PEER REVIEW REPORT

22BG07 – Developing fiscal decentralisation and improving local financial management in Bulgaria

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List of abbreviations

ARV	Annual Rate on Valuation
BfC	Budget for Citizens
CCMA	County and City Management Association
CDSG	Council for Decentralisation of State Governance
CEGG	Centre of Expertise for Good Governance
CIT	Corporate Income Tax
CoE	Council of Europe
DG Reform	Directorate-General for Structural Reform Support
DHLGH	Department of Housing, Local Government and Heritage
DPER	Department of Public Expenditure and Reform
EU	European Union
FFD	Decentralisation Financing Fund
GPG	General Purpose Grants
IMC	Intermunicipal communities
LG	Local Government
LPT	Local Property Tax
MoF	Ministry of Finance
MoRDPW	Ministry of Regional Development and Public Works
NAMRB	National Association of Municipalities in the Republic of Bulgaria
NOAC	National Oversight and Audit Commission
OGP	Open Government Partnership
PIT	Personal Income Tax
PPN	Public Participation Network
VAT	Value Added tax

EXECUTIVE SUMMARY

This report summarises the conclusions reached by the peers during their review mission in Bulgaria and discussed in preliminary form with the local stakeholders during the last day of the visit. The mission was organised by the Centre of Expertise for Good Governance of the Council of Europe (CEGG) and included experts from Armenia, Finland, Ireland, Italy and Portugal. The opinions collected from the local stakeholders, as well as the comparative examples and conclusions drawn by the peers are summarized in the text.

The Recommendations of the Committee of Ministers of the Council of Europe, as well as the findings of the 2021 Monitoring Report of the Congress of Local and Regional Authorities on the application of the European Charter of Local Self-Government in Bulgaria, were used as a benchmark in the peers' assessment.

Overall, our mission found that the Bulgarian authorities have a positive commitment to the process of decentralisation, in spite of the difficulties of the last years. Furthermore, there is a legitimate preoccupation for the efficiency and effectiveness of local spending, for the quality of municipal services and the fair access of every citizen of Bulgaria to services. At the same time, the main findings outlined in the Monitoring Report of 2021 are still valid, in particular in the area of local finance, where a chronic discrepancy persists between expenditure obligations and the local revenue base.

Six broad priority areas for the inter-governmental finance and the process of decentralisation were identified.

Priority area 1.
The local tax base

The own tax base of local authorities is under-exploited in Bulgaria, yielding less than the EU average as a fraction of total public revenues. This happens due to the weak incentives for local fiscal effort, but also the outdated parameters of local taxation which are written in the national laws.

A set of corrections may be considered which will also reduce the need for central transfers: re-assessing the value of individual and commercial property, which has not been updated for almost two decades; introducing a tax on land used for agricultural production, which is currently exempt; transforming the municipal business tax into a real tax, i.e. applied to a proper base (profit, turnover).

Priority area 2.
The transfers from the centre, the equalisation mechanism

The current system of transfers from the centre is mostly task-based and changes from one annual budget to the next, which creates disincentives for autonomous decisions in municipalities. The non-earmarked sum used for equalisation is rather small while some "extra-budgetary allocations" for capital investments are opaque and unpredictable.

Alternative models of tax sharing and non-conditional grants may be considered to increase local budgetary autonomy. For instance, the PIT sharing may be (re)introduced; a simpler system of normatives to finance the most important and costly delegated functions may be considered; the procedures for financing municipal investment programs from the state budget may be defined in law and agreed with the National Association of Municipalities.

Priority area 3.
Review the competencies of municipalities and the cooperation with deconcentrated authorities

Bulgarian municipalities are treated equally under the law, having the same set of attributions irrespective of size and capacity. These tasks are difficult to keep track of and manage in smaller communities. The deconcentrated offices placed at district level do not have enough capacity to assist local authorities with coordination and expertise.

It is advisable to perform a thorough review of the own and delegated functions of municipalities, in parallel with the introduction of a non-conditional financing mechanism based on normatives (Priority area 2). When reassignments of attributions take place, the best practice is that they come with adequate financial resources attached. The district offices (*oblasts*) would need to increase their capacity to assist weaker municipalities with advice and technical support.

Priority area 4.
The transparency of data collection and use for policy making

The Ministry of Finance is the coordination platform for decision-making in terms of local budgets and performance. It sees as its mission to ensure the efficiency and effectiveness of local spending, as well as the quality of and access to municipal services. This in turn generates a tendency to micromanage the local finance and the service provision. However, the diversity of local situations and the broad scope of municipal attribution make this task a difficult one.

The existing database can be improved, combining financial and non-financial indicators, so as to move over time towards the monitoring of performance, beyond the indicators of financial distress used in the present. Benchmarking across municipalities would help improve performance in various sectors and inform discussions in government and the public space. Analytic modules may be included to inform the debate with local partners and the public.

Priority area 5.
The framework for consultation between central and local authorities

A Council for Decentralisation of State Governance (CDSG) exists in which central and local authorities are equally represented to discuss all the national policies with impact on local communities. The association of municipalities (NAMRB) also holds formal and informal consultations with the central authorities and publishes analytic pieces and reports.

However, the CDSG seems to have little visibility while the line ministries adopt regulations with little ex ante consultation.

The CDSG is worth being reactivated and strengthened, while the inclusion of citizens' representatives as observers would increase its visibility and relevance. To better formalise its activity, a calendar and list of topics may be published for the year ahead, in connection with the government's announced legislative agenda. Special working groups may be created to work specifically on budget issues or the municipal performance database, in close contact with the MoF; the budget group will publish a written opinion on the draft state budget.

Priority area 6.
The public communication of local budgets; public participation

Civic organisations have signalled that the level of knowledge among the wider public about local budget and finance is low. This limits the citizens' propensity to participate in local affairs. The complex format in which local budgets are presented makes them hard to understand for the layperson, while the brief calendar window in which the draft budgets are available for consultation makes their organisation difficult.

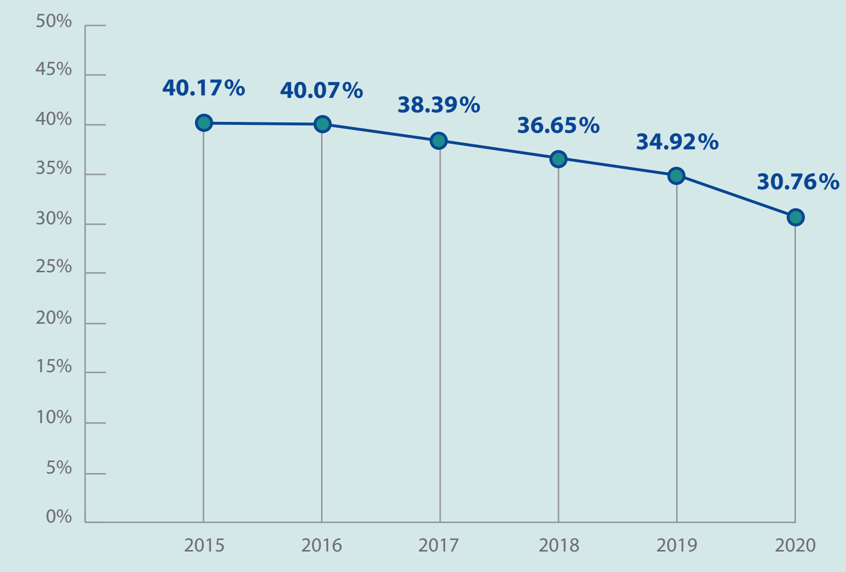
Better instruments can be created to the facilitate the understanding of the main issues and trade-offs incorporated in a budget. Various formats of "Budget for Citizens" (BfC) can be developed to stimulate public participation, with the MoF offering examples of good practice. BfCs should incorporate physical indicators and time series to facilitate the calculation of unit costs for various municipal services; these are prerequisites for moving towards proper program budgeting.

INTRODUCTION

Background, context

Bulgaria, like most countries in Central-Eastern Europe, went through two main stages over the last thirty years as far as the process of decentralisation is concerned. In the first two decades the local authorities with proper functional and political autonomy were (re)built, and the financial mechanisms to support this arrangement was put in place. The economic development, result of the rapid convergence with the rest of Europe and the growing importance of the EU grants, increased the volume and complexity of activity in the local government, a trend also reflected in their budgets.

The global economic crisis of 2007-2009 and its long-lasting impact on the public finance altered the picture to a significant extent. In Bulgaria, like elsewhere, a relative process of re-centralisation occurred after 2010: many unconditional transfers became earmarked, reflecting the preoccupation of the central government for tight control over spending; municipal credit was subjected to tighter rules; and in general, the scope for independent strategic decisions in the local authority was reduced. More funds from the EU Structural Funds became available in Bulgaria after accession, including at the local level, but these too are in general filtered through ministries and central agencies, where the decisions of allocation are usually taken.



Own source revenues in total local budgets: the declining trend.

Overall, the image today is that more resources per capita are available to communities than 15-20 years ago, but with less control over them exerted by the locally elected representatives, under a more opaque regime of central allocations. The chart below[1] illustrates this trend. And while the total volume of resources available to local authorities have increased, their spending responsibilities – and lately, costs due to inflation – went up even more, which creates a chronic structural deficit in local budgets.

One thing that has not changed during this interval is the territorial structure of the local government, based on just one tier of elected authorities: there are 265 municipalities, with directly elected mayors and councils. Therefore, Bulgaria is one of the countries which does not suffer from the problem of administrative fragmentation, common in the region: its territorial units are large enough to have reasonable economies of scale for municipal services. The administrative supervision over the local authorities is performed through 28 districts which are deconcentrated bodies of the central government.

On the upside, a Strategy of Decentralisation 2015-2025 exists with three broad objectives aimed to address the challenges of local governance and which remain as relevant today as they were ten years ago: (i) shift more powers and resources from the state bodies to the municipalities with a view to strengthen local self-government (restart decentralisation); (ii) review the attributions and mechanisms of the district governor and other deconcentrated branches of central bodied for better coordination of the sectoral policies at the sub-national level; (iii) increase accountability and participation in local self-governance. A Council for Decentralisation of State Governance (CDSG) was set up at the central level as a platform for consultation with local representatives, municipal associations and other stakeholders. The Strategy was revised and updated in 2021, with additional emphasis put on optimizing the system of local taxation and the transfer mechanisms, on the cost transparentising and control in municipal services, and the idea that options should be explored to set up a second tier of elected local governance.

On the downside, the political commitment to meet the goals of the Strategy has fluctuated, while the repeated crises (Covid, energy prices) and the political instability in central government during the past two years created additional distractions from the task. The Ministry of Finance has a legitimate concern for the integrity and effectiveness of spending at the local level, but no other promoter of local autonomy exists to counterbalance the resulting tendency to micromanage local budgets from the centre. The CDSG has rarely met and is not consistently used by ministries to consult local stakeholders when decisions are taken which have an impact on local communities and budgets.

The overall effect of all these developments is that Bulgaria appears today as a moderately decentralised country in terms of the fraction of public spending taking place at the subnational level, but with low autonomy when it comes to the decision-making power in local authorities. Municipalities are financed predominantly though central transfers and grants (71%), most of which are strictly earmarked. Local taxation and other own revenues make up for the rest, but this fraction too is consumed largely for co-financing mandated tasks dictated from the centre. The equalisation fund is relatively small and as result the process of balancing the resources in territory relies mostly on the complex and opaque task-based set of transfers. In turn, this system creates strong disincentives for local fiscal effort in municipalities.

1. Mihaylova-Goleminova, S, and D. Kalcheva (2023), *Revenue system of local self-governments in Bulgaria.*

The CoE-EU Joint Project

The European Commission (DG REFORM) under the Technical Support Instrument and the Council of Europe co-fund the project *Developing fiscal decentralisation and improving local financial management in Bulgaria*, which is aimed at offering technical support in the area of good democratic governance and financial decentralisation, with the purpose of developing fiscal decentralisation and improving financial management in Bulgaria. This is fully in line with the country's Strategy of Decentralisation 2015-2025 (updated in 2021) mentioned above, the National Development Programme 2030 and the Recovery and Resilience Plan approved by the Council in 2022. The project is also addressing the EU-wide priorities related to cooperation and quality of public administration at regional and local level by promoting sound multi-level governance practice.

To meet these goals, the Centre of Expertise for Good Governance of the Council of Europe (CEGG) deploys tools such as the present Peer Review, the delivery of a Policy Advice, and the implementation of its toolkit of instruments, such as the Local Finance Benchmarking for local authorities (LFB). The main beneficiary of the project is the Ministry of Regional Development and Public Works (MoRDPW).

This report following the peer review visit is focused on two broad area of policy identified as priorities during the consultations with the Bulgarian authorities: (i) fiscal autonomy and financial equalisation of municipalities; and (ii) the system of multi-level governance.

