CHAPTER III

FINANCIAL MANAGEMENT IN URBAN LOCAL BODIES
Finance is the fuel of municipal administration. Finance moves the machinery of any institution including local Government. Sound financial administration is the crux of the efficient administration of local Government operations. Kautilya in his Arthasastra states that the entire administration of the country can be controlled through financial administration and that is why the administrations in a country must give utmost priority to financial administration. This very analogy is perfectly truer in the context of local bodies. The Economic Survey, 1991-92, has rightly stated:

"The financial sector is the centre of economic activity, its health affects the entire economy. Municipal governments are directly linked with the availability and utilization financial resources."

Financial administration is the art and science of planning, organizing, implementing and evaluating the financial resources to ensure their best use for the achievement of the objectives, goals and targets of municipal programmes, Emphasizing the importance of finance, Thavraj says:

"Finance is the life blood of all monetized socio-economic formations ranging from simple nuclear families to complex national and international organizations. Financial administration relates to the system, which generates, regulates and distributes the monetary resources needed for the system, which generates, regulates and distributes the monetary resources needed for the sustenance and growth of organization. In this respect financial administration is similar to the circulatory system in complex living organisms."
Municipal Financial Administration; can be defined as the art and science of policymaking, planning, decision-making, coordination, control of the processes of securing adequate resources, ensuring their safe custody, genuine allocations among different areas of development activities, effective utilization and avoiding the pilferages and leakage of resources and duplication of efforts to ensure best services to the people living in the area of the local Government. In short, we can say that municipal financial administration is the technique of maximizing financial output, the optimization of financial resources and their judicious utilization.

Finance thus constitutes the lubricant for the wheels of the local government. Without it, the governmental machinery at local level will come to a standstill and the local democracy will become meaningless.

The Reserve Bank of India in its bulletin has rightly stressed the importance of the Local Government finances as follows:

"With the increasing industrialization and urbanization under the impetus of development and planning, the local authorities form a growing part of the expanding public sector, with powers to raise and spend considerable amounts of public funds for development purposes. Local authorities form an important segment of public sector in India. The contribution of the local bodies to income in general and capital formation is of considerable significance, in view of their large number and the area and population they cover."
The robustness of urban local bodies would be reflected in the state of their finances and in their capacity to look after their own needs. The basic requirement of financial sustainability must be intertwined with the need for financial powers. Unfortunately, even as the urban population is growing at a rate faster than the national rate, urban bodies have become increasingly dependent on the Union and the States for financial resources.5

Functional clarity and strengthening of local government finance and management should occupy centre-stage of the follow-up action on conformity legislations. Most municipal authorities today suffer from a wide gap between their perceived needs for services and the financial resources provided to them. This fiscal gap is due to four reasons: (a) unrealistically high standards of services, such as water supply and sanitation, transport, health, and education, which are beyond the financing capacity of urban residents; (b) misallocation of functions and revenues to urban governments; (c) inadequate exploitation of existing tax resources due to inefficiency of ill-motivated municipal functionaries; (d) inefficient mechanisms to produce and deliver public services. The ways to the rational allocation of responsibilities and finances between levels of government, incentive-penalty structures to enhance local efforts to raise revenues and improve the responsiveness of service providers, minimization of waste, adoption of efficient and cost-effective practices and promotion of policies that enhance local initiative. Municipal reforms need to address these issues systematically.6
**Financial Management**

The funds of the local government councils are managed by the key officers of respective councils. Financial management has to do with efficient use of funds. It is a method of showing and ascertaining the financial position of government or business from time to time.\(^7\)

Financial Management can be envisaged as consisting of a cycle of activities as shown in Figure 1 below. The aim of this cycle of activities is to ensure that resources are allocated and monitored in such a way that they have the greatest beneficial impact on over all service objective.\(^8\)

**The Financial Management Cycle**

In order to perform finance functions efficiently, the financial managers of the local government have to:

1. Set the financial objectives of the local government.
2. Prepare plans of action and select policies for achieving the objective.
3. Develop financial plans and incorporate these into the overall plans of the local government.
4. Check the achievement of the objectives and evaluate deviations from the plan.
5. Establish causes for deviations.
6. Take corrective action and/or redesign policy or revise the objective to start a new cycle as illustrated in figure 1 above.

