclusion that it is not equitable as between GNCTD and the municipalities. The latter bear a large burden of making it possible for the civic life to go on and for economic activity to take place. Yet their share in the tax revenues comes from sources which have returned far lower performance in resource generation than those of GNCTD or even as compared to the growth rate of the own tax resources of the municipalities. Apart from failing on the test of equity as between the state government and the municipalities, the system includes a component, viz. compensation in lieu of abolition of terminal tax, which has also deprived MCD, of one of the most potent and fast-growing sources of revenue, namely, octroi (or terminal tax) which, when levied on ad valorem basis would be as buoyant as sales tax. It is worth stressing in this connection that the municipalities with access to octroi as a source of revenue reap rich harvest, with the highest revenue from any of their taxes often coming from it (in Maharashtra, for example, the revenue from octroi is more than half of total own resources of municipalities and is as much as over four times the revenue from property tax). A mention may be made in passing of motor vehicle tax which yields pittance of revenue as compared to the enormous burden it places on municipal infrastructure as well as city environment.

Proposed Alternative System of Devolution

The Commission have, therefore, come to the conclusion that the present system relying on statutory grants-in-aid and scheduler or itemised tax-sharing through assigned taxes requires to be replaced by a system of global sharing of the tax revenues of

GNCTD, with the municipalities. This is in keeping with the current thinking which has been adopted by a national consensus in the sharing of tax revenue of the Centre with the States, by virtue of Government of India accepting the alternative recommendations of the Tenth Finance Commission in favour of global sharing, even though it required amendment of the Constitution. While recommending the new system, the latter listed the main benefits resulting from such an arrangement as follows:

- "(a) With a given share being allotted to the States in the aggregate revenues from central taxes, States will be able to share the aggregate buoyancy of central taxes.*
- (b) The Central Government can pursue tax reforms without the need to consider whether a tax is shareable with the States or not.*
- (c) The impact of fluctuations in central tax revenues would be felt alike by the Central and State Governments.*
- (d) Should the taxes mentioned in articles 268 and/or 269 form part of this arrangement, there will be a greater likelihood of their being tapped."*

The Commission are of the view that the reasons listed above apply with equal force to the present case. Adopting the global sharing system would involve amendment of relevant provisions in the following enactments:

- (i) Section 184 of DMC Act 1957 in respect of Entertainment Tax collected in MCD area;
- (ii) Section 125 of NDMC Act 1994 in respect of Entertainment and Betting Tax collected in NDMC area;
- (iii) Section 20 of the Delhi Motor Vehicles Taxation Act 1962 in respect of Motor Vehicles Tax; and
- (iv) Section 42(r) of DMC Act, which requires payment of grants-in-aid for elementary education.

This is not much of a price to pay for introducing a reform of far reaching consequence. It may be noted that similar approach has been adopted by a number of State Finance Commissions and has received good response.

Recommended Fiscal Transfers

In order to arrive at a reasonable share of GNCTD's tax revenues to be shared with municipalities, it is appropriate to study the pattern of transfers that they had been receiving in the past as also its projection into the future - over the award period. The results of quantitative analysis of this aspect are presented in detail in 'Annexure 14.1.

In a nutshell, the position has been as follows:

- (a) The share of GNCTD's tax revenues transferred to municipalities (including DCB) during the reference period (1985-86 to 1995-96) ranged between a high of 14.16 per cent to a low of 9.4 per cent. The lowest share was in the last year, having consistently declined from the peak attained only four years.
- (b) This decline, attributable to the relative stagnation both of revenues from assigned taxes and of non-Plan grants-in-aid in contrast to the buoyancy of GNCTD's own tax resources, is not likely to reverse but to get aggravated. The share is projected to decline to as low as 7.67 per cent in the last year of the award period, i.e. in the year 2000-01. Over the five year award period, the share is projected at 8.14 per cent as against the average of 11.1 per cent over that of the preceding five years.
- (c) Thus, the decline in the share over the five year period, from the actuals of 1995-96 and the projected of 2000-01 is of the order of 1.73 per cent, while that between the average of last five years of the reference period and that of the five years of award period is as high as 2.96 per cent.

