

Creating a Financial Framework

Volume 1: Financial Policy Making
Financial Planning
Citizen Participation
Evaluating Financial Condition

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ISBN

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Preface

The original Local Government Financial Management (LGFM) series was conceived in the mid-nineteen nineties in Lucenec, in Eastern Slovakia. The United States Agency for International Development (USAID), through a contract with the International City/County Management Association (ICMA), had initiated a local government capacity building programme in Slovakia and financial management was one of the areas targeted for development.

When the City of Lucenec was approached as a potential recipient of technical assistance for the specific purpose of developing a capital improvement budget, they were grateful but not impressed. They saw the need for financial management assistance for the local government and others in Slovakia in much broader terms. Working with a group of dedicated local finance officers in Slovakia, ICMA assembled a small team of LGFM consultants. Together they produced the initial fourteen handbooks in this series.

Over time, the series spread quickly to other counties in the central and eastern European region and beyond. Funding for the adaptation and translation of the materials came from a variety of sources, including The World Bank and private foundations.

While UN-HABITAT had contributed to the initiation of the series, their involvement in the development and dissemination up to this point had been minimal. Nevertheless, they recognised the series' potential for worldwide use. But, they needed to be updated to reflect new ideas in LGFM and revised to make them more user friendly as they crossed national borders and language differences. Among other things, the initial series was based on Slovak laws, regulations, and experience, which varied significantly from those in other countries. UNHABITAT commissioned a written user survey and convened a small group of experts to help determine how best to carry out the revisionist task. The expert group included the Slovak initiators and others who had used the materials in various countries around the world.

While the initial edition of these materials was directed to Slovak local government finance officers, this edition is intended for a much larger audience. It includes not just finance officers but all local government financial management personnel as well as chief executive officers, department heads, elected officials whom we refer to as policy makers, and others in local governments worldwide who might find them useful. National government departments that have oversight responsibility for local finances should also find them useful as should those educational institutions preparing students for jobs within local governments. And, of course, the audience includes financial management trainers and training managers. In other words, this series is aimed at a worldwide mix of training providers and training users.

Kay Spearman
Principal Author

Acknowledgments

The preparation of this revised and updated version of the Local Government Financial Management (LGFM) Series has drawn upon the professionalism and expertise of many persons and institutions.

First, we would like to acknowledge the various authors, both of the original series and the current revision, of each respective chapter in the series. **Introduction and Trainer's Guide** written by Fred Fisher. **Chp 1: Policy Making.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Original essay by Jack Matzer. Original exercises by David Tees. **Chp 2: Financial Planning.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Original essay by Winston Evans. Original exercises by David Tees. **Chp 3: Citizen Participation.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Original essay by Winston Evans. Original exercises by David Tees. **Chp 4: Evaluating Financial Condition.** Original essay by Sanford Groves and Maureen Valente. Published by International City/County Management Association (1990 Washington DC). Exercises by Kay Spearman and Fred Fisher. **Chp 5: Operating Budget.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Original essay by Kay Spearman. Original exercises by David Tees. **Chp 6: Financing the Operating Budget.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Based on original essays by Winston Evans, Kay Spearman and Maureen Valente. Original exercises by David Tees. **Chp 7: Capital Investment Planning.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Based on original essays by Jack Matzer and Allistar Law. Original exercises by David Tees. **Chp 8: Financing the Capital Investment Plan.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Based on portions of original essays by Jack Matzer, Winston Evans and Allistar Law. Original exercises by David Tees. **Chp 9: Accounting.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Based on portions of original essays by Jack Matzer, Winston Evans and Kay Spearman. Original exercises by David Tees. **Chp 10: Performance Measures.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Original essay by Jack Matzer. Original exercises by David Tees. **Chp 11: Asset Management.** Written by Kay Spearman. Exercises by Kay Spearman and Fred Fisher. **Chp 12: Procurement.** Essay rewritten and expanded by Kay Spearman. Exercises rewritten by Kay Spearman and Fred Fisher. Based on original essays by Allistar Law. Original exercises by David Tees.

We also appreciate the participants of the User Survey that was carried out on the original LGFM Series. Their experiences and insights were instrumental in identifying gaps and shortcomings in the original series and thus shaping the content of the current series.

We recognise the input of the participants of the Expert Group Meeting (EGM) held in Kenya in early October 2002. Based on the findings of the User Survey, the EGM made recommendations for major changes, resulting in a more comprehensive, user-friendly and up-to-date series. In particular, we appreciate Fred Fisher of IDIOM, USA and Kay Spearman of Spearman, Welch & Associates, Inc., USA who were the principal facilitators of the EGM and who were both deeply involved in the production of the original series. We equally appreciate the expert input of the other participants, namely, Deborah Welch of Spearman, Welch & Associates, Inc., USA, Luba Vavrova of Local Government Assistance Centre, Slovakia, Eva Balazova of the City of Lucenec, Slovakia, Kristina Creosteanu of Partners Romania Foundation for Local Development, Romania, Galina Kurlyandskaya of Center for Fiscal Policy, Russia, Gangadhar Jha of the National Institute of Urban Affairs, India, Mudite Priede of the Union of Local and Regional Governments of Latvia, Latvia, Bulat Karibjanov of the Local Government Initiative, Kazakhstan, Jack Mbugua of the Nairobi City Council, Kenya, Justus Mika of the City of Gweru, Zimbabwe, Billow Abdi of the Ministry of Local Government, Kenya and Liibaan Hussein of the Burao Water Agency, Somalia.

This revised series underwent a world-wide peer review process. We are grateful to the following individuals and institutions for faithfully and judiciously reading through the various chapters of the series (within a rather tight time frame) and for their positive feedback and encouragement.

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Rafael Tuts
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How to Use This Series

This chapter and others in the series can be used in many ways by a variety of local government (LG) officials and officers, as well as those who want to provide training and consulting services to LGs and related organisations. To support this mix of potential users, each chapter, with the exception of the *Trainer's Guide*, includes two distinct parts. Part One includes a discussion of concepts, principles, and strategies associated with the specific topic covered in the chapter. Basic information is provided first. In the more technical chapters (*Accounting*, *Procurement*, *Financing the Operating Budget*, *Operating Budget* and *Financing the Capital Investment Plan*), Part One is divided into Basic and Advanced Concepts so that the reader or trainer can pick the most appropriate place to begin. Part One is supposed to have something for everyone—meet the needs of developing, developed, centralized, and decentralized countries. To meet this requirement, many of the chapters are divided into Basic and Advanced concepts. Our idea was that the Basic concepts would be for persons who had little or no understanding of the topic and the Advanced concepts were for those who already had a foundation. If we have erred in this balance, it has been to provide more basic information than advanced.

Part Two includes training or management tools that are primarily designed to support group learning. However, many of the exercises in Part Two can also be used to support self-study and, with some adaptation, can be turned into financial management tools to use on the job. Also, the ***Learning Applications*** provided in Part One can be easily modified for group exercises. In other words, this series is designed to be used in a variety of ways to meet the LG financial management learning needs of many audiences.

PART ONE: CONCEPTS, PRINCIPLES AND STRATEGIES

Part One of each chapter is designed to meet two needs. First, it has been written to encourage self learning by LG finance managers, their staff, elected officials, chief executive officers and department heads of LGs, and others who need to know more about specific functions important to LG financial management. To enhance the self-learning process we have inserted ***Learning Application*** exercises where we encourage you to stop for a moment and reflect on what you have been reading as it relates to your own work experience. Each learning application exercise is prefaced by a small box listing the four most important roles and responsibilities associated with LG financial management: the elected official; the chief executive officer (CEO); the finance manager; and the operating department managers. Readers are encouraged to use these reflective moments to think about the issues covered by the *Learning Application* from their own experience and perspective as elected or appointed officials.

Of course, readers are welcome to stop anytime to reflect on what they have read in terms of their own experience, so these are just friendly reminders of the importance of the financial management concepts, principles and strategies that have just been covered in the text. We also encourage readers to check out the training tools in Part Two of each chapter. Many lend themselves to individual learning moments as well.

The Part One essays are also designed to provide trainers, consultants, researchers, and others with in-depth information and ideas about specific roles, responsibilities and processes within LG financial management systems. While these essays are important resources for those who are developing group learning (training) programmes for their LG constituents, they can also be valuable resource guides for central government officials who may be responsible for monitoring LG financial transactions, or providing technical assistance to LGs.

PART TWO: THE MANAGEMENT TOOLS

The Part Two components in each of these chapters are targeted primarily to those individuals who are designing and conducting group-learning experiences in LG financial management. While the main recipients of the training will be LG officers who have financial management responsibilities, many of the chapter materials can also be tailored to work just as effectively with elected officials, chief executive officers (CEOs), operating department heads—such as public works, and others such as staff members of LG associations and public service research organisations.

Another feature of the tools in Part Two is the built-in encouragement for participants to incorporate their own work experiences as part of the learning event. We believe that professionals can and do learn a great deal from each other when given the opportunity. Since most of the tools are based on an interactive approach to learning, these value-added opportunities are not just available but encouraged.

While the training tools in each of the chapters have been organised in a sequence that could be used effectively in a workshop situation, trainers are encouraged to be creative in designing group-learning experiences based on these materials. For example, you can reorganise the various tools in each of the chapters, use some of your own designs, alter those we have included in the chapters so they are more suited for your learning audience, or even find something in a different chapter that might work better given your style of training and the participants' learning needs. ***And don't ignore the various Learning Application exercises that are included in Part One as potentially valuable training tools.*** We have highlighted this statement to draw your attention to this added-value reserve of group learning opportunities.

Finally, we want to remind the practitioners of LG financial management that a number of the tools we have included in the Part Two sections of these chapters can also be adapted for use as management tools. For example, they might be used to help develop policy positions for consideration by your governing body, or help a team of mid-managers to sharpen their skills in developing performance measures, or assist financial clerks to redesign the flow of financial documents within their work units.

A WORD ABOUT TERMINOLOGY

One of the challenges we have faced in developing this set of materials is the wide range of terms that are used in different parts of the world to describe LGs and the key roles associated with LG financial management. For example, LGs are called cities, towns, townships, counties, boroughs, regions, and other things depending on the country where they reside. Equally challenging are the names that are attached to the officials and officers. For example, elected officials are known as elected officials, legislators, councillors, supervisors, board members, or commissioners, to name some of the more common titles.

To reduce the potential for confusion among the readers and users of these chapters, we have decided to be consistent in our use of the most common terms that occur frequently through these chapters. In addition, we have included glossaries of technical terms to help users develop a common frame of reference about various financial processes when working together. Equally important, those who are given the task of **translating these chapters** into other languages can only be effective in this important task if there is consistency in the use of the more commonly used terms. We have highlighted the need for **translators** because they are unique users of these manuals and often come to the translating task with a limited knowledge of the technical aspects of financial management.

SEEKING COMMON GROUND AMONG KEY TERMS, WORDS, AND PHRASES

In the *Learning Application* exercises in Part One of each chapter we have identified four key LG roles that correspond to those individuals whom we consider to be the most important clients of these learning materials. They are: elected officials, chief executive officers (CEOs), finance managers, and department heads. Since these roles are given different names in LGs around the world, we have listed a few of the variations in the following discussion. Hopefully, this will clarify just who is included when we talk about elected officials, CEOs, finance managers, and department heads. We have also included a few more terms that can be problematic in writing for LG audiences.

Elected officials: We use this term to identify those individuals who are chosen, hopefully through a democratic election process, to represent the citizens of their respective LGs in the legislative/governing process. They are also referred to in different parts of the world as: ***policy makers,***^o ***legislators, councillors, supervisors, commissioners,*** and ***board members.*** You may also know them under some other name or term.

Chief executive officer (CEO): This term is used in these chapters to identify the individual who has the sole responsibility for making overall management or executive decisions that affect the whole LG organisation. The CEO position is complicated since it can be filled by either an elected official, i.e., a mayor, or an appointed official, i.e., a city manager. We don't make this distinction in our use of the term CEO. As just stated, the CEO might also hold one of the following titles depending on the country, local laws or tradition: ***mayor; chief administrative officer; city, township,***

town, borough or county manager; general manager, town clerk, or even *commissioner* if the executive powers are shared among several elected officials.

Finance manager: This term is used to identify those individuals within LGs who have significant financial responsibilities on a day-to-day basis. Since we want more than just the chief finance officer to use these chapters, we are deliberately including anyone within the LG who has supervisory responsibilities within the financial management domain. Depending on the location, these individuals might be known as: chief finance officer; director of finance; finance director; accounts manager; chief auditor; controller; and no doubt many more names or terms. We want all those individuals who have finance responsibilities in their LGs to benefit professionally from using these materials.

Department head: We believe the responsibilities for financial management in any LG do not end with those who occupy the roles just outlined. Their success in managing the financial affairs of the LG is also dependent on those individuals who manage the staff and operational units of their respective LGs. Since this term encompasses many different titles, often associated with the mandate of the operating department, we offer only a few as descriptive of who we have in mind. They might be: highway superintendent; water plant manager; director of human services; head nurse; chief mechanic; case work supervisor, or so on.

In addition to the four terms that are used most frequently in the chapters, translators and other users will benefit from what we mean by some other commonly used words or phrases. For example:

Governing or elected body: This is the collection of individuals elected to represent the citizens of your LG as policy makers, decision makers, and community leaders. Depending on where you are in the world, they might be known as the: *legislative body or council; political body; city, town, village, or county council; local parliament; board of commissioners; policy making body*; or some other name.

Local government (LG): LGs are called all sorts of things: *cities, towns, counties, municipalities, parishes, townships, villages, boroughs, regional governments*, and we suspect many other things, but hopefully, you get the picture. Usually, the common element is that they are the lowest self-governing unit of government in the country.

Executive branch: You might come across this term in these chapters, so here is what we had in mind. The executive branch of LG consists of all those departments that operate under the general management of the CEO, whether or not that individual is elected by the citizens, or appointed by the elected body, or some other appointing power.

Legislative branch: This branch of LG consists of the elected officials and their staff members if they have any. Supposedly, they are the *policy makers*, but that term is muddled since many people in LGs have a role in making policies, whether legitimately or through default. (If this statement raises your curiosity, we recommend you go immediately to *Financial Policy Making* and discover how this happens.)

Citizens: These are all of the residents of the LG, including women, and low-income persons. We also use the term community interchangeably. While we recognize different cultures may place a lower value or no value on the input of women and low-income persons in decision-making, our use of the term “citizen” throughout the

series is that it includes ALL residents of the LG and that women and low-income persons have an equal place at the decision-making table.

Annual budget: This is such a common term that we suspect many of you are shaking your head in wonderment. However, it does come in for some confusion and it is important to understand what the *annual budget* means in these discussions. The annual budget, as discussed in these chapters, is both the operating budget and the one-year capital budget based on the multi-year capital investment or improvement programme.

Capital investment plan: Sometimes called the *capital improvement programme*, or mistakenly the *capital budget*. That's why we made the distinction above. The capital budget is the one-year increment of all those long-term investment costs that is folded into the annual budget.

Hopefully, this lead-in to each of the chapters on how to use these materials will help in appreciating some of the subtle differences in who the clients are for the series and how they are referred to around the world.

There are additional resources for this series on the UN-Habitat website at <http://www.unchs.org/default.asp>.

Introduction

A BIT OF HISTORY

This Local Government Financial Management (LGFM) training series has a short but rich history. We believe it's worth relating to you for several reasons. First, many individuals and organisations contributed to its development, and now its redevelopment. They deserve to be recognised. Second, the redevelopment of the series was largely demand driven. Financial management and training professionals who saw the original set of chapters wanted them for use in their own countries. Consequently, they transported the old series across national borders from Slovakia to their own countries and ultimately created a demand for this new version. Finally, there are some lessons to be learned from the "redevelopment" of the original Slovak version of these training materials.

The original series was conceived in the mid-nineteen nineties in the office of Eva Balazova, the Finance Director of a small city, Lucenec, in Eastern Slovakia. The United States Agency for International Development (USAID), through a contract with the International City/County Management Association (ICMA), had initiated a local government capacity building programme in Slovakia and financial management was one of the areas targeted for development. The focus of the USAID assistance to Slovakia's local governments was initially the budget process; more specifically, the capital improvement budgeting process. Under the old centralised socialist approach to local governance there was no need for a capital budget. But the emergence of local self governments in Slovakia established the need for many new administrative and financial systems. Eva Balazova and her colleagues were sitting on a powder keg of potential change in how local governments could, and would, operate in the future.

When the City of Lucenec was approached as a potential recipient of technical assistance for the specific purpose of developing a capital improvement budget, Eva was grateful but not impressed. She saw the need for financial management assistance for her local government and others in Slovakia in much broader terms. Essentially, Eva was telling those who came with external assistance that the development needs for local government financial management were much more complex than just capital budgeting. Eva's insights and tenacity prevailed. Working through Eva and a cadre of other dedicated local finance officers in Slovakia, ICMA assembled a small team of LGFM consultants. Together they produced the initial series of these chapters.

End of story? Not quite. Word spread in the region that these training materials had been developed and had even been designed to make adaptation by other countries easier. For whatever reasons, neither USAID nor ICMA put the fourteen LGFM manuals on their websites so they could be accessed by others outside of

Slovakia. Fortunately, a small women-owned firm in Texas did. Kay Spearman, one of two principals of that private company and a member of the original ICMA technical assistance team who worked with the Slovak finance officers, became the linking pin. Once available, the series spread quickly to other counties in the central and eastern European region and beyond. Funding for the adaptation and translation of the materials came from a variety of sources, including The World Bank and private foundations.

While UN-HABITAT had contributed to the initiation of the series, their involvement in the development and dissemination up to this point had been minimal. Nevertheless, they recognised the series' potential for worldwide use. But, they needed to be updated to reflect new ideas in LGFM and revised to make them more user friendly as they crossed national borders and language differences. Among other things, the initial series was based on Slovak laws, regulations, and experience which varied significantly from those in other countries.¹ Not to be deterred, UN-HABITAT received permission from USAID to revise and republish the series. They commissioned a written user survey and convened a small group of experts to help determine how best to carry out the revisionist task. The expert group included the Slovak initiators and others who had used the materials in various countries around the world.

While it's a fascinating story of how international technical assistance often unfolds, there are a few lessons to be learned for those who will be using the new series.

1. Never under-estimate your own ability to make a difference.
2. Always challenge those who think they know more about what your training and development needs are than you do.
3. Never hesitate to step into a void that others may have created, regardless of their motives.
4. Be willing to take risks in adapting what was not invented in your own back yard.
5. Don't hesitate to help others even though there may not be anything in it for you at the time, or ever.
6. And remember, training and development is individual and organisation capacity building at its best when it is demand driven. Demand it for you, your colleagues, and your institutions.

OVERVIEW OF THE SERIES

With that short history lesson out of the way, it's time to look at what else you can expect from this chapter and the rest of the series. Among other things, you will learn about:

¹ UN-HABITAT has produced other region-specific manuals e.g. UNCHS (1991) *Training Manual on Urban Local Government for English-speaking East and Southern African Countries* and UNCHS (1991) *Training Manual on Urban Local Government Finance for South Asian Countries*.

- Why this set of training materials was developed in the first place and how it has changed.
- The expanded audience of potential users.
- Good governance principles and how they relate to LGFM.
- A revamped conceptual framework that more accurately reflects financial management reality.
- What each volume in the series will cover.
- How to get the most from the series.
- How not to be overwhelmed as either a trainer or user of this series.

COMPARING THE ORIGINAL SLOVAKIA LGFM SERIES WITH THIS SERIES

We want to share with you the original reasons for developing this series of local government financial management chapters. We also want to see if these initial reasons are still valid; if not, why not; and what we plan to do about it. There were at least three good reasons why this series was originally written.

First was the fundamental importance of financial management for the economic health and stability of local self-government in Slovakia and other countries. The effective management of any local government's financial affairs ranks among its most important functions. How well this function is carried out depends in large measure on knowledge of the discipline, ability to perform effectively, and ethical conduct of the finance manager.

This assumption still seems valid with one exception. It's not just the ethical conduct of the finance officer that is important. It's the ethical conduct of all local government employees, the elected governing body, and those they interact with in the community and beyond. Local government corruption almost always involves individuals and organisations outside the official local government family. Consequently effective, ethical LGFM involves more than just the finance manager.

Second was the concern that training materials for training finance managers had been developed in a piecemeal fashion. While many training components related to an efficient finance management system existed at the time, it would be difficult and probably impossible to integrate them into a coherent whole. A comprehensive approach to the development and packaging of materials was needed to help finance officers recognize and appreciate the scope and complexity of a fully functioning financial management system.

This assumption is still valid although we now see the importance of this series for more than just the development of the finance manager as was mentioned in the initial assumption. Very few development agencies or training institutions have taken as comprehensive an approach to developing a LGFM training curriculum as that taken in Slovakia in the mid-nineteen nineties. Nevertheless, the original series left room for considerable improvement. For example, the original version was based on topics, not the interrelated functions of LGFM. This is one of the key changes in this edition of the series. The new conceptual framework is designed to make the series more user-friendly and help users appreciate the interrelated and systemic nature of many of the LGFM functions. We will get into this later when we discuss the conceptual frame

work for this series. The other key change is to emphasize how LGFM concepts and practices are fundamental to implementing the widely accepted principles of good governance.

Third was the absence of a systematic LGFM professional development delivery system that relies on local training resources rather than outside expertise. Such a system would provide training materials in a format designed to facilitate local use by local trainers with no additional technical assistance required after initial field tests and training of trainers.

This assumption is still valid and this new series will, hopefully, make the delivery of the training just that much easier. In this regard, we have cleansed the series of its Slovak examples and bias recognising the need to make it a global resource. We have also expanded the learning audience to include more than just the finance manager.

The original series was designed with all these considerations in mind. It provided a comprehensive perspective on financial management by addressing the basic functions and skills required. It also adhered to the learning needs of the Slovak local government finance officers as they were defined at the time which was, of course, what the series was intended to accomplish. The curriculum design also mirrored earlier UN-HABITAT training packages, such as the Local Elected Leadership series, by providing concepts, principles, and strategies in Part 1 and workshop training designs in Part 2 of each discrete chapter.

As the Slovak finance officers used the original series of handbooks, they discovered that the topical sequencing of the materials was not particularly functional. Nor did the design of training based on the content of individual handbooks provide for optimum learning experiences. There was just too much inter-connectedness and overlap of the various topics to present them in their original format. So, the Slovak financial officers and trainers experimented by reorganising the content of the individual handbooks to mirror the reality of their work environment. When UN-HABITAT convened the experts to provide guidance in developing the new edition, the Slovak experience in experimenting with the content and design of the original series proved extremely valuable. We appreciate their contribution in helping to make a good training product just that more effective.

But, there was another experience of the Slovak finance officers group that needs to be mentioned as a spin off of their involvement in developing the series and using it as part of their profession's development in Slovakia. These finance officers, and they happened to be mostly women, saw an opportunity to influence the direction and the quality of local government financial policies and management practices at the national level of governance. To do this, they needed to be organised so they created the Association of Municipal Finance Officers of Slovakia. This professional association continues to be a driving force in helping define the role of local government finances as an integral part of the nation building process in that country. Never underestimate the importance of training as an integral part of larger institution and nation building strategies.

THE EXPANDED AUDIENCE OF USERS

While the initial edition of these materials was directed to Slovak local government finance officers, this edition is intended for a much larger audience. It includes not just finance officers but all local government financial management personnel as well as chief executive officers, department heads, elected officials whom we refer to as policy makers, and others in local governments worldwide who might find them useful. National government departments that have oversight responsibility for local finances should also find them useful as should those educational institutions preparing students for jobs within local governments. And, of course, the audience includes financial management trainers and training managers. In other words, these volumes are aimed at a world-wide mix of training providers and training users.

This expanded audience, however, has made the adaptation of these materials difficult. It initially looked like they would either have to be so general that they would be of no use to anyone, or so comprehensive in scope that nobody would be able to lift them, let alone use them. In wrestling with this dilemma, we decided to put the main responsibility for determining what to use in each volume and/or chapter, and how to use it, in the hands of the training managers and trainers. Given this fundamental decision, we want to direct the following comments to these individuals. While the following comments might be more appropriate for the Trainer's Guide, they are also important for finance officers, elected officials and others to hear. Thus, we have decided to put them in this Introduction chapter in hope that all training providers and users would read them. In addition, we have provided this Introduction, How to Use the Series, and the Trainer's Guide at the front of each volume so that each volume "stands alone," with all of the information provided in one place.

HOW TO MANAGE THIS MASS OF MATERIALS

Here are several ideas on how to make the use of these volumes more manageable and productive for you and your training clients. If you are a potential training client and listening in on this conversation, these ideas should also help you oversee and monitor your training supplier's performance.

- Know who your training audience will be and match what your training offers with their learning needs. There is nothing more devious in the training world than the trainer defining the client's needs in terms of what the trainer can deliver.
- One of your best marketing and delivery tools as a trainer is to talk to members of your potential target group to learn what they think would be most useful, based on their needs at the time. For example, the development of the original series resulted from a comprehensive survey of key local government officials in Slovakia. The survey included not just the finance officers but mayors who also performed as chief executive officers, members of governing bodies, and the directors of operating agencies. Each role had their special needs in terms of financial management and many of these needs were general to all the roles.

- Think seriously about providing a training programme for senior local government finance officers in your country that includes all the volumes. This is obviously a heavy commitment on the part of trainers and finance officers but essential. It also means you will need to spread the training out over a longer time period. If you want to get the attention of these finance officers but not their attendance, schedule the programme during the budget preparation season.
- Since many finance officers may be concerned about making a long term time commitment, start with those modules that they believe are most important from their point of view. Also think about creating a certificate programme for those who successfully complete training in all volumes in the series. Some kind of official recognition for completing the series will be a good incentive to most professionals.
- As for those elected officials, several briefings using the chapters from Financial Policy Making, Financial Planning, and Citizen Participation in Volume 1, before the budget preparation cycle begins would be useful. Hopefully it would get them thinking about some of the longer term issues in terms of financial management. Follow this with sessions from the chapter on Financing the Operating Budget from Volume 2, before those budget hearings begin. In other words, target the training to their needs.
- Department heads could benefit from sessions on the Operating Budget, Financial Planning, and Performance Measures. These chapters are contained in Volumes 2, 1, and 4 respectively.
- Target those officers who have specialised responsibilities. For example, are there purchasing agents in the larger local governments? If so, schedule sessions using the chapter on Procurement in Volume 4. In some countries, the Procurement chapter might even become one of the study guides for developing national legislation that provides guidelines for local governments. If there are local finance clerks who have responsibilities for asset management, the Asset Management chapter in Volume 4 offers the concepts and training designs to meet their needs.
- Think about briefing sessions on the full scope of LGFM for specific local government teams of elected officials, managers and key financial personnel. One of the best times to do this is just before the budget cycle begins. This way they all get the big picture. It's also a good time to learn about specific training needs. For example, the governing body might have been talking about involving citizens more directly in the budgeting process. Or, they might be faced with some major capital expenditures and need more knowledge and skills on their options in undertaking long term investments in public infrastructure.
- In other words, be creative in cultivating the potentials for using this rich storehouse of learning materials with a wide range of local government audiences.

With these opportunities in mind, here are four important clues on how to use these volumes successfully.

1. Don't panic by their size and comprehensiveness. Remember the old joke about how to eat an elephant? As the joke goes, one bite at a time.
2. Figure out who your training audiences are and give them an opportunity to tell you what they need in the way of training. Remember, your potential audiences for LGFM training are both many and significant. We've only touched on the most obvious in the examples just given.
3. Design the training based on these needs and the knowledge and skill levels of your specific audience.
4. Finally, select from these volumes only what is needed to meet the needs of your specific learning audience. The worst thing you can do is to overwhelm them with either too much stuff or the wrong kind of stuff. We've highlighted what we think might be advanced principles and practices in each of the manuals but the judgement call is really yours as a trainer. And, your judgement about what to include in each training design should be based on the roles and responsibilities of your participants, their learning needs, and their general level of sophistication as a group.

LGFM AND GOOD GOVERNANCE

One of the shortcomings of the original series of chapters was the absence of any explicit attention to the principles of good governance that have become standards in the past decade to define the performance of local governments worldwide. While these principles were implicit in many of the concepts and strategies in specific chapters in the original version, we will make them much more explicit in this edition. Since the good governance principles vary a bit from one official proclamation to another, we will start by presenting two versions and then tie them to financial management as the operating framework for achieving these principles.

In UN-HABITAT's Global Campaign on Urban Governance², these principles are defined as:

- ***Sustainability*** in all dimensions of local development;
- ***Subsidiarity*** of authority and resources to the closest appropriate level consistent with efficient and cost-effective delivery of services;
- ***Equity*** of access to decision-making processes and the basic necessities of community life;
- ***Efficiency*** in the delivery of public services and in promoting local economic development;
- ***Transparency³ and Accountability*** of decision-makers and all stakeholders;
- ***Civic Engagement and Citizenship*** with all citizens participating in and contributing to the common good; and

² For more information on the Global Campaign on Urban Governance, visit <http://www.un-habitat.org/campaigns/governance//>. See also UN-HABITAT (2003) *Tools to Support Participatory Urban Decision-Making*.

³ See UN-HABITAT (2004) *Tools to Support Transparency in Local Governance* for further information.

- **Security** of individuals and their living environment.

For a slightly different look at governance, we turn to The United Nations Economic and Social Commission for Asia and the Pacific (ESCAP). Their interpretation of good governance has eight characteristics:

1. It promotes and encourages participation including that of children.
2. It requires respect for the law and the full protection of human rights.
3. It involves transparency in decision making, and information is freely available and easily understandable to all.
4. It is responsive, implementing decisions and meeting needs within a reasonable time frame.
5. It is consensus-oriented, involving the mediation of different interests in society and sensitivity towards the relative influence of different actors including the poorest and most marginalised.
6. It promotes equity and inclusiveness, such that all members of society feel that they have a stake in that society.
7. It means that processes and institutions produce effective results that meet the needs of society while making the most efficient use of resources and promoting sustainability.
8. It is founded upon accountability, not only of governmental institutions, but also of private sector and civil society organisations.

As you can see, there isn't total agreement even within the larger UN community about what constitutes good governance principles. Nevertheless, most institutions that promote these principles agree that governance is much bigger than just government. The Global Campaign says that governance includes government, the private sector, and civil society.

ESCAP's definition of governance embraces just about every organised entity as well as individual citizens. For example, they include governments, NGOs, the private sector, the media, grassroots organisations, and more. To simplify our task of relating good governance to LGFM, we will take what we believe to be the most important principles in the two UN statements and provide some examples of what they might look like in practice.

- **Rule of law:** This principle is central to LGFM. For example, the budgeting process is established by law, even determining when elected and appointed officials must do what by when. Procurement standards and accounting procedures are often established by law and the development of financial policies by local governing bodies is also an act of law making, albeit local. Local government corruption is more often than not based on financial transactions that violate the rule of law.
- **Transparency:** This principle cuts across a variety of LGFM functions and responsibilities including financial policy making and planning, budget hearings and postings, financial audits, and the involvement of citizens in the full range of financial management activities.

- **Accountability:** This presumably is what the budget process is all about. It holds elected and appointed officials accountable by stating how public funds will be spent. Programme and financial audits should determine if public officials were accountable in their implementation of the budget.
- **Participation and civic engagement:** One of the current hot topics on the international circuit is participatory budgeting. The days when financial management was confined to the backrooms of city hall has passed.
- **Equity and inclusiveness:** These principles, when implemented, assure that financial decisions are made in the best interests of all citizens not just the privileged few. They cut across such financial functions as budgeting, procurement, financial policy making and planning, and the development of performance measures that focus on issues of equity and inclusiveness.
- **Subsidiarity:** This rather daunting term describes the process of determining how best to deliver services in efficient and effective ways. It may mean contracting out services to the private sector, or subsidising NGOs to perform certain services. These decisions cut across financial policy making and planning, the need to establish performance and accountability measures, the budgeting process, and a host of other LGFM activities.
- **Effectiveness and efficiency:** Financial management is really all about these two fundamental principles. Peter Drucker, the management icon, says “Effectiveness is doing the right things” and “Efficiency is doing things right.” Budget decisions should sort out the right things to spend public funds on and the management of the expenditure of those funds and resources should assure that it’s done right. These two principles should be your financial management mantra.
- **Sustainability:** We complete this principled look at LGFM by including UN-HABITAT’s principle # One in their Global Campaign on Urban Governance: sustainability in all dimensions of local development. This covers a myriad of financial decisions: from making certain that maintenance of public buildings, infrastructure and equipment is covered in the annual budget, to long range financial planning of community programmes so their sustainability can be assured.

As you can see, LGFM is a very principled role and responsibility. Keep these good governance principles in mind as you use these training materials for your own professional development and the development of your local government organisation and community.

A NEW CONCEPTUAL MAP TO NAVIGATE BY

We mentioned earlier that the original version of these materials took a topic by topic, or function by function, look at the financial management roles and responsibilities associated with local government and the broader definition of governance. The original version included fifteen handbooks: Introduction; Accounting as a Management Tool; Financial Policy Making; Financial Planning; Operating Budget; Capital

Programming; Debt Management; Cash Management; Revenue Maximisation; Cost Containment; Procurement; Performance Measures; Construction Cost Management; Citizen Participation; and Grants Management.

When the Expert Group Meeting of LGFM users was convened by UN-HABITAT in Kenya to determine the content and format of the new edition of these materials, the members were challenged by the experience and insights of the Slovakia finance officers. Not only had they helped develop the original series, they also had experience using the materials to train other finance officers in their country and the region. Again, Eva Balazova proved to be the key person in helping to take this series to a new level of anticipated performance. After many variations of how to reorganise and revitalise the LGFM series for worldwide use, the team of experts agreed on the following strategy.

1. The short-term operating budget and long-term capital investment plans are the engines that drive local government financial management: The two chapters from the original series that covered these topics remain and are expanded to include materials from other manuals in the original series. In this series they are: Volume 2, Chapter 5, *Operating Budget of* and Volume 3, Chapter 7, *Capital Investment Plan*.
2. In each of these two major LGFM functions there are financing requirements that need to be addressed separately, thus we have two new chapters in this series that are, in a sense, companion learning tools; Volume 2, Chapter 6. *Financing the Operating Budget*, and Volume 3, Chapter 8. *Financing the Capital Investment Plan*.
3. Several of the financial management functions covered in the original series are integral to the operating budget and capital investment planning processes and are incorporated into the chapters covering these topics and their companion chapters that deal with their financing. These functions include: Debt Management; Cash Management; Revenue Maximisation; Cost Containment; Construction Costs; and Grants Management. In other words, the materials covered in these original chapters are now integrated into Volume 2, Chapters 5 and 6, and Volume 3, Chapters 7 and 8.
4. Three new chapters were recommended by the expert team and they are included in this series. They are: *Trainer's Guide*, which is included in all four volumes; *Evaluating Financial Condition*, Volume 1, Chapter 4, and *Asset Management*, Volume 4, Chapter 11.
5. The remaining chapters in this series, which mostly represent cross cutting competencies, are updated and expanded versions of handbooks in the original series. They are: Chapter 1. *Introduction*, which is in all four volumes, Volume 1 includes Chapters 3, *Financial Policy Making*;, Chapter 4. *Financial Planning* and Chapter 5. *Citizen Participation*. Volume 4 includes Chapters 9, *Accounting*, 10, *Performance Measures* and 12 *Procurement*.

We hope this provides a mental picture of how this set of training and management volumes/chapters evolved from the original series. Of course, there are many

ways to slice this complicated set of competencies, functions, and responsibilities within LGFM and we suspect that a few of you are already saying, “Well, the next time they are updated I think they should” We do to but in the meantime we hope you find this new series a bit more easy to use as trainers and public officials responsible for LGFM in your communities.

VOLUME CONTENTS

The contents of the remaining LGFM volumes and chapters are summarised below to give you a brief idea of what to expect from each.

VOLUME 1: CREATING A FINANCIAL FRAMEWORK

INTRODUCTION

TRAINER’S GUIDE

This chapter is designed to help trainers and other key individuals use these materials in a variety of situations with a wide range of participants. It covers the adaptation and possible translation challenges of making the chapters more user friendly in the context of their use and the planning process of developing and delivering effective training. Clues will be included on how to design and deliver interactive learning experiences based on the input of concepts and strategies from the chapters and participant experiences in their application within local governments. The materials can and should be adapted by trainers to meet the learning needs of their clients and ways to do this will be provided. Various training design techniques will be covered, such as how to write a critical incident, case study and role play situation. Finally, there are ideas on how to evaluate training and its impact.

CHAPTER 1: FINANCIAL POLICY MAKING

This chapter examines ways that formal, written financial policies are developed and implemented at the local government level. We will provide a definition of financial policy and describe the benefits to a local government that establishes and uses sound financial policies. We will delineate the basic steps to take in identifying, proposing, adopting, and implementing financial policies. We will also discuss various obstacles to the financial policy making process.

CHAPTER 2: FINANCIAL PLANNING

This chapter will examine ways that financial planning can be developed and implemented in local governments (LGs). The focus of the chapter is primarily on one aspect of financial planning—medium-term financial forecasting of revenues and ex-

penditures. We will provide a definition of forecasting and relate it to good governance, citizens, performance measures, and financial policies. We will also describe the benefits that accrue to LG when implementing a financial forecasting process, considerations for organizing the process, types, and methods of forecasts. Included in the discussion will be obstacles, limitations, and risks inherent in developing a financial forecasting process.

CHAPTER 3: CITIZEN PARTICIPATION

This chapter examines ways that citizens interact with their local governments (LGs). We provide a definition of citizen participation and describe the benefits to a local government that establishes and uses citizen participation policies and techniques. We discuss obstacles to the use of these policies. We provide ten steps to involving citizen participation in resolving an issue. Finally, we provide a compendium of techniques that can be used by local governments to involve citizens in a timely and constructive way in the development and implementation of public programs.

This chapter is written for LG officials, managers, and policy makers. It does not attempt to provide a citizen's point of view towards dealing with LGs. Because some reviewers indicated an interest in Participatory Monitoring which focuses on citizens monitoring the LG, Appendix B: World Bank Information on Participatory Monitoring has been added to the chapter.

CHAPTER 4: EVALUATING FINANCIAL CONDITION

This chapter focuses on identifying, measuring and analysing various financial and demographic factors that affect a local government's financial condition. The financial data needed for the analyses is taken from the local government's financial records. Managers can use the information to: better understand the local government's financial condition, the forces that affect it, and the obstacles associated with measuring it; identify existing and emerging financial problems; and, develop actions to remedy these problems.

VOLUME 2: MANAGING THE OPERATING BUDGET

INTRODUCTION

TRAINER'S GUIDE

CHAPTER 5: OPERATING BUDGET

This chapter is divided into basic and advanced sections. This basic section describes how to design and implement an operating budget system for LGs. It defines operating budget terms, explores concepts, and examines the benefits and potential obstacles associated with establishing and using a system. It provides a 12-step

process for preparing, reviewing, adopting and monitoring the operating budget. The advanced section provides information on cost containment, various management analysis techniques and awarding grants within the LG community.

This chapter deals with budgeting matters in general and does not apply or take into account each individual country's laws or regulations. LGs are responsible for making local decisions, including compliance with any applicable laws, statutes, decrees or regulations.

CHAPTER 6: FINANCING THE OPERATING BUDGET

The concept of “financing the operating budget” combines many functions across the local government (LG) organization. It involves estimating revenues (covered in the Financial Planning chapter), cash budgeting, revenue billing and collections, investing idle or excess cash, setting prices and user fees and the day-to-day monitoring of all of these functions to ensure that sufficient monies are available in the bank to actually pay for the day-to-day operations of the LG—the operating budget. It is important that all of these separate but very interrelated functions are considered when developing policies, procedures and making decisions about the LG programs and services.

This chapter examines how you can use the revenue structure, cash management, internal controls, the accounting system, revenue billing, and collections, investing idle cash, and cash budgeting to assure that the revenues needed to fund the operating budget are available when needed.

VOLUME 3: MANAGING CAPITAL INVESTMENTS

INTRODUCTION

TRAINER'S GUIDE

CHAPTER 7: CAPITAL INVESTMENT PLAN

This chapter is divided in basic and advanced sections. The basic section will describe how to design and implement a capital investment planning and budgeting system at the local level of government. We will define capital investment planning terminology and examine the benefits and potential obstacles associated with establishing a system. We will also discuss the steps involved in preparing, reviewing, adopting, and monitoring a capital investment plan and budget, including an extensive section on actually constructing facilities. The advanced section includes an introduction to value management and real estate analysis.

CHAPTER 8: FINANCING THE CAPITAL INVESTMENT PLAN

It seems that most policy makers and staff are familiar with putting together the capital investment plan—holding public hearings and putting a plan together that will move the LG towards the policy maker’s vision of the future. Unfortunately, few have taken the time to understand the equally important function of financing the capital investment plan. Decisions made about it have a much longer-term effect than those made about the operating budget—they may affect several future generations of citizens.

This chapter examines how the financing for the investment plan is developed and implemented. We will provide definitions of debt management and other related terms. We will also review the benefits of instituting a debt management program, identify and provide examples of policies that should be developed, and discuss the legal environment surrounding the use of debt. We will address types of financing, methods for selecting credit instruments and the mechanics for obtaining financing, as well as a review of credit analysis, disclosure requirements and administration of the debt.

VOLUME 4: MANAGING PERFORMANCE

INTRODUCTION

TRAINER’S GUIDE

CHAPTER 9: ACCOUNTING

This chapter is divided into basic and advanced sections. The basic section includes background information on basic concepts and definitions of accounting, the importance of accounting and good governance, accounting standards, the accounting cycle, and types of accounting. It also includes policies, obstacles and benefits to accounting. There is a section on management accounting and various costing techniques. The advanced section includes information on computer technology, modernizing the accounting system, accounting manuals, fund accounting, utility funds, depreciation, and advanced financial and budgetary reporting.

CHAPTER 10: PERFORMANCE MEASURES

This chapter examines the development and implementation of performance measurement at the local level of government. We will define performance measurement and describe the benefits to a local government that uses it to improve the odds of success in achieving its service goals. We will also discuss the steps involved in setting up a performance measurement system and obstacles that may be encountered along the way.

CHAPTER 11: ASSET MANAGEMENT

This chapter examines how you can use asset management as an effective management tool. We define the term assets, as it is used in this chapter, asset management systems, and plans and describe the benefits of using asset management to better plan capital investments and achieve service delivery goals.

The best place to start developing an asset management plan is with the basics. According to the World Bank, these include:

- Developing basic asset inventories including surplus real property,
- Documenting asset operation and maintenance processes,
- Developing primary asset information systems,
- Preparing basic asset management plans, and
- Developing staff skills and governing body awareness.

We have structured the book to provide information on these basic components from two perspectives. The first deals with the assets that are used to provide day-to-day services to the citizens of the LG. The second recognizes that some countries are in a decentralization process where the central government is giving LGs responsibility for assets for which they have not previously been responsible. For those local governments that may be in the second category, we have provided a section on Surplus Real Property since it represents a different challenge than working with the assets used to provide ongoing services. However, this chapter does not deal with managing apartment or housing units.

CHAPTER 12: PROCUREMENT

This chapter is divided into a basic and advanced sections. The basic section examines the process of procurement in local government with emphasis on procurement planning, legal procedures for the acquisition of goods, services and public facilities, and details of procurement administration. It also includes policies, benefits and obstacles in the procurement process. Steps for a comprehensive procurement process for goods, services and public works are also included. The advanced section deals with construction contract administration, store operations, procurement and e-Government, and procurement and economic development issues.

USING THE SERIES

We have designed the series described above to be used by a variety of individuals and institutions. Obvious among these are the trainers and training institutions on the supply side of training and finance officers on the demand side. But, we see the potential users as many more as alluded to earlier. We hope that chief executive officers (CEO) and department heads in local government will use them along with staff members of municipal associations. There should be interest likewise on the part of community NGOs that are hoping to see citizens get more involved in the budgeting processes of their local governments. And community colleges and other educational

institutions that are preparing entry level public financial management professionals for future employment could easily integrate many of these chapters into their curriculum.

For those mainstream users like finance trainers and finance management professionals we offer the following ideas. Use these chapters:

1. As self-study guides. We hope policy makers, CEOs, department heads, and a range of financial management personnel from local governments will be inclined to pick up these chapters and read them. To add value to the reading we have interspersed each essay with Learning Application tasks. With each of the short application tasks, we have identified in a call-out box who might best benefit from undertaking each of these tasks. Of course, we encourage all users to pause from the reading to critically assess what they have been reading in relation to their own financial management responsibilities and challenges.
2. As workshop learning guides. We anticipate that these chapters will become the basis for a wide range of learning experiences for local government elected and appointed officials. As we mentioned earlier, there are many ways to organise these materials to meet a variety of learning needs within the broad local government community. For example, if you are operating as a trainer or manage a public sector-oriented training institute, think about the following options:
 - A ten-day workshop that includes approximately a half day on each of the substantive topics;
 - A five-day workshop that covers fully three or four of the topics included in the series based on the assessed interest of finance managers in a particular region of the country;
 - Twelve workshops, each one to one and one-half day in length, covering all of the topics;
 - A three-hour program in conjunction with an annual conference of local finance officers that deals with the most important aspects of one particularly high-interest topic in the series.
 - A presentation at the annual meeting of the national association of local governments on the advantages of supporting LGFM training for key local government elected and appointed officials.
 - Teaming up with a formal educational institution to offer a certificate programme based on the series, or to integrate selected materials into their degree programme in public administration, with you being an adjunct instructor who delivers the education modules.

In addition to the options mentioned, there are other ways to use these materials. For example, think about meeting with an interested group of finance officers from the same region every Friday afternoon for several weeks to hold discussions on several of the topics. Rather than give you any more ideas, we suggest you do a bit of brainstorming for other ideas by completing the following Learning Application exercise. By the way, these interludes in your reading are identified by the term just

used, Learning Application. You will find them throughout the texts of Part One of each of the chapters. Trainers have also found them to be useful as learning exercises for workshops and other structured learning events. Just modify them to meet your specific training design needs and add them to your training toolkits.

LEARNING APPLICATION

Take a few moments and jot down some ideas about how these chapters might be used in your country to support the further professional development of your public officials and institutions.

Of these ideas, which ones do you think are the most important?

What can you do personally to help support these ideas so they become real?

PART TWO: MANAGEMENT TOOLS

PURPOSE

The materials included in this overview are designed to be used by the trainer to initiate a series of workshops on financial management. In other words, they are intended to serve as an introduction when several of the topics on financial management are to be covered during the same workshop series. On the other hand, they can be adapted to supplement the content of a program devoted to just one topic. Either way, they are intended to get the training off to a successful start by helping participants get acquainted with each other, providing them with information on workshop content, and letting them experience the type of interaction to be used throughout the workshop series.

While we have stressed in Part One of this chapter and in the Trainer's Guide the importance of adapting these materials to meet the needs of your training participants, we want to reemphasize it again. Many of the exercises can be changed to meet the needs of various audiences with differing levels of knowledge and experience in financial management. Don't hesitate to adapt them to meet the learning needs of your participants.

CONTENTS

A brief description of each learning activity is shown below with an approximation of the amount of time required. If you wish to change the order, to omit something, or to add training material of your own, feel free to do so. In addition, use your judgment and experience about the time needed to complete the tasks involved in the exercises. While we have attempted to judge the times it might take to carry out a group task, for example, it will vary from group to group. Adapt to the learning needs of your participants in these workshops and you will be successful.

0. 1 WARM-UP EXERCISE: GETTING ACQUAINTED

Introductions should be made to acquaint participants with each other and the training staff, let them know what will be expected of them, and help them to feel more comfortable in the learning environment. (15 - 60 minutes)

0.2 EXERCISE: ASSESSING KNOWLEDGE AND EXPERIENCE

Participants individually assess their level of knowledge and experience in relation to a list of financial management topics, and compare results in small groups. (60 - 75 minutes)

0.3 EXERCISE: IDENTIFYING FINANCIAL RESPONSIBILITIES

An alternative to the preceding exercise. Participants work in small groups to identify and compile lists of financial management responsibilities and rate the responsibilities on challenge and the need for training. (60 minutes)

0.1 WARM-UP EXERCISE: GET ACQUAINTED

TIME REQUIRED:

15 - 60 minutes

PURPOSE

This exercise is to help participants get to know each other and the trainer, let them know what will be expected of them, and cause them to feel more comfortable in the learning environment.

PROCESS

After welcoming remarks by the host agency representative and a short description of program objectives, scheduling and logistics, give a brief personal introduction and invite participants to get acquainted. Here are some alternative ways to organize the get-acquainted exercise.

Self-introductions —Ask participants to say a few things about themselves such as their names, the local governments they represent, the number of years they have served as finance officer or some other position, and why they have chosen to take part in this workshop or workshop series.

Paired introductions—Ask participants to pair up to get acquainted, to gather some personal/ professional data on one another, and then, in turn, for each participant to introduce his or her partner to the group.

Small group mixer—Have participants write on a card the name of the finance management area in which they would most like to be more skillful. Since many of the participants may not be aware of the topics to be covered by the training, you may have to make a list of them on newsprint or a blackboard before starting the exercise.

After participants have completed the task, ask them to get up and wander around the training room until they locate another participant with a similar need. After a few minutes, have participants who are interested in the same area of financial management to join together in small groups to discuss what they would like to know or be able to do better about that area. Ask for volunteers from the various groups to introduce their group's members and report on their group's results.

0.2 EXERCISE: ASSESSING KNOWLEDGE AND EXPERIENCE

TIME REQUIRED:

60 - 75 minutes

PURPOSE

This exercise is to help participants relate their own professional experience to the various financial management topics included in the workshop series.

(Note: If participants have not read the essay at the beginning of this chapter and are not familiar with the topics included in the series, substitute Exercise 1.3 for this one.)

PROCESS

Using a questionnaire like the one shown on the next two pages, ask participants to provide some information about their own performance and the performance of their respective local government organizations in relation to various topics.

When participants have completed the task individually, ask them to share their responses in small groups. Suggest that a recorder in each small group make a list of the responses and tabulate them to identify the patterns (i.e., which topics are most often mentioned in response to items in the two boxes).

After about 30 minutes of small group discussion, reconvene the participants. Ask for a summary report from each small group. Encourage a discussion of similarities and differences in small group results.

Assessment of Financial Management Knowledge and Experience: A Questionnaire

INSTRUCTIONS

Read the descriptions of functions performed by local governments in conducting their financial management responsibilities that are presented in Table 1. After you have read each of the functions, fill in the information as requested in the boxes in Tables 2 and 3.

Table 1. Description of Financial Management Functions

Accounting	Provides the basic concepts of accounting and reporting for LGs.
Asset Management	Provides a method for identifying and managing the assets of a LG.
Capital Investment Plan	Examines the process of planning for the financing of future physical development needs to ensure that construction priorities and schedules are coordinated with the availability of needed financial resources.
Citizen Participation	Provides a guide for local government officials in their efforts to involve citizens in a timely and constructive way in the development and implementation of public programs.
Evaluating Financial Condition	Provides a illustrative set of indicators to be used in evaluating a LG's financing condition.
Financial Planning	Examines in depth the process by which local governments anticipate their future financial needs using a variety of planning and forecasting methods.
Financial Policy Making	Explores the nature of financial policy and how policies are formulated and used systematically by local governments to guide and direct their financial affairs.
Financing the Capital Investment Plan	Describes the short and long-term financing portion of the capital investment plan.
Financing the Operating Budget	Describes the revenue and short-term financing portion of the annual operating budget. Also includes cash budgeting and investment of excess.
Operating Budget	Concentrates on the annual operating budget and its use as a primary tool for financial planning and management as well as for estimating annual income and controlling expenditures.
Performance Measures	Describes the use of performance measures to determine if and how well the intended purposes of local government are being achieved and how to set up a performance measurement system.
Procurement	Reviews in detail the lawful, efficient and ethical procurement of goods and services by a local government including a step-by-step tour of the public procurement cycle.

With respect to my own management performance, I would rate the finance functions described in Table 1 as follows:

Table 2

My Performance	Function
The function in which I do the best is:	_____
The function in which I am least successful is:	_____
The function that is the most challenging for me is:	_____
The function that is the least challenging for me is:	_____
The three functions in which I want training the most are:	_____

With respect to my local government’s performance, I would rate the finance functions described in Table 1 as follows:

Table 3

My Local Government’s Performance	Functions
The three functions in which my local government performs best are:	_____

The three functions in which my local government performs the least successfully are:	_____

Worksheet—Financial Functions: Challenges and Training Needs

INSTRUCTIONS

In Column 1, on the left side of the worksheet, make a list of 10 important financial functions performed by the local governments represented by members of your small group. After completing the list, agree as a group on five of the functions on the list as the ones that are the most challenging for the local governments represented. Indicate your group's choices by blackening the appropriate five circles in Column 2. Then, agree as a group on five functions from the list as the ones in which training is needed the most by finance officers representing the local governments. Indicate your group's choices for training by blackening the appropriate five circles in Column 3.

Column 1	Column 2	Column 3
Finance Function	Most Challenging	Training Needed
1. _____	0	0
2. _____	0	0
3. _____	0	0
4. _____	0	0
5. _____	0	0
6. _____	0	0
7. _____	0	0
8. _____	0	0
9. _____	0	0
10. _____	0	0

0.3 EXERCISE: IDENTIFYING FINANCIAL RESPONSIBILITIES

TIME REQUIRED:

About 60 minutes

PURPOSE:

This exercise is to help participants identify the various individuals or roles that perform important functions within local government's financial management process. The intent is to increase awareness of the interrelated nature of the various functions and the importance of team work in carrying out these functions. This is an exercise that can be used with participant groups that include policy makers (elected officials), CEOs, and department heads as well as financial officers.

PROCESS:

Divide the participants into small groups of five to seven and give each participant a copy of the list of FM functions from Exercise 1.2; Table 1. Ask each group to discuss who within the local government family of individuals, departments, boards, and commissions (such as the elected body or the planning commission) need to be involved in each of the twelve functions on the list. Out of the list for each function ask them to identify who does or should take the lead responsibility. Tell them they have about 30 minutes to come up with their responses.

This could get a little messy since many individuals, departments, and various boards and commissions need to be consulted or involved in many if not most of these functions. Remind the participants that the intent is to better understand the complexity of most LGFM functions. Ask each group to record their responses on flip chart paper so they can report on their findings in the following plenary session.

Don't hesitate to add any additional tasks to this exercise that you feel would be useful in helping the participants get a better understanding of the full range of functions within LGFM. For example, you might ask them to identify the roles that citizens should play, if any, in each of these functions.

Trainer's Guide

INTRODUCTION

When the Expert Group met in Kenya to plan this series of training and management materials the members agreed that the utility of the series would be enhanced by including a trainer's guide. While trainers will be the primary users of this guide, there are others that will also find it useful. For example, we have included a few notes for those who might be concerned about translating them into another language or perhaps adapting them to be more congruent with national laws and financing practices. We also see finance managers and other local government managers as potential users of this guide, particularly if they want to have an influence on the quality of training that is being provided for their employees. If your country has an association of finance officers, chief executive officers, or governing bodies, or is thinking about starting one, this guide might be useful. In other words, its potential users go beyond just those in the trainer role. We have tried to write it with this expanded audience in mind. We believe it's important to put training into a much broader context than just designing a learning event for a group of local government officials.

We will start our discussion in a moment by explaining what we mean by this. From there we will look at some of the challenges of adapting, and where necessary, translating the series into another language. We will also discuss some issues involved in planning and sustaining a successful local government financial management (LGFM) training programme. These aspects of training cover a range of training management tasks from doing a training needs assessment, to training trainers, and evaluating the impact of the training investment.

Finally, we will get to the trainer's concerns about how to use these materials to enhance their performance as learning facilitators. We will look at how to design successful learning interventions and how to carry them out successfully. It's one thing to design a successful training programme. It's another to conduct it successfully. In covering these aspects of the training trade, we will provide some clues about various kinds of learning tools such as case studies, role plays, and the use of instruments. We will also talk about the art of facilitating effective learning.

PRE-PLANNING CHECKLIST

Before sending out workshop announcements for LGFM training, it will be helpful to do a bit of preplanning to assure that you get the most from your efforts. To help

you do this we collected a few questions you need to ask yourself and others. Don't hesitate to add to the list as you engage in this preplanning planning.

- Who will be your primary training target group? Local government finance directors? Finance department staff members? Operating department heads? Local elected officials? Central government or provincial officials with local government oversight responsibilities? A mix of these possibilities?
- What are the potential numbers of training participants you might be able to attract from each of those target groups you want to serve?
- Have you thought about doing a training needs assessment of these potential training participants? If so, do you know how you will conduct the assessment?
- What will be the potential market for a training programme that involves the full series?
- Is there a pre-service training potential for this type of training?
- Have you thought about the potential of addressing good governance principles through special workshops for both local government and civil society participants based on the content of this series?

These are the kinds of marketing questions you need to be asking yourself and others before sending out the training announcement. They also get to the questions of what is feasible in terms of time commitments on the part of the participants you hope to attract to your training. Offering a training programme that involves the entire series is ideal for senior finance officers but may present some financial and time constraints. There are several ways to overcome these constraints and they probably involve partnerships. For example,

- Can you partner with another organisation or individuals to plan and deliver the training? Is there a professional association of finance officers, chief executives or governing bodies that would be a likely partner? Or a national association of local governments?
- Are there funding possibilities to help underwrite the cost of the training? International development agencies? Foundations? Professional or trade associations that are concerned about the quality of local government management?
- Have you thought about educational institutions that might want to offer this type of training as part of their continuing education programmes? They have the incentive of being able to offer a certificate or other credential that could enhance the careers of those who complete the series successfully.
- Have you taken time to get acquainted with the entire series with the intent of deciding how you might use selected ones to meet specific training audience learning needs? For example, elected officials? Or, auditors? Department heads of local government operating agencies?

These materials offer a wide array of marketing and partnering potentials. It will be helpful to spend some time thinking about these potentials before making any firm decisions about how you want to use these materials. We mentioned the potential of conducting training needs assessments (TNA) earlier. We believe they are important to help you and your training colleagues determine not only what to offer in terms of training content but also how to work within the time and other constraints your potential training clients might encounter in participating in the training. TNAs can also be important marketing tools. They help those who might need the training to better understand their needs and to help you in return explore some ways to overcome the constraints of participating in the training.

The next set of questions to ask involves the logistics of getting ready to offer the training.

- Will the materials have to be translated into the local language? If so, how will you arrange to have this done? And, how will you pay for the translation? We suspect you have had lots of experience in this process and know the pitfalls to be avoided. Nevertheless, we will make a few comments later about how to make this part of the planning process less troublesome.
- Will you need to adapt the materials to accommodate accounting or budgetary regulations, local legislation, management arrangements, or other peculiarities that might create resistance from the potential training audiences? We have tried to make the volumes as general as possible to minimise adaptation problems while not making them so general that they are useless. If you don't have to translate them into a local language you may be able to handle any essential adaptations with addenda to each chapter that are printed separately and inexpensively.
- Will you need to train trainers to conduct the training? If so, how will you conduct this training? Who will pay for this training?

There are many other questions you will need to be asking as you begin planning to use these materials. Don't hesitate to ask them. Better now than saying later, "Why didn't I think of that when I was considering the use of this series?"

TEN WAYS TO FAIL AS YOU USE THESE MATERIALS

One of the members of the Expert Group who helped to shape the content and format of these materials suggested we include a short discussion of how you can fail in using these materials. It comes from an earlier version of the Local Elected Leadership series also published by UN-HABITAT¹. With a few adaptations to the source document here are some contrary thoughts on how to fail.

¹ UNCHS (Habitat) (1995) Local Governance Manuals: Training for Elected Leadership Series. Set of 13 volumes.

1. Don't bother to discuss the training with any finance officers before they come to your first workshop on this series. After all, you're the training expert, and they are just your training clients.
2. Plan to hold the training in places that are convenient for you and your training team. Don't worry about the training participants. They all have big travel budgets. If they don't, it's their own fault since they put together the budget.
3. The same goes when you hold the training. Your clients should be able to adjust their schedules if they are really interested in the training. And, don't let their excuse that it's "budget time" bother you.
4. Don't waste time checking out the training venue before the workshop begins. Everyone knows it's the content of the training that counts.
5. UN-HABITAT training materials are always so complete that there is no need to check them out before the workshop.
6. Stick to lectures and guest speakers as much as you can and don't bother with small group exercises and other stuff. They waste a lot of time and take up too much space.
7. If you feel you must use exercises, just go with the ones in the chapters. Start with the first and go through them in sequence until time runs out.
8. Don't bother to make changes in the exercises in the chapters. Obviously, the authors knew what they were doing or UN-HABITAT wouldn't have hired them.
9. Always go with the time the authors suggested in the exercises. Even if the participants are really into learning, don't hesitate to shut them off when the time the authors said the exercise should take runs out.
10. Don't bother with evaluations or follow up. Those finance officers are the kind who will call you if they have any questions or want more training.

These comments sound familiar. Sure, we've all known trainers who operated this way. Did you notice the past tense of that last statement? Hopefully they are no longer conducting training!

ADAPTING AND TRANSLATING THE SERIES

We mentioned briefly in the introduction some concerns about the possible translation and adaptation of the LGFM series for use in your country. Given the importance of these potential tasks, we want to share some lessons learned in preparing other training materials for local use.

The tasks of *adapting* and *translating* these materials will depend on a number of circumstances. If the training is to be conducted in your country in English and you have a cadre of seasoned trainers who are adept at modifying training materials to meet their needs, you may be able to use the series as published. Or, you might feel that new materials are needed to more accurately reflect the legal, cultural, political or managerial approaches to financial management in your country. If this is the case, you might want to produce a supplement for use by trainers and others.

For example, it might include different approaches to financial management tasks like oversight or procurement that are different in your country and need to be highlighted in the training; adaptation or abandonment of training tools that are not appropriate or otherwise acceptable to the potential participants of training; and development of new training and management tools that would be more user friendly and acceptable to your training clientele. We encourage these additions and changes.

If you need to translate the chapters into your local language, the tasks become more complex. Before you do anything, you should check with UN-HABITAT to see if any other institution or group has translated the series into your language. If they haven't, consider doing both an adaptation and translation if those who review the original text believe it will be necessary or desirable. The adaptation could include, for example, local case studies, role plays, and critical incidents, and changes of examples in the text to make them more country specific.

The following are some guidelines you might want to consider if you need to undertake adaptation and translation.

- Don't hesitate to make changes in the text and other important features in the materials.

While there are often rules and regulations that warn you not to copy, change, or otherwise mutilate someone else's published documents, they don't apply when working with this series of training materials. One reason UN-HABITAT training materials have been so successful is the freedom that users have to make them more compatible with their own circumstances.

In one country where one of the authors worked, he thought he had been clear about their right to make necessary and useful changes in the text. Only after the in-country version was translated and published in the local language did he discover that few, if any, changes had been made in crucial parts of the materials. Don't assume the permission to alter the materials has been clearly communicated. Even if it is clear to all concerned, don't assume the adaptation of even the most basic materials, such as case studies and role plays, has taken place.

- Assemble a small team of potential users, trainers, language specialists, and other key stakeholders to help with the adaptation and translation.

The task of adapting and translating these materials should not be left to one person although one person should have responsibility for pulling together the insights and inputs of others to produce the final product.

The selection of this team is important and might on rare occasions be problematic. For example, you will need one or two highly respected finance officers to serve on this team who are open to the need for training and understand the importance of introducing new concepts, principles and strategies into the management of financial responsibilities at the local level. Not only should they be familiar and skilled in LGFM principles and practices within your country, they will also provide a reality check on the use of these materials in their work environment. Their task will be to assure that the financial management concepts and strategies are either

compatible with local legislation and practice or represent improved approaches to current practices. In selecting these individuals, it is important to identify those who are open to change and willing to support new ways of doing things.

Include if possible one or two finance officers who also have training experience with adult education principles and strategies. They should also have a commitment to experiential learning, i.e., *learning by doing*. Let them know before they commit to working with your team that they will be responsible for helping to revise role plays, critical incidents, and case situations based on their own field experience and input from other members of the adaptation team.

Having a linguistics specialist on the team, in addition to the translator, may be important. For example, there may be certain words that are problematic even in the same language.

- Agree on some basic ground rules for working together as a team before you begin the adaptation and translation process.

For example, how will your team handle disagreements and differences of opinion about what to adapt and why? Be clear about each team member's role and responsibilities. Establish objectives, expected outputs and outcomes, and realistic time tables for reaching key milestones.

- If you are translating the materials into another language, hire the best translator available and don't allow that person to work in a vacuum.

The translation process is too important and difficult to be carried out without supportive interaction with a small bilingual team of trainers and finance specialists who are responsible for reading the translations and giving constructive feedback. We had an instructive experience when working with a two-language team in the development of the initial set of these materials. Much of the dialogue about how to translate certain technical terms took place between two continents and sometimes the interactions were, well, amusing. As some of the technical terms went from one language to another and then back again to the originating language, the initiator of the discussion often could not recognize the concept that was being discussed. Never underestimate the difficulty and importance of the adaptation and translation processes.

- Share the wealth of your experience and labour with others.

The translation of these learning materials can be a difficult, costly, and time-consuming venture so think about how you can share your final products and experience with others who communicate in the same language. If there is a regional language that is dominant, such as Spanish in Latin America, you may want to encourage joint production to optimize your production investments.

LEARNING APPLICATION

Adapting and, if necessary, translating the financial management series will be among the first and most important actions you will take once the decision has been made to use these materials. Stop for a moment and reflect on how you and others will undertake this responsibility. Jot down your thoughts on what kinds of adaptations might be needed to make this series of training materials more acceptable and useful in your country and culture; some of the key persons to be involved in adapting and translating; and how best to get this part of the process underway.

PLANNING FOR TRAINING IMPLEMENTATION

There are so many tasks associated with planning a successful training programme. For example, how do you get organised to conduct LGFM training? Who can, or will, be your sponsors? How do you market the training and follow-up activities? How do you build the trainer capacity to do this type of training if it doesn't exist? And how will you measure the impact of this training on the individual, the organisation and its various operations, and the community?

To help you sort through these many tasks, we are going to start with a technique that should serve you well in a number of situations. We borrow it from the consulting profession, but it works equally well in the training business and other entrepreneurial ventures. What we are about to discuss is called, among other things, *Contracting with your client*. This is not a legal contract; rather, it's a psychological contract. The concept and strategy has a rich history in the helping professions like consulting, training, and coaching, to name a few. Moreover, it's a great management tool and an effective tool for trainers and finance managers to use as well in conduct-

ing their business. As a trainer, think about how you can use this process as part of your LGFM training offerings.

BUILDING EFFECTIVE WORKING RELATIONSHIPS

Ed Schein wrote an important book called *Organizational Psychology* (Englewood Cliffs, NJ: Prentice-Hall, 1965, p.11.) In that book he took the concept of the “social contract” and gave it an organisational spin. Here’s what he had to say at the time.

The notion of a psychological contract implies that the individual has a variety of expectations of the organisation and that the organisation has a variety of expectations about him. These expectations not only cover how much work is to be performed for how much pay, but also the whole pattern of rights, privileges, and obligations between the worker and organisation.

If you substitute *training manager* for the individual and *training client* for the organisation, then you can easily see how this concept applies. Schein’s definition also relates to many of the issues involved of putting together an operating budget in a local government organisation.

Design Learning (DL) has described what is involved in setting the psychological contract between two people or entities better than any we have seen. The elements DL believes are important to cover in an initial meeting between the training manager and client are these:

- **Personal Acknowledgement.** This is the first exchange of information and feelings between the training manager and the training client. The goal is to make contact and to establish a working relationship. For example, express your appreciation for the opportunity to meet. If the client initiated the contact, then this is a good time to learn why the client decided to get in touch. If you as the training manager initiated the contact, then you might want to say why you wanted to meet and how the contact was made.
- **Communicating and Understanding the Situation.** Talk about the role of the finance official and the challenges inherent in this important community role. If you initiated the discussion, talk a bit about financial management training and what it involves. If the client has reservations about getting involved, this is the time to understand what they are and to discuss them.
- **Client Wants and Needs.** Understand why the client might want to get involved in financial management training, what their expectations are about such training, and why they think it could be an important investment for their department and organisation. If you have initiated this conversation, then it’s important to help the client express what he or she can offer to help make the training effective. It may be financial, logistical, even symbolic such as endorsing the programme. Discuss the client’s

concerns about costs, schedules, and the format of the training and other issues that might be associated with planning and implementing the training.

- **Training Manager's Wants and Offers.** Be clear about what you will need from the client to make the training successful and what you can bring to the training relationship. This can include such issues as the numbers of trainees you think you need to conduct a successful training programme, how the training will be delivered, the quality of the trainers, possible venues, the time commitment required, what the training content and process will be, and other "wants and offers" you have that will factor into this being a successful working relationship.
- **Closing the Conversation.** If you have reached an agreement to go ahead with the training, summarize the key points of the agreement and talk about next steps. Most initial discussions about your offer of financial management training will probably not result in a firm commitment immediately, so you will need to talk about follow-up steps. Otherwise, you may have wasted your time and theirs. Make plans to meet again within the near future to move toward a firm commitment. If this is not the right person or group to work with to initiate elected leadership training, then determine who is and ask if the person you are talking to can help make the contact.

What we have just covered is a process of establishing a working relationship with your training client. It is also a process you might want to work into a training session with finance officers to help them develop better working relations with department heads, the chief administrative officer, and elected officials in developing the annual budget.

SOME THOUGHTS ON FINDING SPONSORS AND CLIENTS

Sponsors of your local government financial management training efforts come in two basic types: those that provide monetary or other concrete kinds of support; and those who lend their name and prestige, and even clout, to support local government training.

Your concrete support list should include the usual grant giving institutions, i.e., bi-lateral and multi-lateral development institutions, foundations, private organisations, national and international NGOs that want to support local government capacity building initiatives, and more. If you have an association of local governments or several associations that represent local governments in your country, they may also be sources of direct support if they believe that financial management training can benefit their mission. The same is true of professional associations. The central government may give funds to support training, or they may be able to help introduce you to third parties they know who would be interested in supporting your training initiatives.

Some of the same sponsors you thought might be able to provide monetary or other direct support might also be able to lend moral support by endorsing your

financial management training efforts or by providing entrée to key stakeholders. Think about conducting a stakeholder analysis to identify potential direct and indirect sponsors. You could do the same to identify potential clients for the training. By stakeholder, we mean any person, group, or organisation that has an interest, pro or con, and would be affected in any way by financial management training at the local governance level and the consequences of such training. As you can see, even the planning of elected leadership training can cut both ways.

THE SPONSORSHIP-FUNDING DILEMMA

Before we go any further, it is essential to talk about the longer-term funding trap that is often associated with many of the kinds of sponsors we just mentioned. Many services and programmes often die on the vine once the sponsor's financial support is discontinued. Given this reality, you need to develop a strategy for sustaining the training after the donor or sponsor leaves town and to plan that strategy before you accept their money.

Here are some suggestions. Develop a sliding scale of participant training fees. As the acceptance and popularity of financial management training grows, you can increase the fees without suffering serious decreases in enrolment. Make sure you build as much of the developmental costs as possible, i.e. materials, translations, training of trainers, into any initiating grant or contribution. If you don't, you may be forced to increase costs later on to recoup these costs. In one country, regional training centres are supported by local governments through a modest membership fee based on population. In turn, the local governments are represented on the centre's policy board and get discounted and often free registrations to attend training programmes.

A POTENTIALLY DIVERSE CLIENTELE

It is easy to define the "clients" of financial management training too narrowly, i.e. as only individual finance officers attending short workshops. As a trainer, training manager, head of a professional association of local government officials, or an elected official concerned about the quality of your local government's financial management you need to think "outside the box" (the box being the traditional way of handling things!) in terms of ways these learning materials can be used. Here are just a few ideas.

- Involve local elected officials, the local policy makers, in LGFM training by focusing on their need to understand the big picture regarding their local government's financial management responsibilities. If there are national meetings of local elected officials, get on their programme to make a short presentation on the potential benefits of supporting LGFM training, not just for their finance officers but other key stakeholders including themselves. The conceptual framework used to put this new series together and the various components is a good place to begin such a presentation.

Follow this with a summary of the kinds of short training sessions you can provide elected officials. For example: a one day session on the various components of an effective and efficient financial management process for their local government; a half day briefing on the operating budget and the financing of this budget timed to happen just before they will be getting the budget from their administrators; a similar briefing on capital programming for those local governments that are establishing a capital programme or faced with major infrastructure expenditures; a similar briefing on assess management and evaluating the financial conditions of their local governments is another possible one-half day training opportunity; and, of course, special sessions on financial planning and policy making and citizen participation in the financial management of their governments are important elected official roles and responsibilities that can benefit from training. As we said, think outside the box in exploiting these materials for your benefit and those who can benefit from training.

- We assume that you already are planning a series of workshops for senior local government finance officers, but don't forget their subordinates who might want to enhance their opportunities to make a career of LGFM. This series, as mentioned before, provides a solid foundation for developing a certificate programme in conjunction with an educational institution, such as a community college or an association serving financial institutions or finance officers.
- Most countries have national government agencies that have oversight responsibilities over local government finances. Professionals in these departments could benefit from training in areas like evaluating financial conditions, asset management, and performance measures.
- One of the co-authors of this series has successfully combined key elected and appointed policy makers with finance officers in one day financial management workshops in Indonesia. She and her local colleagues covered the concepts, principles and strategies of certain topics in morning sessions involving a mix of these participants. In the afternoon, they held skill development workshops for technical and professional staff members on the same topics.

This series is a potential gold mine of opportunities for creative and entrepreneurial trainers and training managers.

MARKETING FINANCIAL MANAGEMENT TRAINING

The potential use of these materials will benefit from creative marketing on your part. While every country has its own values and behaviours regarding marketing, it will be up to each country team to decide what will be most effective in promoting this new training opportunity. Based on our experience and that of others who have carried out successful marketing initiatives, here are some ideas for you to consider.

- Get information out to as many media sources as possible about the financial management series and how you plan to use it. Raise awareness about the need for this kind of training, opportunities for attending such training, and the benefits to be realized. Think about addressing those audiences who are themselves concerned about improving the quality of local governance. These include service clubs, chambers of commerce, and others you are familiar with in your country that support the development of local governments.
- Contact key elected leaders who are trend setters and influential with their colleagues and ask them to help you mobilize support for financial management training. If corruption is a problem in local governments in your country, for example, emphasize the importance of this training. Work with public officials and civic leaders who have expressed concern about the need to curb corruption in local governments.
- If you have one or more local government associations or associations of local government professionals, get them involved in your marketing efforts. If there is no association of local government finance officers, help start one. If there is one, get them involved in your marketing initiatives. If they have a newsletter or journal, get an interview with the editor and provide them with a short article describing the series and how it can help them meet their association's goals and objectives.
- Get invited to their annual meeting or other membership meetings. Offer to make presentations to both explain the series and to solicit interest in follow-up training. Conduct short demonstration training events based on the series.
- Work with trainers and training organisations who have established working relationships with local government and other public and civic institutions. Of course, they may be your competitors. If this is the case, try to figure out how to collaborate so it's a win-win situation for everyone concerned.
- Hold information and demonstration workshops on a sub-regional basis within your country. Often potential training participants expect training to be a series of dull lectures. This series is designed to help you conduct practical, skill oriented, and interactive learning events. Short demonstration workshops can win over those who have had negative experiences with academic-oriented training. It also helps if you can offer these introductory workshops at no cost to the participants. Consider it an investment, an expected cost of launching a new programme.
- Conduct periodic or targeted training needs assessments of local financial management officers and others focusing in part on various roles and responsibilities of potential training participants. Share the results with those who have been assessed and with other key decision makers.
- Once your programme has a sufficient number of graduates, conduct impact assessment evaluations to learn how participants have used their new knowledge and skills to be more effective in carrying out their roles and responsibilities. Use this data and personal testimonies from key par-

ticipants to market new programmes. Also, use the evaluation feedback to strengthen your financial management training initiatives.

- If your region doesn't already have an organisation devoted to building the capacity of other institutions that have the responsibility for local government capacity building, consider creating one. With support from the Local Government and Public Service Reform Initiative of the Open Society Institute in Hungary, Partners Romania Foundation for Local Development (FPDL) has conducted a very successful regional program for capacity building in governance and local government development for central and eastern European countries. They conduct training of trainer programmes based on new materials like this series and provide other on-going support initiatives to trainers and training institutions in the region. FPDL's yearly steering committee meeting involving users of the program assess progress, share ideas and materials, and recommend new initiatives for future support based on their collective needs.

To summarize, raise awareness about the potential benefits of LGFM training in every way possible. If your potential clients for this training don't know what is available, it's hard for them to be motivated to take advantage of it. Hold demonstration workshops at municipal association and other likely meetings. Take your show on the road by offering short one-half or full-day demonstration workshops wherever there is a cluster of potential clients. Join forces with key stakeholders who are concerned with good governance in your country and develop a strategy that involves financial management training as a major component. Create a training capacity building programme and train trainers. Mobilise these trainers to help in the marketing of your programme. Organise it so it's in everybody's self-interest. Carry out impact assessments with participants when they return home from the training. Use the results from these assessments to improve your programme and promote future programmes through personal testimonies from past participants and concrete examples of the training's impact on local government performance.

With this "pep talk" under your belt, it's time to move on to another key component in preparing for training implementation: training trainers.

PREPARING A CADRE OF TRAINERS

Your potential pool of trainers for this financial management series is considerably less than what might be available for a less technical series on leadership or interpersonal skills, for example. Given this potential constraint, it will be important to forge a relationship with a few local government financial managers or individuals with knowledge and skills who you believe will make competent trainers. If there is an association of local finance officers in your country or region, this may be the first place to begin the search for your human resource needs.

Our preference for developing a cadre of trainers is to conduct a training of trainers (TOT) in-country even though the initial market for such training might seem small. The rationale is simple. A TOT is one of the best ways to field test the adapted or translated series. It is also an effective way to identify those potential

trainers you will want to work with initially in your LGFM training programme. It is important to recognise that everyone who completes a TOT workshop will not become a trainer. Nevertheless, they may become boosters for your programme. Assuming you agree with our rationale, here are some ideas about mounting that TOT.

- It's important to have a small team of competent trainers to train other trainers. Our experience in conducting TOTs suggests that a two person team is sufficient to conduct an effective TOT with this training series. But there are no hard and fast rules on how many to include on the TOT training team. Whatever the number, they need an in-depth knowledge about financial management and what's in the manuals, and confidence in their ability and skills to conduct experiential learning events. "Experiential" means interactive, knowledge enhancing, skill-based learning experiences that tap the needs, personal attributes, and experiences of the participants. It is also important for these trainers to be willing to take risks in their designs and training delivery and to be willing to experience occasional failure.
- The quality and number of TOT participants are also important ingredients for achieving TOT success. Before we talk about the quality of your TOT participants, let's talk about numbers. Your TOT for these materials probably should be limited to between eight and sixteen. Many of the training of trainer workshops we are familiar with have organised participants into four person teams who then become responsible for designing and delivering training modules to a group of finance officers on the second week of the TOT. You may be constrained in the numbers you can recruit for your initial TOT because of the requirement that they have knowledge, skills and experience in local government financial management. In terms of recruiting participants for your initial TOT, here are some lessons we've learned over the years.
 - It helps if the TOT participants come from organisations that will support their efforts to participate in financial management workshops once the TOT is completed.
 - Opportunities for success in launching and sustaining LGFM training programmes are enhanced if the participants come as teams who can work together after the training.
 - Requiring previous training experience doesn't seem to be an important factor in the success of TOT participants, although it helps to have mentoring relationships in the initial stages of their development as trainers.
 - When you are fortunate to recruit individuals who have a financial management background and training experience, it is important for them to come to the experience with an open and willing attitude to engage in new learning. The training materials and approach may be quite different from those they have used in the past.