The CoE Peer Review

The rationale of the Peer Review

The Peer Review process has been developed by the CEGG as a tool to provide assistance and advice to member states in preparing, adopting or implementing reforms aimed at strengthening good democratic governance at all levels of government. A Peer Review is essentially an intergovernmental exercise enabling colleagues from other European governments who have carried out similar reforms and legislative changes to offer information, best practice, and provide friendly advice to the requesting authority. It encourages the sharing of alternative perspectives on the issues raised by the host state, and possible solutions to them following a series of meetings and frank discussions in a confidentiality environment with the local officials.

The discussions during the Peer Review mission revolved around a list of policy areas and questions which were identified in advance together with the Bulgarian authorities. Following the meetings held in Bulgaria, the peers decided to work on the initial two clusters of issues presented in Annex A2, and reorder them in accordance with the priorities of the central and local stakeholders, as they emerged from the discussions. Thus, six main areas of reform resulted on which advice and examples are provided; the Bulgarian authorities are encouraged to continue the dialogue with the local representatives and other stakeholders in this structure and address the challenges identified. The six priority areas are:

1. The local tax base.
2. Transfers from the centre, the equalisation mechanism.
3. Review of the competencies of the Municipalities and cooperation with deconcentrated authorities.
4. The transparency of data collection and use for policy making.
5. The framework for consultation between central and local authorities.
6. The public communication of local budgets; public participation.

The Peer Review mission in Bulgaria

The Peer Review meetings took place from the 25th to the 27th of September 2023, in Sofia, with a visit to the Municipality of Samokov and the participation to a citizen consultation organised by the Citizen Participation Forum (CPF).

The peers received in advance a set of background documents which included: the Technical Report with a comprehensive analysis of the existing legal, administrative and operational framework for municipalities in the Republic of Bulgaria[2], the Monitoring Report of the application of the European Charter of Local Self-Government in Bulgaria[3], policy briefs[4] produced by local analysts describing the Bulgarian local finance system, position of the National Association of Municipalities in the Republic of Bulgaria (NAMRB) on the main issues raised, documentations provided by the MoRDPW on the decentralisation strategy 2016 – 2025, and the legal framework on local taxes and fees.

The **Peer Review Team** included the following national experts:

- Markku Mölläri, Ministerial Advisor – Ministry of Finance (Finland).
- Tânia Mourato, Director of the Department for Cooperation and Financial Affairs, General Directorate of Local Authorities (Portugal).
- Sinéad O'Gorman, Principal Officer of the Local Government Finance Unit – Department of Housing, Local Government and Heritage (Ireland).
- Artak Yergenyan, Expert, Ministry of Territorial Administration and Infrastructure, (Armenia).

The **CEGG Team** was made up of:

- Sorin Ionia, Lead expert (Romania).
- Vieri Ceriani, International consultant (Italy).
- Niall Sheerin, Deputy Head of the Centre of Expertise for Good Governance (Council of Europe).
- Natalia Militello, Project Manager (Council of Europe).

2. The Technical report was produced in the framework of this project and is available online.
3. Council of Europe (2021), Congress of Local and Regional Authorities CG(2021)40-20final.
4. Faculty of Management and Administration – University of National and world Economy (2023), *Journal of Management Sciences and Applications, Vol.1* (2023), https://jomsa.science/index.php/jomsa/issue/view/2

The agenda of meetings is presented in Annex A.1. The discussions were frank, and the Ministry of Regional Development and Public Works was supportive of the effort and offered positive feedback at the end of the mission. All the debates were held under the Chatham House rule (information provided can be used but not attributed to any individual or organisation).

Purpose of this report

This post-mission report is the main deliverable of this Peer Review part of the project, written for the main beneficiary (MoRDPW) and the other national partners. It integrates the main data, concerns and opinions expressed during the meetings, plus additional desk research.

The report also summarises the conclusions reached by the peers during their visit and presented in preliminary form in the debriefing session during the last day of the visit to Bulgaria. A reordering of the initial topics was operated to reflect better the emphasis of the discussions and the new issues identified during the visit. There are now six broad priority areas for the inter-governmental finance and the process of decentralisation at large, and the rest of this report follows this structure. The examples and advice drawn from the countries included in the exercise as a reference are organised accordingly.

The report offers recommendations for action in each of the six areas of interest. These are closely aligned with the provisions of the European Charter of Local Self-Government[5] (hereafter referred to as the Charter), in particular Art. 4 (Scope of local self-government), Art. 8 (Administrative supervision) and Art. 9 (Adequate financial resources for local authorities, commensurate with their responsibilities), and based on relevant Council of Europe documents such as:

- Recommendation Rec(2004)1of the Committee of Ministers to member states on financial and budgetary management at local and regional levels.
- Recommendation Rec(2005)1 of the Committee of Ministers to member states on the financial resources of local and regional authorities.
- Recommendation Rec(2011)11 of the Committee of Ministers to member states on the funding by higher-level authorities of new competences for local authorities.
- Recommendation Rec(2019)3 of the Committee of Ministers to member states on the supervision of local authorities activities.
- Recommendation Rec(2022)2 of the Committee of Ministers to member States on democratic accountability of elected representatives and elected bodies at local and regional level.
- Recommendation Rec(2023)5 of the Committee of Ministers to member States on the principles of good democratic governance.

It is also in line with the findings and recommendations of the 2021 Monitoring Report of the Congress of Local and Regional Authorities on the application of the European Charter of Local Self-Government in Bulgaria[6].

5. https://www.coe.int/en/web/conventions/full-list?module=treaty-detail&treatynum=122
6. https://rm.coe.int/monitoring-of-the-application-of-the-european-charter-of-local-self-go/1680a28bb8

PEER REVIEW FINDINGS

General remarks

The Peer Review Team found that the main findings outlined in the Congress Monitoring Report of 2021 are still valid and shared by the Bulgarian central and local authorities, in particular in the area of local finance. They are caused by the chronic discrepancy between expenditure obligations and the local revenue base. The Report mentions in conclusions that "*municipalities barely have any space of discretion on spending priorities when the relevant activities are financed through State transfers*[7]".

A legitimate preoccupation exists at the central level, especially in the Ministry of Finance, for the efficiency and effectiveness of local spending, for the quality of municipal services and the fair access of every citizen of Bulgaria to such services. However, the practice which emerged, based almost exclusively on funds tied to a long list of tasks, and which changes from one year to the next, is not fully in line with Art 14 in the CoE CM/Rec(2005)1, "*shared resources of local authorities should primarily consist of non-earmarked additional resources and/or non-earmarked shared proportional resources decided by a permanent law*".

As the Monitoring Report also notes, the solution found by the central authorities to this trade-off between local financial autonomy and accountability for the funds received does not live up to the requirement of proportionality detailed in Art 8, para 3[8], of the Charter. A better mechanism can be conceived, based on more accurate data on municipal costs and performance, to estimate the adequate level of resources needed for the municipal task fulfilment in an objective, adaptive, reliable and accurate manner.

The predictability, stability and legitimacy of the inter-governmental transfers is of paramount importance, and all the more so since they are and will most likely remain the dominant source of the local budgets. Moreover, it is difficult to quantify and measure the precise local need on every mandated function created for municipalities, as the MoF attempts to do; a simpler system of tax sharing and normative grants, based on a smaller number of indicators and more local flexibility in spending the funds, may go a long way towards meeting the goals of predictability, stability and transparency.

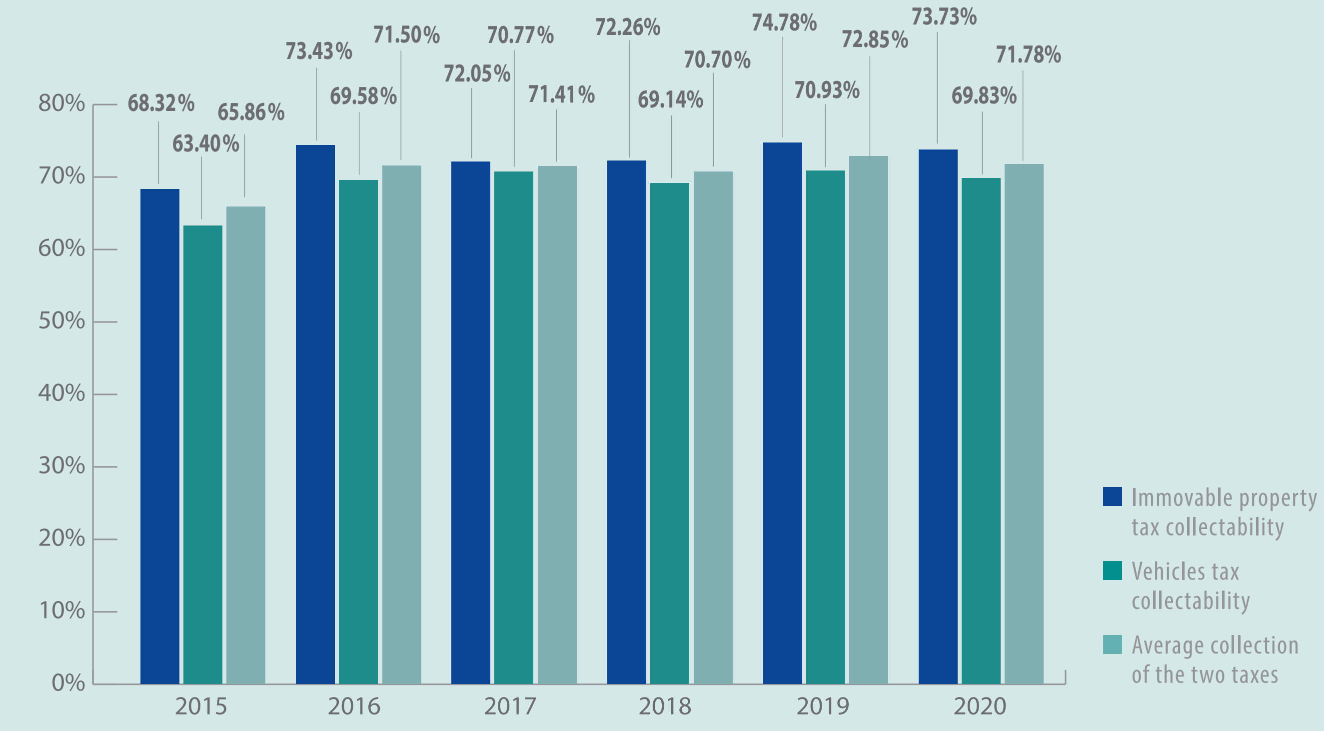
7. Council of Europe (2021), Congress of Local and Regional Authorities CG(2021)40-20final, pag.37.
8. *Administrative supervision of local authorities shall be exercised in such a way as to ensure that the intervention of the controlling authority is kept in proportion to the importance of the interests which it is intended to protect.*

The problem of complexity and opacity of the task-based, earmarked transfers from the centre, which are the main source of funds for most municipalities, is compounded by the practice of discretionary "extra-budgetary allocations". As the peer review team understood, there were instances when funds left unspent in various chapters of the national budget were reallocated towards the end of the year to some local authorities, for investment purposes (but not only), following an allocation process which is not always very transparent to the municipalities.

The effects of this two-speed transfer system are, on the one hand, the suspicions of favouritism among the local stakeholders and the public; and on the other hand, the demotivation of local authorities, who are not stimulated to be proactive and find their own sources of revenue, including by optimising the local tax collection. The principle of incentivising local authorities to engage in fiscal effort could be incorporated in all the corrections applied to the inter-governmental finance. A better and more transparent data system may be developed, preferably in real time, to track performance in municipal services, do benchmarking analysis based on reliable indicators and inform policy decisions at the central level.

Priority areas and recommendations

Priority area 1 The local tax base



Rates of collection for two types of local tax: upward trend.

The own tax base of local authorities is visibly under-exploited in Bulgaria, yielding significantly less than the EU average as a fraction of total public revenues: 4.2% vs 15.4%[9]. This happens for various reasons:

- uneven own fiscal effort by the local authorities themselves (some do not collect what they are owed);
- other reasons which are not under the control of local authorities: legal provisions for assessing the value of property are outdated; there are exemptions for various types of property;
- tight regulation of local taxes by the government in general, which leave little space for local decision-making.

However, in spite of the disincentives mentioned, the chart[10] above proves that the rates of collection for local taxes have increased over time, even below the similar level for some national taxes. This shows that entrusting local authorities with more sources and freedom to administer them may lead to overall improvement in municipalities' fiscal position.

RECOMMENDATIONS FOR ACTION

In principle the current assignment of taxes to the Bulgarian municipalities are in line with Art. 9 of the Charter, para 4, which speaks about the "*sufficiently diversified and buoyant nature*" of the local own sources: the tax and non-tax local revenues are roughly equal and quite diverse. However, the actual practice can be improved by following the provisions of CM/Rec(2005)1 on financial resources at local levels, section 3 (on local taxation guidelines).