The Commission view such decline with great concern and are of the opinion that this cannot be sustained with reference to any of the principles enunciated above. At the same time, the detailed analysis of municipal finances presented earlier leaves the Commission with no option but to underscore the point that both NCTD and NDMC, the

latter's better financial position notwithstanding, have been seriously remiss on both sides of their balance-sheets. They have not raised, even collected, the resources that are well within their reach and they have fallen far short of putting the resources available to them to effective and efficient use. The citizen who pays his tax dues and user charges and in the process also puts up with harassment and worse from an ill-managed system, remains the hapless victim of fiscal, financial and administrative inadequacies of municipal administration in the Nation's Capital.

The Commission are, therefore, of the view that while maintaining the bottom-line of fiscal equity, the recommended fiscal transfers must provide potent incentives for improved performance on the part of MCD and NDMC on both the resource augmentation, and economy and efficiency fronts. Ample scope available to them on both counts and the steps needed to be taken have earlier been set out in Chapters 11 and 12. Further, the Commission suggest that MCD in particular may consider setting up a Board of Internal Revenue at the apex, under the Commissioner, in place of the present system of an Additional Commissioner (Taxes) assisted by an Assessor and Collector.

A beginning could be made with property tax in respect of which a proposal at some length is placed at Annexure 14.2. Simultaneously, GNCTD could also examine the setting up of an Experts Group on economy and efficiency measures in the municipalities for achieving higher quality civic services in cost-effective manner, leading to far greater citizen satisfaction than at present.

The Commission therefore recommend --

- (a) a basic annual fiscal transfer of 9.5 per cent of GNCTD's tax revenue to MCD and NDMC;
- (b) a further annual transfer, on matching basis, subject to a maximum of 1.5 per cent of GNCTD's tax revenue equivalent to excess of revenue over and above the amounts projected by and taken into account by the Commission for the respective years of the award period; and

70%
population
30% are

- (c) another transfer, on matching basis, subject to a maximum of 1.5 per cent of GNCTD's tax revenue equivalent to savings in expenditure against projections made by the Commission for the respective years of the award period.

In the alternative, transfers under (b) and (c) above could be brought under one criterion - that of surplus on non-Plan account that MCD or NDMC or both generate for financing capital expenditure in each year. The transfer can then be made on a matching basis, subject to an overall ceiling of three per cent of GNCTD's tax revenue in that year.

The division of 70 per cent of the amounts arrived at as above between MCD and NDMC may be on the basis of the ratios of the population living in their respective areas and the remaining 30 per cent in the ratio of the physical area under their jurisdiction. As regards DCB, the Commission are precluded from making any recommendations; as the amounts involved are tiny, these could be met by separate grants over and above the devolution recommended above.

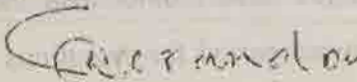
It may be recalled that the Commission have provided, in their projections of requirements of finance by MCD over the award period for operations and maintenance (O & M) of existing assets. That this amount is actually utilised for the specified purpose is important in public interest. GNCTD may consider ways of ensuring that the amount of Rs. 588 crore provided for O & M is so utilised and not spent on personnel or diverted to any other use.

The above recommendations, it may be noted, take care of the concern expressed and specific issue raised by the then Lt. Governor in calling upon the Commission to make an Interim Report. Further, as already stated in the Interim Report of the Commission (September, 1996) any fiscal transfers made by GNCTD to MCD and NDMC will be treated as subsumed into the proposed transfers and may be adjusted from the amounts due as per the recommended scheme of devolution.

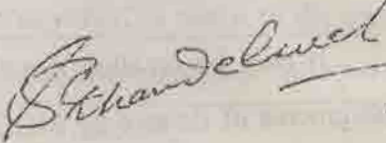
Before concluding, the Commission are happy to place on record their appreciation for valuable assistance rendered by their officers, advisors, consultants and the staff as well as by other institutions, in particular the National Institute of Public Finance and Policy, National Institute of Urban Affairs, Credit Rating Information Services of India Limited (CRISIL), Financial Institutions Reform and Expansion (FIRE) Project whose unstinted labour and co-operation contributed valuably to the accomplishment of the task assigned to them.


31.12.97
(Virendra Prakash)

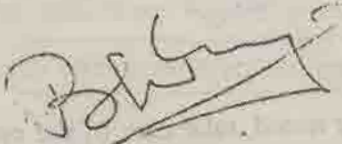
Chairman


(G.N. Tandon)

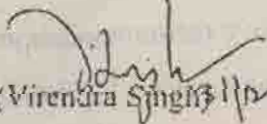
Member


(S.C. Khandelwal)

Member


(Balbir K. Punj)

Member


(Virendra Singh) 1/12/97

Member