Techniques and Tools for Achieving Efficient Management of Local Government Finance:

Traditionally, considerable importance is attached to what can be the money factor in the functioning of organizations in both public and private sectors.\(^9\) One important issue of concern is usually the management of available financial resources. Generally speaking, a number of various approaches for efficient finance management are available. However, the approach to be adapted must take into account the peculiar nature of the project, its environment, purpose and the public it is meant to serve.\(^10\) This is because if a "wrong" or "unpopular" approach is adapted for a particular project, it can mar the project completely.
The different approaches that can be adapted for efficient financial management at the local government level include the following:

1. The use of Budget

The use of budget has been a long standing practice in the local government system. Budgetary control is concerned with ensuring that the financial management plan that has been agreed with the board of management is achieved. Control is affected through monitoring expenditure before and after commitment to prevent under expenditure or over expenditure. An effective use of the budget is good for achieving efficient financial management. A budget is a plan of activity expressed in financial terms; such plans are often short term, typically covering a period of one year. When approved, the budget becomes an authority to raise the amount of revenue and incur the amount of expenditure stated therein.

It is imperative to note that the budgetary process takes four distinct activities. These are as follows: budget preparation, budget authorization, budget execution and budget monitoring and evaluation. In many governmental arrangements, the agencies or bodies responsible for each of these activities are distinct, with varying degrees of autonomy and interdependence.11

At the local government level, the council chairman is ultimately responsible for budget preparation with inputs from the supervisory
councilors and local bodies or agencies. It is then approved by the local legislature. In addition, the State Governor's office gives the prepared budget final approval after thorough scrutiny.

However, getting final approval is often times worrisome as it is characterized by too much scrutiny and delayed sanctions by state government functionaries. On approval, the budget is returned to the local government council through the department of local government. The approved budget then gives authority to the council to raise revenue and incur expenditure in the financial year.

2. Rational Approach

The rational approach is a popular decision making model. It is usually applied where effective and efficient allocation of resources is needed. The rational approach is generally known as "The Modern Financial Resources Allocation and Control Model" within the financial management circle. Using rational approach for proper financial management entails the following:

Determinaton of available resources

- Determination of objectives for which the resources will be allocated;
- Determination of the alternative courses of action for the achievement of objectives;
- Evaluation of the alternative courses of action for the achievement of objective (s);
3. Incremental Approach

Many organizations adopt an incremental budgeting method to produce budget estimates. Incremental approach to financial management involves introduction of gradual changes or adjustment in the allocation and control of financial resources of an organization in order to achieve the desired objectives. Once a system of financial management and control are adopted, only minor or gradual changes or adjustments are required in order to put the system into perfect working condition.\textsuperscript{13}

Incremental approach takes as its starting point the current year's budget and arrives at next year's budget by a series of adjustments to this. The adjustment process is sometimes referred to as rolling forward an existing budget.

Incremental method has some advantages. It is a relatively straightforward process; only marginal changes to the existing budget need to be understood and agreed, thereby minimizing the amount of time that need be spent on budget preparation. Hence, it is a relatively
inexpensive method of estimating a budget. Additionally, it is easy to operate and allows some degree of flexibility and discretion in the use and management of funds.

4. Zero-Based Budgeting (ZBB)

The Zero-Based Budgeting (ZBB) approach involves preparing a comprehensive budget anew, that is from a zero base. The novelty of ZBB is that each year an organization should begin its budgetary process with a clean sheet of paper. In other words, ZBB prepares something 'fresh'. It starts from zero or from the scratch. The construction of a new budget for each service from basic principles is referred to as zero-based budgeting. This approach has the effect of focusing attention on such issues as waste, unnecessary performance, leasing versus purchasing of equipment, and so on.

In zero based budgeting individual cost centre managers are asked to estimate the cost of providing various levels of services, which are then passed up through the organizational hierarchy. At each level in the hierarchy, managers are asked to decide upon the order of the decision packages as a way of ensuring that spending is linked to priorities.14

One of the major strengths of ZBB is that there is a specific link between budget and activity. The budget process involves specifying objectives and considering cost-effective methods of achieving these
objectives. In this way, ZBB eliminates waste, extravagancy, mismanagement of finances of a local government.