- The tools in each of the manuals are designed to be modified at the trainer's discretion. We encourage trainers to tinker with them, to improve upon them, and on occasion, to take only the core design idea and construct their own learning experience around it. In the TOT part of your programme, encourage your participants to incorporate their own ideas based on the needs of their training clients.
- While there are many ways to design TOT workshops, we are partial to one that is about two weeks long. During the initial week, participants work in teams to design a day or more of training based on the materials in the series. The second week these teams of two to four participants conduct one or more days of training to a group of finance officers with minimal assistance from the TOT training staff. In other words, the TOT participants conduct training work sessions with real live experienced participants. Since this particular TOT design has worked remarkably well in many parts of the world we are confident in recommending it.

As stated before, don't expect every participant to become a competent and successful trainer of elected officials based on a two-week TOT. Nor should you be too concerned about the initial quality of the training your TOT participants deliver when they return home based on such a short TOT experience. We have learned over the years that it is better to have trainers from the same country or culture working with local officials, even though they might not be polished trainers, than some outside trainer with long experience. Trainers graduating from your TOT programme will have another advantage. They will be working with materials that are user-friendly.

ASSESSING IMPACT

While it's impossible to cover all the details about planning for implementation of your LGFM programme in this short User's Guide, we want to mention one more planning detail we think is important. It's the importance of assessing the impact of the training on individual learning and behaviour as well as the impact in the organisations where the participants are carrying out their financial management responsibilities. For example, what will be the impact of the training on improved systems of budgeting, introduction of capital programming, the use of performance measures, asset management systems, better procurement procedures, and more?

The importance of collecting data about the impact of training on organisation and community performance, such as participatory budgeting practices, is very important to your ability to sustain your LGFM training. However, determining how you will measure the impact of your training needs to be determined before you conduct the training, otherwise there are few benchmarks against which you can measure success. To learn more about impact assessments, contact UN-HABITAT for a copy of their *Manual for Evaluating Training's Impact on Human Settlements*.

TRAINING DESIGN AND DELIVERY

Training design and delivery includes a lot of planning tasks although they are different from those we just discussed. In the following discussion you will find an overall checklist of some key design and delivery factors to keep in mind; a look at some logistical factors to consider, such as time, venue and equipment; the importance of adaptation and creativity in using these materials; the art of writing learning objectives; and, how to design learning events that will keep your clients coming back.

There are many factors to consider in designing and delivering effective, efficient, and engaging learning experiences. The following checklist targets some of the more important ones. It is followed by more in-depth discussions about each. By the way, *effectiveness* has to do with providing training experiences for your clients that meet your client's immediate and short-term learning needs. *Efficiency* is how you deliver the training. *Engaging* is the process of involving your participants through sharing their ideas, life experiences, and visions about the future.

- Effective, efficient and engaging training is driven by purpose. Your ability to write clear and concise objective statements that describe what you plan to accomplish during the learning experience is the most important design task you will undertake.
- The quality of your learning events will be determined in large measure by the time and energy you invest in adapting these materials to fit the situational context of your participants.
- Complete learning events involve the infusion of new knowledge, ideas and insights and the opportunities for participants to process and apply these infusions based on their individual and collective experiences and needs.

The most insightful learning design can be sabotaged by external factors. Fortunately, most of these externalities are within your control, but they need to be managed.

Since the need to cope with the last set of factors often precedes efforts to sit down and design the training event, let's look at them first.

MANAGING THE EXTERNAL FACTORS

It's impossible to design and deliver an effective training programme without taking into consideration many of the external factors that will often determine just how successful you will be when you begin the training. While most of these may be obvious to many of you, they are still worthy of review.

EXPECTATIONS

To the extent possible, narrow the expectation gap between you as the trainer and the workshop participants. Your workshops are more likely to be effective if the par-

ticipants know ahead of time what they will be learning and the process to be used to facilitate their learning. This can be important if your intended audience is likely to have experienced only lecture-oriented training in the past. You might also consider developing a training calendar that can be provided to client organisations such as municipal associations, so they can announce when workshops on various topics will be available, their length, and location.

We encourage you to negotiate a mutually agreed-upon contract with potential training clients. These clients might be a cluster of local governments, an association of local governments, or even an educational institution that wants to broaden their services to local governments. Individual training contracts allow the trainer and the client organisation to be much more explicit about training content and scheduling. In any case, it is important that information on training content and approaches is specified beforehand so that participants know the learning opportunities being made available to them.

DURATION AND TIMING

The number of workshops to be conducted, their duration, and the sequencing and timing of training exercises depend on a number of considerations. If you can schedule the training as a single programme (e.g., one or two weeks in length) involving participants from many organisations, you will have considerable control over content and schedule. A series of 2 or 3-day workshops designed to cover the entire series presents a different design and scheduling problem. Since the materials provide lots of optional learning exercises for each of the subjects covered in the series, there is a substantial amount of design freedom built into their use. Be particularly careful to include enough time for participants to process the information being covered in every exercise or workshop fully before moving on to the next. Build reflective time into the overall design so that individuals and small groups can informally explore in more depth the issues and topics being covered.

LOCATION AND PHYSICAL FACILITIES

It is important to create an environment that supports learning, one that removes participants from everyday distractions and encourages them to think and act in new and different ways. Some of the worst training venues are those associated with the everyday work activities of the participants. Some of the best locations have been somewhat remote and rustic settings. These kinds of environments seem to foster a greater willingness to be open and to take risks in their interactions with others.

The physical facilities are also important. Look for workshop venues that offer privacy, have movable furniture, and provide enough space for several small groups to meet concurrently. Auditoriums and large, open buildings are usually not flexible enough and lack the intimacy needed for effective interaction. It is also important to arrange things so that participants are not interrupted by non-participants, telephone calls, or other annoyances during training sessions.

EQUIPMENT AND TRAINING AIDS

Be sure that you have access to materials and equipment that can be transported easily or can be supplied by the training venue. Essential items include flipcharts, easels, numerous pads and markers, and an overhead projector or other audio-visual equipment that is compatible with your needs and expectations. If you plan to use power point presentations, check to see that everything is in good working order and have contingency plans when something malfunctions. Our experience tells us that anything that can go wrong will and at the last moment. Prepare participant hand-out materials including instruments, questionnaires, checklists, and worksheets in advance and make provisions to have access to photocopy equipment or service at the training site.

NUMBERS OF PARTICIPANTS

We discussed earlier the number of participants we believe optimum for training trainers. While we won't be dogmatic about the number of finance officers or other public officials you can involve in LGFM training, we think there are some good guidelines to consider. Groups of 16 to 24 are just about ideal for one or two trainers to facilitate. These numbers also lend themselves to small group work sessions of four, six or eight members each. If you begin to include more than twenty four, although we realize this number is arbitrary, it makes the experience less intimate, more impersonal, and cuts down on the time that each member of the group has to contribute to the interaction. Unfortunately, these decisions are often determined by funding constraints.

We've covered only a few of the important external factors that can influence the quality of the learning experience you will be designing and delivering for the benefit of others. While there are obviously many more, we don't want to deprive you of the opportunity to discover them yourself as you initiate your LGFM training programmes.

KNOW WHAT YOU WANT TO ACCOMPLISH AND STATE IT CLEARLY

As we said earlier, effective, efficient and engaging training is driven by purpose. Your ability to write clear and concise objective statements that describe what you plan to accomplish during the learning experience is the most important design task you will undertake. Here are some thoughts about how to do this and maybe even a few that are unconventional.

The best roadmap for guiding you to successful learning experiences is a clear statement of your overall goal and objectives. If you are able to state these clearly, you have increased your chances of success immeasurably. Now writing learning goals and objectives can be dull, deadly business. We don't know a trainer who enjoys doing it. And yet it has to be done. The old adage, "If you don't know where you are

going, you probably won't know when you get there," applies to learning design. It's not a very attractive alternative for either you or your workshop participants.

We are using two terms, *goal* and *objective*, to describe aspects of your learning roadmap. The *goal* we see as the accomplishment of the overall expectations you hope to fulfil with your participants as a result of the learning experience. It's the super-ordinate objective you hope to achieve, a statement of the big learning picture. *Objectives* are sub-goals, or statements of those things you want to accomplish through specific learning experiences during the workshop.

Many training textbooks recommend writing objectives in the following way: *By the end of the training, participants will be able to demonstrate their ability to write a policy statement*, or some other concrete task. This implies that we are going to be testing them in some way to make sure they can do it. This strikes us as being a bit too academic. Given this, we will reveal our own bias about this onerous training-design task, but not before making it clear that you should feel free to write learning objectives in any way that you feel clearly states what you plan to accomplish in the workshop.

We often write learning objectives based on what it is possible to accomplish through experiential learning. This includes:

1. increased knowledge and understanding;
2. new or improved skills, either technical or relational;
3. new or altered attitudes and values; and
4. creative acts.

The first two are standard learning objectives associated with knowledge and skill-based training. The next two are harder to defend. Let's look at the third one on attitudes and values. Some still argue that you can't change these personal attributes through training. We disagree. Take, for example, someone who believes strongly that citizens should not be involved in the local government budgeting process. Now that's an attitude, but it might also be a value that this person believes in. Through a learning experience, this person begins to understand the importance of citizen participation. Beyond the workshop, this person demonstrates this new attitude and value by supporting a move to involve citizens in local budgeting decisions.

There is no question that helping others alter their attitudes and values is a difficult learning objective to accomplish, but often it is the cutting edge of important community changes. Don't shy away from these more emotionally charged learning opportunities.

Regarding the fourth objective, "creative acts," it's more curious than difficult. What if you ask participants to develop an action plan as part of your learning objectives or outcomes? It hardly fits in the first three categories, so we invented a fourth.

The ultimate learning outcome is, of course, behavioural change. If local government officials and others do not change their behaviour as a result of learning new concepts or strategies, acquiring new or improved skills, or even changing a few attitudes and values in a learning experience, then the training investment is lost.

Another important distinction to keep in mind when designing learning programmes is the difference between *outputs* and *outcomes*. For example, when partici-

pants demonstrate that they know how to develop financial strategies to assure that basic local government services can be provided to low income neighbourhoods, this is an “output.” They have learned how to develop such delivery strategies during a workshop. When they go back to the organisation and lead the charge to implement their strategy, based on the knowledge and skills gained in the workshop, it is an “outcome.”

ENGAGE IN ADAPTATION AND CREATIVITY

You need to take advantage of the opportunities in your immediate working environment to make these materials and the training you will be conducting as relevant, timely, and client-centred as possible. Here are a few guidelines to train by:

1. If you decide to use a case study, role play, simulation, or any other tool from any of these materials in your training programmes, adapt it to meet your needs and the learning needs of your participants. Change names, locations, circumstances, and anything else that says, “Not invented here!”
2. Talk to some finance officers or other practitioners before you sit down to finalise your workshop design. Ask them if they have any interesting experiences that might relate to the topics you plan to cover. If so, check to see if you can incorporate them into your design.
3. Whenever possible, exploit your participant’s experiences in the financial management competencies you are covering in the workshop. Use these experiences to create new learning exercises, or to modify those in the materials. For example, you can create a role play right on the spot based on something that might be bothering many in the workshop. Or you can have a participant describe a particularly difficult situation that he or she is experiencing and break the others up into small discussion groups to determine what they might do in this situation.
4. Look in Part One section of each chapter, the *Concepts, Principles, and Strategies* part, for clues to develop your own exercises. For example, many of the Learning Application exercises are ready-made to be turned into workshop learning experiences.
5. Don’t be afraid to deviate from your workshop design or agenda when you see an opportunity for significant learning emerging out of the dialogue and energy that has been created by your participants.

DESIGNING LEARNING EVENTS

If you are able to decide with clarity what you want to accomplish during a workshop, seminar, or some other kind of planned learning event, you have cleared the first and most important training hurdle. We are, of course, assuming that you have also arrived at these conclusions in consultation with your client(s) and their training needs and transformed your ideas into written statements of purpose, goals, and objectives

that are concise, understandable and doable. If so, then the next step is to figure out how to accomplish them within the time allotted. This is the training design part of the puzzle.

As we said in our overview comments leading into this discussion on training design and delivery, effective, efficient and engaging learning events involve three interrelated activities: 1) the infusion of new knowledge, ideas, and insights; 2) the opportunities for participants to process these infusions, based on their individual and collective experiences; and 3) the application of what they have learned to their individual, work team and organisational needs and opportunities. Complete learning designs should, whenever possible, include a mix of input, processing and application.

The first two of these interrelated components are common to most experiential training designs. We provide new ideas, information, concepts and strategies as input, and we design some kind of interactive experience so participants can process the new input. The third, *application*, is less frequently used mostly because it is more difficult to design into training, or so it seems. Application is evident when we have participants complete an action plan design a new revenue reporting form in a financial management workshop, or develop a list of stakeholders who might be important to consider in carrying out a community development project.

The most important thing to remember about these three interrelated components is their complete flexibility. You can start with any one of the components and move to the other two in whatever sequence you want. While it is fairly common to provide a lecture, for example, and follow it with some kind of exercise to process the content of the lecture, it is less common to start with an exercise and then insert the lecture. When you realize you can start with any one of the three components and move to the other two in whatever sequence you choose, you have one of the most important value-added dividends of experiential learning at your command². Before we move on to training implementation, we want to share with you the workshop template that Eva Balazova, the godmother of these materials, uses in designing her learning events. The overall framework includes:

1. The aims and objectives of the workshop;
2. The timeframe and agenda which spell out in detail what the participants can expect from one session to another; and
3. Lessons learned during the experience, back home planning, and evaluation.

Within the overall framework Eva designs around the following agenda:

1. Welcoming statement and introductions of staff and participants;
2. Learning aims and objective: what she and her staff plan to accomplish;
3. Information about the programme and logistics;
4. Ice breaker or energiser, depending on which seems most appropriate given the group;
5. First learning block includes cognitive input from the chapter being covered, i.e. lecturette, guided discussion, interactive presentation using visual aids;

6. Second learning block includes use of experiential materials from the tools or from her experience as a trainer, i.e., case study, role play, assessment instruments, problem solving exercise;
7. Based on the length of the workshop and the maturity of the group in the subject matter Steps 5 and 6 would be repeated; and
8. The completion of the workshop experience includes a participant look at lessons learned, preparation of personal plans by participants to indicate how they plan to use lessons learned back in their organisation, and workshop evaluation.

We believe this template is an effective one to use in designing experiential learning experiences for professionals. Of course, it's up to each individual trainer to arrive at a process that works best based on experience and results. As the expert group reminded us on more than one occasion these materials need to be *descriptive* and not *prescriptive*.

IMPLEMENTING TRAINING DESIGNS

Each of the volumes in the *Local Government Financial Management* series consists of exercises and activities developed and sequenced to provide a comprehensive learning experience for your participants. They include role plays, case studies, simulations, instruments, and other learning opportunities that can be arranged in various combinations. These are designed to help participants make sense out of the concepts and ideas being presented in Part One of the chapter.

The exercises we have included in the chapters are all structured in about the same way although the subject matter from chapter to chapter is different. For example:

- Each exercise begins with a general statement of the objective to be achieved and an estimate of the time required. While staying within the recommended time frame is recommended, don't be a slave to it. Use your judgment. If the exercise has sparked lively and important discussions don't cut it off by saying, "Sorry, but we've scheduled a role play, and we need to get on with it." That's an example of the trainer meeting his or her needs and not the needs of the participants and is very dysfunctional. If it takes longer to complete an exercise than scheduled, you can either make up the time elsewhere in the workshop or discuss with the participants the need to add a bit more time to the schedule.
- Following the objective and suggested timeframe we have provided a step-by-step set of instructions on how to conduct the learning event. We call this the *process*. Occasionally, the process will include variations or alternatives for your consideration particularly if the exercise is to be used with participants who work together and may be interested in improving their team performance. A time estimate may be provided for various steps in the process.

- The process description is often followed by worksheets to be either read or written on by participants. Typical worksheets include cases, role-play situations and role descriptions, instruments to be completed, questions to be answered by small groups, and other participant-involving things. Hopefully the instructions on these worksheets are clear and easy for participants to read. If not, change them to meet your needs. All worksheets included in the chapters are designed and intended for mass duplication.

Each chapter includes an example of a warm-up exercise. Warm-ups are the means by which you begin moving participants from the known to the unknown and start the process of getting them acquainted as early into the workshop as possible with others, the learning process, and you. We haven't included different warm-up exercises in each of the chapters since most trainers and many of the participants have their own favourite exercises they like to use. Don't hesitate to involve your participants in providing and conducting their own warm-up exercises and energisers.

Many of the exercises in this series are designed to involve discussions and group problem solving on specific aspects of financial management. The intent of these exercises is to help workshop participants gain a working knowledge of a useful idea, strategy or process and at the same time some experience in using the new knowledge. For example, participants are introduced to brainstorming in one of the manuals, one of the common methods for generating ideas to solve a problem or make a decision. In another chapter participants are encouraged to use *force field analysis* as an analytical aid in planning ways to remove obstacles to the attainment of an operational goal. Many of the chapters include exercises that have general applicability to more than just the topic being discussed. Given this, you might want to get acquainted with what is available in all of them before designing workshops on specific aspects of financial management.

A number of the training tools are designed to build on participant-contributed situations or problems. Working in small task groups, they are asked to analyse the situation and suggest courses of action to be reported on during a plenary session. In other suggested workshop designs, there are problem-solving activities supported by worksheets. These are intended to be completed by participants working in small groups as an aid to analysis and for later reporting. Worksheets are useful for at least two reasons: they provide a record of small group reactions to the assigned tasks, and they give participants written record of their small group's results to take home with them.

At the completion of each workshop design is a skill-transfer exercise. The intent is to help participants begin the transition back to the "real world" of participating elected officials. It is important that participants begin making definite plans for trying out or changing certain aspects of their performance responsibilities. These plans are more effective if they are made in writing, realistically critiqued, and shared openly with other participants.

We have been talking about the tools in each of the chapters as though they are also workshop designs. They are, and they are not. They are because they include a sequence of training exercises that can be selected to conduct a workshop based on the substantive material covered in Part One of each chapter. They are also sequenced to help you develop a learning rhythm in your workshops.

However, we never intended that you should use all the exercises in one workshop, nor to adhere rigorously to the sequence in which they are presented. In this respect they are not workshop designs. Use your imagination, and your design knowledge, skills, and experience to develop a workshop design that will work for you and your participants.

FACILITATING SUCCESSFUL SMALL GROUP LEARNING ACTIVITIES

With the possibility that we are repeating ourselves on some of these issues, we will nevertheless press on with some clues about how to work with small groups. We will focus on three aspects of managing small group learning: giving instructions, monitoring their progress or lack thereof, and helping them to report out and process what they have learned.

GIVING INSTRUCTIONS

Most experts on giving instructions agree on one thing: begin the instruction by giving participants a rationale for the task or exercise. When participants know *why* they are being asked to do something, they will be far more interested in learning *how*. Beginning with this expert-driven mandate, giving good instructions can be viewed as a simple, four-step process.

- Introduce the exercise by giving a rationale. This should include the objective of the exercise and anything else you might add to help participants see the importance of the exercise from their point of view.
- Explain the task. Describe what participants will be doing. Usually the task of a small group is to produce a product. Use active verbs to describe the product such as, “list the three most important...” or “describe an incident in which you were involved that...” Make the transition from the rationale for the task to the explanation as smoothly as possible.
- Specify the context. It is important for participants to know who they will be working with, under what conditions, and how long. The context of the exercise spells out how they will be accomplishing the task.
- Reporting. Let them know that they will be asked to report out to the larger group the results of their small group discussions. The purpose is not just to explain what happened but to advance the process of learning. Reporting allows participants to share their experiences with one another, hopefully enabling them to expand, integrate and generalize learning from their individual or small group experiences. Ask them to decide on who will represent them in this reporting process before they begin their discussions.

MONITORING SMALL GROUP ACTIVITIES

When participants are busy carrying out the tasks you have assigned them, you need to be busy keeping track of how their work is progressing. We call this monitoring. Monitoring is important for two reasons:

- It gives you feedback on how well participants know what they are supposed to be doing and how committed they are to the task. If you sense confusion, misdirection, or misinterpretation in a group, you may need to restate the task, perhaps by paraphrasing the original instructions or augmenting them with an example.
- It helps you to adjust the time needed for the task. Even the most carefully designed small group exercise will require some adjustments in the amount of time it takes to complete certain tasks. Each participant group is different. Therefore, your concern should be with assuring the small groups enough time to gain the most learning value for its members.

When you have given small groups their instructions, stand quietly and wait until they have convened and have gotten underway on the task. After a few minutes, circulate to find out how things are going. Enter the work area quietly being careful not to interrupt. If you are asked questions, and you usually will be, answer them briefly. If one small group's questions suggest there may be confusion in the other groups, then interrupt the others and re-phrase appropriate parts of the task for all of them.

As groups proceed with the task, there are several aspects of their activities you should be aware of and intervene in if it seems necessary to help them be more productive:

- Is the physical space and seating conducive to participation by all the members, or are some participants isolated?
- Are there changes in the noise level in the group? These changes may indicate that a group has finished its task, just getting down to work, or perhaps confused about the task. In any event, you need to check it out.
- Do participants seem to be working on the task, or are they engaged in idle conversation? If participants are discussing matters unrelated to the task, they may be finished, or they may be avoiding the task. Check it out.

Based on the task given and the time remaining, are participants behind, ahead, or on schedule? If time is running out but participants are still working intently, it may be more desirable to give them more time. When you notice that some groups are finished and others are not, you might offer a time check, "You have two minutes left," for example.

FACILITATING THE REPORTING PROCESS

By reporting, we do not mean a detailed, “this is what we did during our meeting” recital. Rather, the term “reporting” is intended to mean an opportunity to share the most important observations and conclusions of the time spent by a small group on a task.

Logistics are an important aspect of facilitating small group reporting. What group will report when, and who will represent them? What kind of reports will be expected-- on newsprint, orally with no visuals, or by power point? One of the authors worked on a training programme in one of the Pacific Rim nations where every group was expected to make computer-assisted reports.

Time is also an issue in reporting and it needs to be managed. For example, you can have each group report two or three items from its list rather than report every item. Another approach to reporting is to have each small group examine and report on a different aspect of the same topic. Finally, where small groups have been working on the same task and some kind of synthesis or consensus is needed, a polling procedure can be used. For example, have each small group place its recommendations on a sheet of newsprint which is posted for all to see. When all the sheets are posted and reviewed, comparisons can be made, differences noted, and confusing entries clarified.

Three skills are required to facilitate the reporting process effectively:

- Asking initiating and clarifying questions. To help initiate and clarify group reports, you need to be able to ask direct, but not leading, questions. These should be open-ended questions usually beginning with what, when, where, how, or why such as, “What are the implications of this method given your role as a finance manager?”
- Paraphrasing. This is important to be sure you are actually hearing what the participant meant you to hear. Your objective is to assure the participant that you are listening and that you are eager to know if you have heard correctly. For example, if someone reports that, “*Elected officials have difficulty adopting the budgets we prepare for them,*” you might paraphrase or restate what you heard for clarification by saying, “*You mean elected officials know they have the responsibility to adopt the budget but often find it difficult because of conflicting priorities.*”
- Summarizing. While paraphrasing is meant to mirror the meaning with a change of words, summarizing is to synthesize or condense a report to its essentials. The intent, once again, is to test for understanding. Efforts by a trainer to summarize or reduce information to its essentials might begin with phrases like:

“In other words “

“If I understand what you are saying, you mean....”

“In summary, then, you feel...”

SOME THINGS TO CONSIDER IN USING TRAINING TOOLS

While the training exercises in each of the chapters provide some of the important tools needed to construct a series of elected leadership workshops, they still need the skills of the master builder to apply them with success. Here are a few ideas on how to work with these tools more effectively.

BE FLEXIBLE

Flexibility in working with the training materials and the participants may be the most important and often most difficult skill to develop as a trainer. While most of the exercises in the chapters can probably be conducted without a lot of modification, we don't recommend it. There are many reasons for this. You might experience time constraints that will require you to "cut and fit" the exercise to fit the time available. The participants may have different expectations from those assumed when the exercise you want to use was developed. There may be something about the exercise that just doesn't feel right in the culture in which you are working. Your participants may have actually raced ahead of you in discovering something that is important to them, and they want to talk about it in more depth. It's important to be flexible, to seize the opportunity of the moment.

ENRICH THE CONTENT

While we have tried to provide enough content materials in Part I of each of the chapters to get you through most workshops, we encourage you to enrich the content with local examples, new concepts or strategies that you might have discovered, or even evidence that refutes what we have written about so eloquently. The world of local government financial management is changing rapidly, and whatever we write today may be out of sync with tomorrow's reality. As you prepare for each workshop, enrich the content with current examples and new ideas that build upon, or even refute, the concepts, principles, and strategies we have provided.

There is another content enrichment opportunity that is available in every experiential learning experience that yearns to be tapped at any given moment. That's the experience, wisdom, and ideas of the participants. While we have included a number of different approaches to collecting and evoking information and ideas from your participants in the various chapters, we encourage you to invent your own. One of the most successful techniques we have found to get a lot of ideas out quickly and organize them into some logical framework is to use large index cards. Have the participants respond on these cards with their ideas, ask them to attach them to a blank wall with paper tape and then rearrange them into logical categories for processing.

There are, of course, many ways to tap the experience of participants to add to the content of each workshop. These include developing instant case studies or critical incidents based on their experience rather than using ones that have been included in the chapters; asking participants to take various positions in a role play that reflects a situation they might be struggling with in their own communities; or creating an instant simulation based on the needs of the participants. For example,

the simulation might involve a budget hearing where citizens have, for the first time, been given the opportunity to participate in the deliberations.

PROVIDING BALANCE AND RHYTHM

Designing workshops is a bit like writing a musical score. You need to take into consideration things like sequencing events, balancing your instruments and their impact on the overall production, and assuring that the rhythm doesn't bore either the audience or the conductor(s). For example, the arrangement of exercises and presentation should proceed naturally from the more known to the less known, from the less complex to the more complex, from the less interactive to the more interactive. Every component of the workshop should contribute to the attainment of workshop goals. Even the refreshment breaks, meals, and free times should be placed strategically.

And don't forget those ice-breakers, energisers, and openers that are so important to group growth and on-going maintenance. They serve the needs of those who join together to learn and implement what they are learning. Since some of us get these tools confused with each other, it might be useful to describe them and how they differ.

Icebreakers and openers have a lot in common, but also some differences. Icebreakers are relatively subject-free activities whereas openers are often related to the content of the workshop. Icebreakers are typically used when workshop participants don't know each other. They are designed to help members get acquainted and become more comfortable as learning partners. Openers, on the other hand, are tools to help participants ease into the subject matter. They tend to set the stage for interactive learning; help the group, including the facilitator, avoid abrupt starts; and generally help the participants get comfortable with the content material. An opener may be as simple as asking the participants to share in pairs what they think is meant by "asset management" when that particular topic is introduced.

The other type of climate-building and group-maintenance exercise is the energiser. Typically, it's a fun event to get the group's collective energy level up when the group seems to have hit a slump. Don't hesitate to use these group "environmental tools" to open your workshops, to help everyone get acquainted, and to infuse a bit of adrenalin into the learning community when it's fuel tank seems to be on empty. If you want to learn more about these tools, check with your training colleagues or get on the internet and surf for ideas. If these two options fail, just ask your participants to lend a hand. Our experience it that most groups have individuals who are skilled in running these types of exercises and enjoy the opportunity to become involved.

PROCESS THE WHAT, WHY, AND HOW OF LEARNING

Polly Berends, in writing about how we learn, said, "Everything that happens to you is your teacher. The secret is to learn to sit at the feet of your own life and be taught by it." To paraphrase Polly's metaphor about self-learning, everything that happens in a workshop is important. The secret is to keep on top of the *what*, the *why* and the *how* of your learning design and process them. Processing is simply an activity that is designed to encourage your participants to plan, reflect, analyse, describe, and com-

municate throughout the learning experience. These are the events that encourage the transfer of learning from the workshop environment to the real-world working life of your participants. Here are some processing techniques to consider:

- Use observers to report on the process or outcome of an exercise.
- Ask participants to serve as consultants to one another to stimulate thinking and problem solving.
- Divide participants into several smaller groups for rapid processing of new ideas and information and provide for reports and summary discussions.
- Leave time for participants to reflect on what they have been learning and doing.
- Encourage back-home application by having participants develop written plans about what they plan to do to apply what they have learned to their roles and responsibilities as elected officials.

ENCOURAGE PARTICIPATION BUT DON'T OVERDO IT

While an important trainer role is to stimulate participants to exercise more freedom in thought and action, it is important not to force any activity that might cause them to feel threatened or intimidated. This is particularly true if people are attending a workshop involuntarily or with strong reservations. Be sensitive to the feelings and needs of all participants. Don't expect your participants to involve themselves with equal enthusiasm in every single activity.

CELEBRATE OPPORTUNITIES TO LEARN

Every significant learning experience is a cause for celebration. While you will need to determine what is "significant" based on your experience and the norms of your situation, we tend to think that a week or more of training deserves some kind of celebratory event. It may be a closing luncheon, the handing out of certificates of participation, a group photograph, or something more significant depending on the time and personal commitment of your participants. If you have a large number of officials participating in the full series of workshops, you might consider holding one large celebration or reunion once a year. This could provide publicity for your program and also an opportunity to make it more elaborate.

HAVE FUN!

We came across a French proverb while writing this part of the Trainer's Guide that sums up one of the most important qualities of a learning experience. The most wasted of all days is the day when we have not laughed. Think about your own experiences as a trainer or participant and the ones you have treasured and remembered. So, have fun knowing that laughter in the midst of learning is a no-cost, value-added commodity.

LEARNING APPLICATION

While training is the accepted strategy throughout the world for workforce development, it's expensive. A good return on your training investment is assured when (1) the training addresses real performance discrepancies and skill needs; (2) the training is competently designed and delivered by experienced trainers; and (3) those who have attended the training apply their new knowledge and skills to improve work performance. All of these factors must be present for training to meet the expectations of those who invest in it. But it is the third that is the most problematic. Unless those who are trained make the effort to use what is learned to correct discrepancies or to modify or change their behaviour, the investment is lost. Here are some thoughts on what you might do to help participants apply what they learned when they return home from your workshop.

Sharing experiences. The opening session of any skill based workshop is not too soon to raise the importance of how the participants will apply their new-found knowledge and skills when they return home. If this is one of a series of open enrolment workshops on the various roles and competencies, you might ask if any participants have attended earlier workshops on the series. If so, invite them to share their experiences in applying what they learned. This sharing technique can provide continuity and remind other participants that it is important to think about how they will apply what they will be learning to challenges in their local leadership role.

Learning objectives. It is important to include near the start of any organised learning experience a discussion of the objectives you hope to achieve as a group. However, it's not so common to ask participants to develop their own set of learning objectives based on the workshop content and design. We suggest you do. Have them write their own learning objectives and remind them that they will be asked to return to them at the end of the workshop when they prepare an action plan based on what they plan to do when they return home.

Action Planning. In each of the chapters we have included a Learning Application Plan worksheet. We encourage you to have each participant complete this form, or one of your choice as a trainer, before the workshop closes. It's an important way to help participants reflect on what they have learned and how they plan to use what they have learned for their own continuing professional development and the development of their organisation.

BASIC TRAINING TOOLS

While the chapters offer enough training materials to help you design and deliver a full-scale local government financial management training programme, we decided to supplement these with a few basic tools of the trade. Think of these learning components as parts from which you can design and build an experiential learning event. They are largely interchangeable although their success depends on a number of environmental variables. For example, the number of participants you are working with, the time you have available, the mix of participants, and most importantly, what you hope to achieve. Start with your learning objectives and your learning audience and

then decide which of these might be helpful in constructing a winning workshop design.

PRESENTATIONS

Trainers who believe in andragogy, a fancy term for adult education, and experiential learning, which translates roughly into learning-by-doing, are usually horrified to even mention the word lecture in the company of other trainers. Instead we use such terms as *lecturette*, *guided discussion*, and yes, *presentations*. However, there are lots of opportunities when it is both appropriate and essential to present ideas, concepts, strategies, data, and other cognitive stuff to achieve your learning objectives even in the most interactive training experience. Following are a few ideas to help you make presentations that will keep your participants from snoring.

Presentations are useful for explaining new concepts and subject-matter details and to stimulate critical thinking. Used in conjunction with other learning methods, presentations help workshop participants become better informed, involved, and comfortable with learning new things.

Presentations are more than just a way of delivering information. You can use them at the start of a workshop to establish a proper learning climate, promote interest in learning, and reduce participant anxiety. You may present information spontaneously at any point in the workshop to stimulate thought, introduce exercises, clarify or interpret a new concept, or test for comprehension. Finally, you can take advantage of presentations at the conclusion of a workshop to summarize important lessons learned and encourage learning transfer.

Many trainers see the presentation only as a form of information delivery. Viewed from a broader perspective, the presentation is an opportunity for the trainer to get a group of participants involved in their own learning. This is more likely to happen when a presentation includes planned or spontaneous participant-involvement techniques sometimes referred to in the chapters as *guided discussions*. Here are a few clues on how to engage your participants in your presentation:

1. Ask participants to think about and discuss situations in their own work experiences that illustrate a concept you have just introduced to them as a way of helping them see its practical application to their own work.
2. Ask participants to answer questions about material just covered or restate in their own words what they just heard you say as a comprehension check before going on to new material.
3. Give participants a handout that covers some aspect of the material being presented orally and include some blank spaces in the handout for their use in writing down their own interpretations or possible job applications of the material being discussed.
4. Most important, use visual materials to supplement your oral presentations, i.e., flipcharts, chalkboards, overheads, and, if available, computer-assisted materials. These help to keep participants awake, lengthen their attention span, increase the retention of new information, and lessen the chance of your being misunderstood.

In summary, successful presentations are planned with four considerations in mind.

- They are brief, focused on a few key ideas and packaged to deliver information in “bite-sized” chunks.
- They are designed to include provocative beginnings, convincing middles, and strong endings.
- They give participants ample opportunity through question and answer techniques to demonstrate their comprehension, and to compare viewpoints and experiences with the trainer and other participants.
- They respond to the needs of participants to experience multiple ways of accessing information and ideas.

DISCUSSIONS

Discussion is any interaction between two or more people on a topic of mutual interest. The types of discussion used in this series are of two kinds depending on the trainer’s role. In those that are trainer-guided, the trainer takes an active and direct part in guiding and directing the discussion. In what is sometimes called a structured discussion, you will be letting participants manage their own deliberations.

In the trainer-guided discussion, the objective is to encourage participants to think about, relate to, and internalize new ideas related to a particular topic. While usually planned as a way of processing case-study data, role-playing experiences, or other exercises, such discussions may occur spontaneously during a presentation or near the close of a workshop. How productive they are will depend on how experienced you are with the question-and-answer method and your knowledge of the subject.

In a structured discussion, the objective is to engage participants in idea generation or problem solving relative to an assigned topic and to demonstrate the value of teamwork — interdependence. You need little subject-matter expertise to initiate a structured discussion. Normally, you will divide the participant group into several small groups of about equal size and assign the same or different tasks to each group. After tasks are assigned, a period of time is allowed for the small groups to discuss the task. You might want to give instructions to the small groups about appointing a leader, a reporter, and a timekeeper. At the end of the discussion phase, small groups are asked to come back together and to report their findings, sometimes written on flipchart paper which can be taped to a wall of the training room.

Sometimes, the focus of small group discussions is on the process of working together as well as the product of the group effort. There is much learning value in exploring relationships or patterns of interaction among participants as they work together to solve a problem, decide on a course of action, or carry out some other task. You might decide to select one or two participants to be observers. Ask them to monitor the process of interaction among participants as they work together on tasks. Assure that this is being done with the knowledge and consent of other group

members. Their final task is to feed back their observations and conclusions to the group when it has finished work on its assigned task.

In summary, the discussion method can stimulate participant involvement in the learning process. Trainer-guided discussions are of value principally in stimulating logical thinking. However, subject-matter expertise is required if you plan to lead such a discussion. Structured discussions, on the other hand, help participants to become self-reliant, to develop team thinking and approaches, and to be less dependent on the trainer. Your role in discussions of this kind shifts to coach and interpreter. Through mutual exploration, struggle, and discovery, participants in small groups gain insight and the satisfaction that comes from having attained these insights.

CASE STUDIES AND CRITICAL INCIDENTS

Under this heading we will discuss two types of exercises that are used in this series: (a) the longer traditional *case study* used in many professional schools and (b) an abbreviated version of the case study called the *critical incident*.

TRADITIONAL CASE STUDIES

The case study is an actual or contrived situation, the facts from which may lead to conclusions or decisions that can be generalised to circumstances experienced by those taking part in the exercise. Put another way, a case study is a story with a lesson. Cases used in training can take many forms. They may be quite long, complex, and detailed. Or they may be short and fairly straightforward similar to the one-to-three page variety found in the series.

The case method assumes group discussion. The well constructed case stimulates participants to analyse and offer opinions about (a) who was to blame, (b) what caused a person to behave as he or she did, and (c) what should have been done to prevent or remedy the situation. The more important contributions of the case method to training include:

- Discouraging participants from making snap judgements about people and behaviour.
- Discouraging a search for the one “best answer.”
- Illustrating how the same set of events can be perceived differently by people with similar backgrounds.
- Encouraging workshop participants to discuss things with each other and to experience the broadening value of interaction.
- Emphasising the value of practical thinking.

CRITICAL INCIDENTS

Closely related to case studies, critical incidents are brief, written descriptions of situations that are familiar to the workshop participants. They can come from several sources: (a) the workshop participants themselves; (b) participants in earlier workshops; (c) anecdotal information collected by the trainer through interviews and

surveys; (d) secondary source material such as journals, books, and manuals on the topic; and (e) the trainer's fertile imagination. When preparing a critical incident for use in a workshop, there are several design ideas to keep in mind:

- Keep them short—several sentences are usually enough—and simple so they be read and understood quickly by workshop participants.
- Because incidents are short, they need to be tied directly to the workshop objectives.
- Include enough detail about the problem to emphasise the point of the incident.

When asked to write a critical incident, participants are instructed to think of a difficult situation related to the training topic. They should describe the situation briefly, state who was involved in it, and the role they played. Depending on how the incident is to be used, participants might be asked later to explain what was done about the situation and the resulting consequences.

A critical incident can be as simple as a participant saying,

The mayor has been turning in travel, lodging and meal expenses that are far in excess of those allowed in the city's regulations. In fact, it looks like he is using these otherwise legitimate expenses to run his private business on the side. As the city's newly appointed finance director I'm concerned about the consequences of this for the city, the mayor, and, of course, my job. I raised the issue with him a month or so ago and he vehemently denied any wrong doing and told me to mind my own business. When I mentioned this to my assistant who had been with the city for several years, he told me that the previous finance director had been fired for confronting the mayor about his expenses and that I needed to be careful. I've only been in the job for about six months and can't afford to get fired. What should I do?

ROLE PLAYING

Role playing involves asking workshop participants to assume parts of real or imaginary persons, to carry out conversations, and to behave as if they were these individuals. The intent is to give participants the chance to practice new behaviours believed appropriate for their work roles and to experience the effect of behaving this way on themselves and on others who are playing related roles. It is generally believed that on-the-job application of new behaviours increases to the extent that people are willing to try out and evaluate the new behaviours under supervised training conditions. Few training methods offer more effective ways to encourage experimentation with new behaviours than role playing.

To provide the context in which role playing can achieve significant participant learning, couple it with the case study or critical incident method. After reading and discussing a case study or critical incident, invite participants to step into the roles of the individuals featured in the situation. Realism is enhanced when detailed role descriptions are developed for each of the role players.

If an individual is resisting the opportunity to become involved in a role play, it is better not to push them into participating. It is up to the trainer to establish the tone for role playing. Provide firm direction when moving a group into role playing by establishing ground rules and the boundaries of good taste. Bring the role play to a close when it begins to lose its realism and learning value.

Here are some useful steps to take in setting up and directing a role play.

- Introduce the setting for the role play and the people who will be represented in the various roles. If names are not given, encourage role players to use their own names or provide them with suitable names for the roles they will be playing.
- Identify participants to play the various parts. Coach them until you are satisfied they understand the “point of view” represented by each part. Participants may be asked to volunteer for roles, or you may attempt to volunteer them for roles in a good-natured way.
- Ask participants who play roles to comment on what they have learned from the experience.
- Ask other participants to give critical feedback to the role players.

In summary, role playing is a highly interactive, participant-centred activity that, combined with the case-study method, can yield the benefits of both. When case situations, critical incidents, and role descriptions closely represent real-life conditions, role playing can have a significant impact on the participants’ ability to learn new behaviour.

SIMULATIONS

Simulations are like role plays, but bigger. They are often simplified models of a process that is to be learned. Through simulation, workshop participants can experience what it is like to take part in the process and can experience their own behaviours relative to it in a safe environment. They help the participants learn while avoiding many of the risks associated with real-life experimentation.

Simulations are sometimes used to involve participants in organising physical objects to study how they make decisions. One example is to create small teams that are asked to compete against each other on the construction of a tower within designated time and resource constraints. The intent is to examine questions of planning, organisation, and the assumption of leadership within newly-formed teams. Another example of simulation is something called an in-basket exercise. Individual participants are asked to make quick decisions as a newly-appointed manager on how to delegate or otherwise dispose of a stack of correspondence left behind by a previous manager. The intent of this kind of simulation is to investigate how an individual sets priorities, delegates authority, and generally manages time.

As with role plays and case studies, simulations garner their learning value from the authenticity of the situations and the degree of realism provided by participants taking part. What has been said earlier in the guide about setting up the situation and being sure everyone knows what he or she is supposed to be doing applies equally to your trainer role in producing successful simulations.

In summary, simulations are workshop representations of situations participants are likely to be confronted with in their real-life roles. They allow participants to practice new ways of doing things and learn more about their own behaviour in role-relevant situations with a minimum of personal or professional risk.

INSTRUMENTS

An instrument is any device that contains questions or statements relative to an area of interest to which participants respond. Instruments are versatile. They can include questionnaires, checklists, inventories, and other non-clinical measuring devices. Normally, instruments focus on a particular subject about which workshop participants have an interest in learning. They produce a set of data for participants to study, either individually or in small groups or both. Often these instruments are designed to help participants discover more about their own beliefs, values, and behaviours and provide data on the norms of a larger population. Most participants, when confronted with their own data, are inclined to alter aspects of their future behaviour so they can be more effective.

There is a major distinction between just having participants complete an instrument and using it properly. The value of these learning aids is increased measurably when you apply the following steps.

STEP 1: ADMINISTRATION

Distribute the instrument, read the instructions to participants, ask for questions of clarification only, and instruct them to complete the instrument. Monitor the time carefully and encourage participants to help others if they are having problems in completing it. Expect some individuals to take longer than others.

STEP 2: THEORY INPUT

When participants have completed the instrument, discuss the theory underling the instrument and what it measures.

STEP 3: SCORING

Based on the way the instrument is designed, ask participants to score their responses. Sometimes instruments have a built-in scoring mechanism. At other times, it may be necessary to read out the answers and to give other instructions, e.g., how to combine scores. Since some scoring instructions can be difficult, we suggest you take the instrument yourself and become familiar with all aspects of it before trying it out on others. This is even more important if you devised the instrument yourself.

STEP 4: INTERPRETATION

It is generally effective to have participants post their scores on chart paper for others to see. Small groups are often formed to discuss their scores. Special attention should be given to the meaning of low and high scores and discrepancies between

actual and estimated scores, if estimating is done. Participants may be asked if they were surprised by their scores or other participant's scores.

In summary, instruments are used to derive information directly from the experience of workshop participants themselves. Owing to the personal nature of the feedback, instruments can be an effective method for helping participants learn more about specific behaviours and the impact these behaviours have on others. While we have included a number of instruments in the series, we encourage you to develop your own based on the needs of your participants and your own interests in expanding your training design knowledge and skills.

LEARNING APPLICATION

Speaking of *Learning applications* don't forget that each of the chapters includes a number of these efforts to encourage the reader to stop and reflect on what they have just read. These interludes in the Part One text of each chapter have the potential to be very effective training design and learning tools. Don't overlook their potential as you design workshops and learning experiences for your clients. Now, back to this specific opportunity to apply what you have just learned about the design of training programmes and experiences.

In an effort to better understand the many ideas that we have presented on developing effective training programmes for your constituents, we suggest you jot down five to ten of the most important lessons you have learned from this Guide that will help you become better prepared to offer this LGFM series.

Now, take the best of these ideas and describe how you plan to put it into operation in planning and designing your next financial management workshop.

IN CONCLUSION

The secret of being a competent and successful training manager or trainer is not measured by how many guides like this you may have read. It's measured by what others do with what they have learned from you and the learning experiences you have made available to them.

For example, about twelve years ago one of the authors conducted a three-week programme on the topic of managing change in Hungary. There were twenty-seven participants in that workshop but only one responded immediately to the potential of trying to manage changes back home. It was the early 1990s and Ana Vasilache was from Romania, a country that was undergoing significant political, social and economic changes. With new ideas on how to change things and a whole lot of tenacity and courage, Ana began to develop a regional training and capacity building programme to serve local governments and non-governmental organisations in her country and others in the region.

In the twelve years since that workshop on Managing Change, she and her Romanian colleagues established an organisation that has trained over 10,000 participants from 35 countries on four continents. Moreover, their training has included twenty-one national training of trainer (TOT) programmes involving 230 trainers. By the most conservative multiplier the number of officials consequently trained by the graduates of these TOT programmes far exceeded 100,000 at the time this was being written. She attributes the genesis of her success in large part to what she learned in that initial workshop, i.e. concepts, strategies and skills in experiential learning and change management.

As the author recalls the initial workshop that sparked this flurry of training opportunities in Romania and beyond, he admits that he has no verifiable data on the success of the other twenty-six graduates. If we assume that twenty-six of the twenty-seven participants in that change management workshop did very little to apply what they had learned, can we make the outrageous assumption that the workshop was successful? Or, was it a dismal failure? You decide.

We believe there is a lesson or two or more in this short parable. First, never underestimate the influence you can have as a trainer using chapters like the one you are reading. Second, don't expect every training programme you conduct to be 100% successful. You can't control nor dictate the impact that others will have from what they have learned in workshops that you conduct. Training of Trainer (TOT) workshops are notorious for the dropout rate among those who attend. Very few participants in a Training of Trainers programme will become accomplished and dedicated trainers. Not to worry. It only takes one trainer in a TOT who is dedicated to cloning herself to keep the propagation going.

Finally, be encouraged by the success that Ana and her colleagues have experienced and don't be discouraged by short term workshop results. Most external evaluators would consider a programme like the one in Hungary a dismal failure. After all, the percentage of participants who went forth and actually "managed change"

in their organisations and communities appeared to be miniscule. It probably was a dismal failure and waste of funds from conventional measures of success. Unless, you consider the consequences of the one participant who went home and turned her learning into a phenomenal success story that has spanned four continents. Social, political and economic revolutions often start not from the masses but from a few individuals who recognize the power of an idea whose time has come.

In closing this guide we want to go from *inspiration* to *perspiration*. In other words, we want to put you to work. The following worksheet is to help you and your colleagues begin to plan the application of these learning materials in your own country, region or community. Good luck and think outside the box. Ana Vasilache did and was one of seven persons world-wide honoured in 2000 by UN-HABITAT for their contributions to good governance.

Never doubt that a small group of thoughtful, committed citizens can change the world. Indeed, it's the only thing that ever has.

Anthropologist Margaret Mead

PLANNING FOR SUCCESS

The following questions are designed to help you think through how you will put this series of Local Government Financial Management (LGFM) opportunities into action. We suggest that this is a task best accomplished by a few dedicated stakeholders involving not only those who will take the primary responsibility for providing the training but also those who will benefit from the training. Thus the first set of queries to consider. By the way, these questions may not follow your own sense of what the planning logic should be. Given this, don't hesitate to alter the sequence, add your own, or drop some of the tasks we are suggesting. Also to conserve space we have not left enough room after some of the questions to provide adequate answers. Given this, we suggest you plan to use a flip chart to record your answers, preferably working through the questions with one or two other colleagues who will make up the core of your planning team.

THE PLANNING TEAM

1. About how many persons will be on your planning team? ____
2. What expertise and points of view will they represent? For example: potential trainers? If so, who? _____; Finance officers? _____; Representatives of other potential client groups? _____; Potential sponsors of training: _____; Potential funding sources? _____; Language specialists, if necessary? _____; Others? _____.

THE POTENTIAL CLIENTELE OF THE TRAINING:

In each of the following client possibilities, not only think about whether you want to target them, but try to estimate the potential numbers of training participants in each of the categories mentioned. Just check those you want to target and provide a guess-timate of the numbers. This part of the planning will provide a sense of the potential there might be for the training given out-of-the-box thinking and marketing.

1. Senior local government finance officers? ____; #s? ____
2. Staff members of finance departments? ____; #s? ____
3. Operating department heads, i.e. public works, fire protection, library? ____ #s? ____
4. Local elected officials? ____ #s? ____ Members of specific committees of the governing body, i.e. finance or oversight committees? ____ #s? ____
5. State government officials with local government oversight responsibilities? ____ #s? ____
6. Pre-public service students who want to work with local governments? ____ #s? ____
7. Citizens, i.e. those who might serve on citizen boards or committees to help plan and manage the budget? ____ #s ____
8. Others? ____ #s ____.
9. Speaking of potential clients, do you plan to conduct any training need assessments? If so, with whom? ____; And how? ____
10. Now, go back to each of the potential client groups and think about what chapters would be most appropriate for each category of training participant. For example, senior finance officers should ultimately be trained in all the chapters. Elected officials might need to concentrate on topics like operating budgets and their financing, evaluating financial conditions, and a few others with an overview on all of the chapters.

MATERIALS AND TRAINER PREPARATION

1. Will the series have to be translated into a local language? ____ If so, how will you undertake this task? ____
2. Who will pay for the translation? ____ And, the printing in the local language? ____
3. How will you monitor the integrity and accuracy of the translation? ____
4. If translation is not necessary, do you see the need to adapt the materials for local use? ____ If so, what does this mean? ____ How do you plan to carry out these adaptations? ____
5. Who do you plan to work with to accomplish these adaptations? ____ How will you compensate those who do the adaptations? ____
6. What other questions do you need answers to regarding the preparation of the materials for local or national use? ____
7. Who do you plan to use to conduct the LGFM training? ____

8. How will you prepare them as trainers who both understand the content of the materials and the experiential learning process? ____
9. Will you conduct a training of trainers (TOT) to develop a small cadre of trainers who can undertake the initial series of training events? ____ If so, how do you plan to organise and staff such a programme? ____
10. How will you recruit the participants for the TOT? ____ What will be your criteria for selection of these participants? ____
11. How will you finance the cost of the TOT? ____

PARTNERSHIPS, FUNDING, AND OTHER NECESSITIES

1. Do you plan to partner with other organisations or individuals to plan and conduct the training? ____ If so, who are they, and what will they contribute to the endeavour? ____
2. How do you plan to fund the training of LGFM participants? ____ How will you organise these potential funding possibilities? ____ What are the possibilities of sustaining each of these funding options? ____ What is your strategy for sustaining the LGFM training over time? ____
3. How do you plan to market the training? ____
4. What kinds of evaluations do you plan to use to assess the quality of the training experiences associated with LGFM training? ____ How do you plan to assess the impact of the training within the participant's work setting? ____
5. What is the first thing you plan to do to put this plan into action? ____

There are no doubt many more questions to be asked and answered before you begin to spend time and money on launching a new programme of local government financial management training. We hope this volley of queries has helped to begin the dialogue toward action. We encourage you to add to this list of questions as you go down the road toward training implementation. The more you can define the *what*, *who*, *why*, *where*, *when*, and *how* dimensions of this new venture before you even

Financial Policy Making

PART ONE: CONCEPTS, PRINCIPLES, AND STRATEGIES

SUMMARY

This essay examines ways that formal, written financial policies are developed and implemented at the local government level. We will provide a definition of financial policy and describe the benefits to a local government that establishes and uses sound financial policies. We will delineate the basic steps to take in identifying, proposing, adopting, and implementing financial policies. We will also discuss various obstacles to the financial policy making process.

RELATIONSHIPS BETWEEN CHAPTERS OF THE SERIES

The following matrix shows the interrelationships between *Financial Policy Making* and other chapters in the series.

	Financial Policy Making
<i>Introduction</i>	The Introduction provides the framework for using the entire series.
<i>Trainer's Guide</i>	Provides guidelines for using the chapters to provide training.
<i>Financial Planning</i>	Financial planning policies help the LG determine future use of LG resources.
<i>Citizen Participation</i>	Citizen participation policies define when, where, why and how citizens should participate in LG financial decision making.
<i>Evaluating Financial Condition</i>	Financial condition policies help a LG determine when financial problems are beginning. They are like an early warning system.
<i>Operating Budget</i>	Operating budget policies determine how the LG will use current year resources.
<i>Financing the Operating Budget</i>	Financing policies help the LG evaluate the ability of taxes, fees and charges for services and any other sources of revenues to fund the delivery of current year services.

<i>Capital investment Plan</i>	Capital investment plan policies determine how the LG will provide capital investments for the community.
<i>Financing the Capital Investment Plan</i>	Financing policies help the LG evaluate the use of current year and long-term financing for providing capital investments.
<i>Accounting</i>	Accounting policies are the foundation for the LG's accounting and reporting systems, which underpin the entire finance and budgeting systems.
<i>Performance Measures</i>	Performance measurement policies define how and when LG officials and policy makers are held accountable for use of LG resources.
<i>Asset Management</i>	Asset management policies help the LG determine the best use of its assets.
<i>Procurement</i>	Procurement policies determine how LG resources will be spent.

INTRODUCTION

We recognize that basic or introductory concepts are relative—depending upon your background and frame of reference for both finance and local government. Users of this material will range from those who have no knowledge of financial principles or concepts to those who have a very sophisticated understanding. The following are our ideas of what represents the most fundamental principles and concepts needed to understand financial policy making at a beginning level.

BASIC CONCEPTS AND DEFINITIONS

In a UNCHS (Habitat) training publication for local elected leadership, “*policy*” is described as a word with many meanings.

It can be (a) a philosophical or ideological stance; (b) a plan, an expression of future direction, (c) a definition of current action, (d) specific proposals, (e) a way of announcing decisions of government, (f) formal authorization, (g) a negotiated position between two or more parties, (h) a statement of intent, or (i) an unintended, unannounced reality that was never decided formally by anyone including those who are considered to have the “policy making” role.

Financial policies describe the principles and goals that guide the financial management practices of a local government. Financial policies influence financial decision making. They lead to the development of strategies to achieve missions and visions of the organisation. In addition, they provide standards for evaluating and monitoring the performance of a local government’s financial management system.

Note: The following definitions and concepts are primarily for decentralized local governments. Local governments functioning within a highly centralized local government system do not normally have the flexibility of determining their individual policies as described in the following material.

POLICY FRAMEWORK

A **policy framework** is a system or structure of policies, which provide guidelines for decision making. The policy framework, therefore, represents a comprehensive financial strategy for achieving and maintaining sound financial oversight for both direct services provided by the local government as well as oversight for any quasi-governmental or non public sector agencies for whom the local government is also responsible. Policy framework elements usually include:

Policies mandated by the central or national government

- A restatement of any policies mandated by the central government;

Direct services provided by the local government

- The general level and type of services to be provided to citizens;
- The relative emphasis to be placed on the differing sources of revenue available;
- How much the local government will vary its levels of expenditures and taxation if the local economy changes;
- Statement of principle regarding the management of new funds including any services/activities to be performed by contract rather than by local government staff;
- The degree to which capital investments should be financed from **current revenues** (pay-as-you-go principle of paying for goods and services when they are purchased rather than using credit such as loans or bonds) versus issuing **debt obligations** (pay-as-you-use principle of paying for goods and services over time by using credit; this method matches the benefit of the use of the asset, such as a building, with the repayment of the debt) to be paid from future revenues;
- The system of employee wages, pensions, and benefits;
- If debt obligations are to be issued, the terms of overall life, pattern of maturities and types of debt to be used;

Oversight for quasi-governmental or non public sector agencies

- Unambiguous agreements defining the relationships between the local government and any quasi-governmental agencies or public enterprises, i.e. water agencies, local government banks; and

- Guidelines defining local government's involvement with the private sector including conduct of business in an open and public manner based on clear rules and procedures applied in a non-discriminatory way.

FINANCIAL POLICIES

Financial policies are statements created by elected officials to clarify their financial management philosophy. Broadly defined, financial policies are formal positions taken by the local governing body to support the implementation of its financial goals. Policies provide a framework for financial management and guidance for chief executive officers, such as mayors or local government managers, finance managers, and the local governing body in conducting the financial affairs of a local government.

NATIONAL AND LOCAL LAWS ON POLICY MAKING

Each local government must work within the framework of national, state or province laws and policies when they begin establishing their own local government financial policies. It is important that the four groups with which this series is primarily concerned (elected officials, chief executive officers (CEOs), finance managers and department heads) be aware of any central government policies that may impact their ability to formulate or implement new local government financial policies.

Every country has its own approach to policy making. For those countries in newly evolving democracies, policies have historically been made from the top down, e.g., central to local government levels. If you are a local government official in this situation, you may have the opportunity to set policies at the local government level for the first time. Policies set by local governments may be different than those previously set by the central government. As decentralization evolves, local elected officials may find that there are good reasons for doing things differently, and chose to implement new policies.

WHO MAKES POLICY?

Policies are important because they put your government "on record" regarding the most important financial issues facing the community. There is often the impression that policies result from a very deliberate process of decision making on the part of the local governing body following thorough analysis of all the conditions surrounding an issue under consideration and the various alternatives available. In reality, the policy process is very messy. Sometimes it really does happen as suggested. Other times it evolves out of negotiations with several parties, for example, as conditions for a donor-assisted loan agreement for a new water treatment plant.

Policies are made or reaffirmed at budget time when governing bodies allocate resources for the new fiscal year. Or policies may evolve unintentionally. For example, the governing body makes unintentional policy when, while operating with a very tight budget, it ignores preventative and routine maintenance of equipment and other fixed resources. After a couple of years of ignoring the maintenance responsibility, the staff just stops including it in future budget requests. Thus, the governing body unintentionally has adopted a non-maintenance policy.

Sometimes policies are formulated by employees or workers who, by their actions or inactions, define local government policy on a particular programme or service. A local government governing body may enact a “policy” defining a specific level of service to be provided in the community, but it never is implemented for one reason or another. Who, in this case, has really made the policy? As you can see, the policy making process can be a bit complicated and not always under the control of the governing body which is assumed to have the “policy making” role.

It is important that policy making be based on good governance principles. The policy making process must include transparency in the formulation, formal discussions and legal notices, and decision making process, be responsive to issues and concerns of the citizens, be consensus oriented where possible, promote equity and inclusiveness and allow elected officials to be held accountable for that impacts of the implementation of their policies. The areas of financial policy making have considerable impact on citizens, i.e. raising taxes, increasing user fees, choices about the use of surplus cash for investment, etc. All impact the citizens’ wallet.

WHAT POLICIES LOOK LIKE

Financial policies should be coherent statements of intent that are consistent with one another and easily understood. However, this is not always the case. Unfortunately, policies are not always in writing. They are sometimes incomplete, conflicting, and inconsistent. At times they are even competing! A local government’s policy on fund reserves, for example, may change from year to year. It may be written in vague language which is interpreted differently by elected officials or managers. Or it may be used inconsistently, not being applied the same way with all types of reserves.

Inconsistent policies are particularly troublesome. One policy, for example, might deny the use of “one time” revenues, such as grant proceeds, for operating purposes. Another policy might direct the use of proceeds from the sale of local government property or other assets, which can also be considered as “one time” revenues, to be used to balance the operating budget. To make matters worse, there might be a policy calling for a balanced budget in the absence of other policies to limit the size of budget amendments and emergency appropriations.

Conflicting policies are most likely to occur when they are adopted on an *ad hoc* or emergency basis. For example, a local government might have a long-established policy that emphasizes the importance of safety and liquidity in cash investments. Then, during a period of revenue shortage, the governing body might decide at the “last minute” to adopt a policy of investing surplus cash in risky ventures to increase revenue yields. The result is an obvious conflict of governmental intent and a source of confusion and concern for local government staff.

Following are some sample policies to use as a frame of reference as you continue reading through the essay.

Sample Policies

Note: A local government should not adopt the following policies verbatim. However, they do represent examples of suggested language for sound financial management practices.

1. The local government will maintain a year-to-year fund carryover balance of at least 5% of general operating revenues in order to maintain adequate cash flow and to reduce the demand for short-term borrowing.
2. No more than 30% of the local government's cash management investment portfolio will be in long-term securities for a period of longer than three years.
3. The local government will prepare a five-year capital investment programme and annual capital budget.
4. Proposals for local government ownership of businesses must contain a detailed market and financial analysis, a business plan, and an evaluation of alternative ways of conducting the business.
5. Full disclosure of the local government's financial condition will be provided in financial statements.
6. Proceeds from the sale of assets will be used only for capital investment purposes.
7. A mid-year budget review will be held.
8. All fixed assets will be valued and inventoried annually.

CONSIDERATIONS FOR LOCAL GOVERNMENTS IN EMERGING DEMOCRACIES

The establishment of authentic local self-governance in many of the transitional countries significantly alters the roles and responsibilities of local elected officials and their professional staff. This is particularly true when it comes to establishing local financial policies. Local governments begin to think for themselves about what policies make sense for them. In many of these changing situations, local governments may decide to start out using the same policies of the central government and change them incrementally as needed. When they decide to make these changes, there is often no need to seek approval from the central government although these habits are difficult to change in new democracies.

We have noticed a consistent pattern in countries where responsibilities are devolving from the central government to local governments. The first year or two local governments seem afraid to take chances or risks with their new-found freedoms and responsibilities. They are afraid that the central government may take punitive actions against their government or that they will make a major mistake. After exercising the freedom and responsibility for local governance, local officials get more confident in their ability to make decisions and begin to slowly implement changes in central government policies that may still be in place despite the changes in the governing process. What you do will depend in large measure on where your local government may be in this process.

LEARNING APPLICATION

ELECTED OFFICIAL _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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In the first Learning Application in each of the chapters in this series we will be reminding the reader about how to get the most from each of these reflective exercises. First, there will be a box identifying the four key local government roles that most readers represent. These are: Elected Officials, CEOs (Chief Executive Officers such as mayors, local government managers, etc.), Finance Managers (the chief finance official in the local government), and Department Heads (those individuals who are responsible for the management of specific local government departments such as public works, planning, and human resources). Second, we will indicate in the box those readers we believe will benefit most from completing the learning application task. Finally, when more than one official is listed, we see this as an opportunity for these individuals to get together and compare their responses. These Learning Application opportunities can also be modified to become training exercises for group learning. So, our advice is to make the most of these reflective interludes in the text.

Even though we have identified the elected officials through this series as the policy makers, it is important to recognise that many other local officials and even local government employees contribute to this important process. Before moving on, we suggest you take time to think about your own interpretation of what a policy is and who makes them from your unique perspective as an elected official, CEO, finance manager or department head.

From my perspective, financial policies are:

From my perspective, policy making in our local government is the responsibility of:

From my perspective, the financial policies of our local government are (check one): not at all effective:___ somewhat effective:___ very effective:___.

The reason for my assessment is:

In many countries, the central government has significant policy making powers that affect local government financial management. From your perspective, reflect on the short term and long range impact of the central government on your local government's ability to manage its finances effectively.

The short term impact of central government policies on our local government finances is:

And, the long term impact of these policies is:

From my perspective, here are some things our local government might do to minimise the adverse consequences of these central government policies.

THE ILL-EFFECTS OF NOT HAVING FINANCIAL POLICIES

The absence of formal written policies can create serious problems for a local government. Without them, local officials are uncertain about the organisation’s position on various financial management issues. This is further aggravated when there are changes in elected officials or key staff members. Under these circumstances, lack of an organisational “memory” about financial policies can be the source of considerable confusion and potentially bitter conflicts over financial philosophy.

The vacuum created by the absence of leadership in creating financial policy has serious consequences. Bad financial management practices may occur because there are no policies prohibiting them. For example, borrowing from **restricted funds** may take place with no specific plan for repaying the loan with interest. The presence of a vacuum in policy making may encourage appointed officials to make policy, a serious distortion in the relationship between policy making and administration.

Informal, unwritten, incomplete, conflicting, and inconsistent financial policies are harmful to the public image of the local government. They give the impression that local officials do not know what they are doing or do not place a high priority on thoughtful and prudent financial management. Investors and users of financial information must have a clear picture of the basis on which financial decisions are made by the local government. Otherwise, they may be confused and lose confidence in the ability of the local government to manage its financial affairs effectively.

Problems Resulting From No Formal Written Financial Policies

- Uncertainty regarding the financial direction of the local government
- Policy making by administrative officials
- Lack of continuity when elected officials and staff change
- Lack of confidence on the part of investors and users of financial information
- Adoption of improper financial practices
- Low public image

LEARNING APPLICATION

ELECTED OFFICIAL _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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It's time to give you an opportunity to look at how the policy making process works in your local government. Start with listing 3-4 financial management policies of your local government that directly affect your role—either as a elected official, CEO, finance manager or department head. Don't hesitate to list informal, unofficial types of policies if they apply to this task.

- 1. _____
- 2. _____
- 3. _____
- 4. _____

What is the impact of each of these policies on your ability to carry out your role and responsibilities?

What might be done to make these policies better support you in your role?

IMPACT OF DECENTRALIZATION ON LOCAL GOVERNMENT

One of the most difficult issues for local governments in a country that is decentralizing is the conflicting policies that may come from different central government agencies. Each central agency expects their regulations to be followed by local governments. It is difficult to know which to follow and at times following all of them creates great difficulty for local governments. For example, in Indonesia, the Ministry

of Home Affairs appears to have responsibilities for certain areas of fiscal decentralization and the Ministry of Finance also appears to be responsible for certain fiscal areas. Each ministry has issued a set of account codes to be used by the local governments in various aspects of financial budgeting and reporting. The two sets contradict one another. Local governments are confused about whose policies to go by. In the past, Ministry of Home Affairs policies have been followed. But now it appears that the Ministry of Finance is taking the lead in many budgeting and financial areas. It is hard to know how to manage this in times of conflict. Sometimes local officials have to do a little bit for both agencies or try to follow whichever ministry they think is going to win out in the long run and implement their policies.

AREAS COVERED BY FINANCIAL POLICIES

Written financial policies should cover all major financial activities carried out by your local government. Doing this will ensure the development of a comprehensive policy framework which recognizes the relationship of financial intent and actual practice. A complete inventory of your local government's financial activities will help identify gaps where formal policies are needed. The following financial activities are areas where the preparation and adoption of formal, written policies will bring uniformity to your financial transactions and reduce uncertainty:

- Accounting
- Asset management
- Auditing
- Capital investment plan and budget
- Cash management
- Debt
- Development finance including grants, subsidies, loans, and tax policies
- Financial reporting
- Inventory management
- Operating budgets
- Pensions and retirement systems
- Purchasing
- Reserves
- Revenue
- Risk management
- Virements (funds over or under spent and there is a need to make transfers)

Carefully review the list and identify financial activities your local government may be performing which are not included. Also, think about the interrelationship among the activities and the possible policy implications.

Cases in point

- In developing revenue policies, a local government fails to consider the implications of adopting a ***pay-as-you-go*** (practice of paying for good or

services when they are purchased or built rather than relying on credit such as loans or bonds) financing policy for capital investments.

- A local government has written policies relating to the operating budget and the capital investment plan. However, it does not have a policy requiring a linkage of the two. There is no provision in the capital investment process for identifying the on-going operating costs associated with capital investment projects when completed.
- A local government adopts written financial policies covering the budget, capital investments, and its pension system. The policies do not address the effects of deferring maintenance costs or pension contributions and the practice of transferring money from the pension fund to balance the operating budget.

CITIZEN PARTICIPATION IN POLICY MAKING

WHY CITIZEN PARTICIPATION IS IMPORTANT

One of the basic premises of democracy is that people should have input into the policies and decisions that control their lives. When denied this input, people eventually rebel against those setting the policies.

In democracies, we have recognized that every citizen cannot participate in every decision made by the government. We have a system of electing persons to represent us and provide this input into the decisions that control our lives. We vote for officials who represent our views. When we are unhappy with their policies we voice our concerns and sometimes vote them out of office. There is an underlying assumption in democratic societies that public input on policies affecting their daily lives is important. However, the degree to which that public input affects public decision making differs from country to country.

BENEFITS TO LOCAL GOVERNMENT DECISION-MAKERS IN EVOLVING DEMOCRACIES

As an elected official, you have been elected to represent a particular group of citizens, i.e. a specific geographical area or political party. In some democracies, elected officials are expected to represent and reflect the views of the constituency that elected them. In other types of democracies, the elected official may be more free to make decisions that do not necessarily reflect the views of the constituency.

The benefit of satisfactorily representing your constituency is that you will more likely be re-elected. Conversely, if you don't represent the views that your constituency thinks are important, they may want you to change your views or replace you.

In some evolving democracies, the concept of holding an elected official accountable for their policy stands and decision making is just beginning. Some of the early signs of how citizens feel about their new government may be street demonstrations, negative media coverage, or non-governmental or other citizen groups calling for greater accountability and in more dire situations the resignation of their representa-

tives. These types of actions result when citizens feel they want to have input into the policies and programmes that impact their daily lives. Of course, as an elected official you may feel pressure if you are not willing to consider the views of your vocal constituents. For every one vocal person, there are probably ten other people who feel the same way, but just haven't communicated it to you. It is important to find ways of accommodating vocal constituents. This does not mean always following what they demand, but it helps to listen and factor their views into your decision making process, and your policies as an elected body.

LEARNING APPLICATION

ELECTED OFFICIAL _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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It's time to reflect on how well your local government is doing in involving citizens in the financial management initiatives of your local government. Describe the roles and responsibilities that are afforded citizens in the overall management of your local government's financing efforts. On this one you may need to think outside the box. For example, does your government ever establish study commissions to look into issues within your community that might have financial consequences? If your local government has a land use planning process where citizens have input to how vacant land can be used in their neighbourhoods, for example, their input may very well have financial consequences in future budgets. In other words, think broadly about the role of citizens in policy making initiatives, either direct or indirect, that have either direct or indirect financial consequences, both good and bad, on financial management.

Given this broad mandate to reflect, here are some ways that citizens have been involved in either directing or influencing financial policies in my local government and community.

Take each of these examples and list what you think were, or are, the consequences of these policy related inputs by your citizens.

What more should your local government be doing to involve citizens in financial management related activities?

BENEFITS

A carefully formulated financial policy framework with built in flexibility to meet changing needs and conditions is one of the most valuable financial tools available to local officials. Here are some of the benefits of written policies:

FACILITATE FINANCIAL PLANNING

One benefit of establishing financial policies is to encourage policy makers to view financial management in a long-range context. The development of a policy framework involves an examination of the short- and long-range implications of policies. It also involves identifying the relationship among policies. Finally, it involves an analysis of existing and future financial conditions along with the need for new policies or changes in current policies.

An analysis of financial information and condition in advance of the development of policies stimulates a planning approach. The analysis will help to identify gaps, conflicts, and inconsistencies in existing policies. The analysis should include consideration of future fiscal problems and needs along with alternative ways to handle them. It is common for new financial issues that require attention to emerge from this process. For example, a local government may see the need to impose restrictions on risky investments and to require detailed cash investment reporting. Declining revenues, on the other hand, might cause the local government to establish policies calling for the conduct of annual fee surveys and restructuring fees to recover full service costs.

Financial policy formulation assists local officials in adopting a long-term perspective when making short-term policy decisions. A policy requiring multi-year

revenue and expenditure forecasts, for example, should prompt an analysis of long-range financial capacity and an assessment of internal and external financial risks.

AVOID FINANCIAL EMERGENCIES

Financial policies provide a basis for predicting and coping with financial emergencies. Revenue shortfalls, reduced national allocations, lowered credit ratings, grant terminations, statutory revenue or expenditure limitations, and unexpected mandated expenditures can have a severe financial impact unless policies and plans are in place to anticipate and handle them.

Policies on revenue, capital budgeting, debt and reserves are critical to maintain financial solvency. Reserve policies, for example, provide for the temporary financing of unforeseen needs. Debt policies that set the level of short- and long-term debt, type and purpose of debt and reserves for the repayment of debt help to avoid a fiscal crisis. Revenue policies, which provide for diversified revenue base, aggressive collection, limited reliance on restricted revenues, and sound tax administration can help to avoid financial emergencies.

In other words, financial policies help local governments prevent abnormal or unexpected conditions from disturbing the orderly state of financial affairs. The policy formulation process should involve a thorough evaluation of potential financial problems and the design of strategies to prevent, minimize or control them.

FOCUS ON EVALUATING FINANCIAL CONDITION

The preparation of a policy framework focuses attention on the overall financial condition of your local government. Policy formulation fosters a comprehensive rather than piecemeal approach to the analysis of a local government's financial condition. You cannot formulate policies effectively without identifying and analyzing existing and potential conditions and trends.

In order to evaluate financial condition, information must be collected on internal financial policies and practices and external social, economic, political and demographic factors. Analyzing this data will identify practices and trends that can be warning signs of future financial stress. Policies and practices can then be designed to guide corrective action. Analyzing information on financial condition is also useful in making necessary policy modifications and this process is covered in another chapter in this series.

MONITOR FINANCIAL MANAGEMENT PERFORMANCE

Once developed, a policy framework can be used to monitor financial management performance. Policies requiring an annual audit, internal controls, and financial reports designed to meet the needs of different users can be used to monitor the performance of financial managers and hold them accountable for planned fiscal results.

AVOID FINANCIAL “GIMMICKS”

Sound financial policies promote an awareness of the dangers of financial gimmickry and impose controls on its use. **Gimmickry** occurs when a local government changes the basis of accounting, misrepresents revenues, manipulates restricted funds, shifts current expenditures to the next fiscal year, uses inter-fund transfers to cover revenue shortages, and damages the credibility and integrity of local officials by adopting poorly conceived budget amendments. A policy framework offers a basis for understanding the danger of such practices and provides the rationale for rejecting unsound solutions to financial problems which might otherwise be too compelling to resist.

IMPROVE DECISION MAKING

Financial policies help to build consensus and consistency in financial decision making. Once adopted, financial policies help to clarify the goals and objectives of overall financial planning. One practical result of this is to reduce exhaustive debate and discussion each time a decision is to be made on financial issues covered by an established policy. Established policies also provide continuity in the management of financial affairs, particularly when there is a turnover of elected officials or staff.

A policy framework reduces conflict and misunderstanding by providing direction to the staff about financial matters and reducing uncertainty or confusion. Financial policy development creates a collaborative climate for decision making. Policies reduce the need for crisis-oriented decisions and establish reliable guidelines for the conduct of on-going finance operations.

PROMOTE FINANCIAL STABILITY

Anticipation of financial problems and the development of policies to avoid or manage them are essential to achieving financial stability. Policies that require multi-year revenue and expenditure forecasting, capital investment planning, cost recovery and annual fee adjustments for inflation help minimize major year-to-year fluctuations in tax rates and fees. They send a clear signal to the public and users of financial information that the local government places a high priority on financial stability.

Continued adherence to sound financial policies ensures continued financial stability when local government is threatened by fluctuations in the economy, declining local business activity or a decline in budget allocations from the national government.

IMPROVE CREDITWORTHINESS

With adherence to written financial policies, you raise the quality of your local government's credit rating. Investors, banks, and credit-rating agencies view well-defined debt, accounting, auditing and financial reporting policies favourably. A financial policy requiring full disclosure of your local government's financial condition can lead to improved credit ratings, expanded borrowing opportunities and lower interest rates. By adopting a written policy framework, you demonstrate a level of

financial competence and professionalism important to institutions that are in the money lending business.

EDUCATE LOCAL OFFICIALS AND THE PUBLIC

The financial policy formulation process serves as an effective means of educating elected officials and the public about local financial management while building public confidence and support for local government. Written policies are a signal to the public that thoughtful consideration and deliberation go into managing the local government's financial affairs. There are few better ways to improve the credibility and preserve the fiscal integrity of a local government and its officials. For example, a policy endorsing a strong system of internal controls demonstrates to the public local government's commitment to detect and deter waste, fraud, and abuse in local government operations.

Written financial policies are an excellent training tool for newly elected officials. The on-going process of policy development provides an opportunity to educate elected officials on finance concepts, terminology, practices, and standards. This is especially important as local government finance increases in complexity.

LEARNING APPLICATION

ELECTED OFFICIAL _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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We've been talking about the various benefits of financial policies. Another way to look at policy benefits is through the lens of the good governance policies we discussed in the **Introduction** chapter. For example, does your local government have written policies about openness and transparency, accountability, participation in the process, equity and inclusiveness, subsidiarity, and effectiveness and efficiency in the way your local government operates?

Select two or three of these principles and write down one or more policies your local government has in effect that assures citizens that this principle is being fulfilled. Then give your assessment of how effective each of these policies is in achieving the principle.

Principle 1: _____

Policies that relate to this principle are:

1. _____

2. _____

3. _____

Principle 2: _____

Policies that relate to this principle are:

1. _____

2. _____

3. _____

Principle 3: _____

Policies that relate to this principle are:

1. _____

2. _____

3. _____

Now, return to each policy you listed and assess how well you think it performs in achieving the intent of the principle. Assign a percentage to its success. 100% of course would be totally successful and 0% a total failure. In between you have an abundance of choices; 99 to be exact.

OBSTACLES, LIMITATIONS, RISKS AND OTHER CONSIDERATIONS

You will find that developing a financial policy framework is not an easy task. There are many obstacles such as political and staff resistance, the amount of time required, inadequacy of financial information, lack of knowledge about finance concepts and practices, and too few quality standards and benchmarks.

POLITICAL AND STAFF RESISTANCE

Expect political and staff resistance as you begin to develop a formal written policy framework. Some elected officials will tell you that such a process is irrelevant to the way decisions are made and that the policies, if adopted, would not be used. They will claim there are few choices about taxes and spending and that it is impossible to predict the future. There may also be a fear that the media and the public will misunderstand policies. Elected officials may be concerned that political opponents will use the high visibility of written policies against them. Finally, elected officials may find it difficult to see beyond the next election.

Staff members may resist the process as an infringement on their authority and claim they are more qualified to make financial policies than elected officials. It is common for the staff to say that local government finance is a complicated subject best left to the experts. On the other hand, staff may resist by saying they are too

busy with other duties to develop the process. Finally, staff may fear the increased accountability that accompanies the adoption of formal written policies.

TIME REQUIRED

Developing a comprehensive policy framework is a time consuming process. Existing policies may not cover all financial activities. It is not unusual to find policies that have not been committed to writing, that contain inconsistencies, that are incomplete or out of date, that must be pieced together from several sources, which have provisions that conflict with other policies, or that have never been formally adopted.

Many policies come about as the by-product of an accumulation of financial decisions rather than through a deliberate process. They can have a powerful influence over the way a local government's financial affairs are managed despite the fact they do not appear anywhere in written form. Even more confusing is the existence of financial policies that are founded on tradition and usage or that come about as a reflection of government default, delay, or inaction. For example, a local government governing body may have discussed the desirability of establishing adequate reserves but has consistently failed to set specific amounts or percentages. Alternatively, the governing body may have agreed that funding a capital investment plan is a top priority but then allows surplus funds to be used for projects not in the capital investment plan.