Three corrections with significant impact could be considered, to benefit local budgets and minimize the need for central transfers and equalisation:

- The assessment of the value of individual and commercial property could be reviewed; in its current form the taxable value of property has not been updated for almost two decades, which leads to a situation in which the tax value of a property may be 10% of the real market value; the case of Ireland below can serve as guidance.
- A tax on land used for agricultural production, which is currently this is exempt, could be considered.
- The municipal business tax could become a real tax, i.e. applied to a proper base (profit, turnover), instead of a flat fee as it is now.

The first and second reforms will benefit mainly the urban, and respectively the rural municipalities, and so would bolster local finance without creating major territorial disparity. These proposals are fully supported by the NAMRB, and independent experts met during the Peer Review visit. Further tax simulations are advisable to determine how to better implement such changes.

9. Peteri G., 2023. *Comprehensive analysis of the existing legal, administrative and operational framework for municipalities. Technical Report.* CEGG.

10. Mihaylova-Goleminova, S, and D. Kalcheva, 2023. *Op.cit.*

PEER REVIEW FINDINGS

Examples in Peers Member States

ITALY: LOCAL FUNCTIONS AND FINANCE

Italy is not a federal state but there are four layers of government: the State, the Regions (20), the Provinces (110) and the Municipalities (7.900). There is a system of consultation and co-decision between the State and the regions, the provinces and the municipalities. The system is based on permanent bodies ("Conferenze") formed by representatives of the central government and the local authorities and has also a co-decision role in administrative regulations and in the criteria for the allocation of grants.

Provinces take care of local roads and some educational expenses (provide buildings for secondary education). They are financed by the vehicle registration tax and grants from the State (mainly for equalisation). Municipalities provide basic services: tax office, technical office, civil registry, general services, public roads safety and maintenance, local public transport, land management and planning, waste management, social services, nursery services, local police, complementary services in education.

The own taxed of municipalities represent roughly 45% of their total revenues. The main municipal taxes are the property tax and a surcharge on the personal income tax (PIT, see below). These two taxes account for most of the municipal own revenue. The property tax was introduced in 1992 and is levied on residential and commercial buildings and on land. Municipalities may adjust the tax rate within a bracket and give exemptions and rebates. Other revenues come from minor taxes (the hotel tax - Imposta di Soggiorno), the fees for waste management and other fees (like for the occupation of public soil and for advertising).

The municipal PIT surcharge

The municipal PIT surcharge was introduced in 1998 with the purpose of financing new administrative competences that were devolved from the state to the municipalities. It was a proportional surcharge on the national PIT tax base, with the possibility for municipalities to fix the tax rate within predetermined limits: from zero (the tax is not levied) to 0,8%.This solution left the central government with the responsibility of deciding the basic redistributive function: the degree of progressivity and the determination of other basic important features such as family allowances, exemption thresholds and other personal allowances[11].

The local PIT is levied on taxpayers resident in the municipality, independently of their workplace (and of the residence of the employer). Since taxpayers mainly receive services from the municipality where they are resident, the tax responds to the benefit principle.

As an alternative, a revenue sharing of PIT was considered. It could easily supplement the fiscal capacity of local administrations, without administrative complexities. A predetermined percentage of the PIT revenues collected by the State would have been transferred to each Municipality, according to the residence of the taxpayer. But with revenue sharing there would be no tax autonomy for the municipalities and no visibility, nor accountability. The choice was made to implement a local PIT, as a proper tax, separate from the national PIT, visible to the taxpayer, set at rate on which local administrators exert their autonomy (within limits) and for which they are accountable. From the perspective of enhancing local

11. However, in recent years municipalities could differentiate the rates of the local PIT between brackets of the national PIT.

democracy, the local PIT was considered superior to revenue sharing, because it fosters local fiscal responsibility and financial autonomy. Unlike in the case of revenue sharing, taxpayers can identify the level of government responsible for setting the tax, and therefore the local politicians are more accountable.

The local PIT surcharge is collected by the state tax administration, together with the national PIT, without a separate income declaration, and distributed to each municipality with short delay. The assessment of the tax is a competence of the national tax administration. Municipalities co-operate with the state tax administration, transmitting information, but without the power of auditing. If the information provided triggers a successful audit procedure by the state tax administration, municipalities receive a share of the extra revenues. Enforcement and litigation are exclusive competence of the state tax administration, together with the national PIT. In conclusion, local authorities have almost no administrative task to perform. They simply decide the rates of the PIT surcharge and receive the revenues from the State.

PORTUGAL: THE OWN REVENUES OF LOCAL AUTHORITIES

The main local taxes specified in law are:

- Municipal Property Tax (IMI). The IMI's rates are set annually by the municipalities in the area where properties are located within the following range: between 0.3% and 0.45% for urban buildings, and 0.8% for rural properties.
- Municipal Property Purchase Tax (IMT). The rate is variable and depends on the type of property (primary residence versus rental or holiday residence) and the value of the property.
- Surcharge tax. Municipal tax on corporate income that is taxable by the national corporate income tax. This tax decreased considerably during the 2009 financial crisis, but since 2016 it has been increasing.
- Circulation Unique Tax (IUC). It´s a yearly tax that is calculated considering the engine cubic capacity and the CO2 emissions. Revenues are shared among the central government and local governments.

In addition to these, parishes (municipal sub-units) have their own sources of revenue:

- A central general-purpose grant, the Financial Fund of Parishes, which corresponds to 2% of the average of the amount collected with personal income tax, corporate tax, and value-added tax, redistributed among them with different criteria: population density, number of inhabitants and area.
- An amount from municipal delegated functions, paid by the municipality. The amount is negotiated with the municipality according to the number and type of delegated functions.
- Own revenues: user charges related to some public services provided.

The state budget has a specific annex where amounts allocated annually to parishes is set and published.

The Intermunicipal communities (IMCs) also have revenues coming from the central budget: 0.5% of the total transfers from the Financial Equilibrium Fund of the municipalities which integrate the intermunicipal community area. In the case of metropolitan areas, the percentage is 1%. Municipalities also contribute to their respective IMC for the management of intermunicipal projects.

IRELAND: HOW TO ASSESS THE VALUE OF COMMERCIAL PROPERTY FOR TAX PURPOSES

Tailte Eireann, an independent Government agency under the aegis of the Department of Housing, Local Government and Heritage (DHLGH), has responsibility for all valuation matters. Local authorities are under a statutory obligation to levy rates on any property used for commercial purposes, in accordance with the details entered in the valuation lists prepared by the independent Commissioner of Valuation under the Valuation Act 2001. The levying and collection of rates are matters for each individual local authority. The Annual Rate on Valuation (ARV), which is applied to the valuation of each property, determined by Tailte Éireann, to obtain the amount payable in rates, is decided by the elected members of each local authority in their annual budget and its determination is a reserved function of the elected members of a local authority.

Revaluation is a national programme to systematically modernise the rateable valuation of all commercial and industrial property in Ireland by reflecting modern rental values and contemporary market conditions, thereby improving the transparency of the local authority rating system. By the end of 2023 all local authorities with the exception of two, will have been subject to a revaluation.

Having a modern valuation base is very important for the levying of commercial rates on a fair and equitable basis across all property sectors. The Valuation Acts provide fort the revaluation of all rateable property within a rating authority area to reflect changes in value due to economic factors such as differential movements in property values or other external factors and changes in the local business environment. A revaluation will bring more equity, uniformity, fairness, and transparency into the local authority rating system resulting in a more equitable distribution of commercial rates among ratepayers.

A valuation for commercial rates purposes is arrived at by estimating the Net Annual Value of the property in question, at a specified valuation date. The term "net annual value" has a legal definition and is set out in section 48 of the Valuation Act 2001 as "*the rent for which, one year with another, the property might, in its actual state, be reasonably expected to let from year to year, on the assumption that the probable average annual cost of repairs, insurance and other expenses (if any) that would be necessary to maintain the property in that state, and all rates and other taxes payable in respect of the property, are borne by the tenant*". This definition of Net Annual Value is applied to all rateable properties and classes of business on a nationwide basis.

Estimating the Net Annual Value of a rateable property is an evidence-based exercise. During a revaluation, the Valuation Office analyses relevant market rental transactions for all rateable properties in accordance with the legislation, best practice internationally as set out in published Practice Guidance Notes, well-established valuation principles and case law arising from the independent Valuation Tribunal and the Higher Courts. The conclusions drawn from that analysis is applied to similarly circumstanced property using the "comparative" method of valuation which, as the name implies, employs direct comparison with other similar properties.

Tailte Eireann has responsibility for all valuation matters, including the global valuation of property of public utility undertakings. The Central Valuation List is a list of all global valuations which are the valuations of certain designated public utility undertakings in the State. Global valuations are carried out on a five-yearly cycle as provided for by section 53(6) of the Valuation Act 2001 as amended by the Valuation (Amendment) Act 2015.

Tailte Eireann apportions global valuations between local authorities. Each local authority is apportioned an element of a global valuation if property of the utility undertaking being globally valued is situated in its local authority area. Each utility undertaking is valued independently to all other global utility valuations. The apportionment of the global valuation (i.e. the amount of the valuation that will be apportioned to each of the rating authorities and on which they will levy rates for 5 years until the next scheduled global valuation) is determined by Ministerial Apportionment Order (statutory instrument). The Apportionment Order seeks to apportion the global valuation rateable valuation among the rating authorities in an equitable manner, which is generally on the basis of population.

IRELAND: THE TAX ON RESIDENTIAL PROPERTY (LOCAL PROPERTY TAX)

Local Property Tax (LPT) is an annual tax charged on the market value of certain residential properties. The tax operates on a self-assessment basis and the level of compliance has been consistently high since its introduction in 2013, at a time when the public finances were under considerable pressure. Those liable to pay LPT, are, for the most part, the owners of residential properties, including rental properties. The tax is broad in scope with a limited number of exemptions allowed. However, a system of deferral arrangements is available where there is an inability to pay and specified conditions are met.

The local property tax is the largest extension of self-assessment in the history of Ireland, with more than 1.3 million taxpayers obliged to file LPT returns and pay the tax in respect of approximately 1.9 million properties. The purpose of the LPT is to broaden the tax base and to provide a stable and sustainable source of funding for local authorities. The Revenue Commissioners are responsible for the administration and collection of the tax. LPT proceeds are transferred to the Local Government Fund for onward redistribution to local authorities.

Local variation: local authorities have the power to vary the rates of Local Property Tax (LPT) in their areas by up to 15%. If a local authority decides to vary the LPT basic rate downwards (by up to 15%), the resultant loss in LPT income is reflected in a proportionate reduction in discretionary income for the Council. Likewise, if a local authority decides to vary the rate upwards, there is a proportionate increase in such income.

First valuation period: the LPT charge is based on the market value of a property on a specified date, called the valuation date. The precise value does not have to be declared to Revenue but, instead, the relevant valuation band has to be selected. The first valuation period ran from 2013 to 2021 with the tax charged on the value of properties as at 1 May 2013.

Second valuation period: a revised method of calculating LPT liabilities was introduced for the 2022 LPT liability year, with a revision to the basic LPT rate and a widening of property tax bands to take account of property price increases since 2013. The second valuation period began in 2022 with LPT charged on the value of properties based on a valuation date of 1 November 2021. The valuation of a property on this date determines the LPT charge for the four years from 2022 to 2025. Newly built properties are also liable for the LPT charge, once it becomes occupied or suitable for use. All new properties built between valuation dates are retrospectively valued as if they had existed on the preceding valuation date.

Priority area 2 The transfers from the centre, the equalisation mechanism

The current system of transfers from the centre is mostly task-based and volatile, changing from one budget cycle to the next. This creates rigidity in local budgets, sub-optimal allocations in territory and disincentives for autonomous decisions in municipalities. Alternative models of tax sharing and non-conditional grants may be considered, to increase local budgetary autonomy. Moving away from this mechanism of transfers would be in line with principles 7 (*Efficient, effective and sound administration*) and 10 (*Sound financial and economic management*) of the CM/Rec(2023)5.

Moreover, the total non-earmarked sum used today for equalisation is rather small (about 6% of the total transfers) and cannot compensate for the resource imbalances created by the difference in the economic condition of various municipalities. If the PIT will be shared with LGs in the future, the need for a substantial equalisation fund will only increase. Finally, the discretionary "extra-budgetary allocations" for capital investments pervert incentives at the local level and make inter-governmental finance opaque and unpredictable.