The major drawback of ZBB as a finance management tool is that it is time demanding. In other words, it takes lot of time to construct a budget from zero each year.

5. Planning – Programming and Budgeting System (PPBS)

As the name implies, the three main features of PPBS are planning, programming and budgeting; the emphasis here is upon a programmatic approach to both planning and budgeting. PPBS is an approach to budgeting which is intended to provide a system that relates expenditure at each stage of the budget to the purposes of that expenditure.

The application of PPBS as a finance management tool allows for weighting the alternatives, analyzing of cost and benefits of any project or programme before the commitment of financial resources to the project. A further advantage is that programme budgeting looks beyond the immediate future and is concerned with the long-term effects of activities.

PPBS has a number of drawbacks. Technically speaking, PPBS requires information on costs and benefits that is not readily available, and it is also a time-consuming budgetary method.
6. Audit Alarm

Audit alarm is a precautionary method of alerting the appropriate authority or the public about illegal financial transactions or misappropriations that may lead to loss of funds or revenue meant for a project. Audit alarm can be raised by a member of the executive or the general public. This is usually done at any time irregularity is noticed in the management of funds meant for public use. Whenever audit alarm is raised it usually attracts full-scale audit-exercise to ascertain the magnitude of the fraud or irregularity. This method serves as a precautionary warning to those entrusted with the responsibility of the finances.

7. Auditing Approach

The regular audit method complements the good effort of audit alarm. Audit is more or less a practice which may be called a technique for ensuring a more effective internal check on financial management. There should be regular and independent examination of the books of accounts by appointment qualified auditors to ensure that the statement of account as recorded represents a true and fair-view of all the transactions as during the period under investigation.

Regular auditing of account would ensure sanity, prudence and probity in the use and management of finances.
Indian Urban Local Bodies have the status of third tier local government. Constitutionally built-in imbalances in the functions and finances have made the urban local bodies dependent on grants from upper tiers of government. In addition there are urban local bodies that have insufficient financial resources due to their failure to adequately exploit existing sources of revenues. In such a situation, there is need for urban local bodies to exercise prudent financial control practices in order to match mandated functions with available finances and so to ensure financial sustainability.

Management and Finance Practice:

The comparative advantage of local government undoubtedly resides in its superior knowledge of local conditions and the needs of local communities. Local Government can make an important contribution to public well being through the execution of government policies and the delivery of local public services. Local government also has the potential to be the most transparent and accountable level of government. Full realization of that promise, however, requires strong fiscal administration to ensure that citizen interests are reflected in local programs; policies are conducted in fiscally sustainable way; and resources are not lost through inefficient, ineffective, wasteful, or corrupt operations.15
Inefficiency in Financial Practices

There may be inefficiency among urban local governments in the management of their finances, which could adversely affect the efficient delivery of basic civic services. This may include: deficiencies in the procedure for determining the cost of services; low levels of revenue collection; high areas from previous years and high dependence on external sources of finance.\(^\text{16}\)

Many urban local bodies are unable to meet the basic service requirements of their populations. Elected representatives and officials of urban local bodies regularly stress the need for the timely provision of funds from upper tiers of government, but they may not be able to maintain basic civic services nor initiate appropriate action for raising local revenues, Prudent financial control practices should match available resources to the function of urban local bodies.

Prudent Financial Control Practices

All resources need proper planning and control in their utilization to satisfy the public interest.\(^\text{17}\) Financial management initiatives include effective controls over receipts, expenditures, funds, property and other government assets. Legislature should not only appropriate money, but they should also ensure that funds are spent according to their intent, in an economic and efficient manner and produce the intended results. Proper public expenditure management at any level of government should :\(^\text{18}\)
a) adequately control the total level of revenue and expenditure,
b) appropriately allocate public resources between sectors and programs, and
c) ensure that governmental institutions operate as efficiently as possible 19

Prudent financial control practice should also aim to ensure financial sustainability of urban local bodies. The generation of recurrent surplus is thus one of the key indicators of financial sustainability.

