

Urban Local Bodies to Smart cities- The Next Level

The government’s ambitious vision of setting up smart cities across the country soon appears to become a reality. In an effort to strengthen and revitalize urban local bodies (ULBs), the urban development ministry is fast processing the list of 100 smart cities across the country which would be set up by 2022. However, for the development of smart cities’ finances remain to be the critical factor. Apart from identifying the quantum of finances required in order to implement the idea, it is also very critical to identify the financial resources which would remain to be the key to steer this massive agenda. Besides, it is also imperative to have smart leadership not only at the state level but also municipal level to implement the designated plans.

In an attempt to provide the necessary financial support to the smart city projects, the Union Cabinet has planned a total capital outlay of Rs 48,000 crore towards smart cities projects over the next five years. Under the mission, each city would get central assistance of Rs.100 crore per year for five years. In addition to this, the centre has also approved Rs.50,000 crore for the Atal Mission for Rejuvenation and Urban Transformation (AMRUT) (previously called JNNURM). The AMRUT project will cover 500 cities and towns. These plans would be implemented through Special Purpose Vehicles (SPVs) to be created for each city with state governments ensuring steady stream of resources. Out of the corpus of 14th finance commission, some grants would be also allocated to ULBs in order to enhance their financial condition.

In the light of the above, it is essential to take a look at the present finances and the structure of these finances of the ULBs. This report thus gives a detailed insight into the financial pattern of 16 selected ULBs.

Financial Patterns of ULBs: Select Sample

A study of 16 ULBs for FY13 shows that there was an increase of 16.1% in total ordinary income over FY12. This came about due to an increase of 6% in tax income and 32.5% in non-tax income. The 16 ULBs included cover 8 states and is based on data presented by the Ministry of Statistics and Programme Implementation.

Table 1: Income profile of 16 ULBs (Rs crore)

	FY12	FY13	Growth (%)
Tax Revenue	12,996	13,772	6.0
Non-Tax Revenue	8,339	11,050	32.5
Grants	1,352	1,393	3.1
Total ordinary income	22,570	26,215	16.1

Source: MOSPI

Significantly the dependence on tax income is highest for the sample ULBs though over this period, there was a decline in share of tax revenue in total ordinary income from 57% to 53%. The share of non-tax revenue increased from 37% to 42% while that of grants came down marginally from 6% to 5%.

Two major components of tax revenue for ULBs have been property tax and octroi duty. However, there has been no clear pattern for the group as a whole. The share of property tax was a little over 1/3, with the proportion increasing from 34% in FY12 to 35% in FY13.

Table 2: Share of property tax in tax revenue for 13 ULBs(%)

City	FY12	FY13	City	FY12	FY13
Delhi	92	89	Bhopal	90	84
Baroda	51	51	Jabalpur	16	15
Rajkot	90	85	Jodhpur*	2	3
Brihan Mumbai	36	33	Dehradun	63	60
Kolhapur	14	22	Agra	46	54
Pimpri-Chinchwad*	8	10	Lucknow	97	94

*: *Appears to be too low as per government data*

As can be seen from the table the variation in dependence on property tax is high and ranges from 15% for Jabalpur (excluding Jodhpur and Pimpri- Chinchwad) to above 85% for cities like Delhi, Rajkot, Bhopal and Lucknow. The pace of growth in tax revenue here would depend directly on the rate of urbanization and the creation of residential and business spaces. In fact, with rapid shifts taking place to these growing cities there would be a tendency for higher growth coming from this source, notwithstanding the tax rates imposed by the ULBs.

The 14th Finance Commission has pointed out that there is considerable scope for the local bodies to improve revenues from own sources especially property tax which is recognized as the major source of revenue for local bodies the world over. However, local bodies in a few States have not been given the powers to levy this tax so far and legislations for this purpose have either not been passed or still remain under consideration of those State Governments. In most States where tax is being levied, the rates have not been revised periodically. The list of taxable properties is not being updated and a large number of properties remain outside the tax net. Further, some ULBs do not have a systemic approach to listing of vacant lands. Therefore, such lands often go untaxed and the vacant land tax is demanded only when owners approach authorities for approval of building plans.

The Commission has also urged States to empower local bodies to impose this tax and improve own revenues from advertisement tax which include hoardings. Also on the non-tax revenue front there is need to review and periodically update the charges and fees for all the services being provided by the local bodies.

Octroi is another important source of tax revenue for ULBs and this has been important in Maharashtra and to an extent in Rajasthan and MP as the table below shows.

Table 3: Share of Octroi collections in tax revenue (%)

	FY12	FY13
Brihan Mumbai	64	67
Kolhapur	51	54
Thane	72	73
Pimpri Chinchwad	87	84
Jabalpur	43	34
Jodhpur	67	59

The issue of octroi becomes relevant for those ULBs when there is a GST imposed that subsumes this component as there would need to be progressively larger compensations until such time that revenue flows are equalized.

