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Book Review

#CityReflections
Singularities of Municipal Finance

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The devolution of 3Fs –funds, functions, and functionaries - was an essential bedrock of the 73rd and 74th Constitutional amendments of 1994. It envisioned empowering the third tier of Indian governance architecture sufficiently to enable streamlined local access to public services for citizens along with robust accountability for a responsive local government. Isher Ahluwalia's 2011 HPEC report on urbanization underscored the need to sharpen focus on not just financing but fostering financial self-sustainability among this third tier of urban governments enabling them to cater efficiently to meet the needs of an increasingly aspirational society. This sentiment was reinforced by another such report in 2019.

In 2015 the UN SDG 11 linked the growth of sustainable cities and communities as having a significant impact on related SDGs like water security and carbon reduction. Cities were to spearhead a 'vocal for local' movement as engines of growth. Forging outcome-based frameworks, policies, and programs to efficiently harness this latent potential of City assets and resources needed robust data-driven, reformist interventions that could even harness their singularities through sustained cooperative federalism.

In his book '# City Reflections Singularities of Municipal Finance" the author, Sameer Unhale, justifies the need for examining municipal singularities of Indian cities where over 400 million citizens reside in 4000 plus towns and cities. This city population is poised to grow by over 328m to reach 800 million by 2050 (an increase that exceeds the Indian rural population and the entire population of the USA). From financial year 2011 to FY 2018 urban investment in India has jumped from Rs 45,000 cr (0.7% of national GDP) to approximately Rs 1.2 lac crore (0.7% of national GDP). Development focus naturally shifts to sustaining cities for the pivotal role cast on them as crucial 'enablers of growth' to reach the envisioned $ 5 trillion Indian economy.

Unhale further argues that when over 70% of India's GDP and new jobs are expected to come from cities by 2030 they naturally become the locus of economic

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growth. The ripple multiplier effect of this urbanization wave is making city agglomeration hubs of supply chains, stimulating rural markets, evolving industrial paradigms to leverage emerging economies of scale from demographic densities where the median age of just 28 holds great promise, with remittances and circular migration reshaping livelihoods!

To reap this harvest sourcing and strengthening municipal finances is imperative. The World Bank forecasts that India should invest USD 840 billion over the next 15 years or an average of USD 55 billion per annum into urban infrastructure to effectively meet the needs of the 40% population that is projected to live in cities by 2036. Yet there is a serious mismatch of the financial and human capacity of cities vis-à-vis the growing responsibility cast on them.

To recap the growing focus on urbanization Unhale connects a kaleidoscope of dots that impact the backbone of municipal functioning and finance. The analysis span ranges from constitutional amendments, public finance performance indicators, accounting, financing options like municipal bonds and their challenges, the economic-municipal finance interface, poor alignment between Finance commissions and State Finance Commissions (SFCs), MC Audits, Credit Rating, reliable data collection using Big Data and AI tools, vagaries of adopting PPP modes to hive off tradeables, Independent regulatory commissions, recovering user charges, exploring foreign funding, quality infrastructure and Investment indicators, SDGs, aligning with the UN 'New Urban Agenda', SEZs, Smart city and urban mission finances, municipal viability, manpower issues, ethical dilemmas and lessons learnt in the wake of the Covid pandemic. This broad spectrum of municipal governance focuses squarely on municipal accounting and transforming budgets to align with the needs of an emerging and aspirational citizen-client while dwelling briefly on the threats posed by the political economy and issues of reservations that impact financial systems.

Unhale rises to the daunting task of examining the vortex of challenges and complexities within municipal finance in India and its singularities by scrutinizing earlier efforts to bridge the serious persisting data gap at the third tier of governance which defied a rational diagnostics of the complex municipal finance architecture. The wide canvas of the contents captures a gamut of themes drawing lessons from national and global municipalities. Broadly the urban reform roadmap can be classified into three inter-dependent perspectives –

1) quality of life,
2) cities as economic engines and
3) quality of democracy.

Delivering on these counts depends to a large extent on the financial sustainability and accountability of Urban Local Bodies (ULBs) that need smart, innovative leveraging of assets to supplement municipal finances for buttressing their vital contribution to local, state, and national GDP.

Despite the 74^{th} amendment to the Indian constitution, the book dwells on how systemic, strategic, structural, and procedural problems in municipal finances have defied any easy solutions. The 11^{th} and 12^{th} Finance Commissions took the lead by identifying three vital indices of Decentralisation, Deprivation (especially of drinking water and sanitation), and Devolution that impacted core municipal service funding. The 13^{th} FC went beyond these indices to earmark 33% of the municipal grants as performance grants to flow to the ULBs on fulfilling 9 fundamental municipal governance conditionalities to be self-certified by the States. Yet 38% of performance grants remained unutilized. This reform sought to lay a uniform bedrock of systemic, institutionalized, efficient, benchmarked, and streamlined institutions of municipal governance across the country that would foster investor confidence through an enabling municipal environment capable of handling multiple social, economic, and financial responsibilities. Yet only the Service Level Benchmarking (SLB) architecture for Urban Sanitation benchmarks and indicators was carried forward by the 14^{th} FC without prescribing how this evidence-based SLB template could be adapted for use in other vital sectors like urban transport by developing suitable benchmarks and indicators.