The formulation of a consistent policy framework when such practices as these have persisted can be extremely time consuming and an obstacle to progress. The development of a policy framework requires adequate time for the elected officials to establish financial goals and adopt written official positions required to put the goals into effect. Staff and other input will be needed to properly generate and evaluate policy options.

INADEQUATE FINANCIAL INFORMATION

Another barrier to the preparation of financial policies is the lack of adequate financial information. Your local government may not have enough information to evaluate and predict its financial condition. A management letter may not accompany annual audits. The annual financial report may not include explanatory notes. Historical data needed to project trends may not have been compiled. Information on ***overlapping debt*** may be unavailable. Projections of revenues and expenditures may not extend beyond one year. It is extremely difficult to identify the need for policies in the absence of information on a local government's financial condition and practices.

LACK OF KNOWLEDGE ABOUT CONCEPTS AND PRACTICES

Another barrier to the development of financial policies exists when elected officials are not familiar with local government finance concepts, terminology, and practices. The financial education of elected officials through reports and workshops is a vital staff responsibility. The educational process should include interpreting financial reports, audits, debt statements, and other financial documents. Information provided to elected officials must be prepared in clear, non-technical language. Elected officials must be well informed about the local government's current practices in

each area of financial operation along with an understanding of best practices and standards.

FEW STANDARDS AND BENCHMARKS

The development of policies may be handicapped by the limited availability of benchmarks and standards. This is particularly a problem for local governments new to the process of self-government. Previously, major financial policies may have been prescribed by the central government. A special effort will be necessary to locate “rules of thumb” and benchmarks to guide policy making. Elected officials may find themselves exploring new but informative financial territory. Time will be needed for the development of comparative local government data and for individual governments to accumulate sufficient historical data to project trends.

LEARNING APPLICATION

ELECTED OFFICIAL _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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We have identified some but not all obstacles to the development of written financial policies.

List other barriers, which you can imagine or have experienced.

What works and what does not work in overcoming obstacles?

STEPS IN FINANCIAL POLICY DEVELOPMENT

A systematic approach can simplify the development of financial policies. The approach we have in mind consists of eight steps.

STEP 1. GET ORGANISED

A first step in policy development is to clearly define who will be responsible for what in implementing the process. This includes clarifying the roles of citizens, governing body members, chief executive officer, and staff.

CITIZENS

The degree to which citizens are involved in the process is a matter policymakers will need to decide regardless of the organising method adopted. Several options are available for soliciting citizen input.

- Appoint citizens to the policy committee, or establish a separate citizen advisory committee.
- Obtain citizen reactions to policy recommendations through public meetings or formal hearings.
- Solicit suggestions from those citizens and organisations that might be most affected by the proposed policy, i.e. businesses, community groups representing minority members of your community, financial institutions, etc.

GOVERNING BODY MEMBERS

Elected officials, as local government's designated policy makers, have a wide range of roles in this process. Here are a few of the more important ones.

- Identify areas where policies are needed.
- Direct staff to explore what other local governments are doing in this area of policy concern. In other words ask them to carry out a comparative analysis.
- Based on what they have learned ask them to prepare an analysis of the potential policy options
- Make sure that all the potential stakeholders in the proposed policy have been consulted.
- Approve the final policy.

CHIEF EXECUTIVE OFFICER

- Identify areas where policies are needed.
- Involve your staff in conducting research into specific policy needs and how other local governments have dealt with the issues associated with specific policies under consideration
- Develop policy options to be considered by the local governing body.

- Based on their deliberation of the policy options, draft the final version of the policy for their consideration.
- Submit the draft policy to the local governing body for their adoption.
- Implement the approved policy.

STAFF

- Identify areas where policies are needed.
- Propose options to the chief executive officer.
- Assist in writing policy drafts.
- Be prepared to implement the policy or policies once they have been adopted by the elected body.

APPROACHES FOR ESTABLISHING FORMAL POLICIES

As you can see from the discussion of who might do what with whom in developing policies there are overlapping responsibilities within most local governments. Here are some potential options to consider

One approach is for elected officials to establish a governing body committee on financial policies. The governing body and finance staff should assist the committee and be responsible for periodic consultation with the committee.

Another approach is for elected officials to ask the chief executive officer to prepare a recommended policy framework. The chief executive and the finance staff would subsequently follow through and prepare a report for the local government governing body, usually with the participation of other department heads. Sometimes a chief executive will see the need for formal written financial policies and initiate the development process without a request from elected officials.

A third alternative is for the governing body to set up a policy committee or task force consisting of a mix of elected officials and staff. Finance personnel with expertise are assigned to work with the committee. This approach has distinct advantages. All the key players, the chief executive or designee, selected governing body members and key staff members, are involved in the development process. Such a collaborative effort can heighten opportunities for agreement or creative compromises and reduce the likelihood of unwanted surprises.

STEP 2. DEFINE THE PROCESS

Formalizing the process to be followed is the next important step. It is essential that this process be transparent to citizens and the local governing body. Most important is to decide if a comprehensive or piecemeal approach is to be followed. The comprehensive approach involves developing financial policies for all financial activities of the local government. This approach has the advantage of showing the interrelationships among policies and, thereby, revealing potential conflicts and inconsistencies. However, the comprehensive approach is complex and time consuming. Governing body members may be prone to resist it as overly burdensome.

The piecemeal approach, on the other hand, involves selecting one or two specific financial activities (e.g., budgeting and debt) and developing written policies for these activities. This approach reduces the scale of the effort and serves as a pilot

project for testing the methodology. Care will have to be taken using the piecemeal approach, however, to consider the implications of proposed policies on those not currently being considered and on linkages among policies.

There are other approaches as well. It may be desirable, for example, to focus the policy development process on a current and particularly serious financial problem. Examples are difficulty in borrowing money or responding to adverse audit comments. Still another approach is to concentrate policy development on key financial issues such as financial disclosure, risky investment practices or new revenue sources.

Careful selection of the methodology to be used is directly related to project success. Employ a deliberate process based on a thorough analysis of all the conditions surrounding an issue and various alternatives. Develop policies on a coordinated basis. Your primary concern should be direction and results. You may find it helpful to prepare a matrix comparing the various policies. Develop a timetable covering such steps as the start date, proposed meetings and public hearings, and report completion. The timetable will assist in making staff assignments and ensuring that the project progresses smoothly.

STEP 3. REVIEW EXISTING POLICIES AND PRACTICES

The third step is to identify and review existing policies and practices. Generally, you will find it necessary to investigate many sources to find evidence of financial policies. They may be found in local and central government laws and regulations, budgets, governing body minutes, finance procedures and manuals, agreements, and administrative practices. Don't overlook the fact that many unofficial and informal policies are not in writing but exist only in the minds and past practices of staff and elected officials. These people will need to be interviewed in order to identify the thought processes that have led to the creation of existing budget, debt, investment, and other financial policies.

Careful examination of financial practices is another way to gain insight into existing policies or lack of policies. By comparing your local government's financial practices against established standards of local government finance and other best practices you will gain an understanding of policy gaps or inadequacies.

What is not found during the review is just as important as what is found. For example, when looking at accounting practices you may learn that there are no written accounting procedures or that your practices do not comply with generally accepted accounting standards. As you examine revenue practices you may learn that revenue surveys are not conducted, there are no revenue guidelines, fee decisions do not address cost recovery and fixed assets are not inventoried or valued. These findings indicate immediately the need for appropriate policies.

STEP 4. BENCHMARK POLICIES AND PRACTICES

While you are scrutinizing your policies and practices, you should begin collecting information on appropriate standards or benchmarks from other sources, i.e., practices that are recognized as representing best practices from the standpoint of organi-

sational improvement. From the list of sources shown below, you should be able to identify those, which are relevant to local governments in your country.

- Other local governments
- Local professional associations
- Central government ministries
- University institutes working with local governments
- Associations of local governments
- Banks and financial institutions

Considerable information is available on financial policies. Many local governments have developed complete or partial policy frameworks. Examples of policies are found in budgets, capital investment plans, financial reports, manuals, and policy documents. Universities, research agencies, and ministries of finance are another good source. Usually they are familiar with what has been published locally on various areas of public finance. They may have conducted research on financial policy development.

Banks, financial institutions, bond insurance companies, credit rating agencies and other experts have devised rules of thumb and benchmarks through experience and observation which are helpful for financial condition analysis and policy development.

Shown below are several common benchmarks. Keep in mind, however, that these benchmarks are based on the experience of cities in the United States and should be regarded only as illustrations of type and form.

- Uncollected taxes should not exceed five to eight percent of total taxes assessed/levied.
- A deficit of more than five to ten percent of the total operating budget in any one year may be a danger signal.
- Short-term debt outstanding at the end of the fiscal year should not exceed five percent of operating revenues.
- Annual debt service as a percentage of recurring revenues should not be more than 15 percent.
- National revenue as a percentage of recurring revenue should not exceed 50 percent.
- The liquidity ratio of cash and short-term investments to current liabilities should not be less than one to one.
- You will have to determine the validity of these types of policy guidelines for your local government based on your country's perspective and legal framework. If a trend compares unfavourably, you will at least know which issues to address. Even a subjective analysis of how trends in your local government may influence your financial condition can be beneficial. Moreover, trends may indicate that your local government's financial practices are inadequate and demonstrate the need for financial policies. A steady pattern of declining investment earnings, budget overruns, revenue shortfalls and low tax collections point to probable deficiencies in your financial management practices and policies.

Local governments with limited experience in self-government will have a limited number of years of reference and comparative data. As a result, benchmarks will not be of immediate value. Where this is the situation, it will be necessary to begin gathering and analyzing historical and future financial data. This will enable local officials to begin using trends to analyze and interpret the changes in financial condition. By focusing on factors and trends over a relatively long period of time, it will become clear that financial problems are intensifying or improving and that there is or is not a need for new or modified financial policies.

STEP 5. DRAFT POLICY STATEMENTS

After diagnosing the current state of your local government's policies and identifying desired policies, you are ready to draft policy statements. Written statements should be clear, concise, understandable, attainable, realistic, and defensible. Be prepared to explain the assumptions and rationale underlying recommended policies. Ask questions about the proposed statements of policy such as:

- What is the purpose of the policy proposal?
- Is it to correct or prevent a financial problem?
- Does the statement relate to a benchmark or standard?
- How does the policy relate to other policies?
- Does the policy change an existing policy?
- Does the policy address conflicts or inconsistencies in existing policies?

Keep in mind that policies should meet local needs and should be flexible. Generally, it is helpful to group policy statements by financial activity such as budgeting, debt, etc. Preparation of a policy chapter or brochure facilitates distribution. Examples of policy statements are found in the appendix following this essay.

STEP 6. REVIEW AND ADOPT POLICIES

After policy statements are drafted, department heads and the policy committee, if one is established, should review them. Subjecting the statements to vigorous examination will ensure that they are clear and defensible. You may want to have them critiqued by citizens and expert advisors as well.

Once the review is completed, the written policy statements are presented to the governing body for adoption. They should be accompanied by an explanation of the process followed in developing them. It is advisable to schedule workshops to review and discuss new policy statements. If appropriate and desirable, a public hearing can be held.

Most important is to encourage formal adoption of the policies. Elected officials should understand the significance of policies as goals for the financial management of the local government and as a statement of the kind of financial condition desired.

STEP 7. IMPLEMENT AND PUBLICIZE POLICIES

After policy statements are adopted, they should be reinforced and used in decision making. Policies should be used to guide preparation of the operating budget and capital investment plan and other discussions of financial issues. They should be integrated into evaluations of financial condition to show the extent to which the local government's practices comply with its policies. Policies should be used by the staff and external auditors to evaluate the performance of the financial management system. Performance evaluation criteria should incorporate statements of policy for guidance of the finance staff. Adherence to financial policies is the best insurance the local government has for the maintenance of a sound financial position.

Other methods for disseminating policy statements include:

- Referring to them in the operating budget, capital investment plan and annual financial report;
- Distributing copies to financial institutions and credit rating agencies;
- Incorporating them into disclosure statements;
- Sending copies to the appropriate ministries;
- Referring to the policies when making policy-related recommendations to the governing body; and
- Distributing copies to professional and governmental associations.

STEP 8. MONITOR THE IMPLEMENTATION OF POLICIES

Continual monitoring and adjustment are critical to effective financial policies. The policy process should be fluid and flexible. They require fine-tuning, redefining, and updating in response to new problems and needs. New financing methods, changes in national legislation, new standards, emerging financial issues and financial stress are just a few of the factors that may require policy modification. Regular reviews are important if financial policies are to continue serving as relevant guides for the efficient management of a local government's financial affairs.

LEARNING APPLICATION

ELECTED OFFICIAL _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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Because of the importance of written financial policies, we suggest you develop a strategy for reviewing and strengthening the financial policy process in your local government.

What will you do after the workshop when you return to your local government?

Does your policy framework need an overhaul or a minor tune-up?

What policy areas need attention?

Prepare a list of objectives you want to achieve.

INTERNET RESOURCES

Following are some resources on Policy Making that you may find helpful.

East Asia Decentralizes—Making Local Government Work in East Asia [HTTP://WEB.WORLDBANK.ORG/WBSITE/EXTERNAL/COUNTRIES/EASTASIAPACIFICEXT/EXT/APDECEN/0,,CONTENTMDK:20516472~PAGEPK:64168427~PIPK:64168435~THE SITEPK:1169052,00.HTML](http://WEB.WORLDBANK.ORG/WBSITE/EXTERNAL/COUNTRIES/EASTASIAPACIFICEXT/EXT/APDECEN/0,,CONTENTMDK:20516472~PAGEPK:64168427~PIPK:64168435~THE SITEPK:1169052,00.HTML)

Mainstreaming Sustainability into Local Government Policy Making (2002-2003)

<http://www.sustainable-cities.org.uk/AspProcess/papersummary.asp?id=52>

Involving young people in LG policy making

www.jrf.org.uk/knowledge/findings/government/632.asp

Engage citizens in policy making in LG

www.oecd.org/dataoecd/62/23/2501856.pdf

Local Government and Public Service Reform Initiative—It examines local government policy-making activity and its role in the integration (not assimilation) of diverse communities.

http://lgi.osi.hu/documents.php?id=745&m_id=&bid=30..contentMDK:20516472~pagePK:64168427~piPK:64168435~theSitePK:1169052,00.html

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Local Government and Public Service Reform Initiative—It examines local government policy-making activity and its role in the integration (not assimilation) of diverse communities.

http://lgi.osi.hu/documents.php?id=745&m_id=&bid=3

APPENDIX A: SAMPLE FISCAL POLICIES

To establish and document a policy framework for fiscal decision making, the chief executive officer, finance manager and staff should develop and maintain a comprehensive set of financial management policy statements.

Following are samples of the kinds of policies that local governments should be adopting to provide the structure for managing their financial resources and processes.

These are actual policies taken from local governments around the world. We have not tried to edit or assimilate the policies into one recommended set. Instead, we recommend that you pick and chose those samples that are most applicable for your local government and country.

ACCOUNTING

Author's comment: Each country has its own set of generally accepted accounting standards and principles. Many countries are members of and use the International Federation of Accountants (www.ifac.org). IFAC has a Public Sector Committee which focuses on the accounting, auditing, and financial reporting needs of national, regional and local governments, related governmental agencies, and the constituencies they serve. The Public Sector Committee has issued standards (IPSASs) which sets world-wide standards for financial reporting by governments and others in public sector organisations.

- The local government will establish and maintain accounting practices in accordance with generally accepted accounting principles (GAAP) and generally accepted auditing standards (GAAS).
- The local government will establish and maintain a comprehensive, integrated accounting system which provides a timely, reliable basis for making financial decisions and providing an accurate picture of the local government's financial condition.
- The local government shall establish and maintain an internal control structure with adequate separation of functions designed to provide reasonable assurance that local government assets are safeguarded and the potential of significant errors in the local government's financial records are minimized. From time to time these procedures should be reevaluated.
- Procedures shall be developed and maintained that will ensure financial transactions and events are properly recorded so all financial reports may be relied upon as accurate, complete and up-to-date.
- Procedures will be designed and maintained to ensure that adequate safeguards exist over the access to and use of financial assets and records.

AUDITING

- The local government will have an annual audit performed by an audit firm, independent of the executive, which will issue an opinion on the

financial integrity of governmental accounts, the annual financial statements and provide a management letter detailing areas that need improvement.

- Every five years, the local government shall change auditing firms to perform the annual audit.
- The local government's accounting practices and financial reporting shall conform to generally accepted accounting principles (GAAP) as promulgated by the (accounting association, national agency, organisation or entity).

FINANCIAL REPORTING

- The local government will prepare and present regular reports that analyze, evaluate and forecast the local government's financial performance and economic condition.
- The local government will issue an annual report in conformity with generally accepted accounting principles (GAAP) and that provides full disclosure. This report should be issued no later than six months after the close of the fiscal year.
- The local governments shall identify clear mechanisms for the coordination, management and reporting to the governing body and public of any extra-budgetary activities.
- The local government will publish full information on the level and composition of its debt.
- The local government will publish full information on the level and composition of its assets.
- Results achieved relative to the goals and objectives of major budget programmes will be presented annually to the local governing body.
- Monthly reports shall be prepared for review by the CEO and governing body and include: comparisons of expenditures and revenues to current budget; expenditures and revenues projections through the end of the year; the status of fund balances; and remedial actions necessary to maintain the local government's financial position.

FINANCIAL CONDITION

- The local government will issue a 5-year financial condition forecast each year.
- The local government will establish benchmarks for key trends and monitor and issue reports on these trends on a quarterly basis.
- Independent experts should be invited to assess fiscal forecasts, the macroeconomic forecasts on which they are based and all underlying assumptions.

ANNUAL OPERATING BUDGET

- A five-year forecast of revenues and expenditures, to include a discussion of major trends affecting the local government's financial position, shall

be prepared in anticipation of the annual budget process. The forecast shall examine critical issues facing the local government, economic conditions, and the outlook for the upcoming budget year.

- The local government will project revenues and expenditures for the next three to five years and will update the projections annually.
- New policies being introduced in the operating budget and capital investment plan will be clearly described.
- Budget information will be presented in a way that facilitates policy analysis and promotes accountability.
- Fiscal policy objectives and an assessment of fiscal sustainability should provide the framework for the annual budget.
- The local government shall assure fiscal stability and the effective and efficient delivery of services, through the identification of necessary services, establishment of appropriate service levels, and careful administration of the expenditure of available resources.
- The local government shall operate on a current funding basis. Expenditures shall be budgeted and controlled so as not to exceed current revenues plus the planned use of fund balance accumulated through prior year savings.
- The CEO shall authorize periodic staff and third-party reviews of local government programmes for both efficiency and effectiveness. Privatization and contracting with other governmental agencies will be evaluated as alternative approaches to service delivery. Programmes, which are determined to be inefficient and/or ineffective, shall be reduced in scope or eliminated.
- Budget data will reflect recent revenue and expenditure trends, underlying macroeconomic developments, and well-defined policy commitments.
- The local government will develop a programme to integrate performance measures and productivity indicators with the annual budget.
- Debt or bond financing will not be used to finance current operating expenditures.
- Within the resources available each fiscal year, the local government shall maintain capital assets and infrastructure at a sufficient level to protect the local government's investment, to minimize future replacement and maintenance costs, and to continue service levels.
- The local government will conduct a cost analysis of all services on a regular basis.
- The local government will project future operating costs associated with new capital investments and will include them in the operating budget forecasts.
- The chief executive officer or designee will perform a mid-year budget review and analysis and provide the information to the governing body.
- The local government will adopt and maintain a balanced budget.
- Expenditure deferrals into the following fiscal year, short-term loans, or use of one-time revenue sources shall be avoided to balance the budget.
- The local government shall take immediate corrective actions if at any time during the fiscal year expenditure and revenue re-estimates are such

that an operating deficit (i.e., projected expenditures in excess of projected revenues) is projected at year-end.

CAPITAL INVESTMENT PLAN AND BUDGET

- A summary report on the contracts awarded, capital projects completed and the status of the local government's various capital programmes will be prepared at least quarterly and presented to the CEO and governing body.
- The local government will develop and follow multi-year maintenance and replacement schedules.
- The local government will allocate xx% of its general operating fund revenues for cash capital investments.
- The local government will develop a multi-year plan for capital investments, update it annually, and make all capital investments in accordance with the plan.
- The local government will develop criteria to evaluate and prioritize each capital investment.
- The local government will conduct an annual review of the state of the local government's capital equipment and infrastructure, setting priorities for its replacement or renovation based on needs, funding, alternatives, and availability of resources.
- The local government shall annually review the needs for capital investments and equipment, the current status of the local government's infrastructure, replacement and renovation needs, and potential new projects. All projects, ongoing and proposed, shall be prioritized based on an analysis of current needs and resource availability. For every capital project, the full cost of operation, maintenance and replacement should be calculated and reported.

FUND BALANCES/RETAINED EARNINGS

- The local government will maintain the fund balance and retained earnings of the various operating funds at levels sufficient to protect the local government's creditworthiness as well as its financial positions from unforeseeable emergencies.
- The local government shall strive to maintain the General Fund undesignated fund balance at 10 percent of current year budget expenditures.
- In utility operating funds, the local government shall strive to maintain positive retained earnings positions to provide sufficient reserves for emergencies and revenue shortfalls. In utility funds, an operating reserve will be established and maintained at 20 percent of the current year's budget appropriation for operation and maintenance, which is defined as the total budget less debt service and capital project expenditures.
- Σ Fund balance/retained earnings shall be used only for emergencies, non-recurring expenditures, or major capital purchases that cannot be accommodated through current year savings.

- The local government shall maintain sufficient reserves in its debt service funds, which shall equal or exceed the reserve fund balances required by debt instrument legal requirements.

RESERVES

- The local government will maintain a year-to-year fund carryover balance of at least xx% of general operating revenues in order to maintain adequate cash flow and to reduce the demand for short-term borrowing.
- The local government will maintain an emergency reserve at a level not to exceed xx % of the operating fund budget to provide for temporary funding of unforeseen needs of an emergency or non-recurring nature and to permit orderly adjustment to changes resulting from reductions or termination of revenue sources.

REVENUES

- The local government will make realistic forecasts of revenue using more than one forecasting method and clearly state the assumptions underlying the forecasts.
- The local government shall strive to maintain a balanced and diversified revenue system to protect the local government from fluctuations in any one source due to changes in local economic conditions, which adversely impact the source.
- The local government will design, maintain and administer a revenue system that will assure a reliable, equitable, diversified and sufficient revenue stream to support desired local government services.
- The local government shall endeavour to reduce its reliance on any one form of revenues by revenue diversification, implementation of user fees, and economic development.
- In order to maintain a stable level of services, the local government shall use a conservative, objective, and analytical approach when preparing revenue estimates. The process shall include analysis of probable economic changes and their impacts on revenues, historical collection rates, and trends in revenues. This approach should reduce the likelihood of actual revenues falling short of budget estimates during the year and should avoid midyear service reductions.
- The local government shall seek to eliminate all forms of subsidization to utility/enterprise funds from the General Fund.
- The local government shall maintain high collection rates for all revenues by keeping the revenue system as simple as possible in order to facilitate payment. Since revenue should exceed the cost of producing it, the local government shall strive to control and reduce administrative costs.
- The local government shall pursue to the full extent allowed by state/province law all delinquent taxpayers and others overdue in payments to the local government.

- Intergovernmental revenues will not exceed more than one-half of the estimated revenues for the current operating budget.

USER FEES

- The local government will conduct an annual review of selected fees and charges to determine the extent to which the full cost of associated services is being recovered by revenues.
- The local government will review all fees and charges at least once every four years.
- The local government will place increased emphasis on user charges to finance the cost of local government services.
- For services that benefit specific users, the local government shall establish and collect fees to recover the costs of those services. Where feasible and desirable, the local government shall seek to recover full direct and indirect costs.
- User fees shall be reviewed on a regular basis to calculate their full cost recovery levels, to compare them to the current fee structure, and to recommend adjustments where necessary.
- Utility rates and user fees shall be set at levels sufficient to cover operating expenditures, meet debt obligations, provide additional funding for capital investments, and provide adequate levels of working capital.

GRANTS

- The local government will pursue national, state/province, foundation, and other source grants-in-aid when they are consistent with the local government's priorities and policy objectives.
- All grant submittals shall be reviewed for their cash match requirements, their potential impact on the operating budget, and the extent to which they meet the local government's policy objectives.
- An annual report on the status of grant programmes and their effectiveness shall be prepared.

DEBT MANAGEMENT

- The local government will not use long-term debt for current expenses.
- The local government will retire short-term debt within twelve months.
- The local government's long-term debt will not exceed \$ xxx per capita.
[Author's note: total long-term debt is divided by population of local government to arrive at per capita amount.]
- The local government will limit long-term borrowing to capital investments which cannot be financed from current revenues.
- The local government's annual debt service will not exceed xx% of the total operating revenues.
- Debt financing shall only be used to: purchase capital assets that cannot be acquired from either current revenues or fund balance/retained earnings; and fund infrastructure investments and additions. The useful life of

the asset or project shall exceed the payout schedule of any debt the local government assumes.

- The local government shall not assume more debt than it retires each year without conducting an objective analysis as to the community's ability to assume and support additional debt service payments.
- The local government shall use a competitive bidding process in the sale/issuance of debt unless the nature of the issue warrants a negotiated sale..

CASH MANAGEMENT

- The local government will invest at least xx % of its idle cash on a continuous basis.
- The local government will maintain at least xx % of its portfolio in liquid investments, which are available on a daily basis without loss of principal.
- The local government's investment officer will file monthly reports of investment activity with the local governing body which include information on type of investment, purchase date, maturity date, face value or purchase cost, market value, rate of interest and amount of interest received.
- Where permitted by law, the local government will pool cash from separate funds and sources to maximize interest earnings.
- The local government will establish guidelines that emphasize the safety and liquidity in the investment of its funds.
- The local government should invest its cash reserves to: insure the absolute safety of principal and interest; meet the liquidity needs of the local government; and, achieve the highest possible yield.
- All aspects of cash management operations shall be designed to ensure the absolute safety and integrity of the local government's financial assets.
- Cash management activities shall be conducted in full compliance with prevailing local, state/province and national regulations.
- At all times, the local government shall maintain a cash position sufficient to meet daily liquidity requirements.

PROCUREMENT

- The local government will centralize its purchasing function.
- The local government will solicit competitive bids for all purchases over \$ xxxxxx.
- The local government will conduct an annual auction of surplus and obsolete personal property.
- The local government will conduct an annual inventory of all personal property.
- The local government will establish a programme of delivery inspection to ensure that items delivered meet specifications.
- Procurement regulations should be standardized and accessible to all interested parties.

- The local government shall make every effort to maximize any discounts offered by creditors/vendors and use competitive bidding to attain the best possible price on goods and services.

ECONOMIC DEVELOPMENT

- The local government will initiate, encourage and participate in economic development efforts to create job opportunities and strengthen the local economy.
- The local government shall endeavour, through its regulatory and administrative functions, to provide a positive business environment in which local businesses can grow, flourish and create jobs.
- The local government shall encourage and participate in economic development efforts to expand the local government's economy and tax base and to increase local employment.
- The local government's economic development programme shall seek to expand the non-residential share of the tax base to decrease the tax burden on residential homeowners.
- The local government's economic development programme shall encourage close cooperation with other local jurisdictions, chambers of commerce, and groups interested in promoting the economic well being of this area.
- The local government shall use enterprise zones as allowed by law to encourage new investment and business expansion in target areas as designated by resolution of the local government governing body.
- The local government shall coordinate with state/province and national agencies on offering any incentive programmes for potential economic expansion.

ASSET MANAGEMENT

- The local government will centralize its asset management.
- The local government will solicit competitive bids for all sales of property valued in excess of a monetary value established by the governing body.
- The local government will conduct an annual auction of surplus and obsolete assets.
- The local government will conduct an annual inventory of all assets.

RETIREMENT SYSTEM

- The local government shall ensure that the Employees' Retirement Fund is adequately funded and operated for the exclusive benefit of the participants and their beneficiaries.
- The governing body will assure that sufficient funding will be available to pay for the liabilities created by retirement benefit improvements and other plan changes.

RISK MANAGEMENT

- The local government will establish a self-insurance programme to provide for protection against major losses in excess of \$ xxxxxx.
- The local government will purchase excess insurance coverage for catastrophic losses up to \$ xxxxxx.
- The local government will establish a risk management programme to minimize losses and reduce costs.
- The local government will establish a risk reserve at a level that, together with purchased insurance policies, adequately protects the local government's assets against loss.
- Major fiscal risks should be identified and quantified where possible, including variations in economic assumptions and the uncertain costs of specific expenditure commitments

IN CONCLUSION

As you can see, there are many fiscal policies that are needed to assure that your financial management house is in order. For many smaller local governments this litany of policy statements may be overwhelming. For those larger local governments that have not given much thought to assuring that their fiscal practices are backed up by policy declarations, this may be a wake-up call. Whatever your local government's circumstances might be in terms of having policies in place to guide your financial management decision making processes, there is no better time than NOW to perform a reality check on your local government's fiscal policies.

If you are an elected official, ask your CEO to provide an update for the governing board on the status of your fiscal policies, based on the suggested policies listed above.

If you are the CEO or Finance Director, call a meeting of your management team and spend some time reviewing the policy statements just listed. You might photocopy these pages and ask each member of your team to check off those policies statements that are important to the financial health of your local government but aren't part of your current financial management practices. After all, policies are operational guidelines and mandates. This meeting will be a good time to make some decisions about what you need to do to get your fiscal policies up to date.

Based on this staff meeting, prepare a report for your elected officials on the current status of your fiscal policies. Request an opportunity to hold a work session with them to discuss action steps that can be taken to update and strengthen your local government's fiscal policies.

PART TWO—MANAGEMENT TOOLS

PURPOSE

Financing a local government requires managers to assist elected leaders to translate goals into programmes and services through declarations of financial policy. In other words, policy is the critical juncture between the way local government officials have decided to finance their programmes and services (goals and purposes), and how these financial intentions can be implemented (strategies and plans).

Don't forget to look back at the Learning Applications! Many of them can be easily adapted for group exercises and may be more appropriate for persons who are just being introduced to the concepts of policy making.

CONTENTS

This workshop is designed to broaden the understanding about the nature and importance of policy in the financing of public programmes. It also provides skills to develop and implement a policy framework suitable for managing the financial affairs of your local governments.

A brief description of each learning activity is shown below with an approximation of the amount of time required. To conduct a workshop that includes all of the components described below will take approximately 1 1/2 days. A workshop can be condensed into a single day, however, by omitting the mini-case study (2.4). If you wish to change the order, to omit something, or to add training material of your own, feel free to do so.

1.1 WARM-UP EXERCISE: FINANCIAL POLICY NEGLECT

Participants, in small groups, review an incident that involves a potentially costly decision for a local government that might have been avoided with proper policy guidance. (45 minutes)

1.2 FINANCIAL POLICY INVENTORY

Participants complete an inventory of their current financial policies, indicating opposite each policy if it is observed in practice and if it is reviewed and updated periodically. (30 minutes)

2.3 TRAINER PRESENTATION

Brief concept presentation based on the preceding essay that focuses on the consequences of not having financial policies, characteristics of good financial policies, the policy framework, and obstacles to policy implementation. (30 minutes)

14 MINI-CASE STUDY: THE LANDOWNER'S GIFT (OPTIONAL)

Participants read and discuss in small groups a situation that involves making a significant decision with long-term implications for the local government in the absence of financial policy guidance. (90 minutes)

1.5 EXERCISE: AN APPROPRIATE POLICY

Participants review a set of policy statements on revenue maximization and analyze the appropriateness of each statement for adoption by their own local governments. (60 minutes)

1.6 EXERCISE: THE FINANCIAL POLICY MATRIX

Participants, working individually and in small groups: 1) develop specific policy statements that conform to criteria supplied by the instructor; and 2) begin constructing a policy frame-work relative to their finance category using a matrix supplied by the instructor. (105 minutes)

1.7 EXERCISE: BARRIERS TO POLICY IMPLEMENTATION

Still working in small finance topic groups, participants identify obstacles to the implementation of finance policies in their respective categories and ways to overcome or minimize these obstacles. (60 minutes)

1.8 CLOSING EXERCISE: LEARNING TRANSFER

Participants reflect individually on what they have learned and make commitments to put it to use back home after the workshop. (30 minutes)

1.1 WARM-UP EXERCISE: FINANCIAL POLICY NEGLECT

TIME REQUIRED

40 minutes

PURPOSE

As pointed out in the preceding essay, financial policies are statements of fiscal intent and guides for financial decision making. To achieve their maximum usefulness, financial policies must be thoughtfully conceived, agreed to by elected officials, and published in written form. The importance of pre-approved written policies can be demonstrated best by observing the unfortunate results when local elected officials are expected to make a decision with long-term financial implications without financial policy guidance.

PROCESS

Provide each participant with a copy of the incident, “Ready! Fire! Aim!” on the next page. Ask participants to read the incident. When they have read the incident, divide them into four or five small groups. Ask each group to answer the three questions that follow the incident and report back with its answers in twenty minutes.

When the small groups have reported back, ask each group how it answered each of the three questions. Encourage a general discussion and comparison of viewpoints particularly with respect to the role of financial policy as guidance in making decisions with important financial implications.

Ready! Fire! Aim!

Two years ago, your local government received a four-year grant from a foreign donor to finance the community's efforts to implement a toxic waste removal project in fulfilment of a portion of its local Agenda 21 programme commitments. The terms of the grant agreement were generous although a bit unconventional. The donor agreed to fund the programme totally for the first two years. In the third and fourth years, however, the donor's participation was to be based on the extent to which the local government had actually achieved the performance objectives it had stipulated in the grant agreement for the preceding two years of the programme.

In order to ensure its compliance with the terms of the grant agreement, the local government governing body approved the purchase of expensive toxic waste abatement equipment utilizing a new and some-what experimental technology. Since current revenues were not sufficient to pay for the equipment, the finance director recommended borrowing the needed capital and retiring the loan from grant receipts over the four-year term of the grant. If the equipment performed as promised by the manufacturer, the director advised the local government governing body, the local government would have no difficulty performing as anticipated and funds from the grant would be sufficient to meet the community's debt obligations.

Questions

1. What is the finance director failing to consider in advising the local government governing body to assume the debt obligation?
2. Is the risk taken by the governing body in approving the equipment purchase under these terms an acceptable one? Explain your answer.
3. What kind of policy would help the finance director and local government governing body avoid or minimize the financial risk?

1.2 EXERCISE: FINANCIAL POLICY INVENTORY

TIME REQUIRED

45 minutes

PURPOSE

Provide participants with an opportunity to recall and evaluate their respective local government's current financial policies.

PROCESS

Distribute copies of the inventory form on the following pages of the hand-book so that each participant has a copy. Ask participants to use the form to inventory the financial policies of their own local governments following the instructions at the top of the form. Read the instructions with them and remind them that the policy statements are illustrative. That is, they don't cover everything, and there may be differences in wording from one local government to another.

Trainer's note. Suggest that participants work alone on the inventory. However, encourage participants who are attending the workshop from the same local government to collaborate in completing the inventory.

Give participants about 20 minutes to complete the inventory. When participants have completed the exercise, ask for volunteers to discuss their results as follows.

Ask for a show of hands—if “yes,” raise your hand—to each of the following questions:

1. Does your local government have financial policies? How many?
2. Are your local government's financial policies consulted and used as a basis for decision making by the local governing body and finance staff?
3. Is it the practice of your local government to regularly review and update its financial policies?
4. Which financial policies not currently developed by your local government should be considered for adoption in the near future? (Identify three of the most significant policies you have identified.)

Trainer's note. Count the hands that go up in reply to question 1. Before moving on to the 2nd question, ask how many of these policies are in writing. Also ask how many participants checked “yes” to at least half the policy statements on the list. Continue by counting the hands that go up in reply to questions two and three. Calculate what % of the total ... opposite the question. Also, ask participants to report their re-

sponses by policy category to identify the categories in which policies are being used and the categories in which they are not being used.

Inventory of Current Financial Policies						
Policy Statement	Our local government has a similar policy		Policy is used as a guide for decision making		Policy is regularly reviewed and updated	
	Yes	No	Yes	No	Yes	No
CAPITAL INVESTMENT PLAN AND BUDGET POLICY						
The local government will project future operating costs associated with new capital improvements and will include them in the operating budget forecasts.						
The local government will develop and follow multi-year maintenance and replacement schedules.						
The local government will allocate xx% of its general operating fund revenues for cash capital investments.						
The local government will develop a multi-year plan for capital improvements, update it annually and make all capital improvements in accordance with the plan.						
The local government will develop criteria to evaluate and prioritize each capital project.						
RESERVE POLICY						
The local government will maintain a year-to-year fund carryover balance of at least xx% of general operating revenues in order to maintain adequate cash flow and to reduce the demand for short-term borrowing..						
The local government will maintain an emergency reserve at a level not to exceed xx% of the general fund budget to provide for temporary funding of unforeseen needs of an emergency or non-recurring nature and to permit orderly adjustment to changes resulting from reductions or termination of revenue sources.						
The local government will establish an equipment reserve fund to replace capital outlay items.						

Inventory of Current Financial Policies						
Policy Statement	Our local government has a similar policy		Policy is used as a guide for decision making		Policy is regularly reviewed and updated	
	Yes	No	Yes	No	Yes	No
DEBT POLICY						
The local government will not use long-term debt for current expenses.						
The local government will retire short-term debt within twelve months.						
The local government's long-term debt will not exceed \$ xxx per capita.						
The local government will limit long-term borrowing to capital improvements or projects which cannot be financed from current revenues.						
The local government's annual debt service will not exceed xx% of the total operating revenue..						
CASH MANAGEMENT POLICY						
The local government will invest at least xx% of its idle cash on a continuous basis.						
The local government will maintain at least xx% of its portfolio in liquid investments which are available on a daily basis without loss of principal.						
The local government's investment officer will file monthly reports of investment activity with the local government council which include information on type of investment, purchase date, maturity date, face value or purchase cost, market value, rate of interest, and amount of interest received.						
When permitted by law, the local government will pool cash from separate funds and sources.						
The local government will emphasize safety and liquidity of its funds.						

Inventory of Current Financial Policies						
Policy Statement	Our local government has a similar policy		Policy is used as a guide for decision making		Policy is regularly reviewed and updated	
	Yes	No	Yes	No	Yes	No
PURCHASING POLICY						
The local government will centralize its purchasing function.						
The local government will solicit competitive bids for all purchases over \$ xxxxxx.						
The local government will conduct an annual auction of surplus and obsolete personal property.						
The local government will conduct an annual inventory of all personal property.						
The local government will establish a program of delivery inspection to ensure that items delivered meet specifications.						
RISK MANAGEMENT POLICY						
The local government will establish a self-insurance program to provide for protection against major losses in excess of \$ xxxxxx.						
The local government will purchase excess insurance coverage for catastrophic losses up to \$ xxxxxx.						
The local government will establish a risk reserve at a level that together with purchased insurance policies adequately protect the local government's assets against loss.						
The local government will establish a comprehensive safety program including safety training, inspections, and accident analysis.						

Inventory of Current Financial Policies						
Policy Statement	Our local government has a similar policy		Policy is used as a guide for decision making		Policy is regularly reviewed and updated	
	Yes	No	Yes	No	Yes	No
OPERATING BUDGET POLICY						
The local government will project revenues and expenditures for the next four years and will update the projections annually.						
Debt or bond financing will not be used to finance current operating expenditure.						
The local government will develop a program to integrate performance measures and productivity indicators with the annual budget.						
The local government will perform a mid-year budget review and analysis.						
The local government will place increased emphasis on user charges to finance the cost of municipal services.						
REVENUE POLICY						
Intergovernmental revenues will not exceed xx% of the current operating budget.						
The local government will make realistic forecasts of revenue using more than one forecasting method and clearly state the assumptions underlying the forecasts.						
The local government will conduct an annual review of selected fees and charges to determine the extent to which the full cost of associated services is being recovered by revenues.						
The local government will develop criteria to evaluate and prioritize each capital project.						
The local government will review all fees and charges at least once every four years.						

1.3 TRAINER PRESENTATION

TIME REQUIRED

30 minutes

PURPOSE

This presentation is to provide participants with information and perspectives on the development and use of financial policies as guides for decision making.

PROCESS

Prepare the presentation based on information covered by the preceding essay on financial policies. Concentrate on the consequences of not having financial policies, characteristics of good financial policies, the policy framework, and obstacles to policy implementation.

Outlined information on note cards may help you cover the information systematically and stay on schedule. Ask questions from time to time during the presentation as a check on participant comprehension and to hold their attention. Augment the presentation with visual aids including pre-printed newsprint sheets and overhead transparencies as a further aid to comprehension.

1.4 MINI-CASE STUDY: THE LANDOWNER'S GIFT

TIME REQUIRED

90 minutes

PURPOSE

This case is to illustrate the risk of making decisions with uncertain financial consequences in the absence of specific policy guidance.

Trainer's note. Including this case study will increase the length of a workshop from one (rather long) day to 1 1/2 days. We believe allowing enough time to include it is desirable from a learning standpoint, but it can be excluded without jeopardizing the workshop if the time cannot be justified. Don't hesitate to revise the case study to make it more relevant to your participant's situation if you believe this would be helpful. For example, change the currency to your local currency. Give the family that is making the gift a name that is common in your country. Change the details about the physical surroundings to make it more real to your participant's experiences.

PROCESS

Working in small groups, tell participants they are to read a situation in which a local government is about to accept a gift of property from a large landowner in the community without first evaluating the long-term budgetary implications of the gift.

Provide each participant with a copy of a case situation, "The Landowner's Gift," (see next page). Ask participants to read the case and, in their small groups, discuss the case and the discussion questions at the end of the case.

Tell participants that, after 45 minutes, they are to return to the general session with their group's answers to each question printed on sheets of newsprint and be ready to discuss their results with other group participants.

Share the small group results, followed by a large group discussion.

Case of The Landowner's Gift

Near the centre of the local government in a fenced, wooded area, stands a tall, steel tower and associated metal storage buildings, relics of a once profitable grain storage and processing business. The twisted and rusted structures and piles of abandoned and deteriorating equipment litter over 20 acres of the other-wise beautiful, tree-lined property. The site has long been criticized by citizens and other business owners as an ugly blight on their fair local government, a dangerous hazard to the health and safety of local residents. The dilapidated tower, rising nearly 35-40 meters out of the surrounding trees, is a visible and constant reminder of the unresolved problem facing the community.

Last week, attorneys representing the family of Gnosh Gorski, deceased patriarch of the family that owns the property, approached local government officials with an offer to donate the land to the local government for the price equivalent of \$US 1. The conditions for the land donation stipulated by the family's attorneys were simple enough: the local governing body was to fulfil these two requirements;

1. Publicly declare and, in writing, affirm its unqualified intent to forgive all unpaid taxes on the property, past and present; and
2. Certify the local government's intent to restore, develop and maintain the property exclusively and forever as a public park for the benefit of community residents and visitors.

Local government officials are elated with the offer. It represents the culmination of years of effort by several generations of governing bodies to find a solution to the problem that has become a source of such dissatisfaction to so many local government residents. The governing body is unanimous in its resolve to accept the family's offer, and few members of the local government administration can ever recall such a spirit of ebullience from local government councillors on any matter to come before them. A special governing body meeting has been called to approve a resolution accepting the family's offer. A press briefing is being arranged by the mayor to announce the historic event.

The local government has no policy on gifts and donations to the local government. The local government's newly appointed director of finance has outstanding professional credentials. When employed, she received instructions from the mayor to concentrate her efforts on ways to bring greater efficiency and accountability to the local government's financial management system. The director began an examination of the local government's current financial practices and methods as a basis for developing a formal financial policy framework. This was taking place during the same week the attorneys for the Gorski family contacted the local government with its offer. The announcement persuaded the director to shift her attention to the policy implications of a gift of this magnitude. From her investigations several facts quickly emerged.

1. The current tax value of the property is the equivalent of \$US 55 million. Given the local government's current tax rate of \$US 1.55 per \$1,000 in value, the property produces \$US 85,250 in tax revenue each year. Cur-

rent property taxes are unpaid, and unpaid taxes for the last five years plus accrued penalties are calculated at \$US 425,000.

2. A quick estimate of the cost to clear the property of all existing improvements and debris is about \$US 1.2 million including disposal costs. Offsetting this cost is income to the local government of approximately \$US 90,000 from the sale of salvaged iron and steel.
3. Restoration of the land as a park site including the relocation of water lines and new sewerage appurtenances is expected to exceed \$US 2.5 million. Other **costs** related to the construction of recreation facilities, purchase and placement of playground equipment, and the development of wetland areas, jogging trails, nature paths and other as yet unplanned improvements represent a capital cost to the community in excess of five million US dollars. The impact on the annual operating budget for on-going park maintenance, insurance and utility cost has yet to be calculated.

Questions

1. What information or advice about acceptance of the landowner's gift should the finance director in this case give the chief executive officer and local governing body?
2. What would be the most appropriate action for a local governing body to take under the circumstances described in the case?
3. What lessons are provided by this case about the importance of financial policy as a guide for local government decision making?
4. What specific statement of policy would be a useful guide for a local governing body in considering the acceptance of large gifts of land?

1.5 EXERCISE: AN APPROPRIATE POLICY

TIME REQUIRED

90 minutes

PURPOSE

Assess current local government revenue maximization practices in relation to seven policy statements.

PROCESS

Working in small groups of five to six, participants are given a handout (following pages) that contains a worksheet for use in answering questions relative to seven policy statements on local government revenue maximization. Ask participants to complete the seven worksheets in the handout working alone before discussing the results with other small group members. The individual task should take about 30 minutes to complete.

Tell members of each small group that, when everyone has completed the seven worksheets, they are to discuss their respective answers to each of the policy statement questions and, after they have done this, to answer these general questions as a group:

- How is revenue maximization being practiced by the local governments in your group?
- In what policy areas is interest greatest within your group for revenue maximization?
- What are the principal obstacles to revenue maximization discussed by your group?
- What actions can individual local governments take to realize greater yield from existing revenue sources (i.e., reducing collection costs, lowering delinquency rates, making payment more convenient).

After about 30 minutes, ask a spokesperson from each small group to present the group's answers to the four questions. Engage participants in a general discussion focused primarily on their answers to the final question.

Worksheets

Evaluating Sample Revenue Policies

Each of the following pages contains a policy statement on revenue maximization. Read the first policy statement and answer the questions that follow it. Make your answers as specific as possible. When you have answered all of the questions relative to the first policy statement, move on to the second policy statement and follow the same procedure. Continue until you have answered all of the questions for all seven policy statements included in the handout.

Start with Policy Statement # 1 on the next page:

Policy Statement # 1: The local government will periodically collect and analyze information on the revenues it uses, including how much revenue each source is raising.

Is your local government doing this?

(check one) Yes ☐ No ☐

If “yes,” how often is the information collected and what use is being made of it?

If “no,” should your government be doing it?

(check one) es ☐ No ☐

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

Policy Statement # 2: The local government will periodically collect and analyze information on the revenues being used by other local governments.

Is your local government doing this?

(check one) es ___ No ___

If “yes,” how often is the information collected and what use is being made of it?

If “no,” should your government be doing it?

(check one) es ___ No ___

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

Policy Statement # 3: *The local government will establish a professional and aggressive programme for recovery of delinquent accounts, with annual reports on efforts and results prepared for elected officials.*

Is your local government doing this?

(check one) Yes ☐ No ☐

If “yes,” what is actually being done with respect to which revenue sources and with what degree of success?

If “no,” should your government be doing it?

(check one) Yes ☐ No ☐

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

Policy Statement # 4: *The local government will conduct an annual review of selected fees and charges to determine the extent to which the full cost of associated service is being recovered by revenues.*

Is your local government doing this?

(check one) Yes ☐ No ☐

If “yes,” what information is collected each year and how is cost recovery determined?

If “no,” should your government be doing it?

(check one) Yes ☐ No ☐

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

Policy Statement # 5: *The local government will review all fees and charges at least once each four years.*

Is your local government doing this?

(check one) Yes ____ No ____

If “yes,” for which fees and charges is the review carried out and with what degree of success?

If “no,” should your government be doing it?

(check one) Yes ____ No ____

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

Policy Statement # 6: The local government will place increased emphasis on user charges to finance the cost of local government services.

Is your local government doing this?

(check one) Yes ☐ No ☐

If “yes,” which user charges are used most extensively to finance the cost of local government services?

If “no,” should your government be doing it?

(check one) Yes ☐ No ☐

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

Policy Statement # 7: The local government will conduct a cost finding analysis before committing to programmes of privatizing services.

Is your local government doing this?

(check one) Yes ☐ No ☐

If “yes,” what is the nature of the cost finding analysis conducted before making a commitment to privatize a service?

If “no,” should your government be doing it?

(check one) Yes ☐ No ☐

If “yes,” what will it take to implement such a policy?

If “no,” why do you feel your local government cannot or should not engage in this practice.

1.6 EXERCISE: THE FINANCIAL POLICY MATRIX

TIME REQUIRED

105 minutes

PURPOSE

This exercise gives participants skill practice in composing financial policy statements and in developing a comprehensive financial policy framework for a local government.

PROCESS

Tell participants they will be working in small groups to either develop or revise existing financial policies for use in their own local governments. Explain that the exercise includes the use of criteria by participants to assess the policy statements they have written and a matrix designed to clarify the relationship of each policy to other financial management areas which could be affected by the policy. Because of time limitations, explain that participants will be working on policies in only one area of financial management. Encourage participants to discuss their progress with other participants in their small groups since participants in each small group will be working on policies for the same financial area.

Begin the exercise by listing the nine financial management categories shown in the box below on a sheet of newsprint or an overhead transparency. Be sure to number the categories. You may choose less than nine categories for smaller participant groups. Use your judgment on this.

1. Accounting, financial reporting, auditing
2. Annual operating budget
3. Capital investment plan/budget
4. Revenue
5. Reserve
6. Debt management
7. Cash management
8. Purchasing
9. Risk management

Since a small group should have at least five participants, a good method is to divide the particular group by five to decide how many categories to use, and then, for the exercise, pick the categories that are of most interest to a majority of the workshop participants. To assign participants to category groups, ask them to “count off.” This is done by having the first participant say “1,” having the second participant say “2,” and so forth, until one participant has been assigned to each category selected for the exercise. Then start over again with the next participant who will say “1.” Continue until all participants have a number and there are approximately the same

Sample

<p>Finance Category Operating Budget</p>	<p>1. The local government will project revenues and expenditures for the next four years and will update the projection annually.</p>	Accounting	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Financial Reporting	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Auditing	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Operating Budget	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Revenues	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Reserves	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		CIP & Budget	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
<p>Finance Category Operating Budget</p>	<p>1. The local government will project revenues and expenditures for the next four years and will update the projection annually.</p>	Debt Management	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Cash Management	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Purchasing	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Risk Management	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Fixed Asset Mgmt.	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Planning	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0
		Development Finance	Influences this area	0	Needs a policy	0	Conflicts/inconvenient	0	Needs Procedures	0

Finance Category		Influences this area				Needs a policy				Conflicts/Inconvenient			
1. _____													
2. _____													
3. _____													
4. _____													
5. _____													

number of participants in each small group. Tell participants with the same number that they will be working on the financial management area that corresponds with their number.

When participants have “counted off” and know which financial management category they will be working on, describe the two tasks (explained below) and tell participants they will have about one hour to complete them.

Task One

The first task is for participants to develop several financial policies for their own local governments that are appropriate for the financial management category to which they are assigned. Remind participants to refer to the appendix of the preceding essay for financial policy samples that are representative of proper style and wording. Encourage participants to consult frequently with one another. Suggest further that participants use three criteria to evaluate their proposed financial policies:

1. This policy is an accurate reflection of my government’s fiscal purpose or intent in this area.
2. This policy fits well into a frame-work of policies that can guide our elected officials in making the right financial decisions.
3. This policy would be a reliable guide for evaluating changes to the financial practices of my local government.

Before participants begin work on this task, copy the next page containing the three criteria as a handout and give each participant a copy.

Task Two

Before participants leave for their small groups, distribute a second handout—see subsequent pages of this chapter— containing a matrix and a set of instructions. Explain that the purpose of the matrix is to help participants identify the impact of the policies they have developed on other areas of financial management. The matrix is also useful in identifying the need for additional policies, disclosing possible conflicts or inconsistencies, or possibly the need for more detailed implementing procedures. Read the instructions aloud and ask participants enough questions to satisfy that the instructions have been understood.

After one hour, ask the small groups to come back together and ask for one or two participants from each small group to report on the policies they have developed and what they learned about policy impact from the matrix task. Encourage a general discussion of policy development and the inter-relationship of financial policies.

Three Criteria for Evaluating Financial Policies

1. The policy is an accurate reflection of my government's fiscal purpose or intent in this area.
2. The policy fits well into a framework of policies that can guide our elected officials in making the right financial decisions.
3. The policy would be a reliable guide for evaluating changes in financial practices of my local government.

Policy Matrix Worksheet

INSTRUCTIONS

The following pages are for your use to analyze the implications of the policies you developed in the first part of this exercise for fourteen areas of financial management in your local government. To begin, enter your policies in the space provided on the left side of the matrix.

For example, let's say, you have been working on policies for Annual Budgeting and that one of your policies reads as follows: ***We will project revenues and expenditures for the next four years and will update projections annually*** (see the example in the box to the right). Continuing with this example, the first question to answer is: ***Does this annual budget policy influence the area of Accounting?*** If the answer is "yes," this answer can be recorded by blackening the circle just below the label "Influences this area" under the financial area called Accounting. If the answer is "no," the circle is left blank and you can move on to the next question under Accounting, ***Do we need a policy?***

This process continues until all of the questions related to Accounting have been answered by either blackening a circle to indicate a "yes" answer or leaving it blank to indicate a "no."

After finishing the Accounting category, continue across the matrix and on to the next page. For each area, answer the same questions and record your responses as you did for Accounting. You will find that some of your policies have influence on some of the areas and not on others.

When you have finished all of the areas, go back to the first page of the worksheet and repeat the process for each of the remaining policy statements in your category.

When the matrix is completed (both pages) for each of your policy statements, note which circles are blackened under ***Needs a policy***, ***Conflicts/ inconsistencies***, and ***Needs procedures***. These responses represent possible "action" priorities for your local government.

1.7 EXERCISE: BARRIERS TO POLICY IMPLEMENTATION

TIME REQUIRED

60 minutes

PURPOSE

Participants identify barriers inside the organisation and outside that can block or impair the implementation of financial policies and what might be done to identify and remove these barriers.

PROCESS

Tell participants that they will be working individually for about 30 minutes to identify barriers to policy implementation that exist inside and outside their organisations. Explain that they are to compile two lists of barriers to policy implementation, the first list consisting of barriers within the local government organisation and the second list consisting of barriers in the local government's external environment.

When the barriers have been identified, ask participants to answer these questions about each barrier on the two lists.

1. Why is this a barrier?
2. What can be done to reduce or eliminate the barrier?

Circulate enough copies of the worksheet so that each participant has a copy and ask them to enter their answers to the previous questions on the worksheet.

At the end of 30 minutes, ask for volunteers to report some of the barriers they have identified, first inside their organisations then outside. If there are no volunteers from any of the financial management areas included in the preceding exercise, ask for participants who have been working in these areas to make reports. As participants report barriers, ask what might be done in each case to reduce or eliminate the barrier. Encourage discussion of similar and not so similar results from the various reports.

Worksheet on Identifying and Removing Barriers to Policy Implementation

Financial Management Category _____

I have identified the following barriers to financial policy implementation inside my local government.

I have identified the following barriers to financial policy implementation outside my local government.

These inside barriers to policy implementation can be reduced or eliminated by:

These outside barriers to policy implementation can be reduced or eliminated by:

1.8 CLOSING EXERCISE: LEARNING TRANSFER

TIME REQUIRED

30-45 minutes

PURPOSE

This exercise is to help participants transfer the learning experiences of the workshop into their real-world activities. The focus of this exercise is on raising expectations, engaging in realistic planning and making personal commitments. Most of the work is done on a personal basis with some interpersonal sharing.

PROCESS

Spend at least half an hour at the end of the workshop to focus the attention of participants on important concepts and encourage them to continue experimenting with these concepts in their management activities. Begin by giving participants about fifteen minutes to work independently on a simple learning transfer questionnaire.

When participants have completed the questionnaire, ask them to share quickly with the group two or three things they intend to do differently in their financial management roles to close the workshop.

Trainer's note. It is generally agreed that the purpose of training is to improve the way people do things by showing them a better way. In fact, the success of a training experience can be measured by the amount of personal growth and change that takes place both during training and after the training is over.

Commitments to learning and change made at the close of a workshop can help participants overcome learning resistance in themselves and in the work environment. A trainer can help learners make a successful transition from the world of learning to the world of doing through a few simple planning exercises.

A Learning Transfer Questionnaire

Take a few minutes to reflect on the financial policy making process, the new ideas you encountered in this workshop, and how you feel about them. Then, in the space below, write a sentence or two to describe something interesting you have learned about yourself during this workshop.

Based on what you have learned about yourself and the many possibilities for change presented by this workshop, what two or three things do you intend to do differently in the development of financial policies?

1.

2.

3.

Finally, what obstacles in yourself or in your work environment do you expect to experience during your efforts to implement these changes? What will you do to remove or minimize these obstacles?

Expected obstacle

1. _____

2. _____

3. _____

Action to remove it

1. _____

2. _____

3. _____

Financial Planning

PART ONE: CONCEPTS, PRINCIPLES, AND STRATEGIES

SUMMARY

This essay will examine ways that financial planning can be developed and implemented in local governments (LGs). The focus of the chapter is primarily on one aspect of financial planning—medium-term financial forecasting of revenues and expenditures. We will provide a definition of forecasting and relate it to good governance, citizens, performance measures, and financial policies. We will also describe the benefits that accrue to LG when implementing a financial forecasting process, considerations for organizing the process, types, and methods of forecasts. Included in the discussion will be obstacles, limitations, and risks inherent in developing a financial forecasting process.

RELATIONSHIPS BETWEEN CHAPTERS IN THE SERIES

The following matrix shows the interrelationships between Financial Planning and other chapters in the series.

	Financial Planning
<i>Introduction</i>	The Introduction provides the framework for using the entire series.
<i>Trainer’s Guide</i>	Provides guidelines for using the chapters to provide training.
<i>Financial Policy Making</i>	Financial policy making provides the framework for the opportunities for financial planning.
<i>Citizen Participation</i>	Financial planning is the long-term plan for where the community is going. Citizen participation in deciding the direction is essential.
<i>Evaluating Financial Condition</i>	Financial planning helps ensure that the LG’s financial condition does not worsen over time.
<i>Operating Budget</i>	The operating budget is one of the primary methods of implementing financial planning.

<i>Financing the Operating Budget</i>	The operating budget is one of the primary methods of implementing financial planning.
<i>Capital Investment Planning (CIP)</i>	The capital investment plan is one of the primary methods of implementing financial planning.
<i>Financing the Capital Investment Plan</i>	The capital investment plan is one of the primary methods of implementing financial planning.
<i>Accounting</i>	Accounting and reporting provide a method for holding LG officials and policy makers accountable for implementing financial planning.
<i>Performance Measures</i>	Performance measures help the LG ensure that its financial planning process is effective and efficient and accomplishing the priorities and goals of the LG.
<i>Asset Management</i>	The largest investment a LG makes is in its assets. These include streets, clinics, water systems, fire trucks, etc. Financial planning is the roadmap for procuring or building assets.
<i>Procurement</i>	Procurement is one of the primary ways of acquiring the assets, materials and supplies to implement the financial plan.

INTRODUCTION

We recognize that basic or introductory concepts are relative—depending upon your background and frame of reference for both financial planning and local government. Users of this material will range from those who have no knowledge of financial planning principles or concepts to those who have a very sophisticated understanding. The following are our ideas of what represents the most fundamental principles and concepts needed to understand financial planning at a beginning level.

BASIC CONCEPTS AND DEFINITIONS

DEFINITIONS

Financial planning is a process in which coordinated comprehensive strategies are developed and implemented to achieve a LG's financial goals and policies. These strategies are developed in response to projections of a picture of the future over various timeframes. LGs assess the probability of those future projections coming true and prepare a response (a financial plan) to mitigate adverse financial consequences. This type of traditional financial planning focuses on an “inside out” perspective—looking at the current LG situation and forecasting it into the future.

Financial forecasting is a process for a LG to produce projections of future years' revenues and expenditures based upon a set of specific policy and economic assumptions. Forecasts are the financial management tools that can project the future financial impact of current program policies, economic trends, and assumptions. When applied beyond the annual budget, forecasts link the annual budget to other

longer term LG planning and development efforts. Multi-year financial forecasts of revenues and expenditures tie the annual budget together with capital programming, debt planning, labour contracts, strategic plans, and economic and community development planning.

WHAT ARE THE FINANCIAL PLANNING TOOLS AND TECHNIQUES USED BY LGS?

To pose this question to LG officials would yield different answers depending upon the experience of the person answering the question. To some, this may be the latest financial planning technique. However, LGs occasionally are caught up and overlook the basics of:

- Strategic planning
- Budgeting
- Financial forecasting, and
- Economic development strategies.

Properly applied, these basic strategies can assure financial health of the community for the future.

Financial planning means different things to different people. The reason for this is that there are a number of different types of financial planning tools and techniques available. The more common planning tools and techniques include: budgeting, financial forecasting, capital programming, debt planning, trend monitoring, strategic planning, and economic development planning. A brief description of these follows:

Budgeting is by far the most commonly used tool in the financial planning toolbox. Budgeting is the public policy process of allocating scarce resources to achieve a desired result. An annual budget allocates revenues to provide services and maintain facilities.

Financial forecasting is a process that produces projections of future years' revenues and expenditures based on a set of specific policy and economic assumptions.

Capital investment planning is a process that produces a multi-year capital investment plan (CIP) for short- and long-term physical development of a community. The capital investment plan (CIP) can be thought of as a link between the community's master plan for physical development and fiscal plans funded in the annual budget.

Debt planning is a process that determines the type and optimum amount of debt (i.e., loans, bonds) needed to finance a community's short- and long-term capital investment program. Debt planning links the capital investment program with the annual operating budget in which debt service is funded.

Trend monitoring uses numerous economic and financial indicators to monitor the financial condition of a community and LG. LGs regularly monitor and track these indicators over time to identify key trends that are under way. Many of the in-

dicators are used by financial institutions, underwriters and rating agencies as tools in credit analysis to evaluate a LG’s financial condition.

Strategic planning is a systematic process by which a community anticipates and plans for its future. The result is a written document called a strategic plan that guides the community toward its vision of the future. To achieve it, a financing plan must be developed to support it.

Economic development planning is a process that utilizes LG policy and incentives to stimulate growth and economic activity in a community. Tools such as fiscal impact analysis and scenario analysis are used to assess the impact of various economic development strategies on a LG’s future revenues and operating expenses.

As you can see, financial planning has many and varied tools and techniques to meet different needs. However, this chapter focuses primarily upon financial forecasting as one of the basic tools of financial planning. Budgeting, capital programming, debt planning, and evaluating financial condition are addressed and discussed in detail in other chapters in this series.

The European Union countries usually consider financial planning as a important element of strategic planning and economic development planning. For example, in Latvia the overall “master” planning process is called “Spatial Planning and Strategic Development Programming.”

LEARNING APPLICATION

POLICY MAKER_X_ CEO_X_ FINANCE MANAGER_X_ DEPARTMENT HEAD_X_

In the first Learning Application in each of the chapters in this series we will be reminding the reader about how to get the most from each of these reflective exercises. First, there will be a box identifying the four key LG roles that most readers represent. These are Policy Makers (elected officials), CEOs (Chief Executive Officers such as mayors, city managers, etc.), Finance Managers (the chief finance official in the LG), and Department Heads (those individuals who are responsible for the management of specific LG departments such as public works, planning, and human resources). Second, we will indicate in the box those readers we believe will benefit most from completing the learning application task. Finally, when more than one official is listed, we see this as an opportunity for these individuals to get together and compare their responses. These Learning Application opportunities can also be modified to become training exercises for group learning. Therefore, our advice is to make the most of these reflective interludes in the text.

When I think of financial planning and forecasting in my LG, the following things come to mind:

1. _____

2.

3.

LINKAGES TO OTHER PLANNING EFFORTS

Financial forecasting does not exist in a vacuum. If it is not related to and integrated with other planning efforts, it will be useless as a tool for the governing body and management. Financial forecasting should be linked to the annual budget, capital programming, debt planning, trend monitoring, and long-range strategic planning efforts.

BUDGETING

Financial forecasting is a part of the unified process of budgeting. Budgeting links together policy development, financial planning, service/operations planning, and communication. In the annual budget, the financial forecasting process includes:

- A projection of the current year's revenues and expenditures to the end of the fiscal year on which the next year's budget is based.
- An estimate of the next year's proposed revenues which should include a listing of all current and proposed revenue sources, prior years' actual revenue collections experience, and the underlying assumptions on which the revenue estimate is based.
- An estimate of next year's proposed expenditures by central government accounting classification, department, program or other activity.
- A listing of prior years' actual expenditures.
- And an explanation of the events or conditions that require changes in operations to comply with changes in law to initiate new levels of service or to adjust operations to ensure financial stability or solvency.

CAPITAL INVESTMENT PLANNING

Financial forecasting should be linked to the capital investment program (CIP). LGs in developing countries generally finance capital investments with own source revenues or with central government subsidies dedicated for a specific purpose. In many cases, LGs fund capital investments with money left over after the mandated or obligatory tasks are funded in the annual budget. Making funding decisions this way usually deprives capital investments of much needed capital and leads to infrastructure decline.

LGs should develop a multi-year capital investment plan for investments and establish project priorities for funding subsequent years. Establishing a policy to set aside a certain percentage of annual revenue for investment funding is one way to provide minimum funding year-to-year. Operating budget planning can then rely on these plans for each subsequent investment increment, and the forecast can reasonably rely upon the investment plan for future years' forecasts with more certainty than without the plan. A LG should not neglect its capital plant and infrastructure, even in difficult economic times.

Another aspect of capital programming is identifying the future operating costs of newly constructed facilities. This information, containing dates and estimated operating expenses, should be included in the capital investment plan to show the relationship of completion of construction and the opening and start-up operation of a new facility. In the year in which the facility is scheduled to open, the initial operating expenses (wages, supplies, services and replacement equipment) must be funded in the operating budget for that portion of the year in which the facility is operational. Until this is done, the facility should not be opened. Operating impact for the first full year should be included in subsequent forecasts as high priority funding requirement.

DEBT PLANNING

Debt planning comes into play when investments are financed with either bank loans or LG bonds. You will need to determine your country's laws on allowing LG debt. Usually, there are two components of debt planning: existing debt service (principal and interest payments) based on credit financing that has been incurred and is being paid off over a specified maturity period; and future debt service. Future debt service is the amount of principal and interest that may be incurred based on the execution of the capital investment plan using bonds or bank loans to provide the necessary future financing. The most important assumption, in addition to the size, date of issuance, maturity date and structure of the debt, is the overall interest rate that will be incurred for the new debt. Interest rate assumptions on debt must consider national economic conditions, availability of capital, maturity date, and structure of the debt and creditworthiness of the LG.

TREND MONITORING

Another important activity to link to forecasting is a trend monitoring system. Trend monitoring is a LG's effort to monitor key economic and fiscal statistics and track

them over a period of time to identify important trends. Various statistics are used and could include:

TAX BASE

- Value of real estate per capita
- Number and value of building permits
- Population
- Income tax collections per capita
- Bank deposits
- Collections from largest taxpayers as a percent of total taxes

DEBT STRUCTURE

- Debt per capita
- Debt as a percent of LG assets
- Debt service as a percent of total revenues or total annual budget

OPERATIONS

- Total revenues and largest revenue sources
- Property tax collection rates
- Expenditures per capital
- Cash balances/liquidity

An annual analysis of favourable and unfavourable trends can provide an important early warning system for LGs. Policy makers should be aware of improvements made as well as apparent deterioration in the trends. Encouraging council adoption of an action plan to identify, monitor and correct adverse trends is perhaps the most important strategic function that management can provide. Incorporating such an action plan into the multi-year forecast and reporting on its future achievement or non-achievement is an excellent way of linking these two planning efforts.

STRATEGIC PLANNING

LGs in many countries are beginning to create strategic plans. As the plans takes on additional importance, there will be a need to link forecasting to it. Strategic planning is a technique that is based on organizational analysis, environmental analysis, and an attempt to identify internal and external factors that will shape an organization's future. Once certain future conditions are identified, planners develop a vision statement, mission, goals, objectives, and strategies to influence and change the organization 5 to 10 years in the future. Once adopted, the strategic plan can serve as a blueprint for changes to operations and the need for a different mix or use of resources to achieve LG goals.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

We have identified some but not all linkages to financial forecasting. What other linkages to financial forecasting are important in your LG? Why are these linkages important?

WHAT IS THE PURPOSE OF FINANCIAL FORECASTING?

A financial forecast serves two basic purposes.

- It quantifies the future impact of current decisions, programs and policies (impact analysis), and
- It identifies and provides information for analyzing the revenue and expenditure adjustment options needed to close the difference between revenues and expenditures (gap analysis.)

In both situations, the forecast relies on specific policy and economic assumptions. The difference is: when used for impact analysis purposes, the focus is on policy assumptions. When used for gap analysis, it focuses upon economic assumptions. For example, a revenue and expenditure forecast projects the future cost of debt service (principal and interest) of a five-year bank loan used to finance local development and investments (impact analysis). It might also be used to project the amount of additional revenues needed if central government shared revenue is adjusted annually based on inflation averaging 15% over the next five years (gap analysis). Used this way, revenue and expenditure forecasts can improve planning, budgeting, and LG decision making.

Throughout this chapter, the terms “forecasting,” “financial forecasting” and “revenue and expenditure forecasts” are used interchangeably. They refer to the preparation of all formal forecasts of revenues and expenditures from short- to long-term regardless of the number of years. Multi-year forecasts will refer more specifically to forecasts covering one to ten or more years, but usually medium-term forecasts ranging from one to five years.

The financial forecasting process is determined by local elected and appointed officials to meet the unique needs, objectives, and constraints of the LG. As a result, there are many possible approaches and no clear-cut solutions. Nevertheless, some generalizations can be made about the process and products expected from multi-year financial forecasts:

- Unlike the annual budget, which is generally balanced with revenues equaling expenditures, forecasts tend to be unbalanced, with expenditures exceeding revenues. The reason for this is the methodology of forecasting which is based on current policies and programs and economic assumptions. These policies and assumptions affect revenues and expenditures differently because they grow at different rates, causing a balanced budget to be unbalanced in the future.
- Expenditure forecasts are primarily extensions of current service programs or planned and approved investment programs that are controlled by the LG. Revenue forecasts, on the other hand, are based partly on economic assumptions that are beyond the LG's control, and partly on policy assumptions regarding the level of taxes and fees that are within the LG's control.
- If the actual conditions differ from the assumptions in the forecast, then the actual revenues and expenditures will differ from the projections. Differences between actual and projected revenues can usually be traced to:
 - Financial control problems for locally generated revenues (such as fees and charges, since they are usually within the LG's control);
 - Unforeseen economic conditions that might affect income tax collections;
 - First time changes in central government allocated transfers to LGs that don't have a historical record of accomplishment.

Differences between actual and projected expenditures can usually be explained by changes in LG policies and programs made to balance the budget, meet citizen requests, or deal with unanticipated national mandates or natural disasters.

GOOD GOVERNANCE, CITIZENS AND FINANCIAL FORECASTING

One of the basic concepts of good governance is "transparency" or the ability to see through and inside the policy making processes. Forecasting revenues and expenditures is a good example of the importance of citizens and other interested organizations being able to "see through" the process. For example, most countries require that a LG budget be balanced (projected revenues must equal or be greater than projected expenditures.) But at times, the LG staff overestimates revenues so that more expenditures (services to citizens) can be included in the budget. This can happen because staff or the chief executive officer choose to do it, or they are being pressured by the policy makers. When the adopted budget is announced to the public it appears that a certain number or level of services will be provided in the forthcoming year. But over the year, as revenues do not meet the projections, services will need to be cut back or deleted so that the total revenues received are not exceeded. These reductions in service levels are not usually announced to the public.

It is important for citizens to understand the importance of annual budget forecasts. Normally, when a single staff agency or a multi-department forecasting team prepares the forecast, the citizens' role is to comment on the resultant forecast in public sessions, usually conducted during the annual budget review. However, if a

higher level of citizen participation is desired, you can use citizens and businesses in situations where their input can be successfully utilized. This helps avoid governance by token participation. One way to accomplish this is to include citizens on the forecasting team. These citizens should provide skill sets that are not available from LG staff such as a statistician or computer specialist. Another way is to invite finance, economics, and business specialists from local universities, businesses, and government to participate in round-table discussions concerning the local, regional, and national economic trends. This information can be very helpful in acquainting elected officials with economic issues and their relationships with LG financial trends.

Rule for good forecasting: Estimate revenues conservatively (low) and expenditures liberally (high).

TYPES OF FINANCIAL FORECASTS

Financial forecasting has been previously defined as the process that produces a projection of future years' revenues and expenditures based on a set of policy and economic assumptions. When we talk about types of financial forecasts used in LG, the most frequently used classification is based on length—short-term (up to one year), medium-term (1-5 years) and long-term (10+ years.) For annual budgeting, short and medium-term forecasting is more useful and relevant than long-term, and will be the focus of this chapter. Long-term planning is used most often in economic development planning and strategic planning.

Length of Forecasts			
	Short-term	Medium-term	Long-term
Number of years	0-1 year	1-5 years	10+ years
Uses	<ul style="list-style-type: none">• Operating budget• Cash management• Monitor budget implementation	<ul style="list-style-type: none">• Budgeting• Policy analysis• Fiscal impact of legislation• Identify financial trends• Capital investment programming	<ul style="list-style-type: none">• Strategic planning• Physical and economic development planning• Fiscal impact analysis

SHORT-TERM (0-1 YEAR)

Short-term forecasts cover a period up to one year. The primary uses of short-term forecasts are related to the development of the operating budget and cash management.

Short-term forecasting helps management prepare a budget for next year based on reasonable assumptions. It also eliminates surprises by identifying variances from expected performance early in the fiscal year, which, if properly used, provides

time for management action rather than waiting for a crisis to happen. Finally, it provides a tool to monitor the budget and assure compliance with the legal appropriations. When problems are identified, corrective actions can be initiated, eliminating the problems.

OPERATING BUDGET

In developing the operating budget, annual forecasts of revenues and expenditures are needed for next year's budget. These forecasts may occur at different times. For example, some LGs prepare preliminary estimates of next year's revenues and expenditures as one of the first steps in the budget calendar, six to nine months before the start of the fiscal year. These early estimates are used by the CEO, governing body, and management to aid in setting priorities and budget guidelines. The estimates are continually updated, refined, and ultimately adopted and included as part of the annual budget.

CASH MANAGEMENT

A second example of the use of short-term forecasts is in cash management. LGs should forecast monthly cash inflows and outflows as a part of preparing the annual budget for two reasons:

- To project interest earnings on invested bank account balances (assuming that your country allows for the investment of cash in order to earn interest), and
- To identify any cash shortfalls and the possible need for interim financing (assuming that your country allows for LG financing) during the year.

MONITOR BUDGET IMPLEMENTATION

Another example of the use of short-term forecasting is to monitor budget implementation. It is prudent to monitor the budget after adoption to forecast the actual performance of revenues and expenditures compared to budget. If significant variations from budget are forecast based upon actual operating results, swift management actions may be needed to bring the budget back into balance.

MEDIUM-TERM (1-5 YEARS)

Medium-term forecasts cover the period of one to five years into the future. The principal uses are for budgeting, policy analysis, legislation, and capital programming.

BUDGETING

For example, in budgeting, medium-term forecasting is used to project gaps between anticipated revenues and expenditures during the next one to five years. This prompts policy discussion, and hopefully, decisions to close these gaps. If decisions are implemented, the actual revenues and expenditures will not be the same and the

forecast gap will not be the same. The altered level will be the result of actions taken in response to the forecast.

POLICY ANALYSIS

Forecasting is also used to aid policy analysis. For example, wage negotiations often have implications beyond the current year. Identifying alternative scenarios and the future years' impact from these negotiations is critical information for policy decision making today.

Any decisions regarding funding capital investments may have multiple impacts. They can:

- Reduce the availability of funds for operating expenditures in the current year.
- Potentially increase operating costs when the facilities are completed in future years.
- Have multi-year implications both in paying debt service and in operating the facilities when they are complete.

All capital investment decisions should be made understanding what the future cost is and how it will be funded. These situations need to be considered with the future impact identified at the time the policy decisions are made. Once the decision is made, the forecast can reflect it as a future year's committed cost.

FISCAL IMPACT OF LEGISLATION

Medium-term forecasts are useful in determining the fiscal impact of legislation, especially tax or revenue legislation. For example, changes in the allocation formula for central government shared revenues will have multi-year impact. Forecasting the impact of this change, and presenting this information to the governing body, is one way to forestall or reduce the adverse impacts upon the LG.

IDENTIFY FINANCIAL TRENDS

Medium-term financial forecasts help management and policy makers identify financial trends that will require management/council action to avoid potentially disastrous financial results. Being prepared eliminates surprises and reduces management by crisis. Forecasts also promote more efficient operations of LGs.

CAPITAL INVESTMENT PROGRAMMING

Medium-term financial forecasts are also useful in capital programming. Capital investments normally have a life greater than a year. As a result, expenditures related to such investments may continue for several years.

There are two types of expenditures: construction expenditures and debt service charges, i.e. bank loan repayments. Because current revenues are limited, a current revenue financing approach that does not borrow monies for capital investments but only uses revenues currently available to the LG tends to stretch out the completion

of a project over a number of years. To understand more about different approaches for capital investment financing, refer to the Financing Capital Plan chapter.

Another multi-year expenditure related to capital programming is debt service. LGs incur these expenditures when they borrow money from banks or other lending institutions to construct a capital investment. The principal amount is repaid with interest over the term of the loan. Annual debt service charges represent fixed costs of the LG once the transaction (borrowing) is completed, and must be funded in the annual budget. Medium-term financial forecasts identify these projected construction and debt service costs by year, so that each year's increment can be anticipated and funded in the annual budget when needed.

The last use of medium-term forecasts in capital programming relates to the operating and maintenance costs associated with opening a capital facility such as a new fire station. Operating and maintenance costs include staff to operate the facility and supplies, services and equipment to maintain it. These costs are normally funded in the operating budget when the facility opens. Including this item in a medium-term forecast alerts the LG of the need for an increase in the annual operating budget.

LONG-TERM (10+ YEARS)

Long-term forecasting is most widely used in strategic planning, physical and economic development planning, capital programming, and debt planning. Long-term financial planning is unique and should be studied by serious advocates of financial planning.

In summary, a long-term financial plan covers a period of ten or more consecutive years. It should set out in detail:

- The expenses,
- Sources of funds,
- Cash flow projections,
- Estimated asset creation,
- Estimated changes in levels of equities and borrowing, and
- Estimates of contingencies.

The plan should outline the reasons the LG is engaged in particular activities, identify all significant forecasting assumptions, and estimate the short-term effects of assumptions that involve a high-level of uncertainty.