RECOMMENDATIONS FOR ACTION

The reforms which may be contemplated are:

- Restore the PIT sharing which existed before 2008, origin-based and non-conditional in use, for example with a share of 20% ceded to municipalities.
- The creation of a simple and stable system of normatives to finance the most important and costly delegated functions; the current set of standards for the delegated competencies, over 130 in number, are hardly manageable in smaller municipalities and not in line with the principle of proportionality detailed in CM/Rec(2019)3.
- From the residual PIT left at the central level, another share could be earmarked for equalisation across municipalities; ideally this would be stable in time as a percentage of PIT collected and represent more than the current sum used for equalisation; the allocation rule would also need to be stable in time, simpler than the current mechanism and perceived as legitimate by the local authorities (for instance, by using a proxy for the local fiscal capacity).
- The discretionary "extra-budgetary allocations" would better be avoided, because they generate loose budget constraints at the local level, which is the opposite of the stated goal of MoF; a multi-annual fund to (co)finance capital investments in municipalities could be set up instead, with a clear and transparent mechanism of allocation based on calls and scoring points, and possibly prioritising the co-financing of EU projects in order to improve the absorption rate of EU funds, which is a national priority.
- In line with Art. 4, para 1 of the Charter, it is advisable that the procedures for financing municipal investment programs from the state budget are defined in law and agreed with the National Association of Municipalities. Art. 9 of the Charter says that the local authorities shall be consulted, in an appropriate manner, on the way in which redistributed resources are to be allocated to them.

PEER REVIEW FINDINGS

Examples in Peers Member States

ITALY: THE EQUALISATION SYSTEM

The equalisation system targets two layers of government: Provinces and Municipalities. It is regulated by a State law and is based on the equalisation of the fiscal gap, i.e. the difference between standard expenditure needs (SEN) and standard fiscal capacity (SFC). There are two separate equalisation systems, one for Provinces and the other for Municipalities. Standard expenditure needs are calculated for each function, based on regression analysis. For each function appropriate variables have been selected and weights have been attributed to the variables, resulting from statistical analysis. Fiscal capacity is calculated applying the standard rates to the potential tax base. This method, known as the Representative Tax System (RTS) is preferred to the Historical Revenue Approach (HRA) and is recommended (both by CoE and OECD) as a best practice. The HRA, which is based on the actual amount of own tax revenue collected by municipalities, has a strong drawback: it generates incentives for the local authorities to reduce their fiscal effort. In fact, if local governments collect less tax revenue, they may compensate it with higher equalisation grants. If they raise more tax revenue, their equalisation grants are reduced.

The Italian equalisation system is horizontal: municipalities with a positive fiscal gap (standard revenues above standard expenditures) provide financing to the equalisation fund, that redistributes funds to the municipalities with negative fiscal gap (standard expenditure above standard revenues). The horizontal equalisation has created tensions among jurisdictions, because "rich" municipalities are reluctant to finance "poor" municipalities.

ARMENIA: HOW TO ALLOCATE CAPITAL INVESTMENT GRANTS

The Government of Armenia created a clear procedure for the allocating grants to municipalities for the development of the economic and social infrastructure. Municipalities submit applications through the regional administration bodies before May 5th of the year preceding the implementation of the investment program. Upon receiving the applications, the Ministry of Territorial Administration and Infrastructure sends them for analysis to the sectoral ministries and other relevant specialized bodies. The application includes a letter of obligation from the municipality leader confirming that the expenses required for the operation, maintenance, and upkeep of the new infrastructure will be covered from the municipality budget for a period of ten years.

The Ministry of Territorial Administration and Infrastructure prepares a summary of the applications and sends them for evaluation to the inter-ministerial committee set up by the Prime Minister's decision. Within 10 working days of receiving an application, the inter-ministerial committee issues a conclusion on the impact of the proposed investment on the development of the municipality and its contribution to solving the urgent local problems.

The criteria for financing from the state budget are: distance from the capital, distance from the regional centre, high altitude, proximity to the state border, the small municipal budget (up to 60,000 Euro per year), a loan of 20% or more as a private investment, 51% or more local co-financing. In this context, funding from the State budget ranges from 30% to 90% for a number of programmes aimed at investing in municipality infrastructure.

The highly formalised process has increased the transparency of allocations and the quality of projects presented for financing. It has also improved the investment climate in municipalities, reducing the uncertainty and thus the risk premium incorporated in the work contracts, which eventually means a better use of public resources. Clear rules and regulations are crucial for municipalities and the central government alike, enabling effective planning of budget expenditures, making the monitoring of projects implementation easier and facilitating the introduction of key performance indicators.

With this mechanism Armenia implements the provisions of Article 4, section 1, of the Charter, which says that the procedures and regulations for financing municipal investment programs from the state budget should be defined in law and be agreed with the National Association of Municipalities. It also responds to the requirement in section 6 that the local authorities shall be consulted, in an appropriate manner, on the way in which redistributed resources are to be allocated to them.

IRELAND: THE ALLOCATION OF DISCRETIONARY FUNDING AND EQUALISATION

Central Government has traditionally provided non-programme funding to local authorities, in the form of an annual contribution towards meeting the cost of providing a reasonable level of service to their customers. Until 2014, this funding allocation was in the form of General Purpose Grants (GPGs). In 2014 a level of baseline funding was agreed and was funded by the centrally collected Local Property Tax (LPT).

Local Property Tax Baselines. Under the LPT allocation model, every local authority is entitled to receive a minimum amount of funding under the LPT allocation process, known as the baseline. Where a local authority's LPT income is lower than their agreed baseline, central government provide equalisation to ensure they are allocated a minimum of their agreed baseline funding. There are variances across the country in terms of LPT income levels, but it is important that all local authorities receive at least this baseline level of funding to help ensure they can deliver adequate levels of service. The over-all level of baseline funding to all 31 local authorities for a number of years, until 2023 was set at €352.9m.

Review of the LPT Baselines. It was argued that the level of baseline funding, which varied from authority to authority, no longer fairly reflected the differing expenditure needs and income raising abilities of local authorities. It was accepted that the circumstances of local authorities vary considerably from one another in terms of geographic area, population, service needs and the ability to raise their own income locally, and that these circumstances have seen significant changes in the last 20 years.

A working group, which included representatives from the local government sector, was set up earlier this year to review and establish a new model to determine Local Property Tax baseline funding levels. The work of the group has now concluded, and included recommendations that, from 2024, the baseline funding of some local authorities needed adjustment according to the criteria recommended by the working group. The group also recommended that no local authority should see a reduction in baseline funding upon the application of this model.

The increase in baseline funding for 2024 was guided by the review that has taken place and the recommendations of the working group. Furthermore, the Minister for Housing Local Government and Heritage ensured that every authority received an increase in baseline funding of at least €1.5m. Accordingly, the overall LPT Baselines of Local Authorities in 2024 will be increased from €353m to €428.4m.

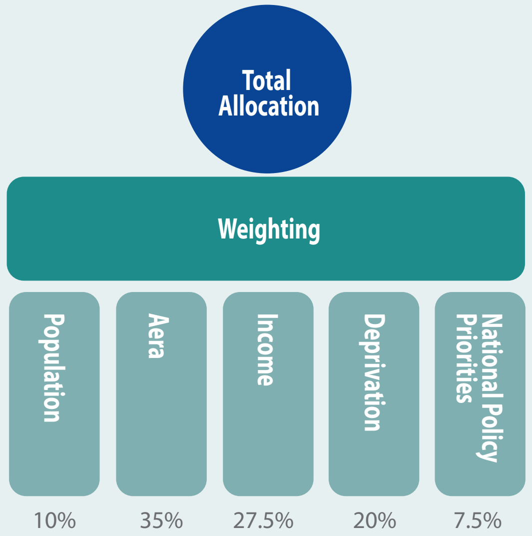
The final recommendations of the group are as follows:

– That the Minister allocate local authority LPT baselines for 2024 in accordance with the allocation model developed by the working group.

– That the model will determine the allocation of baseline funding to local authorities according to the following indicators and weightings.

That the application of this model will not result in a reduction of current LPT baseline funding levels (i.e. 2023 levels) for any local authority.

– That this model is used to review local authority baselines every 5 years, following updated census data.



The equalisation mechanism: indicators and weightings used.

Further information on the indicators and weightings. Non-programme funding was historically allocated using a "need and resources" model which involved the annual analysis of more than 300 data inputs per local authority. This was ceased due to complexity. The 2023 working group initially considered 5 indicators and 11 sub-indicators. Each sub-indicator was examined by the group, and excluded from the model where its impact was highly correlated with that of another indicator. The result was that the final agreed model retained the 5 main indicators, with only 2 further sub-indicators (for National Policy Priorities) required.

Population. The model allocates 10% of the total funding in proportion to the population of the authority; based on 2022 census figures.

Area. The model allocates 35% of the total funding in proportion to the area of the authority.

Income. The model allocates 27.5% of the total funding based on the locally raised income per capita in the authority. This income comprises of Goods and Services income and Commercial Rates income. Authorities receive an allocation proportionate to their distance from the highest income per capita.

Deprivation. The model allocates 20% of the total funding based on the Pobal Deprivation Index for Municipal Districts (MD) (or City Electoral Areas (CEA)). Those areas with a minus Deprivation Index Score receive an allocation in proportion to (1) the score and (2) the population of the area. There is a maximum allocation of €1.35m per MD (or CEA) and a minimum allocation of €406k per local authority.

National Policy Priorities. The model allocates 7.5% of the total funding based on an authority's performance in relation to two main national policy priorities (1) 3.75% in relation to housing targets (based on NOAC key performance indicators) and (2) 3.75% in relation to climate targets (based on Emissions targets from the Sustainable Energy Authority of Ireland).

PORTUGAL: CENTRAL TRANSFERS AND THE EQUALISATION PROCESS

A general-purpose grant exists coming from the Financial Equilibrium Fund (FEF), the value of which is equal to 19.5% of the arithmetic average of personal income tax (PIT), corporate income tax (CIT) and value added tax (VAT). This fund is divided into two sub-funds, having different purposes, each subsequently being redistributed among municipalities according to specific criteria:

– The Municipal General Fund, to finance municipal legal assignments which is distributed according to population, surface area, and other cost factors.

– The Municipal Cohesion Fund, to equalise municipalities, particularly with respect to fiscal capacity and differences in opportunities. Its allocation is based on municipal tax capacity compared to national average and an index of municipal social development.

The Municipal Social Fund, an earmarked grant, aims to correspond to specific expenses related to the attributions and competencies transferred from the central administration to the municipalities concerning education and related to a first round of decentralisation.

In addition, there is a variable participation of 5% in personal income tax (generated by the municipality residents). There is also a share of 7.5% in the VAT revenue collected in the accommodation, catering, communications, electricity, water and gas sectors.

On these aspects and to provide transparency the State Budget orders the General Directorate of Local Authorities to communicate the municipalities which variables/base data are used to calculate the stated funds. The state budget has a specific annex where amounts allocated annually to municipalities is set and published. When new powers are transferred to local authorities, the State Budget provides additional allocations under the Decentralisation Financing Fund.

Priority area 3 Review the competencies of municipalities and the cooperation with deconcentrated authorities

Bulgarian municipalities are treated equally under the law, having the same set of attributions irrespective of size and capacity. This is not unusual in European context, but the large number of such functions, created by various acts and sometimes by secondary legislation, is difficult to manage in smaller and poorer communities. In the words of a stakeholder during the peer review mission, "*many mayors don't even get to know before the end of their mandate how many functions they have to perform, and even if they knew, there would be no money to carry them out*".

The cooperation with the deconcentrated offices placed at district level is weak and these territorial branches of the government do not have enough capacity to assist local authorities with coordination and expertise. The idea to explore the creation of a second tier of elected authorities was initially included in the Strategy of Decentralisation 2015-2025, but it resulted from the discussions that it is not currently a priority for the government. Additional functions for municipalities are another option on the agenda, and something requested by the more capable local authorities, but in general the central government would like to fix and consolidate the existing system first, before reassigning additional competencies to municipalities.

RECOMMENDATIONS FOR ACTION

- It is advisable to perform a thorough review of the own and delegated functions of municipalities, in parallel with the introduction of the new non-conditional financing based on normatives described above at Priority area 2. Ideally the delegated functions will be much less numerous than the others and would have a clear funding mechanism, even in a form of an earmarked grant (see the example of education in Portugal).
- The functions that do not meet the criteria for being defined as delegated may become own functions of the municipality; the local stakeholders offered during consultations the examples of local police, firefighters or emergency services. However, according to the representatives of the central government, this redefinition of attribution can only come after the main decisions are made about how to make the system of transfers more efficient. When reassignments of attributions take place, the best practice is that they come with adequate financial resources attached, as requested by CM/Rec(2011)11 on the funding by higher-level authorities of new competences for local authorities, more specifically "*The increase of net local costs stemming from a transfer of competence from a higher level to local authorities, not aiming to change the level of service to the user, should be compensated. Compensation should be based on estimates of the expected net cost of the new competence. The cost of the transfer of staff, including the estimated wages and conditions of employment, should be included. The cost of obligations resulting from acquired pension rights of staff transferred should also be included in the compensation*".
- For competencies which are too complex and costly for the municipalities and have a larger catchment area above their level, alternative solutions may be explored, in the long run and after consultations (see example of Finland below).
- It is advisable that the district offices (oblasts) increase their capacity to assist weaker municipalities with advice and technical support, in particular on functions which require advanced expertise (EU project writing, urbanism and land management, the corporate governance of municipal companies etc).