Against this need projection, Unhale juxtaposes the current inadequacy of municipal resources by referring to the 2022 RBI report on municipal finances in India which is a maiden effort to compile and analyze budgetary data of 201 municipal corporations for the three years ending 2019-20. Although the ULBs share in central taxes has steadily increased since 2010 from 1000 cr (1995-2000) to Rs 87144 cr in 2015-2020 (14^{th} FC) the increase is not proportionate to the urban population. As India inches towards the 500 million urban population landmark Indian municipal corporations' revenue receipts are only 0.6 – 0.7% of GDP. In this 'Own tax revenue' comprises only 31-34% of total revenue and non-tax revenue is 30% of total revenue receipts. Fees and user charges account for the highest share of non-tax revenue followed by income from investment, mainly in the form of interest earned and dividends, rental income from municipal properties, and sale and hire charges. Total expenditure has increased to 1.05% of GDP in 2019-20. Borrowing accounted for only 0.05% of GDP - all with huge inter-state variations.

Unhale dwells at length on the narrow scope of its tax generation unless innovative ideas like vacant land tax, share in land use conversion charges, betterment tax, professional tax, advertisement, and entertainment tax sources are plumbed. All FCs emphasized the need for a GIS-mapped Unit Area Value-based Property tax regime since this tax has become a prominent source now as other taxes such as octroi and local body tax stand subsumed in the GST imposed by the 101^{st} amendment to the Constitution. The GST council has yet to frame a compensation mechanism to bridge this loss to MCs for which there is a demand for sharing up to $1/6^{th}$ of central and state GST. This demand is justified as the responsibilities of the sub-sovereign Cities increase with the addition of concurrent list items to their tasks.

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Streamlining accounting practices and adopting accrual accounting could resolve many of the financial leakages in municipal budgets. Yet reportedly there has been poor adoption of the 2001 CAG task Force's 2004 'Report on accounting and budget formats for ULBs" based on which MoUD formulated the NMAM (National Municipal Accounting Manual) highlighting the need for adopting Accrual Double Entry Accounting System with supporting quarterly reporting on balance sheets, income and expenditure statements, cash flow, receipt and payment statement. Yet no CODE to enforce this reform has been prepared and accounts languish despite 13th FC efforts to enforce this regime. Hence the CAG report of 2015-16 captures only 9-14 States' adoption of this systemic reform. Only Tamil Nadu went all the way to even create software to ensure automated data flow to NMAM. Replicating TN success in all ULBs would resolve accounting delays, wrong entries, poor asset mapping for leveraging finances and loans, transparency, enhance ringfencing expenditure and incomes allocated to each function, baseline data support to SFCs and FCs in framing their periodic awards, etc.

Unhale distinguishes the latest practices that are sought to be mainstreamed into cities from traditional accounting when he highlights the need for using Fintech (needed for JAM- jandhan, aadhar, mudra schemes), Digi-wallets, PFMS (Public Financial Management System) that facilitates SNA (Single Nodal Account) ringfenced for each mission and separately for DBT (Direct Benefit Transfers). For logical budgeting and accounting, municipalities need to begin their budgets with an opening statement for assessing the net worth of the municipality and adopt the 7-digit accounting code in their COA (Charter of Accounts) to enforce the RFD type (Results Framework Document) structure. On the 15th FC recommendation, MoHUA initiated a City Finance Portal to create a National Urban Payment Platform that used simple digital accounting formats to overcome the reform inertia. Rather than engaging Chartered Accountants, it is imperative to build in-house accounting competency in Municipalities.

All the above imperatives need authentic data banks. Data and its analysis are the new oil for evidence-based policymaking. However, municipality finances suffer from a lack of authentic baseline data collection and availability protocols. Adopting formalized uniform accounting practices would strengthen traditional accounting while mainstreaming modern aspects.