The plan should also adhere to basic financial management principles, i.e. adequate and effective provision of the long-term expenditure needs of the LG, as well as annual benefits and costs of different options in determining the plan. Once adopted, the governing body should issue a report in subsequent years in an annual plan of any significant changes between what is contained in the long-term plan and the council's funding policy, investment policy and borrowing policy. The council should explain how any material inconsistencies would be addressed in future years.

Strategic planning is both a process and a product. As a process, it uses organization and environmental analysis in an attempt to identify internal and external strengths, weaknesses, opportunities, and threats that will shape an organization's future direction. This information is then used to formulate strategic alternatives over the next ten to twenty years. A strategic planning exercise typically creates layers of goals, objectives, and strategies that provide a target path for the operations of an organization. In a LG, strategic planning typically involves the governing body in a systemic process that seeks to establish a new direction for the organization and thus overcome the traditional incremental decision making. The product is a plan that establishes the organization's future strategic direction. That direction must ultimately be reflected in the annual budget. While the budget has always been a choice between different revenue sources and program expenditures, in the future the budget must reflect strategic choices. Budgets can be used to implement specific components of the strategic plan, such as initiatives to stimulate economic development. On the other hand, the lack of a strategic financing plan may, by default, constrain development, local planning, and investments.

PHYSICAL AND ECONOMIC DEVELOPMENT PLANNING

Long-term forecasting can also be used for physical and economic development planning for a community. To forecast a community's economic development potential ten to twenty years into the future, forecasters initially must determine the past and current state of the local economy. This would include documenting: population characteristics, such as size, age mix, ethnicity, and education level), income structure, and employment mix. Together, these reveal the capacity of local residents to pay taxes and other income sources covering public expenditures. Historic trends document past financial problems and provide forecasters an indication of whether there may be financial problems ahead.

FISCAL IMPACT ANALYSIS

Another tool, used to project long-range changes in population, income, and land use on the local economy, is a fiscal impact model. The model assumes that changes in: the size and composition of the population; income levels and distribution, or land use patterns, will affect both revenues and expenditures of the LG. Fiscal impact analysis attempts to determine the magnitude of such impacts by modelling various scenarios using current policies and potential policy changes to determine what impact these might have in the future. For example, a large tract of vacant land may be ripe for development, but what type of development should the LG plan for: public housing, private residential, or commercial? Each alternative and related land use will create different impacts upon the LG in revenue generation and expenditures.

Fiscal impact modelling helps clarify the impact of different policy scenarios so that LG decision makers can gauge and assess the long-term consequences for both the LG and the community. Related to the economic development impact is the impact that such a development has on LG's capacity to serve it. If a fiscal impact

model can estimate the effect of population shifts, income groups, and land use on LG revenues and expenditures, then the budgetary effects can also be projected under different scenarios. This can aid LG budget planning as well as long-range debt planning since the timing and the size of future LG investments in infrastructure can be determined and financing arranged to meet future requirements.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

Consider your LG's financial forecasting efforts over the last 1 to 5 years. Identify specific examples of short-term, medium-term and long-term financial forecasts currently used in your LG.

List other ways your LG could use and apply financial forecasts that you are currently not doing.

With whom should you discuss these forecasting needs and what are the major points you would want to stress in these discussions?

RESOURCES FOR PRODUCING FORECASTS

There are four primary resources required to produce forecasts:

- Staff with required skills,
- Development time (based on quality and availability of data),
- Data and information needs, and
- Computer equipment.

The requirement for each depends upon the intended uses of the forecast, quality of the data and the qualifications of the forecasting team. The ideal team to support the forecasting effort should include a top policy maker, the finance director, analysts who are knowledgeable in economics, statistics and data processing, and a senior financial person to lead the project. A policy maker is included on the team to ensure that users' needs are incorporated into the resulting forecast process. The finance director's role is to bring knowledge of the local financial management practices, accounting and budgeting to the process. The finance officer should also coordinate the involvement of other senior officials to determine their needs and to locate the data needed to support the forecasting processes. The project team leader is usually a senior finance officer or budget officer and is given the following responsibilities:

- Building a coalition of key people concerned with the forecast, and handling the liaison with other departments.
- Insuring that administrative and technical aspects can be executed in a timely fashion.
- Recommending key decisions to top management, such as the economic and policy assumptions to be built into the forecast.
- Guiding overall development and operation of the forecasting system.
- Presenting the resulting forecasts to the CEO, governing body and/or its committees, and others as appropriate.

FORECAST TEAM

Skills of the forecast team are very important. An understanding of economics is necessary to ensure that the revenue and expenditure forecasting assumptions reflect the influences of national, regional, and local economies. If the LG employs an economist, then that person should be included on the team. An alternative is to contract with a local university or consulting firm to provide this expertise on the team, or at least to review the economic assumptions.

Other organizations such as the national government (Ministry of Finance and others), banks, financial institutions and business organizations are often involved in economic forecasting. They may have resources on which the LG might draw. Statistical skills are important. The preferred forecasting methodologies for income tax and other economic sensitive revenues involve the use of statistical techniques such

as multiple regression analysis. These techniques can also be used for forecasting fees and user charges.

DEVELOPMENT TIME

Development time is the amount of time it takes to prepare the forecast. Preparing an initial forecast requires more time than subsequent updates. The level of detail increases the time required to produce a forecast. A considerable amount of that time is devoted to gathering historical revenue and expenditure data and testing forecast methodologies. Unless your staff is experienced in preparing forecasts, they will be learning-on-the-job and this will increase the development time. Once the initial year's data and information is gathered, subsequent years require only updating. As a result, the time for preparing the forecast is reduced. Automated budgeting and financial accounting systems can also reduce the data gathering time. Smaller LGs might consider building on the experience of other LGs and even using their computer spreadsheets if they agree.

DATA AND INFORMATION REQUIREMENTS

Historical data is required for the forecasting process and most forecasting methodologies use a historical experience base to arrive at a new forecast. Actual revenue and expenditure data for the last five years is usually a minimum requirement. For some forecasting methodologies, a series of ten to fifteen years of observations is best, i.e., regression analysis. If your LG lacks this historical data, the only practical solution is to use what you have. In this case, you need to recognize that this may place limitations on the forecasting methodology. Build your database by adding subsequent years' data and over time you will reach the necessary levels.

Characteristics of Successful Financial Forecasts include:

A good forecaster, someone who:

- understands the situation the forecast is being prepared for,
- knows what is required for successful decision making in that area,
- ensures the forecast is meaningful and useful,
- is interested in real improvements in decision making,
- understands the forecasting technique and its value—knows strengths and weaknesses,
- understands the environment in which forecast occurs,
- communicates successful forecasts to others, and
- trains other managers on various techniques and general procedures for adapting forecasts to their own situations.

Local governments that:

- notice and reward success
- provide support from top management
- give the forecaster access to resources required to utilize forecasting

- provide specialists in formal forecasting techniques
- provide computer support
- provide opportunity for reducing uncertainty which improves the value of decision making

COMPUTER SKILLS

Data processing skills are needed because most statistical techniques require the use of computers. Automation of the forecasting increases the efficiency of the team who prepare the forecast. Programming skills are not necessary since electronic spreadsheet software packages are available.

Using these tools, the forecaster can do “what if” scenarios and quickly break out the expenditures by different cost or program categories by changing a few assumptions or selecting a different variable. Personnel with these skills can be found at local universities or private consulting or accounting firms, if not available on the LG’s staff.

Multi-year revenue and expenditure forecasts can be prepared without computers—it just takes longer. On the other hand, computers are necessary if the LG desires to perform detailed revenue and expenditure forecasts or test different “what if” scenarios such as using varying inflation rates or other economic assumptions to test different program policy options.

FORECASTING ROLES AND RESPONSIBILITIES

Multi-year forecasting is a cooperative effort among elected and appointed LG officials. There are three categories of people who should play a key role in preparing or reviewing a multi-year forecast of revenues and expenditures.

LEGISLATIVE

The legislative category includes the governing body and appropriate committees. Council representatives should concern themselves with approving the overall financial and program policies of the LG on which forecasts are based. Their role in the forecasting process depends upon whether or not it was their initiative. If the impetus for financial forecasting came from the council, then the elected officials may feel that they deserve an active role in the design of the forecasting system. However, this may be carried out through a committee of the council. If the impetus for the forecasting process came from the CEO, then the council’s role may be more properly limited to providing policy guidance to the CEO and the forecasting team. Regardless of whose idea it is, the governing body should review any resulting forecasts.

EXECUTIVE

The executive category includes the CEO. The CEO’s role is to develop and recommend financial policies to the council for consideration and to execute their policy decisions. The CEO translates policy guidance from the council into specific direction

that can be applied to the forecast. In the forecasting process, the CEO should review the forecast, ensure that the forecast adheres to the policy guidance, make changes, as needed, and present the recommended forecast to the governing body.

FINANCE AND MANAGEMENT STAFF

This category includes the finance director and staff, the forecast team, and department directors. The finance director is usually the person assigned the responsibility to prepare the forecast. The finance director has the knowledge of finance, budgeting, and accounting, as well as access to the information needed to support the planning process. The finance director also has an established relationship with the CEO and the LG Finance/ Economic Committee through the budgeting process that uses the forecasting process. The finance department staff generally has the knowledge of the administrative and financial management practices, accounting, and budgeting processes to support forecasting. They may also have the computer and statistical skills needed to analyze the data and perform the analysis required in forecasting.

A forecasting team is organized by the finance director to carry out the forecasting assignment. The finance director either forms an ad hoc team or creates a permanent unit in the finance organization. The forecasting team can be made up of finance and budget personnel, or persons with more diverse skills from throughout the organization and even include consultants or citizens with specialized skills. The source of the personnel comprising the team is less important than the skills on the team.

Department directors may or may not be involved in the forecasting process. This depends upon the approach taken to prepare the forecast. For example, in a centralized approach where much of the forecast is done by a single agency, such as the finance department, the department directors are generally not involved. In a decentralized approach, department directors may be asked to provide forecasts for the department programs based on current service levels or future commitments, and may even serve on the forecasting team. Additionally, if revenue collection were decentralized, then the finance department would request the collecting agency to forecast the revenue collections based on its experience.

Of these key persons, two are essential to the success of the forecasting project—the strong and continuing support of the CEO, the governing body, and the managerial and organizational support of the finance director. Without such a unified commitment during the development period, the forecasting project may be viewed as meaningless by department directors and middle management. This, in turn, undermines the use of the forecasts. Without the finance director's support, the project will lack the commitment of staff and resources to make the project successful.

CONTRIBUTORY ORGANIZATIONS AND UTILITY DISTRICTS

Many local governments have contributory organizations and utility districts that affect their annual budgets.

A contributory organization is a semi-autonomous legal governmental entity created by the LG. A foundation agreement adopted by the LG defines, in general terms, the core activities to be performed by the organization. Examples include

ports, markets, commercial enterprises such as hotels and restaurants, tollways, communications, housing, etc. The number of contributory organizations and scope of their duties varies among LGs and countries. Because these organizations may receive contributions from the LG and/or contribute to the LG, contributory organization staff should be included in the forecasting process. Their business activities and future financial condition may have an impact on the LG and should be included in the forecast. Additionally, they may consider developing similar forecasting processes to complement the governmental forecasting process with agreed-upon assumptions.

A utility district is a central/province government operated enterprise that serves a geographic area with a public service, such as water and sewer or electricity. A utility district is created by central/province government and responsible to the central/province government for its actions. Utility districts are generally not included in the forecasting process because they do not receive contributions from the LG or contribute a portion of the profits to the LG. However, the LG should establish contact with these organizations to be alert to any future changes. This includes changes in the level of service, rate schedules or addition of new facilities that might affect LG operations and service costs.

PERFORMANCE MEASURES AND THE FINANCIAL FORECASTING PROCESS

Performance measures provide a basis for making decisions that reflect citizens' priorities and deliver on the public's desire to get value for their money. Financial planning and forecasting projects the cost of achieving those priorities into the future and allows policy makers to evaluate various alternatives for achieving those priorities. For policy makers, the integration of financial planning/forecasting and performance information makes it possible to make better business decisions—to invest resources where taxpayers receive the highest return on their investment. Without good planning and performance information, decision-makers are, in effect, guess-makers.

FOUR METHODS OF FORECASTING

The proper approach to forecasting depends upon the period considered. Short-term forecasts generally do not require a sophisticated approach. Long-term forecasts, such as developing a community economic development plan, require a much more sophisticated model because of the uncertainty involved. While both short- and long-term are of interest, the focus in this section is on the medium-term forecast (one to five years.)

Medium-term forecasts have the most utility with management and policy makers because they are:

- An extension of current policy,
- More certain and therefore credible, and
- Occur within the term of the current LG elected officials.

Forecasts do not always have to be accurate to be effective. In fact, in forecasting, accuracy is less important than the process. The process itself may turn out to improve the effectiveness of the LG operations. For example, if a LG forecasts a revenue shortfall in two years, the magnitude of the shortfall is less important than the fact that there will be one. If the LG acts to address the future shortfall now, then the forecast process has influenced policy makers to act earlier than they would have otherwise, thereby improving the LG's future years financial condition.

In general, there is a trade-off between the cost of collecting data for the forecast and the amount and accuracy of information in the methodology. The simpler methods cost less, require less experienced forecasters, and involve less time to produce a forecast. The more complex methods involve a greater number of variables, are more amenable to systemic analysis, and provide more useful information for analyzing policy choices.

This section identifies four methods of forecasting revenues and expenditures for medium-term forecasts. These methods vary from the simple to the complex, from the inexpensive to expensive—and from those that require few skills to those that required highly skilled personnel. The choice of method depends upon the types of revenues and expenditures being forecast, the needs of the user, the capabilities and the skills of the forecaster, and the time allotted.

Summary of Advantages and Disadvantages of Four Forecasting Methods

Method	Advantages	Disadvantages
Expert or Best Judgment	<ul style="list-style-type: none"> • Produces reasonably accurate forecasts. • Relatively low costs. 	<ul style="list-style-type: none"> • Lack of an explicitly stated technique makes it difficult to determine what was right or wrong when analyzing the forecast methodology.
		<ul style="list-style-type: none"> • Dependence upon a single individual may hamper LG's effectiveness if that person leaves the organization.
		<ul style="list-style-type: none"> • Likely to prove weak when the forecast is extended beyond one year, because of the greater number of factors that must be taken into account.
Trend	<ul style="list-style-type: none"> • Simple technique to use. 	<ul style="list-style-type: none"> • Does not predict a turning point in a variable (i.e., it will continue to project increases [decreases] in the variable regardless of what the economy does because it is historically based.)
	<ul style="list-style-type: none"> • Fairly accurate predictor of the next one or two future years. 	<ul style="list-style-type: none"> • Not useful in policy analysis (i.e., to anticipate economic or demographic changes in the community.)

	<ul style="list-style-type: none"> • Reliable tool for revenues and expenditures not sensitive to economic conditions. 	
	<ul style="list-style-type: none"> • Inexpensive. 	
Deterministic	<ul style="list-style-type: none"> • Simple to use. 	<ul style="list-style-type: none"> • Relies on fixed relationships between inputs and activities.
	<ul style="list-style-type: none"> • Accurate for revenue and expenditure short and medium forecasts for variables not subject to changes in economic conditions. 	<ul style="list-style-type: none"> • Uses averages as a major variable in the forecast, making it less responsive to changes in the economy.
	<ul style="list-style-type: none"> • Useful for economically determined variables over long periods of time because changes in business cycles tend to cancel out and averages become more dependable. 	<ul style="list-style-type: none"> • Depends on assumptions usually based on experience.
	<ul style="list-style-type: none"> • Accurate and suitable for forecasting growing areas. 	<ul style="list-style-type: none"> • Less likely to accurately forecast revenues and expenditures in areas of decline using the deterministic method
	<ul style="list-style-type: none"> • Inexpensive. 	
Econometric	<ul style="list-style-type: none"> • Only methodology that lends itself to projecting revenues or expenditures based on changes in the economy. 	<ul style="list-style-type: none"> • More costly.
	<ul style="list-style-type: none"> • More accurate than other techniques because, unlike the best judgment method, it is based on behavioural relationships that can be measured and evaluated. 	<ul style="list-style-type: none"> • Requires a person
	<ul style="list-style-type: none"> • It (regression technique) is not limited to forecasting in one direction like trend line techniques. 	<ul style="list-style-type: none"> • Trained in economics and statistics to develop the forecasting equations.
	<ul style="list-style-type: none"> • Tests whether a relationship between variables is, in fact, statistically significant. 	<ul style="list-style-type: none"> • Requires considerably more time for data collection and input for regression analysis.
	<ul style="list-style-type: none"> • Considers multiple variables in making projections rather than the single variables in deterministic techniques. 	<ul style="list-style-type: none"> • More complex than the other alternatives and has more potential for errors.

EXPERT OR BEST JUDGMENT

The “expert” or “best judgment” method relies upon a person or “expert” to forecast revenues and expenditures. It is difficult to say much about the “expert” forecast since there is no single technique or procedure employed in this method of forecast-

ing. The “expert” simply uses his subjective feelings, long-term experience, expertise, and familiarity with revenue and expenditure patterns to make a forecast. The successful expert is someone who knows the financial system, the local economy and knows how to obtain additional information. The key ingredient in this method is finding the “expert.” Long-time finance or budget officers are often referred to as forecasting “experts” in a LG.

The expert method can be appropriately used as a “best guess” for revenue sources where there is little information on which to base a future year’s estimate. One of those categories might be transfers from the central government. Often these revenues are set by formula using information not available to local officials, and adjusted at the last moment with uncertain impacts across the country. An option in using the “best guess” technique is to simply assume that the transfer revenue will be a particular amount. For example, transfers from the central government for a specific program last year are a reasonable estimate for next year, or based upon information from the central government, they will be x% below/above last year.

TREND FORECASTING

Trend forecasting is a technique that relies entirely upon time as the only determining variable. Trend technique depends upon the year-to-year change of a prior year’s variable (i.e., revenue source or expenditure category) to forecast revenues and expenditures. By determining the changes in past years, certain revenues and expenditures can be projected quite accurately into the future.

Local officials wishing to use trend techniques in forecasting should be aware of the underlying assumptions inherent in the methodology. Trend techniques assume that time is the sole important determinant used to produce fairly accurate future forecasts of revenue and expenditure streams. It also assumes that the growth rate in a future year will be the same as it was in immediate past years. This assumption can be made more realistic by considering a longer period over which to measure the past changes.

A review of a year-to-year change of a variable (revenue source or expenditure) can produce different conclusions about the type of change that has occurred and how that will be used for projections. There are three possibilities:

- If a variable has not changed in the past, the variable may be assumed to not change in the projection period;
- If the variable has increased by a constant amount each year in the past, it is reasonable to assume that it will increase each year by the same absolute amount from prior years; and
- If the variable increased each year by approximately the same percentage, then that percentage rate of increase (or decrease) may be used as a constant growth rate in the future as it has been used in the past. For example, if a revenue source has increased 9% each year for the last five years, one can assume that next year’s increase will be approximately 9%.

Note that the trend technique assumes that the past is a good predictor of the future. Unfortunately, that is not always true.

To use the trend technique to forecast a variable, you take the following steps:

- Select the variable (revenue source or expenditure category) that you want to forecast.
- Gather actual data about the performance of the variable over several past years. The accuracy of the trend line forecast will improve when a longer history of the revenue or expenditure is used. Generally, forecasters rely on the most recent five years of a revenue source or expenditure for forecasting, but a six to ten year base is not uncommon and enhances the reliability of projections based on the trend line.
- Review the data for each year looking for one-time occurrences (rate changes, base changes.) Clean the data, i.e., the one-time occurrences should be identified and removed from the variable to avoid skewing the results.
- Analyze the data to see if they represent a constant percentage change or an absolute amount of change each year over time. Plotting these points on a graph may be helpful.
- If the trend appears to approximate a straight line (linear), then an absolute amount of change each year is a reasonable assumption. If the plotted points appear to follow a nonlinear path, a constant growth rate is a reasonable assumption.
- Use the following formula, to determine the percentage rate of change or growth rate of a variable (revenue or expenditure) between periods, where g equals the percentage growth rate of a variable; V is the variable and t is the period of time.

$$g_t = \frac{(V_t - V_{t-1})}{(V_{t-1})} \times 100$$

- To use the formula for multiple years, calculate the growth rate for each year, total the rates and divide by the number of years to produce an average annual compound growth rate.
- To apply the growth rate to make next year's projection, convert the annual compound growth rate to a decimal by dividing by 100; add 1.00 and multiply that sum by the latest period amount to arrive at next period's projected revenue or expenditure.
- Repeat the process for the next period.

Example using formula

Revenues 2006 = 100,000

Revenues 2005 = 98,000

Step 1: $\frac{(100,000 - 98,000)}{98,000} \times 100 = g$

Step 2: $\frac{2,000}{98,000} \times 100 = g$

Step 3: $0.0204 \times 100 = g$

Step 4: $2.04\% = g$

The trend method is appropriate for forecasting revenues and expenditures that are not tied to economic conditions and where the rate of change year-to-year is not

absolute, but shows a fairly constant percentage change without significant annual variations. For example, local fees and taxes might fit these conditions.

Let's look at an example of how a LG would forecast its local taxes and fees revenues (currency in millions) which have been slowly increasing over the last five years as shown in the table below; our objective is to project the fees for 20XX using the trend technique.

The actual data for each year was obtained from the finance department's end of year accounting records. The year-to-year change was calculated using the formula described above, and the sum of the annual changes divided by 5 equals a +2.91% constant growth rate. This growth rate divided by 100 converts the percentage rate to a decimal plus 1.0 times the most recent actual or estimate produces the 2011 forecast for property taxes of 32.53 million (your country's currency). The table shows the results of the above calculations for each year.

Forecast of a LG's Local Fees and Taxes for 2011
Using 6 Base Years 2005-2011 (in millions)

Estimated Revenue Source	Actual 2005	Actual 2006	Actual 2007	Actual 2008	Actual 2009	Actual 2010	Projected 2011
Local taxes and fees	27.4	28.5	29.0	30.4	30.5	31.6	32.52
% Change from prior year		+4.01	+1.75	+4.83	+0.33	+3.61	+2.91

DETERMINISTIC FORECASTS

Deterministic methods are used for forecasting both revenue sources and expenditures, which use other factors than time to project a variable for short and medium-terms. For revenue sources, this may include property taxes, local fees for services, alcohol/ tobacco fees, and other administrative fees. For expenditures, this may include wages and salaries, insurance, and social assistance payments. These deterministic methods may also be used with fiscal impact analysis. A variant of the deterministic approach may be most useful when considering longer-term projections in policy analysis. They can be used to assess the impact of such decisions as zoning, community economic development planning, and comprehensive plan development.

Deterministic forecasts use other factors than time in "determining" projections. These factors may include changes in population, customers served, or other social and economic variables that directly affect revenues or expenditures. The most common deterministic forecasts rely on pre-established formulae in calculating a projected revenue or expenditure. For example, the forecaster may determine that over the last few years the local fee revenue collected averaged 13.65 (your country's currency) per resident. The forecaster then might project that, since it is anticipated that the population will increase by 1,000 during the next year, there will be an additional 13,650 (in currency) collected from these fees.

A more realistic use of deterministic forecasting is to project expenditures using real inputs on the expenditure side of the budget. For example, let us assume that the LG prescribes that no more than 75 cases be assigned to a social assistance worker at any one time. If it is anticipated that 1,000 new residents will include 300 new social assistance cases, then a deterministic estimate of the number of new caseworkers who must be hired is 4 (300 new cases / 75 = 4 new social assistance workers.)

Each of these examples includes some particular assumptions that should be understood before proceeding to use deterministic forecasting. Deterministic forecasting assumes that there are fixed relationships between the inputs and the activities. For example, in the above example, each social worker cannot assume any more than 75 cases. It makes no distinction between type and complexity of cases or experience of personnel, nor does it consider the possibility of increased worker productivity for handling marginal increases in workload. It also explicitly assumes that the level of service being provided at that fixed level is constant, and of course, adequate. That may not be the true situation. Lastly, deterministic forecasting relies on the use of averages, and averages do not fluctuate with significant changes in the economy. In this case, using averages per capita may understate the forecast revenue or expenditure in an expanding economy, or overstate them in a declining economy.

STEPS IN THE DETERMINISTIC METHOD

Use the following steps when forecasting with the deterministic method:

- Select the variable (revenue source or expenditure category) to forecast.
- Determine the formula applicable to forecasting the specific revenue or expenditure, for example, the number of units x unit price = total revenue or expenditure.
- Gather actual historical data about performance of the variable by identifying the critical factors that determine the outcome of the variable over the past years. Generally, forecasters rely on the most recent five years of a revenue source or expenditure for forecasting.
- Analyze each component of the data. Identify in each component the factors that cause the component to change or to remain constant over time. These factors might be: population changes; changes in the number of customers; tax rate changes approved by the governing body or central government; changes in policy; service levels or areas; or other factors. Also, note that factors are within the control of LG or other levels of government.
- Identify any limitations imposed by law or local policy upon the revenue source or expenditure.
- Make assumptions about the components in the formula that will grow/decline without LG action (i.e., population, customers served) and identify the components that are subject to change by LG actions (i.e., tax rates, fee schedules or salary levels.) Base the initial forecast on continuation of existing rates, schedules and salary levels based on your analysis in item 4 above

- for the year to be projected, and assume that other components will continue to change as they have in the past.
- Apply the formula and produce the forecast variable.

FORECASTING REVENUES WITH DETERMINISTIC METHOD

Let's try to apply these steps to an example, to forecast property taxes for a hypothetical LG. The formula used for calculating property taxes is:

$$\begin{aligned} & \text{Tax Base (land area in square meters)} \\ & \quad \times \\ & \text{tax rate (Currency/square meter)} \times \text{collection rate} \\ & \quad = \\ & \text{current property tax revenue.} \end{aligned}$$

This could be made more precise by subdividing the land area into different uses for tax purposes that might have different rates applied. In the table below, the data shows that the tax base area is slowly growing each year by a constant amount due to adjustments to the area of the LG and new development. We may assume that it will continue in the near term. The tax rate is set by the governing body and the current rate is assumed to continue. The collection rate is the five year historical average since there is little year-to-year change. By using the predetermined formula, (the tax base times the tax rate times the historic collection rate of 90 for taxes not collected in this fiscal year) produces the projected tax collections for 2012, based on these assumptions. Modifying any one of the components of the variable changes the projected revenue. The table below displays the data elements and projected revenue.

Historical Property Tax Base, Tax Rate, Collections, and Projections 2006-2012

Revenue Source Property Tax	2006 Actual	2007 Actual	2008 Actual	2009 Actual	2010 Actual	2011 Estimate	2012 Projected
Tax Base (Sq. meters in 000's)	5,990	6,010	6,030	6,150	6,170	6,190.	6,210
Tax Rate (Currency/ sq. meters)	3.20	2.90	3.00	3.00	3.00	3.05	3.05
Total Revenue Due (Currency in 000's)	19,168	17,429	18,090	18,450	18,879	18,888.	18,940
Collection Rate	.91	.89	.90	.92	.91	.90	.90

Collections (Currency in 000's)	17,443	15,512	16,281	16,974	17,180	17,000	17,046
Tax Rate Limit	3.50	3.50	3.50	3.50	3.60	3.60	3.60

FORECASTING EXPENDITURES WITH DETERMINISTIC METHOD

To forecast expenditures using the deterministic method, the same systematic approach is followed and a predetermined formula applied. For example, to estimate the cost of staffing a new facility, the following data should be gathered: the estimated number of persons to be hired based on other comparable facilities; the average salary and wages for full time equivalent (FTE) positions at a comparable facility, and the portion of the year that the facility will be in use in its first year. Taking the number of personnel, times the average salary per FTE, times the fraction of the year the facility will be open, will produce a projection of the staffing cost for the opening year of operation. Subsequent years' costs can be forecast based on full year's staffing, plus additional personnel and adjustments for inflation.

ECONOMETRIC OR STATISTICAL FORECASTING

Econometric forecasting combines economic principles with statistical theories. (For ease of reading, we will refer to this method as econometric forecasting.) Econometric models permit the forecaster to consider the effects of several variables on a revenue or expenditure. The objective is to identify independent variables such as disposable income, population, prices, inflation, etc., that provide the "best fit" to a historical data series. These can be used to project future changes in a revenue source or expenditure tied to the economy, such as income tax or fuel prices.

Regression analysis is the most common approach to econometric forecasting. This process involves four steps to forecast revenues or expenditures independently using statistical regression analysis.

- Specify a functional relationship between a particular revenue source and expenditure and one or two independent variables; one approach is to use a set of independent variables that provide the "best fit" to a series of historical revenue data points. Forecasters use statistical regression techniques to test each variable and choose those that provide the best fit based on a set of criteria.
- Collect historical data for the dependent variable (revenue source or expenditure) being analyzed and each of the independent variables. Forecasters rely on the most recent five years of a revenue source or expenditure for forecasting.
- Statistically estimate the hypothesized relationship using linear regression.
- Use the projected values of the independent variable to produce the forecast of the revenue or expenditure series.

Econometric forecasting is best suited to forecasting revenue variables that are responsive to economic conditions.

MODEL BUILDING

The above discussion has covered the various methods of forecasting revenues and expenditures. Now let's consider how we can bring these together.

Model building is a common approach. A model is a systematic approach to planning and forecasting that includes the use of scenarios. Collectively, a model presents a view of a future condition based on a set of assumptions. By changing the assumptions, the forecaster can measure the effect changes in policy or economic conditions will have upon the model. This information is useful to policy makers to understand the long-term impact of changes in variables or policy decisions.

Models can be built with or without computers. Without computers, a model takes longer to build and is limited in the number of scenarios that can be run. Using a computer and spreadsheet-based software to construct a model is preferred for financial planning and forecasting. Computers are being used for a number of financial planning and forecasting applications, such as fiscal impact modelling, econometric and statistical modelling, economic development modelling, cost revenue analysis and strategic financial planning.

The advantages of using microcomputer based models and spreadsheet software for financial planning and forecasting include:

- The ease of construction and ability to revise the model,
- The speed and flexibility to prepare "what if" scenarios,
- The relative low cost of computer and spreadsheet software,
- The need for only an analyst or two to maintain the system—no programmers—and
- Its potential to improve understanding of relationships among variables.

Computer modelling aids decision making. Assuming that a model is properly constructed, using a few keystrokes to change an assumption and produce a new forecast in a few minutes is of critical importance to decision makers. Time is then spent analyzing the impact of the change and potentially influencing the decision making process. This is known as computer decision support, which emphasizes data analysis, rather than data capture. Decision support makes it easier for LG officials to analyze data to identify relationships, patterns, and implications of decisions.

On the down side, building a computer model may require a person skilled in computer spreadsheet applications and forecasting methodology. Computer modelling can also be extremely complex, and may easily produce errors in the forecast if the person developing the model is not particularly cautious.

Before undertaking a multi-year (medium- term) forecasting project, the forecaster should consider the needs of the LG, the applicability of different forecasting methods, the specific revenues and expenditures to be forecast, the availability and

accuracy of prior year's data, costs associated with each method, and the skills of personnel building the model and producing the forecast.

MONITORING AND EVALUATION

Unfortunately, many forecasts, when completed and presented to management and governing body, are relegated to a place on the bookshelf and not looked at again until it is time to dust it off and update it in the next fiscal year. This approach overlooks the value of relating forecasts to the annual budget and to continually refining the forecasting methodology.

Ideally, forecasts represent a baseline on which subsequent years' annual budget instructions and priorities are based. To tie the forecasts and annual budget process together, revenue estimates proposed for the annual budget are compared to the multi-year forecast and variances explained and justified. This action increases the accountability of the forecaster and helps make the forecast more realistic if he/she knows that they will have to explain major differences in estimates.

This type of "reality" check also has another benefit. It permits the forecaster to review the methodology used in the forecast when explaining variances in the budget estimate; and, ultimately to evaluate the actual experience of revenues collected or expenditures disbursed. The knowledge gained from this experience can be used to improve future years' forecasts.

FORECASTING REVENUES AND EXPENDITURES

While there are a variety of approaches that LGs can take to forecast revenues and expenditures the challenges faced by LGs, and the steps taken to overcome them, are similar. This section provides the basic elements of revenue and expenditure forecasting.

REVENUE FORECASTING

As mentioned earlier, forecasting revenues can be accomplished either by a central office (i.e., finance or budget office) or by individual departments coordinated by a central office. It really depends upon which office or department has access to historical data and information on which a forecast is based. In some LGs, a separate division of the finance office or budget office may be set up to do the forecasting project. In larger LGs, the finance or budget office may coordinate the forecasting project and rely upon knowledgeable departments to provide the forecasts for them to consolidate. LGs should choose the approach that fits their organizational experience.

LGs are likely to face the challenge of forecasting four sets of revenues: local taxes and fees, sales from LG assets, shared taxes from the central government, and subsidies. Local taxes and fees are probably the easiest to forecast since the data is readily available and decision making is within the local officials' control. The others are more problematic. The revenue from LG assets (sales) is driven, in part, by the real estate market and laws of supply and demand. The volatility is muted somewhat

by the fact that a portion of these revenues are combined with more stable revenues such as rents, earning tax from LG enterprises, and revenue from contributory organizations.

Shared taxes from the central or province governments and subsidies are dependent upon them providing projections of future year's revenue, or the data and information so LGs can make the calculations and their own forecasts. Around the world, LGs have had considerable difficulty obtaining this information in a timely manner, if at all. In many countries, the problem is compounded by laws and regulations that are constantly changing. Additionally, the reduction in LG revenues from the central or province governments will force LGs to increase the portion of the budget funded from local revenues, making forecasting to plan for this change even more important.

When all the revenue sources are projected, the forecaster adds the projected revenue sources by year. The result is a forecast of a LG's baseline revenues for future years. Using this forecast, alternative scenarios with different assumptions for revenues, economic base, or rate structures can be used to project alternative revenue streams in future years.

Trend analysis and econometric projection methods may require 10 to 15 years of historical data to obtain reasonable regression analysis results. Thus, a major cost of the overall forecasts may be the cost of gathering this data and making it available in an accessible form. There are two problems associated with gathering and using this historical data. First, there may be changes in definitions of the data and secondly, there may be changes in the rates or bases of the revenue sources that have occurred over time. Major revenue sources are usually reported on a consistent basis over the time, but this may not be true for minor revenue sources.

Forecasters can address this problem by aggregating many small revenue sources into a single common category, (fees and charges), and using this combined source for projection purposes. Another problem is accounting for discretionary changes in the rate or tax base of a revenue source. To insure that the data is put on a consistent basis, it is necessary to "clean" the data to eliminate purely administrative changes. This attempts to factor out the effects of discretion changes in tax rates and base changes by estimating what revenues would have been without the changes. This task involves considerable investigation into the past rate changes and base changes. As a result, most forecasters concentrate on cleaning only the major revenues sources.

Other factors to consider in preparing forecasts include:

- Forecasting is an art, not a science. Accuracy will always depend upon the validity of economic and policy assumptions.
- The forecasting process is like good wine—it improves with time. Start simply, and do not expect the first forecast to provide you with miraculous insights.
- Confidence in the forecasting process and insight into how the process and resultant forecast can be used has a "ripple effect." Confidence will come first to the project manager. Officials on higher management levels will learn to value forecasting gradually.

- Multi-year financial forecasts may work to your political disadvantage. If the forecasts are wrongly cited as predictions, their content can be used to buttress adversaries' arguments against you. On the other hand, politicians can use forecasts for their own purposes to direct attention to their proposals.
- Local tax and fee revenue limits and expenditure limitations may discourage potential users of financial forecasts. However, forecasts can consider these realities and use them to illustrate the future effects of such actions. Forecasting may also aid planning efforts when new constraints are present or possible, such as changes in the law by Parliament or the Ministry of Finance.

EXPENDITURE FORECASTING

Three general categories of expenditure disaggregation will be discussed: 1) LG-wide—by accounting classification; 2) organizational—department by object code, and 3) programmatic—program/activity by sub-object code. Selecting the level of disaggregation used in the forecast at the beginning is important because it determines the information and level of detail that will be required for the forecast and the source of that information (LG finance/budget office or departments.)

LG-WIDE EXPENDITURES—BY ACCOUNTING CLASSIFICATION

Using LG-wide expenditures, broken into accounting classifications, organizes the expenditure forecasts by the objects of expenditure, (e.g., personnel services, materials, debt and other services, transfers and equipment.) Shown at a LG-wide level, this forecast is high level and relatively easy to accomplish. With only five or six objects of expenditures to forecast, a deterministic or trend line approach is appropriate and can be done by the finance/budget office.

While relatively simple, this approach provides no basis to analyze why expenditures are increasing or decreasing, other than to reflect past years' trends or the assumptions made in a deterministic model. Dividing these major classifications into other expenditure sub-objects provides more detail, more elements to forecast, and potentially a more accurate forecast. However, organization by accounting classification provides little explanation for the increase or decrease of an expenditure or which LG program or department contributed to it.

ORGANIZATIONAL APPROACH

A second category for disaggregating expenditures is to use an organizational approach based on the hierarchy of departments and divisions, combined with existing accounting classifications. This approach provides more detail to the forecast as expenditures are projected by department, division and accounting classification rather than LG-wide. A deterministic or trend line method is also appropriate in this approach. Forecasts built organizationally provide detailed information for analysis that is not available in a simple accounting classification approach. A key disadvantage is that it does not reflect information on a program basis (this assumes that a program crosses more than one department).

Approach 1 may be more helpful when looking at new services.
Approach 2 may be more helpful when looking at existing services.

PROGRAM BUDGET MODEL

A third category for disaggregating expenditures is based on the program budget model. A deterministic or trend line approach works here, too. This approach utilizes existing processes, involves the same personnel who develop the budget, gathers sufficient detail to analyze changes, and utilizes the experience of front line program managers in forecasts. Disadvantages include the increased workload of the detailed program orientation.

In general, the degree of disaggregation used depends upon the budget and accounting system used in the LG. If the disaggregation is done to the same level as the preparation of the annual budget, it will facilitate the time that it takes to prepare this aspect of forecasting.

DETERMINE GENERAL APPROACH

Once the disaggregation method is selected, the next step is to determine the general approach for making the forecast projections. Generally, forecasters use the disaggregated expenditures and project according to a consistent set of assumptions about service levels, productivity, and price level changes. The major difference in approach relates to the unit of analysis (base) that is used in carrying out the projections. The practice ranges from projection of “real” inputs to projection of total expenditures. Two approaches will be discussed here.

Approach 1: This approach uses “real” inputs to project expenditures. These inputs might include the number of employees, the number of litres of fuel purchased, the fixed cost of maintenance agreements or agreed-upon unit prices for commodities, existing debt service, etc. This information is then used to calculate the detailed cost of personnel, materials, services, debt, and equipment purchases. For example, to calculate the cost of personnel, the forecaster multiplies the average salary per person times the number of personnel. To calculate the cost of fuel, the forecaster multiplies the number of litres of fuel purchased by the average price of fuel.

This approach provides a detailed projection by object of expenditure and by forecast year using the appropriate projection methodology selected. A more detailed projection is possible if this approach is applied to individual departments or programs. The advantage of this alternative is that its detailed development permits extensive analysis capabilities. The disadvantage is complexity. Generally, there is insufficient staff and time to accomplish this task at this level of detail.

Approach 2: A second approach uses specific increments added to a common budget base to project expenditures. The first step in this approach is standard. The forecaster establishes a constant level of service budget as a baseline. Departments or program managers then advise the forecaster of incremental changes to this baseline for future years, using criteria determined by the budget office. The detailed orientation of an incremental approach to expenditure forecasting permits analysis of both the base and changes in subsequent years, makes better use of department staff time, gathers critical information from knowledgeable sources about future year

changes, and involves department personnel in the forecasting process. The disadvantage continues to be considerable staff time needed to put together forecasts of expenditures. Because this is a more effective method of forecasting expenditures, more text is devoted to this approach.

The forecaster develops a baseline constant level of service budget. Using the current year budget as a starting point, the forecaster adjusts the current budget so that it represents a true baseline. Items subtracted are one-time purchases of capital equipment, supplies, and contracted services. Other items removed include one-time personnel expenses of retiring or terminating employees (i.e., payment for unused vacation, sick leave, or severance pay.) Items added to the base are annualized salaries for employees funded in the base year for part of the year, and merit pay for a portion of employees. With these adjustments, the forecaster sets the base budget for each department or program, and sends it to departments for their review and projected future years' program adjustments.

The forecaster includes an explanation of how the base year number was determined, with instructions and forms for departments to follow and complete to provide input to the forecasting process. The forecaster requests department or program managers to calculate the cost of added/decreased services and to prepare detailed descriptions and explanations of the changes. The incremental service level changes or costs should be a part of LG policy (approved by a LG ordinance or resolution) or mandated by a higher level of government. The increment is classified according to categories, such as:

- Mandated service level changes or costs due to national law changes
- Mandated service level changes or costs due to local ordinances or policy changes
- Productivity increases approved by governing body or management
- Funding for costs of operating new capital facilities scheduled to be opened
- Funding for costs of services due to extensions of service area
- Funding for new and replacement equipment

Once the information is prepared by the departments, it is sent to the forecaster. If acceptable, the forecaster adds it to the appropriate future year's baseline to produce the future year's projected expenditures. This assumes, of course, that the baseline current service level remains unchanged and factors that might affect a rapidly growing LG (population, service connections) are generally held constant. While inflation is always a consideration—it is not built into the scenario by departments. If it is used, it will be applied uniformly later. LGs must consider individual situations carefully in applying assumptions that will drive the forecasts.

Management reviews the projections of future expenditures. Decisions are made about additions/changes to be included in the expenditure forecast to best represent future years' current service committed costs. All approved changes are added to the respective baseline budget by respective year and totalled. The resulting fiscal year totals represent projected expenditures. Items requested but not included in this forecast are shown on a separate list of unfunded needs.

LEARNING APPLICATION

POLICY MAKER ☐ CEO ☐ FINANCE MANAGER ☐ DEPARTMENT HEAD ☐

Turn your attention now to the method of forecasting, and identify five major revenues sources and expenditures in your LG. Based on the discussion in the material, what method would you use to forecast each of these revenues and expenditures? Explain your choice of methods for each of the items.

Does your LG use any other method to forecast revenues and expenditures?

POLICIES

To build a solid framework for financial planning, we need policies for the various financial planning tools and techniques identified in the basic concepts section of this chapter. Based on this assumption, the framework should include policies on:

budgeting, forecasting, capital programming, debt planning, trend monitoring, strategic planning, and economic development planning, at a minimum.

Following are samples of these types of policies:

Sample Policies

To design, maintain, and administer a revenue forecasting system that will assure a reliable, equitable, diversified, and sufficient stream to support desired LG services.

To identify priority services, establish appropriate service levels and administer the expenditure of available resources to ensure fiscal stability and the effective and efficient delivery of services.

To annually review and monitor the state of the LG's capital equipment and infrastructure, setting priorities for its replacement and renovation based on needs, funding alternatives, and availability of resources.

To establish guidelines for debt financing that will provide needed capital equipment and infrastructure improvements while minimizing the impact of debt payments on current revenues.

To invest LG's operating cash to ensure its safety, provide for necessary liquidity, and optimize yield.

To initiate, encourage and participate in economic development efforts to create job opportunities and strengthen the local economy.

To prepare and present regular reports that analyze, evaluate, and forecast the LG's financial performance and economic condition.

To comply with prevailing central government, province, and local statutes and regulations, as well as current professional accounting principles and practices.

BENEFITS OF FINANCIAL PLANNING

Financial planning, and specifically forecasting, can be important tools for the chief executive officer, legislative council, and management. Properly applied, financial planning and forecasting produce positive benefits for LG and citizens. For example, they:

- Link the LG's policy with specific financial plans to achieve a governing body's long-range strategic goals—The importance of adopting financial policies was stressed in Financial Policy Making of this series. The governing body's long-term policy goals and direction serve a very important purpose. They make staff decision making easier by communicating council expectations and reducing the options to be considered.
- Develop a picture of the LG's financial future and create more time to respond to adverse events—When a picture of a LG's financial future is developed, elected officials have the opportunity to decide whether it is acceptable or not and what actions need to be taken. If the governing body decides there are adverse events in their future, they now have advance notice to respond to the event before it becomes reality and a crisis.

- Prepare the LG for shifts in responsibility—In many countries, national governments have shifted a number of responsibilities to LGs, and in some cases without adequate resources. This situation requires that LGs acquire the financial planning skills to analyze these potential shifts while they are being planned and to persuasively argue for the resources to support them, if needed.
- Improve the quality of financial decision making—LGs have a need to plan for the future—next year, five years or ten years from now. Financial planning uses analytical tools to fine tune the picture, analyze data and develop plans that effectively respond to the issue with the ultimate benefit—a better decision. For example, in debt planning the LG must limit its total capital investment spending plan and spread it out over a number of years based on the LG's capacity to pay. Financial planning analytical tools help determine what the LG can afford to pay annually for debt service to finance the CIP.
- Develop alternative decision strategies—By creating a vision of the future, financial planners can identify potential adverse events. These can be used, not only to develop an appropriate response, but also to use different assumptions of that future to test how alternative strategies would fare under different assumptions.

Financial forecasting in a more focused context provides similar benefits. The benefits range from acting as an early warning system, improving budget planning and decision making, supporting legislative and borrowing programs, to educating the citizenry through disclosure of public information. Financial forecasting can:

- Serve as an advance warning system—When prepared and presented early in the budget planning process, forecasting future revenues and expenditures can alert elected and appointed officials of the financial limitations under which the next year's budget (and future years) is developed. This helps elected officials understand the financial situation, eliminates surprises, and provides time for them to take the necessary preventive actions.
- Improve the policy development and budget preparation process—Financial forecasting can provide information about potential changes in services, new demands for service, anticipated revenues and any expected surplus or deficits. Early forecasts give local elected officials an opportunity to provide policy direction, set budget priorities, and establish budget guidelines based on this information. This direction can be incorporated into more detailed budget instructions given to departments to aid in budget request preparation. This saves considerable time and effort in preparing budget requests. Budget priorities may be program oriented by indicating a preference for increased spending in one program or service over another. Priorities may also be resource oriented, by indicating a priority for property taxes over user fees and charges.
- Evaluate alternative financial plans—Financial forecasting can illustrate the immediate and longer-term fiscal implications of various economic and policy scenarios. It also helps in determining the extent in which governments can

afford them. As a result, elected and appointed officials can better evaluate competing budgetary proposals and alternative financial plans.

- Aid decision making—Financial forecasting can increase the awareness of elected and appointed officials of the long-range implications of decisions. It also helps decision makers to understand the cumulative effects of decisions—resulting in better decisions from the start.
- Support lobbying the national legislature—Financial forecasts applied to projecting the financial impact of proposed legislation such as the changes in formulae for sharing revenue between central government and LG or shifts in responsibilities to LG. Forecasts can be effective in convincing the Parliament of the impact of these changes and convincing them to modify the proposal. Similarly, financial forecasts can help convince the national legislature (Parliament) of the need for new revenues or restructuring of existing ones.
- Support borrowing and credit evaluation—Financial institutions that underwrite loans to LGs view financial forecasting as a necessity. These institutions and other agencies that evaluate the creditworthiness of LGs view forecasting as a sound financial management practice.
- Promote open government and disclosure of public information—Financial forecasts can help the LG show political organizations, businesses, media, and citizens the long-term costs of various service programs and economic policies. In turn, this improves their understanding of LG.

There are many reasons why LGs don't prepare multiyear forecast of revenues and expenditures. The following are some of the most common that we have heard over the years:

- Prior central government economic planning has given all planning a bad name.
- LG revenues are too unstable and unpredictable to forecast for future years.
- Forecasting multiple years' revenues and expenditures is difficult with a 20-30% annual inflation rate.
- Staff is too busy with the day-to-day activities. There isn't time to plan.
- LGs are limited in their ability to raise revenue and have little flexibility to manage revenue sources. It seems pointless to spend time identifying a problem that can't be solved.
- There is no reliable historical data to use for forecasting.
- Elected officials are not interested in planning for the future—just for the next election.
- The computer equipment, software, or skills do not exist to prepare forecasts.
- There's no law that requires it.

LEARNING APPLICATION

POLICY MAKER ____ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

Now that we have reviewed the benefits of financial planning and forecasting (and some of the reasons people have given not to plan), consider how it can be applied in your LG. Recall from your unique role in your LG several multi-year decisions that you have made in the past. How beneficial were these decisions in supporting your financial resource requests to the governing body or other levels of government? In addition, how beneficial were they in supporting the implementation of multi-year projects?

Looking back on your experience with financial planning and forecasting in general, what might you and the LG management team do to improve the quality and success of your financial planning and forecasting initiatives?

OBSTACLES, LIMITATIONS, RISKS, AND OTHER CONSIDERATIONS

Multi-year forecasts represent a powerful tool for council and management; however, they should be used only after considering the obstacles, limitations, and risks inherent in financial planning and forecasting.

Introducing change into LG policies and practices is a difficult task. Being a successful change agent is even more difficult. There will be many obstacles to introducing financial planning and forecasting into LG where the longest forecast is the annual budget. Some of these obstacles include: political and staff resistance, a constantly changing LG revenue system, lack of development time, lack of knowledgeable and skilled personnel, and insufficient historical data.

Political and staff resistance—The norm in many LGs is the status quo. You can expect to be questioned about the merits and need for financial planning and fore-

casting. Elected officials may question the value of forecasting future years and uncovering problems when current year problems are not being adequately addressed. Staff may also question the need for financial planning because they feel that they are too busy with everyday activities to spend time on planning. Staff sometimes fears that the requirement of financial planning to document assumptions on which forecasts are made may undermine their current information and erode trust in staff judgment.

Changing LG revenue system—The central government's propensity for adding/dropping/shifting revenues to and from the LG revenue system, and altering the coefficients on which LG shared taxes depend, is a real problem for forecasters. It is made even more difficult when these changes are made annually or late in the budget process and made to achieve political objectives. It leaves LGs at the mercy of officials in the Ministry of Finance and Parliament who make those decisions, assuming this is the situation in your country.

Lack of development time—Financial planning and forecasting take additional time to produce a reliable product. This is particularly true for the LG that is starting its first financial forecast. Considerable development time is needed to collect the information and data needed in forecasts, develop, and test the forecasting methodology to produce the forecast. Persons assigned to forecasting responsibility should be dedicated full time to the task for a portion of the year to complete the project successfully. Preparing the forecast outside the traditional budget calendar is recommended, to avoid conflict with pressing budget issues.

Lack of knowledgeable and skilled personnel—Another critical item to financial planning and forecasting is personnel. Elected officials are unlikely to have been exposed to the benefits and processes associated with financial planning and forecasting. We suggest that they attend a finance workshop to increase their awareness of these techniques. Since many finance directors are economists or accountants by training, they are more likely to be familiar with forecasting. However, they may lack requisite computer modelling and statistical training that is helpful in applying some forecasting methodologies. This, too, can be acquired by training or borrowing personnel with the applicable skills from a local university or local consulting firm on a temporary basis.

Lack of historical data—This stems from several possible situations:

- Historical data does not exist because revenues were dropped from the LG revenue system (e.g., tax on entrepreneurial income.)
- Replacement revenue streams (e.g., property tax) have not been in place at the local level long enough to establish a historical base for projection purposes.
- Current LG revenue system may be so new that the LG does not have historical data before that date.
- Your LG may not be responsible for collecting the revenue (i.e., shared taxes) and has no documentation about the details of the revenue source.

All of these situations create a serious obstacle to financial planning and forecasts that depend upon historical data. The only plausible solution is to develop the database on information that exists and add to it each year, and over time, it will

become sufficient. For historic revenue data that resides with another government agency two options exist. 1) Have them provide the historic data that you need and you do the forecast or 2) let them do the forecast and advise you of the result. Working with external agencies (especially higher levels of government) always seems to be difficult and frustrating as these agencies frequently have little reason to be cooperative or to help a local government with their problems.

Dilemma of circularity—Forecasts involve a certain amount of circularity. The future is decided by people and is not out of our control. Policy makers want to know what the future is projected to be like so that they can act, yet the actions they take will also determine what the future will be like, hence the circularity.

One of the best examples of where this can happen is the forecast of growing demand for some public service or facility. If that demand is later realized then it might have been “correctly” forecast, or it might have occurred because of the forecast and the action that it spurred. For example, in past decades U.S. electric companies forecast enormous growth in the demand for electricity and expanded their generating capacity accordingly. Later, having huge capacity, they lowered the price of electricity for users of large quantities and invented new uses for electricity. So, do the early forecasters of great demand now have the right to claim their forecasts were accurate? Probably, because the result of the action also helped to create the demand for more electricity. It is this intertwining of forecast and action, action and forecast, which presents the dilemma of circularity.

Importance of assumptions—Many draw a distinction between the terms “forecast” and “projection or extrapolation.” A projection or extrapolation is merely a mathematical calculation of likely consequences based on relationships between variables. For example, a simple population projection extends in time the past relationships between birth, death, and migration rates. A “forecast” is more than a projection because it also involves selecting particular values of the variables involved. So, a “forecast” of population requires that you first select the specific birth, death and migration rates that are most likely to occur in the future and then to project their future values. Estimating the right future values for these birth, death and migration rates is much more challenging because you must make assumptions about the parameters of the future values. It is extremely important that you understand that forecasts require numerous assumptions. Without assumptions, forecasting is impossible. However, assumptions can be very self-serving and in the end dominate the outcome of the forecast.

A limitation of forecasting—Financial forecasting is not a panacea for all the problems of LG. It has limitations that you must consider before instituting a financial planning and forecasting program.

- **Forecasts are not predictions**—Forecasts are projections of what will happen only when certain conditions and assumptions come true. As such, they are intended to influence policies that affect these assumptions. Unless the public understands this distinction, forecasts can lead to a loss of credibility. The danger is greatest when forecasts, year after year, project a revenue shortfall. Since revenue shortfalls cannot be permitted to exist and never do because actions taken by the LG eliminate them, the forecasts may

be criticized as giving false alarms if they are viewed as predictors instead of projections.

- Forecasts are not intended to solve problems—Forecasts are tools to help identify problems before it's too late to take corrective action. Once a problem is identified, forecasting can be used to test alternative solutions or scenarios. For example, if a revenue shortfall is projected, then the forecast can test the impact that alternative revenue changes may have on the forecast or the impact that expenditure reductions may have. Forecasts are dependent upon the underlying data, methods, and assumptions.

STEPS IN FINANCIAL FORECASTING

The approach to organizing the financial forecasting process depends on the organization and needs of the LG making the forecast, the resources available, the time allotted to complete the forecast, and the degree of management and political support. The person who has been given the responsibility should ask basic questions about the expected output, and based on the answers develop an approach that achieves the expected outcome in the most efficient and effective manner.

To simplify, all future references to this person, team, or department in this chapter will refer to them generically as “the forecaster.”

STEP 1: DEFINE THE PURPOSE

The first step in determining an approach to forecasting is to define its purpose, its scope, audience, and other project parameters. The person who provided the impetus for the forecasting project is the most likely person with whom to discuss these issues. Usually, the CEO or governing body provides this direction. At a minimum, the forecaster should obtain the answers to the following questions:

- What is the purpose of the forecast?
- What benefits will accrue to the LG from performing the forecast?
- Where in the budget calendar does the multi-year forecast fit? —Beginning, middle, or end?
- When is the forecast needed?
- Will the forecast be used internally or externally?
- Who is the audience that will review and receive the forecast?
- How many years will be forecast?
- What resources are committed to the project? Are they adequate? Staff, computers, other?
- Who is responsible for the project—finance director, budget officer, CEO, other elected officials?
- Who should be included on the forecasting staff—finance staff only, other departments, elected officials, and citizens?

STEP 2: ADDRESS CITIZEN INPUT OTHER TECHNICAL ISSUES

- Has citizen input been received? Planning should always involve citizen input because it determines future direction.⁴
- Will the forecasts be prepared centrally or by departments for their respective areas or a combination of both?

Centralizing the preparation offers advantages: 1) consistent assumptions, 2) fewer highly skilled people involved, and 3) a uniform methodology applied to similar subjects. The disadvantage is that the central office may not have the data, knowledge, and experience to make accurate forecasts. A combination of both may be the way of addressing a pure centralized or decentralized approach.

- Will the forecast project revenues in the aggregate or individually?

Although it is possible to forecast in the aggregate, separate forecasts of each major revenue source provides better control of the variables and allow more opportunities for analysis.

- Will the forecast project expenditures based on accounting classification, department organization, programs, or a combination of these?

To simplify matters, the forecast of expenditures should be organized consistently with the capabilities of the accounting and financial reporting system.

- What major assumptions are included in the forecast that must be applied uniformly?

For example, inflation, salary adjustments, commodity price changes, etc. How will that be done?

- What data and information sources will support the project?
- Are they current, accurate, and available?

When the answers to these questions are obtained, the forecaster needs to decide the approach to forecasting.

STEP 3: DECIDE ON YOUR APPROACH TO FORECASTING

For the initial effort at forecasting, a simple and practical approach is advisable. For a centralized, single department approach; use the following steps to organize the initial multi-year forecast:

- Document the need for, and benefits of, a multi-year forecast;
- Determine the interests and needs of the CEO and governing body regarding the decision making process;
- Obtain the necessary management and political support;
- Assign responsibility for the forecasting project to a single department such as finance or budget;
- Designate a senior finance or budget officer as project leader. (Relieve them of other responsibilities until the project is completed—this will be a full time effort);

- Assign other staff (if possible) with the proper skills to support the project;
- Ensure the necessary information, equipment, space and time is provided to complete the forecast;
- Ensure that an action plan is prepared to guide the project with specific outputs, deadlines, assigned tasks and individual responsibilities included therein;
- Monitor the work at planned intervals that represent completed stages of the project;
- Complete the forecast project;
- Coordinate the finished product with the appropriate supervising officials, and
- Prepare the materials to present the forecast with recommended actions to address the issues raised in the forecast.

Since it is important to succeed on the first effort, keep it simple. As you gain experience with forecasting and a permanent staff is retained, other approaches may be tried.

STEP 4: DETERMINE DATA AND INFORMATION REQUIREMENTS

LGs should gather and analyze the following type of data concerning own source revenues, (i.e., local taxes and fees, sale of LG assets, and shared taxes and subsidies from the central government.) The source of this data is typically found in LGs' prior and current years' budgets, prior years' audits and accounting records, local and national laws or department program activity records.

Revenues

- Five years of historical revenue data.
- Actual revenues collected by source (house tax, agricultural tax, earnings tax, etc.).
- Definition and description of the revenue source.
- Legal basis for the revenue source.
- Specific revenue data: number of customers/accounts, rates and bases of revenue source, collection rates, exemption policies, formulae, and any other related factors.

Expenditures

- Five years of historical expenditure data.
- Actual expenditures by account, department, or program.
- Descriptions of account classification, program, or department organization.
- Legal or contractual basis for account, program, and department expenditures.

- Expenditure specific data: (detailed enough to relate significant year-to-year increases/decreases to policy, program or one-time changes).

Gathering data on the current year presents a different problem for the forecaster—the actual data for the entire fiscal year is not available, and it is constantly changing as revenues are collected and expenditures are made throughout the year. In this situation, the forecaster should compare the budget for current year to the latest current year estimate, and explain significant variations for revenues and expenditures. This allows the forecaster to determine accuracy of the current budget to year-end estimates and include the most accurate information in the forecast base.

The historical and current data should be analyzed to determine an appropriate methodology to make the forecast. The forecaster should also consider gathering other related financial information from the central/province government and local sources that may be helpful in understanding the forecasting environment and existing plans that will influence the forecast in the future. Occasionally, banks, financial institutions, and universities may be sources of this information, as they gather economic data for their own purposes.

The forecaster should be cautious about incorporating plans into the forecast, particularly if these plans have not been adopted by the governing body. The forecaster should incorporate only plans that the council is either obligated or mandated to do or has made a binding commitment to implement in the future. Some of these mandates or commitments, as well as other useful information about the economy, may be found in the following documents:

- Central/province government approved budget—subsidies and transfers
- Bank loan agreements—principal and interest payment schedules and maturity dates
- Contracts for public services—financial commitments and adjustment provisions
- Central/province government and local strategic plans—program priorities
- Central/province government and local development plans—future project priorities and plans to complete projects under construction
- Central/province government and local economic forecasts—inflation estimates, population projections, business indicators, construction and building activity

After analyzing the historic and current data and applying an appropriate methodology, the forecaster should document the basis on which the forecast was made. It is important to be able to explain how the forecast was made and determine the reason for differences between projections and actual.

The following revenue and expenditure information should be documented in the forecaster's records:

- Revenues
 - Assumed revenue bases and fees
 - Assumed economic changes that will impact revenues

Committed central/province government and local policy changes that will occur in the forecast period
Projected revenues by source for forecast periods
Explanations of key assumptions by source
An explanation of the forecast methodology

- Expenditures

Assumed expenditure base and committed programs
Assumed policy changes that will have an impact on expenditures
Committed central/province government and local policy changes that will occur in the forecast period
Projected expenditures by account, program or department for the forecast period
Explanations for program increases and decreases
An explanation of the forecast methodology

STEP 5: DETERMINE RESOURCES

The forecaster should prepare a project plan, which includes the following:

- Staff resources and time required for data collection,
- Staff resources and time required for data analysis,
- Staff resources and time required to design and test a spreadsheet for forecasting,
- Number of computers needed,
- Software needed,
- Specific listing of the various tasks to be achieved in the order in which they need to occur.
- Estimated time to complete each task.

The project plan should be a task-by-task itemization for achieving the forecast with specific due dates and responsibilities assigned for each step.

STEP 6: MANAGEMENT AND POLITICAL SUPPORT

The most essential ingredient to a successful forecasting process is a strong and continuing commitment from the CEO. The CEO must convey during the development process that the forecasts will actually be used, or it will be difficult to get the continued support from others in the LG to complete the process. This is especially true if department directors and their staff are involved in the forecasting process. If they perceive that their work will not be used, the process will be viewed as useless. When this happens, the inputs from department management and resulting forecasting process will become meaningless.

In the forecasting processes, gaining management and political support are important first steps. Here are some suggestions to gain management support for a forecasting proposal:

- Determine whether and where financial planning, and specifically financial forecasting, can help top management and policy makers.
- Chart a course to accomplish multiyear financial forecasting.
- Identify the benefits and pitfalls of forecasting.
- Tie forecasting to existing budget planning processes. (For example, as the first step of the budget calendar.)
- Acquire planning and forecasting tools and expertise through staff development training.
- Present the forecasting proposal to management for consideration and approval.
- If approved, seek guidance on obtaining political support.

Here are some suggestions to gain policy maker support:

- Seek the advice and counsel of the CEO.
- Identify the potential political benefits and pitfalls.
- Focus the forecasting proposal on a policy oriented effort to direct or redirect a LG's financial future.
- Coordinate the proposal with other interest groups and political parties, as appropriate.
- Present it to the CEO, governing body, and appropriate committees.
- Adjust the forecasting proposal based on the elected officials' response.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

Now that we have discussed organizing the forecasting process, it is time for you to look at your LG.

Identify the key persons in your LG that would need to be involved in a forecasting project.

What role would each person play?

Who would be the best person to organize such an effort?

How would you gain the management and political support?

List the critical steps that would need to be taken in your LG to establish a multi-year financial forecast on an annual basis.

STEP 7: DETERMINE LENGTH OF THE FINANCIAL FORECAST.

Review the information provided in the section on basic concepts and decide on the best length for your purposes.

STEP 8: EVALUATE METHODS OF FORECASTING BASED ON LENGTH OF FORECAST.

Review the information provided in the section on basic concepts and decide on the best method for your purposes.

STEP 9: DECIDE ON APPROACH FOR FORECASTING REVENUES.

Review the information provided in the section on basic concepts and decide on the best method for your purposes.

STEP 10: DECIDE ON APPROACH FOR FORECASTING EXPENDITURES.

Review the information provided in the section on basic concepts and decide on the best method for your purposes.

STEP 11: COMBINE THE REVENUE AND EXPENDITURE FORECASTS.

Here are some tips for combining these two forecasts. With revenues and expenditures projected for future years, the forecaster prepares a table or chart showing the totals of projected revenues and expenditures for the respective fiscal years, and creates a balance for each period. The purpose of the table is to focus attention on the revenue shortfall or “gap.” The forecaster can show what types of policy changes need to be considered to close the gap. Using various assumptions about changes in the economy, tax rates, fees and expenditure levels, the forecaster can illustrate the nature and magnitude of these changes. The changes generally should be actions or policies that are within the LG authority. For example, delaying the construction of capital investments can free up revenues. Postponing the opening of capital facilities can defer operating expenditures. Increasing the property tax rate or service fees can produce additional revenues.

Once the base line budget and projections are made, the forecaster can produce an unlimited number of “what if” scenarios. These scenarios show the impact of applying various changes in policy or on the revenue and expenditures for future years. They also may include economic changes in inflation (high, most likely, and low) or changes in the growth of the economy (vigorous, most likely, none, decreasing) over the forecast periods. The value in producing multi-year forecasts is to help the coun-

cil anticipate and plan for potentially adverse financial events, and to provide policy options that result in decisions made early enough to avoid adverse effects.

STEP 12: UNDERSTAND LINKAGES TO OTHER PLANNING EFFORTS.

Review the information provided in the basic concepts to ensure that you have considered how this forecast integrates with other planning processes. It is important that numbers generated for one type of planning be synchronized with the other planning processes. For example, do not use one set of numbers for the CIP and then a significantly different set of numbers for the debt planning process.

LEARNING APPLICATION

POLICY MAKER ☐ CEO ☐ FINANCE MANAGER ☐ DEPARTMENT HEAD ☐

Because of the importance of financial forecasting to financial management decision making, we suggest you develop a strategy to implement financial forecasting in your LG. Complete the following assessment for your LG. Only check those where the answer is Yes.

Financial Planning/Forecasting Assessment Checklist

Policies/Goals

- ☐ Is financial planning a high priority of LG?
- ☐ Has the governing body adopted a written policy on financial planning and forecasting?

Financial Planning

In which of the following types of financial planning is your LG engaged?

- ☐ Annual budget?
- ☐ Financial forecasting?
- ☐ Capital programming?
- ☐ Debt planning?
- ☐ Trend monitoring?
- ☐ Strategic planning?
- ☐ Economic development planning?

Financial Forecast

- ☐ Is a multi-year financial forecast prepared/updated annually?
- ☐ Is the financial forecast prepared for management use only?
- ☐ Is the financial forecast presented for both management and governing body use?

Financial Forecast Document

- ☐ Does the forecast include an executive summary?
- ☐ Does the forecast explain revenue and expenditure assumptions included in the forecast?
- ☐ Does the forecast include at least 3 to 5 years of projection?
- ☐ Does the forecast include all major revenues?
- ☐ Does the forecast include all expenditures?

_____ Does the forecast include all LG funds?

Based on the answers given to the assessment above, and the blank spaces (meaning you answered “no”), what first steps should your LG take to improve its forecasting ability?

What is the state of financial forecasting in your LG?

Who do you need to discuss your concerns with in the organization?

What objectives do you want to achieve from that meeting?

INTERNET RESOURCES

Municipal Financial Planning. Chapter 13. 13.1 RELATIONSHIP TO OUR VISION. Deciding how to distribute limited financial resources effectively is an ...

www.cnv.org/c/DATA/2/107/~CHAPTER%2013%20MUNICIPAL%20FINANCIAL%20PLANNING.PDF

Urban Institute Facilitator's Guide for A Case Study on Municipal Financial Planning. Ronald Forbes. Paper Pub. ID# 409392 ISBN 409392 20 pages May 1999 \$5.00

www.uipress.org/Template.cfm?Section=Bookstore&Template=/Ecommerce/ProductDisplay.cfm&ProductID=3305

Five Year Capital Works Plan. Municipal Financial Statements. Municipal financial statement information provides audited Public Sector Accounting Board.

www.municipal.gov.sk.ca/mrd/gapmr/index_gafm.shtml

Municipal Financial Tools for Planning and Development—This publication was developed to help municipalities identify a range of potential financing tools available to support planning and development ...

www.mah.gov.on.ca/userfiles/HTML/nts_1_3089_1.html

Public Finance and Economic Growth Projects: Poland – RTI. Krakow Municipal Creditworthiness Enhancement Project (CEP) ... Financial Planning and Budgeting. An integrated multi-year financial planning model suitable ...

www.rti.org/page.cfm?objectid=6B89D20A-E395-4110-A7EFC884DAB1417D

FINANCIAL PLANNING TOOL FOR WATER UTILITIES (FPTWU) ... The result of the municipal water tariff reform is long-term sustainable development of the ...

www.oecd.org/document/43/0,2340,fr_2649_34343_2389355_1_1_1_1,00.html

Municipal Financial Tools for Planning and Development—It describes a number of municipal financial and planning incentives that. encourage redevelopment, revitalization and improvement of existing ...

www.mah.gov.on.ca/userfiles/page_attachments/Library/1/2566879_financialtools_e.pdf

Municipal Financial Management and Credit worthiness—Key components of municipal financial management. Planning – perspective and medium term; Budgeting (recurrent, development and revenue) ... PPT presentation

info.worldbank.org/etools/docs/library/117196/sloga/docs/sloga/ModF-EN-PP.ppt

Government Finance Officers Association - City of San Clemente, California's Long-term Financial Plan ...

www.gfoa.org/services/df/budget/index.shtml

PPPUE: Tools for pro-poor municipal PPP: The plan should outline how the municipal management intends to identify, recruit or promote ... The financial plan is a key component of the business plan.

www.pppue.undp.org/toolkit/MOD142.html

The Institute for Urban Economics—The treatise closely scrutinizes economical, legal and social aspects of introducing the long-term financial planning for municipal budgeting. ...

PART TWO: MANAGEMENT TOOLS

PURPOSE

Budget making and the entire financial management process in a LG depend on realistic revenue and expenditure forecasts. These forecasts are important not just to prepare next year's budget, but also to formulate the multi-year capital plan and to guide long-term planning and economic development efforts. Forecasting begins straightforwardly enough with the collection of current data from the LG itself and elsewhere, and the analysis of that data using standard statistical formulas and computer programs.

The process gets more complicated, however, because of many factors such as changes in central government requirements, the economy, and in community needs and expectations on both the revenue and expenditure sides. Further complicating the process is the need to make assumptions: assumptions about the way data is collected and compiled, assumptions about the right statistical techniques to use, and assumptions about the local effects of forecast events including how people, businesses and the economy will respond to them. Most difficult of all is the choice of policies relative to the assumptions. The challenge for the LG manager is finding the right balance between the realities uncovered through data analysis with the perception of politicians that conditions are much better, or worse, than the basic data suggests based on the particular axe they might be grinding at the time.

This workshop is intended to provide a working understanding of financial forecasting, emphasizing the forecasting process as a basis for making realistic and responsible financial decisions in an uncertain environment.

Don't forget to look back at the Learning Applications! Many of them can be easily adapted for group exercises and may be more appropriate for persons who are just being introduced to the concepts of financial planning.

CONTENTS

A brief description of each learning activity is shown below with an approximation of the amount of time required. If you wish to change the order, to omit something, or to add training material of your own, feel free to do so.

2.1 WARM-UP EXERCISE: A FINANCIAL PLANNING INVENTORY

Participants complete an instrument that identifies the extent and areas of financial planning/forecasting in which their LG is currently engaged. It also provides an opportunity to set priorities for action. (45 minutes)

2.2 TRAINER PRESENTATION

Brief concept presentation based on the preceding essay that describes the value and role of continuous, systematic financial planning and forecasting. (30 minutes)

2.3 EXERCISE: REVENUE ESTIMATING

Participants use figures and a seven-step trend projection process to derive an annual revenue estimate from a set of figures provided by the instructor. (60 minutes)

2.4 EXERCISE: INCREMENTAL EXPENDITURE FORECASTING

Participants practice using an incremental approach to prepare an expenditure plan that calls for progressive improvement in services within constraints imposed by policy. (120 minutes)

2.5 CASE STUDY: THE FINANCE MANAGER'S DILEMMA

Participants read a case that illustrates the complexity of forecasting revenues at a time of community change and uncertainty and decide what they would do as director of finance in the situation. (90 minutes)

2.6 CASE STUDY: THE POLICY MAKER'S DILEMMA

Participants use the case study from Exercise 4.4 and decide what they would do as a policy maker in the situation (90 minutes).

2.7 CLOSING EXERCISE: LEARNING TRANSFER

Participants reflect individually on what they have learned and make commitments to put it to use back home after the workshop. (30 minutes)

2.1 WARM-UP EXERCISE: A FINANCIAL PLANNING INVENTORY

TIME REQUIRED

45 minutes

PURPOSE

Instruments, like the one used in this exercise, are a valuable link between the concepts being discussed and the current practices of participants. Completing an instrument can help identify areas of strength and areas where improvement can be beneficial.

The purpose of this instrument is to help participants assess the areas of financial management in which their LGs are engaged in planning and forecasting and to set priorities for improvement.

PROCESS

Distribute copies of the Financial Planning/Forecasting Assessment Inventory (on the next page). Ask participants to complete the inventory, following instructions.

After participants have completed the inventory (approximately 15 minutes), ask them to select two or three priorities (high rated) areas of planning/forecasting that they feel their LG should begin using. When participants have made their selections, ask them to write down one thing that might be an obstacle to the implementation of planning/forecasting in each of these areas, and what could be done to minimize each obstacle. Ask volunteers for reports to end the exercise.

Financial Planning/Forecasting Assessment Inventory

INSTRUCTIONS

Each of the statements in the column on the left is a description of a LG's practice with financial planning and forecasting. Read the first statement. Then, to the right of the statement, check the block in one of the blocks under "level of activity" that most nearly describes the experience of your own LG. In the next column on "need for improvement," check the block that describes the amount of improvement that you feel should be made by your LG relative to this area of planning and forecasting. Continue with the other statements until you have checked one block in each category for all statements on the inventory.

Evidence of financial planning and forecasting	Current level of activity				Need for Improvement		
	Never	Infrequent	Occasional	Continuous	Low	Moderate	High
POLICIES AND GOALS							
1. The governing body has adopted a written policy on financial planning and forecasting.	—	—	—	—	—	—	—
2. They use the policy when deliberating and decision making.	—	—	—	—	—	—	—
FINANCIAL PLANNING							
3. Financial planning is used in preparing the annual budget.	—	—	—	—	—	—	—
4. Financial planning is used to perform an annual financial forecast.	—	—	—	—	—	—	—
5. Financial planning is used in setting priorities for capital investment projects.	—	—	—	—	—	—	—
6. Financial planning is used in making debt management decisions.	—	—	—	—	—	—	—
7. Financial planning is used to monitor financial trends.	—	—	—	—	—	—	—
8. Financial planning is used in conjunction with preparing strategic plans.	—	—	—	—	—	—	—

9. Financial planning is used in conjunction with preparing economic development plans.	—	—	—	—	—	—	—
FORECASTING							
10. A multi-year financial forecast is prepared and updated annually.	—	—	—	—	—	—	—
11. The financial forecast is prepared for management use.	—	—	—	—	—	—	—
12. The financial forecast is used by the governing body as well as management.	—	—	—	—	—	—	—
13. A formal forecast document is prepared.	—	—	—	—	—	—	—
14. The forecast includes financial projections for a 3-5 year period.	—	—	—	—	—	—	—
15. The forecast includes all major sources of revenues.	—	—	—	—	—	—	—
16. The forecast includes all major categories of expenditures.	—	—	—	—	—	—	—
17. The forecast includes all local government funds.	—	—	—	—	—	—	—

2.2 TRAINER PRESENTATION

TIME REQUIRED

180 minutes

PURPOSE

This presentation is to provide participants with information and perspectives on the use of financial planning and forecasting to guide current and multi-year planning at all organizational levels.

PROCESS

Prepare the presentation based on information covered by the preceding essay on financial planning. Concentrate on making a case for the importance of continuous financial planning and applying it to all areas of financial management. Focus the presentation on what finance managers must know to choose and use various financial forecasting methods, emphasizing the inexact nature of the practice, and difficulties that will be encountered when applying it in politicized environments.

Outlined information on note cards may help you cover the information systematically and stay on schedule. Ask questions from time to time during the presentation as a check on participant comprehension and to hold their attention. Augment the presentation with visual aids including pre-printed newsprint sheets and overhead transparencies as a further aid to comprehension. If the technology is available, power point presentations can also be effective.

2.3 EXERCISE: REVENUE ESTIMATING

TIME REQUIRED

60 minutes

PURPOSE

This exercise is to provide participants with practice using the trend technique, a particularly relevant and useful method for estimating LG revenues.

PROCESS

Tell participants they will be practicing with a common method for forecasting LG revenues, called the trend technique. Explain that the trend technique is appropriate for forecasting revenues (or expenditures) that are not tied to economic conditions. In other words, the technique works best when the rate of change from year-to-year is not necessarily fixed but does show a fairly constant percentage change without significant annual fluctuations. The technique, for example, would be appropriate for estimating annual changes in fees and taxes, which are set at the discretion of the LG. On the other hand, it would not be appropriate for estimating shared revenues that are transferred from the national government.

Give each participant a copy of the worksheet on the next page. Ask them to read the instructions preceding the exercise, follow the instructions, and be prepared to report the results of the exercise at the end of 30 minutes. Participants could also work in small teams of 2-3 to complete this exercise.

Revenue Estimating Using the Trend Technique

INSTRUCTIONS

This exercise is designed to produce a revenue estimate as a starting point for the current year based on a straight-line extension of the trend established in prior years. There are seven steps in the exercise. Complete each step completely before beginning the next.

Step 1: For purposes of this exercise, we are providing hypothetical data on local taxes and fees presumed to come from a LG's end of year accounting records.

Forecast of a LG's Local Fees and Taxes for 20x7 (in millions) Using Six Base Years, 20x1-20x6

Revenue Source	20x1 Actual	20x2 Actual	20x3 Actual	20x4 Actual	20x5 Actual	20x6 Estimate	20x7 Projected
Local taxes and fees	27.4	28.5	29.0	30.4	30.5	31.6	_____
% Change from prior year	_____	_____	_____	_____	_____	_____	_____

Step 2. Analyze the hypothetical data provided (in the box) to ensure a constant percentage change or an absolute amount of change each year over the five years.

Step 3. Use the following formula to determine the percentage rate of change or growth rate of the hypothetical revenue between time periods,

$$g_t = \frac{(V_t - V_{t-1})}{(V_{t-1})} \times 100$$

where "g" equals the percentage growth rate of the revenue; "V" is the revenue and "t" is the period of time.

Step 4. To use the formula for multiple years, calculate the growth rate for each year, total the rates and divide by the number of years to produce an average annual compound growth rate. Enter the results in the box.

Step 5. To apply the growth rate to make next year's projection, convert the annual compound growth rate to a decimal by dividing by 100, add 1.00 and multiply that sum by the latest period amount to arrive at next period's projected revenue or expenditure. Enter the results in the box.

Step 6. Repeat the process for the next year, and the next, until the projected revenue for 20x7 is obtained. Enter results in the box.

Step 7. Given the information provided by the instructor at the start of the exercise, and the actual experience of just estimating the local taxes and fees example, which specific revenues in your LG do you believe can be reliably estimated using the trend technique? Enter these revenues on the lines below. Discuss with other participants in your group to see if they identified the same or similar revenues.

2.4 EXERCISE: INCREMENTAL EXPENDITURE FORECASTING

TIME REQUIRED

120 minutes

PURPOSE

This exercise is to provide participants with practice using an incremental approach to prepare an expenditure plan that calls for progressive improvement in services within constraints imposed by policy.