Elected representatives are power seekers and their major decisions are oriented at gaining votes. Therefore they may not take adequate measures to collect sufficient own sources. They may also make unnecessary or irregular expenditure. Public officials should constrain such action by the elected representatives, but they may prefer to keep quiet in order to avoid conflicts with the elected representatives especially if they are popular. Political power supersedes administrative power.

As a result, prudent financial practices are not necessarily adopted by urban local bodies. There are some large urban local bodies which are better governed, but the financial condition of small and medium-sized towns are often poor.
Diagram 1: Prudent Financial Controls
Control 1: This control covers tied grants received from upper tiers of governments. The grant should only be expended in accordance with authorizations of management and the direction of the issuer. However, an urban local body should also exercise financial control (1) to ensure that the amount of any tied grant is either equal to or more than the relevant earmarked expenditures.

Control 2: Appropriate resources are needed at the urban local body level to ensure the provision of basic services. An urban local body should try to meet the administrative, operation and maintenance costs (all expenses other than those covered by tied grants) out of its own source revenue collection. This is the aim of control 2.

Control 3: The result of the above two controls is either a recurrent surplus or a deficit. Any surplus is available for capital expenditure and so will complement capital receipts. Capital receipts, in the form of grants or loan, should be expended in line with the requirements of the issues. Therefore control is directed towards ensuring his balance between capital expenditure and capital receipts.

Generally we conclude that financial performance improve if urban local bodies exercise the defined control measures. Prudent financial control practices are helpful to small and medium-sized urban local bodies and especially to urban local bodies of developing countries.
With rapid urbanisation and the pressure on urban areas for service delivery, the role of urban local governments is undoubtedly becoming important and, here, their financial capacity can hold the key. At the same time, there are several issues in urban governance that need to be addressed yet. Delegation of decision making powers to urban local bodies (ULBs), which are traditionally considered as a part of the system of State government and acting on behalf of it, is one of them. The constitutional mechanisms like inter-governmental fiscal transfers were an attempt to reduce the fiscal gap of ULBs, but they were not effective in translation / implementation at ground.

India has been experiencing a rapid growth of urban areas and an increasing level as well as pace of urbanization in the last few decades. This led to the world looking at Asia and its two main pillars India and China with rather greater attention. The urban population has been growing at a rate of 30-40% per decade since after 1961, which is well above the rural population growth rate of 20%. The level of urban population has also been increasing from a fairly stable level of 10% of total population at the beginning of the 20th Century to a current level of around 30%. With increasing levels of population and its growth, the demand for urban civic infrastructure services also rises, which is expected to be catered through adequate supply of it. Yet the performance of urban local governments are far from satisfactory – the production of these service is insufficient and inefficient, the service quality is very poor and the municipal
organizations are not geared to delivering them in a professional manner.

1.1. Financial equilibrium trap

Increasing level and pace of urbanization calls for the gearing up of municipal service delivery on one hand, and the emergence of growth opportunities would require efficient supply of civic infrastructure – water supply, drainage, solid waste management, roads and street lights – on the other. As pointed out in Government of India (1996) (Rakeshmohan committee) infrastructural investment requirements are very large in a rapidly growing country like India. Besides the delivery efficiency, the supply of civic infrastructure is dependent, to a good extent, on the amount of financial resources available for undertaking various development projects of civic
infrastructure services. Here, municipal finances hold an important key to the production and delivery of these civic infrastructure services.

Municipal finances hold the key to the overall status and progress of service delivery in right direction. Poor finances of municipality results in > poor basic services, low capital investment, low credibility, poor revenue collection efficiency, corruption and the lack of innovation in resource mobilization. This vicious cycle (as shown in the figure) leads to poor delivery and low quality of services, which will hamper the growth potential of the MC. Here, understanding the structure / pattern of finances of MCs and its growth hold greater promise in the move towards improving the municipal revenue.

It is well evident from literature that there is a significant pressure on the amenities and services in cities and yet the city finances are woefully inadequate in terms of meeting the pressure. The quantum of financial resources available to several municipal corporations is less than what is required for the legislations. The result is the lack of incompatibility between the investment requirements of civic infrastructure for economic growth and that of the pool of resources available for expenditure on various municipal services. The existing literature suggests that the causes for this state of affairs could be traced to both the inadequacy of available resources
on one hand and gross inefficiency in the spending by urban local bodies on the other.  