Wide spectrum sector-specific training and capacity building of municipal staff is constantly needed to make municipalities "a spectrum of relevance" that is capable of tackling emerging challenges through infusing nuances of a dynamic accrual accounting system that is adaptive to new arenas. Broadly new financial competencies would encompass training in Big data management and analysis, using ICT tools; playing municipal bond markets; managing mission-based SPVs (Special Purpose Vehicles), and accessing and deploying financial support from VGF (Viability Gap Funding). New capacity-building arenas would require ensuring SDG compliance, unravelling complex pricing and taxing mechanisms in Voluntary Carbon Markets and Green accounting using environment pricing. Ringfencing City

GDP and unlocking the land value estimated at over 15000 cr by using land-use planning reforms like TDRs (transferable Development Rights) is a specialised emerging field to lend buoyancy to municipal funds. Exploring the utility of the World Bank's Local Area Economic Development (LED) is needed in Smart cities based on a SWOT (strengths, weaknesses, opportunities, and threats) analysis of CDPs (city Development plans) that incorporates business needs of multiple stakeholders in economic growth like the public, business entities, NGOs to name a few. Simultaneously the recent COVID experience poses Municipalities with the challenge of contingency planning and catering to impacts of the new regime of WFH or 'work-from-home'.

Change is the only constant today. This oxymoron translates into all the capacity-building areas listed above. This is a formidable challenge even for the Union and State governments. But keeping the growing urbanscape a focus shift to fast track the mainstreaming of such changes in municipalities will strengthen the bottom of the economic pyramid of India where change is being forced at an unprecedented rate. Catching this tide at its crest can surely be a game changer in the development pace of the country.

Cities being the principal catalysts for guiding urbanization through systemic decentralization have to forge innovatively towards fiscal empowerment. However, the reform roadmap outlined above will remain a Utopia unless major institutional and structural challenges are addressed that persist despite two decades having lapsed since the 74th Amendment. No mechanism has evolved to enable the Finance Commissions (FCs) to base their recommendations on the reports of the SFCs. Nor is there any continuity evident in the recommendations of the Finance Commissions due to significant variations in the approaches they employ for assessing the financial requirements of the ULBs or for determining the revenue-sharing arrangements and fixing the criteria for allocating the grants-in-aid to ULBs of different demographic, economic and social compositions.

In the absence of robust and reliable data base performance trends are not captured as Indian Municipalities are not bound by any prescribed benchmarks or indicators to derive standards for revenue-raising or service delivery. Hence they continue to operate at sub-optional levels without sufficient effort to eliminate inefficiencies that fester and prevent internal mobilization and management of own resources. Any motivation to improve is jettisoned due to the availability of easy financial bailouts from intergovernmental transfers. Hence economy-wide huge costs of inefficiencies continue to plague the municipalities and taxpayers.

This book is virtually a compendium on the peculiarities of municipal finances that make it a daunting but essential challenge for cities to perform in the face of grossly inadequate finances and service delivery capabilities. Yet there is no easy solution except to take this challenge head-on so that cities at the triple bottom line of the national economic pyramid diligently build *atmanirbharta* for the 'greater good of the greatest number' to unleash the collective economic future of the country that resides here. The large agenda of tackling the traditional backlog of reforms when coupled with huge new challenges is Herculean and needs prioritisation. By capturing the sheer size of this challenge Unhale has forayed bravely into the diagnostics of municipal finances in India that is the backbone of ULBs. However, encapsulating these issues within a hundred pages can at best be a beginning to trigger further area-wise research by others. Perhaps the small size of the book militated against better segregation of municipalities into categories by size, area, and population that impact their finances directly, and often the Union grants have been accused of using a "one size fits all" policy prescription ignoring the feedback on how this formula skews releases and is inequitable.

Structurally this book could have benefitted from certain formatting changes – like the use of sub-headings for easy referencing. The data from municipalities is useful to supplement invaluable arguments forwarded but the narrative loses its impact when interrupted by examples that could have been segregated and confined to boxes for an easy read. Moreover the title talks of City reflections but it does not specify if the focus is municipalities of India or Maharashtra (as most examples cited are from that State). Mountain municipalities have totally distinct singularities of cost-benefit and user charges that need inclusion in this analysis. Further, the 2 chapters at the beginning and end that make a quick comparison of municipalities in India and abroad could perhaps have been clubbed at the beginning to give a telescopic overview and set the agenda for emphasising the criticality of municipal reform languishing at the third tier of governance in India. Chapter sub-headings too could have been used to the advantage of the impact on the reader.

A section on abbreviations would have facilitated easy referencing, especially in an era of multiple schemes and missions that generously use these acronyms, etc. At the end a section on references could have listed numerous previous studies on this subject that may have been used by the author but left unbridged gaps would have become a useful survey of literature to facilitate further research by those who want to explore any single aspect of these issues in-depth.

Yet this comprehensive compilation is a must-read being the first of its kind. It definitely acknowledges the need for cleaning the financial maypole of the Municipal Augean stables so that we can begin to see a path through these woods that are dark and deep, yet municipalities have miles to go before they sleep! This book is sure to catalyze more meaningful debate on this ever-growing area of concern in our urban economic landscape.