PROCESS

Tell participants they will be practicing with a common method for forecasting LG expenditures called “incremental expenditure forecasting.” Review the methods briefly by explaining that a finance officer provides the heads of various LG departments with their respective base budgets and asks them to calculate the cost of any added or decreased services, and to include detailed descriptions of these changes. These “incremental” service level changes or costs should take into account changes approved by governing body policy or mandated by a higher level of government.

Divide participants into small groups of between 5-8 people. Give each participant a copy of the worksheet on the next page. Ask them to read the fact situation including the details on road types, road restoration needs and road equipment ages and conditions. After reading these details, ask groups to prepare an expenditure forecast that projects progressive improvement in the road system over the next three years within the governing body’s fiscal guidelines. Tell groups to be prepared to report their expenditure proposals to one another at the end of 60 minutes. Conclude with a plenary discussion of this forecasting approach and explore reasons why participants may have come up with different conclusions in their calculations.

Note to the trainer: It will be extremely useful to adjust the monetary value of both the currency and the items that are included in the budget to make the forecasting exercise realistic and relevant. For example, there are still countries in the world where inflation has made the local currency relatively useless in relation to the same units of comparative currencies, i.e. at the time this was being written one Euro would purchase about 34,000 Romanian lei.

Expenditure Forecasting Using an Incremental Method

THE SITUATION

As finance director for a small LG, you have been asked by the CEO to submit an expenditure forecast for the next three years and to include a plan for the systematic improvement of certain services. One of the services specified by the CEO is road construction and maintenance.

The CEO tells you that the governing body is making 50,000,000 (in your country's currency) available over the next three years for capital investments or equipment purchases. The council also has agreed to hold down spending for administrative overhead, and to give priority to road construction and maintenance including related equipment purchases.

The existing road network in your town is as follows:

- Trunk roads = 10 kilometres
- Principal roads = 40 kilometres
- Minor roads = 104 kilometres (70 paved; 34 gravel)

The basic road network is adequate for current traffic volumes except for a major trunk road leading from the LG centre to the LG airport. In general, however, road maintenance has become a problem owing to under funding, undermining of paved surfaces in certain hilly areas from underground springs, and the deterioration of older streets in the downtown area. Also, some unsurfaced roads in the fringe areas of town are becoming impassable due to erosion.

Routine road maintenance costs in your country's currency/kilometre are estimated as follows:

	Trunk roads	Principal roads	Local roads
Cleaning drains, maintaining shoulders, etc.	60,000	30,000	15,000
Street lighting bulb and mast replacement	120,000	60,000	27,000
Street sign replacement	30,000	30,000	9,000
Grading (gravel roads)	-	-	9,000

It has been agreed, in principle that efforts should be made to restore road surfaces to a reasonable state of repair in the next three years. A survey has disclosed the following needs:

	Trunk roads (km)	Principal roads (km)	Minor roads (km)
Resealing	2	3	8

Resurfacing (asphalt)	3	11	18
Resurfacing (gravel)	-	9	15
Reconstruction	2	9	14
Need work	70%	56%	53%

Resealing and resurfacing are normally carried out with the LG's own employees and equipment. However, some work has been contracted out to private firms. Average comparative last year's costs in your country's currency per kilometre were:

	Resealing	Resurfacing (asphalt)	Resurfacing (gravel)
Trunk roads			
Direct labour	600,000	3,000,000	-
Contract	630,000	2,760,000	-
Principal roads			
Direct labour	450,000	2,250,000	-
Contract	418,000	2,092,500	-
Minor roads			
Direct labour	300,000	1,500,000	150,000
Contract	315,000	1,800,000	195,000

Road reconstruction is always contracted out. Average costs per kilometre are estimated at:

Trunk roads	7,500,000
Principal roads	6,000,000
Minor roads	3,600,000

The road department's fleet of vehicles and equipment consists of:

Vehicle	Unit replacement cost	Years in service	Average operating life (years)
2 dump trucks	1,500,000	1	5
1 paving vehicle	15,000,000	3	10
2 road rollers	3,750,000	10	10
1 bulldozer	3,000,000	9	10
1 road grader	2,550,000	9	8

Departmental and supervisory overhead costs pertaining to the road department's work are to be limited to 10% of operating and maintenance costs.

In addition to maintenance and rehabilitation of the existing system, a number of new construction projects have been identified as necessary over the next three years. These include:

1. Street construction in new residential and commercial areas:
 - Construction of 10 kilometres of principal road.
 - Construction of 35 kilometres of minor road.
2. Upgrading of street lighting:
 - 15 kilometres
3. New traffic signals at several major intersections:
 - 8 intersections

Place expenditure forecast in the space below:

2.5 CASE STUDY: THE FINANCE DIRECTOR'S DILEMMA

TIME REQUIRED

180-240 minutes (2-3 hours)

PURPOSE

This case study is to provide participants with insight on the use of forecasting to project the effect on a LG's revenues of changes in the national and local economy.

PROCESS

Distribute copies of Stack City's Sagging Revenues and ask participants to read the case. If possible, arrange to provide participants with copies of the case to read before the workshop.

After participants have read the case, divide them into small groups of four to seven. Ask each group to answer the questions at the end of the case.

After 90-120 minutes, reconvene the participants and ask for reports from each of the small groups. Discuss the various interpretations of the case and design improvement ideas.

Stack City's Sagging Revenues

Stack City is a small industry-dependent town of 28,500 people located in the country's largest steel producing region. Stack City is adjacent to a large central city that serves as the trade centre for the region and has attracted most of the region's retail activity. Stack City, however, is home to a major steelworks that employs 7,125 workers and is the city's largest employer. The steelworks occupies a vast 1500-acre complex consisting of coke ovens, blast furnaces, and rolling mills. In the valley separating the steelworks from the centre of Stack City are endless rows of LG-owned tenements that provide housing for steelworkers and their families and a major revenue source for Stack City's LG.

A nationwide recession is having a serious effect on the national economy but, so far, its greatest impact has been in other parts of the country. Local officials, concerned about general economic uncertainty and aware of the risks faced by a town dependent on a single industry, already have taken steps to diversify the city's revenue base. For example, to take advantage of Stack City's reputation as the region's steel capital and its location on a major highway that crosses the country, the CEO and other local officials have been instrumental in obtaining funding from the steelworks' owner for the construction of an LG-operated museum to house the owner's priceless collection of impressionist art. The museum, conveniently located near the highway, has become a popular tourist attraction. It has also become a stimulus for a thriving museum-related food and overnight accommodation businesses along the highway.

In recent months, the diversification strategy seemed to be working. Evidence of a generally strong business climate was encouraging news to local officials, and employment at the steelworks continued to be high. However, rather suddenly, a host of economic problems began to surface, taking the CEO and governing body by surprise. Planned construction for expanding the steelworks, including an additional blast furnace, was indefinitely postponed. This was followed by a request from management of the steel company to halt the remodelling of two large LG-owned tenement buildings that were being readied for occupancy by steelworker families. In addition, a private corporation halted plans for building a multi-storey housing complex after filing for their building permit. About the same time, the owners of several small businesses reported that quarterly sales were down significantly from the same period a year earlier. In addition, a similar decline in receipts from ticket sales was reported by the museum manager owing to far fewer visitors to the museum than expected. Something was wrong but local officials could not determine just what was causing the problem or how serious it was. LG officials knew little about the financial problems of local businesses and particularly the steelworks. Surprise and disbelief were the reactions of these officials to an announcement that one of the major mills at the steelworks was closing in sixty days leaving 715 employees out of work. It was obvious that the mill closing would have a profound impact on the community, but exactly what the effect would be on the Stack City budget was not certain.

The following table shows the adopted budget for the current fiscal year.

Stack City Actual and Budgeted Revenues and Expenditures (000s)										
	2011 Budget	% of total	2010 Actual	% of total	2009 Actual	% of total	2008 Actual	% of total	2007 Actual	% of total
REVENUES										
STATE SHARED										
Wage Tax	-	0%	-	0%	-	0%	-	0%	39,568	50%
Dependent income tax	17,860	20%	18,900	21%	18,369	22%	21,967	27%	-	0%
Legal persons (corps)	12,400	14%	12,600	14%	13,568	16%	14,580	18%	-	0%
Road tax	15,875	18%	14,400	16%	13,000	16%	12,960	16%	12,640	16%
TAXES & FEES										
Building taxes	14,100	16%	9,900	11%	6,549	8%	4,370	5%	4,365	6%
Property taxes	5,200	6%	5,135	6%	5,125	6%	5,026	6%	5,456	7%
Museum entrance fees	3,760	4%	1,800	2%	430	1%	-	0%	-	0%
LG ENTERPRISES										
Sale of LG property	8,460	10%	13,990	16%	13,325	16%	10,241	13%	5,000	6%
Rent (Housing)	10,795	12%	11,990	14%	12,600	15%	12,255	15%	12,155	15%
TOTAL REVENUES	88,450	100%	88,715	100%	82,966	100%	81,399	100%	79,184	100%
EXPENDITURES										
City administration	21,620	23%	24,014	27%	21,785	26%	21,538	26%	21,000	26%
Housing	17,860	19%	13,500	15%	12,456	15%	12,210	15%	12,000	15%
Environmental	13,160	14%	13,000	14%	12,790	15%	12,628	16%	12,123	15%
Local services	12,220	13%	11,780	13%	10,725	13%	10,660	13%	10,401	13%
Transportation	8,480	9%	8,253	9%	7,470	9%	7,385	9%	7,204	9%
Culture	5,640	6%	5,589	6%	4,980	6%	4,264	5%	4,000	5%
Subsidies to LG										
Enterprises	4,680	5%	4,268	5%	3,735	4%	3,739	5%	3,680	5%
Safety	4,150	4%	4,000	4%	3,560	4%	3,526	4%	3,445	4%
Body culture (Sports)	2,200	2%	2,100	2%	1,826	2%	1,936	2%	3,258	4%
Health	2,158	2%	2,010	2%	1,868	2%	1,886	2%	1,758	2%
Trade	1,417	2%	1,352	1%	1,071	1%	1,066	1%	856	1%
Other	435	0%	335	0%	738	1%	605	1%	33	0%
TOTAL EXPENDITURES	94,020	100%	90,201	100%	83,004	100%	81,443	100%	79,758	100%
EXCESS (DEFICIT) OF REVENUES OVER EXPENDITURES	(5,570)		(1,486)		(38)		(44)		(574)	
OTHER FINANCING SOURCES										
Bank loans & interest	5,545		1,496		-		-		515	
Surplus from prior yr.	25		15		53		97		156	
Total	5,570		1,511		53		97		671	
Total surplus	-		25		15		53		97	

Responding to the impending problems, Finance Director Gus Klimpt began an analysis of the city's financial status. The report disclosed that the city would probably lose revenue from several sources. The national government was supplementing its own budget by reducing the amount of shared taxes going to LGs by decreasing the allocation share to LGs for dependent income and business and road taxes. According to the finance department report, if existing government service levels were maintained, the LG would experience a substantial shortfall in the coming budget year.

The report suggested that the earlier estimates of revenue from business taxes owing to the start-up of museum related businesses were too optimistic. In addition, the expected revenue from museum tour fees and related concessions was equally overestimated. It became clear to Klimpt that Stack City was being affected by the national recession far more than he had originally believed possible. Because income falls during a recession, revenues derived from LG's share of the income tax falls as well. Declining construction at the steelworks and other businesses means fewer new families coming into the community and a commensurate reduction in the occupancy of city owned tenements and the rental revenue from that source. The following table shows recent revenue and other financing sources trends in Stack City by source.

Operating and Capital Budget Revenue and Other Financing Sources Comparison (000s)										
	Current Year				Prior Year			Second Prior Year		
	Adopted Budget	6 mo. Actual	% of Budget	Revised Estimate	12 mo. Actual	6 mo. Actual	% of Total	12 mo. Actual	6 mo. Actual	% of Total
STATE SHARED										
Wage Tax	-	-	0%		-	-	0%	-		0%
Dependent income	17,860	7,144	40%		18,900	9,450	50%	18,369	9,185	50%
Legal persons (corps)	12,400	4,960	40%		12,600	6,300	50%	13,568	6,784	50%
Road tax	15,875	7,144	45%		14,400	7,200	50%	13,000	6,500	50%
TAXES & FEES										
Building taxes	14,100	6,768	48%		9,900	5,841	59%	6,549	3,929	60%
Property taxes	5,200	5,200	100%		5,135	5,135	100%	5,125	5,125	100%
Museum entrance fees	3,760	1,450	39%		1,800	918	51%	430	225	52%
LG ENTERPRISES										
Sale of LG property	8,460	8,460	100%		13,990	5,876	42%	13,325	5,330	40%
Rent (Housing)	10,795	5,300	49%		11,990	5,995	50%	12,600	6,300	50%
TOTAL REVENUES	88,450	46,426	52%	-	88,715	46,715	53%	82,966	43,378	50%
OTHER FINANCING SOURCES										
Bank loans & interest	5,525	5,525	100%		1,496	680	45%	-	-	
Surplus from prior yr.	25	25	100%		15	15	100%	53	53	100%
Total	5,550	5,550	100%		1,511	695	46%	53	53	100%
TOTAL REVENUES & OTHER	94,000	51,976	55%		90,226	47,410	53%	83,019	43,431	52%

Klimpt knew that the nationwide recession already was affecting LG revenue, primarily because of the allocation reductions from the national government. The

mill closing would have an additional impact through the loss of mill and mill-related jobs and the loss of income from rent payments by families occupying city-owned tenements. Budgeted revenues for rental income has already been significantly reduced from the prior year due to the major renovations at the city tenement buildings. The impact on real estate tax income would depend on how many of the workers actually lived in Stack City.

After looking at the revenues, he turned his attention to expenditures. Of course, he would recommend reducing expenditures where possible during the current year, but the money budgeted for renovations at the city tenement buildings (Housing) had been contractually obligated in last month's council meeting. It was a major capital expenditure in this year's budget. In addition, there were numerous unfilled positions in the City Administration budget, resulting in only 40% of monies expended to-date. The following table shows all of the current and prior year expenditures.

Operating and Capital Budget Expenditure Comparison (000s)										
	Current Year				Prior Year			Second Prior Year		
	Adopted Budget	6 mo. Actual	% of Budget	Revised Estimate	12 mo. Actual	6 mo. Actual	% of Total	12 mo. Actual	6 mo. Actual	% of Total
City administration	21,620	10,486	49%		24,014	12,055	50%	21,785	11,539	53%
Housing	17,860	11,609	65%		13,500	6,480	48%	12,456	6,041	48%
Environmental protection	13,160	6,659	51%		13,000	6,435	50%	12,790	6,548	51%
Local services	12,220	6,354	52%		11,780	6,243	53%	10,725	5,148	48%
Transportation	8,480	4,231	50%		8,253	4,011	49%	7,470	3,735	50%
Culture	5,640	2,679	48%		5,589	2,755	49%	4,980	2,490	50%
Subsidies to LG	4,680	4,680	100%		4,268	4,268	100%	3,735	3,735	100%
Safety	4,150	2,158	52%		4,000	2,101	53%	3,560	1,780	50%
Body culture (Sports)	2,200	888	40%		2,100	840	40%	1,826	776	42%
Health	2,158	1,133	53%		2,010	1,050	52%	1,868	986	53%
Trade	1,417	751	53%		1,352	811	60%	1,071	475	44%
Other	435	372	86%		335	332	99%	738	139	19%
TOTAL EXPENDITURES	94,020	52,000	55%		90,201	47,381	53%	83,004	43,392	52%

Finance Director Klimpt found himself confronted with many more questions than answers. Answers to these questions, he believed, would come from the findings of an economic analysis needed to develop good revenue projections. Traditionally, Stack City had made revenue projections based on national government estimates, with adjustments derived from the finance staff's knowledge of local trends and business activity. At a recent workshop conducted by a LG assistance centre in the central city, Klimpt had been exposed to several sophisticated approaches to revenue projections. One of these, regression analysis, was said to be useful for showing the relationship between two variables over time and could be used to make short-term predictions for the future. Another, input-output analysis, was an effective way to analyze the economic impact of changes such as a mill closing.

Team Tasks

1. Using the analytical forecasting tools you have learned about in this chapter, and the information and data provided in the case study and spread sheets, make a series of six-month projections on the city's key revenue sources. Be prepared to report on what analysis you performed and the results of the analysis.
2. Based on these projections, your team is to prepare a list of three to five major recommendations on how expenditures can be cut to correspond to the budget shortfalls that are expected to occur within that six-month period.

2.6 CASE STUDY: THE POLICY MAKER'S DILEMMA

Note: This exercise is designed to be used with either groups of policy makers (elected officials) or CEOs, to increase their understanding of how to cope with the challenges of financial planning.

TIME REQUIRED

120 minutes

PURPOSE

Using the case study in exercise 4.5, Stack City's Sagging Revenues, participants will gain insight into the use of information and data for making policy decisions about how to cope with an impending shortfall of local government revenues.

PROCESS

Distribute copies of Stack City's Sagging Revenues (in Exercise # 4.5) and ask participants to read the case. If possible, arrange to provide participants with copies of the case to read before the workshop.

After participants have read the case, divide them into small groups of four to seven and tell each group that they have about seventy-five minutes to develop a group response to each of the following tasks:

1. Based on the information contained in the case study narrative and financial spreadsheets, develop a list of the most serious issues confronting the Stack City governing body.
2. Rate each of these issues in terms of their importance to the longer-term financial well being of the city, and the short-term urgency of taking action as a governing body. 1 = not at all important or urgent; 3 = somewhat important or urgent; and 5 = very important or urgent. Multiply your importance and urgency scores for each issue and put your issues in rank order based on the total of each score. (Note: The process of multiplying the individual scores tends to separate the most important and urgent from the less important and urgent.)
3. Based on the information from tasks # 1 and # 2, develop a suggested plan of action to discuss with your CEO, Finance Director, and other key city officials in an executive session.

Before they break into small task teams, ask them to prepare their responses on sheets of newsprint paper for presentation in plenary session.

Reconvene the teams in about one hour and fifteen minutes and ask for team reports. Discuss the various reports and summarize the lessons learned from this experience.

2.7 CLOSING EXERCISE: LEARNING TRANSFER

TIME REQUIRED

30-45 minutes

PURPOSE

This exercise is to help participants transfer the learning experiences of the workshop into their real-world activities as finance directors. The focus of this exercise is on raising expectations, engaging in realistic planning and making personal commitments. Most of the work is done on a personal basis with some interpersonal sharing.

PROCESS

Spend at least half an hour at the end of the workshop to focus the attention of participants on important learning and encourage them to continue experimenting with these ideas in their management activities. Begin by giving participants about fifteen minutes to work independently on a simple learning transfer questionnaire. When participants have completed the questionnaire, ask them to share quickly with the group two or three things they intend to do differently in their roles with respect to financial planning, to close the workshop.

Trainers note. It is generally agreed that the purpose of training is to improve the way people do things by showing them a better way. In fact, the success of a training experience can be measured by the amount of personal growth and change that takes place both during training and after the training is over.

Commitments to learning and change made at the close of a workshop can help participants overcome learning resistance in themselves and in the work environment. A trainer can help learners make a successful transition from the world of learning to the world of doing through a few simple planning exercises.

A Learning Transfer Questionnaire

Take a few minutes to reflect on financial planning and forecasting, the new ideas you encountered in this workshop, and how you feel about them. Then, in the space below, write a sentence or two to describe something interesting you have learned about yourself during this workshop.

Based on what you have learned about yourself and the many possibilities for change presented by this workshop, what two or three things do you intend to do differently that involve financial forecasting?

1.

2.

3. _____

Finally, what obstacles in yourself or in your work environment do you expect to experience during your efforts to implement these changes? What will you do to remove or minimize these obstacles?

Expected Obstacle

1. _____

2. _____

3. _____

How will you remove the obstacle?

1. _____

2.

3.

Citizen Participation

PART ONE —CONCEPTS, PRINCIPLES, AND STRATEGIES

SUMMARY

This essay examines ways that citizens interact with their local governments (LGs). We provide a definition of citizen participation and describe the benefits to a local government that establishes and uses citizen participation policies and techniques. We discuss obstacles to the use of these policies. We provide ten steps to involving citizen participation in resolving an issue. Finally, we provide a compendium of techniques that can be used by local governments to involve citizens in a timely and constructive way in the development and implementation of public programs.

This chapter is written for LG officials, managers, and policy makers. It does not attempt to provide a citizen's point of view towards dealing with LGs. Because some reviewers indicated an interest in Participatory Monitoring which focuses on citizens monitoring the LG, Appendix B: World Bank Information on Participatory Monitoring has been added to the chapter.

RELATIONSHIPS BETWEEN CHAPTERS OF THE SERIES

The following matrix shows the interrelationships between Citizen Participation and other chapters in the series.

	Citizen Participation
<i>Introduction</i>	The Introduction provides the framework for using the entire series.
<i>Trainer's Guide</i>	Provides guidelines for using the chapters to provide training.
<i>Financial Policy Making</i>	Financial policy making provides the framework for the opportunities for citizen participation. If participation is not required in policies then many LGs will not invite citizen participation into the financial decision making process.
<i>Financial Planning</i>	Financial planning is the long-term plan for where the community is going. Citizen participation in deciding the direction is essential.

<i>Evaluating Financial Condition</i>	Citizens have a stake in the financial health of their LG, even when they are not paying taxes or revenues directly to the LG. If the financial condition worsens then the quality of public services provided for citizen's will be impacted.
<i>Operating Budget</i>	The operating budget is a plan for the acquisition, maintenance and use of LG assets to deliver public services. Citizen participation in that decision making process is essential.
<i>Financing the Operating Budget</i>	The operating budget is a plan for the acquisition, maintenance and use of LG assets to deliver public services. Citizen participation in that decision making process is essential.
<i>Capital Investment Planning (CIP)</i>	The capital investment plan is a plan for the acquisition, maintenance and use of LG assets to deliver public services. Citizen participation in that decision making process is essential.
<i>Financing the Capital Investment Plan</i>	The capital investment plan is a plan for the acquisition, maintenance and use of LG assets to deliver public services. Citizen participation in that decision making process is essential.
<i>Accounting</i>	Accounting and reporting provide the method for holding LG officials and policy makers accountable..
<i>Performance Measures</i>	Performance measures help the LG ensure that its citizen participation process is effective and efficient and accomplishing the priorities and goals of the LG.
<i>Asset Management</i>	The largest investment a LG makes is in its assets. These include streets, clinics, water systems, fire trucks, etc. It is important that citizens participate in setting priorities for acquiring or building assets. It is equally important that citizens monitor the LG's use of its assets to ensure that they are being adequately utilized.
<i>Procurement</i>	Procurement is one of the primary ways of disbursing monies. Citizen participation can require that it be an open and transparent process.

INTRODUCTION

We recognize that basic or introductory concepts are relative—depending upon your background and frame of reference for both citizen participation and local government. Users of this material will range from those who have no knowledge of citizen participation principles or concepts to those who have a very sophisticated understanding. The following are our ideas of what represents the most fundamental principles and concepts needed to understand citizen participation in financial decision making at a beginning level.

BASIC CONCEPTS AND DEFINITIONS

CITIZEN PARTICIPATION FRAMEWORK

GOOD GOVERNANCE

The concept and principles of good governance¹ provide the foundation for citizen participation. Good governance has eight major characteristics. It is participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive and follows the rule of law. It assures that corruption is minimized, the views of minorities are taken into account and that the voices of the most vulnerable in society are heard in decision-making. It is also responsive to the present and future needs of society. Each of these is discussed more at length below.

Participation² by both men and women is a key cornerstone of good governance. Participation could be either direct or through legitimate intermediate institutions or representatives. It is important to point out that representative democracy does not necessarily mean that the concerns of the most vulnerable in society would be taken into consideration in decision making. Participation needs to be informed and organized. This means freedom of association and expression on the one hand and an organized civil society on the other hand.

Rule of law—Good governance requires fair legal frameworks that are enforced impartially. It also requires full protection of human rights, particularly those of minorities. Impartial enforcement of laws requires an independent judiciary and an impartial and incorruptible police force.

Transparency³ means that decisions taken and their enforcement are done in a manner that follows rules and regulations. It also means that information is freely available and directly accessible to those who will be affected by such decisions and their enforcement. It also means that enough information is provided and that it is provided in easily understandable forms and media.

Responsiveness—Good governance requires that institutions and processes try to serve all stakeholders within a reasonable timeframe.

Consensus oriented—There are several actors and as many view points in a given society. Good governance requires mediation of the different interests in society to reach a broad consensus in society on what is in the best interest of the whole community and how this can be achieved. It also requires a broad and long-term perspective on what is needed for sustainable human development and how to achieve the goals of such development. This can only result from an understanding of the historical, cultural and social contexts of a given society or community.

1 For further information on urban governance visit the UN-HABITAT website at <http://www.un-habitat.org/Campaigns/governance>.

2 For additional information see UN-HABITAT (2003) *Tools to Support Participatory Urban Decision-Making*.

3 See UN-HABITAT (2004) *Tools to Support Transparency in Local Government* for more information.

Equity and inclusiveness—A society’s well being depends on ensuring that all its members feel that they have a stake in it and do not feel excluded from the mainstream of society. This requires all groups, but particularly the most vulnerable, have opportunities to improve or maintain their well being.

Effectiveness and efficiency—Good governance means that processes and institutions produce results that meet the needs of society while making the best use of resources at their disposal. The concept of efficiency in the context of good governance also covers the sustainable use of natural resources and the protection of the environment.

Accountability is a key requirement of good governance. Not only governmental institutions but also the private sector and civil society organizations must be accountable to the public and to their institutional stakeholders. Who is accountable to whom varies depending on whether decisions or actions taken are internal or external to an organization or institution. In general an organization or an institution is accountable to those who will be affected by its decisions or actions. Accountability cannot be enforced without transparency and the rule of law.

These eight principles are the foundation upon which meaningful citizen participation sits. Where appropriate throughout this chapter, these concepts are reinforced within the context of citizen participation.

UN MILLENNIUM DEVELOPMENT GOALS

Additionally, we want to reinforce the UN Millennium Development Goals (MDGs) – which range from halving extreme poverty to halting the spread of HIV/AIDS and providing universal primary education, all by the target date of 2015.

Specifically, the goal on promoting gender equality and empowering women is emphasized at several points in this chapter to remind LG officials that citizen participation includes ALL citizens, not just the wealthy or men, but also includes women and low-income persons.

WHY LG OFFICIALS AND STAFF SHOULD CARE ABOUT CITIZEN PARTICIPATION

Within the good governance framework, following are specific reasons that LG officials should involve citizens. By local government officials we mean elected and appointed officials as well as local government staff personnel. These are some reasons why local government officials should make citizen participation an integral part of their financial management responsibilities:

- To ensure that all citizen participation legal requirements are met in the most effective manner i.e., hold public meetings.

UN Millennium Goals	
1.	Eradicate extreme poverty and hunger
2.	Achieve universal primary education
3.	Promote gender equality and empower women
4.	Reduce child mortality
5.	Improve maternal health
6.	Combat HIV/AIDS, malaria and other diseases
7.	Ensure environmental sustainability
8.	Develop a global partnership for development

- To educate and provide support, thus legitimizing the local government's decision-making processes.
- To provide decision makers with new insights and solutions to local government problems including complex finance and budget issues, i.e., priority setting.
- To meet and respond to the needs of citizens. All citizens, including women and low-income persons.
- To advise elected officials on appropriate techniques to solicit public input in public policy related matters.
- To anticipate and be prepared for the time when citizen participation is the norm rather than the exception.
- To provide leadership and advice to other local government officials about techniques used in meeting citizens' information needs.
- To effectively communicate financial information to the public, businesses and community organizations.
- To serve as a means to get tangible work from volunteers to support local government financial and other activities.

DEFINITIONS

Citizen participation is any process through which citizens influence public decisions that affect their lives and the lives of other citizens. The participation can be active as when citizens interact with their elected officials or the staff of a local government to influence a public policy decision. Or the participation can be comparatively passive as when citizens simply attend a public meeting to receive information on the status of a new government program or when they show up to vote at an election. The most effective citizen participation brings people together to learn and discuss as well as to give their input, and these opportunities are particularly useful for building a consensus that can be a meaningful guide for government action. The focus of this chapter is on citizen participation in the financial planning and decision making processes.

Stakeholders - those individuals and groups who are most directly concerned with issues and have a "stake" or "claim" to the decision to be made regarding that particular issue.

A concept underlying every democratic society is that those who are affected by public decisions have the right to participate in making those decisions. In fact, in a democratic system it is fair to say that it is the public that determines where it wants to go, and it is the role of the elected representatives of the public and their staffs to get them there. Citizen participation is an affirmation of every citizen's right to have a voice in government and government's duty to find opportunities to inform, educate and involve citizens in meaningful ways in the process of public planning and decision making.

Openness in or access to the public policy decision making process is a fundamental concept of a free and democratic society. Openness means that decisions should be made, not "behind closed doors," but "out in the open." The intent is the expression of both a real and symbolic principle that all interested citizens will be informed and encouraged to dialog with their public officials toward more enlightened

public decisions. Denied this right and opportunity, citizens who have an interest in local government will lose it and even become cynical about their elected leaders and the role of government generally. In many democracies, the principal of citizen accessibility to the activities of local government is so important that guarantees of access are written into “open meeting” laws. Where such laws are enacted, they assure citizens notice of and access to meetings of governing bodies and other public bodies except under conditions that are enumerated in the law.

For those countries undergoing decentralization from the national to the local government level, the issue of citizen participation may be especially challenging. This is a time of tremendous change for both the national and local government personnel. Local governments in this situation must deal with a change in the mindset of personnel at the national level as well as with new expectations from citizens at the local level.

National government personnel may resist sharing decision-making power with local officials. Others insist on a standardised approach insisting that all local governments deal with citizen participation identically—not allowing for the differences between local governments and the various cultures that may exist throughout the country.

Local government appointed and elected officials may have a lack of knowledge on how to involve citizens or even may not be interested in getting citizen input for public policy issues. On top of all of this, citizens have new expectations for what the local government can accomplish that may be unrealistic in the short term. Citizens may become cynical if the local government does not appear to want their involvement in decision-making. Hopefully, this chapter will offer ideas for encouraging citizen input in a variety of ways.

PUBLIC INFORMATION AS PARTICIPATION

When a public notice is posted or distributed, or citizens meet to learn about a new government program, a local government is engaging in citizen participation. Any effort by a local government to inform or educate citizens is important, for meaningful citizen participation depends on an enlightened public. In order to give informed comments and feedback and play a meaningful role in decision making, citizens must understand the issues. Citizens cannot evaluate alternatives intelligently unless they are adequately informed.

There are two types of information that a local government might provide to help citizens participate more effectively. The first type of information is to furnish citizens with details on a specific issue, program or activity such as a change in policy on public procurement, review of the annual budget or specific project included in the LG’s capital improvements program. The second type of information is rather general and more educational in nature as when a public official talks to a class of school children or explains the working of local government to a civic club, professional group or business organization. Whether specific or general in nature, a flow of timely and understandable public information is essential for citizens to participate effectively.

Examples

- Public hearings on capital improvements (investments) program
- Budget hearing
- Speeches for civic groups or school children
- Informational matters for businesses, educational institutions or community groups
- Required annual reports that provide information on local government activities

FACTORS THAT TRIGGER CITIZEN PARTICIPATION

When is the right time to involve citizens in the affairs of a local government? The answer to this question is easy enough—anytime the staff or governing body believes that the participation of citizens would result in a better outcome (e.g., a more informed decision, a better designed plan, a more voter-acceptable revenue package) than were citizens not involved. Shown below are some examples of how to involve citizens.

- Seek input from governing body-citizen based commissions to ensure the annual budget reflects the needs of the citizens.
- Ask citizens with financial backgrounds to evaluate various alternatives for raising revenue in terms of cost, fairness and public acceptance.
- Organize a group of STAKEHOLDERS to plan ways to resolve an issue of environmental sustainability concerning a chemical plant that is a historic generator of toxic waste but can provide a strong and needed boost to the local economy.
- Set up focus group meetings to find out how citizens feel about the privatization of a service previously provided by government.
- Conduct a survey to learn how the citizens feel about the need to impound stray dogs, cats and other animals.
- Create a resident committee to recommend two intersections among five with extremely high accident rates for the installation of traffic signals. There is only enough money for signals at two intersections.
- Create a citizens' task force to determine the causes, effects and offer possible solutions to reduce crime and vandalism among young people in the community.

WHO PARTICIPATES?

A well established principle of organizational change that applies to the activities of local government is that people tend to support what they help to create. Following this principle, it is important to involve in specific government issues those individuals and groups who are most directly concerned with those issues. Such concerned individuals and groups are sometimes called “stakeholders.” Citizen participation programs are more effective if they identify those individuals or groups that have a

stake in a decision to be made or a problem to be solved. Typically, these stakeholders, individuals or groups, consist of the following:

Organized interest groups—these are groups of individuals who share a common philosophical interest in an issue, and are willing to commit themselves to the “right” decision or outcome from their perspective (e.g., environmental groups, labour unions).

Individuals—persons who are personally interested in or have expert knowledge relative to a specific issue.

Underrepresented groups—those who are not prone to participate on their own and who are a part of the “silent majority” in any community.

Community organizations—these are individuals who organize to promote a common interest related to a particular area of public service such as public housing, condominiums or the district or community in which they live (e.g., tenant associations, cooperative housing associations, community associations).

Business and professional clubs/associations—these are organizations of businesses or business professionals that support and promote a strong and healthy business climate (e.g., chambers of commerce, professional and service clubs).

Political clubs—organizations that represent various political parties or party coalitions in a community.

Other public organizations—these include contributory organizations, educational institutions, NGOs, other LGs, other levels of state administration districts and special agencies within state administration.

CITIZEN ROLES IN THE PARTICIPATION PROCESS

The roles of individual citizens and citizen groups will vary by issue. In countries where the idea of citizen input is new, citizen interest must be nurtured and special attention paid to providing opportunities for citizen input. Some citizen groups may represent particular segments of the overall “public interest” (e.g., preserving green spaces and wetlands from the encroachment of new development). Some will work on behalf of the economic, political or social interests of their various constituencies. Local government officials can play an important role in discerning which interests need to be represented when addressing a particular public issue and seeing that as many of them as possible are present when the issue is being addressed. Local government officials may be the best equipped of all the parties to keep the focus on the real “public interest” that underlies any issue or discussion. Moreover, it is the local government that is most likely to be aware of the various legal and policy considerations that must be observed in reaching a decision. Shown below are descriptions of some citizen participation techniques or roles that citizens may choose or be asked to play.

Role	Issue or Activity
------	-------------------

Self-interest	Providing input on a specific topic like zoning, animal restraint laws, or the sale of an asset, like park land.
Advocacy	Citizen task force charged with examining a specific subject and to offer evidence supporting a recommendation.
Shared power	Community groups and boards gather facts and present information on technical issues based on citizens, academic, business leader or consultant input.
Expert resource	Persons who have firsthand experience provide information to enlarge the understanding of public officials about a problem or issue.
Service quality feedback	A sizable number of citizens asked to offer reactions and opinions about service quality or other matters that could affect decisions on the allocation of public funds.

SUMMARY OF CITIZEN PARTICIPATION TECHNIQUES

The term “technique” is used in this chapter to describe any method planned by a local government to inform, educate, or solicit the assistance of citizens in planning and decision making.

Note that these techniques can be used at a LG-wide or sub-LG level to get citizen participation.

Fifteen summaries of common citizen participation techniques are described in the following tables. Two types of techniques are identified: Type 1) techniques that are specifically designed to involve citizens in the decision making process; and Type 2) techniques designed to educate and inform citizens but not necessarily to obtain their ideas and opinions. More detail, including the advantages and disadvantages of these fifteen techniques, along with descriptions and examples of their use can be found in Appendix A: Citizen Participation Techniques.

Type 1 - Techniques	Definition/Purpose	Example
Public hearings or meetings	Formal structured hearing, usually called by the governing body	Meet legal requirements to inform citizens about the proposed budget
Town hall meeting	Informal assembly usually held in a recreation building, school, church, bank or other facility	Status report on capital improvements program in specific geographical area
Citizen opinion/attitude survey	Gathering information about citizens' attitudes without holding a group meeting	Reactions to a proposal to pay increased fees for cultural events

Focus group	Meeting of selected citizens to gauge the probable response of a larger group	Find out the nature and strength of citizen sentiment about a controversial local issue
Advisory committee and task force	Group of citizens appointed to provide advice on issue(s); may be on-going or, in the case of a task force, focused upon a single issue	Investment committee to suggest alternatives for investing unused cash
Boards and commissions	Groups of citizens appointed to provide control, management and maintenance of a specific function	Advisory board for review and evaluation of the annual budget process
Technology application (Cable TV, Internet)	Cable TV is an alternative to “over the air” TV; TV signal is sent through a coaxial cable to homes, apartments and offices	Live broadcast of the governing body meeting; posting of LG job openings
	Internet—large group of computers exchanging information; citizens can send to and receive information from the LG	Send electronic mail rather than phoning or physically going to LG hall
Community association/board	Group of citizens organized around a common interest or issue	Group formed to defeat a proposed fee increase for the use of a LG facility such as a recreation building
Community office	Funded and operated by the LG, this is a “satellite LG hall,” established to serve a geographical area where citizens can come to receive certain services	Services could include health care, social assistance, payment of fees, requesting police assistance

Type 2 - Techniques	Definition/Purpose	Example
Ombudsman	A nonpartisan public official who investigates people's complaints about government officials or agencies	Resolving a complaint over a code enforcement citation
Open door program (accessibility)	A method to encourage citizens to visit LG hall or a community office on a walk-in basis	Come in without an appointment to complain because your trash was not picked up this morning
Public information	Information provided in the form of press releases, interviews, pamphlets, etc.	Publication of a flier that describes LG health care services

Education programs and popular reporting	Direct information/education programs that provide citizens an opportunity to meet face-to-face with their elected representatives	Speech to school children about the budget
	Popular reports are easy-to-understand summaries of the LG's financial condition and achievements	Use of graphs to demonstrate where financial resources were spent in the past year
Citizen service request office (complaints, suggestions and information)	Centralized clearinghouse established to receive and respond to citizen requests for assistance and information	LG representative acts as an agent for the citizen to refer a payment complaint to the department concerned, and reports back to the citizen with the result
Media relations	Interaction with the media (newspapers, radio and television)	Press release written and submitted to the press on the LG's proposed capital improvement program

WHICH CITIZEN PARTICIPATION TECHNIQUE TO USE?

A strategy for selecting a citizen participation technique is to focus on the purpose to be achieved by involving the citizen. Typical purposes are to:

- Inform the public about local government initiatives and keep them informed as they take part in the decision-making process;
- Educate the public about the rationale for a local government initiative, or the advantages and disadvantages of alternatives;
- Solicit information from the public to augment other sources of information;
- Consult with the public to learn what they know and how they feel about a local government initiative;
- Involve the public in planning to develop program goals, strategies and visions for the future;
- Obtain feedback from the public about the impact of a local government initiative on them or their neighborhood;
- Provide feedback to the public on the impact of local government initiatives in general and follow-on activities; and
- Involve members of the public directly in decision making through participation in the activities of ongoing boards, commissions, and committees.

The following table shows which citizen participation techniques are best suited for attaining each of these purposes.

Matching Citizen Participation Techniques to Purposes

Technique	Inform	Educate	Solicit	Consult	Plan		On-go-ing
Public hear- ing	•	•	•	•			
Town hall meeting	•	•	•	•		•	
Opinion survey	•		•	•		•	
Focus group	•		•	•		•	
Advisory committee	•	•	•	•	•	•	•
Boards/com- missions	•	•	•	•	•	•	•
Cable TV Internet	•	•	•	•		•	•
Community assoc.	•	•	•	•	•	•	•
Community office	•	•	•	•	•	•	•
Ombudsman	•	•	•				
Open-door	•	•	•				
Public infor- mation	•	•					
Education programs	•	•					
Citizen serv- ice office	•	•					
Media rela- tions	•	•					

Techniques of citizen participation are sometimes compared according to the intensity of involvement and the degree of impact their participation might have on government policies and programs.

Citizens' Participation: An Example from the City of Trnava, Slovakia

Around the middle of the 4-year election term, the mayor of the City of Trnava held meetings with citizens of particular constituencies. To prepare for these meetings:

- Posters about the meeting were placed on notice boards and other places normally used to publicize notices;
- Leaflets were mailed to individual constituencies;
- Invitations were issued through regional radio stations, regional newspapers, and the municipal radio and cable television stations.

The mayor's staff reserved the meeting rooms, designated seating arrangements for elected representatives to receive input from the citizens, supplied attendance sheets and arranged for other details to encourage citizen participation.

A structured program was prepared for the meeting which basically guided all the meetings and proceeded as follows:

- Introduction of the mayor and other elected representatives, i.e., deputy mayors and councillors for a particular constituency;
- Introduction of leading LG officials and directors of municipal companies stating areas of their responsibilities;
- Mayor's introductory address lasting approximately 20-30 minutes;
- Discussion time with individual speakers asked to give their names;
- Municipal office workers recorded citizen questions and comments according to their responsibility;
- Where possible, questions or comments were responded to immediately. Where this was not possible to do at the meeting, citizens were informed subsequently in writing.

SPECIAL NOTE ON IMPORTANCE OF CITIZEN PARTICIPATION TO FINANCIAL MANAGERS

If you are a financial manager, you probably feel most comfortable when you are working with systems, numbers, and processes. As a result, the prospect of voluntarily interacting with the "public" may be a bit unsettling. To minimize or exclude public participation in financial planning and management, the argument is sometimes heard from financial managers that involving citizens is too expensive and time consuming. Besides, continues the argument, citizens lack the necessary technical expertise and sometimes become emotionally involved in issues rather than detached and rational. Do these arguments sound familiar?

We want to introduce you, as a local government financial manager, to another way of thinking about citizen participation. We don't need to remind you that the business of financing local government gets more complicated all the time. The most astute financial managers are constantly looking for new ideas and resources they can use to help them cope with this growing complexity. In any community there are citizens with extensive backgrounds, responsibilities and financial credibility in

business, banking, or the non-profit sector. There are also citizens who may have no financial background but who may have an intelligent, common sense way of approaching issues. These citizens are accessible to you and deeply interested in being of help inasmuch as they have a vital, personal stake in the fiscal soundness of their community.

In financial management, the most common opportunity for citizen participation occurs with the discussion and adoption of an annual budget. But there are many other areas where public input can be helpful, such as establishing principles or rules for community property fund management, establishing purchasing and payment guidelines, serving on revenue and investment commissions, gathering community support for capital investment programs or general development programs. In other words, you can be a better financial manager to the extent you recognize and take advantage of the expertise that exists all around you in your community.

But there are other reasons for involving citizens. Not involving them in the affairs of local government can have grave consequences in a democratic society where people expect an opportunity to be heard and to exercise their influence. Leaving them out risks losing their confidence in local government, possibly causing them to withhold their support for important public improvement proposals. And it may even lead citizens to begin undermining government programs either by passive inaction or direct confrontation.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

This Learning application is designed to help you think about citizen participation in all those other financial management situations from your unique role in local government, i.e. policy maker, CEO, finance manager, and department head. This may be a bit more challenging so here's an example. As the head of the public works department, you believe you can cut the costs of trash collection by scheduling special pickups of large items at certain times of the year. But, you aren't sure the citizens will agree with your proposed plan.

From my role perspective, here are the things we already do to involve citizens in those activities of our local government that involve finances in one way or another.

And, here are some ways we can involve the citizens even more effectively in these activities.

In addition, I believe we could do even more and here are my ideas of what might be done to increase citizen participation.

More importantly, I plan to take the following actions to get my ideas “on the table” for discussion and possible action.

INVOLVING CITIZENS

Around the world, public officials share a common complaint about citizen participation. A mayor recently lamented. “I really would like to improve our citizen participation, but our citizens don’t want to be involved. We hold public hearings, but no one shows up.” Citizens, on the other hand, complain about the way we operate down at LG hall.

On the other hand, how many times have you heard a conversation like the following—whether you are in Asia, Africa, Europe, South America or elsewhere in the world? “Did you hear—those people down at LG hall are talking about balancing the budget this year? That means another campaign to raise taxes. I paid more taxes this year than ever before, and now they’re going to try to talk us into another increase. If I was on the governing body, I’d show them how to live within their means.”

Between these two extremes of perceived apathy and vocal hostility there is a middle ground. There is a place for the responsible involvement of informed and concerned citizens in their local government. But finding the place is challenging for the local official. Have you ever wondered, for instance, why people don’t get involved in the process of local government? The following table provides a few reasons from the citizen’s perspective.

Reasons Citizens Don’t Participate

- People may not be able to attend a public meeting, hearing or citizen participation event on the scheduled date. They may have to work or have other commitments. Some locations may be difficult to get to without a personal car or may be at a location that is considered unsafe.
- People may not have heard of a public meeting or read the published notice on the sign boards or may not have heard or read about it because of short notice.
- In some cases, otherwise interested citizens may find it difficult to get in touch with the staff person in charge for more information about the meeting and, failing in the attempt, may decide not to attend.
- In many cultures, womens’ and low-income persons’ opinions, concerns and values are not considered important. They may actually be excluded from participation in decision making.
- People feel uncomfortable when they don’t know much about the issue to be discussed at a public meeting or what might be expected of them as meeting participants.
- People with little or no experience as participants in public meetings may be suspicious of government’s intent for inviting them as manipulative and self serving.
- In a neighbourhood meeting, people may be reluctant to be the only ones expressing a particular viewpoint, especially if taking the position might make them unpopular with neighbours, friends, associates, clients or employees.
- People are reluctant to spend time discussing and debating issues when they believe the final decision has already been made.
- People do not like to supply information if they feel that their contribution will not be valued or seriously considered.
- Some local governments have attempted to address these misgivings about citizen participation by encouraging citizens and groups to get involved in local government and community projects. This chapter identifies many ways that local officials can use to inform and educate citizens about the public issues that face their communities and to involve

citizens meaningfully and productively in public planning and decision making.

TEN STEPS FOR CONNECTING CITIZENS TO YOUR LOCAL GOVERNMENT

The following ten step process is primarily written for the elected public official—but it is also an excellent resource for the mayor, department head or finance manager. Regardless of your role in the local government, the path to involving citizens in local government is always challenging.

One of your missions as a local government official is to empower citizens, including women and low-income persons, to participate in the planning and decision-making of their local government. To do this, consider using the following ten-step process—especially for resolving important issues or issues where there may be considerable disagreement in the community.

STEP 1: IDENTIFY THE ISSUE: DEFINE IT IN ITS BROADEST TERMS

Take the broadest possible view of the issue. Ultimately, stakeholders will clarify the problem and help to further define and refine the issue. To broadly define the issue:

1. Forecast possible scenarios that may result from different decisions on the issue. For example, “If this occurs, then this will happen,” or “If we take action now, we can resolve this issue less expensively or prevent a larger or related problem from occurring.”
2. Be able to explain the issue in non-expert terms. Most people do not understand technical jargon in areas other than their own field of expertise. Use of complicated, technical language can often make citizens feel intimidated.
3. Put the issue in the context of how relevant it is to people’s daily lives or to the lives of future generations. (If it is not relevant, perhaps it is not an issue to be concerned about.)
4. Identify ways to inform the public so that they are able to see all sides of the issue and its potential impact on the whole community. Citizens need your help to see beyond their own personal interests or viewpoints and take into consideration the needs and perspectives of others.

Concern yourself with only those issues that actually have or will have an impact on people’s daily lives.

STEP 2: IDENTIFY THE STAKEHOLDERS WHO STAND TO WIN OR LOSE

Identify the potential winners and losers for the issue. Who will be affected by the service you are considering cutting or the zoning policy you want to amend? Ensure that everyone who may be affected by the decision is included in the decision-making process.

1. Create a list of obvious members of the community (external) and your local government personnel (internal) who have a stake in the issue.
2. Now make a list of anyone else that may be affected. Bring together a small group to brainstorm with you. Include colleagues, members of the management team or the governing body—those most familiar with the issue. Using a flipchart, write across the top, “Who else will be affected by the issue?” and then record the various answers. Remember that in brainstorming all answers are seriously considered and recorded.

Connecting citizens to local government requires the inclusion of everyone. No one affected by an issue should be left out of the decision-making process.

STEP 3: IDENTIFY THE VALUES AND BELIEFS HELD BY THE STAKEHOLDERS

Citizens in the community may have different values based on age, social norms, culture or religion. One example of this is whether women are included in decision making. These differing values can contribute to different perceptions and expectations from citizens. An issue that is charged with emotion can lead to highly charged and hostile confrontations if it is not handled carefully. By first identifying the values you will likely encounter, you can identify where there may be clashes, and will be better able to choose the most appropriate forum for involving stakeholders in the decision-making process.

Although citizens hold a wide variety of values as individuals, there usually are a certain core cultural values held by a majority of citizens of any community. To ensure that ALL citizens of the community are included, you may have to challenge those core values. Again, an example is the way that women are consistently left out of the decision making process in many cultures and countries. IN some societies the core values say that only men need be consulted and that they can also speak for womeb so there is no need to ask women what they think or want. Understanding core values or current changes in core values can help you assess with greater accuracy why and how your citizens may react to certain issues. It will also alert you to difficulties you may face in achieving consensus and promoting a sense of community. It is still essential that as a representative of the LG you strive to include ALL persons in the community in citizen participation.

Be comfortable with ambiguity. Changing values means there will be times when there are not clear or absolute ways to connect citizens to local government.

STEP 4: IDENTIFY THE POTENTIAL OUTCOMES

Use the small group to brainstorm again with you. Using a flipchart, write across the top, “What are the potential outcomes on this issue?” and then record the various answers. Remember that in brainstorming all answers are seriously considered and recorded. As a secondary part of the exercise, for each of the potential outcomes, record the needs being met and the pros and cons and impacts on the various stakeholders.

You will probably need to let go of the solution you personally hoped to achieve. Your major role as a local official, finance manager, or department head is to facilitate public discussion and set in motion processes for discussion and deliberation, you will not be able to serve effectively as a bridge to the public's diverse views and ideas if you hold too tightly to your own solution. Identify the needs your solution addresses and include them in the public discussion. There may be many other stakeholders who have the same needs; there may also be many different solutions that address those needs.

STEP 5: IDENTIFY AND BALANCE CONCERNS OF EXPERTS, SPECIAL INTERESTS, AND THE MEDIA

Experts are an important part of the process since effective decision-making requires adequate information that is correct. Be careful about relying on the experts as both sources of information and determiners of the solution to the issue. Your role as an elected official is to balance the expert's view with the view held by the public.

One of the major problems citizens have with local governments is their perception that special interest groups have too much power and influence over the decision-making processes. Special interests are a critical part of society, but theirs should not be the only voices heard on issues.

In many countries, the media may play a large role in framing issues for local government public consideration. Be aware that many journalists approach local government issues from a conflict or confrontation perspective—focusing on confrontational situations and sensationalism.

STEP 6: IDENTIFY THE ETHICAL ASPECTS OF THE ISSUE

As you consider an issue identify any ethical considerations—issues of fairness, justice or honesty—that might affect how an issue is discussed or resolved. Each country and various cultures within a country has its own standards for ethical behaviour and these should be considered when identifying major stakeholders, how you select forums for dialogue and citizen participation and even in what issues to identify for discussions. Also challenge those if needed to ensure that all citizens, including women and low-income persons are included.

STEP 7: IDENTIFY OBSTACLES TO RESOLUTION

It may be difficult to reach a smooth or quick resolution to an issue confronting your community. Following are some of the reasons:

- Complexity of the issue: The issue may be multifaceted and interwoven—the answer to one issue may require work on two or three other issues. This can make people feel overwhelmed and citizens may prefer to avoid issues altogether.
- Special interest groups: Opposing values can lead to conflict, confrontation and disengagement.

- Lack of good information: Without an adequate and comprehensive presentation of issues, it is difficult to raise the public's consciousness about issues or to help citizens in weighing the various options for resolution.
- Lack of understanding of the issue(s): If citizens lack accurate or complete information or do not educate themselves about an issue, they will not be prepared to participate in resolving the issue in an informed way.
- Local government obstructions: If your local government does not provide easy and open access to information or forums for resolution, or if your governing body or LG personnel are not trained in how to facilitate open discussion, citizens will perceive there to be too many obstacles from the local government.
- Over-reliance on experts: Citizens and governing bodies can feel inadequate and ill prepared in the face of experts. An expert who has used so much jargon that the audience is lost, bored, or both will often be met with silence. While not intending to do so, the expert can have the effect of disempowering the governing body, citizens and even the local government personnel.
- Lack of interest: If an issue is not thought to be relevant to the daily lives of citizens, the citizens will not likely be interested in it. They may appear to be apathetic and disengaged because they do not see how the issue affects them, their families, or their community.
- Lack of trust: This goes both ways. Citizens are often cynical about the processes of government or about the ability of those working in government to solve problems effectively. At the same time, local officials do not always trust the judgment of citizens and question the sincerity of the public in wanting to resolve issues for the common good.
- Mixed signals sent by those in power: Citizens are often told that one course of action will be taken while, in actuality, others steps are followed. When local officials do not, in effect, do what they say they will do, citizens become confused and cynical.
- Diverse points of view: Differing perspectives can slow down the resolution of an issue since confusion can arise over misinterpretations of comments made, definitions used, and feelings expressed.
- Lack of effective processes and leadership: Resolution depends on leadership that welcomes input and initiates processes that enable all stakeholders to work together effectively.

Your patience and perseverance will be needed to overcome the obstacles you are likely to encounter when working through an issue.

STEP 8: SELECT THE MOST EFFECTIVE METHOD / FORUM.

It is important that you take this step seriously and remain flexible. If one method does not work, try another one. In fact, you may WANT to try different methods depending on where the issue is in the decision-making process. Citizens should be provided with the opportunities to:

- Speak out

- Interact with local officials and other citizens
- Be involved in the formation of a resolution to the issue
- Be part of the action plan or solution
- Select a method that maximizes the amount and quality of dialogue among the stakeholders and increases the understanding of various stakeholder perspectives.

STEP 9: DECIDE WHAT ROLE YOU WILL PLAY—ACTOR OR OBSERVER

As a public official, your role will vary with the issue involved and the method of involving citizens in the dialogue. You will always plan an active role as a chief supporter of citizens working together to resolve issues. But, there may be times you will function in an indirect, neutral role as a facilitator rather than an active participant. The point of helping citizens to become problem solvers is so that local government staff and elected officials will no longer be the sole source of the solution.

STEP 10: DEVELOP AN ACTION PLAN: TIME FRAMES, BUDGET

An action plan provides a clear road map for what needs to be accomplished to effectively connect your citizens to the local government. The following table identifies the kinds of information that needs to be provided for each step or action item.. You can complete the plan on the basis of your specific community needs. At the end of the process you will need to evaluate and determine what to do differently in future processes to ensure that you are meeting your expected outcomes.

Connecting Citizens To Your LG Action Plan

Action item	Person(s) responsible	Resources Needed	Estimated completion date	Actual completion date	Expected outcomes	Method/ person responsible for monitoring outcomes
1.						
2.						
3.						
4.						
5.						
6.						
7.						
8.						
9.						
10.						

TIMING AND OTHER CONSIDERATIONS

Citizen participation initiatives require time and resources (personnel and operating) to be effective. Local officials should consider the following when planning a citizen participation program.

SCHEDULE OF EVENTS

- Develop a clear and concise schedule of events at the beginning of the project.
- Include major milestones and decision points in the schedule.
- Provide a variety of activities or ways in which citizens can participate.
- Communicate any scheduling changes to all interested parties as far in advance as possible. Try to communicate any changes in the same ways that the original information was provided.

LEAD TIME

- Allow enough lead time in the schedule for individuals and groups to get materials, review them and make plans to attend scheduled activities.
- Recognize that many community groups rely on voluntary resources and meet infrequently (i.e., monthly); therefore, internal communications between members may be slow. Large organizations may need time to circulate materials and coordinate responses.

HOLIDAYS

- Do not schedule citizen participation activities during seasonal holidays when prospective citizen participants are engaged in other activities.

SPEED OF DECISION MAKING

- Recognize that some organizations can make decisions quickly because of their organizational structure and staff capabilities. Others, such as community groups and neighbourhood associations, may not be able to make decisions without polling their broader membership. A group that needs more time to ratify a decision may feel pressured by the decision process to make a decision prematurely.

COORDINATION

- LG staff should coordinate citizen participation activities with all affected groups so that the burden is not transferred to the group. A group's volunteer resources are usually unable to handle the increased workload.

LENGTH

- Determine the length of the citizen participation process after considering all factors that go into the final decision.

A VALUABLE TOOL BUT NO PANACEA

Citizen participation is a tool for improved planning and decision making, and monitoring decisions to make sure that they are carried out. It should not be regarded as a solution to local government's problems but rather an important contributor to solving problems so that they stay solved. It is a complement to existing decision making processes, not a substitute.

When local government is isolated from the public, citizens may come to regard their officials with suspicion and mistrust. Breaking down these barriers takes considerable time spent in efforts to inform citizens, familiarize them with how government works and the issues it faces, and involve them in resolving problems that are of direct concern to them. Consistent efforts to reinforce the belief that citizen views and ideas are needed and wanted can help to overcome the cynicism and distrust that so often characterizes the relations of citizens with their public officials.

There are several ways to get maximum value from the involvement of citizens. As already mentioned, how citizens are used in planning, decision making, and monitoring depends on the objective or what is to be accomplished more satisfactorily with citizen input than without it. A group of neighbourhood residents, selected at random, might be a poor choice for a task force to develop criteria for the attraction of new businesses to locate in the community. However, they might be ideal for a focus group on increasing resident accountability for the health and safety of a neighbourhood. Find opportunities to encourage positive and healthy interaction among citizens, particularly when there is a climate of suspicion and distrust. Bring people together in familiar surroundings, make them feel comfortable, use simple language they can understand to explain the issues and what is expected of them, and convince them that what they are being asked to do is important and is expected to make a difference. Appendix D contains a detailed list of steps for planning and implementing a citizen participation program.

CITIZEN PARTICIPATION POLICY

The formulation of public policy is a local government's way of declaring its intent to commit itself and its resources to a specific set of principles and goals. Most local governments have no citizen participation policy and let citizens participate in governmental affairs only when necessary to satisfy legal requirements. For example, Slovak Republic law requires that "the municipal budget be published for at least 15 days in a way which is common in the LG so that the population can comment on it." Most countries have some legal requirement similar to the Slovak requirement for citizen participation in the budget decision-making process, but many do not include citizen participation requirements in other public policy areas of local government.

Laws requiring citizens to be invited to participate in some limited “live review” of the budget should be viewed as a starting point for much more extensive public involvement in governmental decision making. In other words, governing bodies should mandate citizen participation in all activities of local government as a matter of policy. The adoption of a statement of policy on citizen participation by the governing body is the public’s assurance that their local government is serious about citizen participation. The policy should require specific implementation procedures that all departments and programs are expected to follow. Such a statement should include, at a minimum, types of citizen participation, providing the public with information, and “open” meetings. (See Financial Policy Making for additional information on the development of public policies). The policy should be designed for local needs, prepared in writing, and legally adopted by the governing body.

GOALS OF A CITIZEN PARTICIPATION POLICY

A GOAL is a long term, attainable statement of intent for a local government. Goals should reflect a local government’s priorities and the community’s interests. In the case of citizen participation, the following goals, in some form, should be considered for inclusion in a policy statement on citizen participation.

- to ensure the best possible living environment for citizens;
- to encourage citizens to play an active role in caring for and enriching the community;
- to ensure the public has full and timely access to and influence on public policy and decision-making, assuring full disclosure and ready access to public information;
- to ensure equal representation for all interests in decision making processes, balancing different values and needs, including women and low-income persons;
- to foster trust among citizens, local government officials and staff;
- to develop a new, citizen-centred approach to LG governance.

POLICY IDENTIFIES WHEN TO INVOLVE CITIZENS

The policy should call for compliance with all legal requirements for citizen notice and hearing. Additionally, it should go much further and require initiating citizen participation activities at the beginning of any new decision making process when a issue will alter or influence government’s relationship with its citizens. Examples of issues to be considered for inclusion in a policy statement:

- health and welfare of citizens,
- the character of a neighbourhood or a district,
- public values or expectations,
- streetscapes (e.g., landscaping, trees),
- traffic, parking characteristics, and pedestrian movement,

- public safety,
- tax rate, fees or service charges,
- economic health and the sustainability of growth,
- levels of service (e.g., tram or bus transport)

CITIZEN PARTICIPATION IN BUDGET DECISION-MAKING POLICY ILLUSTRATION

Shown below are illustrative policy statements about the involvement of citizens in local government's annual budgeting process. Opposite each policy statement is a rationale for the policy.

Together these policy statements open the door to a variety of ways for citizens to become involved. We recognize that different countries are at different points on implementing citizen participation at the local government level. However, the allocation of local government resources through the budgeting process is an excellent first step to begin to get citizens participating and connecting with their local government.

Policy Statement	Rationale
The budget will be prepared in such a manner that citizens and elected officials have no difficulty understanding the local government's priorities.	One of the stated purposes of the budget is to present a picture for the citizens of the LG government's operations and intentions for the year. Presenting a budget document that is understandable furthers the goal of effectively communicating finance issues to both elected officials and the public.
In addition to required public hearings, the governing body or governing body commission will hold work sessions on the budget which will be open to the public.	Work sessions provide all citizens with a forum for meaningful participation in the budget process. They enable citizens to: obtain an understanding of the budget that cannot be acquired by the document itself, provide public input to the proposed budget, and to monitor the governing body's or governing body commission's changes to the proposed budget.
Copies of the proposed budget will be made available to citizens and elected officials prior to the work sessions.	Providing citizens with copies of the proposed budget in advance of the work sessions enables them to become better informed on the issues facing the governing body and the administration during the budget work session.
The local government will maintain a policy of full and open public disclosure of all financial activity.	Full and open public disclosure of all financial activity provides the public with assurance that its elected officials and administrators communicate fully all financial matters affecting the public.

A Sample Policy Statement on Citizen Participation

We, the governing body of xxxxxxxxxxxx, believe that:

All citizens, including women and those who have traditionally not had a voice in LG, represent an integral part of local government functions, programs and activities since they receive services and benefits of local government and elect local officials to represent them, and

Consulting with citizens on issues that directly affect them or their community at the beginning of the process represents a new approach to governance,

Participation in the local decision making process fosters trust among residents, elected officials and staff; It has been demonstrated that citizens involved in the decision making process play an active role in caring for and enriching their community:

It is the intent of this governing body, therefore, that:

Citizens will be provided timely information about decisions that are being considered by the local government and will be provided the opportunity to participate in the decision making process.

Citizen participation programs will be designed and conducted in connection with the establishment of new LG policies or significant changes to existing policy.

All local government departments, offices, agencies and staff will cooperate to the fullest extent possible by including citizens in decision making.

If questions arise, the need for citizen participation should be determined in consultation with those individuals, organizations, and other local governments that might consider the action significant.

Note: A policy statement such as this implies responsible judgment on the part of decision makers. For example, how big does a decision have to be to constitute a decision? How important does an issue have to be before it is considered "significant"? These are questions that should be addressed by local officials and the policy made more specific to meet each local government's needs.

LEARNING APPLICATION

POLICY MAKER X CEO X FINANCE MANAGER X DEPARTMENT HEAD X

One of the first places to test your local government's commitment to citizen participation is in the citizen's role in the annual budget process. This learning application is designed to help you look at this one important aspect of financial management (FM) and citizen involvement (CI). You'll have an opportunity to think about all the other aspects of FM and CI in a few moments. In this Learning application we want

you to think about the budget process from your own unique role perspective as a policy maker, CEO, finance manager, or department head.

From my role perspective, here are the things our local government already does to involve citizens, including women and low-income persons, in the annual budgeting process.

I believe our local government could improve these present practices by doing the following things.

I also believe we could improve the quality and frequency of citizen involvement in the budgeting process by:

BENEFITS OF CITIZEN PARTICIPATION

In summary, citizen participation benefits local government in many ways: aids decision making, increases understanding, cooperation, and appreciation of what

local government does, reduces conflict, generates support for the implementation of a project or community plan and makes local government more open to citizen problems, concerns and issues. Citizen participation is fundamental to a democratic society.

ELECTED OFFICIAL'S PERSPECTIVE

From the elected officials' perspective, citizen participation:

- Allows local government officials to make better decisions by bringing into the process a deeper and broader understanding of problems, issues and concerns.
- Increases chances of acceptance of government decisions and proposals if citizens have been given a voice in the process.
- Motivates individuals and groups to become more involved in their community, thereby spreading responsibility and accountability for what happens in the community over a larger number of citizens.

PUBLIC'S PERSPECTIVE

From the public's perspective, citizen participation early in the decision-making process:

- Increases understanding, minimizes conflict and create conditions for a wider public consensus in decision making.
- Ensures that their issues and concerns are heard and taken into consideration, thereby assuring that the overall public interest is better served. The overall public interest includes women and low-income persons.
- Provides assurances that their local government officials are open and approachable. When citizens perceive their government as open to them, they are more likely to gain knowledge and understanding of local government issues and, thus, become more able to assist in the resolution of these issues.

LOCAL GOVERNMENT STAFF'S PERSPECTIVE

From the local government's perspective, citizen participation:

- Brings insight on local issues to the forefront for consideration. These may come in the form of suggestions for improvement or problems that need to be solved.
- Helps identify the trade-offs between competing interests and viewpoints.
- Helps community districts develop a sense of local pride in their respective areas by gaining some measure of influence and control over the decisions that affect their areas.
- Assists the local government in establishing priorities and thereby promotes better financial planning and budgeting by allocating funds in response to identified community needs.
- Brings citizens and community groups with experience and expertise beyond that which exists in the LG organization into the process and thereby enlarges overall understanding of problems and provides a more accurate basis for decisions.
- Develops leadership and knowledge within the community—a critical ingredient of the democratic process. When citizens learn how local government operates, they are more inclined to want to be a part of the process.
- If the local government is doing a good job, people who are involved gain respect and appreciation and as a result will be more cooperative and supportive of local government. Citizen involvement provides an effective training ground for future elected officials.
- Produces tangible work (i.e., from volunteers) that directly benefits the community. Citizens contribute a significant number of volunteer hours in local governments in all parts of the world. For example, one LG in the United States calculates that 80,000 hours of work each year is attributable to the work of community volunteers.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

From your perspective as a policy maker, CEO, finance manager, or department head, think about all the obstacles you might encounter in getting citizens involved in your local government's financial management initiatives.

From my perspective as a _____ (fill in the blank), I either have encountered the following obstacles or barriers to greater citizen participation in our financial management initiatives, or would expect them if opportunities for citizen to participate are expanded.

Given these potential barriers, here are some ideas on how our local government can overcome them.

Looking at citizen participation from my own role perspective, I think our biggest challenge in achieving more meaningful citizen participation in the annual budget process is

And, here are some ideas on how our local government might increase citizen participation in the budgeting process.

Finally, here are the pros and cons involved in achieving more participation as it relates to my specific role as a policy maker, CEO, finance manager, or department head.

Note: We hope that this look at citizen participation from your own role within your local government will encourage you to have a discussion with others, such as policy makers, etc., to share your thoughts and ideas about this topic. This kind of shared learning application could result in significant breakthroughs in how your local government involves citizens, not only in the annual budgeting process but in other areas of financial management.

POTENTIAL OBSTACLES TO EFFECTIVE CITIZEN PARTICIPATION

There are potential obstacles to the implementation of an on-going effort to involve citizens in local government activities. Nevertheless, one of the basic cornerstones of a democracy is citizen participation and we encourage you to find ways to overcome the following obstacles.

CITIZENS CAN CHALLENGE YOUR ESTABLISHED WAYS OF DOING THINGS.

The involvement of citizens may be resisted in governmental activities that in the past were the sole responsibility of elected officials or bureaucrats. The challenge is most pronounced where the involvement of citizens results in a shift toward decentralized policy making authority and empowering neighbourhood districts at the expense of a traditional political power base. A word of caution for local governments that have not involved citizens extensively in the past: move slowly into citizen participation by first involving citizens in areas of activity that pose little threat to existing power bases. Of course the downside to this is that you may never see change. You will need to find a balance.

MANAGERS AND ELECTED OFFICIALS NEED TOOLS ON HOW TO PRESENT THE IDEA OF CITIZEN PARTICIPATION

In countries where citizen participation is a new idea, managers and elected officials may not have the knowledge or skills to know how to effectively involve citizens in the decision-making process. Based on the ideas presented in this chapter and other information available on citizen participation, local government managers should take the initiative to hold workshops and community meetings on the basics of civic participation. Like all new processes in good governance, it is important to build a base of understanding and commitment to citizen involvement before undertaking major changes in managing financial responsibilities.

THE POTENTIAL OF UNREASONABLE EXPECTATIONS

Don't expect too much from citizen participation too soon. It is no guarantee that public decisions reached in collaboration with a representative citizens' group will satisfy the expectations of all citizens. Citizen participation only permits different views to be aired and discussed through an open process. As a rule, final decisions will be made by the mayor and governing body. While there is no magic in citizen involvement, on-going dialog between citizens and government officials can be useful to reduce tension within the community over unresolved issues and produce a better understanding of real needs and concerns.

LACK OF LOCAL GOVERNMENT CAPACITY

While involving citizens in budgeting and other financial management processes can strengthen the governance process and provide valuable contributions to the everyday operation of local governments, it may require human resource investments by your local government to assure its success. For example, elected and appointed officials and operational staff members may need training in citizen participation techniques to assure that the process provides added value to the planning and delivery of public goods and services. Effective citizen involvement may also require the reallocation of your human resources to assure that the needs of citizens are met. For example, a decision to establish neighbourhood service centres will almost certainly require new expenditures in facilities and the reallocation of staff. It's important to consider the potential consequences of greater citizen involvement before too many commitments are made to implement participatory initiatives.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

Involving citizens effectively in local government decision making is important to the long-term success of local government. However, we often hear that citizens are not interested in local government and, therefore, do not want to participate. Do you agree with this statement?

If you do, list the reasons you believe keep people from participating more actively in your local government.

What actions could be taken successfully in the next six months to involve your citizens more fully in the decision making processes of your local government?

INTERNET RESOURCES

Citizen Participation Toolkit <http://www.toolkitparticipation.com/>

Learning Initiative on Citizen Participation and Local Governance <http://www.ids.ac.uk/logolink/initiatives/workshops/PRIFeb05.htm>
Toolkit for Enhancing Citizen Participation <http://www.cysd.org/toolkit.htm>
Community Groups and Planning Action: The Need for Citizen's Participation in Decision-Making <http://www.gdrc.org/icm/ppp/prague.html>

APPENDIX A: CITIZEN PARTICIPATION TECHNIQUES

Following are a number of citizen participation techniques used by local governments.

1. PUBLIC HEARING OR MEETING

DEFINITION/PURPOSE

A public hearing or meeting is a formal, structured event. (For ease of reading, the authors use public hearings as synonymous with public meetings.) It is commonly used to gather citizen comments related to the annual budget. A public hearing may be a requirement of law or policy.

PROCESS

The governing body calls a public hearing by posting notice in a public place (on sign boards) or publishing the notice in a local newspaper prior to the meeting. The date, time, location and purpose of the hearing is included in the notice. The governing body usually holds the hearing during regularly scheduled governing body meetings at LG hall. The governing body sets the format of the public hearing and it may include presentations by staff. The governing body establishes rules that govern the public hearings and may limit speaking time to ensure that all citizens are given an opportunity to be heard. Where large numbers of citizens are expected, speakers may be required to sign up in advance to speak before the governing body.

ADVANTAGES/DISADVANTAGES

A formal public hearing reaches large numbers of people and provides opportunities for the public to comment directly on an issue. There can be an opportunity to respond directly and immediately with questions and comments and to clarify facts or ideas. All sides of an issue can be heard. A public hearing provides a forum for community leaders to express their positions on issues and provide for venting of anger or frustration. A public hearing is an inexpensive means of obtaining citizen comments on an issue.

A public hearing has limitations. It is not an effective forum for conveying complex ideas or detailed information. Public hearings do not provide for in-depth discussions or appreciation of different viewpoints as they can be dominated by vocal individuals with narrow interests. Public hearings are not well suited to building consensus or making a decision. Facilitation is critical and difficult—public hearing can stray off the planned agenda. It can be difficult to prevent confrontation.

2. TOWN HALL MEETING

Appendix E contains a checklist for local officials on how to set up and conduct a successful public hearing or town hall meeting.

DEFINITION/PURPOSE

Town hall meetings are a variation of the formal public hearing, serving the same purpose—to solicit citizen comments—but it is less formal. Meeting dates and times are coordinated with local residents and are held in the community or neighbourhood.

The agenda focuses on a single issue. The informal structure of the town hall meeting allows for in-depth discussion, direct and immediate response to questions and comments, and clarification of facts or ideas. It may be a requirement of local policy.

PROCESS

As an example, a town hall meeting is called to discuss the development of a neighborhood improvement plan. First, LG staff gives a presentation on the issue which provides a common informational basis for citizens in attendance. Members of the responsible departments answer any citizen questions and record the comments of the citizens. Local elected officials are usually present and moderate the discussion.

ADVANTAGES/DISADVANTAGES

Because the town hall meeting is informal and focused on a single issue, it is an effective technique to solicit, receive and discuss public comments on an issue. Town hall meetings, because of size and informal structure, are better suited to build consensus for decision making.

The logistics of setting up and conducting a meeting outside LG hall, the need to hold multiple meetings in different parts of the community, and expenses may be viewed as disadvantages to this technique. However, from a different perspective, the first two objections can be positive aspects of the technique. If LG hall is seen as being out of touch with the citizenry, town hall meetings can be a perfect opportunity to get out into the community, change that perception, and demonstrate commitment to citizen participation. Facilitation is critical to a town hall meeting to keep it on the planned agenda.

Advertising a Public Meeting

A governing body in a small community was anxious that all its citizens would be informed about a town hall meeting being held to consider the merits of a proposed comprehensive land-use plan. On advice of staff, the governing body invested in a fifteen-foot banner and hung it on the outside of the LG hall, facing the busiest LG street. Everyone who passed through town saw the sign, and many commented on it favourably when they came to the meeting.

3. CITIZEN OPINION/ATTITUDE SURVEY

DEFINITION/PURPOSE

This technique is used to gather factual information about citizens' attitudes and opinions, usually regarding the quality and financing of local government services.

An opinion survey can include the general population or a specific group of users. It may cover all municipal services or just one service, such as the use and condition of parks and open space. The results are used to determine citizens' priorities for services, evaluate existing services, and investigate the citizens' willingness to support tax or fee increases.

PROCESS

Developing a quality citizen attitude survey may require the assistance of an outside specialist with public opinion survey experience if this expertise is not available within your staff. If so, the local government staff can assist the process by developing suggested questions for the survey, while the specialist prepares the questionnaire, conducts the survey, and evaluates the results. The survey can be conducted in person or by mail. In more developed setting, it may be possible to do telephone interviews but this often denies lower income citizens from participating so this factor needs to be considered. The more personal the survey (getting answers to the questions in person versus by mail), the more expensive, but hopefully, the more accurate the surveys will be.

ADVANTAGES/DISADVANTAGES

A scientifically conducted survey, based on a representative sample of the entire community, has the advantage of recording the answers of all the residents, not just the voter, the politically active or the influential. By conducting a survey on a recurring basis (every two to three years) using similar questions, local officials can determine any changes in public opinion and whether actions taken in the interim have been effective in influencing public opinion.

One LG's Experience with a Citizen Opinion Survey

In 1993, a major metropolitan LG in Eastern Europe faced two issues related to citizen participation: advertised meetings resulted in little turnout, and many of the government programs offered by the previous system bore no relationship to customer demand. The solution was to design and conduct an opinion survey to determine citizen interest. In January, 1994, the LG contacted 287 households by telephone. The survey focused on the 14 largest programs and asked about: (1) satisfaction with service provided, (2) desire for increases or decreases in service levels, and (3) willingness to pay more taxes or charges for program increases. The intent was to establish a link between service level and customer demand. The survey also asked the public's opinion on the priorities of programs and some of the more politically difficult issues in the budget.

The survey revealed some interesting insights into public opinion and provided objective information about citizens' opinion of LG services. For example:

- The program with the highest community satisfaction was culture (77 percent) followed by primary education (72 percent) and central heating (60 percent). The lowest scoring programs were streets (19 percent) and financial assistance to the poor (25 percent) and water and sewer (34 percent).
- Sixty four percent supported service increases in water and sewer; 58 percent in solid waste, 57 percent in streets, and 54 percent in parks. However, only in primary education, water and sewer, and parks were the majority of supporters willing to pay more.
- Eighty percent supported the LG's top priorities of streets, housing and schools.
- On issues that were politically difficult, 81 percent believed that the LG should contract out programs to reduce costs, and 97 percent believed that utility rates should be based on actual use, rather than everyone paying the same rate.

4. FOCUS GROUP MEETING

DEFINITION/PURPOSE

A focus group is a meeting of selected citizens. It is designed to gauge the probable response of one or more large groups to a local government proposal or initiative.

PROCESS

A focus group is usually facilitated by a consultant. However, local government personnel can be trained in the process as well. Approximately ten people are selected for each group. They represent a cross-section of the community. The group is asked questions in an objective manner about the proposal or initiative. The individual's and group's responses are either recorded by audio tape or with extensive written

notes so the information can be analyzed later. The same interview process is repeated three or four times with different groups to gather comparative information.

ADVANTAGES/DISADVANTAGES

They provide a detailed understanding of people's concerns and values by bringing together people who represent different perspectives. Focus groups tend to be less expensive than an opinion survey and less time consuming than a full fledged opinion survey.

They also are spontaneous in that participants may volunteer information that you might not have thought to ask in an opinion survey. They are not effective for providing information to the general public. They are not designed to build consensus or make decisions. They are not scientific, and it is difficult to quantify the results. The findings point you in the right direction, but it is wise to use the feedback as a guideline for further research. The success of focus groups often depends on the availability of outside expertise.

Tact and Consideration with Citizens

A focus group was planned to discuss LG taxes, a contentious issue in that community, and the citizens were there in large numbers. Most people accepted their table assignments when they were handed numbered name tags, but one of the more aggressive citizens complained: "I want to sit with several of my neighbours who feel exactly like I do." "I understand," said the staff organizer, firmly, but with a smile; "but we want to give everyone a chance to speak with people who might not agree with them. You may even convince someone to consider your point of view." The complainer reluctantly sat down where she was told. Later, after a particularly lively and creative discussion, she admitted to the focus group facilitator that the "opposition" did not look nearly as fierce face to face.

5. AD HOC AND ADVISORY COMMITTEES/TASK FORCES

DEFINITION/PURPOSE

An advisory committee is a group of citizens appointed to provide continuing advice on issue(s) to the governing body. A task force is a group of citizens appointed to work on a specific objective or problem. It exists only for the time necessary to complete the task. A task force may also be a sub-committee to a larger advisory group and is limited in size so that it can be an effective working body. In both cases, the selection of members is critical. Membership must be broad enough yet not too large, and must be representative.

Advisory committees are good for organizing and coordinating input from a wide range of people. They are especially useful for developing consensus for action on complex issues that touch upon many facets of the community.

PROCESS

Expectations of the role of the committee or task force must be clear to all parties. Putting these expectations in writing is an excellent way to guide the committee or task force in their assignment as well as to terminate it when the job is complete.

Advisory committees and ad hoc task forces are effective in focusing attention on an important issue for a short period of time. They are useful in organizing input from a wide range of people and developing consensus for action on complex issues that touch upon many facets of the community. They are disbanded when the work is complete. However, without clear guidelines, specific tasks and limits, they can assume a life unto themselves.