In this context, it is useful to take a stock of the finances of urban local governments and analyse their performance on the set measures to get hold of where they are heading and how well do they measure. For example, dependence on one type of revenue source and stagnant revenue do not go well with any MC. At the same time, the lack of adequate resources, which affects the municipal performance, can be on account of several reasons – poor tax base and levy, incomplete exploitation of user charges and low amount of transfers from upper tiers of government. Incomplete decentralization both in finances and functions can also result in imbalance of resources vis-à-vis functions. Inefficient spending could also occur on account of resource crunch, organization structure and systemic problems, over-staffing and inadequacy of appropriate manpower. The resource gap would make the municipal bodies resort to borrowings, which needs to be backed up by user charges.

Municipal corporations, as institutions of local government, are constituents of the third tier that play an important role in local economic development; they have a sizeable proportion of overall public financial resources but are nevertheless subject to the scrutiny in terms of physical and financial performance. Normally, an analysis of municipal finance begins with taking stock of their revenue and expenditure in terms of the composition, trends and balance.
**Availability of Civic Amenities**

Urban local bodies are expected to render a minimum level of services to the citizens in order to ensure providing a minimum standard of living to the citizens. The performance of urban local bodies on this aspect is gauged by comparing their levels of revenue expenditure on water supply, roads, sewerage and street lighting against that of the norms established by Zakaria Committee set up as early as in 1960-61.

After ascertaining the lack of required civic amenities, the per capita revenue and expenditure are compared with growth in total receipts and expenditures to see whether there are any inherent constraints to the provisions of services before the urban local bodies. This needs to be further extended by identifying the constraints to the local bodies in meeting the norms of service provision in the revenue sources – tax, non-tax and transfers.24

**Revenue Performance**

The ability of a municipality to generate revenue depends upon an array of factors: (i) the level of economic activity in the region; (ii) fiscal powers delegated to local government; (iii) tax efforts of municipal government itself; and (iv) transfers out of sharable poor of revenue by the state government to local government. The revenue performance of the municipality / municipal corporation can be gauged by computing following two groups of indicators:
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<th><strong>Group I</strong></th>
<th><strong>Group II</strong></th>
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<tr>
<td>Growth of per capital total tax revenue</td>
<td>Shared tax / Gross tax revenue <em>(Decentralization Ratio)</em></td>
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<tr>
<td>Growth of total revenue receipts</td>
<td>Grants / Total expenditure <em>(Dependency Ratio)</em></td>
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<tr>
<td>Composition of tax and non-tax revenue of top performers</td>
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The rise/fall in the first group of indicators would indicate either rise/fall in fiscal powers delegated to local government or the improvement/deterioration in the tax effort or administration of local government. Movement in second group of ratios would on the other hand, would reveal the trend in level of dependency and decentralization.

**Expenditure Performance**

The level of expenditure is, to some extent, reflective of the level of services rendered by an urban local body. While the trend in per capita expenditure would provide first approximation of the level of services rendered by a municipal government, a further segregation into discretionary and non-discretionary components, relative share of revenue and capital expenditure, share of establishment /administrative/Wages-salaries as a proportion of total / revenue expenditure would reveal the quality of expenditure and ability of the local bodies to meet its state objectives.

**Availability of Civic Amenities**

Urban local bodies are expected to provide certain minimum levels of services to the citizens. However, the availability of civic
amenities in an MC is directly influenced by: (a) expenditure on services (b) per capital income and expenditure (c) growth of income and expenditure. We attempt to gaze the performance of ULBs in this section.

**Expenditure on Services**

The adequacy of services provided by the municipal corporations is assessed through comparing the expenditure incurred on major/core services, namely, water supply, sewerage, solid waste management, roads, street lighting, public health and sanitation with Zakaria Committee norms. Although, Zakaria Committee was established as early as in 1960-61, the norms were revised to 1997-98 and projected to 2000-01. This comparison has also been extended to include all other major services ie., education and recreation (play grounds), in addition to the core services, that form the expenditure on all services.