Examples in Peers Member States

FINLAND: A CASE OF REORGANISATION OF COMPETENCIES

Starting with January 2023 the organisation of public healthcare, social welfare and rescue services was radically transformed in Finland. The responsibility for organising these services was transferred from municipalities to the newly created "wellbeing counties", in fact a second tier of government with elected councils. The objective of the reform is to improve the availability and quality of these three important and expensive public services throughout the territory of Finland, after years in which their provision at local level proved to be suboptimal. Under the reform, a total of 21 self-governing wellbeing services counties were established in Finland, on top of the existing 309 municipalities. In addition, the City of Helsinki became responsible for organising health, social and rescue services within its own area. The joint county authority for the Hospital District of Helsinki and Uusimaa district will be responsible for organising demanding specialised healthcare separately laid down by law. The highest decision-making power in each wellbeing county is exercised by the county council, whose members and deputy members were elected in county elections in 2022; from 2025 onwards, county elections will be held every four years in conjunction with municipal elections. The newly created counties have no taxation power, being financed entirely through transfers. Municipalities will remain responsible for promoting the public health and ensuring the wellbeing of their residents, and the public sector will remain the organiser and primary provider of services. Private sector actors and non-profits will supplement public health and social services. Five collaborative areas for healthcare and social welfare are created to secure specialised services and citizens will continue to be allowed to use health and social services across the new regional boundaries.

PORTUGAL: REASSIGNMENT OF FUNCTIONS TO LOCAL AUTHORITIES

Deepening the decentralisation of competencies to local authorities implies creating the legal and operational conditions to implement the transfer, to inter-municipal entities, municipalities and parishes, of the competencies provided for in the approved sectoral norms based on the Framework Law on Decentralisation (50/2018 of 16 August)[12].

In 2018 Portugal has started an important decentralisation process which stipulates the transfer of responsibilities to local authorities and intermunicipal entities between 2019 and 2023. Municipalities have gradually joined in the process between 2019 and April 2023. As a result, the areas of municipal responsibility are:

1. Education, all that refers to non-tertiary education, except management of teaching staff and definition of curricular contents.
2. Social action at the local level, especially in the fight against poverty (social integration Income attendance and social support services).
3. Health, local equipment and management of non-clinical personnel care facilities.
4. Municipal civil protection.
5. Culture, local heritage and museums not classified as national, licensing artistic shows.

12. https://files.dre.pt/1s/2018/08/15700/0410204108.pdf

6 Managing state unused real estate assets.

7 Housing, owning and managing social housing of the state and management of urban rental and rehabilitation programmes.

8 Management of port-maritime areas with no port use: secondary fishing ports, recreational boating and urban areas for tourism development.

9 Beaches: licensing commercial activities and equipment construction, management and equipment of coastal, river and lake beaches integrated in the public domain of the state.

10 Co-management of protected areas of land.

11 Communication ways (urban and secondary roads).

12 Citizen service: citizen's shops.

13 Proximity policing, participation in the definition of a policing model.

14 Fire safety in buildings.

15 Public parking.

16 Licensing raffles, tombolas, advertising contests at a local level.

17 Justice: "**justices of the peace**" network (volunteer commitment court), social reintegration and support for victims of crimes.

18 Transport on inland waterways.

19 Afforestation and reforestation.

20 Firefighters associations.

The main goal of this transformation is to bring public management closer to the citizens, in conditions of budget neutrality. The Decentralisation Financing Fund (FFD) is an allocation from the central budget to cover the new competences transferred to municipalities. In 2023 it includes a 1,200 mil Euro allocation to FFD to finance the new assignments allocated to municipalities, namely in the areas of education, health, social support and culture, as follows: around 1,020 mil Euro for education; 128 mil Euro for health care; 56 mil Euro for social support; and about 1.2 mil Euro for culture. In relation to the remaining areas, there is no transfer of funds from the state budget to the municipalities, but in many cases the legal power to collect revenue previously belonging to other entities has been given to them (ex: fees for beach concessions).

There was also a reinforcement of several parishes' powers in domains integrated in the legal sphere of the municipalities. The Decree-law 57/2019 of 30 April, in a logic of subsidiarity, allows that by mutual understanding a certain redistribution of attributions and financial resources from the municipality to the parish in the following areas: the management and maintenance of green spaces, cleaning of public spaces and maintenance of urban furniture, fairs and markets, maintenance of schools. The funds transferred to the parishes can be collected in a specific online portal[13].

13. https://portalautarquico.dgal.gov.pt/pt-PT/transferencia-de-competencias/dos-municipios-para-as-freguesias/

Priority area 4 The transparency of data collection and use for policy-making

The Ministry of Finance is currently at the centre of decision making when it comes to local budgets, with financial information collected directly from municipalities and non-financial indicators provided by other sectoral ministries. A legitimate preoccupation exists at this level for the efficiency and effectiveness of local spending, as well as for the quality of municipal services and the fair access of every citizen of Bulgaria to such services. This in turn generates a tendency to micromanage the earmarked transfers, which are numerous and task-based, by incorporating weighted costs and performance indicators into the system, and making allocations conditional on improvements, in formally or informally. The small number of Bulgarian municipalities makes this inclination towards central micromanagement of the local affairs deceptively attractive.

While in principle the MoF intends to be as objective as possible in its allocation decisions, the diversity of the municipal services and the complexity of formulas, incorporating indicators that even out or create perverse effects at the local level, make the effort in the current structure more difficult than it could be.

RECOMMENDATIONS FOR ACTION

- The existing database can be improved and developed, combining financial and non-financial indicators, to monitor performance in various municipal services, not only early warning signals in the local budget executions. Benchmarking across municipalities would help improve performance in various sectors and inform discussions in government and the public space (see the Italian example below). Such broader coverage is distinct from the narrower goal of the MoF to detect signs of financial distress in municipalities in order to offer them advice or send inspections in territory.
- Such a database can be built gradually over time and include analytic modules which would be open to the local government partners and the public. The transparency in use and accessibility would be fully in line with the principles of good governance outlined in CM/Rec(2023)5, more precisely principle 6 (Openness and transparency) and principle12 (Openness to change and innovation).
- Such an investment can be financed from Bulgaria's Recovery and Resilience Plan, under the EU priority to digitalize the public administration.

Note: priority area 4 is logically connected with 1 (The local tax base) and 2 (Transfers, equalisation). A more efficient system of own sources (1) may reduce the pressure on transfers from the centre (2). A more stable and rule-based allocation of central transfers goes hand in hand with opening up the database of indicators (4) and the decision-making process towards the local authorities, the civil society and the public at large. Over time, Bulgaria may develop a more complex, professional and institutionalised system of monitoring performance in local government, as the Irish example shows.

Examples in Peers Member States

ITALY: BENCHMARKING THE PERFORMANCE OF LOCAL GOVERNMENTS[14]

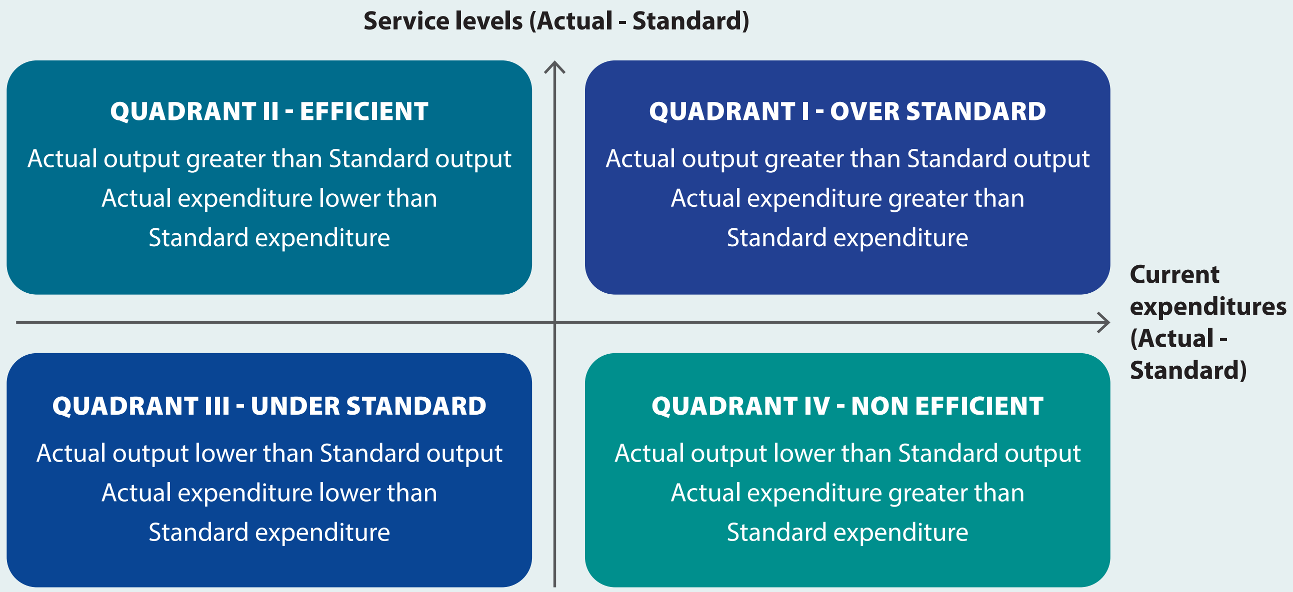
The gap between the standard and the actual expenditure for each service provides a good reference point to judge the level of expenditure of each municipality but is not a good indicator of local governments' efficiency in the provision of local services. Actual expenditure may be above (below) the standard because the municipality is providing more and better (less and worse) services than the standard.

Therefore, it is also useful to evaluate the performance of each community in the production of services in respect of a reference point (the national average, or a standard level). Using the methodology applied for calculating the SENs and an appropriate set of variables it is possible to calculate **standard levels of output (SLO)**, which can be compared with the **actual level of output**.

Consequently, a performance evaluation could be based on the **joint analysis** of two indicators: the **expenditure gap** (the difference between actual expenditures and standard expenditures) and the **output gap** (the difference between actual outputs and the standard level of outputs). This joint analysis has been carried out mapping each local administration into a four quadrants model like the one reported in the chart below.

Performance analysis

Local authorities in quadrant I (over-standard) are administrations that spend more than the standard and, at the same time, produce more services than the standard; on the opposite, local authorities in quadrant III (under-standard) are spending less than the standard providing also less services than the standard. These cases can be considered as "normal" under the principle that local governments should be free to exercise their autonomy in order to satisfy the local demand for public services.



14. This method of benchmarking the performance of municipalities has been implemented in Lithuania (see: Final Report on Equalisation in Lithuania) and in Italy (https://www.opencivitas.it/en/performance-analysis-municipalities).

On the other hand, local authorities located in quadrant II (efficient) can be considered as potential benchmarks for identifying best practices, because they are able to provide services above standard spending less than their standard expenditures needs. Instead, local authorities in quadrant IV (inefficient) are potential candidates for improvements of their performance, since they show a level of actual services below standard and a level of actual expenditure above their standard expenditure needs.

This kind of analysis has been implemented for benchmarking, to identify best practices and to stimulate inefficient local administrators to improve their performance. It has not been intended for imposing penalties on local authorities that show a poor performance.

IRELAND: HOW TO ORGANIZE THE PERFORMANCE MEASUREMENT AND MANAGEMENT

The National Oversight and Audit Commission (NOAC) is the national independent oversight body for the local government sector in Ireland. It was established in July 2014 under the Local Government Reform Act 2014 to provide independent oversight of the local government sector (local authorities and associated bodies), including Regional Assemblies. NOAC's functions are wide ranging, covering all local authority activities and involving the scrutiny of performance generally and financial performance specifically. NOAC also has a role in supporting best practice, overseeing implementation of national local government policy and monitoring and evaluating implementation of corporate plans, adherence to service level agreements and public service reform by local government bodies.

NOAC also annually produces a local authority performance indicator report which examines 42 indicators under 11 headings. These indicators cover a wide range of the functions carried out by Local Authorities in 11 specific areas of housing, roads, planning, water, waste/environment, fire service, library/recreation, youth/community, corporate, finance and economic development. These are used in the individual performance reports. As a follow up to this work, six validation meetings are carried out with selected local authorities annually. The financial indicators measured and reported on by NOAC include Revenue Collection Rates: Collection Levels of Commercial Rates, Collection Levels of Rent and Annuities and Collection Levels of Housing Loans.