6. *STANDING BOARDS AND COMMISSIONS*

DEFINITION/PURPOSE

To ensure a broad representation on policy and geographical issues, governing bodies often select governing body committee chairpersons plus some representatives from geographical districts to serve on boards. Boards and commissions provide control, management and maintenance of a specific function.

PROCESS

Such boards and commissions are often established by local policies and stipulate how they are constituted, the qualifications of the members, and the duties of the board or commission. Board and commission members serve at the pleasure of governing body for a term specified by law but typically have the same term as the governing body.

Many local government elected bodies establish permanent standing committees to deal with complex policy development or planning issues over a longer period of time. Advisory committees may consist only of elected officials, or part elected representatives and part citizens, or all citizens depending upon local law and practice.

ADVANTAGES/DISADVANTAGES

They are effective for providing citizen oversight of specific local government activities. Citizens bring specialized expertise into local government and gain experience for future leadership roles.

Boards and commissions are not effective in providing information to the general public or developing consensus outside their area of responsibility. They can become so narrowly focused on a single function that they lose sight of larger, LG-wide issues.

7. TECHNOLOGY APPLICATION (CABLE TV, INTERNET)

Traditional communication has been one-way and relies upon the media— newspaper, radio and television—to keep the citizen informed on local government issues. Recent advances in technology, such as Cable TV and the Internet, have given LGs new communication tools.

DEFINITION/PURPOSE

Cable TV provides an alternative to “over the air” broadcasts of radio and television. It uses a coaxial cable to send multi-channel TV programming to homes, apartments or offices throughout a defined service area.

The Internet is a network that allows computers from all over the world to exchange messages and electronic files. This network of computers has now grown to include thousands of computers in public and private agencies.

Cable TV and the Internet can be used by a local government to enhance citizen participation in three different ways:

Information dissemination—Internet: and Cable TV: An electronic bulletin board can provide information on governing body agendas, recreation schedules, cultural event schedules, bus route and schedules, instructions how to get a business license, etc.

- A local government access channel on Cable TV provides:
- A public bulletin board that informs the public in advance of scheduled public meetings for the governing body, boards and commissions, and council committees. It can be updated immediately for last minute schedule changes.
- Job announcements.
- Other activities scheduled at LG hall.
- Coverage of council meetings from beginning to end as well as rebroadcasts at times convenient for citizens.
- Programs with reports about council proceedings, hosted “talk shows” or discussions with the mayor or members of the council and press commentaries.
- Viewer call-in programs through which viewers can directly question government officials about issues and policies.

The World Wide Web can also replace traditional telephone, fax and mail services. It can be a way for council members to establish a home page that can be accessed. Ease of getting information puts your municipal government in a more favorable light.

Communication to/from citizens— Internet: Electronic mail (email) is an alternative to telephone, fax or regular mail. It can be the way citizens access local government in the future to report service problems, have an inspection performed or apply for a license.

The W by constituents to keep abreast of district activities. It can also be used by the LG to inform the public about LG activities or by citizens to access LG documents or applications without having to come to LG hall.

PROCESS

Cable TV, where it is an option, often operates as a subscription service in which citizens pay a monthly fee for services. In the U.S., private cable companies obtain permission from the LG to provide this service in the LG and to use the street right-of way for their cable. In exchange, the LG is compensated for the use of right-of way and may require that one or more public access channels be provided for local government use.

Access to the Internet is made through an Internet Service Provider (ISP). The ISP connection is made via local telephone for a monthly service charge. The subscriber is responsible for providing all equipment needed to access the Internet including personal computer, modem, software and peripheral equipment. Anyone paying the required fees and having the required equipment can access the Internet and World Wide Web.

The Internet is a wide-open entity that is by design loosely controlled. Issues to be examined include: security, corrupt or virus-infecting data, and who will manage the content on the LG's Internet site. These are basic issues that local government should address in an Internet use policy. Local officials interested in accessing the Internet or putting their local government on the Internet should refer to the guidelines included in Appendix A.

ADVANTAGES/DISADVANTAGES

Cable TV is a cost effective tool for informing the public; however, not every household subscribes to cable TV, limiting its effectiveness to reach and communicate to all citizens. The cost of subscribing to cable TV may also be a disadvantage.

Internet: As more and more use is made of the Internet for disseminating information, local government will save valuable staff time and paper costs. It provides the ability to market the community to relocating businesses or vacationing tourists.

The major disadvantage of these newer communication processes is their discrimination against those who cannot afford such services or do not have access to these services. There is no better way to alienate citizens than to provide services or information that are essentially prohibited in one way or another to various constituents within your governance domain.

8. *NEIGHBOURHOOD AND COMMUNITY ASSOCIATIONS*

DEFINITION/PURPOSE

A group of citizens organized around a common interest in an issue(s) related to a specific geographical area, such as zoning, land use, or neighbourhood planning. It provides a forum for discussing problems and exchanging ideas between LG staff

and association members. The association has been successfully used to administer neighbourhood projects and service delivery contracts.

PROCESS

Neighbourhood associations may be a legal entity or informally organized. Membership is open to all residents, property owners, business licensees and representatives of not-for-profit organizations in that area. Each association elects a board of officers to lead the organization annually and to represent the interests of the association to outside groups. Committees within the association are established to focus on specific issues such as planning, traffic or economic development.

Council can establish an office in LG hall for coordinating and communicating with neighborhood associations. The following is a suggested list of basic functions for such an office:

- Notify interested persons of meetings, hearings, elections and other events.
- Provide for the sharing of information and maintain a list of reports, studies, data sources and other available materials.
- Provide referral services to individuals, neighbourhood associations, and others.
- Keep an up-to-date list of neighbourhood associations and their principal officers.
- Assist neighbourhood volunteers in coordinating projects on behalf of neighbourhood “live-ability.”
- Encourage individuals to work with existing neighbourhood associations where possible.
- Assist in reproducing and mailing newsletters and other printed matter when supplied by a neighbourhood association.
- Act as a liaison while neighbourhood associations and municipal agencies work out processes for municipal involvement.
- Assist in contracts with other municipal agencies on behalf of neighbourhood associations or other interested individuals.
- Assist in educational efforts related to citizen participation in municipal government.

ADVANTAGES/DISADVANTAGES

Neighbourhood associations tend to lack permanence. They often are created in response to a single issue, in which residents mobilize to address the issue, and then disband when the problem is solved or interest subsides. To promote the long-term continuance of neighbourhood associations, local officials should provide support in terms of staff and resources.

9. COMMUNITY OFFICE

DEFINITION/PURPOSE

This is a variation of the neighbourhood board/association described above, but it is typically funded and operated by the LG. It can provide one or a group of services depending upon needs. Services typically include: neighbourhood services, health care, social assistance, and aid to pensioners. It extends municipal services into a geographical district or neighbourhood of the LG, and brings local government to the citizen rather than the citizen travelling to a LG hall.

PROCESS

Local government officials determine which services can best be provided by community based offices. They should consider the benefits and costs of decentralizing an activity from both LG and citizen viewpoints. Operational funding is provided through the annual budget.

ADVANTAGES/DISADVANTAGES

It is more accessible to the public and fosters close rapport and improved communication with citizens. The office becomes a part of a community and creates an increased level of trust toward government. After a neighbourhood office is established in a community, involving citizens in citizen participation activities is much easier.

The office workers tend to focus on issues within their geographical area and may overlook LG-wide issues and needs. Decentralizing some services may increase costs for people and resources.

10. OMBUDSMAN

DEFINITION/PURPOSE

An ombudsman is a nonpartisan public official who investigates people's complaints about government officials or agencies. The scope of work varies by LG, but usually involves complaints of unjust or harsh treatment on matters such as housing, taxation, voting, or old age pension payments.

PROCESS

Local government elected officials determine the need for an office of ombudsman in accordance with state or local law. If there is a need, they generally establish its duties and responsibilities by ordinance. An ombudsman is appointed following local personnel policies.

After investigating a complaint, the ombudsman may dismiss it or may seek correction of the problem by persuasion, publicity or occasionally by recommending prosecution.

ADVANTAGES/DISADVANTAGES

An ombudsman meets the citizens' need for impartial and informal handling of complaints. The program is designed to improve government's response to citizens' concerns in a fair and impartial fashion. It is particularly effective in helping citizens deal with the complexities of bureaucracy in large LGs.

11. OPEN DOOR PROGRAM (ACCESSIBILITY)

DEFINITION/PURPOSE

It encourages citizens to visit LG hall or a community office at any time on a walk-in basis. Establishing regular hours of operation for LG hall shows that LG hall and staff are accessible and open to citizen issues and concerns.

ADVANTAGES/DISADVANTAGES

An open door program facilitates communication with citizens. Opening LG facilities to the public on all days that employees work may increase costs, but will generate far greater intangible benefits due to the perception that government is open, there to serve, and available to hear concerns and issues.

12. PUBLIC INFORMATION

DEFINITION/PURPOSE

Publication information is provided in the form of press releases, interviews, pamphlets, etc. There may be a public information department responsible for this function. Public information keeps citizens informed of the activities of the LG.

PROCESS

Local government officials who decide to use the public information staff to support citizen participation activities must insure that the staff is seen as objective and a credible source of information.

ADVANTAGES/DISADVANTAGES

A strong and effective public information program creates a positive environment. Well-informed citizens are able to participate more intelligently, have a better under-

standing of program issues and impacts of various actions and a historical perspective to the program being initiated.

Citizens have been known to criticize the public information staff for not supplying objective information, believing that the public information staff acted as a marketing organization for the LG. When this happens the public information efforts undermine the citizen participation program.

13. EDUCATION PROGRAMS AND POPULAR REPORTING

DEFINITION/PURPOSE

Direct education programs are those in which LG officials or staff present a program directly to the public, in person; for example, a talk with school children about local government activities. Indirect education programs still provide public information, but use printed material to convey the message instead of a person. Popular reports are designed to communicate—simple and straight forward—avoiding complex terms and bureaucratic jargon.

Direct education programs provide personal contact with the citizen. Indirect education programs provide information. Popular reports are an easy-to-use method for providing important financial and operating information to citizens.

PROCESS

Typical educational materials include pamphlets, newsletters, publications and reports. Some of the more innovative local governments have attempted to demystify financial reporting for annual budgets and end of year accounting reporting. The current expression for this practice is “popular reporting.”

ADVANTAGES/DISADVANTAGES

A direct education program provides an opportunity to present information, interact with the audience, ask and answer questions, respond immediately to concerns and issues, and put a “human face” on what otherwise might seem like a faceless bureaucracy.

Citizens like popular reporting because it summarizes information, uses charts and graphs to display complex ideas, and is easy to read. Documents such as the Budget in Brief and Annual Performance Report convey a lot of information in a 20-25 page booklet. The booklets are widely disseminated to the general public and often used in citizen education and citizen participation programs.

14. CITIZEN SERVICE OFFICE (COMPLAINTS, SUGGESTIONS AND INFORMATION)

DEFINITION/PURPOSE

A citizen service office is a centralized clearinghouse established to receive and respond to citizen requests for assistance or information. It provides a single point of contact, thus simplifying contacting LG hall from the citizen's point of view. No longer does the citizen have to know who to contact or which department to call to be able to get information or have a service request handled.

PROCESS

These requests generally come to the office by mail, telephone or in person. The office is designed to:

- provide the information, or if a service request, record the request, route it to the proper department for action, and when it is completed, notify the citizen of the action taken
- help council and citizens get action on requests for information and service
- improve responsiveness of local government to the council
- coordinate the municipal service response effort of the local government
- provide an internal communication network available to all LG departments.

ADVANTAGES/DISADVANTAGES

Centralizing information and service requests permits the LG to track the requests and ensure that they are acted upon within a specified time frame. The result builds credibility with the citizen that local government actually works for them.

Establishing a citizen's service centre can be costly and a major disadvantage; however if a local government decides to create such a department, consider using resources that are already doing this type of work within the organization. Anyone whose current job consists of dealing with customer information and service requests more than 60% of the time is a potential resource to staff a central agency.

15. MEDIA RELATIONS

DEFINITION/PURPOSE

Every citizen participation program requires working with the media (newspaper, radio and television) to reach the general public. The media assists citizen participation at the beginning of the process by announcing the program and inviting public

involvement; during the middle, by reporting the progress of the initiative; and finally at the end, by reporting its results and implementation.

PROCESS

Sometimes, local officials have to encourage the media to cover citizen participation programs. Two commonly used methods are press releases and press conferences. These help the media gather the important facts with minimal effort.

Radio and television may be the major avenues by which citizens hear the news, but the opportunity to get your message across is much smaller, 30 to 60 seconds, and the competition for air time is much greater. Local government radio and television coverage depends upon the extent to which it is current and newsworthy. Any news releases for radio or television must take these conditions into account. Therefore, brevity is critical and the story line must be short, to the point, and easily understood.

Here are some suggestions for establishing a good working relationship with the media:

- Be honest and straight forward in responding to questions; honesty is the best policy.
- Avoid “no comment” responses—it sounds evasive.
- Return phone calls promptly; reporters usually have deadlines they are attempting to meet.
- Do not speculate or answer hypothetical questions.
- If you do not have a factual answer to a question, apologize, and say that you do not have it readily available, but you will get the information for them. Depending on their deadline, they may or may not need it.
- Do not downplay controversial items (the media thrives on controversy); if you do, you lose credibility.
- If the media catches you off guard regarding an event that has just occurred, say you just heard about it and will have a response after you have had an opportunity to study it. Get the answer out quickly.
- If you choose to establish a personal relationship with the media, remember that you cannot dictate how a story will be reported.
- If you disagree with the way a story has been covered, address the issue with the reporter in private or ignore it altogether. Do not complain to the newspaper editor or the radio or television news director.

ADVANTAGES/DISADVANTAGES

Establishing a media relations program can be an effective way to positively promote local government activities. Using the media relations office as a central point of contact for all media improves press relations and enhances the media's access to information. When accurate and timely information is provided to the public the image of local government is improved. Local government officials should be cautious, however, not to over market the LG to the point that the office is viewed as a propaganda tool.

GETTING MEDIA ATTENTION

A local government in a heavily populated urban area embarked on an ambitious program of sponsoring community meetings about the pressing issues of growth and transportation. After failing to interest the newspaper editor in printing articles of any size or depth, the LG produced and paid for its own six-page, four-color supplement, which was inserted in the Sunday edition of the paper. It was read by 250,000 people, and the governing body saw the fruits of its labours and investment rewarded. This single, ambitious effort increased interest and attendance at the public meetings. As a by-product, the project finally attracted free media attention; reporters realized that these issues did concern a broad range of citizens in the community.

APPENDIX B – WORLD BANK INFORMATION ON PARTICIPATORY MONITORING

PARTICIPATORY MONITORING AND EVALUATION

WHAT IS PARTICIPATORY MONITORING & EVALUATION?

Participatory monitoring & evaluation (PM&E) is a process through which stakeholders at various levels engage in monitoring or evaluating a particular project, program or policy, share control over the content, the process and the results of the M&E activity and engage in taking or identifying corrective actions. PM&E focuses on the active engagement of primary stakeholders.

WHY IS PARTICIPATORY MONITORING AND EVALUATION IMPORTANT?

Participation is increasingly being recognized as being integral to the M&E process, since it offers new ways of assessing and learning from change that are more inclusive, and more responsive to the needs and aspirations of those most directly affected. PM&E is geared towards not only measuring the effectiveness of a project, but also towards building ownership and empowering beneficiaries; building accountability and transparency ; and taking corrective actions to improve performance and outcomes.

WHAT ARE THE PRINCIPLES OF PARTICIPATORY MONITORING & EVALUATION?

Conventionally, monitoring and evaluation has involved outside experts coming in to measure performance against pre-set indicators, using standardized procedures and tools. PM&E differs from more conventional approaches in that it seeks to engage key project stakeholders more actively in reflecting and assessing the progress of their project and in particular the achievement of results.

CORE PRINCIPLES OF PM&E ARE:

- primary stakeholders are active participants – not just sources of information
- building capacity of local people to analyze, reflect and take action
- joint learning of stakeholders at various levels
- catalyzes commitment to taking corrective actions

ADDITIONAL INFORMATION ON PARTICIPATORY MONITORING:

<http://www.ids.ac.uk/ids/bookshop/briefs/Brief12.html>

www.ids.ac.uk/ids/particip

<http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTSOCIALDEVELOPMENT/EXTPCENG0,,contentMDK:20509352~menuPK:1278203~pagePK:148956~piPK:216618~theSitePK:410306,00.html>

<http://www.worldbank.org/participation/forsterprinciplesPME.pdf>

<http://siteresources.worldbank.org/INTPCENG/214574-1116505633693/20509339/communitybased.pdf>

APPENDIX C: CASE STUDY FROM SOUTH AFRICA

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SUMMARY

A science park, spanning 200 hectares and intending to be a densely developed light industrial site presented a threat of pollution, chemical accidents and ground water contamination to communities living nearby. Environmental controls which would minimize adverse impacts were needed in the context of lax standards and poor enforcement by a generally under resourced state. Opposition by citizen groups evolved into a collaboration with the local authority to develop a preventative system of environmental management for the Park. The system included the setting of performance standards for industries, the evaluation of prospective investors and the setting of conditions and monitoring of compliance therewith by industries occupying the Park.

1. INTRODUCTION

During 1997 a large development was planned for Cape Town called Capricorn Park, which would involve the creation of a science park spreading out over 200 hectares of land. The park was planned to be the size of the central business district of Cape Town and its developers estimated that it would create approximately 40,000 jobs. It was advertised as a project which would provide much needed skills training to the citizens of Cape Town in the fields of science and technology, in a campus like setting.

Communities and environmental groups were concerned at the proximity of what was in fact to be a densely developed light industrial site close to the coast and adjacent communities. The developers claimed that they were not in a position to fully disclose what types of industries would occupy the site, and instead gave a very broad list of possible future occupiers. The list included the electronics industry, which raised a number of concerns. The first was the history of underground contamination in the past at sites such as Silicon Valley where electronic plants had apparently stored chemicals in leaking underground tanks. The second was the fact that the Capricorn Park site was located on a shallow aquifer, the contamination of which would adversely affect the nearby coastline which is a large bathing amenity adjacent to low income communities. The third was the possibility of accidents or spills involving toxic chemicals which could endanger the lives of adjacent residents who live very close to the site.

2. ENVIRONMENTAL IMPACT ASSESSMENT

The local Council had sold the land to the park developer subject to a three-tiered agreement, which made provision for a broad brush environmental impact assessment of the whole site followed by more detailed environmental impact assessments as the site was developed and a final site specific environmental impact assessment for each industry before it received its service connections. At the time the only statutory provision relating to environmental impact assessments was contained in a policy provision promulgated under the Environment Conservation Act, no 73 of 1989 which required a “planned analysis, involving public participation” before commencement of any large scale land developments. This provision states that every person has the right to an environment which is not harmful to their health and well-being, and requires that reasonable steps be taken in order to conserve and sustain the environment and protect it from pollution.

3. FAILURE TO DISCLOSE SUFFICIENT IMPACTS

After the broad brush environmental impact assessment was completed the developer made application to the local authority for subdivision of the land in order to begin developing. The local authority was required to zone the land as a result of this application with conditions as it saw necessary in order to protect, among other things, the environment. It was argued by the environmental group, the Wildlife and Environment Society, that there was insufficient disclosure of information in this environmental impact assessment to enable the local authority to exercise its decision making power in terms of the Constitution and to take reasonable steps to discharge its duty to protect the environment. The developer stated that in view of the fact that it had not secured contracts with occupants of the site it could not accurately speculate about future industries and their impacts. It also did not choose to disclose detailed information about impacts regarding those industries from whom it had secured undertakings. The broad brush environmental impact assessment therefore dealt mainly with issues of storm water, surface landscaping and aesthetic features of the development. It did not look in sufficient detail, or in a meaningful way, at possible air and ground water pollution, traffic impacts and risk of accidental chemical releases and spills, noise and water consumption, issues which were of importance to surrounding communities.

4. CHALLENGE TO SUBDIVISION APPLICATION

Once the subdivision was granted, an objection was lodged by Wildlife and Environment Society in terms of the applicable provincial Land Use Planning Ordinance which governs town planning. This law requires the provincial Premier to approve

or deny the subdivision, or make changes to it as he/she sees fit, if an objection is made. The objection was made on the basis that there had been insufficient disclosure of information for a proper impact assessment to take place, in particular into the cumulative impacts of the development. Without such impact analysis the local authority it was argued was not in a position to act reasonably in order to protect the environment as required by the environmental clause and the just administration clause of the Constitution. This encompassed in particular the requirement of running a planned analysis with full public participation. This it was argued could not be fulfilled in the absence of adequate information. Before reasonable steps could be taken by the Council in its environmental governance an adequate analysis of impacts and mitigatory measure would be required which would guide it, and which likewise was not possible without comprehensive disclosure. This challenge considerably delayed the development during which time the Wildlife and Environment Society began considering what course of action should be adopted in order to best protect the diverse interests which would be affected by the development. The objective of the Society was not to halt the development which was seen as an important source of future employment and an economic growth point for the region. During this period the Society disseminated information and gave a voice to the many other residents and environmental groups which were concerned with the development (hereafter referred to as "environmental groups").

5. *INTEGRATED ENVIRONMENTAL MANAGEMENT*

South African regulatory standards relating to the environment are laxer and less clear than those which apply in Europe and North America. Furthermore, industrial activities are not regulated in a uniform manner. In some areas there is very little formal regulation, such as in the area of environmental air quality standards. Although there are regulations as to what may be emitted into the workplace, the question of what emissions may be vented into the environment generally, through smokestacks or otherwise is far more poorly controlled. Local authorities control smoke emissions. Industrial emissions are very much the subject of the regulators discretion. Permits are issued requiring compliance with standards set on an ad hoc basis by a national pollution control officer who has an almost total discretion as to what may be emitted.

A development of the type planned for Capricorn Park would be covered by many areas of regulation, some of which are more effective than others, for example, waste disposal, ground water quality management, coastal zone management, air pollution, hazardous installations, noise pollution, municipal services, such as sewers and storm water drainage, workplace health and safety, building regulations and town planning regulations, to name but a few. In most respects, once a right to conduct industrial activity is granted, the protection of the environment in such a development is governed through criminal prosecution of offenders who are proven to have violated an environmental standard. The standard of proof in such cases is guilt beyond reasonable doubt. Fines for contraventions are very low and have not been shown to act as a deterrent. Regulatory resources for inspection and prosecution for

environmental crimes is seen by many as a low priority. Large scale developments therefore present a very real threat of causing serious environmental damage.

In this context environmental groups were of the view that it would be more practical and protective of the environment and surrounding communities to develop an environmental management strategy for the park which would prevent environmental damage, rather than prosecute polluters. During the period of delay caused by the Premier having to consider their objection to the development, they proposed a proactive strategy of environmental enforcement for the Park, should it proceed to be authorized.

6. *PROACTIVE ENVIRONMENTAL MANAGEMENT*

A proactive environmental management strategy, based of course on adequate disclosure of information, with the following features was put forward by the environmental groups:

- Oversight body: A representative body, incorporating the developer, local authorities and environmental groups' representative was proposed to in order to develop and audit the management strategy.
- Policy review of developers proposals: Review of industry profiles and development of a system of information disclosure for future activities of occupants of the Park, including initial disclosure on intended industrial activity, monitoring of activities once in operation and auditing of compliance with the environmental management system.
- Setting of detailed standards and procedures: After the review, standards and procedures would be developed which would include controls on waste (minimization, recycling and handling), water and energy consumption, air emissions, management of hazardous substances and emergency responses.

7. *APPROVAL OF THE SUBDIVISION*

During the course of the above negotiations subdivision approval was granted to the developer but subject to certain conditions. These included the requirement that an integrated environmental management system be developed for the Park and that an Environmental Advisory Board be constituted, including a representatives from civil society, the developer, and various government departments, to oversee the implementation of the management system. In particular the Board was required to assess industries wanting to occupy the park, and to advise the local authority on conditions it should impose on activities of such applicants. These conditions would then become land use conditions which could be withdrawn if there was non-compliance therewith. It seemed that the Premier had been informed of the proposals emanating from civil society and had given tacit approval to these in these conditions. The problem of trying to create an environmental management system where no regula-

tory framework existed for one was hopefully overcome through the use of land use rights referred to above.

8. DEVELOPMENT OF AN ENVIRONMENTAL MANAGEMENT STRATEGY

The Council then proceeded to develop an Environmental Management Strategy based on the processes and features set out hereunder. The process was developed by consultants employed by the Council. The first three components, namely the development of a background information package, the investors application procedure and the development of significant issues to which quantifiable performance criteria could be attached were developed by the consultant initially employed by the environmental groups. This arrangement arose as a result of negotiation with the Council in order to give more legitimacy to the process.

8.1 BACKGROUND INFORMATION FOR ENVIRONMENTAL MANAGEMENT

The environmental management approach for the park was based on two legs, first detailed assessments of applications of investors with regard to environmental performance, and second the development of an environmental management system for the park. In some instances occupants would be required to develop in addition their own environmental management system.

The environmental management system structure consisted basically of a policy plus an implementation, auditing and review plan. Investors were advised that a management system along the following lines was being finalized which was based on a number of internationally recognized environmental management principles and would include the following item:

- history, description and aims of the development;
- roles of the local authority, developer, property owners association during the different phases of the development;
- legal requirements, set by South African law as well as the local authority and who would be responsible for checking on compliance therewith;
- discussion of other requirements to which the project was committed, such as “the polluter pays” principle;
- the environmental policy of the Park;
- the environmental management program — objectives, targets, responsibilities and timelines;
- operating procedures for the park; and
- the fact that applicants would be individually evaluated for potential of adverse impact on the environment and in certain instances would be required by the local authority to develop and implement in addition their own environmental management system.

Investors were also informed of:

- applicable principles relating to environmental management systems generally, for example, Receiving Environment Standards and the principle of integrated Pollution Control;
- environmental auditing systems including:
 - auditing of the environmental management systems of the individual occupants as permitted by the local authority, and
 - process consumption and waste audits in which water and energy usage and the compositions and quantities of outputs streams are examined and compared to the companies performance criteria (i.e., permitted performance conditions)
- design and operational limitations of the Park; (These included for example rules regarding the design of chemical storage tanks; transfer; handling and storage of materials on site; noise abatement; disposal of waste products; equipment maintenance and other issues);
- further restrictions on use based on zoning which could be applied after the assessment procedure for occupants had been completed; and
- applicable legislation and principles applying to the Park. (This included reference to the law relating to hazardous substances, health and safety in the workplace, and emergency procedures and operational hazards both applicable under South African law and in some instance developed beyond this for the purposes of the Park Environmental management system, for example, the Environmental Protection Agency list of priority pollutants list of hazardous substances.)

8.2 THE INVESTORS APPLICATION PROCEDURE

One of the most important tools of management employed in the Park is prevention of environmental harm, rather than punishment after the fact, of environmental transgressors. Investors will therefore be required to disclose information about their planned activities to the Environmental Advisory Board which then assesses the sensitivity of the proposed operations with regard to the environment, in order to make it possible to evaluate whether the applicant is suitable for investment at the Park. The assessment results in a recommendation to the Council which will approve or disapprove the activity, or place conditions thereon.

Once the required information is submitted, the applicant is rated green for general approval, orange for cases which will be examined and possibly further information requested, and red for cases which are refused. Orange cases are for example those applicants who burn oil or coal, who have inadequate measures planned for dealing with a number of environmentally hazardous activities, such as the handling and storage of organisms or which use or produce asbestos, PCB's and dioxins. The initial ratings are evaluated by the environmental control officer, an employee of the local authority, who then passes them on for further investigation by the Environmental advisory board, who can also hear representations from the applicants. The executive committee of the local authority is the final decision making body.

Informative documentation is supplied to potential investors in order to assist them in the application process. The Environmental Control officer liaises with potential investors during the procedure in order to assist them in finding ways to conform with environmental norms and standards of the Park so that they can be admitted. Applicants may also still have to apply to other government departments for permits where applicable.

The application questionnaire covers a number of topics, including the following:

- nature and size of undertaking and whether technology used is the best available;
- choice of location and identification of possibly dangerous activities;
- disclosure of information regarding other existing activities elsewhere;
- noise levels likely to be emitted by the plant;
- projected water consumption, and wastewater disposal;
- energy consumption; and use of energy efficient machinery;
- identification of risky organisms used in biological or medical industries;
- practices for transporting, handling and storage of hazardous materials;
- site inputs and outputs, and waste products and reduction programs;
- details of hazardous components of inputs, products and wastes;
- details of storage facilities for hazardous process inputs; and
- provisions which have been made for spills and accidents.

In many of the activities where potential exists for detrimental effect on the environment, the applicant is rated “orange” until satisfactory arrangements can be made to minimize the risk, for example, proper arrangements made for the removal of waste, where no such arrangements were originally contemplated by the applicant.

Six significant issues to which quantifiable “Performance Criteria” can be attached.

The next step in developing the Environmental management system was the drawing up of a list of potentially significant issues to which quantifiable “Performance Criteria” (i.e., environmental performance conditions) could be attached for occupants of the Park. Monitoring mechanisms were developed to check for compliance with these standards. After completing the information disclosure questionnaire, applicants would have to satisfy these standards before being permitted to commence operations in the Park.

Examples of the application of some of these criteria is contained below:

- Emissions to stormwater: Stormwater from the Park is discharged into a take in the centre of the Park. In order to prevent contamination of the lake, discharges of substances into the stormwater system which might have this effect are not permitted. Performance criteria include a ban on discharges into the stormwater, a routine for the environmental site officer for checking accidental and intentional discharges and control parameters (i.e., standards) for monitoring quality of stormwater (e.g., per-

missible pH, conductivity, coliform and dissolved oxygen levels; maximum allowed concentrations of heavy metals and numerous other compounds).

- **Quality of water inflow into lake:** In cases of spillages, washwater and stormwater in materials handling, transfer and storage areas, water has to be drained away from storm water systems to a special sump, to prevent contamination of the lake. This requires preventative design in the handling, transfer and storage areas, including concrete floors in and bunding around these areas. Silt and litter traps are required at entry points of stormwater to the lake. Design of the above features and monitoring of maintenance thereof is conducted by the environmental site officer.
- **Emissions to sewers:** Permission is required from Local Authorities for industrial discharges into sewers. Investors who have had conditions set for discharges to sewers are responsible for appropriate monitoring thereof. Permissible pH and conductivity of sewerage discharges are set at specified levels. There is a program for monitoring of pH and conductivity of sewerage by the environmental site officer at various sites at increasing levels of frequency leading finally (as is recommended) to continuous monitoring after the site has been 75% developed.
- **Solid waste and disposal practices of individual owners:** Hazardous waste in particular is identified. All hazardous waste has to be treated on site or removed by the producer or an independent removal contractor. Containers for waste have to be approved by the local authority Medical Health Officer, and waste containers continuously covered, save where solid waste is being removed or deposited in them. All hazardous waste producers must keep a record of hazardous waste produced and the fate thereof. Operators must set annual targets for the reduction of hazardous waste produced and the fate thereof. Operators must set annual targets for the reduction of hazardous waste produced for a given level of activity. Audits of the above are carried out by the environmental site officer. There is a separate set of controls on storage and handling as well as audits for substances which are defined as hazardous chemicals.

APPENDIX D—PLAN AND IMPLEMENT A CITIZEN PARTICIPATION PROCESS

PLANNING

1. Identify the key issues
2. Define the objective; relate it to overall organizational goals
3. Seek organizational commitment from local officials to a participating approach within LG hall
4. Consult with others at LG hall
 - Coordinate other departments', agencies', and/or affected governments' involvement. Determine need for a facilitator. Review schedules and availability of key persons
 - Determine program requirements (personnel and financial resources)
 - Determine information requirements
5. Identify key persons, departments or organizations that will be affected
 - Develop a profile of the community
 - Identify persons, agencies, etc., by name
 - Clarify issues
 - Develop contacts and rapport
 - Interview community leaders

PROGRAM DEVELOPMENT

6. Draft Participation Program
 - Circulate information, issues, and options
 - Determine the decision making process for the program
 - Determine objectives for each stage of citizen participation
 - Design citizen participation opportunities with techniques
 - Establish monitoring and evaluation efforts
7. Meet with key persons affected by the process or program
 - Confirm issues and options
 - Confirm objectives for each step of citizen participation
 - Confirm selection of facilitator, if applicable
 - See advice on the overall design of the programs and techniques used in each stage
8. Finalize program design
 - Finalize program requirements (personnel and financial resources)
 - Finalize information requirements
 - Finalize monitoring and evaluation efforts
 - Finalize schedules and work assignments
9. Consult with key persons and other public agencies on final design as applicable
 - Analyze results

Make changes as needed
Revise the draft
Determine additional decision making processes as needed

PROGRAM APPROVAL

10. Obtain a decision on final program design and schedule
 - Publicize the decision with the rationale
 - Emphasize accountability

PROGRAM IMPLEMENTATION

11. Involve participants in implementation and evaluation

EVALUATION

12. Evaluate the program
 - Seek comment from key persons and others on the consultative part of the program
 - Evaluate the results of the participation program; did it achieve the objectives?
 - Document the evaluation for use the next time a participation process is planned

APPENDIX E—CHECKLIST FOR A TOWN HALL MEETING

PRE-MEETING PLANNING

- ___ Has a meeting space been located and reserved?
- ___ Has the meeting space been checked and arrangements made for keys, seating set-up and clean-up?
- ___ Does the meeting space have adequate lighting? Can the room be darkened?
- ___ Are audio visual equipment, microphone and extension cords available at the meeting space? If not, who will provide?
- ___ Is location accessible by mass transport? Is there ample parking for autos?
- ___ Are participant handouts prepared: agenda, information sheets, feedback forms?
- ___ Is sign in or registration form prepared? Are there adequate pens and paper?
- ___ Are name tags needed?
- ___ Are signs posted to direct participants to the correct building/ meeting room?
- ___ Are refreshments being provided: coffee, tea, mineral water?
- ___ Are flip charts, easels, markers and paper available in the meeting room?
- ___ Have facilitators, note takers and presenters been assigned?
- ___ Do other local officials who plan to attend know their roles?

MEETING NOTICE

- ___ Has a mailing list been developed? Updated?
- ___ Has the public notice for sign boards and advertisement in newspaper been posted/published? Is the wording of the objective consistent?
- ___ Has the news media been contacted? Press release written?
- ___ Have key community persons, council members and departments been personally contacted regarding the meeting?

AT THE MEETING

- ___ Are seats placed in a circular arrangement to encourage discussion among the participants? Don't use the stage.
- ___ Are there too many chairs? People tend to sit in the back. Avoid a front table—use chairs only.
- ___ Identify water closets (WC) and smoking areas.
- ___ Clarify the role of the facilitator, if used.
- ___ Review the rules of the meeting and attempt to get buy-in.
- ___ Ensure that the participants understand and accept the objective of the meeting.

- ___ Start on time and finish on time. Advise participants at the beginning of the meeting how long the meeting will last and expected time to adjourn.
- ___ Make sure flip charts and other audio visual aids can be seen by the participants in the room.
- ___ Keep presentation as short as possible (15 minutes maximum).
- ___ Provide maps, clear instructions and signs to break-out rooms for small group discussions, if needed.
- ___ Ensure that participants complete and turn in meeting evaluation forms.
- ___ Make sure that participants leave the meeting knowing what has been accomplished and what will happen next.

After the Meeting

- ___ Transcribe flip charts and meeting notes.
- ___ Add names from registration to mailing list.
- ___ Review the evaluation forms and summarize them.
- ___ Make copies of notes or summaries of the meeting available as soon as possible.

PART TWO—MANAGEMENT TOOLS

PURPOSE

Citizen participation is a process that provides individuals an opportunity to influence public decisions that affect their lives or to have a direct voice in the decision making process. Local governments in the past have been inclined to exclude or minimize public participation in government programs as too expensive or time consuming. This is seldom true today. Government officials are increasingly concerned about the growing alienation of their citizens and the reluctance of many citizens to support programs just because they are told they should do so. As a result, these officials are seeking ways not only to educate and inform citizens about public issues but also to solicit citizen input into the process of planning and financing government programs.

These workshop designs are intended to broaden the understanding of finance managers about the practical use of citizen participation techniques to inform and involve citizens in local government policies and programs.

Don't forget to look back at the Learning Applications! Many of them can be easily adapted for group exercises and may be more appropriate for persons who are just being introduced to the concepts of citizen participation.

CONTENTS

A brief description of each learning activity is shown below with an approximation of the amount of time required. If you wish to change the order, to omit something, or to add training material of your own, feel free to do so.

3.1 WARM-UP EXERCISE: PROS AND CONS

Participants share and discuss their experiences with citizen participation, both positive and negative. (45 minutes)

3.2 TRAINER PRESENTATION

Brief concept presentation based on the preceding essay that emphasizes the merits of encouraging citizen involvement in civic affairs and the local government's role in promoting the active and continuing involvement of citizens in financial policy making and administration. (30 minutes)

3.3 MINI-CASE STUDY: NOT WELL ADVISED

Participants read and discuss a case that illustrates the unfortunate consequences of abruptly changing the format for an announced public meeting. (90 minutes)

3.4 EXERCISE: MAKING CITIZEN PARTICIPATION WORK

Participants work in small groups on a task that consists of matching several situations that call for the involvement of citizens with the appropriate meeting types and then sharing their results with examples. (45 minutes)

3.5 EXERCISE: PARTICIPATORY BUDGETING

Participants work in 4 teams to plan strategies for gaining the commitment of the local governing body and management staff to undertake participatory budgeting (120 minutes)

3.6 EXERCISE: SERVING THE PUBLIC INTEREST

Participants work in small groups on crafting proposals to involve citizens after reading an incident about a governing body that makes a decision that arouses violent public criticism. (120 minutes)

3.7 CLOSING EXERCISE: LEARNING TRANSFER

Participants reflect individually on what they have learned and make commitments to put it to use back home after the workshop. (30 – 45 minutes)

3.1 WARM-UP EXERCISE: PROS AND CONS

TIME REQUIRED

45 minutes

PURPOSE

This exercise is to help participants recall and share experiences with citizen participation. This exercise will work effectively in workshops that include participants representing all four of the roles involved in financial management, a combination of these roles, or for single role workshops. If you have participants from different roles then it is an opportunity to explore the similarities and differences in their experiences and perceptions.

PROCESS

Ask participants to recall two personal or personally observed experiences with the involvement of citizens with local government and especially with government finance. The first experience should be one in which the interaction was successful; the second experience not successful. Distribute copies of the worksheet on the next page. Suggest that participants use the worksheet to describe both experiences, emphasizing what happened in each case and what local government officials did or did not do that accounts for or at least contributed to what happened.

After giving participants about 15 minutes to complete their worksheets, divide them into small groups of about five people. Give them about 20 minutes to share and discuss their experiences.

When the small groups reconvene, ask for any insights or patterns that might suggest what to do or not do when working with citizens.

If the participants are working in a local government that is operating under a more nationally centralised approach to local financial management, this is the right time to put this issue into perspective for the rest of this workshop on citizen participation. Ask participants to share their insights and experiences about this aspect of financial management and citizen participation. And, suggest that they keep this issue in mind as they engage in other learning activities in the workshop.

Worksheet: Incidents in Citizen Participation

In the space below, describe an incident in which one or more citizens interacted successfully with a local government. Include a brief description of the situation, your involvement with it, how it came about and the persons who participated in it.

In your opinion, what did government officials do or not do in the situation that caused or contributed to its success?

Next, describe an incident in which one or more citizens interacted unsuccessfully with a local government. Include a brief description of the situation, your involvement with it, how it came about and the persons who participated in it.

In your opinion, what did government officials do or not do in the situation that caused or contributed to its lack of success?

3.2 TRAINER PRESENTATION

TIME REQUIRED

30 minutes

PURPOSE

This presentation is to provide participants with information and perspectives on the positive and constructive participation of citizens in the affairs of a local government.

PROCESS

Prepare the presentation based on information covered by the preceding essay on citizen participation. Concentrate on providing a rationale for the participation of citizens in local government affairs, when and in what way to involve citizens and common techniques of citizen involvement. Outlined information on note cards may help you cover the information systematically and stay on schedule. Ask questions from time to time during the presentation as a check on participant comprehension and to hold their attention. Augment the presentation with visual aids including pre-printed newsprint sheets and overhead transparencies as a further aid to comprehension.

3.3 MINI-CASE STUDY: NOT WELL ADVISED

TIME REQUIRED

90 minutes

PURPOSE

The case illustrates the importance of using the right meeting format when involving citizens in local government affairs.

PROCESS

Working in small groups, tell participants they are to read a case that illustrates how relations with citizens can be threatened when a meeting advertised as informational is suddenly changed to a meeting meant to solicit public input on a thorny local issue. Provide each participant with a copy of the case “Not Well Advised” (see next page). Ask participants to read the case and, in their small groups, to discuss the case, answering the questions that follow the case.

Tell participants that, after 45 minutes, they are to return to the general session with their group’s answers to each question printed on sheets of newsprint and be ready to discuss their results with other group participants.

Mini-Case Study: Not Well Advised

The council budget committee staff sets up the meeting room in the usual format—committee members on a raised platform at the front of the room, staff and citizens below in auditorium seating—the format that has been used hundreds of times for informational presentations (see exhibit showing the budget committee room configuration). The purpose of the meeting is for the staff to present the committee's proposed budget to the public before its formal adoption by the governing body as required by the central government. The budget committee consists of nine members of which five are members of the governing body.

As the meeting is about to be called to order, the LG's finance director notices that an unusually large number of people has entered the room, filling up, every empty seat. She remembers being told that the opposition party might be using the occasion of this budget meeting to question the recent governing body ratification of a fare increase by the local transit authority. Even though the meeting has been advertised in the community as an opportunity for the public to be informed about the proposed LG budget, it soon becomes apparent to the finance director that many of the people in attendance are hoping they will be permitted to speak about the transit fare increase. It is at this point that the finance director approaches the committee chairperson and suggests taking a few minutes from the regular meeting so that citizens who want to be heard on the transit issue can have a chance to speak.

The chairperson, acting on the finance director's advice, announces that he is departing from the committee's advertised agenda. He explains his decision as follows:

"We realize that many of you have come here because you are concerned about the transit fare issue. And we want you to have a chance to be heard. So we're going to depart from our scheduled order of business to give you that opportunity. However, in thirty minutes, the public input period will end and the committee will return to its advertised agenda."

The chair person ends his statement by asking those who wish to speak to come forward to the speakers stand and identify themselves by name before addressing the committee.

The first citizen stands up. Ignoring the chairperson's request to come forward to identify herself, she launches into a tirade against the LG for permitting the authority to raise transit rates without giving the public a chance to comment. A second person jumps up and asks why only thirty minutes are being given to citizens to present their views while transit authority representatives have been allowed to meet privately for many hours with LG officials.

Without a procedure for participation and finding it difficult to hear or even see clearly, anxious citizens resort to shouting and waving their arms wildly to be recognized. As the meeting degenerates into a shouting match, the chairperson sees no alternative but to end it although only fifteen minutes have passed.

As the angry, disappointed citizens leave the room, the chairperson turns to the finance director and says: "If you have any ideas in the future about involving citizens in this committee's work, keep them to yourself. I don't ever want to go through this again."

Questions

1. Why was the chairperson badly advised in abruptly converting the informational meeting into a meeting designed to solicit public input?
2. When the chairperson decided to change to an advisory mode, what might have been done to prevent the meeting from disintegrating?
3. What, in general, is the chief drawback of public hearings and similar informational meetings as forums for encouraging public participation in government?

3.4 EXERCISE: MAKING CITIZEN PARTICIPATION WORK

TIME REQUIRED

75 minutes

PURPOSE

Give participants skill practice in choosing the right form of participation when there is a good reason to involve citizens in local government affairs.

PROCESS

Handout copies of the worksheet on the next page. Tell participants they will be working in small groups of five or six participants on an exercise that calls for them to match seven purposes for involving citizens in the affairs of a local government with seven common formats for citizen involvement.

Ask participants to work independently on the matching exercise. When finished, ask them to convene into groups of 5-6 participants to share their results with other members of their small groups. Explain that each group is to deliberate on each participant's results and to find a group solution to the matching exercise. Finally, ask participants in each small group to discuss their experiences with each type of citizen participation. Tell participants to select one example for each of the seven types and to print each example on a sheet of newsprint for reporting later in a large group meeting. Suggest that participants write down the examples agreed upon by the group in the space on the right side of their individual worksheets for future reference. Tell each small group it has 45 minutes to complete these tasks and return for a large group discussion.

In 45 minutes, ask small groups to report back and ask for reports from each group on the results of the matching task and to share some of their thoughts about the exercise.

Trainers note. The matching is done by reading each of the seven purposes for participation on the left side of the worksheet. From the list of seven types of participation at the top of the worksheet, select the one that is the most appropriate for each purpose. Use the space to the left of each purpose for citizen participation to enter the number corresponding with the type of participation that is felt to be the most appropriate.

Worksheet: Choosing the Right Method

Types of Participation

1. Advisory committee
2. Citizen survey
3. Focus group
4. Interview
5. Public hearing
6. Workshop
7. Written/electronic media

___ Gather information on a variety of issues from a large number of citizens.

(Example) _____

___ Stimulate thought and the flow of creative ideas for problem solving or decision making.

(Example) _____

___ Identify the nature and intensity of feeling within a group about a set of issues.

(Example) _____

___ Solicit input/reaction from time to time from a select group on work in progress.

(Example) _____

___ Obtain points of view and information about a subject from representatives of a target group.

(Example) _____

___ Inform people about or persuade them to support a project.

(Example) _____

___ Explain why, when, where and how a project is to be carried out.

(Example) _____

3.5 EXERCISE: PARTICIPATORY BUDGETING⁴

TIME REQUIRED:

120 minutes

PURPOSE

To provide participants with an opportunity to plan strategies for gaining the commitment of a local governing body to undertake a participatory budgeting process and the commitment of the management staff to support the elected officials in this new approach.

PROCESS

Divide participants into four teams and inform them that two of the teams will be responsible for developing a strategy for gaining the commitment of local elected officials to undertake a participatory budgeting process for the next fiscal year. The other two teams are to develop strategies for preparing key management staff to support the participatory budgeting process.

Provide two teams with the task assignment entitled Getting your local governing body on board and the other two teams with the task assignment entitled Getting your management team and employees on board. Tell the teams that they have one hour to develop their strategies. Also inform them that they are expected to present their strategies to the other participants and need to be prepared with visual aids, etc.

Reconvene the participants and ask the two teams responsible for the governing body strategies to report. Follow each report with questions for clarification only. After the second report and questions for clarification, hold a short discussion about the similarities and differences in the reports and the lessons to be gained from each team's efforts.

Follow those reports and discussions with the team reports on working with the key management staff members. Follow the same procedure suggested for the other two teams. Or, if you have better ideas on how to handle this exercise, by all means use them.

HANDOUTS:

TEAMS ONE AND TWO

The Chief Executive Officer (CEO) has just returned from a national meeting of local government CEOs and called a meeting of her management team to brief them on the meeting and to ask for their help on something that came up at the meeting. An official from UN HABITAT gave the keynote address at this meeting. It was on the proc-

⁴ For information on how to implement a participatory budget see UN-HABITAT (2004) *Frequently Asked Questions about Participatory Budgeting*.

ess of participatory budgeting and the benefits that local governments can gain from engaging in this process. The CEO was inspired by the presentation and wants to put the possibility of your local government adopting such an approach on the next governing body meeting agenda. She also knows that the governing body had considered more citizen involvement in the budgeting process and voted it down about two years ago. She has asked your team to develop a strategy that she can use to convince the governing body to reconsider involving citizens in the budgeting process for the next fiscal year and beyond.

TEAMS THREE AND FOUR:

The Chief Executive Officer and Finance Director have asked your team, consisting of the managers of all the key operating and support departments of your local government, to develop a strategy for working with the governing body to implement their new participatory budgeting policy. They haven't provided your team with much information about this policy since they want your "unbiased" ideas on how you can support this new participatory venture. Essentially, they want to know who should do what with whom to make sure that this new policy is implemented successfully.

3.6 EXERCISE: SERVING THE PUBLIC INTEREST

TIME REQUIRED

120 minutes

PURPOSE

To gain experience in developing proposals for the involvement of citizens in local government decision making.

PROCESS

Ask participants to read a critical incident in which a governing body, acting as an agent for the community to give a badly needed boost to the local economy, makes a decision that outrages local residents. Handout a copy of the incident, "Where's the Public Interest?" Divide participants into several small groups. Ask each small group to answer the three questions at the end of the incident. Explain that each small group is to report back in one hour with answers to the questions including the agenda for the first task force meeting printed on a sheet of newsprint.

When small groups reconvene, ask for each group to share its answers to the three questions and present an agenda for the first task force meeting. Encourage a comparison of thoughts and approaches and a discussion of the implications of the exercise for them ore active involvement of citizens in a local government's programs and planning processes.

Critical Incident: Where's the Public Interest?

A leading manufacturer has been investigating several LGs including River Bend as a site for its newest assembly plant. LG leaders see the plant acquisition as a major economic boost for River Bend and a source of training and an employment source for hundreds of local residents. The importance of not losing this opportunity is evident to anyone familiar with the serious economic woes that have beset the community over the past two decades (several major business failures, the highest level of unemployment in the town's history, a loss of more than 10 percent in the commercial/industrial tax base, and so forth). The possibility of acquiring an employer of this magnitude is the most important developmental opportunity to come the community's way in many years. As one governing body member puts it, "this plant coming here is truly a gift from heaven."

Only one obstacle stands in the way. A public park located near the centre of town is the only site acceptable to company officials for their new plant. For many years, the park has been a popular recreational attraction for hundreds of LG inhabitants who live and work in walking distance of the park. In fact, the park is one of the few open spaces left in an otherwise densely developed urban area.

Company officers have made the LG an attractive offer to purchase the park and insist on a quick decision because the company is considering a similar site in a neighbouring town. At an emergency meeting, the council votes 7 to 2 to accept the company offer. The next day an announcement about the council action and the site selected by the plant appears in the local newspaper. One councillor, asked by a newspaper reporter if citizens should have been consulted by the council before accepting the company offer, replies: "As representatives of the people, councillors are not expected to check back with their constituents every time there is a decision to be made. We're just doing the job they elected us to do."

Two days later, the council room is filled to overflowing with angry citizens protesting the impending loss of their beloved park. The council is vehemently scorned and derided for giving up the park. There are suggestions of violent protest at future meetings. There are threats of action to force the resignation of councillors and the dismissal of staff who supported the council in its decision.

Shaken by the confrontation and fearful of possible violence, the mayor calls an emergency meeting of the governing body at which councilors vote unanimously to appoint a task force to make recommendations for the active and continuous involvement of citizens in local government policies and programs. The work of the task force is given the highest priority and its recommendations are urgently awaited by the council. In closing the meeting, the mayor puts into words the fear that grips each member of the council: "I just hope and pray it's not too late."

Questions

1. Based on the limited facts presented in the River Bend situation, do you believe the governing body did the right thing? If so, did they do it the right way? Explain your reasoning.
2. How do you interpret the words uttered by the mayor at the close of the council meeting?
3. Assume you are the finance director of River Bend and have been appointed to chair the LG's new citizen participation task force. Who would you appoint to serve with you on the task force? Considering what has just happened in the community, what would you visualize as a successful product or outcome of the task force efforts? What would you propose as an agenda for the first task force meeting?

3.7 CLOSING EXERCISE: LEARNING TRANSFER

TIME REQUIRED

30-45 minutes

PURPOSE

This exercise is to help participants transfer the learning experiences of the workshop into their real-world activities as finance directors. The focus of this exercise is on raising expectations, engaging in realistic planning and making personal commitments. Most of the work is done on a personal basis with some interpersonal sharing.

PROCESS

Spend at least half an hour at the end of the workshop to focus the attention of participants on important learning and encourage them to continue experimenting with these learning in their management activities. Begin by giving participants about fifteen minutes to work independently on a simple learning transfer questionnaire. When participants have completed the questionnaire, ask them to share quickly with the group two or three things they intend to do differently in their roles with respect to citizen participation to close the workshop.

Trainers note. It is generally agreed that the purpose of training is to improve the way people do things by showing them a better way. In fact, the success of a training experience can be measured by the amount of personal growth and change that takes place both during training and after the training is over.

Commitments to learning and change made at the close of a workshop can help participants overcome learning resistance in themselves and in the work environment. A trainer can help learners make a successful transition from the world of learning to the world of doing through a few simple planning exercises.

A Learning Transfer Questionnaire

Take a few minutes to reflect on citizen participation, the new ideas you encountered in this workshop, and how you feel about them. Then, in the space below, write a sentence or two to describe something interesting you have learned about yourself during this workshop.

Based on what you have learned about yourself and the many possibilities for change presented by this workshop, what two or three things do you intend to do differently in involving citizens in local government planning and programs?

1.

2.

3.

Finally, what obstacles in yourself or in your work environment do you expect to experience during your efforts to implement these changes? What will you do to remove or minimize these obstacles?

Expected Obstacle

1.

2.

3.

Action to Remove It

1.

2.

3.

Evaluating Financial Condition

PART ONE: CONCEPTS, PRINCIPLES, AND STRATEGIES

SUMMARY

This essay provides local government (LG) elected and appointed officials with a method for monitoring their LG's financial condition. The information can be used to:

- Better understand the LG's financial condition—the forces that affect it and the obstacles associated with measuring it,
- Identify existing and emerging financial problems, and
- Develop actions to remedy these problems.

This monitoring is accomplished using a process that identifies and organizes key factors that affect financial condition so that they can be measured and analyzed. The data needed to perform the analysis is taken from a LG's financial records and from national (central government) census information.

This process will help any LG that finds itself in one or more of the following situations:

- Under the strain of a few identifiable financial problems and wants to gain a broader perspective on these problems,
- Senses that financial problems are emerging but is having difficulty pinpointing their origin or developing a strategy for coping with them, and/or
- In good financial condition but needs a systematic way to monitor changes and anticipate future problems.

The completed analysis of financial condition for key factors should be compiled and presented in a written report and made available to the LG's policy makers as well as citizens, committees, employees, bond rating agencies, and others interested in the LG's financial health. Each year the key indicators should be updated so that the monitoring is ongoing.

RELATIONSHIPS BETWEEN CHAPTERS OF THE SERIES

The following matrix shows the interrelationships between Evaluating Financial Condition and other chapters in the series.

	Evaluating Financial Condition
<i>Introduction</i>	The Introduction provides the framework for using the entire series.
<i>Trainer’s Guide</i>	Provides guidelines for using the chapters to provide training.
<i>Financial Policy Making</i>	Financial policy making provides the framework for evaluating the financial condition of the LG.
<i>Financial Planning</i>	Financial planning is the long-term plan for where the community is going. Financial condition is a current status. To achieve the long-term plan various elements of the current financial condition may need to change. The indicators help pinpoint those areas.
<i>Citizen Participation</i>	Citizens have a stake in the financial health of their LG, even when they are not paying taxes or revenues directly to the LG. If the financial condition worsens then the quality of public services provided for citizen’s will be impacted.
<i>Operating Budget</i>	Elements of the operating budget are an integral part of the framework that determines a LG’s overall financial condition. For example, revenues, expenditures, etc.
<i>Financing the Operating Budget</i>	Elements of the operating budget are an integral part of the framework that determines a LG’s overall financial condition. For example, revenues, expenditures, etc.
<i>Capital Investment Plan (CIP)</i>	Elements of the capital investment plan are an integral part of the framework that determines a LG’s overall financial condition. For example, revenues, expenditures, capital assets, etc.
<i>Financing the Capital Investment Plan</i>	Elements of the capital investment plan are an integral part of the framework that determines a LG’s overall financial condition. For example, revenues, expenditures, capital assets, etc.
<i>Accounting</i>	The accounting records provide a large portion of the data used in evaluating financial condition.
<i>Performance Measures</i>	Evaluating financial condition is looking at indicators or measures. Some of these are performance related and others are more demographic in nature. The concepts of performance measures apply to evaluating financial condition. After indicators are established, performance measures can be set to improve the various aspects of a LG’s financial condition.
<i>Asset Management</i>	The largest investment a LG makes is in its assets. These include streets, clinics, water systems, fire trucks, etc. Financial condition is one way of evaluating how well those assets are being maintained and utilized. Assets that are rapidly deteriorating will eventually affect the financial condition of the LG.

INTRODUCTION

We recognize that basic or introductory concepts are relative—depending upon your background and frame of reference for both evaluating financial condition and local government. Users of this material will range from those who have no knowledge of evaluating financial condition principles or concepts to those who have a very so-

phisticated understanding. The following are our ideas of what represents the most fundamental principles and concepts needed to evaluating financial condition at a beginning level.

The set of indicators provided in this chapter are illustrative. Each country will need to define the terms, data elements and indicators that make the most sense for them. If you are in a highly centralized country, many of these indicators are beyond the control of the governing body and LG managers. But we believe that all countries can use some of the indicators. It is a matter of evaluating your current country situation and determining which of the indicators will provide insight into the financial condition of your LG. We encourage you to work with other LGs within your country to arrive at a common set of indicators that allow you to constantly evaluate and improve your LG's financial condition.

We encourage you to work with an accounting professional in developing the indicators for your country since there are accounting and budgeting terms and concepts that are implicit to the understanding of the development of some of the indicators. The indicators are based on a United States framework with its fund accounting, accrual accounting, etc. For those countries that use cash accounting, the worksheets will need to be modified accordingly to reflect accruals and due to and due from accounts. Please refer to the Accounting¹ and Operating Budget² chapters to become familiar with some of the basic concepts of budgeting and accounting. This understanding is important for both trainers and trainees.

BASIC CONCEPTS AND DEFINITIONS

The term financial condition has many meanings. In a narrow accounting sense, it can refer to a LG's ability to generate enough cash over thirty or sixty days to pay its employees and bills. It can also refer to a LG's ability to generate enough revenues over its normal budgetary period to meet its planned expenditures and not incur deficits.

In an even broader sense, financial condition can refer to a LG's ability, in the long run, to pay all the costs of doing business, including expenditures that normally appear in each annual budget, as well as those that will appear only in the future years in which they must be paid. Unless monies have been set aside for future payments, these costs will have to be paid at that time from the annual budget. These are called unfunded future costs. Examples of these future costs are pension costs and payments for accrued employee leave. Although these costs will eventually appear in a budget, a short-run financial analysis (one to five years) may not reveal them. This long-run balance between revenues and costs warrants separate attention.

Finally, financial condition can refer to a LG's ability to provide services at the level and quality that are required for the health, safety, and welfare of the LG and that its citizens desire. A LG lacking service-level solvency might in all other respects be in sound financial condition, but be unable to support education, health, police or fire services at an adequate level, and suffer cash, budgetary or long-run solvency problems if it tried to provide adequate services.

In summary, financial condition can be broadly defined as a LG's ability to finance its services on a continuing basis. More specifically, financial condition refers to a LG's ability to (1) maintain existing service levels, (2) withstand local and regional economic disruptions, and (3) meet the demands of natural growth, decline, and change.

DEFINITIONS

Definitions are included in the text as needed.

FRAMEWORK FOR EVALUATING FINANCIAL CONDITION

In almost every country, LGs produce budgets showing revenues and expenditures, and are required to balance their budgets in one fashion or another. Most LGs also produce year-end financial statements that include balance sheets and operating statements, but these are prepared only for a one-year period and do not show in a multiyear perspective the emergence of favourable or unfavourable conditions.

They show the flow of money in and out of the LG during a particular year, but they do not provide the information needed to evaluate long-term financial condition. For example, they do not show:

- Maintenance costs that are being postponed.
- Accumulated unfunded pension liabilities or employee benefit liabilities.
- Reductions in purchasing power caused by inflation.
- Decreasing flexibility in the use of monies that results from unfunded central government mandates.
- Erosion of streets, water plants, buildings, and other capital assets.
- Impact of economic and demographic changes to changes in revenue and expenditure rates.

Most financial problems do not develop suddenly. Instead they build over time. Generally speaking, they can be traced to one or more of the following situations:

- A decline in revenues.
- An increase in expenditure pressures.
- Decreasing cash and budgetary surpluses.
- A growing debt burden.
- The accumulation of unfunded liabilities.
- The erosion of capital plant.
- A decline in tax base or an increase in the need for public services.

In summary, the basic questions that officials must address are:

Can the LG continue to pay for what it is now doing? Are there reserves or other ways for financing emergencies? Is there enough financial flexibility to allow the LG to adjust to change?

If a LG can meet these challenges, it is in sound financial condition. If it cannot, it is probably experiencing or can anticipate problems.

LEARNING APPLICATION

In the first Learning Application in each of the chapters in this series we will be reminding the reader about how to get the most from each of these exercises. First, there is a box identifying the four key LG roles that most readers represent. These are Policy Makers (elected officials), CEOs (Chief Executive Officers such as mayors, city managers, etc.), Finance Managers (the chief finance official in the LG), and Department Heads (those individuals who are responsible for the management of specific LG departments such as public works, planning, and human resources). Second, we will indicate in the box those readers we believe will benefit most from completing the learning application task. Finally, when more than one official is listed, we see this as an opportunity for these individuals to get together and compare their responses. These Learning Application opportunities can also be modified to become training exercises for group learning. So, our advice is to make the most of these reflective interludes in the text.

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

From your unique role, consider what you have just read. Does your LG experience any of these problems currently? Jot these down and then describe your greatest concern about the impact they may be having on your LG's financial condition.

DEVELOPING THE INDICATORS

We recommend the following steps for developing the indicators.

STEP 1 ORGANIZE THE PROJECT

A first step is to clearly define who will be responsible for what in developing and interpreting the indicators. This includes clarifying the roles of citizens, governing body members, and the chief executive officer and his/her staff.

Citizens—The degree to which citizens are involved in the process is a matter policy makers will need to decide. It may be helpful to inform those citizens and organisations that might be most interested in the results of the financial evaluation, i.e. businesses, community groups representing minority members of your community, financial institutions, etc.³ If there are financial experts in your community, you may want to ask for their help in developing the indicators.

Governing body members—Upon completing the financial evaluation, elected officials, as LG's designated policy makers, will have a role in this process. Here are a few of the more important ones.

- Identify areas where financial policies are needed.
- Direct staff to explore what other local governments are doing in identified areas of policy concern. In other words, ask them to carry out a comparative analysis.
- Approve the final policies.

Chief executive officer—It is very important that the chief executive be involved in: 1) choosing which indicators to develop, 2) adjusting the definition of the indicators to allow for the uniqueness of the community and the LG, and 3) interpreting the indicators' significance

The CEO or finance director should direct the following: 1) identify areas where policies are needed, 2) involve staff in conducting research into specific policy needs and how other local governments have dealt with the issues associated with specific policies under consideration, 3) develop policy options to be considered by the local governing body, 4) based on their deliberation of the policy options, draft the final version of the policy for their consideration, 5) submit the draft policy to the local governing body for their adoption, and 6) implement the approved policy.

TIME AND RESOURCES REQUIRED

The persons performing the financial evaluation should understand the causal factors related to each trend, appreciate the interrelationships among the trends, and be familiar with the LG's organization and operations—including its recent political, administrative, and financial history. They should keep three things in mind:

1. No single indicator is conclusive. All the indicators chosen for study should be examined simultaneously, along with other political and administrative characteristics of the LG.
2. If the LG has changed its basis of accounting or reporting procedures during the years covered by the study, the indicators should be adjusted accordingly.

3. The benchmarks used by credit-rating firms are not universal standards but guidelines that must be evaluated in light of the characteristics of each LG and each country.

The use of spreadsheet software on a personal computer can greatly reduce the time spent on performing calculations, developing graphics, and typing the analysis and other narrative that are part of each indicator. Therefore, a staff person with some experience in using spreadsheet software should be part of the analysis team.

The amount of time required for the initial study depends on the quality of the LG's financial records, the background and knowledge of the individual(s) working on the study, and the number of indicators selected for developing. Once the initial study is completed, the annual updates require only a few days.

A staff person with knowledge of both accounting and spreadsheet software, working with audited, consistent financial data, and developing at least 20 indicators (about the minimum number of indicators for a balanced, comprehensive analysis of financial condition), should be able to complete the initial study in about two weeks' time.

The initial analysis should include three to five years of historical data. If at least three years of data are not available, the study should begin with what is available, and the data should be recorded for future use.

The study can be done at any time during the year, but the best time is before budget preparation, when the staff will already be developing most of the information; the study can also provide valuable background for budget decisions. Another good time to do the study is just after the completion of the audit report, when financial data from the previous year are first available; the study can put the audit report in better perspective.

STEP 2 *EVALUATE THE INDICATORS*

Many countries are in a decentralizing process. We provide 3 models that demonstrate different characteristics of LGs at different points in the decentralization process. Your country is probably somewhere between two of the models. The purpose of the characteristics is to provide a frame of reference for determining which basic indicators may apply in your country. The CEO and finance director have primary responsibility for determining which indicators are most applicable for your LG.

	Centralized—Model 1	Mid-decentralized—Model 2	Decentralized—Model 3
Revenue	Minimal own source revenues. Revenues may be tied to providing specific services.	Developing own source revenues. About 30-50% of total revenues.	Primarily own source revenues. About 80-100% of total revenues.

Services provided	Mandated services (e.g. education, health, streets, etc.) provided by all LGs.	Provide past mandated services, more flexibility in management of how services are provided. May provide new services.	Provide services based on community-identified needs.
Debt	Long-term bonds and notes are not issued by a LG. There may be short-term borrowing from the central government bank.	Beginning to issue long-term bonds and notes. Beginning to borrow various instruments from financial institutions	Long-term bonds and notes issued by a LG. Borrowing from financial institutions.
	Use following initial indicators	Use initial indicators plus following indicators	Use all indicators
Revenues	2. Restricted revenues 3. Intergovernmental revenues 5. One-time revenues 9. Revenue shortfalls	1. Revenues per capita 4. Elastic tax revenues 6. Property tax revenues 7. Uncollected property taxes 8. User charge coverage	
Expenditures	10. Expenditures per capita 11. Employees per capita	12. Fixed costs 13. Fringe benefits	
Operating position	14. Operating deficits 16. Fund balances 17. Liquidity 18. Current liabilities	15. Enterprise losses	
Debt		19. Long-term debt 20. Debt service	21. Overlapping debt
Unfunded liabilities		22. Unfunded pension liability 23. Pension assets 24. Accumulated employee leave	
Capital plant		25. Maintenance effort 26. Capital outlay 27. Depreciation expense	

Community needs and resources	28. Population	29. Median age 30. Personal income per capita 31. Poverty households or public assistance recipients 32. Property value 33. Residential development 34. Vacancy rates 35. Employment base 36. Business activity	
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You do not have to develop all the basic indicators. Some may be inappropriate or unnecessary for your situation. If, for example, your LG has no debt, the debt indicators can be disregarded. Availability of data is another issue to consider. For example, Indicator 25, Maintenance Effort, focuses on whether a LG is adequately maintaining its streets and other capital assets. If departmental records do not include information on street expenditures, then you need to decide whether expenditures can be reasonably estimated and whether the cost of that effort is worth the benefit. If you find that some data are not available for the current and prior years, you may consider beginning to collect the information so that it will be available in the future.

You may be tempted to choose based on your intuitive knowledge of the LG's finances. This approach can defeat the underlying assumption of this method: that a LG can have problems and not know it. Therefore, eliminate only those indicators that are clearly inappropriate and try to develop the rest.

Which of the indicators will be most important depends on the structure of your LG and its economic, demographic, and political characteristics. At first glance it might appear that some of the more general indicators, such as Revenues per Capita (Indicator 1) or Expenditures per Capita (Indicator 10), would be the most valuable because they cover the broadest range of issues. But considering only the broad indicators and not the others in each indicator group may leave important issues under-examined. For example, looking only at Revenues per Capita might not reveal trends such as an increasing dependence on onetime revenues (Indicator 5) or an increasing percentage of uncollected property taxes (Indicator 7). It is difficult, if not impossible, to give advice on which indicators should be developed by any particular jurisdiction. Officials in each LG need to examine the indicators closely and decide themselves, which are most important.

STEP 3 COLLECT DATA FOR WORKSHEETS

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

1. Review the “Description” section of each indicator. After reading the “Commentary” section, identify anything that might be a concern for you in developing the indicator.
2. Review the “Suggestions for Further Analysis” for each indicator, then note whether you think you will do any of the suggested analytical procedures and if this will require additional data collection.

STEP 4 DEVELOP THE INDICATORS AND PLOT THEM OVER TIME

The description of each indicator includes a trend worksheet that explains which information is needed, where to get it, and how to do the calculations. Do not hesitate to change the trend worksheets to meet your needs. The worksheets are only guides.

Plot the financial indicators over at least three to five years. This period is likely to include at least one turn in the national or regional economy and to provide enough perspective to reveal emerging trends.

To plot the economic and demographic indicators use whatever current data or estimates are available for the past five years, plus data from the last census or other reports covering two ten-year intervals in the last twenty-year period. This will provide the longer-term perspective needed for evaluating economic and demographic change.

CONTROLLING FOR INFLATION

Many of the indicators that use currency require that those figures be expressed in constant “adjusted for inflation” currency. This is usually done by using an inflation index published by a central government agency or university in your country. If this type of information is not available, you will have to make your own estimates of inflation rates.

For this chapter’s purposes, we are going to use dollars. Only indicators that compare dollar figures to non-dollar figures (e.g., net operating expenditures to population) need to be adjusted for inflation. Those indicators that compare dollar figures to other dollar figures (e.g., restricted revenues as a percentage of net operating revenues) do not need to be adjusted because both figures would be adjusted with the same price deflator, and the relationship between them would remain constant whether constant dollars or real dollars were used.

STEP 5 EVALUATE THE RESULTS

The primary tool for evaluating the indicators is trend analysis—examining each indicator over a period of at least five years and preferably longer. Trend analysis offers several advantages. First, it allows officials to determine how fast an indicator is changing and in which direction. Second, it permits one trend to be compared with another. Third, it permits the local trends to be compared with regional and national

trends. And finally, it provides a database that can be used to make the two- and five-year projections necessary for effective budgeting, capital projections, capital facility planning, and general policy making. In addition, the information on trends will help demonstrate to bond-rating firms that the LG is aware of and in control of its finances, although it may be experiencing some problems.

The steps in completing the trend analysis are as follows:

- Identify unfavourable trends. Each indicator has a section entitled “Warning Trend.” If an indicator is moving in the direction of the arrow it should be considered—at this point—potentially unfavourable.
- Determine when the unfavourable trend began. How fast is the indicator changing? Is it getting better or worse? How serious is the problem? If an unfavourable trend is evident for three or more years, it should be carefully examined as a potential problem. Determine whether the problem exists based on your general knowledge of the LG and the existence of mitigating circumstances.
- Consider mitigating circumstances. A mitigating circumstance neutralizes what at first glance appears to be an unfavourable trend. For example, problems associated with a rise in per capita expenditures could be mitigated by a proportionate rise in per capita revenues. This assumes that a revenue-rich LG can afford higher per capita expenditures, especially if the revenue growth is unrestricted. If, however, the revenue growth is caused by a rise in restricted revenues such as grants, and the growth in expenditures is due to an increase in programs supported by general revenues such as recreation or police services, then the rise in per capita expenditures may indeed be a warning signal.
- The rule of thumb is that no single trend implies a good or a bad financial condition. It only points to a situation that should be examined more closely. Each potentially unfavourable trend needs to be broken down into its component parts, analyzed in light of its causes and significance, and evaluated in relation to other trends. The indicator narratives are designed to help you accomplish this evaluation.
- Identify the causes underlying the unfavourable trend. Is the trend due to a decline in the tax base, insufficient controls over expenditures, ineffective revenue collection procedures, or inflation? What are the possible strategies for dealing with the problem? The discussion of each indicator includes a section entitled “Suggestions for Analysis.” These suggestions will help you to identify possible causes.
- Compare the indicator trends to one another. Each indicator should be analyzed in relation to the other indicators. One helpful approach is to plot the indicators you are comparing on the same graph or to use overlapping graphs. For example, revenue and expenditure growth could be analyzed together. If revenues per capita are growing in proportion to expenditures per capita, there may be no problem, but increasing expenditures and decreasing revenues are a sure sign of problems.

You can also analyze groups of related indicators, such as the nine revenue indicators. You might find, for example, that seven are moving in a favourable direction and two are moving in an unfavourable one. The comparison would highlight the unfavourable trends, but it would also allow you to conclude that revenue indicators are favourable overall.

- Compare the economic condition of the LG to national trends. Is the LG's economy declining while the national economy is growing? If so, what will be the effect of a regional or national downturn? The answer to this question requires a certain amount of guesswork, but the issue is worth considering and is important to credit-rating firms.
- Determine whether further analysis should be done. Additional analyses are described that can help you better understand the magnitude of a problem or isolate the particular influences that may be contributing to an unfavourable trend. Digging deeper can sometimes help you focus your effort as you begin developing remedial steps.
- Compare the trends to the benchmarks used by credit-rating firms. Credit-rating firms often use indicators, and these firms have developed benchmarks for evaluating the indicators. Where applicable, these benchmarks have been included in discussions of the indicators. You will have to determine the validity of these benchmarks for your own LG, but if a trend compares unfavourably, at least you will know which issues to address when you seek a credit rating.

The credit-rating industry looks at virtually all the remaining indicators in one way or another, even though no generally accepted, quantifiable benchmarks exist for them. The absence of normative standards underscores the importance of considering other factors.

- Take other factors into consideration. Five of the factors discussed do not have any quantifiable indicators, but the descriptions of the factors include evaluation questions to help you think subjectively about their influence on your LG's financial condition. You might want to develop a summary paragraph for each of these factors, assessing it as a positive or negative influence and noting your reasons.
- Add your professional judgment. Because of the tremendous diversity among LGs world-wide and the number of possible mitigating circumstances, no single set of rules can apply to all LGs. As was noted earlier, this process does not provide solutions to problems. It does provide a systematic means of organizing and quantifying the information that needs to be considered. The final interpretation of the data is up to the financial decision makers of the individual LG.

STEP 6 DEVELOP POLICY STATEMENTS

Once you have determined where problems exist and understand their nature and magnitude, you should devise strategies for dealing with them. The development of effective strategies begins with understanding the causes of problems and the interre-

relationships among them. Next, you must relate your understanding of the problems to specific community needs and objectives. One way to do this is by specifying LG financial objectives in policy statements. Financial Policy Making⁴, another chapter in this series, provides extensive information on developing policies. Most of the indicator narratives close with suggestions for policy statements, which are included to help local officials formulate action steps to prevent or improve unfavourable trends. The precise content or wording of these suggested policy statements may not be right for every LG; you are encouraged to alter the suggested statements to meet local needs. Using policy statements to set financial goals gives you a means of measuring your progress in improving your LG's financial condition.

INDICATORS

The following indicators are based on terminology and definitions from the United States. They are a comprehensive approach to evaluating a LG's financial condition. For you to use the indicators, you must evaluate them to see if they make sense for your LG and your country. The terminology may be different and some indicators will not be possible

For example, "net operating revenues" probably is defined differently in your country. So, many of the terms used in the indicators will need to be specifically defined for your country. Consider these indicators as illustrative and a starting point for developing a set of indicators for your country. We suggest that you work together with other LGs to accomplish this.

LGs in sound financial condition can afford to continue paying for the services they now provide. In addition to basic services usually funded by "own source" revenues, this would include the ability to maintain programs that are currently funded by external sources such as grants. Current service levels also include the maintenance of capital facilities, such as streets and buildings, in a manner that protects the initial investment and keeps the facilities in usable condition. Finally, continued provision of services requires funds for future liabilities that may currently be unfunded, such as pension, employee leave, debt, or lease-purchase commitments. To determine if your LG can continue providing the current service level we will look at revenues, expenditures, capital plant, debt and unfunded liabilities.

In the following pages each indicator is presented with the following information:

- Graph illustrating the warning trend
- Formula
- Description
- Suggestions for analysis.

The graph preceding the discussion of each indicator is an example to help you visualize the warning trend. Create your own graph for each indicator using the data you collect for your LG.

We strongly recommend that after the data for each indicator are collected and the ratios calculated, a graph should be constructed to represent visually the multi-year trends occurring in the LG's finances. The graphs are an important part of the indicator system because they are a powerful tool for communicating with elected officials, citizens, employees, and potential investors.

However, with personal computers, electronic spreadsheets, and special graphing programs, managers can now easily create many different types of graphs. Some types of graphs are better for showing trend information than others. If you find that an indicator is moving in the direction shown, that indicator is reflecting a potential problem that requires further analysis.

Examples are provided based on the following assumptions:

That the country uses fund accounting.

That the unit of currency is a U.S. dollar.

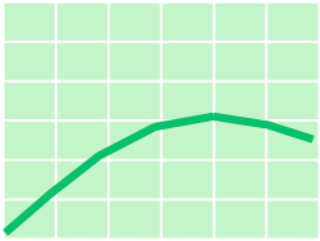
REVENUES

Revenues determine the capacity of a LG to provide services. Important issues to consider in revenue analysis are growth, flexibility, elasticity, dependability, diversity, and administration. Under ideal conditions, revenues would be growing at a rate equal to or greater than the combined effects of inflation and expenditures. They would be sufficiently flexible (free from spending restrictions) to allow adjustments to changing conditions. They would be balanced between elastic and inelastic in relation to inflation and the economic base; that is, some would grow with inflation and the economic base and others would remain relatively constant. Revenue sources would be diversified and primarily own source revenues—not overly dependent on residential, commercial, or industrial land uses, or on external funding sources such as transfers from the central government. User fees would be established and administered at the LG level and would be regularly evaluated to cover cost increases for related services.

Analyzing revenue structure will help to identify the following types of problems:

- Deterioration of the revenue base,
- Practices or policies that may adversely affect revenue yields,
- Lack of cost controls, or poor revenue-estimating practices,
- Inefficiency in the collection and administration of revenues,
- Overdependence on obsolete or intergovernmental revenue sources,
- User fees that are not covering the cost of services, and
- Changes in the tax burden (especially property tax) on various segments of the population.