In India only a few MCs like Mumbai, Nashik and Asansol have met both the expenditure norms of public works. Among other cities, Surat, Bangalore, Nagpur, and Jaipur could only meet the expenditure norms on core works, whereas several others failed to meet the same.25

**Per capital income and expenditure**

The per capita income and expenditure of an urban local body (ULB) are important parameters that determine the availability of civic
services and, thereby, the municipal performance, therefore it is interesting to observe the relative performance of ULBs within the group on these parameters.

Good level of per capita income is essential for the provision of core (basic) services by an MC as laid down by the Zakaria committee norms. In the absence of strong income from internal sources, the poorly performing ULBs have to augment their revenue by improving the levy and collection of taxes and utilize new taxes to strengthen the same, some of which we discuss in the next chapter. At the same time it is also necessary to ensure that the per capita expenditure also high but should also ensure that most of the spending goes into productive capital assets, which we also discuss in the section on expenditure performance.

**Revenue Performance**

The revenue performance of a municipal corporation can be observed in terms of: (a) growth of tax revenue (b) growth of total (tax as well as non-tax) revenue, (c) composition of tax and non-tax of top performers among the municipal corporations, (d) shared revenue to total revenue (decentralization) and (e) transfers from state government to total revenue receipts (dependency). In the following sections, we provide how each of the municipal corporations has fared on each of the above parameters in the group.
**Growth of Tax Revenue**

Good growth of tax revenue is an important indicator which reflects the strength of a municipal corporation to undertake service provisioning responsibilities.

Since some of the MCs in India have shown a low tax revenue growth in the past and some of them have shown even decline, it is imperative that the MCs take a comprehensive evaluation of their tax avenues / sources, levy methods and collection efficiency. The MCs have to strive to perform well on all these counts in order to provide a sustained financial performance and improved service delivery.

**Growth of Revenue Receipts**

The growth of total revenue receipts is an indication of healthy state of the finances of a ULB. Most of the ULBs have, however, shown in the past below average growth of revenue receipts. The reasons for the poor revenue receipts of certain MCs need to be explored further. While higher dependence on grants is not recommended, a declining share of grants to the MCs, if found to be the case, warrants reconciliation of grant system (particularly, revenue grants) in tune with the rising gaps in local finances (due to rise of population, economic growth and responsibilities). However, the MCs have to augment their revenues by resorting to all means such as: i) improving the tax revenue, particularly property tax, through better levy methods and collection procedures, ii) enhancing the tax base through
proper assessment, iii) revising tax rates in tune with rise of property value / local economic development and financial requirements of civic bodies. This essentially means that the MCs need to be on reform and innovation path for sustained performance.

**Composition of Tax and Non-tax Revenue**

Achieving a good proportion of own revenue to total revenue receipts is one way of establishing credit worthiness, and a greater share of tax revenue in its is desirable as it is a reliable revenue source. A proportion of more than 50 per cent is considered to be good and that more than 70 per cent is considered to be favourable from the view point of creditworthiness.²⁶

Though there are no provisions, a normative proportion of tax and non-tax revenue at 40-30 and 30-20% of total revenue could be considered as attainable by the municipal corporations. The ULBs shall strive to improve their tax share, particularly that of property tax, by improving revenue mobilization.

**Decentralization**

Apart from the measures of revenue growth and composition, the revenue performance of ULBs can be gauged through decentralization and dependency. Decentralization measure is defined as the proportion of shared tax in the tax revenue, which underscores the importance of share revenue as opposed to own revenue. High decentralization makes the states to rely of the state governments to...
some extent in sharing the revenues, particularly in the absence of well established sharing formulas and strict adherence made to them by the State governments. Therefore, complete devolution of tax resources should be done by corresponding States in order to make the MCs more independent, as emphasized in the 74th constitutional amendment.

Expenditure performance of the MCs can be analyzed from the broad indicators of: (a) level of revenue expenditure, (b) share of expenditure components – capital, maintenance and establishment, (c) the quality of expenditure (share of spending on discretionary vis-à-vis non-discretionary services), and (d) the extent of cost recovery.