The NOAC's statutory functions are wide, and specifically the Commission is required to:

- Scrutinise performance of any local government body against relevant indicators as selected by NOAC (to include customer service) or as prescribed in Ministerial regulations;
- Scrutinise financial performance, including Value for Money, of any local government body in respect of its financial resources;
- Support best practice (development and enhancement) in the performance of their functions by local government bodies;
- Monitor and evaluate adherence to Service Level Agreements entered into by any local government body;
- Oversee how national local government policy is implemented by local government bodies;

PEER REVIEW FINDINGS

– Monitor and evaluate public service reform implementation by any local government body or generally;

– Monitor adequacy of corporate plans prepared by Regional Assemblies and councils and evaluate implementation of the plans by any local government body or generally;

– Take steps under its other functions for the purpose of producing any report requested under the Act as well as produce reports under its own initiative; and

– Carry out any additional functions conferred by Ministerial order.

Approach and Objectives of NOAC. In implementing its mandate NOAC aims to:

– Be established in its role and have forged a working relationship with its stakeholders, including the Department of Housing, Local Government and Heritage, the Chief Executives and elected members of the local authorities;

– Conduct evidence-based scrutiny that delivers quality, objective, balanced and relevant reports, which will afford the local government sector the opportunity to improve its performance, enhance the existing culture of continuous improvement and embed best practice within the system as a whole;

– Add value to the local government sector and provide recommendations to build on the efficiencies and savings delivered by the sector to date, with a focus on customer service and cost effectiveness;

– Establish a collaborative approach with the relevant bodies and agencies at the heart of NOAC's work;

– Identify and focus upon those aspects of local authority functions and activities that are important to the citizen/customer;

– Facilitate engagement around improved performance; and

– Monitor the adequacy of local authority corporate plans and assess how well these are being implemented.

Key activities of NOAC include Performance Indicators, Corporate Plans, Public Spending Code and the Scrutiny Programme/Profile Meetings. The majority of NOAC's work is carried out by a number of working-groups, set up to focus on particular areas and to further various projects. Other work of NOAC is carried out directly by the Chair. NOAC's secretariat and ancillary services are provided by the Department of Housing, Local Government and Heritage. NOAC's operations are, however, independent, as required by legislation.

The Working Groups of NOAC consist of the board members and are supported in their work by the Secretariat

1. **Local Government Governance, Efficiency and Reform (Working Group 1**). Its role is to assist in NOAC's functions under section 126C (1) (d), (e), (f) and (g) of the Local Government Reform Act 2014. Specifically, the working group would:

– Monitor and evaluate adherence to any agreement in the nature of a service level agreement entered into by one or more local government bodies;

– Oversee how national policy in relation to local government is implemented by local government bodies;

– Monitor and evaluate the implementation of public service reform by local government bodies; and

– Monitor the adequacy of the corporate plan prepared by a Regional Assembly and by a Council.

2. **Performance Indicators (Working Group 2).** Its role is to oversee the production of an annual report on local authority performance indicators. Its work mainly relates to section 126C of the Local Government Reform Act 2014 and includes reviewing the performance indicators and appropriate guidance for local authorities, determining the verification process that should be applied to the submitted data and drafting NOAC's commentary on the compiled data, as well as any follow-up functions that may be required. This data can be used to compare and contrast performance and is key in producing the individual Scrutiny Reports of Local Authorities.

3. **Communications and Customer Survey (Working Group 3).** Its role is to carry out NOAC's functions under section 126C (1) (a) of the Local Government Reform Act 2014. That is, to scrutinise local authority performance against relevant indicators that relate to customer service and under section 126C (1) (c) to support the development and enhancement of best practice. The group is committed to delivering on the activities or functions that should be the subject of surveys and also develops requests for proposals, reviews and questionnaires. Additionally, it interacts with external stakeholders, in particular, through its branding and communication such as through the Good Practice Seminar which is held annually.

4. **Financial Management and Performance (Working group 4)**. Its role is to:

– Scrutinise financial performance including relating to value for money,

– To oversee how national policy in relation to local government is implemented by local government bodies, and

– To monitor and evaluate the implementation of public service reform by local government bodies.

– Additionally, the group collates and prepares the annual Local Government Quality Assurance Report under the Public Spending Code. The Public Spending Code was developed by the Department of Public Expenditure and Reform and it applies to all public bodies in receipt of public funds and ensures that the best possible value for money is obtained whenever public money is being spent or invested.

Scrutiny meetings with Local Authorities. As well as its standard work in relation to publishing a variety of reports on local authority activity and service delivery, in 2017 NOAC commenced compiling profiles of each local authority. These profiles are based primarily on the material in NOAC's own reports to date and meetings with the Chief Executives, but also include information provided by the authorities themselves outlining the particular context within which they each operate. Following these profile meetings, the Chief Executive and management team attend a full NOAC board meeting to answer questions from NOAC members on topics such as finances, customer service, corporate planning, housing issues, performance indicators, tourism initiatives, employment within the county and, economic and community development.

PEER REVIEW FINDINGS

Priority area 5 The framework for consultation between central and local authorities

A Council for Decentralisation of State Governance (CDSG) was created in 2013 as a platform for consultation in which central and local authorities are equally represented; the secretariat is hosted by the MoRDPW. In principle all the national policies with impact on decentralisation would be discussed in this forum. In parallel, the association of municipalities (NAMRB) holds formal and informal consultations with the central authorities and publishes analytic pieces and reports. However, the framework is mostly formal, since the CDSG seems to have very little visibility and has not held any meetings lately. Line ministries seem to adopt regulations in their sector with little consultation and not sufficiently communicated.

RECOMMENDATIONS FOR ACTION

- The CDSG is worth being reactivated and strengthened; the inclusion of citizens' representatives as observers may increase its visibility and relevance. This forum would provide the space where all major policy measure with impact at the local level are presented and debated before final decisions are taken. This would not only increase the transparency and trust in the system, but also would stabilise expectations by making clear for all stakeholders what the intended course of action over the medium and long term should be.
- To better formalise the activity of CDSG, a calendar of meetings and tentative thematic agenda may be decided and published for the year ahead, in connection with the government's announced legislative agenda.
- A special working group may be formed within CDSG to work specifically on budget issues, with more frequent meetings and in close contact with the MoF. This working group will publish a written opinion on the draft state budget, focusing on the components with impact on local finance.
- Another working group may be created, including the technical staff of NAMRB, to work with the MoF on the development of the database mentioned above in Priority area 4. The structure of working groups can be developed in time, as more experience accumulates; the case of Ireland shows how sophisticated such an arrangement can be.

Examples in Peers Member States

FINLAND: THE NEGOTIATION PROCESS BETWEEN CENTRAL AND LOCAL LEVELS

Serious efforts have been made in recent decades on improving the negotiation process between local and central levels. The Ministry of Finance plays a key role in arranging meetings between the Association of Municipalities and the different ministries. The two main bodies involved in the process are the Advisory Committee and the Working Group for preparing the Programme for Local Government Finances.

The Advisory Committee includes representatives of the Ministry of Finance, Ministry of Social and Health Affairs, Ministry of Education and Culture and the Association of Municipalities, which is the legal representative of the local sector. The Committee is in charge with:

- In the preparation phase, development plans and legislative projects concerning the finances and administration of municipalities;
- The state budget proposal from the parts concerning municipal finances;
- Government proposals regarding the finances and administration of municipalities before their consideration in the Government Council;
- Cost sharing arrangements between the state and municipalities;
- Other significant matters concerning the finances and administration of municipalities.

The Working Group for preparing the Programme for Local Finances includes experts from the same organisations, plus some other ministries which have responsibilities with impact on municipalities. Twice a year, this working group prepares a report listing the measures concerning municipalities and their financial effect on municipalities. There is also an assessment of the financial status of municipalities and how their position in this respect has changed since the previous report. The last part consists of a forecast, based on the general economic trends, showing what developments are to be expected in different types of municipalities, by size (under 2000 inhabitants; 2000-6000, 6000-10k, 10-20k, 20-40k, 40-100k, over 100k). The calculations show what is likely to happen with the local tax revenues and the municipal debts, and thus assist the local authorities with information and guidance for preventive measures.

The report itself is usually 70 pages long and published as a part of the state budget. It is useful reference for municipalities: the macro and micro economic data helps them in their own budget planning and approval. The weak point of the report is that the forecasts are not sufficiently detailed to capture the full range of variations between the local situations, as it deals only with categories of municipalities. The intention is to have individual forecasts for each municipality in the future. There has also been a permanent preoccupation to make this report more reader-friendly, with more intuitive pictures and tables, because one of its main goals is to allow comparisons over time, flag changes and reflect on their causes. The spring version is usually published in March and the autumn version in October. The following link leads to the programme pages: it is mostly in Finnish, with a brief English summary. The Power Point set gives a flavour of what type of graphs are used https://vm.fi/kuntatalousohjelma

PEER REVIEW FINDINGS

Finnish Local Government Act: Chapter 3, Relationship between central and local government

Section 10 Monitoring municipalities and oversight of legality

(1) The Ministry of Finance shall monitor the activities and finances of municipalities in general and ensure that their self-governing status is taken into account whenever legislation concerning local government is drafted.

(2) If a complaint on the grounds of procedural error is made, the Regional State Administrative Agency may investigate whether the municipality has acted in accordance with legislation in force.

Section 11 Negotiation process between central and local government

(1) The negotiation process between central and local government shall consider the legislation on local government, central government measures that are far-reaching and important in principle concerning the activities, finances and administration of local government, and the coordination of central and local government finances, as laid down in sections 12 and 13. In the negotiation process the municipalities shall be represented by the Association of Finnish Local and Regional Authorities.

Section 12 Programme for local government finances

(1) A programme for local government finances shall be prepared as part of the negotiation process between central and local government. Preparation of the programme for local government finances shall form part of the preparatory work for the general government fiscal plan and the central government's budget proposal.

(2) The programme for local government finances shall include the part of the general government fiscal plan that deals with local government finances. Provisions on the general government fiscal plan are laid down in and under the Act on the Implementation of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union and on Multi-annual Budgetary Frameworks.

(3) The programme for local government finances shall include an assessment of the adequacy of funding for meeting the duties of municipalities (principle of adequate financial resources). The programme shall contain an assessment of changes in the municipalities' operating environment and demand for services, and in the functions of local government, and shall provide an estimate of the trend in local government finances. Local government finances shall be assessed as a whole, as part of general government finances and in terms of different groups of municipalities. The assessment shall distinguish between the statutory and other functions of municipalities and shall assess the cost-effectiveness of the activities of municipalities.

(4) An assessment of the trend in local government finances and of the impact of the central government's budget on local government finances shall be made in connection with the central government's budget proposal.

(5) The programme for local government finances shall be prepared by the Ministry of Finance together with the Ministry of Social Affairs and Health, the Ministry of Education and Culture, the Ministry of the Environment, the Ministry of Transport and Communications, the Ministry of Employment and the Economy and, if necessary, other ministries. The economic forecasts and the assessment of the trend in local government finances, which form the basis for the programme for local government finances, shall be prepared by the Ministry of Finance. The Association of Finnish Local and Regional Authorities shall participate in the preparation of the programme for local government finances.

Section 13 Advisory Committee on Local Government Finances and Administration

(1) The negotiation process between central and local government shall include consideration of matters concerning the activities, finances and administration of local government by the Advisory Committee on Local Government Finances and Administration, which operates in conjunction with the Ministry of Finance.

(2) The Advisory Committee's task shall be to monitor and assess the trend in local government finances, and ensure that the programme for local government finances is taken into account in the drafting of legislation and decisions concerning local government. Provisions on the more detailed tasks of the Advisory Committee and its composition and sub-committees shall be laid down by government decree.

IRELAND: CO-OPERATION AND COMMUNICATION BETWEEN CENTRE AND LOCAL GOVERNMENT. A COMPLEX STRUCTURE

The Inter-Ministry Level; the Interdepartmental Group on Local Government. The programme for government – Our Shared Future states a commitment to making local government stronger, more accountable and more responsive to the communities it serves. This builds on previous programmes for government which contained ambitions to identify potential measures to boost local government leadership and accountability including commitments to ensure that local government funding, structures and responsibilities strengthen local democracy and, consider devolution of new powers to local authorities.

As part of its local government remit, the Department of Housing, Local Government and Heritage has responsibility for policy, legislation, Oireachtas (parliament) accountability and, at a broad level, oversight, in respect of the operation and administration of the local government system. As part of its other policy functions, it also has lead policy responsibility in relation to a number of specific functional or service areas such as planning, housing and fire services.