INDICATOR 1: REVENUES PER CAPITA

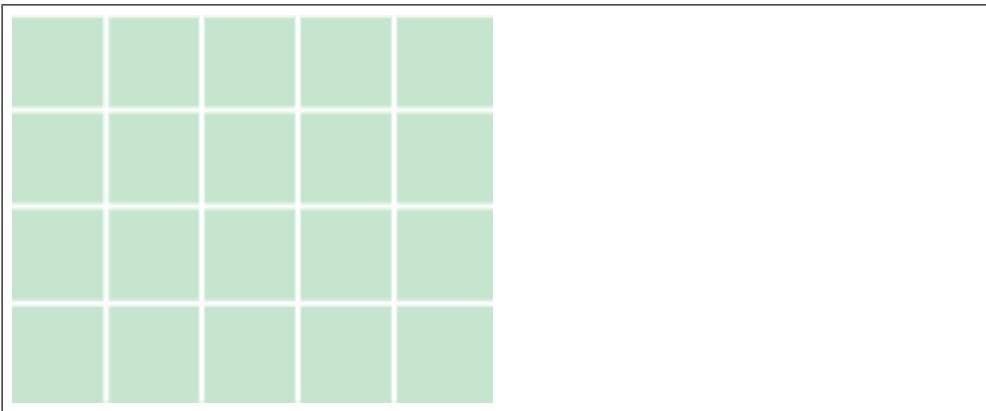
	<p>Examining per capita revenues shows changes in revenues relative to changes in population size. As population increases, it is reasonably expected that revenues and the need for services would increase proportionately and therefore that the level of per capita revenues would remain at least constant in real terms. If per capita revenues are decreasing, the LG may be unable to maintain existing service levels unless it finds new revenue sources or ways to save money. This reasoning assumes that the cost of providing services is directly related to population size.</p> <p>When presenting this indicator in a report, you should define for the reader what your LG's "net operating revenues" includes.</p> <p>Revenues per capita is adjusted for inflation, i.e., current dollars are converted to constant dollars. In graphing this indicator, you can include two lines showing both current and constant dollars to demonstrate the impact of inflation. After adjusting revenues for inflation, you may be surprised to find that the effects of inflation may have created much of the growth in revenues.</p> <p>Although the formula for this indicator shows total population in the denominator, you may also want to calculate this indicator using "number of house-holds" as the denominator. In many LGs, the overall population may be dropping, but the number of households may be stable or even increasing, as smaller households form. Because many services are delivered on a per household basis, the cost of services may more logically be related to the number of households than to the total number of residents.</p>
<p>Warning Trend— Decreasing net operating revenues per capita (constant dollars)</p>	
<p>Formula— $\frac{\text{Net operating revenues (constant dollars)}}{\text{Population}}$</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Net operating revenues	Worksheet 2 (W2), line 13					

2	Consumer price index (CPI) for the LG area	Central govt or uni- versity					
3	CPI in decimal	Line 2 / 100					
4	Net operating revenues in CPI based-year dollars	Line 1 / Line 3					
5	Current population	W7, Line 1					
6	Net constant dollar operating revenues per capita	Line 4 / Line 5*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are starting points for this analysis. If revenues are decreasing, the following issues should be considered:

- Is the LG experiencing general economic decline? Is the decline a temporary or continuing trend? See indicators for Community Needs and Resources.
- Is the decline related to changes in population, such as a decrease in population groups that historically generated the largest portions of revenue- such as property taxes? See indicators for Community Needs and Resources.
- Is the decline due to problems inherent in the revenue structure, such as overdependence on inelastic revenues during a period of inflation? See Indicator 4, Elastic tax revenues.
- Are central government or local restrictions (such as tax limitations) preventing the LG from instituting the appropriate taxes, fees, or charges?
- Is there a limited amount of “own source” revenues?
- Can revenues be increased by any of the following measures?

- Revising revenue collection procedures
- Reducing tax delinquencies,
- Instituting or increasing service charges, fines and penalties, license and permit fees,
- Instituting or increasing charges for use of facilities, equipment, or personnel,
- Updating property assessments,
- Establishing special assessment districts,
- Investing a greater proportion of idle cash,
- Selling surplus property or equipment,
- Securing special-purpose or grant funding from public or private agencies.

If revenues per capita are increasing, the following issues should be considered:

- Is it reasonable to assume that the increased level of revenues will continue? If these revenues are being used for new programs that will require continued funding, what plans does the LG have for the time when these revenues are no longer available?
- Is the increase in revenues per capita a sign that costs will increase in future years—as would be the case, for example, if the new revenues were derived from an increase in building construction? Will the additional revenues cover the additional costs? If not, is there a plan for funding these costs?
- Is the increase in revenues per capita due to a decline in population rather than to an increase in revenues? If so, will the decline in population eventually create a decline in revenues? Is the decline in population accompanied by an increase in the number of smaller households, which can result in higher service costs to the jurisdiction?
- Do the increased revenues per capita represent an increase in the tax burden, measured by comparing changes in revenues per capita to changes in personal income, business income, or other measures of community wealth? If the tax burden is increasing, will residents and business owners be less able to pay? Might they be tempted to relocate to a LG that has a lower tax burden?

Suggestions for further analysis—When analyzing revenues, officials should develop trend lines for both (1) total revenues per capita and (2) any individual revenue source that makes up 5 percent or more of total revenues, such as property taxes, business licenses, fines, and user fees. If the LG organizes its revenues into specific groups, such as restricted, unrestricted, or self-supporting, then these groups can also be a focus of additional analysis.

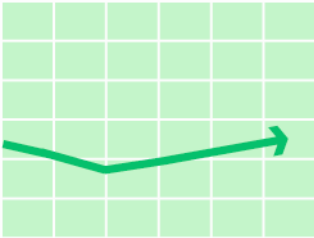
You may also want to consider whether the revenue structure has changed over the past five years. This can tell you if some revenue sources are growing faster than others, if the revenue burden is shifting from one segment of the population to another (e.g., from property owners to utility consumers) and if the growth in the rates

of some revenues has not been keeping pace with that of others. Any such changes in revenue structure should probably receive attention from policy makers.

Suggestions for policy statements—Policy statements can be developed to require procedures for budgeting and analyzing revenues. The following policy statements can help local officials relate this indicator to their financial decision making.

- A diversified and stable revenue system will be maintained to shelter the LG from short-run fluctuations in any one revenue source.
- Revenues for the next _____ years will be projected and updated annually. Each existing and potential revenue source will be re-examined annually.

INDICATOR 2: RESTRICTED REVENUES



Warning Trend— Increasing amount of restricted operating revenues as a percentage of net operating revenues

Formula— $\text{Restricted operating revenues} / \text{Net operating revenues}$

A restricted revenue is legally “earmarked” or set aside for a specific use, as may be required by law, bond covenants, or grant requirements. For example, a country may require that petro tax revenues be used only for street maintenance or construction.

From one perspective, it would seem that many of these restrictions, especially those relating to outside funding, should not affect a LG’s financial health. For example, with grants the LG has the option of not accepting the revenue and of not providing the service. This option, however, is not always easy to exercise; LGs develop economic and political dependencies on these revenues and on the programs they support. Also, many LGs finance their own essential services with intergovernmental revenues, which makes it doubly hard to cut them out.

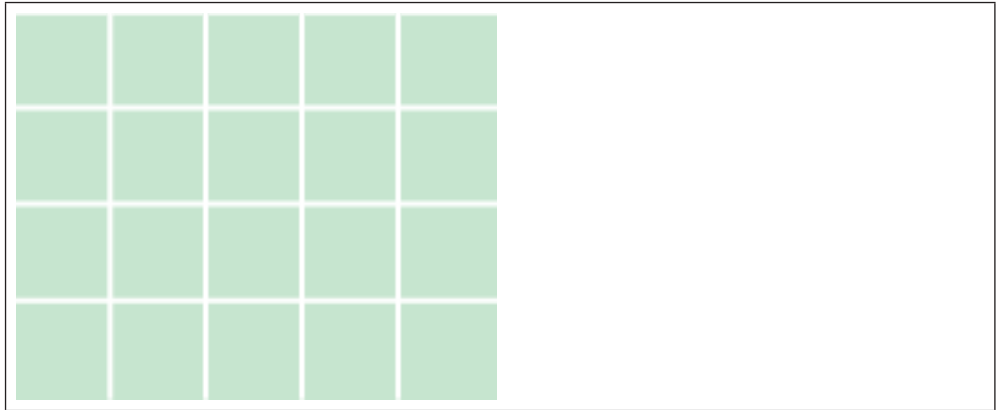
As the percentage of restricted revenues increases, a LG loses its ability to respond to changing conditions and to citizens’ needs and demands. Increases in restricted revenues may also indicate overdependence on external revenues and signal future inability to maintain service levels.

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Net operating revenues	Worksheet 2 (W2), line 13					

2	Restricted operating revenues	W2, line 14					
3	Restricted operating revenues as a percentage of net operating revenues	Line 2 / Line 1*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

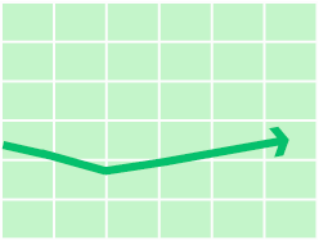
- Is the trend due to a decrease in unrestricted revenues? If so, see Indicator 1, Revenues per capita.
- If restricted revenues are supporting new programs or a higher level of service, will the revenues continue to be available, or will the LG have to assume the responsibility for the programs or services in the future?
- If restricted funds cease to be available, will the LG realistically be able to reduce or eliminate the affected programs?
- Are unrestricted sources subsidizing restricted revenue programs?
- Is the LG using a portion of the restricted revenues to support central accounting, personnel, and other overhead services?
- Can revenue restrictions be removed by LG choice, such as a charter revision or council policy? If not, can the LG join with other LGs to persuade the central government, province, or other authorities to remove the restrictions?

Suggestions for further analysis—To examine the use of restricted revenues, construct a worksheet in which you:

- List each of the restricted revenues and identify the service or expense area to which it contributes, including any overhead activities such as accounting or personnel.
- Assess how essential this service is to the LG and its citizens. Rate the service from 1 (very essential) to 5 (not very essential).
- List other revenue sources that could fund the service if the restricted revenue source were withdrawn.
- Rate the likelihood that the revenue source will continue: Is legislation proposed or pending? Are “public interest” or “industry” organizations offering vocal support for, or opposition to, the revenue? Rate the likelihood from 1 (very likely) to 5 (not very likely).

Suggestions for policy statements—There are no benchmarks for setting the amount of restricted revenues desirable in a budget; you will need to decide when the level of restricted revenues—and their areas of use—appears to be threatening your LG’s financial health in the short or longer term.

INDICATOR 3: INTERGOVERNMENTAL REVENUES

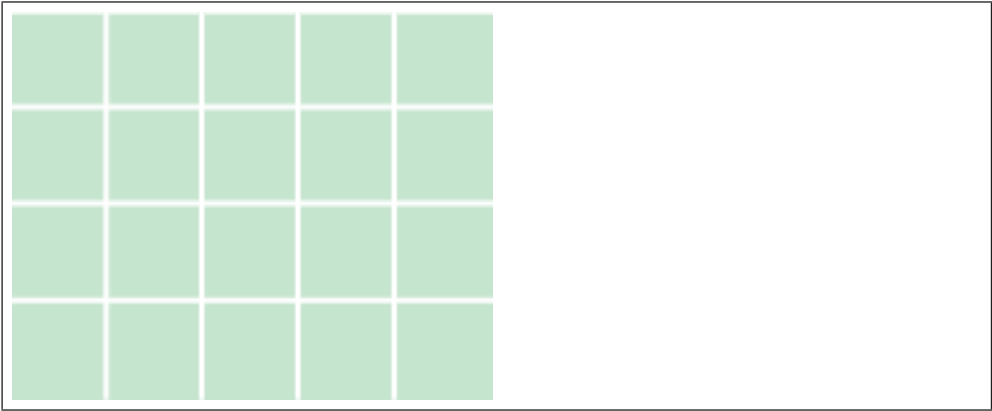
	
<p>Warning Trend— Increasing amount of intergovernmental operating revenues as a percentage of gross operating revenues</p>	
<p>Formula— $\frac{\text{Intergovernmental operating revenues}}{\text{Gross operating revenues}}$</p>	
<p>Intergovernmental revenues (revenues received from another level of government) are important because an overdependence on such revenues can be harmful. In most countries, the central government and provinces have struggled with their own budgetary problems in the last decade, and frequently they have withdrawn or reduced payments to LGs as one of their cutback measures. LGs with budgets largely supported by intergovernmental revenues have been particularly harmed during this period, but almost all LGs have shared the pain. The reduction of intergovernmental funds leaves the LG with the dilemma of cutting programs or funding them from other revenues. In many countries intergovernmental revenues may be 75%-90% of a LG's revenues. It is essential that these revenues be predictable and that the process for their allocation be transparent.</p> <p>Even in those countries where intergovernmental revenues are a much lower percentage of total revenues, a LG might want to maximize its use of intergovernmental revenues, consistent with its service priorities and financial condition. For example, a LG might want to rely on intergovernmental revenues to finance central government or province-mandated services. The primary concern in analyzing intergovernmental revenues is to know and monitor the LG's vulnerability to reductions of such revenues, and to determine whether the LG is controlling its use of the external revenue—or whether these revenues are controlling local policies.</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Net operating revenues	Worksheet 2 (W2), line 13					
2	Restricted operating revenues	W2, line 14					

3	Restricted operating revenues as a percentage of net operating revenues	Line 2 / Line 1*					
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*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

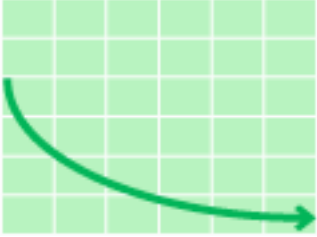
- Does your LG depend on intergovernmental revenues to fund ongoing, basic services? Do you have contingency plans in case the revenues are significantly reduced or discontinued?
- Have fixed-term grants for special programs been accepted? Will the LG be able to continue the special programs when such grants end? What will be the political, social, and economic consequences if such programs are discontinued?
- Are matching funds for intergovernmental revenues increasing as a percentage of operating expenditures? What is the LG's dollar commitment in matching funds, additional reporting requirements, or un-reimbursed overhead costs? Have all these costs been anticipated, budgeted, and recorded?
- Are intergovernmental revenues authorized by ongoing legislation or agreements, as in the sharing of a valued added tax (VAT) by the central government and LGs? Do the agreements suggest that the revenues will continue, and at what level?

Suggestions for further analysis—To demonstrate the role of intergovernmental revenues in your LG's financial health, you might want to create tables, bar graphs, or pie charts showing the major sources and uses of such revenues and any expected changes in the revenues you receive.

Suggestions for policy statements—While it would be difficult to set definitive policy guidelines on levels or kinds of intergovernmental revenues, it is feasible to set guidelines on procedures to be followed before grants and other revenues are accepted. The following policy statements can help local officials relate this indicator to their financial decision making.

- All potential grants shall be carefully examined for matching requirements (both dollar and level-of-effort matches). The funds necessary to match intergovernmental grants shall not exceed _____ percent of net operating revenues.
- Intergovernmental revenues used for operating purposes shall not exceed _____ percent of net operating revenues.
- Intergovernmental assistance shall be used to finance only those capital investments that are consistent with the capital investment plan and LG priorities, and whose operating and maintenance costs have been included in operating budget forecasts.

INDICATOR 4: ELASTIC TAX REVENUES

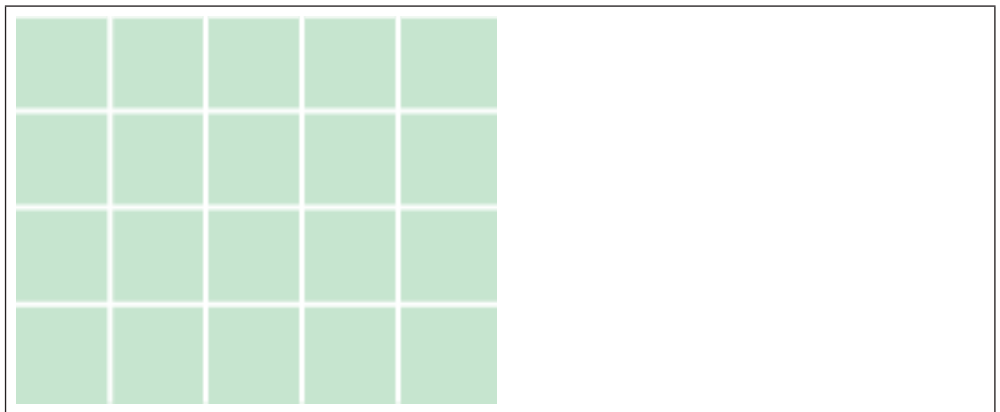
	
Warning Trend—Decreasing amount of elastic operating revenues as a percentage of net operating revenues	<p>The yields of elastic revenues (revenues that directly respond to changes in inflation and the economic base) are highly responsive to changes in the economic bases and inflation. As the economic base expands or inflation goes up, elastic revenues rise in roughly proportional or greater amounts, and vice versa. A good example is sales tax revenue, which increases during good economic periods with the increase in retail business and declines during poor times, even though the tax rate remains the same. Yields from inelastic revenue sources, such as license fees or user charges, are relatively unresponsive to changes in economic conditions and require that LG officials change fees or charges to obtain a change in revenue. The yields from these revenues usually lag behind economic growth and inflation because local governing bodies are reluctant to increase them each year. If properties are not reassessed frequently, property tax revenues can also be inelastic, especially in periods of economic growth.</p> <p>A balance between elastic and inelastic revenues mitigates the effects of economic growth or decline. During inflation, it is desirable to have a high percentage of elastic revenues because inflation pushes up revenue yield, keeping pace with the higher prices the LG must pay. If the percentage of elastic revenues declines during inflation, the LG becomes more vulnerable because inflation pushes up the price of services but not the yields of new revenues. The reverse is also true (i.e., a low percentage of elastic revenues is desirable in times of deflation), but significant deflation has seldom occurred in recent years.</p> <p>During a recession, a high percentage of inelastic revenues is an advantage. This insulates the tax base to some degree from the reduced yield it can receive during a recession.</p>
Formula— Elastic operating revenues / Net operating revenues	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005

1	Net operating revenues	Worksheet 2 (W2), line 13					
2	Revenues from taxes with an elastic tax base	W2, line 15					
3	Elastic operating revenues as a percentage of net operating revenue	Line 2 / Line 1*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the cause (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

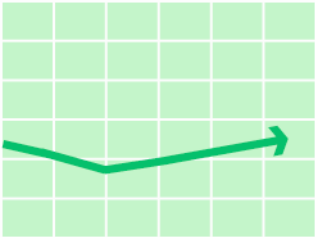
- Do revenues rely heavily on inelastic tax sources? Can more elastic taxes, such as income or sales tax, be instituted or increased?
- If the LG has a sales or value added tax, can it be extended to goods and services whose sales and prices respond more directly to changes in economic conditions?
- Has general economic decline or the out-migration of population or business created the decline in the elastic portion of the LG's revenue base? Could redevelopment programs help?
- Do local restrictions on taxes (e.g., on the source taxed or the amount collected) limit the elasticity of the revenue structure?
- Can inelastic taxes and fees be made more elastic by more frequent property assessments, routine increases in user fees, or similar local governing body and administrative modifications?

Suggestions for policy statements—It would be difficult to set an exact target for the proportion of elastic to inelastic revenues, but the following policy statements can help local officials relate this indicator to financial decision making.

A balance will be sought in the revenue structure between the proportions of elastic and inelastic revenues. New sources of revenue will be sought to achieve the desirable balance.

Each time a new revenue source or a change in the rate of an existing source is considered, the effect of this change on the balance of elastic and inelastic revenues will be thoroughly examined.

INDICATOR 5: ONE-TIME REVENUES

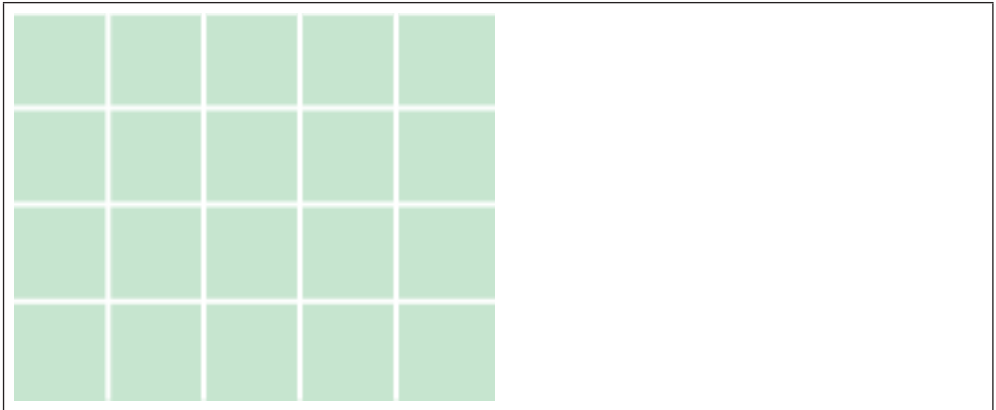
	<p>A one-time revenue is one that cannot reasonably be expected to continue, such as a single-purpose grant, sale of a major asset, or use of reserves. Continual use of one-time revenues to balance the annual budget can indicate that the revenue base is not strong enough to support current service levels. It can also mean that the LG is incurring operating deficits (see indicator 14, Operating Deficits) and would have little room to manoeuvre if there were a downturn in revenues (such as occurs during a regional or national recession or because of the sudden expenditures occasioned by a natural disaster). Use of one-time revenues increases the probability that the LG will have to make large cutbacks if such revenues cease to be available, as may happen when the central government reduces a major grant program or when reserves are depleted.</p> <p>Reserves, like loans, are technically not considered revenues. They are included here as examples of “one-time revenues” in the sense that they are a source of funds for balancing the budget.</p>
<p>Warning Trend— Increasing amount of one-time operating revenues as a percentage of net operating revenues</p>	
<p>Formula— One-time operating revenues / Net operating revenues</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Net operating revenues	Worksheet 2 (W2), line 13					
2	One-time operating revenues	W2, line 16					

3	One-time operating revenues as a percentage of net revenues	Line 2 / Line 1*					
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*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the cause (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Are one-time revenues being used to fund ongoing expenditures as opposed to one-time expenditures? What is the probability that these revenues will cease to be available? Is there a contingency funding plan?
- If one-time revenues are being used for one-time expenditures, such as a new building, are there other, ongoing revenues to pay the operating expenses of the building and the programs it will house?
- Is the use of reserves or balances from prior years significantly reducing the LG's ability to weather unexpected financial problems, such as natural disasters or a surge in inflation?
- Is the LG experiencing operating deficits (i.e., an excess of current expenditures over current revenues)? See Indicator 14, Operating deficits.

Suggestions for further analysis—If the trend analysis shows a high or increasing level of reliance on one-time revenues, you may want to pinpoint what the one-time revenues are, how they are being used, and what the prognosis is for their continued availability. A chart can help with the answers. To complete this chart,

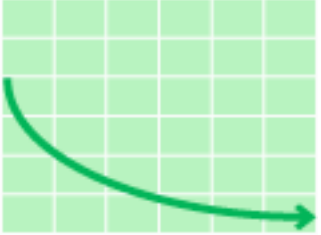
- List the sources of one-time revenues and identify the service or expense area to which they contribute.
- Determine whether the service is a one-time expense (such as a special clean-up program) or an ongoing program.
- Note how essential this service is to the LG and its citizens. Rate the service from 1 (very essential) to 5 (not very essential).

- List the revenues or decreases in expenditures that could replace the one-time revenue if necessary.

Suggestions for policy statements—While it would be difficult to set target levels for one-time revenues in your revenue structure, policy statements can be developed for procedures in the use of one-time revenues. The following policy statements can help local officials relate this indicator to their financial decision making.

- One-time revenues will be used only after an examination determines whether they are subsidizing an imbalance between operating revenues and expenditures, and then only if a long-term (three- to five-year) forecast shows that the operating deficit will not continue.
- One-time revenues will be used only for one-time expenditures.

INDICATOR 6: PROPERTY TAX REVENUES

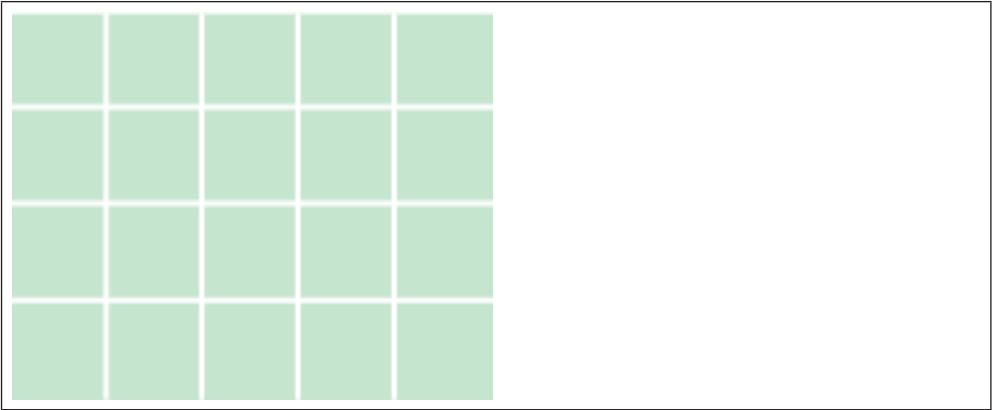
	<p>Property tax revenues should be considered separately from other revenues because LGs in many countries rely heavily on them. A decline or a diminished growth rate in property taxes can have a number of causes. First, it may reflect an overall decline in property values resulting from the aging of buildings, a decline in local economic health, or a decline in total number of households, which can depress the housing market. Second, it may result from unwilling default on property taxes by property owners. Third, it may result from inefficient assessment or appraisal. Finally, a decline can be caused by deliberate default by property owners, who realize that delinquency penalties are less than short-run interest rates and that non-payment is therefore an economical way to borrow money.</p>
<p>Warning Trend— Decline in property tax revenues (constant dollars)</p>	
<p>Formula— Property tax revenues / (constant dollars)</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Property tax revenues	Worksheet 2 (W2), line 1					
2	Consumer price index (CPI) for the LG's area	Central govt or university					
3	CPI in decimal	Line 2 / Line 100					

4	Property tax in revenues in CPI base year dollars	Line 1 / Line 3*					
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*Plot the appropriate years and these figures on the following graph. Rate of change can also be computed and graphed (current year minus prior year; remainder divided by prior year).



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Have market values declined due to poor economic conditions? In which sectors—residential, commercial, or industrial—has the decline occurred? Can an economic development strategy be designed that will increase taxable property values?
- Has the assessed value of properties or classes of properties dropped as a percentage of market value? If so, is the drop caused by an inefficient assessment system or by the fact that reassessments are not sufficiently frequent? Can assessed value be increased without putting an unreasonable burden on property owners?
- Is the percentage of non-taxable property increasing? Is this due to an increase in LG ownership or other tax-exempt status or to an increase in tax incentives designed to attract or retain businesses? In the first case, can payments in lieu of taxes be instituted? In the second case, what are the projected long-term revenue impacts of the incentive policies?
- Are property tax delinquencies increasing? See Indicator 7, Uncollected property taxes.

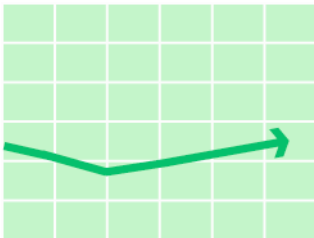
Suggestions for further analysis—Whether property tax revenues are increasing or decreasing, you may want to construct a table that shows property taxes by type (real vs. personal) and by class (residential, commercial, industrial) for the period you have chosen. The table should enable you to identify sectors in which change has occurred. To demonstrate the impact of any changes, you could also compute the rate

of change in property tax revenues (current year minus prior year; remainder divided by prior year) and graph these figures.

Suggestions for policy statements—Policy statements could be developed to suggest both levels of increase in property tax revenues and procedures for raising revenues through the property tax. The following policy statements can help local officials relate this indicator to their financial decision making.

- Sound appraisal procedures will be maintained to keep property values current. Property will be assessed at _____ percent of full and fair market value.
- The year-to-year increase of actual revenue from the property tax will not exceed _____ percent.
- All property will be reassessed at least every _____ years.

INDICATOR 7: UNCOLLECTED PROPERTY TAXES

		Every year, a percentage of property owners is unable to pay property taxes. If this percentage increases over time, it may indicate overall decline in the LG's economic health. Additionally, as uncollected property taxes rise, liquidity is decreased, and there is less cash on hand to pay bills or to invest.
Warning Trend— Increasing amount of uncollected property taxes as a percentage of net property tax levy		Credit industry benchmarks—If property taxes are a substantial portion of your LG's operating revenues, then credit rating firms will look at the cash flow. For LGs where they are a substantial portion of total operating revenues, Credit-rating firms assume that a LG normally will be unable to collect some percentage (in the U.S. it is from 2 to 3 percent) of its property taxes within the year that the taxes are due. In the U.S. if uncollected property taxes rise to more than 5 to 8 percent, rating firms consider this a negative factor because it signals potential instability in the property tax base. An increase in the rate of delinquency for two consecutive years is also considered a negative factor. Different countries will have different benchmark collection rates.
Formula— $\frac{\text{Uncollected property taxes}}{\text{Net property tax levy}}$		

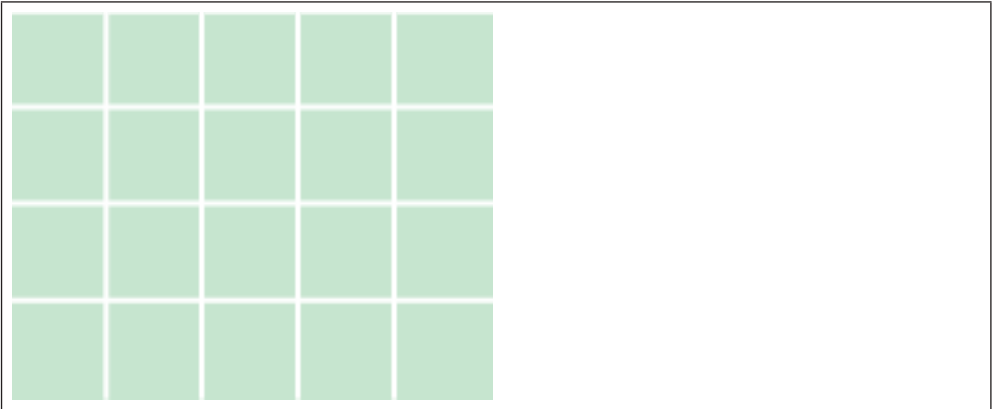
Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005

1	Total (Gross) property tax levy	LG**					
2	Exoneration of property taxes levied	LG					
3	Abatements of property taxes levied	LG					
4	Other reductions to gross property taxes levied	LG					
5	Net property tax levy	Line 1 minus Line 2, 3 & 4					
6	Uncollected property taxes	LG					
3	Uncollected property taxes as a percentage of net property tax levy	Line 6 / Line 5*					

*Plot the appropriate years and these figures on the following graph.

** Tax collector's records may have the gross and net property tax levy as the same. Some LGs technically levy property taxes on non-taxable property and subsequently exonerate that levy. Also the LG may have a procedure for resolving contested property tax levies (abatements) and a procedure to reduce the bills of low-income or fixed-income taxpayers, elderly taxpayers or other special classes.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for the analysis.

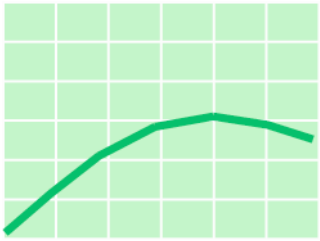
- Is general economic decline affecting taxpayers' ability to make their tax payments? Is a growing proportion of low- or fixed-income property owners having difficulty paying property tax bills? Would optional instalment payments lessen the impact of one or two large payments?
- Is the proportion of distressed properties within the LG increasing? Can rehabilitation programs be initiated? Can new uses be found for property whose original use is no longer economically viable?
- Are collection procedures adequate, especially in regard to delinquent taxes?
- Is the percentage of uncollected taxes higher than is assumed in revenue estimates?
- Can delinquency penalties be tied to the prime interest rate or to other short-term interest rates to discourage non-payment as a means of borrowing? Can delinquencies be made public to discourage this practice?
- Does the LG have the authority to place a lien foreclosure on property for non-payment of property taxes?
- Is the time lag between the due date for property tax payments and the date of lien foreclosure short enough to encourage timely payment?

Suggestions for further analysis—If uncollected property taxes are rising, further investigation is needed to determine which classes of property taxpayers are not paying; whether non-payments are rising in commercial, industrial, or residential properties; whether certain neighbourhoods are experiencing more trouble than others; and whether one demographic group, for example, the elderly, is having more trouble than others. If, for example, the investigation shows that uncollected property taxes are high among low-income elderly, it might make sense to examine the possibility of instituting tax-relief programs that allow property taxes to be deferred until they can be paid from estate proceeds.

Suggestions for policy statements—Policy statements could suggest both an acceptable level of uncollected property taxes and procedures for collecting property taxes. The following policy statements can help local officials relate this indicator to their financial decision making.

- The annual level of uncollected property taxes will not exceed _____ percent.
- An aggressive policy of collecting property tax revenues will be followed.

INDICATOR 8: USER CHARGE COVERAGE

	<p>The term user charge coverage refers to whether fees and charges cover the entire cost of providing a service. This indicator focuses only on programs (such as recreation or inspection services) and not on business enterprise services, like water utilities, which are examined in Indicator 15, Enterprise Losses. If the user charges cover all the costs, the coverage is 100 percent. If charges cover only half the costs, the coverage is 50 percent. As coverage declines, the burden on other revenues to support the services increases. Because the typical LG accounting system does not employ cost-accounting techniques, it is easy for inflation and other factors to erode user charge coverage without being noticed.</p>
<p>WarningTrend— Decreasing revenues from user charges as a percentage of total expenditures for related services</p>	
<p>Formula— Revenues from user charges / Expenditures for related services</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Revenues from fees and user charges	Worksheet 2 (W2), line 2					
2	Expenditures for services for which there is a fee or user charge	W3, line 15					
3	User charge coverage	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Note: A separate analysis should be done for each service with a charge or fee which represents a significant portion of the operating budget.

Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

Are revenues from fees and user charges lower than the cost of providing the service? If so, is this for any of the following reasons:

- Were the full (direct and indirect) costs not calculated when rates were set?
- Is the charge not reviewed frequently enough to take inflation and other economic pressures into account?
- Is there a conscious decision not to cover 100 percent of the service costs? Are there social reasons not to increase the charge? Do national or other laws inhibit charge adjustment?

Is user charge coverage declining because the demand for service is decreasing? Is decreased demand due to any of the following causes:

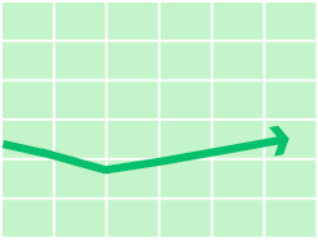
- A decrease in the need for services?
- A decrease in the quality of services provided?
- An increase in user fees or charges?
- Inadequate marketing?
- Are cost control and revenue collection procedures effective?

Suggestions for further analysis—If overall user charge coverage of costs is decreasing, a detailed analysis of each charge should be made to pinpoint the causes. In LGs where tax limitations are in effect, switching to (or increasing) user charge funding could help generate additional revenues. It would therefore be useful in association with this indicator to examine new areas in which user charges could be initiated. Analysis could also be undertaken to see if non-residents who are using LG services can be charged for their use of those services. The impact of user charges on low-income residents is another area for possible study.

Suggestions for policy statements—Policy statements could be developed to suggest both a desirable level of user charge coverage and procedures for analyzing coverage in the future. The following policy statements can help local officials relate this indicator to their financial decision making.

- For each service associated with a user fee or charge, a set percentage of direct and indirect costs (e.g., 50 percent, 75 percent, 100 percent) will be covered by fees and charges. Fees and charges will be set to ensure that the specific level of coverage is met.
- The full costs of user-fee-supported activities will be recalculated each year to determine the impact of inflation and other cost increases.
- User charges will be revised automatically each year, with (or without) the review of the governing board, to adjust for cost increases or decreases.

INDICATOR 9: REVENUE SHORTFALLS

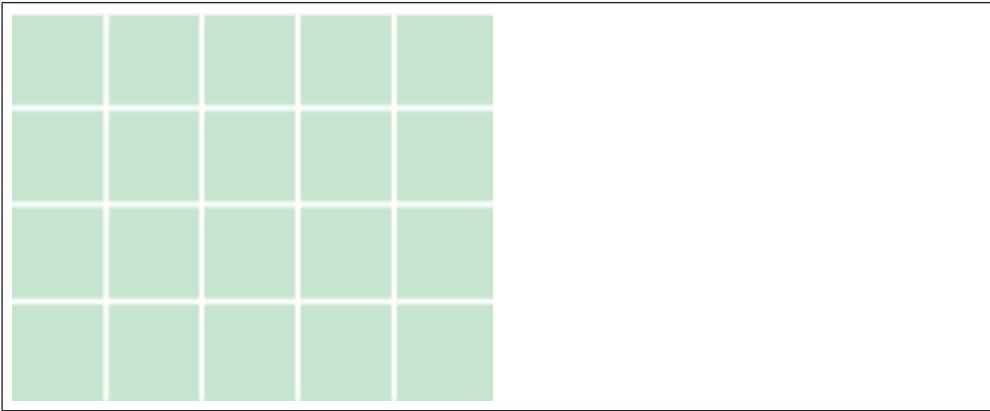
	<p>This indicator examines the differences between revenue estimates and revenues actually received during the fiscal year. Major discrepancies that continue year after year can indicate a declining economy, inefficient collection procedures, or inaccurate estimating techniques. Discrepancies may also indicate that high revenue estimates are being made to accommodate political pressures. If revenue shortfalls are increasing in frequency or size, a detailed analysis of each revenue should be made to pinpoint the source.</p>
<p>Warning Trend— Increase in revenue shortfalls as a percentage of actual net operating revenues</p>	
<p>Formula— Revenue shortfalls / Net operating revenues</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Actual net operating revenues (May or may not include property taxes)	Worksheet 2 (W2), line 13					
2	Net operating revenues budgeted (initial budget)	W2, line 17					
3	Revenue shortfalls	Line 2 minus Line 1					

4	Revenue shortfalls as percentage of actual net operating revenues	Line 3 / Line 1*					
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*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is this trend caused by a deteriorating revenue base?
- Is it due to adverse regional or national trends or to a local problem? Can the problem be identified? See Indicator 1, Revenues per Capita.
- Is the trend due to province or central government initiatives?
- Are revenue estimates made optimistically high in order to balance the budget?
- Is the trend due to ineffective estimating procedures? Would the following procedures improve estimates?
 - Centralizing the organizational responsibility for preparing the estimates,
 - Developing historical data on each revenue source, or
 - Using regional and state agencies to improve the economic assumptions used to make estimates.

Suggestions for further analysis—If revenue shortfalls are increasing in frequency or size, a detailed analysis of each revenue should be made to pinpoint the cause.

Suggestions for policy statements—Policy statements can be developed to suggest procedures for forecasting revenues and adjusting for shortfalls. The following policy statements can help local officials relate this indicator to their financial decision making.

- All revenue forecasts shall be conservative.
- Regular reports comparing actual to budgeted revenues will be prepared by the _____ (e.g., finance director, treasurer) and presented to the _____ (e.g., manager, governing body).

LEARNING APPLICATION

Policy Maker ☒ CEO ☒ Finance Manager ☒ Department Head ☒

After reviewing the revenue indicators, which are most useful from your role perspective in the LG, and why?

EXPENDITURES

Expenditures are a rough measure of a LG's service output. Generally, the more a LG spends in constant dollars, the more services it is providing. (This formula does not take into account how effective the services are or how efficiently they are delivered.) To determine whether a LG is living within its revenues, the first issue to consider is expenditure growth rate.

Because most LGs are required to have a balanced budget, it would seem unlikely that expenditure growth would exceed revenue growth. Nevertheless, the annual budget can be balanced in a number of subtle ways that will create a long-run imbalance in which expenditure outlays and commitments grow faster than revenues. Some of the more common ways are to borrow, use reserves, use bond proceeds for operations, or siphon small amounts from intergovernmental grants. Other ways are to defer maintenance on capital assets or to defer funding of a future liability such as a pension plan. In each of these cases, the annual budget remains balanced, but the long-run budget develops a deficit. Although long-run deficits can be funded through

windfalls such as grants or revenue surges created by inflation, allowing such deficits to develop is risky.

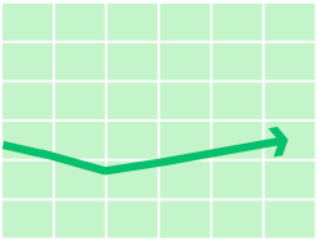
A second issue to consider is expenditure flexibility. Expenditure flexibility is a measure of a LG’s freedom to adjust its service levels to changing conditions, and considers the level of mandatory or fixed costs. Ideally, a LG’s expenditure growth rate will not exceed its revenue growth rate, and the LG will have maximum flexibility to adjust spending. An increase in mandatory costs such as debt service, matching requirements, and pension benefits renders a LG less able to adjust to change.

Analyzing your LG’s expenditure profile will help you to identify the following types of problems:

- Excessive growth of overall expenditures as compared to revenue growth or growth in community wealth (personal and business income),
- An undesirable increase in fixed costs,
- Ineffective budgetary controls,
- A decline in personnel productivity, or
- Excessive growth in programs that create future expenditure liabilities.

The indicators shown in the next section can be used to monitor changes in expenditures. The expenditure indicators are discussed in detail in the following pages.

INDICATOR 10: EXPENDITURES PER CAPITA

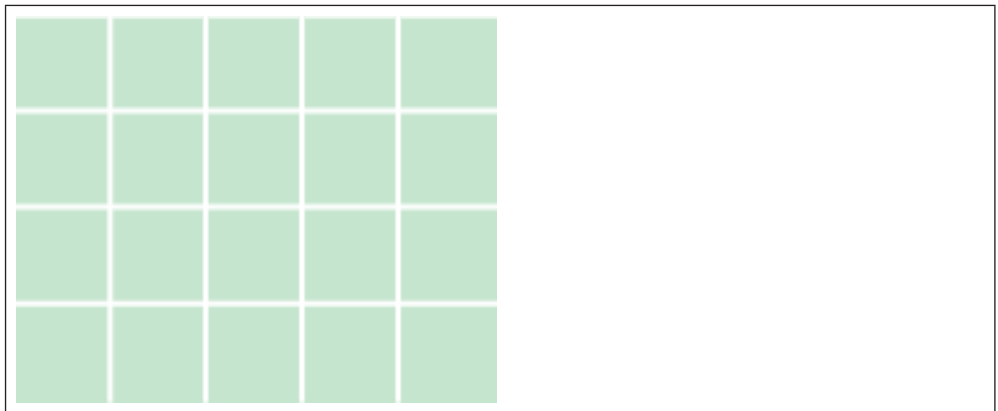
	<p>Changes in per capita expenditures reflect changes in expenditures relative to changes in population. Increasing per capita expenditures can indicate that the cost of providing services is outstripping the community’s ability to pay, especially if spending is increasing faster than the residents’ collective personal income. From a different perspective, if the increase in spending is greater than can be accounted for by inflation or the addition of new services, it may indicate declining productivity—that is, that the LG is spending more real dollars to support the same level of services.</p>
<p>Warning Trend— Increasing net operating expenditures per capita (constant dollars)</p>	
<p>Formula— $\text{Net operating expenditures (constant dollars)} / \text{Population}$</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005

1	Total net operating expenditures	Worksheet 3 (W3), line 11					
2	Consumer price index (CPI) for the LG's area	Central govt, university					
3	CPI in decimal	Line 2 / 100					
4	Net operating expenditures in CPI base-year dollars	Line 1 / Line 3					
5	Current population	W7, Line 1					
6	Net operating constant dollar expenditures per capita	Line 4 / Line 5*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is the increase caused by increased levels of existing services or by the addition of new services? Are there increased revenues to pay for these increased services? Can user charges be instituted or increased to pay for these services? If not, should services be reduced?
- If the increase cannot be explained by the addition of new services, is personnel productivity or service efficiency declining? Can changes in management practices or technology deal with this?

- Is the increase linked to an increase in fixed costs, or is it due to increases in programs that can be cut back at the discretion of the LG? See Indicator 12, Fixed Costs.
- Is the increase due to an increase in externally funded programs that are now fully funded and will be for their duration, or is it due to externally funded programs for which only seed money has been supplied, and for which the LG will have to assume future funding responsibility? In the second case, how will these programs be funded in the future?
- Is the increase due to an increase in mandated services? Can the level of LG that mandates the services provide funding?
- Is the increase due to construction of capital facilities that were funded by debt, meaning that the expenditure burden will be spread out over many years? Will the debt service plus operating costs of the new facilities strain future budgets? See the debt Indicators, 18-21.
- Are per capita expenditures rising faster than per capita revenues? Is this straining the LG's ability to pay? Are fund balances and reserves being used to balance the budget? See Indicator 14, Operating Deficits.
- Are per capita expenditures rising faster than personal income or business activity? Is this straining citizens' and businesses' ability to pay taxes?
- Can expenditures be reduced by any of the following means?
- - Consolidating support services to achieve economies of scale
 - Cross-training personnel to avoid duplicating functions and reduce idle time.
 - Contracting services or replacing full-time technical staff with consultants or service bureaus. (Note: services should be contracted out only after a thorough analysis has determined contracting out to be the less costly option. In some cases, the LG can still provide services at a lower cost than any private contractor could.)
 - Using more advanced management controls, information systems, or technologies.
 - Transferring functions to other levels of government.
 - Eliminating programs that are no longer important.
 - Pooling funds with other LGs for self-insuring, investing idle funds, etc.
 - Entering into mutual aid, service, or cooperative purchasing agreements with other LGs.

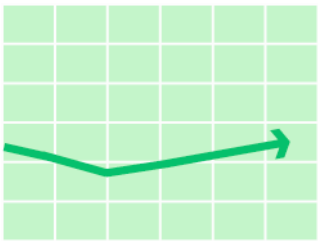
Suggestions for further analysis—Like the analysis of per capita revenues, analysis of per capita expenditures should focus first on total expenditures and then on changes in individual expenditure categories. Expenditures can be evaluated based on fund, function (public safety which includes police, fire and health departments), or organizational unit (human resources, public works, governing body). For this analysis, you should construct a worksheet. First, list the category of expenditure. Then, for each year you want to consider, write in the amount for each category and

calculate the percentage of the total year's spending that it represents. (Note: since you are simply calculating percentages of a total, you do not need to use constant dollars. However, when you look at trends for any of these categories in dollars rather than percentages, be sure to compute constant dollars.)

Suggestions for policy statements—Policy statements can be developed to suggest procedures for monitoring expenditures. The following policy statements can help local officials relate this indicator to their financial decision making.

- Reports comparing actual revenues and expenditures to budgeted amounts will be prepared regularly.
- Where possible, performance measures and productivity indicators will be integrated into the budget.

INDICATOR 11: EMPLOYEES PER CAPITA

	Because personnel costs are a major portion of any LG's operating budget, plotting changes in the number of employees per capita is a good way to measure changes in expenditures. An increase in employees per capita might indicate that expenditures are rising faster than revenues, that the LG is becoming more labour intensive, or that personnel productivity is declining.
Warning Trend— Increasing number of LG employees per capita	
Formula— Number of LG employees / Population	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Number of LG employees	Worksheet 3 (W3), line 12					
2	Current population	W7, line 1					
3	Number of LG employees per capita	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.

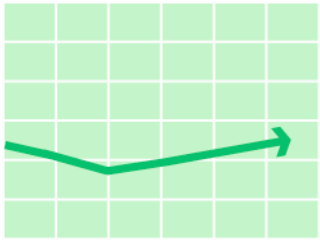


Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is employee productivity decreasing? Can measures be developed to evaluate and improve productivity?
- Has loss of grant funding required the LG to pay for workers previously hired under the grants? If not, might this happen in the future
- Have the community's population characteristics changed, necessitating higher service levels?

Suggestions for further analysis—The overall trend in LG employment may mask important underlying trends. For example, while overall LG employment may appear steady or even to have decreased slightly, it may actually be on the rise. Let us say, for example, that employment in public safety is increasing while employment in public works is decreasing. The net effect appears to be stability. But if the jobs in public works have been contracted out, the LG is indirectly employing additional people. Additional analysis can identify such patterns by (1) examining changes in employment patterns by department or service area, and (2) examining decreases in employment to see whether contracting out has substituted private-sector workers for LG employees.

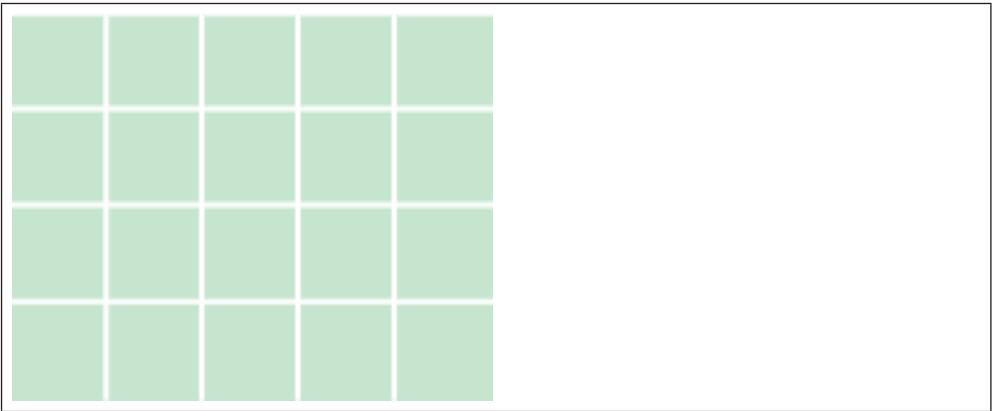
INDICATOR 12: FIXED COSTS

	<p>The operating expenditures of every LG are composed in part of mandatory and fixed expenditures over which officials have little short-run control. These include expenditures to which the LG is legally committed (such as debt service and pension benefits), as well as expenditures imposed by higher levels of government (for example, education). The higher the level of fixed expenditures, the less freedom local officials have to adjust spending in response to economic change. Fixed costs become especially important during periods of financial retrenchment, since mandatory expenditures such as debt service are usually unaffected by a reduction in service levels.</p>
<p>Warning Trend— Increasing fixed costs as a percentage of net operating expenditures</p>	
<p>Formula— Fixed costs / Net operating expenditures</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Total fixed costs	Worksheet 4 (W4), line 8					
2	Total net operating expenditures	W3, line 11					
3	Fixed costs as percentage of net operating expenditures	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

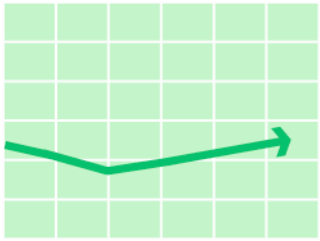
- If increases are due to services mandated by other governmental units, can funding be obtained from the units mandating the services? Can the quantity or quality of these services be reduced?
- For externally mandated services for which funding is provided, are all reimbursable charges (including overhead) consistently billed at actual cost?
- Is external funding for mandated services decreasing, or not keeping pace with inflation and other cost increases?
- Are increases in fixed costs created by increases in debt service? Will old bonds be paid off soon, thereby reducing fixed costs? Can debt service schedules be modified through long-term refunding? See Indicator 20, Debt Service.
- Are increases in fixed expenditures due to previous decisions, such as debt commitments, over which the LG no longer has control, or are they due to yearly decisions over which it has future control?
- If increases are due to past decisions, are all the cost implications of these decisions clear for the current and future years? Is there a plan for funding these costs? Are new decisions that will commit the LG to future spending similarly analyzed?

Suggestions for further analysis—Either an increase or a decrease in fixed costs can be a signal for further investigation. For example, if a LG postpones issuing new debt for much-needed capital projects, fixed costs for debt service will decrease as old debt is paid off, and this may appear to be a favourable sign. But if money that should be used to meet new debt service is being used for operating expenses, it may be difficult to issue the new debt as planned. Any decreases in fixed costs should therefore be carefully examined to ensure that important goals are not being deferred.

Suggestions for policy statements—Policy statements can be developed to suggest procedures for analyzing future fixed costs. The following policy statements can help local officials relate this indicator to their financial decision making.

- Before the LG undertakes any agreements that create fixed costs, the cost implications (both operating and capital) of such agreements will be fully determined for this and future years.
- All externally mandated services for which funding is available will be fully costed out (including overhead) to allow for complete reimbursement of expenses.

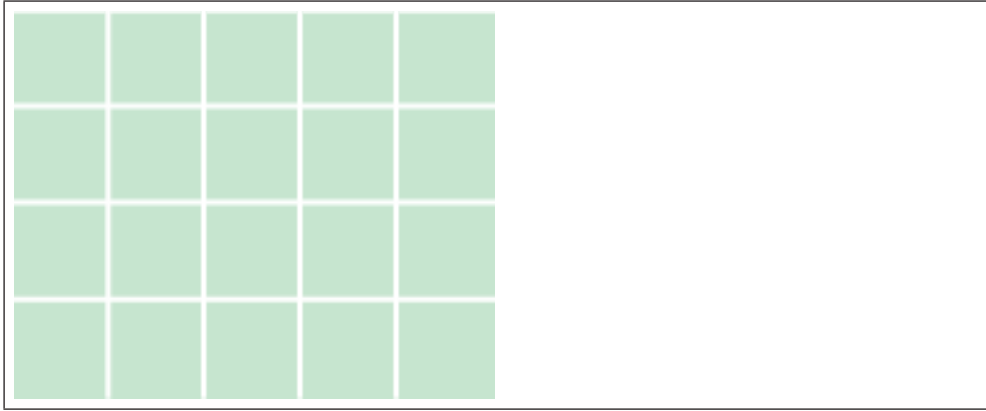
INDICATOR 13: FRINGE BENEFITS

	<p>The most common forms of employee benefits are pension plans, health and life insurance, vacation, sick and holiday leave, deferred compensation, automobile allowances, disability insurance, and educational and incentive pay. Benefits represent a significant share of operating costs, often amounting to more than 30 percent of employee compensation. Some benefits, such as health and life insurance, require immediate cash outlays; some, such as pension benefits or accumulated vacation pay, can be deferred for ten to twenty years; others, such as accumulated holiday and sick leave, may require either payment for the opportunity cost of not having the work done or payment to additional employees to handle the work. Because the funding and recording of employee benefits is a complex process, these costs can escalate unnoticed, straining the LG's finances.</p>
<p>Warning Trend— Increasing fringe benefit expenditures as a percentage of salaries and wages</p>	
<p>Formula— Fringe benefit expenditures / Salaries and wages</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Cost of fringe benefits	Worksheet 3 (W3), line 2					
2	Salaries and wages	W2, line 1					
3	Fringe benefit expenditures as a percentage of salaries and wages	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph. This indicator can also be computed as Expenditures for Fringe Benefits plus Paid Absences divided by Salary and Wages.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- What is the origin of the increase? Have new employee benefits been provided? Has the quality or quantity of existing employee benefits been increased? Do the LG's records make this information explicit?
- Has the cost of current benefits increased? Can the LG reduce or control such costs?
- Has the LG begun programs to reduce the cost of health insurance benefits, such as self-funding insurance, direct contracting for services, implementing wellness efforts, or switching to managed care health plans for employees?
- Are non-salary benefits, such as vacation pay, holiday pay, and educational incentives, being costed on a dollar basis and included in the budget?
- If the LG is assuming a greater share of fringe-benefit contributions, can these costs be isolated and negotiated separately with employee groups?
- Are accumulated pension and leave benefits funded on a current basis (i.e., fully funded)? If not, is there a plan for funding them when they are due to be paid? See Indicator 22, Unfunded Pension Liability, and Indicator 24, Accumulated Employee Leave.

Suggestions for policy statements—Policy statements can be developed to suggest procedures for analyzing future costs of employee benefits. The following policy statements can help local officials relate this indicator to their financial decision making.

- All non salary benefits, such as vacation pay, holiday pay, and educational incentives, will be costed out, and their impact on future budgets will be assessed.
- All compensation negotiations will focus on total compensation: direct salary plus employer share of employee benefits.

- Cost analysis of salary increases will include the effect of such increases on employer share of related employee benefit

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After reviewing the expenditure indicators, which are most useful from your role perspective in the LG, and why?

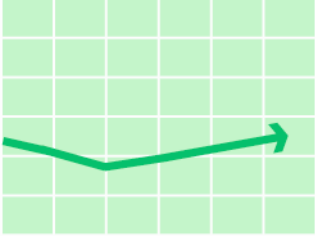
OPERATING POSITION

During a typical year, a LG generates either an operating surplus or an operating deficit. An operating surplus develops when current revenues exceed current expenditures, an operating deficit when the reverse occurs. In rare instances, revenues and expenditures balance exactly. An analysis of operating position can help to identify the following situations:

- A pattern of continuing operating deficits,
- A decline in reserves,
- A decline in liquidity,
- Ineffective revenue forecasting techniques, or
- Ineffective budgetary controls.

The indicators in this section can be used to monitor changes in operating position. An operating surplus or deficit may be created intentionally, by a policy decision, or unintentionally, because of the difficulty of precisely predicting revenues and expenditures or trends in the underlying local and national economies. Deficits are usually funded from unreserved fund balances; surpluses are usually used to increase fund balances.

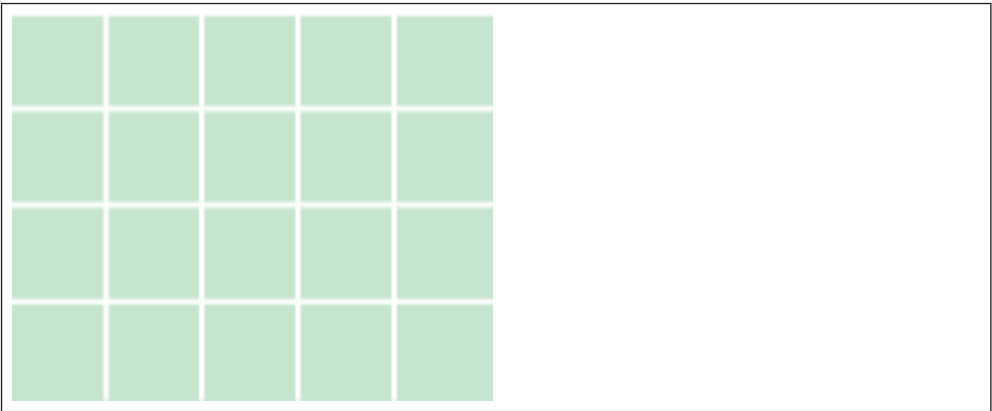
INDICATOR 14: OPERATING DEFICITS

	
<p>Warning Trend—Increasing general operating deficits as a percentage of net operating revenues</p>	
<p>Formula—General fund operating deficits / Net operating revenues</p>	
<p>An operating deficit occurs when current expenditures exceed current revenues. This may not mean that the budget will be out of balance (“budget deficit”), because reserves (“fund balances”) from prior years can be used to cover the difference. It does mean, however, that during the current year, the LG is spending more than it is receiving. This may be caused by an emergency (such as a natural catastrophe) requiring a large immediate expenditure. Or the spending pattern may be part of a policy to use accumulated surplus fund balances. An operating deficit in any one year may not be cause for concern, but frequent and increasing deficits can indicate that current revenues are not supporting current expenditures and that serious problems may lie ahead.</p> <p>Budgetary analysis does not always reveal operating deficits because they can be temporarily financed by short-term loans or by accounting transactions that, for example, inappropriately accrue future revenues or transfer surplus fund balances from other funds. An analyst looking for operating deficits should consider each fund separately, so that a surplus in one fund cannot hide a deficit in another. Analyzing funds separately also helps to pinpoint emerging problems.</p> <p>Credit industry benchmarks—A credit-rating firm would regard a current-year operating deficit as a minor warning signal; funding practices and the reasons for the deficit would be carefully assessed before it would be considered a negative factor. The following situations, however, would be given considerably more attention and would probably be considered negative factors.</p> <ul style="list-style-type: none">• Two consecutive years of operating fund deficits.• A current operating fund deficit greater than that of the previous year.• An operating fund deficit in two or more of the last five years.• An abnormally large deficit—more than 5 to 10 percent in one year.	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	General fund operating deficit	Worksheet 1 (W1), line 14					
2	Net operating revenues	W2, line 13					
3	General fund operating deficit as percentage of net operating revenues	Line 1 / Line 3*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.


- Was the deficit anticipated during budget preparation? Is it expected to continue in future years? Will surpluses or other sources of funding be available?
- Is the deficit being funded by borrowing from surpluses in other funds? Can these other funds afford the loan without creating problems later?
- Was the deficit due to revenue shortfalls? See Indicator 9, Revenue Shortfalls.

- Was the deficit caused by expenditure overruns? Were these due to inaccurate expenditure estimates at budget time or to ineffective expenditure controls during the fiscal year?
- Was the deficit caused by an emergency? Are sufficient reserves left for future emergencies? See Indicator 16, Fund Balances.

Suggestions for policy statements—Policy statements could be developed to define budgetary procedures that would help prevent operating deficits. The following policy statements can help local officials relate this indicator to their financial decision making.

- All current operating expenditures will be paid for with current operating revenues.
- Budgetary procedures that fund current expenditures at the expense of future needs, such as postponing expenditures, accruing future revenues, or rolling over short-term debt, will be avoided.

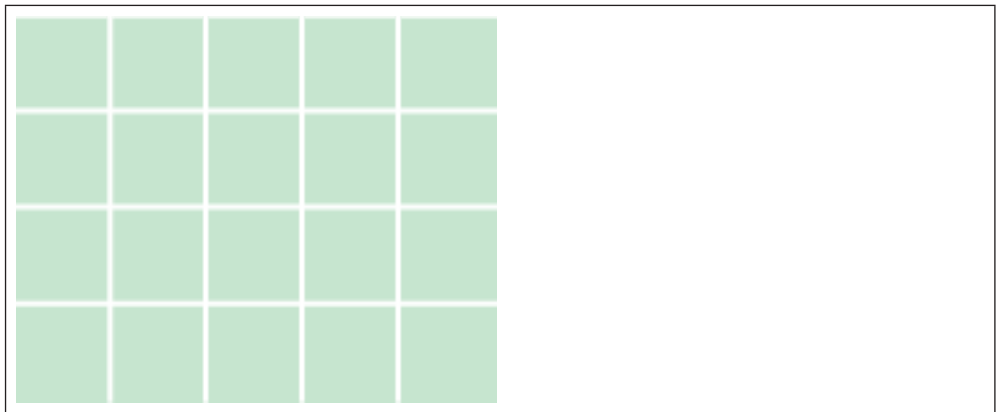
INDICATOR 15: ENTERPRISE LOSSES

	<p>Enterprise losses are a special and highly visible type of operating deficit because enterprise programs are expected to function as if they were commercially operated private entities, rather than governmental “not for profit” entities. This means that the costs (expenses, including depreciation) of providing goods and services to the public are to be recovered through user charges. In addition, enterprise operations may need to issue revenue bonds to finance capital investment projects, and the interest rates and covenants associated with the issuance of such bonds can be significantly affected by the operating position of the enterprise.</p>
<p>Warning Trend— Recurring enterprise losses (deficits) (constant dollars)</p>	
<p>Formula— Enterprise profits or losses in constant dollars</p>	<p>Enterprise fund programs common to LG are those for water, gas, and electric utilities; swimming pools; airports; parking garages; and transit systems. In times of financial strain, a LG can raise taxes to increase support for an operating fund program. Enterprises, however, are typically subject to the laws of supply and demand, and managers of such programs who raise user fees or rates may find that revenues actually decrease because customers limit their use of the service.</p>

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Enterprise operating results (net profit or loss)	Worksheet 1 (W1), line 15					
2	Consumer price index (CPI) for LG's area	Central govt, university					
3	CPI in decimal	Line 2 / 100					
4	Enterprise operating results in base-year dollars	Line 1 / line 3*					

*Plot the appropriate years and these figures on the following graph. An analysis should be done for each enterprise.



Suggestions for analysis—If the warning trend is observed, try to identify the cause (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

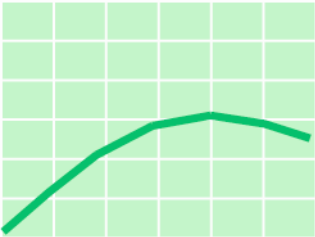
- Are operating efficiency and productivity decreasing?
- Are revenue rates high enough to cover costs? Are they periodically reviewed? Is analysis performed for each class of customer to determine costs?
- Are cost controls adequate?
- Is the demand for enterprise services decreasing for any of the following reasons?
 - o Decreased need for services,
 - o Decreased quality of services,
 - o Increased prices,
 - o Inadequate marketing, or
 - o Competition from other providers.

- Are retained earnings dropping lower than the LG considers desirable?
- Are retained earnings being used to subsidize operating losses? See Indicator 14, Operating Deficits.
- Are reserves being used for purposes other than those originally intended?

Suggestions for policy statements—A policy statement could be developed to suggest a level of fees and charges that would prevent enterprise programs from operating at a deficit. The following policy statement can help local officials relate this indicator to their financial decision making.

- All fees and charges for each enterprise fund will be set at a level that fully supports the direct and indirect cost of the activity. Indirect costs include annual depreciation. (See Indicator 27, Depreciation Expense.)

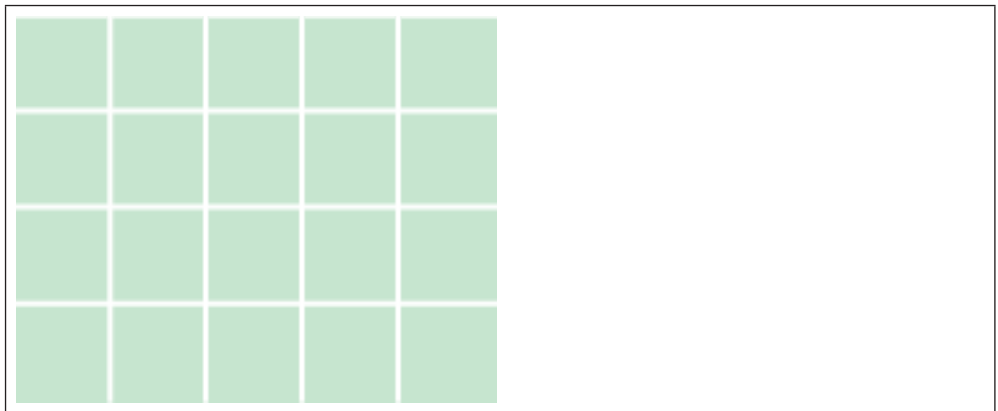
INDICATOR 16: FUND BALANCES

	<p>Positive fund balances can also be thought of as reserves, although the “fund balance” entry on a LG’s annual report is not always synonymous with “available for appropriation.”</p>
<p>Warning Trend— Declining unreserved fund balances as a percentage of net operating revenues</p>	<p>The size of a LG’s operating fund balance can affect its ability to withstand financial emergencies. It can also affect its ability to accumulate funds for capital investments without having to borrow. In countries that allow it, LGs usually try to operate each year at a small surplus to maintain positive fund balances and thus maintain adequate reserves.</p>
<p>Formula— Unreserved fund balances / Net operating revenues</p>	<p>General reserves are usually carried on the books as an unreserved fund balance in the operating fund. Sometimes special reserves are maintained in a separate fund. For example, reserves for replacing equipment such as computers or copying machines may be kept in the fund balance of an internal service fund (i.e., a fund used to charge operating departments for the use of equipment). Reserves can also be appropriated as a budget item in some form of contingency account.</p> <p>Regardless of the way in which reserves are recorded, an unplanned decline in fund balances may mean that the LG will be unable to meet a future need.</p>

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Unrestricted fund balance of general operating fund	Worksheet 1 (W1), line 18					
2	Net operating revenues	W2, line 13					
3	Unrestricted fund balance of general fund as percentage of net operating revenues	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

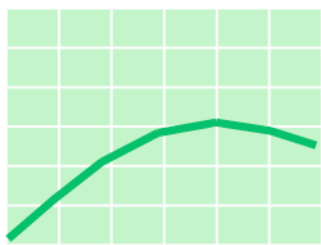
- Are fund balances dropping lower than is considered desirable? Can they be rebuilt?
- Are fund balances being used to subsidize operating deficits? See Indicator 14, Operating Deficits.
- Are reserves being used for purposes other than those they were originally set aside for?

Suggestions for policy statements—There are no set rules for determining the appropriate level of reserves. Much depends on circumstances, such as the kinds of natural disasters or hardships that the LG is subject to and the adequacy of its insurance coverage, the flexibility of the LG's revenue base, the overall financial health of the LG, province regulations, and national economic conditions. The following policy

statements can help local officials relate this indicator to their financial decision making.

- A reserve will be established to cope with emergencies. This reserve will be maintained at _____ percent of the operating fund.
- A contingency reserve fund will be established to provide for nonrecurring unanticipated expenditures, or to meet unexpected small increases in service delivery costs. This reserve will be maintained at _____ percent of the operating fund.

INDICATOR 17: LIQUIDITY



Warning Trend— Decreasing amount of cash and short-term investments as a percentage of current liabilities

Formula— Cash and short-term investments / Current liabilities

Credit industry benchmarks—A liquidity ratio of less than one to one (a current account deficit) is considered a negative factor, but it would be mitigated by a trend of three or more years that shows that the ratio will exceed one to one in the coming year. A less than one-to-one ratio for more than three years is considered a decidedly negative factor.

Liquidity refers to the flow of cash in and out of the LG treasury. LGs often receive their revenues in large instalments at infrequent intervals during the year. If revenues are received before they need to be spent, the LG will have a positive liquidity or positive cash flow position. Excess liquidity or “cash reserves” are a valuable cushion against unexpected expenditures. If a LG has a negative cash flow and no cash reserves, it must either borrow money from a bank or a higher level of government or issue some type of short-term notes (such as tax anticipation notes) or put off paying its employees and bills.

A good measure of a LG’s short-run financial condition is its cash position. Cash position, which includes cash on hand and in the bank, as well as other assets (short-term investments) that can be easily converted to cash, determines a LG’s ability to pay its short-term obligations. This is also known as liquidity, and the immediate effect of insufficient liquidity is insolvency—the inability to pay bills. Low or declining liquidity can indicate that a LG has overextended itself in the long run. A cash shortage may be the first sign.

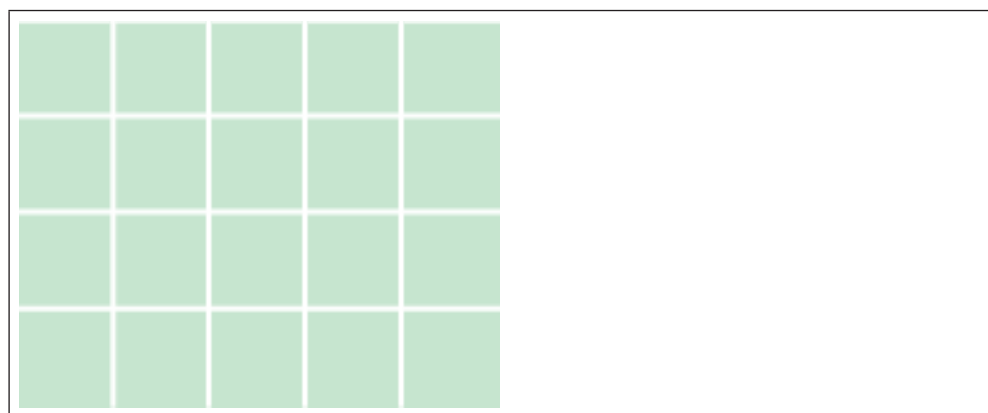
Businesses use a standard ratio of liquidity called the “quick ratio”: cash, short-term investments, and accounts receivable divided by current liabilities (short-term debt, current portion of long-term debt, accounts payable, accrued and other current liabilities). If this ratio is less than one to one (or less than 100 percent), the commercial entity is considered to be facing liquidity problems. Most of a commercial entity’s accounts receivable, however, are collected within thirty days; a LG’s receivables are usually not collected that quickly. Accordingly, the ratio of cash and short-term investments to current liabilities is a better measure of a LG’s liquidity.

Comparing cash and short-term investments to current liabilities is also referred to as current account analysis. In this terminology, an excess of liabilities over cash and short-term investments (a ratio of less than one to one) would be referred to as a current account deficit, and the reverse (a ratio of greater than one to one) would be a current account surplus.

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Cash and short-term investments	Worksheet 1 (W1), line 3					
2	Total current liabilities	W1, line 9					
3	Cash and short-term investments as a percentage of total current liabilities	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

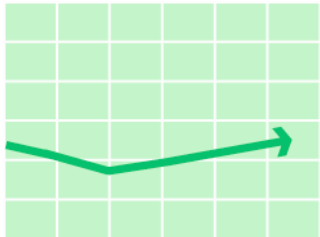
- Are current expenditures higher than can be supported by current revenues? See Indicator 1, Revenues per Capita; Indicator 10, Expenditures per Capita; and Indicator 14, Operating Deficits.
- Is there an efficient system in place for generating bills for money owed to the LG?
- Are bills collected promptly? Is there a good system for identifying overdue accounts?
- Are reimbursements for grant expenditures and other intergovernmental payments requested and paid promptly?
- Does the LG's reporting system show monthly cash availability?
- Are cash needs anticipated early enough to acquire the cash?

- Are projected expenditures and revenues routinely compared? Can large expenditures be scheduled to coincide with revenue flows?

Suggestions for policy statements—Policies could be set both for levels of liquidity and cash management procedures. The following statements can help local officials relate this indicator to their financial decision making.

- A cash-flow analysis will be made of all funds on a regular basis. Disbursement, collection, and deposition of all funds will be scheduled to ensure maximum cash availability.
- The account system will provide regular information about cash position and investment performance.
- When permitted by law, cash from several different funds will be pooled for investment.
- At least _____ percent of all idle cash will be continuously invested.

INDICATOR 18: CURRENT LIABILITIES

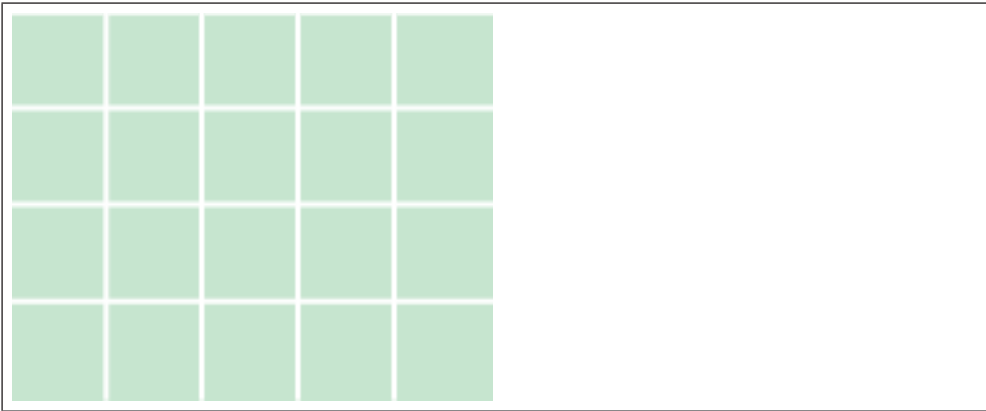
	<p>Current liabilities are defined as the sum of all liabilities due at the end of the fiscal year, including short-term debt, current portion of long-term debt, all accounts payable, accrued liabilities, and other current liabilities.</p> <p>A major component of current liabilities may be short-term debt in the form of loans from other levels of government or from banks. Although short-term borrowing is an accepted way to deal with uneven cash flow, an increasing amount of short-term debt outstanding at the end of successive years can indicate liquidity problems, deficit spending, or both.</p>
<p>Warning Trend— Increasing current liabilities at the end of the year as a percentage of net operating revenues</p>	<p>Credit industry benchmarks—The credit industry considers the following situations negative factors: (1) Short-term debt outstanding at the end of the year exceeding 5 percent of operating revenues (including tax anticipation notes but excluding bond anticipation notes), and (2) a two-year trend of increasing short-term debt outstanding at the end of the fiscal year (including tax anticipation notes). Note that these benchmarks are only for the short-term debt portion of current liabilities.</p>
<p>Formula— Current liabilities / Net operating revenues</p>	<p>Credit industry benchmarks—The credit industry considers the following situations negative factors: (1) Short-term debt outstanding at the end of the year exceeding 5 percent of operating revenues (including tax anticipation notes but excluding bond anticipation notes), and (2) a two-year trend of increasing short-term debt outstanding at the end of the fiscal year (including tax anticipation notes). Note that these benchmarks are only for the short-term debt portion of current liabilities.</p>

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005

1	Total current liabilities	Worksheet 1 (W1), line 9					
2	Net operating revenues	W2, line 13					
3	Current liabilities as a percentage of net operating revenues	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is short-term debt being used to fund an operating deficit? See Indicator 14, Operating Deficits.
- Are accounts payable being postponed to cope with revenue shortfalls or over expenditures? See Indicator 17, Liquidity.
- Are the accounts receivable that may be securing short-term debt valid and currently collectible?
- Are techniques for collecting accounts receivable effective?
- Are there procedures for prompt recognition and collection of money owed to the LG?
- Are techniques for managing and projecting cash flow accurate and efficient?
- Are expenditure overruns causing increased borrowing?

Suggestions for policy statements—Policies should be developed to provide guidelines for: (1) levels of outstanding short-term debt, and (2) procedures for using and retiring short-term debt. The following policy statements can help local officials relate this indicator to their financial decision making.

- Tax anticipation notes will be retired annually, and bond anticipation notes will be retired within six months of the completion of the project.
- Short-term debt outstanding at the end of the year will not exceed 5 percent of net operating revenues (including tax anticipation notes but excluding bond anticipation notes).

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After operating position indicators, which are most useful from your role perspective in the LG, and why?

DEBT INDICATORS

Debt is an effective way to finance capital investments to even out short-term revenue flows, but its misuse can cause serious financial problems. Even a temporary inability to repay debt can damage a LG's credit rating, which can in turn increase the cost of future borrowing.

LGs usually use short-term debt to make up for uneven cash flows. Revenue shortfalls or over expenditures may occasionally prevent repayment of a short-term debt during the year in which it was borrowed, in which case the LG may choose to repay the loan and then re-borrow the money. The original loan is, in effect, repaid from the proceeds of the new loan. This is called "rolling over" the debt and has the net effect of turning a short-term debt into a long-term debt. If this practice continues over a number of years, and the amount of outstanding debt increases each year, it may be an indication that the debt is being used to finance operating deficits—a sure sign of financial problems.

The most common forms of long-term debt are long-term loans, general obligation and revenue bonds. Even when these types of debt are used exclusively for capital projects, LGs need to ensure that their outstanding debt does not exceed their ability to repay as measured by the wealth of the community (property value or personal and business income). Another way to evaluate ability to repay is to consider the amount of principal and interest, or debt service, that the LG is obligated to repay each year. Also to be considered are overlapping debt and other LG's debts against which the LG has pledged its full faith and credit (such as school or sewer districts). These terms are defined in subsequent pages.

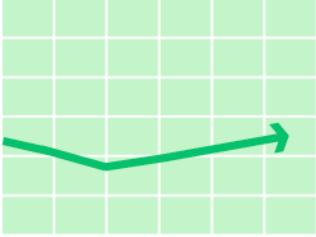
Under the most favourable circumstances, a LG's debt is proportional in size and rate of growth to its tax base; does not extend past the useful life of the facilities that it finances; is not used to balance the operating budget; does not require repayment schedules that put excessive burdens on operating expenditures; and is not so high as to jeopardize the LG's credit rating.

An examination of your LG's debt structure can reveal the following:

- Inadequacies in cash management procedures or expenditure controls,
- Increasing reliance on long-term debt,
- Decreasing expenditure flexibility (due to increased fixed costs in the form of debt service),
- Use of short-term debt to finance current operations,
- Sudden large increases or decreases in future debt service, or
- The amount of additional debt that the community can absorb.

The indicators shown in this section can be used to monitor changes in debt structure. The debt indicators are discussed in detail in the following pages.