**Revenue Expenditure**

The level and structure of expenditure has some major implications to the finances of the MCs. The revenue expenditure, comprising expenditures on establishment (staff salaries and administration) and maintenance, assumes importance, as it relates to the provision of civic services and their maintenance. However, very high proportion of revenue expenditure in total expenditure can be detrimental to the expansion of capital assets and generation of future revenue streams.

**Relative shares of Expenditures**

The expenditure structure of municipal corporations also throws some lights on the relative importance assigned to each
component in the total expenditure and it has a bearing on the financial position and service delivery. While a low proportion of spending on establishment is desirable, too low proportion may hamper its service delivery; likewise, expenditure on capital works is important as it provides future sources of revenue, but very high expenditure on it would have a bearing on the finances and even necessitate external support in the form of either grants or borrowings. Some of the MCs have an unsustainably high proportion of (more than 50 per cent) total expenditure on establishment, which affects the finances and service delivery capacity. Likewise, some of MCs have an abysmally low capital expenditure (less than 10 per cent to almost zero), which is equally detrimental to the health of civic finances and its long term sustainability. It is therefore necessary to develop certain guidelines / norms for the MCs towards spending on capital and its maintenance and reforming the staffing pattern.

**Quality of Expenditure:**

The MCs have been assigned some of the essential functions as defined under the respective municipal legislation. Here, it was laid down that they shall give primary attention to providing essential services like water supply, sewerage, street lights, solid waste management and public (primary) health. A disproportionately high spending on non-discretionary items like education, parks and roads is not highly desirable unless the MC has already attained satisfactory levels of services on discretionary items. The composition of
expenditure on works in all MCs in India clearly indicates that the expenditure incurred on important municipal functions (or, discretionary items) like provision of water supply, drainage, sewerage and soil waste management has been comparatively less than the expenditure incurred on non-essential functions (or, non-discretionary items) like provision of parks, roads and education. This implies the need to rationalize the discretionary spending by the MCs through some kind guidelines, or to improve public accountability of expenditure through citizen characters and social audits.27

Recovery of Cost

Cost recovery of services is an important integral measure of the municipal finances and it is liked to the self-sustainability of the MCs. It can be broadly measured as a ratio of municipal fees & user charges to revenue expenditure incurred for the provision of respective services viz., water supply, health services, education and electricity.

Cost recovery has to be an integral part of the service provision, especially when the service costs can be measured and beneficiaries can be identified, such as in the case of water supply, roads, education and health care facilities. The other alternatives of public-private partnerships could be explored for overcoming some of the costs, which requires a particular mention. Public private partnerships ensure that the operating costs of services are recovered and users pay for utilizing these services.
**An Overview:**

Finance is very important in the running of organizations or governments. Local governments have a number of functions to carry out. As such, its finances need to be efficiently managed and judiciously utilized.

Financial management is about efficiency in financial matters. It is about effective use of available financial resources. It is about financial alertness. Efficient financial management is necessary for the successful execution of projects and delivery of quality services at the local level.

Efficiency in financial management in any organization is always achieved through organizational determination to pursue excellent performance. It entails self-discipline on the part of top, middle, and low level managers in the organization. In this article, we have tried to define what is meant by local government. We also discussed the role of local government and threw more light on the meaning of financial management. Thereafter we discussed the various financial management methods, tools, and techniques such as: the use of the budget, rational approach, incremental approach, zero-based budgeting amongst others.

However, the efforts, of local governments' executive to attain some financial autonomy in running their councils are being disturbed by the intervention of state governments in local functions.
It follows that as much as possible, the federal government should reduce or eliminate areas of conflict between local and state governments.

An insight into the municipal finances in India reveals that most of the ULBs are generating small revenue surplus with low resource gaps. More than that, they are spending lower than that required for providing a minimum level of civic amenities. This apparent contradiction is on account of some of the design issues of inter-governmental system under which the ULBs are not independent in functioning and decision making e.g. control over staff, raising of revenue and expenditure, and accessing debt, which points to the decentralization yet to come in true sense. There are also regional disparities in financial performance. The design of inter-governmental transfers may attempt to address it partly. But, there is scope for improving own performance by improving tax collection and raising user charges in the ULBs, which also paves the way for public-private partnerships and accessing of market funds for financing their project.
REFERENCE


22. *Ibid.*, p. 120