The Department of Housing, Local Government and Heritage established in late 2022, an Interdepartmental Group on Local Government as a first step in realising the commitments of the Programme for Government by raising awareness across all Government Departments of the independence of the sector, the role the sector plays in delivering services to the citizen, and how each central Department interacts with the sector.

The Interdepartmental Group on Local Government aims to:

- Secure a "whole-of-government" awareness of the local government sector and how it can support the formation and delivery of national policy.
- Create a "whole-of-government" approach to the formation of national policy and its impact on local government.
- Establish a framework for a cross-government approach to service delivery at local level.
- Secure a common approach to budgets, costs and targeting of resources.

In particular, this group will examine ways to build a stronger interdepartmental perspective and more joined-up approaches with other Departments in matters relating to Local Government, and bring about a greater understanding across all of Government of the complexities and challenges faced by local authorities and how best to support the sector in managing the challenges. The group has initially focussed on current and future demands on the local government sector and the structures and requirements that are in place to manage the delivery, staff resources and funding of services.

PEER REVIEW FINDINGS

The Relationship between Department of Housing Local Government and Heritage (DHLGH) and the Department of Public Expenditure and Reform (DPER). The Local Government Finance section in the DHLGH has a close working relationship with the relevant vote team in the DPER. Each Government Department has an assigned team in DPER to deal with funding issues and the annual estimates process. This working relationship involves the DHLGH's vote team in DPER monitoring proposals going to Government that relate to local authority functions and services from other Government Departments, and alerting the DHLGH to same. The DHLGH vote team in DPER engages with the relevant vote teams within their Department and the DHLGH engages with the proposing Government Departments regarding the funding of additional functions and services. The engagement revolves around funding arrangements and the principal that additional service provision incurs additional costs which the local authorities should not bear from their own resources. This working relationship has prevented local authorities from being required to fund significant proposals from the Department of Environment, Climate and Communications in 2022, with that Department subsequently revising the funding models for their proposals.

The County And City Management Association (CCMA). This is the 'representative voice' of the local government management network. The CCMA operates through a number of established committees, each of which is concerned with a specific policy area: Housing, Building and Land Use Committee; Climate Action, Transport, Circular Economy and Networks Committee; Rural Development, Community, Culture and Heritage Committee; Business, Tourism, Enterprise, Innovation And Urban/Town Economic Renewal Committee; Water, Environment and Emergency Planning Committee; Finance Committee; Corporate Committee. Each Committee is made up of county and city council chief executives and directors of service / heads of finance. The committee interfaces with government departments and other relevant organisations.

The CCMA represents its members on external committees, policy steering/working groups and organisations, develops evidence-based positions and makes submissions on relevant issues. The strategic objectives of the CCMA are set by the CCMA Executive - an eight-member committee comprising of the CCMA Chair, Vice Chair, Chief Executive of Dublin City Council, Chief Executive of Cork County Council and four elected chief executive members. They are influenced by the economic, political and legislative environment in which the CCMA operates, and their objectives are to:

- Influence and shape emerging and future policy affecting local government through direct engagement with key stakeholders on a range of diverse subjects.
- Advocate on behalf of the system for necessary resources, identify strategic choices to be made in the allocations of resources and demonstrate the system's capability to ensure the provision of value for money.
- Develop and present an accurate and positive view of the worth of local authorities in the public domain by building an understanding of the broad range of work that local authorities are involved in and the issues that drive and influence it.
- Demonstrate evidence of best practice and innovation within the sector for the purpose of supporting the wider development of such practices for example in the areas of shared service and procurement.
- Support individual members of the CCMA.
- Ensure that the public sector reform agenda is pursued and has a measurable positive impact.

The CCMA Executive leads on key issues to be tackled – mainly high-level issues, which shape the agenda of the CCMA and the six committees. Through the committee structure, the CCMA evaluates and disseminates the impact of specific policy measures on the local authority sector. This informs and influences the position adopted by the Association. The CCMA works in partnership with central government departments and agencies to develop and implement effective, streamlined legislation. As representatives of management of local authorities, the CCMA are key stakeholders in the areas of planning, the provision of infrastructure, housing, environment and sanitary services as well as recreational, social inclusion and cultural and tourism services and as such are consulted with by a broad spectrum of organisations. CCMA identifies, shares and publicises good practice with relevant stakeholders through submissions to Government, the development and promotion of material on the work of local authorities, internal communications and media communications. In 2021, there were 57 CCMA submissions made to 19 different government departments or agencies.

Examples of work of CCMA Committees:

- Agricultural inspections – engagement underway on potential funding from Department of Agriculture, Food and the Marine (DAFM) for measures to be carried out at farm level, which will result in an improvement in water quality.
- Local Authority Vets – discussions are ongoing regarding the potential transfer of Local Authority vets and services (except for Control of Dogs) to the DAFM.
- Supporting the development of a National Waste Management Plan for a Circular Economy.
- Supporting the development of Codes of Practice for CCTV and Mobile Recording Devices.
- Working with Department of Environment Climate and Communications on the Community Climate Action Fund and related Posts.
- Reimagining Transport' – final document being developed by Working Group to assist Local Authorities with decarbonising fleet and meet lower emission targets.
- Supporting the Roll-out of National Broadband Plan.
- Road Safety Strategy – Prioritising Sectoral Actions.
- Progression of Action 19 Night-Time Economy Taskforce Report to establish Pilot NTE areas across the sector.
- Focus on 'Town Centre First Policy' to progress key actions, sign off and approval for TROs in 26 areas, extensive engagement with the Departments of Housing Local Government and Heritage and Rural and Community Development.
- Engagement and collaboration with the Department of Enterprise, Trade and Employment (DETE) re Local Enterprise Office Steering Group, Strategic Working Group.
- Lead for National Steering Group on Economic Opportunities for Climate Action.

The Local Government Management Agency. This is a state agency established in 2012 under an establishment order to have an oversight and management role on the reform agenda of local government. It is an agency of the Department of Housing, Local Government and Heritage, primarily funded by local authorities. It provides a range of professional services to local authorities, working collaboratively with all 31 local authorities to support the coordinated and cost-effective delivery of local government services and policy. It also helps local authorities to implement change and enhance performance. It has implemented over 41 projects, mainly on a shared services basis to enhance the efficient and effective delivery of local government services.

Priority area 6 The public communication of local budgets: public participation

Civic organisations and even some representatives of local authorities have repeatedly signalled that the level of knowledge among the wider public about local budget and finance is low. This in turn limits the citizens' participation in community affairs. One cause of this is the technical format in which local budgets are discussed in the council, which makes them hard to understand for the layperson. Another is the uncertain calendar of public consultations on local finance (see Priority area 5) and the short interval of time in which the draft budgets are available for consultation every year.

The inadequate format of local budget presentation for public debate represents a clear departure from the provision of the CoE CM/Rec(2022)2 which says that "*all information provided for the purpose of scrutiny should be made available in a format that is accessible and relevant to those for whom it is intended*".

RECOMMENDATIONS FOR ACTION

- Better instruments can be created to the facilitate the understanding of the main issues and trade-offs incorporated in a budget, and the citizens' participation in the budget consultation process. Various formats of "Budget for Citizens" (BfC) exist, from the simplest to the more sophisticated and interactive, to stimulate this process of public participation, reviving and scaling up an older initiative under OGP[15]. The Irish example below is an illustration of how public participation can be institutionalized.
- It is advisable that both the central and local authorities are involved in the process, with the MoF offering examples of good practice. The process of developing BfCs can advance in steps, from simple to more complex, and the task for preparing them should be carefully planned in terms of staffing and timing, in the central and local government.
- Simple budget summaries in attractive layout, published to inform the consultation process, can be the starting point for the BfC initiative. In the second step, the incorporation of physical indicators allows the calculation of unit costs for various municipal services, and their evolution in time. This is a prerequisite for moving towards program budgeting, as implied by art 33 of CM/Rec(2004)1: "*the central authority should ensure that arrangements are made for drawing up comparisons of budgets and performance for local or regional authorities of comparable size and socio-economic characteristics that are widely accessible (through publications or Internet site postings) and accompanied by explanatory texts (such as the meaning of indicators used, etc).*"
- Finally, interactive products could be created (gamification) to broaden the appeal of budget consultations and involve a large number of citizens in them with minimal cost. CDSG and NAMRB may set up a small expert unit of BfC to explore the international best practice and adapt in Bulgaria appropriate models to be offered to municipalities.

15. https://www.opengovpartnership.org/members/bulgaria/commitments/BG0059/

PEER REVIEW FINDINGS

Examples in Peers Member States

IRELAND: FORMS OF PUBLIC PARTICIPATION OF CITIZENS

The 2014 Report of the Working Group Report on Citizen Engagement with Local Government recommended the establishment of Public Participation Networks (PPNs) in each of the 31 Local Authority areas.[16] PPNs were established following the enactment of the Local Government Reform Act 2014, section 46 of which sets out the legislative basis for PPN.

A Public Participation Network (PPN) provides representation for the community sector in Local Authority policy-making structures, giving local volunteers a greater say in local government decisions which affect their own communities. Membership of a PPN is open to all volunteer-led/not-for-profit groups in a local authority area, and over 18,000 groups nationwide are currently members of a PPN. PPNs have three key functions and areas of activity:

– facilitate participation and representation in policy and decision-making fora;

– build the capacity of member groups to carry out this role; and

– serve as a networking and information hub for member groups in their area.

The main way in which PPNs facilitate participation in local democracy is through the nomination and election of representatives on to Local Authority Committees and Boards. The most recent Annual PPN Report indicated that 1,013 PPN representatives sat on 397 local authority Boards and Committees in 2021.[17]

Where community representation is required on local authority committees, such as Strategic Policy Committees or Local Community Development Committees etc, it must be sourced through the PPN. PPNs also act as networking and information hubs for local volunteer-run groups. They keep the community informed of relevant local issues, events and supports through regular newsletters and events. They also provide space for community groups to grow and develop through training on topics such as governance, social media, communications, and specific policy issues.

16. Working Group Report on Citizen Engagement with Local Government.
17. Public Participation Networks, Annual Report 2021.

CONCLUSIONS

The peer review mission found that the Bulgarian authorities are determined to continue the decentralisation process and strengthen the local governance, which is reflected in the Strategy of Decentralisation 2015-2025, updated in 2021. MoF and MoRDPW are the main central actors guiding this effort, in two important directions: to improve the system of local and finance; and at the same time develop better mechanisms of accountability and performance measurement.

The reality is more complex and nuanced than the Strategy. However, outdated legal provisions about local taxes and the increasing importance of central financial transfers made the country look in some respects more centralised than it was a decade and a half ago, even though the total pool of resources available have increased at all levels. The main problems are the narrow margin of decision at the local level and a relatively low public participation in debates over the budgets. A more sophisticated system of data collection and processing is necessary to inform the policy decisions at the centre, but also in order to stimulate more meaningful public discussions about the municipal finance and services.

The peer review mission summarised the findings, opinions and conclusions after the meetings in the form of six priority areas, offering recommendations for action for each of them. The areas are obviously inter-related: improving the local own tax base (1) would naturally reduce the pressure on central transfers and the equalisation mechanism (2), while making the latter more predictable, simpler and non-conditional would encourage significantly the local fiscal effort and thus boost collection from the local taxation.

A more stable and rule-based allocation of central transfers goes hand in hand with opening up the database of indicators (4) and the decision-making process towards the local authorities, the civil society and the public at large. All these changes need to be operated following a proper process of consultation with the local stakeholders and the public (5), which is conditional upon the development of innovative and user-friendly instruments to communicate local budgets to the wider public.

The CEGG remains committed to provide assistance and advice to the central and local authorities, by deploying its menu of tools, on all these directions of action aimed at strengthening the good democratic governance in Bulgaria.

ANNEXES

ANNEX 1. Institutions and organisations met by the Peer Review Team

25/09/2023	Ministry of the Regional Development and Public Works (MoRDPW)
	Ministry of Finance (MoF)
26/09/2023	Municipality of Samokov: Mayor, deputy mayor
	National Association of the Municipalities in Republic of Bulgaria (NAMRB)
	Citizen Participation Forum (CPF)
27/09/2023	Foundation for Local Government Reform (FLGR) and NAMRB
	Debriefing with MoRDPW, MoF, NAMRB, FLGR and CPF

ANNEX 2. Policy areas and questions identified by the MRDPW prior the Peer Review visit

A. Fiscal autonomy and financial equalisation

– Improvements and legislative changes to fiscal autonomy / fiscal decentralisation – including the four NAMRB proposals for a new financing model.

– Examples of good practice from Council of Europe member States that grant more fiscal autonomy while ensuring efficient use of locally available funds and addressing territorial inequalities.