The expenditure of these ULBs has been captured under three headings: ordinary expenditure, repayment of loans and payments as salaries and wages. This excludes any capital projects undertaken by the authorities and is largely confined to the revenue expenditure.

Table 4: Structure of expenditure of ULBs (Rs crore)

	Number of reporting ULBs	FY12	FY13	Growth (%)
Ordinary expenditure	16	12,174	14,794	21.5
Repayment of loans	9	368	189	-18.8
Salaries and wages	15	7,581	9,852	30.0
Total *		20,123	24,835	23.4

*: Has been summed over those which have reported numbers. It is not revealed if the zero non-loan repayment is due to there being no loans or absence of information.

Within the set of 16 ULBs, 10 have provided information on the allocation of the ordinary expenses across different headings. Here again, the classifications have been fairly uniform as general administration and tax collections along with road wash and water supply have almost similar shares in the total expense at around 7%.

Table 5: Components of Ordinary expenses (10 ULBs)

(Share in total)	FY12	FY13
General administration and tax collection	7.3	6.0
Public health	4.7	4.3
Safety and convenience	1.3	0.4
Road wash	6.1	4.7
Water supply	6.7	7.3
Education	2.7	2.6
Miscellaneous	57.1	62.3

The government has been talking of creating smart cities and while this effort will be on, the ULBs have to gear themselves to meeting the challenges of enhancing the quantity and quality of urban infrastructure. Therefore

road maintenance, health, education, water supply etc. would become progressively more critical for urban development and they will be required to invest also in these structures.

An important component of the expenditure of the ULBs has been the staff costs. The ability to spend beyond these costs is limited by the income which is earned through different forms. As most ULBs do manage with the funds that they earn, their ability to invest in capital projects has been restricted to the extent that grants have been provided like the JNNURM fund. The larger ones have been borrowing from banks and FIs while others have accessed the bond market. The Finance Commission did point out that only 10 States reported borrowings by urban local bodies and of the Rs. 920 crore borrowed by them in 2012-13, Rs. 854 crore was borrowed by municipal corporations. Of these, municipal corporations in Madhya Pradesh and Maharashtra accounted for Rs. 548 crore. Further, as market or institutional borrowings are less popular among urban local bodies the Commission recommended that State Governments should remove restrictions on the borrowing powers of urban local bodies and give them freedom to mobilize resources, based on their credit ratings.

The ratio of wage bill to total ordinary income has been provided for 15 ULBs to get a sense on the flexibility that is there with them for incurring other expenses. This ratio has come down in some ULBs but should not be interpreted as cuts in labour costs as the wage bill has been up and a lower ratio is due to the higher growth in income.

Table 6: Growth in Wage Bill and Ratio of Wage Bill to Ordinary expenses (%)

	Growth in wage bill	FY12	FY13
Delhi	17.0	39.2	40.2
Baroda	10.6	51.0	47.6
Rajkot	15.8	49.8	45.8
Shimla	12.1	61.3	74.4
Amravati	4.1	47.4	32.8
Brihan Mumbai	38.1	33.2	39.4
Kolhapur	9.1	42.3	38.4
Sholapur	14.0	36.1	35.8
Thane	19.2	32.2	38.2
Pimpri- Chinchwad	3.7	21.7	21.6
Bhopal	26.1	37.1	41.1
Jabalpur	7.7	31.2	22.9
Jodhpur	17.6	41.4	35.0
Dehradun	10.9	50.8	55.7
Agra	6.0	32.3	37.8

The table does show considerable variation in this ratio and also indicates the room available for them to spend on new projects as well as maintenance given the limited fiscal room that is available in the federal fiscal structure.

Going ahead

The 14th Finance Commission has recommended grants to the extent of Rs 87,143.8 crore for next 5 years. The grant assessed for each State for each year is fixed. In the case of municipalities, the division between basic and

performance grant will be on an 80:20 basis. The basic grant would be divided into tier-wise shares and distributed across each tier, namely the municipal corporations, municipalities (the tier II urban local bodies) and the nagar panchayats (the tier III local bodies) using the formula given by the respective state finance commissions.

Performance grants would be contingent on making available reliable data on local bodies' receipt and expenditure through audited accounts; and improvement in own revenues. For computing the increase in own revenues in a particular year, the proceeds from octroi and entry tax must be excluded. In addition, the urban local bodies will have to measure and publish service level benchmarks for basic services. The service level benchmarks of the Ministry of Urban Development may be used for this purpose.

Along with the other suggestions made by the Commission on enhancing collections on both tax and non-tax revenue, ULBs would need to gear up to borrow funds in the market or through FIs to finance the growing needs of urbanization.

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