– Lessons to be learned from reforms to tax system / revenue sharing / fiscal equalisation framework and the impact on local autonomy, equity and fairness?

– How does Bulgaria's local government equalisation system compare to other States – revenue equalisation; expenditure-needs based; fiscal-gap based?

– How can the allocation mechanisms of grants, transfers and subsidies be improved to ensure provision of basic services at local level while ensuring more financial autonomy of municipalities as well as fiscal equity between municipalities?

– What lessons can be learned from recent territorial administrative reforms in Europe to help improve fiscal decentralisation and financial management?

B. Multi-level governance

– How can the repartition of expenditure functions between central and local authorities in Bulgaria be improved?

– How can cooperation be improved between central local authorities in determining expenditure needs?

– What measures exist to ensure accountability mechanisms at municipal level and increase transparency, participation and inclusion?

– What are the key parameters / guidelines for effective fiscal planning and reporting, investment planning, accounting, and auditing of local finances?

– What options are available to address differences in service performance?

ANNEX 3. Basis for a sequenced roadmap to support the decentralisation reform process across all levels of government

Following the Peer review report, the Ministry of Regional Development and Public Works requested to establish a concise and sequenced roadmap that delineates the key steps and milestones which will serve as the foundation for guiding and supporting the decentralisation reform process across all levels of government. This roadmap would aim at providing a systematic and organised approach to ensure effective implementation and successful outcomes in the decentralisation initiatives, and it will be agreed with the MoRDPW. The roadmap should include the measures listed below:

PRIORITY 1: The Local Tax Base

1. Under-Exploited Own Tax Base:

Recommendation: Review and update property assessment values, consider taxing agricultural land, and transform the municipal business tax into a real tax (applied to profit or turnover).

Measures to be included in the roadmap:

What measures can be realistically taken to address legal provisions, exemptions, and tight regulations affecting local taxes?

PRIORITY 2: Transfers, Equalisation

2. Task-Based Transfers and Equalization Mechanism:

Recommendation: Explore alternative models of tax sharing and non-conditional grants to increase local budgetary autonomy. Improve the predictability and stability of inter-governmental transfers.

Measures to be included in the roadmap:

What measures can be taken to make inter-governmental finance more transparent and predictable?

PRIORITY 3: Competencies of Municipalities and Intermunicipal Cooperation

3. Review of Competencies and Cooperation:

Recommendation: Thoroughly review municipal functions, redefine attributions, consider alternative solutions for complex competencies, and enhance intermunicipal cooperation.

Measures to be included in the roadmap:

What measures can be taken to strengthen intermunicipal cooperation to increase the capacity and to assist weaker municipalities?

PRIORITY 4: Transparency, Data Collection and Performance Management in Local Budgeting

4. Central role of the Ministry of Regional Development and Public Works:

Recommendation: Enhance transparency through benchmarking in cooperation with NAMRB. Improve and develop a database combining financial and non-financial indicators to monitor municipal service performance in consultation with the Ministry of Finance.

Measures to be included in the roadmap:

What challenges may arise in incorporating weighted costs and performance indicators into the system?

What are the roles of the regional authorities and the civil society organisations?

PRIORITY 5: Support the decentralisation reform process across all levels of government

5. Effective coordination, monitoring and evaluation:

Recommendation: Establish an effective coordination, monitoring and evaluation mechanism for decentralisation and multilevel governance, possibly through a Council of Ministers' decree, where all levels of government are involved, and socio-economic partners and citizens' organisations are included.

Measures to be included in the roadmap:

What specific activities can be delegated to working groups, under the coordination, monitoring and evaluation mechanism, to contribute to budget issues and database development?

In this framework, explore the possibility to prepare periodically one main document at the national level as *Annual report on the state of decentralisation and multi-level governance in the country*, which is approved by the Council of Ministers and gives specific recommendations for improving the state in individual policy areas, including fiscal decentralisation and local financial management;

Keep the role of the Council for Decentralisation of State Governance (CDSG) as a consultative body at high political level to review and steer the decentralisation reform process.

PRIORITY 6: Public Communication of Local Budgets - Public Participation

6. Public Communication and Participation:

Recommendation: Create better instruments for understanding local budgets, facilitate citizens' participation through various formats of «Budget for Citizens» (BfC), and involve both central and local authorities in the process.

Measures to be included in the roadmap:

How can the government ensure that the development of BfCs involves both central and local authorities?

What steps can be taken to progressively advance from simple budget summaries to more complex and interactive products?

ANNEX 4. Recommendations formulated by the representatives of civil society organisations during the citizen consultation organised by CPF

1. Recommendations from civil society organisations to national institutions aimed at achieving a balance at the local level between responsibilities for service provision, decision-making rights, and resources to finance services:

– To carry out a review and analysis of the services provided at the local level and for the state to transfer to the municipalities those that meet the principle of subsidiarity (for example: municipal police, fire brigade, ambulance, etc.), and those that do not meet the criteria for "delegated" to switch to the local services group.

– To refine the equalisation subsidy by introducing more objective criteria to reduce financial differences between different municipalities.

– To increase the transparency of the information provided by the Ministry of Finance regarding the financial results of municipalities (income, expenses, prices of services provided), so that comparisons and analyses can be made by all who are interested.

– To organize information and media campaigns on the part of Ministry of Regional Development and Public Works to increase citizens' awareness and understanding of financial management at the local level.
– To adopt changes in the Law on Local Self-Government and Local Administration to broadcast the meetings of the Municipal Council online, to introduce a register of citizens' questions to municipal councillors, to increase the quality and efficiency of public consultations, as well as to expand the powers of village mayors with services, financial resources, development of public councils and fixing of the minimum population of a town hall (300 - 500 people).
– To adopt changes in the Electoral Code to introduce a majoritarian electoral system at the local level (except for Sofia, Plovdiv, and Varna).
– To adopt changes in the Personal Income Tax Act with the aim of ceding 20% of the tax to the municipalities.
– To adopt changes in the Law on Direct Participation of Citizens in State Power and Local Self-Government to ease the requirements for initiating and holding local referenda and introducing mandatory implementation of referendum decisions, as well as specifying the conditions for creating a new municipality or changing the borders of an existing municipality.

2. Recommendations from civil organisations to local authorities aimed at improving local democratic governance:

– To present the report and the project of the municipal budget in a language understandable and accessible to citizens - development and introduction of an appropriate format.
– To introduce municipal funds for financing civic initiatives in all municipalities.
– To work to increase the capacity and motivation of the local administration to work with citizens.
– To introduce tools and approaches to increase the quality and effectiveness of public consultations/discussions.
– To take steps to shift to a program budget.
– Discuss their plans and intentions with citizens and involve them in the development and implementation of local policies.
– To inform periodically the citizens about the municipal activities and the achieved results.
– To introduce appropriate forms for researching the needs of the population.
– To use the "Public Forum" approach to discuss topics and issues important to the public.

3. Recommendations to civil society organisations themselves, aiming to increase their role and participation in the decentralisation process:

– To work in close interaction with local communities to realize and recognize common interests and defend them within the law.
– To inform citizens about the powers and opportunities of local authorities to solve local problems and realize local priorities and interests.
– Research the needs of citizens and make efforts to include them together with the local government in discussions of the intentions and plans of the municipalities, as well as in the development and implementation of local policies.
– Monitor and analyse the activities of local authorities and exercise control over the expediency of spending funds from municipal budgets.
– To support and participate in initiatives for legislative changes aimed at providing more powers and resources to municipalities to solve local problems and to improve the quality of life of the citizens.
– To make efforts and look for appropriate means to improve the dialogue with the local authority.
– To initiate public forums and discussions on topics and issues important to local communities.
– Organize information campaigns, research, and disseminate good practices and actively participate in consultative bodies at local level.

ANNEX 5. Brief biographical notes about the participating experts and peers18

VIERI CERIANI, special adviser of EU Commissioner Paolo Gentiloni, was undersecretary of State at the Italian Ministry of Economy and Finance during the Monti Government (2011 - 2013) and an adviser of the Minister of Finance on tax policy issues (2013 - 2018). Vieri held the position of Chief Executive Officer of SOSE between 2016 and 2018, a company owned by the Ministry of Economy and active in the production of standard expenditure needs and equalisation systems for the Italian municipalities and provinces. In this capacity, he contributed to the development of a project with the Lithuanian government (financed by the European Commission - Structural Reform Support Service) for implementing a system of standard expenditure needs and equalisation grants for the Lithuanian municipalities. As Council of Europe international experts, Vieri is active in projects on fiscal decentralisation and good governance in Armenia and now in Bulgaria.

SORIN IONIŢĂ is president of the Bucharest-based think tank Expert Forum, doing advocacy and analysis on good governance and EU issues in Eastern Europe. He is an expert in Public Administration Reform and Development; consultant with the European Commission on anti-corruption, the Council of Europe (current activities in Finland, Ukraine and Hungary), the World Bank, the United Nations Development Programme on Eastern Europe and the Balkans; former civil society representative in the European Economic and Social Committee (EESC, on Transport-Energy and Environment). Sorin is also an associate lecturer at Maastricht School of Management (MSM) and Babeş-Bolyai University (Cluj). Frequent guest in current affairs news programs on TV and radio, and a blogger, he graduated from the Bucharest Polytechnic School (IPB); Bucharest University (UB); Central European University (CEU). He has a PhD in Political Science and was a Fulbright fellow at Georgetown University, Washington DC.

MARKKU MÖLLÄRI is currently Ministerial Adviser in the Ministry of Finance of Finland, leader of the International Affairs Team in the Department for Local Government and responsible to work in the NGO negotiation board. Markku has been member of the Council of Europe European Committee on Democracy and Governance several years with different functions: he chaired the Committee, the Local economic crisis 2008 working group, and is currently chairing the *Green public administration* working group. In the OECD, he belongs to the *Fiscal network changing ideas of tax policies in regional and local level*, and he has been preparing the reports on the COVID-19 effects on local level and between governments in the CoE and OECD. In Finland, Markku has been working with questions on municipal structure, economy, and democracy. With over 10 years' experience in Finnishmunicipal economy crisis procedure for municipalities in severe difficulties, Markku has also been reforming the Local Government Act, introducing the Governmental policy on administration reforms and tax and state grant systems, and worked in updating the current data systems in local economy and basic service indicators. Markku is also member of national boards for *Young people's involvement*, the board for *Services for disabled people* and the *National languages network*. He holds a master's degree on Economics and on Philosophy.

18. In alphabetical order.

TÂNIA MOURATO is the Director of the Department of Cooperation and Financial Affairs of the General Directorate of Local Authorities in Portugal since 2020. The directorate is responsible for calculating and processing transfers from the State Budget to local authorities, monitoring the economic-financial management of the local administration and the application of the current accounting system and monitoring the process of decentralisation of powers from central administration to local administration. Prior to this, Tânia was the Head of Division of Human Resources, Training and Intermunicipal Projects/Public Policies, in the Intermunicipal Community of the West Region, with responsibility for developing intermunicipal applications for European funds and their implementation and between 2009-2013 she was Deputy Mayor of the City Council in Arruda dos Vinhos. She received a master's degree in Political Science and was a postgraduate in Municipal Management and Public Financial Management.

SINÉAD O'GORMAN has responsibility for the Local Government Finance Unit in the Department of Housing, Local Government and Heritage of Ireland. This unit seeks to ensure that the finances of local authorities are on a sustainable footing and that the local government sector has an appropriately structured funding system to meet existing and emerging challenges. This includes management of the Local Property Tax allocations, the Local Government Fund and Commercial Rates policy. The unit also has responsibility for the local government accounting framework. Sinéad has worked in this area since 2018, progressing legislation to modernise the commercial rates system in 2019 and undertaking a review of baseline funding of local authorities in 2023 to inform the revised allocation of local property tax in 2024. Sinéad devised the COVID commercial rates waiver scheme which provided support to business and financial certainty to local authorities from 2020 to 2022. Prior to this, Sinéad worked in a local authority for 10 years.

ARTAK YERGENYAN is an expert on legal and policy advice in the areas of local government, decentralisation, good democratic governance, public administration and territorial-administrative reform in the "*Democratic Development, Decentralisation and Good Governance in Armenia – Phase II*" Project. In close cooperation with international and local experts, Artak had the opportunity to author laws on "*Local duties and payments*", "*Local self-government*" and "*Administrative division*", which are currently operating in Armenia. He developed the draft laws on: "*Financial equalisation*", "*Hotel tax*", "*Powers of Public Authorities and Fiscal decentralisation*", "*Providing Subventions to Communities from state budget*", and studies such as: "*Assessment of the current state of mandatory funding decentralised powers in Armenia*", "*Comprehensive strategy for fiscal decentralisation and the resulting financial equalisation in Armenia*", "*Comprehensive strategy on new policy of providing grants, subventions and loans to communities from state budget*".

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