INDICATOR 19: LONG-TERM DEBT

	
Warning Trend— Increasing net direct bonded long-term debt as a percentage of assessed valuation	<p>Direct debt is bonded debt for which the LG has pledged its full faith and credit. It does not include the debt of overlapping jurisdictions, such as separate school or sewer districts, even if the LG has pledged its full faith and credit for such debts.</p> <p>Self-supporting debt is bonded debt that the LG has pledged to repay from a source separate from its general tax revenues. Examples would include a water bond that is repaid from the income of the water utility, and special assessment bonds that are repaid from special charges levied on specific properties within a special assessment district.</p>
Formula— $\text{Net direct bonded long-term debt} / \text{Assessed valuation}$	<p>Net direct debt is direct debt minus self-supporting debt. An increase in net direct bonded long-term debt as a percentage of assessed valuation can mean that the LG's ability to repay is diminishing—assuming that the LG depends on the property tax to pay its debts. Long-term debt dependent on other revenues, such as sales tax, should be calculated as a percentage of the revenue sources on which it depends.</p>

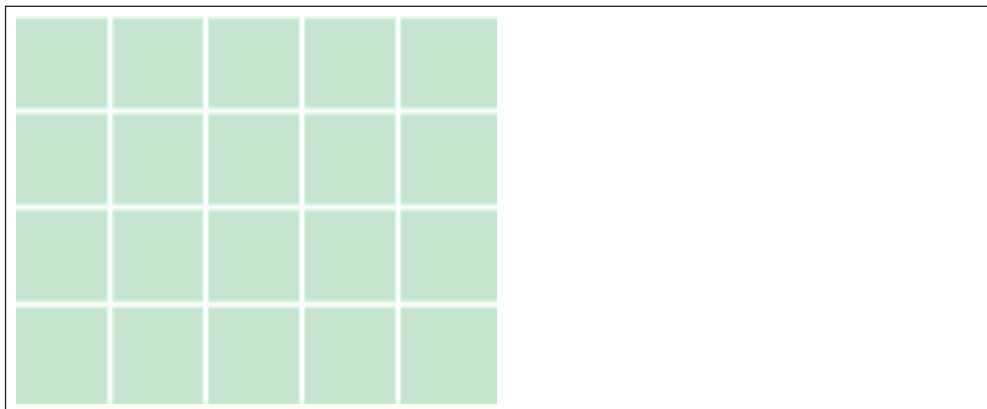
<p>Credit industry benchmarks—Credit industry benchmarks for assessing long-term debt often include the net direct bonded debt of the LG, as well as the bonded debt of overlapping jurisdictions that is geographically applicable to the LG. In this chapter, net direct bonded debt plus overlapping bonded debt is referred to as overall net debt. Warning signals for overall net debt are as follows:</p> <ul style="list-style-type: none"> • Overall net debt exceeding 10 percent of assessed valuation • An increase of 20 percent over the previous year in overall net debt as a percentage of market valuation • Overall net debt as a percentage of market valuation increasing 50 percent over the figure for four years earlier • Overall net debt per capita exceeding 15 percent of per capita personal income • Net direct debt exceeding 90 percent of the amount authorized by state law. 	<p>The long-term debt indicator uses assessed valuation in the denominator and assumes that property taxes are the primary source of debt repayment. You may, however, want to use a different denominator if your LG's primary source of revenue is not the property tax.</p> <p>Debt can also be monitored on a per capita basis. This approach is especially useful for communities that do not rely heavily on property taxes and that cannot easily compute a substitute revenue base for comparison. The per capita measure relates debt increases to changes in population size. As the population increases, capital needs and, hence, long-term debt, would be expected to increase. If, however, long-term debt is increasing as population stabilizes or declines, debt levels may be reaching or exceeding the LG's ability to pay. This assumes that the ability to generate revenue and to repay debt is directly related to population size, but this may not be true if the population change is caused by a change in family size and not in number of households. In this case, substituting per household for per capita figures in the denominator may make sense.</p> <p>Long-term debt should not exceed the LG's resources for paying the debt. If this does occur, the LG may have difficulty obtaining additional capital funds, may have to pay a higher rate of interest for them, and may have difficulty repaying existing debt.</p> <p>When graphing this indicator, it might be helpful to draw in warning lines as suggested in the section on credit industry benchmarks.</p>
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Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Assessed valuation	Worksheet 7 (W7), line 7					
2	Net direct long-term debt	W1, line 10					

3	Net direct long-term debt as a percentage of assessed valuation	Line 2 / Line 1*					
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*Plot the appropriate years and these figures on the following graph. Population or personal income can also be substituted in place of or in addition to assessed valuation.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

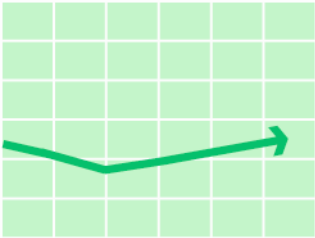
- Is assessed valuation, population, or another primary revenue base declining? See Indicator 24, Population, and Indicator 26, Property Value.
- Is long-term debt increasing? If so, consider the following questions:
 - Is the LG becoming more reliant on long-term debt to finance capital projects?
 - How much additional debt will need to be incurred in the next three to five years?
 - Are debt proceeds being used to fund ongoing operations?
 - Is the increase a trend, or is it caused by a debt issued for a one-time-only capital project, such as a new LG building?
 - What was the amount of long-term debt before the increase? Was it low to moderate, or was the amount already straining the LG's ability to pay? See Indicator 20, Debt Service.

Suggestions for policy statements—A number of policy statements can—and probably should—be set to suggest desirable levels of over-all net debt as well as procedures for issuing new debt. For example, statements could be developed to match the credit industry benchmarks (e.g., overall net debt will not exceed 10 percent of assessed valuation, or overall net debt per capita will not exceed 15 percent of per capital personal income). Of course, tighter limits than those suggested by the credit industry benchmarks could also be set.

The following policy statements can help local officials relate this indicator to their financial decision making.

- Proceeds from long-term debt will not be used for current, ongoing operations.
- Long-term borrowing will be confined to capital investments too large to be financed from current revenues.
- Bonds will be paid back within a period not to exceed the expected useful life of the capital investment.
- Where possible, special assessment, revenue, or self-supporting bonds will be used instead of general obligation bonds.
- Good communication with bond rating agencies will be maintained, and a policy of full disclosure on every financial report and bond prospectus will be followed.

INDICATOR 20: DEBT SERVICE



Warning Trend— Increasing net direct debt service as a percentage of net operating revenues

Formula— $\text{Net direct debt service} / \text{Net operating revenues}$

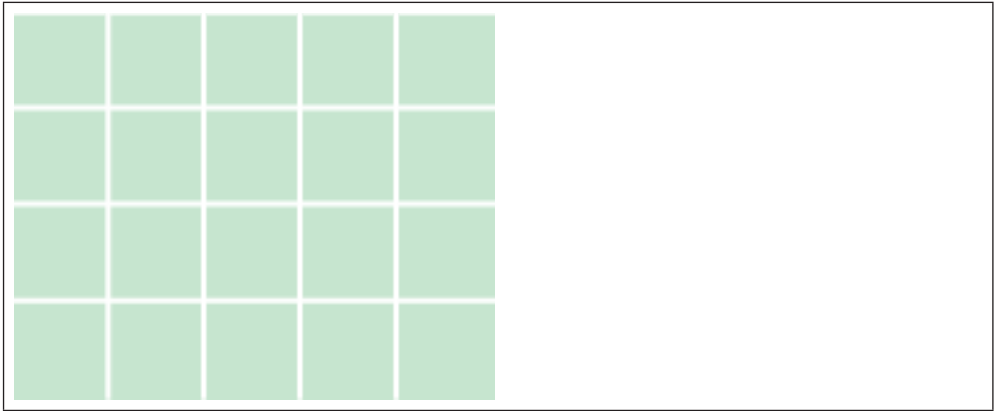
Debt service is defined here as the amount of principal and interest that a LG must pay each year on net direct bonded long-term debt plus the interest it must pay on direct short-term debt. Increasing debt service reduces expenditure flexibility by adding to the LG's obligations. Debt service can be a major part of a LG's fixed costs, and its increase may indicate excessive debt and fiscal strain.

Credit industry benchmarks—Debt service on net direct debt exceeding 20 percent of operating revenues is considered a potential problem. Ten percent is considered acceptable.

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Total net direct debt service	Worksheet 3 (W3), line 8					
2	Net operating revenues	W2, line 13					
3	Net direct debt service as a percentage of net operating revenues	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



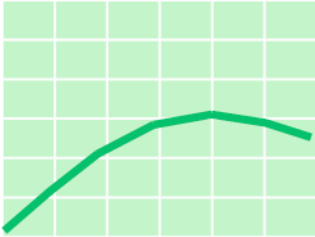
Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (what can be done?). The following are suggested starting points for this analysis.

- Is the increase caused by an increase in long-term or short-term debt? If so, review indicators 18 and 19, Current Liabilities and Long-term Debt.
- Is the increase due to increases in the interest rate rather than to increases in principal? Can the LG improve its credit rating to reduce interest rates in the future?
- Can debt issued at a relatively high interest rate be refinanced at an appreciably lower rate to reduce the annual amount of debt service?
- What are the projected debt service requirements over the next ten years? Will they increase or decrease dramatically at any point?

Suggestions for policy statements—Policy statements could be developed to suggest desirable levels of debt service as well as procedures for analyzing future debt service. The following policy statements can help local officials relate this indicator to their financial decision making.

- Total debt service for general obligation debt will not exceed 10 percent of net operating revenues.
- Before bonded long-term debt is issued, the impact of debt service on total annual fixed costs will be analyzed.

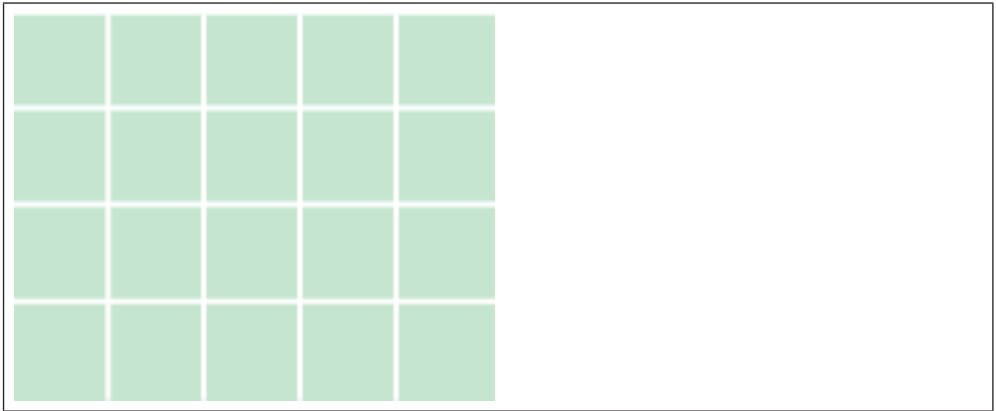
INDICATOR 21: OVERLAPPING DEBT

	<p>Overlapping debt is the net direct debt of another LG or governmental entity that is issued against a tax base within part or all of the geographic boundaries of the LG. Examples of other governmental entities that may overlap LGs are schools, street lighting or sewer districts. The level of overlapping debt is only that debt applicable to the property that the LG and governmental entity share.</p> <p>Overlapping debt is important because it measures the ability of the entire community's tax base to repay the debt obligations issued by all of its governmental and quasi-governmental jurisdictions. Also, if other jurisdictions default, the LG may have a contingent, moral, or political obligation to assume the debt or provide the services or both. As with long-term debt of the LG itself, increases in overlapping debt can be measured in terms of assessed valuation or other appropriate tax base or repayment source.</p>
<p>Warning Trend— Increasing long-term overlapping bonded debt as a percentage of assessed valuation</p>	
<p>Formula— Long-term overlapping bonded debt / assessed valuation</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Overlapping long-term debt	Worksheet 1 (W1), line 11					
2	Assessed valuation	W7, line 7					
3	Overlapping long-term debt as a percentage of assessed valuation	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis

- To what extent is your LG directly liable for the debt of other governmental entities or agencies?
- Are overlapping governmental entities financially healthy? If one were to default, would your LG be under pressure to assist it financially or to provide the service?

Several other data sources can be substituted for assessed valuation in the denominator of this indicator. Per capita personal income is an alternate measure of ability to repay debt. Population can be another choice, if your LG does not rely heavily on property taxes. Where the total population is decreasing but the number of households is stable, “per household” can be substituted for population.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After reviewing debt indicators, which are most useful from your role perspective in the LG, and why?

UNFUNDED LIABILITIES

An unfunded liability is one that has been incurred during the current or a prior year, that does not have to be paid until a future year, and for which reserves, or funds, have not been set aside. It is similar to long-term debt in that it represents a legal commitment to pay at some time in the future. If such obligations are permitted to grow over a long period of time, they can have a substantial effect on a LG's financial condition.

Two types of unfunded liabilities are considered here: pension liability and employee leave (compensated absences) liability. Both have significant potential to affect a LG's financial condition because:

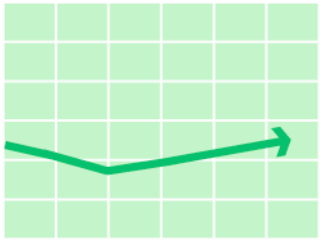
1. They do not show up in the ordinary financial records in a way that makes their impact easy to assess, and
2. They accumulate gradually over time.

Pension and employee leave liabilities may go unnoticed until they have created severe problems. An analysis of a LG's unfunded liabilities can answer the following questions:

- Is the pension liability increasing? How fast is it growing? How much is unfunded?
- Are pension contributions sufficient so that pension system assets and investment earnings are keeping pace with the growth in benefits?
- Is the amount of unused vacation and sick leave per employee increasing?
- Are policies for the payment of unused vacation and sick leave realistic compared to the LG's ability to pay?

The following indicators can be used to monitor changes in unfunded liabilities.

INDICATOR 22: UNFUNDED PENSION LIABILITY

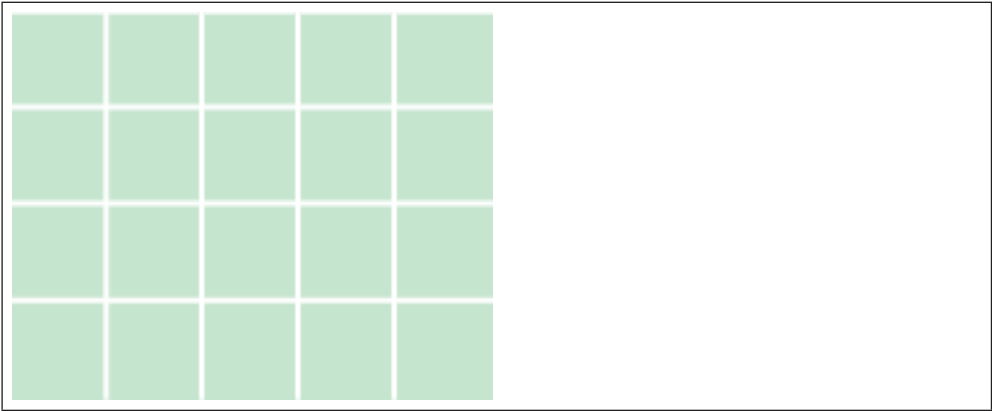
	
<p>Warning Trend— Increasing unfunded pension liability as a percentage assessed valuation</p>	
<p>Formula— $\text{Unfunded pension liability} / \text{Assessed valuation}$</p>	
<p>Pension plans can represent a significant expenditure obligation. Basically, there are two ways to fund pension plans: either when benefits need to be paid (“pay as you go”), or as benefits are accrued, in which case the money is invested in a reserve against the time when benefits will have to be paid (“full funding”.) Under the pressure of balancing the annual budget, some governments choose the pay-as-you-go approach or a partial funding approach. Either approach can work on a short-term basis. Deferral, however, can create a more serious problem in a future year than is being avoided in the current year—if the dollars are not available in the future year to meet the pension obligations.</p> <p>Growth in unfunded liability for vested benefits places an increasing burden on the tax base. The significance of this burden in relation to the community’s ability to pay can be measured by comparing the unfunded liability to changes in assessed valuation. This comparison assumes that the ability to pay is directly related to assessed valuation, as would be the case if property taxes were the primary source of revenue for the payment of vested benefits. If another revenue source will be the primary source for the payment of pension liabilities, that source can be substituted for assessed valuation. In cases where assessed valuation or other categories of the revenue base do not seem appropriate, the per capital measure can be used to show the growth of pension liability in relation to population growth; this measure assumes that the community’s ability to generate revenues is directly related to population size.</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Unfunded pension liability (vested benefits)	Worksheet 6 (W6), line 1					
2	Assessed valuation of property	W7, line 7					

3	Unfunded pension liability (vested benefits) as a percentage of assessed valuation	Line 1 / Line 2*					
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*Plot the appropriate years and these figures on the following graph.

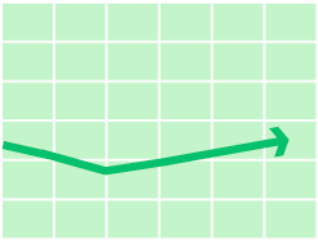


Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?) The following are suggested starting points for this analysis:

- In the next five to ten years, is there sufficient funding to pay anticipated benefit disbursements? If not, is there a plan for increasing funding?
- Have recent changes in pension plan benefits or actuarial assumptions increased the unfunded pension liability? Can employee contributions be increased or future benefits reduced?
- Has the interest earned from pension assets decreased? Is this due to general economic conditions, increases in pension plan costs, or poor cash and investment management?
- Have employee contributions dropped because workers are withdrawing from the plan? Has the proportion of participants receiving benefits increased due to retirement, termination, or change in payment policies? If such factors are creating a problem, can new policies be adopted to deal with them?
- Have actuarial assumptions been too optimistic? Has the plan been designed and analyzed by a professional actuary?

Suggestions for policy statements—The technical nature of this indicator makes it difficult to suggest any policy statements, except perhaps that “The budget will provide for adequate funding of all retirement systems.”

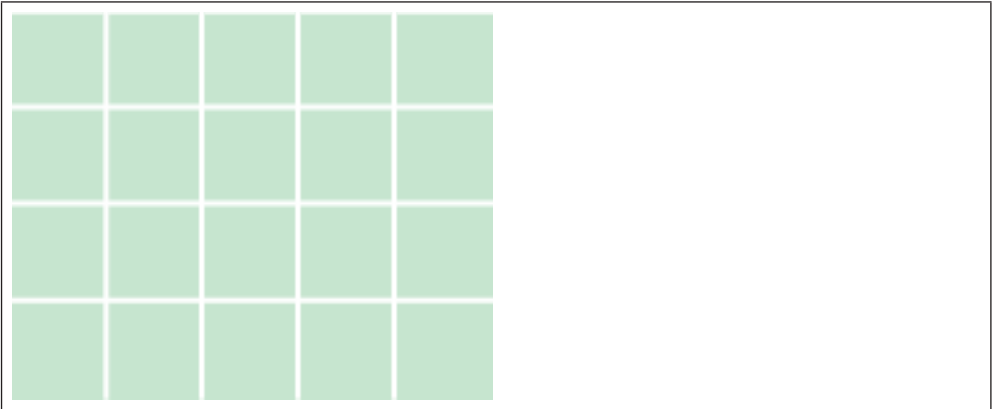
INDICATOR 23: PENSION ASSETS

	<p>A pension plan's assets are held primarily as cash or investments. A decline in the ratio of plan assets to benefits due can indicate serious problems in the management of the pension plan. An additional ratio to consider the annual amount of pension receipts as a percentage of annual benefits paid, which focuses more specifically on a pension plan's ability to meet its current cash requirements.</p>
<p>Warning Trend— Decreasing value of pension plan assets as a percentage of benefits paid</p>	
<p>Formula— Pension plan assets / Annual pension benefits paid</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

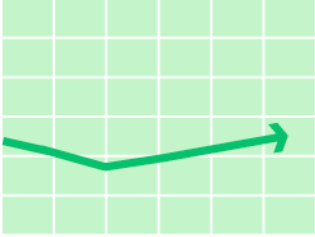
Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Pension plan assets	Worksheet 6 (W6), line 3					
2	Pension benefits paid	W6, line 4					
3	Pension plan assets as a percentage of benefits paid	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the trend is observed, you should try to determine its causes and its significance and to devise action steps for addressing it. A starting point for this analysis would be to review the “Suggestions for Analysis” under indicator 22, Unfunded Pension Liability.

INDICATOR 24: ACCUMULATED EMPLOYEE LEAVE



LGs usually allow their employees to accumulate some portion of unused vacation and sick leave to be paid at termination or retirement. Although leave benefits initially represent only the opportunity cost of not having work performed, these benefits become a real cost when employees are actually paid for their accumulated leave, either during their employment or at termination or retirement.

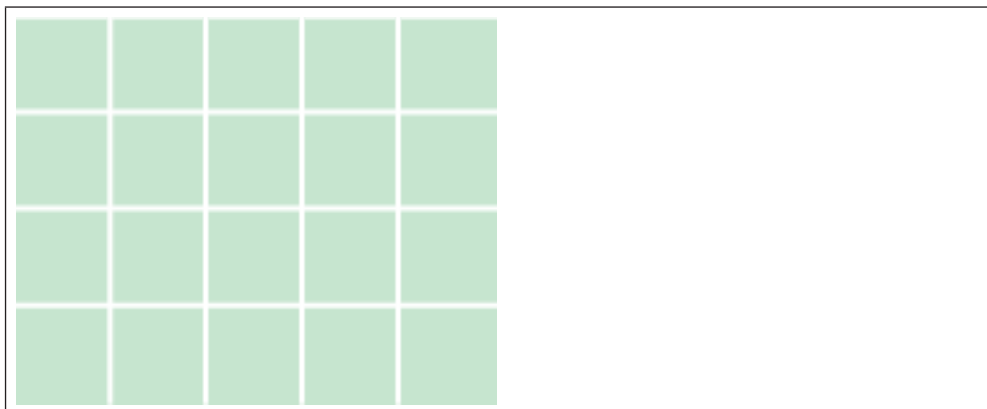
Warning Trend— Increasing number of unused vacation and sick leave days per employee

Formula— Total days of unused vacation and sick leave / Number of employees

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003		2005
1	Total days of unused vacation and holiday leave	Worksheet 3 (W3), line 13					
2	Total days of unused sick leave	W3, line 14					
3	Total days of unused vacation and sick leave	Line 1 + Line 2					
4	Number of LG employees	W3, Line 12					
5	Days of unused vacation and sick leave per employee	Line 3 / Line 4					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?) The following are suggested starting points for this analysis.

- Has the increase been created by changes in policies on accumulated leave? Are long-term costs of changes in benefit packages estimated before agreements are confirmed?
- Is the increase caused by a greater accumulation of leave under existing leave policies? Do workloads or cash-out policies discourage employees from taking vacation and thus contribute to the accumulation of these benefits?
- Are there reports that show the current amount of accumulated leave benefits?

Suggestions for policy statements—Policy statements could be developed to specify maximum allowable levels of accumulated annual leave and procedures for cash-out of vacation benefits. The following policy statements can help local officials relate this indicator to their decision making.

- Employees are allowed to accumulate a maximum of _____ hours of vacation leave, after which additional vacation leave must be used or forfeited. (This policy statement may vary depending on the class of employee.)
- Employees may apply for cash payments for accumulated vacation leave only if at least _____ hours of vacation leave have been taken in the preceding twelve months.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After reviewing unfunded liabilities indicators, which are most useful from your role perspective in the LG, and why?

CAPITAL PLANT

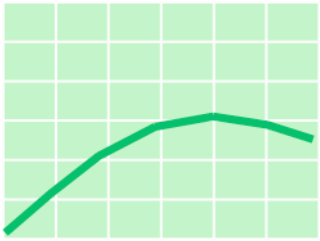
Most of a LG’s wealth is invested in its physical assets or capital plant—streets, buildings, utility networks, and equipment. If these assets are not properly maintained or are allowed to become obsolete, the results are often (1) decreasing usefulness of the assets, (2) increasing cost of maintaining and replacing them, and (3) decreasing attractiveness of the LG as a place to live or do business.

LGs often defer capital plant expenditures because to do so is a relatively painless way to temporarily reduce expenditures and ease financial strain. Continued deferral can however, create serious problems that are made even more serious by the huge sums of money invested in capital facilities. Some of the problems associated with continued deferred maintenance are the following:

- Safety hazards and potential liability risks that may result, for example, from a deteriorating bridge or cracked sidewalk,
- Reduction in residential and business property value,
- Loss of efficiency that can result, for example, when an obsolete truck is more often in the garage than on the street,
- An increase in the cost of bringing the facility up to acceptable standards—if, for example, resurfacing has been delayed for so long that a street has to be completely reconstructed,
- The potential for a huge future obligation created by a maintenance and replacement backlog.

The condition of the capital plant is especially difficult to monitor because few LGs maintain comprehensive, centralized records of capital assets apart from enterprise funds. Additional information can be found in Capital Investment Planning of this series. The indicators shown in this section can, nevertheless, be used to monitor changes in the condition of the capital plant.

INDICATOR 25: MAINTENANCE EFFORT

	<p>Enduring assets, such as streets, LG buildings, and bridges, are built at tremendous cost, and their decline can have far-reaching effects on business activity, property value, and operating expenditures. Deferring maintenance of such assets can also create significant unfunded liability.</p> <p>In general, maintenance expenditures should remain relatively stable (in constant dollars), relative to the amount and nature of the assets. A declining ratio between maintenance expenditures and size of asset stock may be a sign that the LG's assets are deteriorating. If the trend persists, deterioration will push up maintenance expenditures.</p>
Warning Trend— Declining expenditures for maintenance of general capital assets per unit of asset (constant dollars)	
Formula— Expenditures for repair and maintenance of general capital assets (constant dollars) / Quantity of assets	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Net operating revenues	Worksheet 2 (W2), line 13					
2	Restricted operating revenues	W2, line 14					
3	Restricted operating revenues as a percentage of net operating revenues	Line 2 / Line 1*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

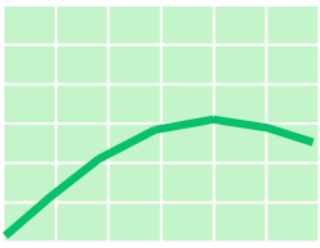
- Is maintenance of capital assets being deferred to such a degree that any of the following are occurring?
 - Unit costs for repair and replacement are increasing.
 - The useful life of an asset is being reduced.
 - Business activity or property value is decreasing.
 - Operating costs are increasing.
- How large is the potential future cost caused by deferred maintenance? Is there a plan for funding it?
- Are future maintenance costs projected before new capital facilities are built?
- Is there a schedule that shows the cost and timing of future maintenance and replacement needs for all LG assets? Are operating costs also taken into consideration?

Suggestions for policy statements—Policy statements could be developed to suggest levels of spending as well as budgeting procedures for maintaining capital assets. The following policy statements can help local officials relate this indicator to their financial decision making.

- The budget will provide sufficient funding for adequate maintenance and orderly replacement of capital plant and equipment.
- All assets will be maintained at a level that protects capital investment and minimizes future maintenance and replacement costs.
- All equipment replacement and maintenance needs for the next five years will be projected, and the projection will be updated each year. A maintenance and replacement schedule based on this projection will be developed and followed.

- Future maintenance needs for all new capital facilities will be fully costed out.

INDICATOR 26: CAPITAL OUTLAY

	<p>Expenditures for operating equipment—such as trucks and computers—drawn from the operating budget are usually referred to as capital outlay. Capital outlay items normally include equipment that will last longer than one year and that has an initial cost above a significant minimum amount, such as five hundred dollars. Capital outlay does not include capital budget expenditures for construction of infrastructure such as streets, buildings, or bridges.</p>
<p>Warning Trend— A three or more year decline in capital outlay from operating funds as a percentage of net operating expenditures</p>	<p>The purpose of capital outlay in the operating budget is to replace worn equipment, vehicles, etc. or to add new items. The ratio of capital outlay to net operating expenditures is a rough indicator of whether the stock of equipment is being adequately replaced. Over a number of years, the relationship between capital outlay and operating expenditures is likely to remain about the same. If this ratio declines in the short run (one to three years), it may mean that the LG's needs are temporarily satisfied, since most equipment lasts more than one year. A decline persisting over three or more years can indicate that capital outlay needs are being deferred, which can result in the use of inefficient or obsolete equipment.</p>
<p>Formula— Capital outlay from operating funds / Net operating expenditures</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Capital outlays	Worksheet 3 (W3), line 5					
2	Total net operating expenditures	W3, line 11					
3	Capital outlays as a percentage of net operating expenditures	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed try to identify the causes (Why is it happening?), assess the significance (Is it important? and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

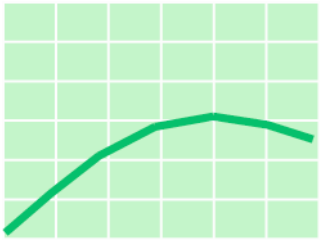
- Is needed capital outlay being deferred? Is this leaving your LG with worn or obsolete equipment?
- Can improved maintenance extend the efficiency and life of the equipment? For example, does your LG have official maintenance and replacement schedules, and are such schedules developed for each new piece of equipment?
- Is the decline due to an inability to make large-scale purchases in a single year? Can an internal service fund be established to charge departments a lease fee covering operating and replacement costs, thereby building a replacement fund over a number of years? Or can a simple reserve fund be established for the same purpose?
- Is the decline in capital outlay due to the recent acquisition of equipment with a relatively long life, or the acquisition of more efficient equipment that reduces overall needs for equipment replacement?

Suggestions for further analysis—If a major portion of your LG's equipment purchases is made through a separate fund, then that fund should be analyzed in conjunction with Indicator 21, Maintenance Effort.

Also, basing this indicator on departmental or functional categories (e.g., park maintenance or street repair) can focus the analysis on specific programs and the equipment they require.

Suggestions for policy statements—See the suggested policy statements under Indicator 21, Maintenance Effort.

INDICATOR 27: DEPRECIATION EXPENSE

	<p>Depreciation is the mechanism by which the cost of a capital asset is amortized over its estimated useful life. Not every country allows LGs to charge depreciation. Depreciation is usually recorded only in enterprise and internal service funds. Total depreciation cost is generally a stable proportion of the cost of capital assets, because older assets that have been fully depreciated are often removed from service and replaced by newer assets.</p> <p>If depreciation costs are declining as a proportion of capital asset costs, the assets on hand are probably being used beyond their estimated useful life. This can result in the inefficiencies and higher costs discussed under Maintenance Effort and Capital Outlay, Indicators 21 and 22. If the ratio is declining because of assets are not being replaced, it can indicate that the enterprise or internal service funds lack the resources to remain solvent. It could be, however, that the estimated useful life of an asset or assets was initially underestimated or that the scale of operations has been reduced; either instance could also produce a decline in the ratio of expenses to cost of assets.</p>
<p>Warning Trend— Decreasing depreciation expense as a percentage of total depreciable capital assets (at cost) for enterprise funds and internal service funds</p>	
<p>Formula— Depreciation expense / Cost of depreciable capital assets</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003		2005
1	Depreciation expense	Worksheet 1 (W1), line 13					
2	Cost of depreciable capital assets	W1, line 12					
3	Depreciation cost as percentage of depreciable capital asset cost	Line 1 / Line 2*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Are the assets being used past their useful life? Is this increasing operating costs or lowering the quality of services? See Indicators 25 and 26, Maintenance Effort and Capital Outlay, for further analysis.
- Were the lives of the assets initially underestimated, thereby creating a premature decline in this ratio?
- Has the scale of operations in the enterprise or internal service fund changed or declined, thereby requiring lower depreciation charges?

LEARNING APPLICATION

POLICY MAKER _X_	CEO _X_	FINANCE MANAGER _X_	DEPARTMENT HEAD _X_
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After reviewing capital plant indicators, which are most useful from your role perspective in the LG, and why?

COMMUNITY NEEDS AND RESOURCES INDICATORS

The community needs and resources indicators encompass economic and demographic characteristics including population, personal income, property value, employment, and business activity. Community needs and resources is a category in which tax base and economic and demographic characteristics are treated as different sides of the same coin. On the one side, tax base determines a community's wealth and its ability to generate revenue (that is, the level of personal, commercial, and industrial income). On the other side are economic and demographic characteristics that affect community demands, such as demands for public safety, capital investments, and social services.

Changes in community needs and resources are interrelated in a continuous, cumulative cycle of cause and effect. For example, a decrease in population or jobs lowers the demand for housing and causes a corresponding decline in the market value of housing; this in turn reduces property tax revenues. The initial population decline also has a negative effect on retail sales and personal income, causing LG revenues to drop even further. But because of fixed costs in its expenditure structure that are impervious to declines in population or business activity, the LG cannot always balance the revenue loss with a proportionate reduction in expenditures. The LG may, in fact, be forced to raise taxes to make up for lost revenues: this puts a greater burden on the remaining population. As economic conditions decline and taxes rise, the LG becomes a less attractive place to live and the population may decline further. The cycle continues.

Community needs and resources are difficult to translate into indicators because the data are not easy to gather. The following nine indicators represent only those for which some data are reasonably available.¹ Some LGs will nevertheless have difficulty gathering some of the information.

In addition to analyzing Indicators 28-36, you may want to look at some more subjective issues, such as locational advantages and current land use, especially as they relate to the LG's ability to generate revenue. Also important are the LG's plans and realistic potential for future development. The commercial and industrial base should be considered for its ability to generate revenue and employment, and its vulnerability to regional and national economic cycles. Also to be considered is the relationship of the commercial and industrial base to the larger economic region, especially the balance of exports and imports. Other considerations are the LG's occupational characteristics, the skills and educational levels of its population, the age and condition of its housing, and the prognosis for new construction and redevelopment. Such information is difficult to quantify, but it is useful in evaluating financial condition.

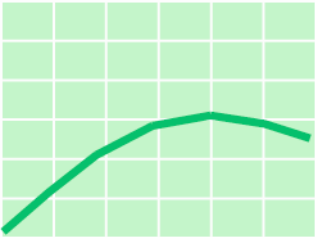
An examination of local economic and demographic characteristics can identify the following situations:

¹ For example, LGs with their own income or occupation tax can easily monitor personal income, but those without these taxes will find the information almost impossible to get—other than from the national census—unless the province makes the information available.

- A decline in the tax base as measured by population, property value, employment, or business activity.
- A need to shift public service priorities because of a change in the age or income of residents or in the type or density of physical development.
- A need to reassess public policies if, for example, the jurisdiction has lost businesses to surrounding communities, or national or regional economic conditions have changed.

Changes in economic and demographic characteristics are most useful for long-run financial analysis and can be monitored by using the indicators shown in this section.. Each indicator is discussed in detail in the following pages.

INDICATOR 28: POPULATION

	<p>The exact relationship between population change and other economic and demographic factors is uncertain. Population change can however, directly affect LG revenues: for example, some taxes are collected on a per capita basis, and many intergovernmental revenues and grants are distributed according to population. A sudden increase in population can create immediate pressures for new capital outlay and higher levels of service. In the case of LG land annexations, where the capital infrastructure is already in place, there may still be a need to expand operating programs.</p> <p>A decline in population would at first glance, appear to relieve the pressure for expenditures, because the population requiring services is smaller. But in practice, a LG faced with population decline is rarely able to make reductions in expenditures that are proportional to the population loss. First, many costs, such as debt service, pensions, and governmental mandates, are fixed and cannot be reduced in the short run. Second, if the out-migration is composed of middle- and upper-income households, then those remaining in the LG are likely to be the poor and aged, who depend the most on LG services. In addition, the interrelationship of population levels and other economic and demographic factors tends to give population decline a cumulative negative effect on revenues: the greater the decline, the more adverse the effects on employment, income, housing, and business activity.</p>
<p>Warning Trend— Rapid change in population size</p>	
<p>Formula—Population</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Population	Worksheet 7 (W7), line 1					

*Plot the appropriate years and these figures on the following graph. It might also be helpful to plot the rate of change (Current year minus prior year; remainder divided by prior year).



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (what can be done?). The following are suggested starting points for this analysis.

If population is declining, consider the following questions:

- Is out-migration due to poor job opportunities or other adverse economic or social conditions? For example, is the tax burden on businesses relatively high compared to that of nearby communities? Are young adults out-migrating?
- Has the rate of in-migration decreased because of housing or job scarcity?
- Has demand for industrial and commercial real estate decreased? Might governmental action reverse this trend? See Indicators 26 and 27 (Property Value, and Business Activity).
- Has the number of smaller households increased, thereby creating additional service costs to the LG? If so, are smaller households increasing in number because there are fewer families with children?
- Are housing construction patterns providing more multifamily units or smaller units?

Can local officials address the population decline by any of the following means:

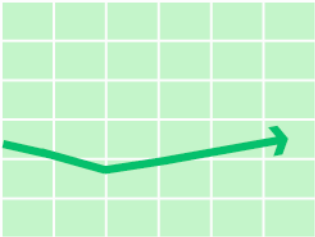
- Encouraging more housing starts by reducing building code restrictions, development fees, or other land-use restrictions?

- Zoning to encourage residential development?
- Developing or improving a program for marketing available land for development?

If population is increasing, consider the following questions:

- Is the increase due to the annexation of developed land, housing redevelopment, or new housing construction?
- Is the cost of servicing the new residents equal to revenues obtained from them? Is the level of business activity growing along with the increase in residential development?
- Is growth straining one or more of the following: water supply, sewer system capacity, traffic circulation, off-street parking capacity, electric and other utility capacities, waste disposal capacity, quality of atmosphere, or open space resources? What are the capital costs of enlarging the infrastructure for these services? What are the new operating costs?
- Should developer fees, user fees, land dedication, or construction requirements be instituted or increased to ensure that new development pays its way?
- Can and should local officials institute growth controls?

INDICATOR 29: MEDIAN AGE

	<p>As in the case with changes in population size, the relationship between the population's median age and other economic and demographic factors is not clear. Evidence does not indicate, however, that an aging population and an increase in the number of senior citizens can hurt both the revenue and expenditure profiles of a LG.</p>
<p>Warning Trend— Increasing median age of population</p>	<p>Revenues may be affected for two reasons. First, the income of senior citizens is often in the form of social security and pension payments, which might not change at the same rate as the general economy, and in many countries, senior citizens may have full or partial exemptions from property taxes and user fees. Second, older persons may spend less money than younger persons. As the proportion of senior citizens increases, expenditure rates for government services may increase because senior citizens tend to require a more expensive mix of services, especially in the area of health and welfare.</p>
<p>Formula—Median age of population</p>	<p></p>

	<p>As younger age groups leave a community or decrease as a percentage of population, business activity can decrease in greater proportion, especially if most of the people leaving are between twenty-five and forty years of age: people in this age group usually spend more of their income than those in any other age group. If this age group leaves, the community also loses a significant portion of its labour force, which can further damage the local economy. If, however, the increase in median age is caused by a drop in the number of families with young children, this can have a favourable effect on expenditures because it reduces needs for school, recreation, and related programs.</p>
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Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Median age	Worksheet 7 (W7), line 2					

*Plot the appropriate years and these figures on the following graph. It might also be helpful to plot the rate of change (Current year minus prior year; remainder divided by prior year).

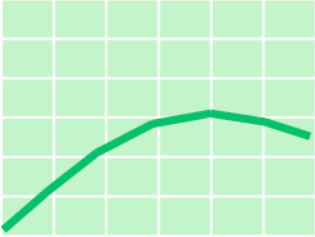


Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (what can be done?). The following are suggested starting points for this analysis.

- Is the increase in median age due to a net out-migration of young families with children? If this pattern is undesirable, can the community be made more attractive to young families?

- Is the increase in median age due to a net out-migration of young adults? Can local officials help create better opportunities for this age group?
- Is the increase in median age due to the in-migration of older citizens? Is this in-migration creating needs for a higher level or a different mix of services?

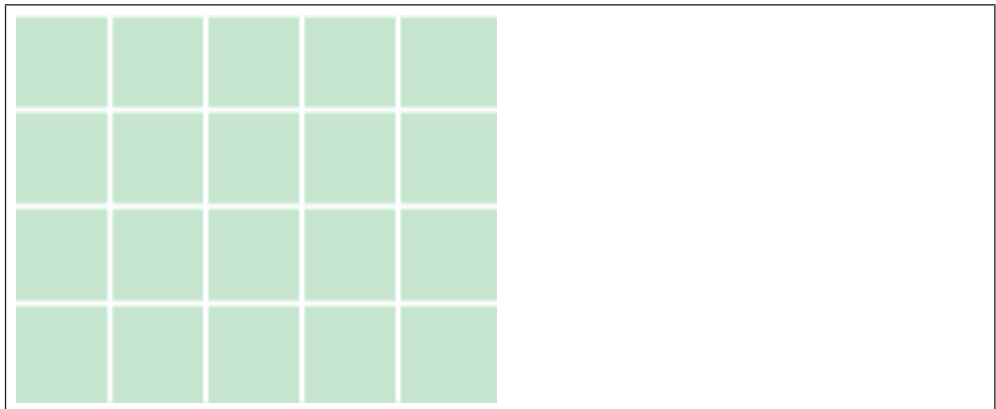
INDICATOR 30: PERSONAL INCOME PER CAPITA

	<p>Personal income per capita is one measure of a community’s ability to pay taxes: the higher the per capita income, the more property tax, sales tax, income tax, and business tax the community can generate. If income is evenly distributed, a higher per capita income will usually mean a lower dependency on LG services such as transportation, health, recreation, and welfare. Credit rating firms use per capita income as an important measure of a LG’s ability to repay debt. They compare per capita income with per capita LG expenditures to determine whether growth in income is keeping pace with growth in expenditures. If not, a community’s tax burden is increasing, which may contribute to a future inability to meet financial obligations.</p> <p>A decline in per capita income causes a drop in consumer purchasing power and can provide advance notice that businesses, especially in the retail sector, will suffer a decline that can ripple through the rest of the local economy.</p>
<p>Warning Trend— Decline in the level, or growth rate, of personal income per capita (constant dollars)</p>	
<p>Formula— Personal income (constant dollars) / Population</p>	
	<p>Changes in personal income are especially important for communities (such as suburbs) that have little commercial or industrial tax base, because personal income is the primary source from which taxes can be paid. In communities with a large commercial and industrial base, personal income is less important.</p> <p>Distribution of income is also important. Two communities with the same per capita income may have different income patterns among their households. One may have a small number of extremely high-income households and a large number of low-income households. Another may be composed entirely of middle-income households. The first LG may have service demands associated with the large number of low-income households; the second may have fewer service demands and a robust economy.</p>

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Personal income	Worksheet 7 (W7), line 3					
2	Consumer price index (CPI) for LG's area	Central govt or university					
3	CPI in decimal	Line 2 / 100					
4	Personal income in base-year dollars	Line 1 / line 3					
5	Current population	W7, Line 1					
6	Personal income per capita in base-year dollars	Line 4 / line 5					

*Plot the appropriate years and these figures on the following graph.

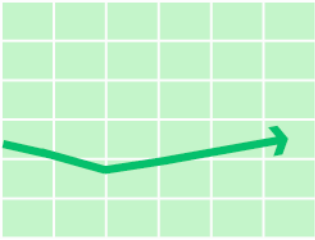


Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is the decline due to a general decline in economic conditions over which local officials have little control?
- Is the decline being felt throughout the region or only in your LG? Can economic development strategies be devised to attract and retain higher-income households? Can LG powers be used to encourage development of higher value housing? Can services and capital infrastructure be upgraded to make the LG a more desirable place to live and do business?

- Is the decline due to an out-migration of middle-or upper-income households? Will the LG be left with a population that needs a higher level of services but that provides a lower level of per capita revenue? See Indicator 1, Revenues per Capita.
- Is the decline due to an in-migration of low-income households?
- Is the decline in personal income creating a decline in LG revenues? If so, can a proportionate change in expenditures be made? If not, are there sufficient resources for maintaining existing service levels, or are there plans for future cutbacks?

INDICATOR 31: POVERTY HOUSEHOLDS OR PUBLIC ASSISTANCE RECIPIENTS

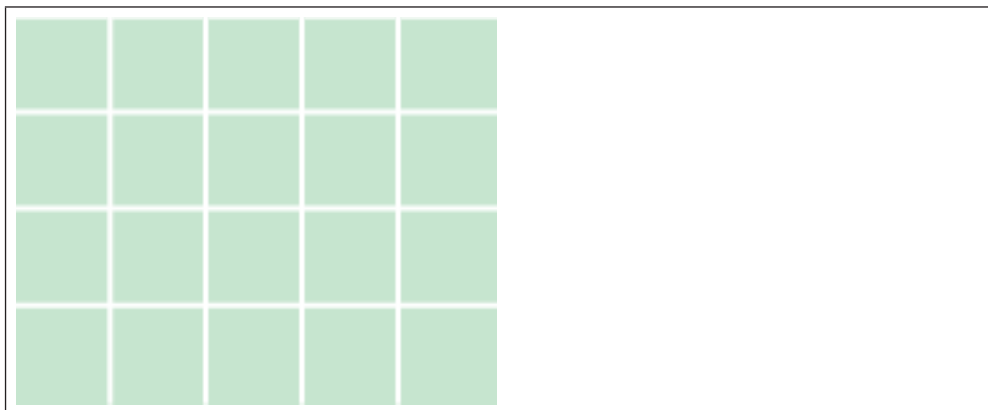
	<p>In addition to measures of overall change in personal income, an increase in the proportion of poverty households or public assistance recipients can signal a future increase in the level and unit cost of some services, because low-income households have relatively higher needs and a relative lack of personal wealth.</p>
<p>Warning Trend— Increasing households or public assistance recipients / households in thousands</p>	
<p>Formula— Poverty households or public assistance recipients / households in thousands</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Poverty households	Worksheet 7 (W7), line 5					
2	Public assistance recipients	W7, line 4					
3	Residential households	W7, line 11					
4	Households in thousands	Line 3 / 1,000					

5	Poverty households or public assistance recipients per thousand households	Line 1 or line 2 / line 4*					
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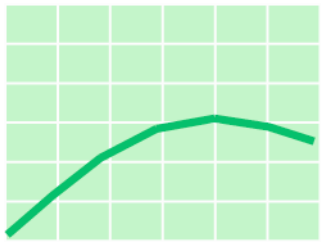
*Plot the appropriate years and these figures on the following graph. Population can also be used.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is the increase part of an overall decline in income that will have adverse implications for revenues and expenditures? See indicator 30, Personal income per capita.
- Is the increase due to unemployment or to a decline in local business conditions? See indicators 35 and 36, Employment base and Business activity.
- What is the sex and median age of the head of household for the poverty households or public assistance recipients? Are the heads of households primarily senior citizens, retired persons, young adults, or single mothers with dependent children?
- Can programs run by voluntary associations or government programs paid for through province or central government funding be used to increase the job skills and general employability of low-income residents?
- Are poverty households located in particular geographic areas. Does this have secondary impacts on property value because of resident's inability to provide adequate maintenance? Are housing assistance payments available to low-income families?

INDICATOR 32: PROPERTY VALUE

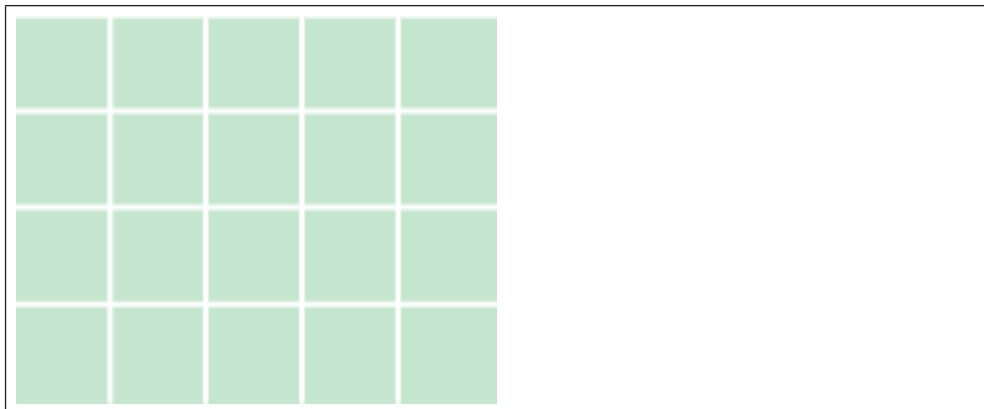
	<p>For those countries in which property tax is a major source of revenues for LGs, property value is important. Especially in a LG with a stable or fixed tax rate, the higher the aggregate property value, the higher the revenues. Communities experiencing population and economic growth are likely to experience short-run, per unit increases in property value. This is because in the short run, the housing supply is fixed and the increase in demand created by growth will force prices up. Declining areas are more likely to see a decrease in the market value of properties.</p>
<p>Warning Trend— Declining growth or drop ion the market value of residential, commercial, or industrial property (constant dollars)</p>	<p>The effect of declining property value on governmental revenues depends on the LG's reliance on property taxes. The extent to which the decline will ripple through the LG's economy, affecting other revenues such as those from sales tax, is more difficult to determine. All of the economic and demographic factors are closely related. A decline in property value will most probably not be a cause but a symptom of other, underlying problems.</p>
<p>Formula— Change in property value (constant dollars) / Property value in prior year (constant dollars)</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Market value of property (residential, commercial & industrial)	Worksheet 7 (W7), lines 8-10					
2	Consumer price index (CPI) for the LG's area	Central govt, university					
3	CPI in decimal	Line 2 / 100					
4	Property value (constant dollars)	Line 1 / line 3					
5	Change in property value	Line 4 current year minus line 4 prior year					

6	Percentage change in property value	Line 5 for current year / line 4 for prior year					
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*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is the decline due to regional trends over which local officials have no control? Will the decline have a negative effect on revenues? Are contingency plans being made?
- Is the decline due to a decline in population or business activity? See Indicators 24 and 27, Population and Business Activity.

Is the decline due to a deterioration of the capital plant? Can any of the following means be used to upgrade the capital plant?

- An improved maintenance and replacement program,
- New or better construction,
- Redevelopment and other long-term financing,
- The use of one-time grant dollars,
- The use of impact fees for improvement of roads, parks, water, or sewer facilities, or
- Stimulation of private investment.

Is the decline due to deterioration in the housing stock? Can any of the following means be used to upgrade the housing stock?

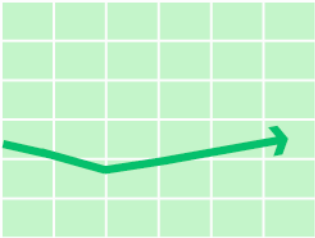
- Redevelopment programs,
- Rehabilitation loans,
- Housing grants,

- Mortgage subsidies,
- Code enforcement,
- Special assessment districts, or
- Incentives for new development or rehabilitation.

Suggestions for further analysis—Rapidly increasing property value, as well as rapidly decreasing property value, can be a sign of potential trouble. If property value is growing significantly faster than personal or median income, and reassessment is capturing this growth, more citizens may become unable to pay their property taxes—especially older citizens on fixed incomes.

To assess the potential for this situation, compare the rate of change (present year minus previous year; remainder divided by previous year) in this Indicator 25 to the rate of change in Indicator Personal Income per Capita.

INDICATOR 33: RESIDENTIAL DEVELOPMENT

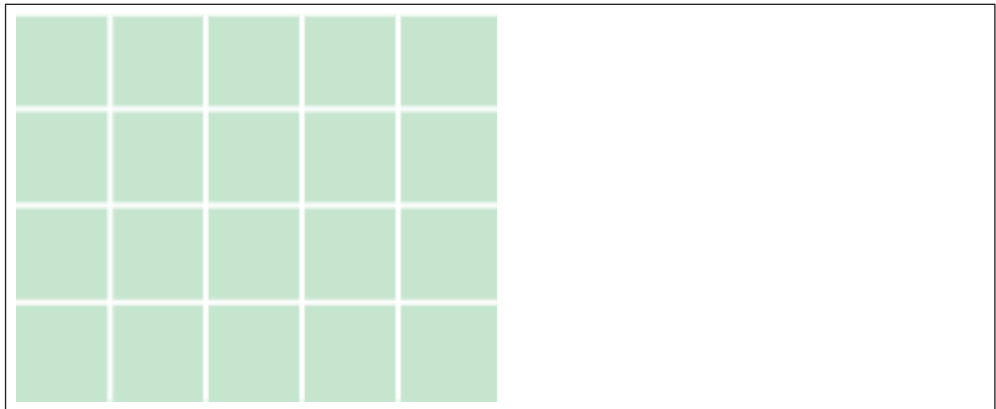
	<p>The net cost of serving residential development is generally higher than the net cost of serving commercial or industrial development, because residential development usually creates more expenditure demands than revenue receipts.</p> <p>The location of new residential development is important. Houses built on the outer fringes of a LG can impose far greater initial costs on a LG than houses built within already developed areas. This is because the LG must provide capital items such as streets, sewer lines, and water mains to service the new development. The effect of new residential development on the financial condition of a particular LG depends on the LG's economy, tax structure, development fee structure, and expenditure profile. The effect can be more precisely measured through fiscal impact analysis.</p>
<p>Warning Trend— Increasing market value of residential development as a percentage of market value of total development</p>	
<p>Formula— Market value of new residential development / Market value of total new development</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Market value of residential development	Worksheet 7 (W7), line 8					
2	Market value of total development	W7, line 6					

3	Market values of residential development as a percentage of market value of total development	Line 1 / Line 2*					
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*Plot the appropriate years and these figures on the following graph.

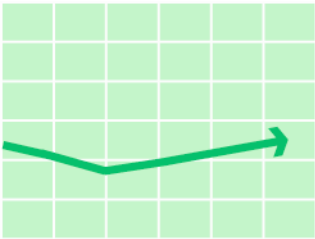


Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Does existing residential development pay for itself? If not, do revenues from commercial and industrial development make up the difference? Can these questions be better answered through fiscal impact analysis?
- Can the government develop a more diverse economic base through any of the following means?
 - Land aggregation and redevelopment programs.
 - Increasing the level of services on which businesses depend (e.g. parking, public transportation, street lighting) or upgrading the capital infrastructure.
 - Tax incentives, fee abatements, and decreased regulation for certain kinds of businesses.
 - A program to attract business by promoting the LG's advantages.
- Will new residential development generate enough revenues to pay increased operating costs? If not, will additional non-residential development make up the difference?
- Will the LG have to pay for additional infrastructure necessitated by new residential development? Can these costs be passed on to another level of government, to a special district, or to the developer?
- Should a policy of controlled growth be considered?

A second way to analyze the level of residential development is to compare the number of households to the value of non-residential development (that is, households divided by value of non-residential development). In many respects, the number of households more accurately represents service demands than does the dollar value of development. Whatever measure is used, if the amount of residential development is increasing relative to that of non-residential development, a LG should consider it a signal for further analysis.

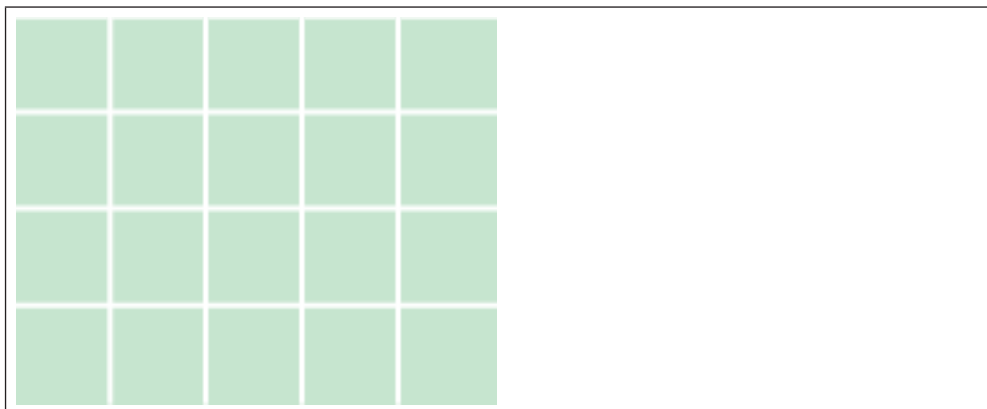
INDICATOR 34: VACANCY RATES

	<p>If the economy is sluggish or declining, demand for residential, commercial, and industrial rental property may drop and vacancy rates may increase. If the LG is an attractive place to live and do business, the demand for all types of rentals generally will be high and vacancies low. A surge in recent development can create a short-run increase in vacancies. Although this would not necessarily indicate problems, it can be a sign of overbuilding and should therefore be watched. In any event, tracking changes in vacancy rates can provide an early warning of potential economic and demographic problems.</p>
<p>Warning Trend— Increasing vacancy rates in residential, commercial, or industrial buildings</p>	
<p>Formula— Vacancy rates</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Residential vacancy rates	Worksheet 7 (W7), line 12*					
2	Commercial vacancy rates	W7, line 13*					
3	Industrial vacancy rates	Line 2 / Line 1*					

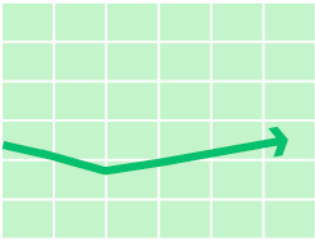
*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is the increase in vacancies due to an overall decline in their local economy? See indicator 36, Business activity.
- Are vacancies in commercial and industrial buildings due to obsolete building styles or designs? Can local officials encourage or help owners to renovate?
- Are vacancies in commercial and industrial buildings being created by firms that have moved to a neighbouring LG. Can your LG regain its competitive advantages? See indicator 36, Business activity.

INDICATOR 35: EMPLOYMENT BASE

	
Warning Trend— Increasing rate of local unemployment or a decline in the number of jobs within the community	The unemployment rate and the number of jobs within the LG are considered together because they are closely related; for the purpose of this discussion, they will be referred to as the employment base. Employment base is related directly to business activity and personal income. Changes in the unemployment rate are related to changes in personal income, and are thus a measure of, and an influence on, the LG's ability to support the business sector. A change in the number of jobs available in the LG is a measure of, and an influence on, business activity.
Formula— Local unemployment rate and/or the number of jobs within the community	If the employment base is growing, if it is sufficiently diverse to provide a cushion against short-run economic fluctuations or a downturn in one sector, and if it provides sufficient income to support the local business community, then it will have a positive influence on the LG's financial condition. A decline in the employment base—as measured by unemployment rate or number of available jobs—can be an early sign that overall economic activity is declining and that government revenues may be declining as well.

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005
1	Net operating revenues	Worksheet 2 (W2), line 13					
2	Restricted operating revenues	W2, line 14					
3	Restricted operating revenues as a percentage of net operating revenues	Line 2 / Line 1*					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

INDICATOR 36: BUSINESS ACTIVITY

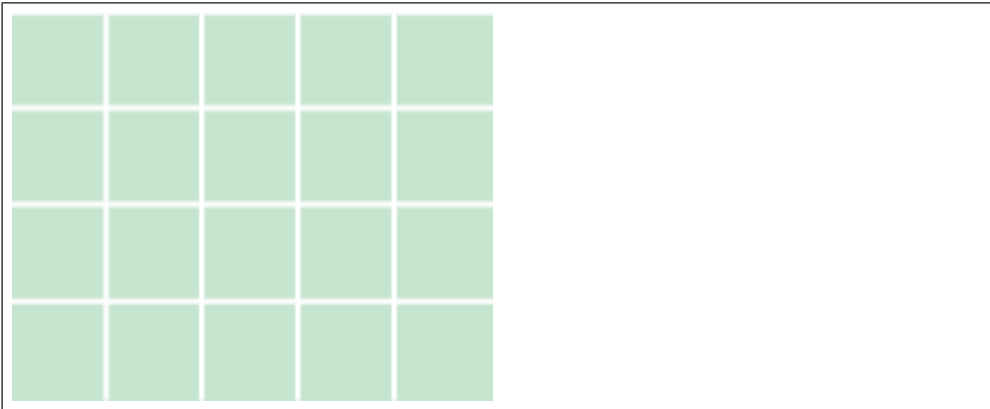
	<p>The level of business activity affects a LG's financial condition in two ways. First, it directly affects any revenue yields that are a product of business activity, such as those from sales or gross receipts taxes. Second, it has indirect influences: a change in business activity affects demographic and economic areas such as personal income, property value, and the employment base. Changes in business activity also tend to have cumulative effects. A decline in business activity can for example, harm a LG's employment base, income, and property value, which can in turn create further decline in business activity. Data on business may or may not be available and will vary from LG to LG.</p>
<p>Warning Trend— Decline in business activity as measured by retail sales, number of business units, gross business receipts, number of acres devoted to business, and market or assessed value of business property (constant dollars where appropriate)</p>	
<p>Formula—See trend worksheet</p>	

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Trend Worksheet							
Line	Description	Source	2001	2002	2003	2004	2005

1	Retail sales	Worksheet 7 (W7), line 17					
2	Number of business units	W7, line 18					
3	Gross business receipts	W7, line 19					
4	Number of hectares devoted to business	W7, line 20					
5	Market or assessed value of business property	W7, line 9 + line 10					

*Plot the appropriate years and these figures on the following graph.



Suggestions for analysis—If the warning trend is observed, try to identify the causes (Why is it happening?), assess the significance (Is it important?), and devise action strategies (What can be done?). The following are suggested starting points for this analysis.

- Is the decline due to regional or national trends beyond local control? Will the decline have a negative effect on revenues? Are contingency plans being made?
- Is the decline due to a change in population, income, or employment base? See Indicators 24 and 25.
- Is business activity declining because firms are going out of business or because they are relocating to other communities? In the second case, can the LG use any of the following means to attract and retain firms?
 - Increasing the level and quality of public services on which businesses depend.
 - Decreasing LG fees and regulations.
 - Improving the physical attractiveness of the LG.

- Providing businesses with tax incentives, fee abatements, and development inducements.
 - Making more industrial and commercial land available for development.
 - Being more aggressive in promoting the advantages of the LG.
- Is the LG maintaining its percentage share of business activity compared to the region or country, as measured by retail sales or other measures? If not, is this due to any of the following causes?
 - The emergence of stronger competition in other areas.
 - Local business services lagging behind local or neighbouring demand.
 - A decline in the supply of property suitable for business development.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After reviewing community needs and resources indicators, which are most useful from your role perspective in the LG, and why?

WORKSHEETS

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

WORKSHEET 1—DATA FROM FINANCIAL STATEMENTS

Worksheet needed for indicators

Line	Description	Used for indicator #	2001	2002	2003	2004	2005
1	Cash						
2	Short-term investments						
3	Cash + short-term investments	17					
4	Accounts payable (vouchers)						
5	Accrued liabilities						
6	Short-term debt						
7	Current portion of long-term debt						
8	Other current liabilities						
9	Total current liabilities (Sum lines 4 through 8)	17,18					
10	Net direct bonded long-term debt ¹	19					
11	Long-term overlapping bonded debt ²	21					
12	Cost of depreciable capital assets	27					
13	Depreciation expense	27					
14	Fund operating deficit (surplus)	14					
15	Business enterprise net profit (loss)	15					
16	Fund balance						
17	Reserves against fund balance						
18	Unreserved fund balance	16					
19	Uncollected property taxes	7					

WORKSHEET 2—REVENUES

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Line	Description	Used for indicator #	2001	2002	2003	2004	2005
	Local operating revenues						
1	Property tax revenues	6					
2	Revenues from fees and user charges that are intended to support service costs identified on Worksheet 3 line 5	8					
3	Revenues from other fees and user charges						
4	Other local revenues. List individual sources if the source is greater than 5% of total revenues						
5	Aggregate for sources that are individually less than 5% of total revenues						
6	Total local operating revenues (sum of lines 1-5)						
	Non-local operating revenues						
7	Intergovernmental operating revenues (may include shared revenues and transfers from higher levels of government)	3					
8	Other non-local operating revenues						

9	Total non-local operating revenues (line 7 plus 8)						
10	Gross operating revenues (line 6 plus line 9)	3					
11	LESS: revenues restricted to capital investments						
12	LESS: mandated capital investment transfers and special-purpose revenues						
13	Net operating revenues (line 10 minus line 11 minus line 12) ³	1,2,4,5,9,14,16,18,20					
14	Restricted operating revenues	2					
15	Elastic operating revenues	4					
16	One-time operating revenues	5					
17	Budgeted net operating revenues	9					

WORKSHEET 3—EXPENDITURES

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Line	Description	Used for indicator #	2001	2002	2003	2004	2005
	Net-operating expenditures ⁴						
1	Salaries and wages ⁵	13					
2	Fringe benefits ⁶	13					
3	Supplies (commodities)						

4	Purchased or contracted services						
5	Capital outlay ⁷						
	Net direct debt service ⁸						
6	Principal (long-term debt only)						
7	Interest (long- and short-term debt)						
8	Total net direct debt service (line 6 plus line 7)	20					
9	Other expenditures						
10	Transfers to other funds if not already included above						
11	Total net operating expenditures (sum of lines 1,2,3,4,5,8,9, and 10)	10,12,26					
	Other items						
12	Number of LG employees ⁹						
13	Days of unused vacation leave						
14	Days of unused sick leave						
15	Expenditures for services for which there is a fee or user charge						

WORKSHEET 4—FIXED COSTS SUMMARY

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Line	Description	Used for indicator #	2001	2002	2003	2004	2005
1	Debt service						
2	Province mandates (expenditures)						
3	Central government mandates (expenditures)						
4	Pension payments						
5	Lease-purchase payments						
6	Other long-term contracts						
7	Other fixed costs						
8	Total fixed costs (Sum of lines 1 through 7)	12					

A fixed cost is one over which the LG has little control in the short run because it is fixed by contractual agreement or mandated by law. The categories suggested on this worksheet represent some common fixed costs. Each LG needs to identify its own fixed costs and adjust the categories accordingly.

WORKSHEET 5—REPAIR AND MAINTENANCE OF ASSETS

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

The data collected on this worksheet are exclusively for Indicator 25, "Maintenance Effort." The indicator is calculated separately for each class of asset. Therefore, each class should contain similar types of assets all of which can be measured in the same way (e.g. hectares, linear meters). The way in which each class of asset will be measured will depend on common usage and the availability of information. Data on the expenditures of dollars by asset class may not be available in accounting records but may be available in department records. Data on the amount of asset will most likely be available only from departmental records.

Line	Description	Used for indicator #	2001	2002	2003	2004	2005
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1	Residential streets Dollar expenditure ¹⁰ amount (Quantity ¹¹)	25					
2	Arterial streets Dollar expenditure amount (Quantity)	25					
3	Curbs & side-walks Dollar expenditure amount (Quantity)	25					
4	Buildings Dollar expenditure amount (Quantity)	25					
5	Park facilities Dollar expenditure amount (Quantity)	25					
6	Bridges Dollar expenditure amount (Quantity)	25					
7	Other ¹² Dollar expenditure amount (Quantity)	25					

WORKSHEET 6—PENSION PLAN DATA

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

In this worksheet, include only “defined-benefit” pension plans. A defined-benefit pension plan is “a pension plan stating the benefits to be received by employees after retirement, or the method of determining such benefits. The employer’s contributions under such a plan are determined actuarially on the basis of the benefits expected to become payable. Central government plans should be excluded unless that part of a state pension plan directly attributable to the LG can be identified.

Line	Description	Used for indicator #	2001	2002	2003	2004	2005
1	Unfunded vested benefits ¹³	22					
2	Pension plan receipts ¹⁴	22					

3	Pension plan as- sets	23					
4	Pension benefits paid ¹⁵	23					
5	Investment in- come	23					

WORKSHEET 7—ECONOMIC-DEMOGRAPHIC DATA

Note: Worksheets will need to be reviewed for applicability in your country. Terms may be defined differently in your country.

Line	Description	Used for indi- cator #	Long run historical data base		Current Year Up-dates				
			1990	2000	20__	20__	20__	20__	20__
1	Population	1, 10, 11, 19, 28 & 30							
2	Median age of popula- tion	29							
3	Personal income of population	30							
4	Public as- sistance recipients	31							
5	Poverty households	31							
6	Total prop- erty value— market	33							
7	Total prop- erty value— assessed	19, 21 & 22							
8	Property value—resi- dential (Market and/or as- sessed)	32, 33							

9	Property value—commercial (Market and/or assessed)	32,36							
10	Property value—industrial (Market and/or assessed)	32,36							
11	Number of residential households	31							
12	Vacancy rates—residential	34							
13	Vacancy rates—Commercial	34							
14	Vacancy rates—industrial	34							
15	Local unemployment rate	35							
16	Number of jobs within LG	35							
17	Retail sales	36							
18	Number of business units	36							
19	Annual gross business receipts	36							
20	Number of hectares devoted to business	36							

You will need to find the information for the data given above. It may be available from higher levels of government including various central government ministries. If not available from government sources, then it may be available from your country's universities.

Long run historical data base—It is important to have this long-term historical information so that trends can be looked at in proper perspective.

When comparing different sources of data, especially for income-related data, check to see if population bases are the same and if definitions are the same. The term, “income,” especially can be defined different ways.

When comparing data over time, keep in mind any other changes during the same time period that would also affect the data, such as land annexations into the LG.

POLICIES FOR EVALUATING FINANCIAL CONDITION

This section is designed to help you evaluate the usefulness of your LG’s governing body policies in protecting and improving its financial condition. Although a broad range of statements, decisions, and activities could be construed as financial policies, financial policies are defined here as goals for the financial operation of a LG. Setting goals is important for financial health because it gives local officials a long-range perspective on their current approach to financial management. It also helps officials agree on the kind of financial condition they want for their LG.

In most communities, policies already exist in budgets, in capital investment plans, in the comprehensive plan, in a charter, in a grant application, in council resolutions, and in administrative practices. When financial policies are scattered among these kinds of documents, are unwritten, or are developed case by case, decisions are often made without consideration of other current policy decisions, past policy decisions, or future policy alternatives. This kind of policy making can lead to the following:

- **Conflicting policies.** The governing body may be making decisions that conflict with each other.
- **Inconsistent policies.** The governing body follows certain policies on one issue, then reverses itself on a similar issue.
- **Incomplete policies.** The governing body may not be making any policy at all on some aspects of financial management.

A formal set of policies can help the CEO and the governing body discover conflicts, inconsistencies, and gaps in their financial policies. It also can help the manager and governing body develop similar expectations regarding both managerial and governing body financial decision making.

To aid in developing the policy framework for evaluating financial condition most of the indicators in the section on Developing the Indicators provide policy statement suggestions for that particular indicator.

BENEFITS

Developing the recommended financial indicators does not and cannot explain specifically why a problem is occurring, nor does it provide a single number or index to

measure financial health. What it does provide are flags for identifying problems, clues about their causes, and time to take anticipatory action. Using the steps we recommend for developing the indicators and evaluating your LG's financial condition provides the following additional benefits:

- Provides for better planning and policy making. By graphing the indicators using a five-year history and then considering what the next few years probably look like begins to introduce long-range thinking into the financial planning process. It places the events of a single year into a longer perspective and permits local officials to follow changes over time. Policy makers can see the past effect of policies or lack of policies and decide to handle the future differently. So, this process has the advantage of providing a starting point for elected officials in setting or evaluating current financial policies. By looking at what the past has been, they can establish how they want the future to look and set policies accordingly.
- Pulls together "already existing" information from your LG's budget and financial reports, combines it with economic and demographic data, and creates a different way of looking at your LG's financial condition. This helps LG officials gain a better understanding of the LG's current financial condition as well as the path that it is currently on. These indicators can be plotted on a graph and used to identify existing problems of which local officials may be unaware or identify potential problems before they reach a serious condition. They offer a way to quantify a significant amount of information and present a straightforward picture of the LG's financial strengths and weaknesses to elected officials, citizens, credit-rating firms, and other groups with a need to know. Best of all, the indicators do not require complicated mathematical techniques or computer procedures (although a personal computer can be used to perform calculations and generate graphs).

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After reviewing the benefits identified above, are there other benefits that you believe your LG will receive from evaluating its financial condition?

OBSTACLES

You will find that making changes to the way LG conducts its business is not an easy task. There will be obstacles and barriers, such as political and staff resistance, time required, lack of performance information, lack of knowledge of the practices and standards, and the existing financial accounting system that impede your progress.

Resistance to change—In today's complex and ever changing society, most managers would agree with the statement "change is the only certainty." But that doesn't mean that everyone accepts change equally well. You can expect that in developing new analytical techniques and evaluating financial factors for management there will be some resistance from politicians and staff. Many elected officials who are wedded to past techniques, reports and formats will not see the value of producing new information and reports. They will argue that the current practice meets all the requirements and any others mean more work without producing any significant benefits. To this group of officials, additional data, information, and analysis undermines their existing information power base and the way that they have been making decisions in the past. They are unwilling to learn new methods and techniques.

Some staff members may also resist developing new techniques and management reporting systems because of the additional work that is required. They may say they are too busy with other duties to take on additional projects.

Lack of necessary financial and performance data—Another barrier or obstacle to developing indicators may be the lack of adequate accounting and other financial and performance information. For many LGs, "the data does not exist" may be a common complaint. If the data is not available, you will need to establish systems to collect and compile the needed data annually. Compiling the data over 5-10 years will provide an historical database from which to analyze historical trends and predict future years for forecasts.

Lack of knowledge of concepts and practices—Another obstacle exists when elected officials are not familiar with the terminology, techniques, processes, and practices of using financial condition indicators. Education of elected officials on these concepts using workshops and briefings is a staff responsibility. Information provided to elected officials should be presented in simple, non-technical terminology that can be easily understood. Elected officials must be well informed about the LG current management practices and efforts to improve the process and products. Their support is essential to achieving that goal.

Nature of LGs—Private sector firms can easily determine whether they are financially sound. The basic test is profit, which roughly translates into efficiency. For the LG, profit is not the motive and efficiency is only one of many objectives. A LG's objectives may include "public safety," "public health and welfare," "political satisfaction," and other qualities that can be measured only subjectively.

Limitations of LG accounting practices—LG accounting systems should be based on “auditability” and on giving high visibility to the monies passing through LG accounts. Accounting systems typically stress legal compliance and tracking the path of each unit of money in and out of the local treasury. Because of this focus, some countries consider fund accounting more important than program cost accounting or the measurement of long-term financial health. It is a very short-sighted focus and should be augmented with a methodology for evaluating the long-term financial condition of the LG.

LG financial analysis—There is a lack of world-wide normative standards for the characteristics of a LG considered in strong financial condition. Even within a country, this type of information may not be available. What, for example, is a healthy per capita expenditure rate, level of reserves, or amount of debt? Many countries are just now beginning to develop these kinds of benchmarks.

Some attempts have been made to develop in-country standards by averaging data for various LGs or otherwise comparing one LG to another. But, depending on the size of the country, communities may differ widely in characteristics such as land size, geography, demographics, revenue structure, and responsibility or authority to provide services. So, it will continue to be a challenge for countries to develop benchmarks that are appropriate for LGs.

The international credit-rating industry has benchmarks for evaluating LGs, but these benchmarks usually have to be considered in combination with central government benchmarks. Only in a few countries are LGs allowed to issue their own debt without it being tied to or through the central government. For those countries, additional more subjective criteria such as the diversity of the LG’s tax base or revenue sources are examples of benchmarks being used.

LEARNING APPLICATION

POLICY MAKER _X_ CEO _X_ FINANCE MANAGER _X_ DEPARTMENT HEAD _X_

After reviewing the obstacles identified above, which are most applicable from your role perspective in the LG, and why? Are there other obstacles that you anticipate in the process of developing indicators for your LG. How will you overcome them?

ENVIRONMENTAL AND ORGANIZATIONAL ASPECTS OF FINANCIAL CONDITION

These factors are described separately because they have no associated quantifiable indicators for identifying warning trends. A complete assessment of a LG's financial condition should not, however, ignore these five factors. This describes the particular aspects of each factor that can positively or negatively influence financial health; it also gives evaluation questions to help you assess the overall significance of each factor in your LG's financial condition.

EXTERNAL ECONOMIC CONDITIONS

External economic conditions include trends in inflation, employment, economic wealth, interest rates, and business activity. By and large, these conditions are beyond the control of LGs, which can usually only react to them. Anticipation and preparation are the best means of adjusting to changes in external economic conditions.

In the long run, this means building a local economic base that is protected from sudden downturns in the business cycle but that can still take advantage of upturns. We realize that for some countries, this may be a very long-term process. To build such a base, a LG must spend enough on the development and maintenance of its capital plant and provide a level of services that will encourage businesses to stay and expand. It must also have a stable, revenue-producing commercial and industrial sector whose markets will not diminish during national recessions and whose tax rates are under local control. The LG must carefully apply land-use controls and other LG powers. Tax rates should be competitive with those of other LGs providing similar services, so that businesses and residential development are not drawn away. The LG needs a nearby labour force that suits the available jobs, access to funding for capital expansion, plus other resources such as transportation routes providing good access to business markets. The availability of natural resources such as oil and minerals also influences the economic strength of some industries.

The lack of easily collected data and the existence of deficiencies in analytical procedures make it difficult to measure accurately the impact of external economic conditions at the local level. Because most of the current techniques are costly and require expertise not usually available to LGs, assessing these factors is generally not cost effective. This chapter does not include indicators that explicitly measure the impact of external economic conditions at the local level.

While you may not be able to explicitly measure the influence of such conditions on your LG, the following questions can help you evaluate how well your LG may be able to adjust to changes in external conditions.

- What is the composition of your LG's tax base? How sensitive is it to changes in the national and province economy? To help you answer these questions, see the following Indicators: 1, Revenues per Capita; 2, Restricted Revenues; 4, Elastic Tax Revenues; 6, Property Tax Revenues; 24, Population; 27, Business Activity.
- What is the level of revenues from intergovernmental sources? See Indicator 3, Intergovernmental Revenues.
- What mix and level of services is your LG required by law or local practice to provide?
- What is the level of fixed costs in your LG's budget? See Indicator 12, Fixed Costs.

INTERGOVERNMENTAL CONSTRAINTS

By virtue of national constitutions and laws, most LGs are creatures of the state. In many countries, the central government dictates the framework in which LGs must operate. These constraints can affect LG structure, service responsibilities, and financing powers. LG officials may find that such constraints limit the flexibility of their decision making.

In recent years, countries that are devolving and decentralizing responsibilities to LGs have mandated new services and/or spending levels for programs. Simultaneously, these higher levels of government may have reduced aid to LGs as a mechanism for coping with their own budget problems. These actions have severely harmed many LGs' financial condition.

Intergovernmental constraints are difficult to measure because they are a highly subjective and variable factor. The following questions can however, help you to analyze the effect of intergovernmental constraints on your LG's financial condition.

- What is the level of revenues from intergovernmental sources? What requirements for expenditures are tied to these sources? See Indicator 3, Intergovernmental Revenues.
- What is the level of expenditures for mandated programs? See Indicator 12, Fixed Costs.
- How close is your LG to its tax rate ceiling, if applicable?
- How close is your LG to its debt ceiling, if applicable?

NATURAL DISASTERS AND EMERGENCIES

Natural disasters include fires, earthquakes, hurricanes, typhoons, blizzards, floods, tornadoes, and similar events that require significant LG expenditures, and can devastate the local economy. To the extent that they can be anticipated, such events can be budgeted for, thereby lessening their impact on financial condition. A policy to maintain adequate reserves for emergencies and a high-quality risk management program can help protect the LG financially. But when the natural disaster is of a

huge scale, it can burden the LG with substantial costs that will probably not be fully alleviated by intergovernmental assistance.

Natural disasters and emergencies can cause financial harm in many ways. First, they may damage or destroy LG equipment, capital facilities, and property. Second, they may require the LG to provide emergency police, fire, sanitation, and general welfare services. Third, the LG may have to help the LG replace or repair lost private property. Fourth, the natural disaster may temporarily undermine the health of the local business community. If business activity and employment decrease, governmental revenues may drop and expenditure pressures may increase until the commercial sector can recover. And last, if the disaster is of large enough proportions, residents and businesses may leave the area permanently, altering the economic and demographic base of the LG.

While a LG cannot predict the exact timing and magnitude of a natural disaster, planning and preparation will help if and when one does occur. The questions that follow can help you to evaluate the impact of a natural disaster or emergency on your LG's financial condition.

- Has your LG analyzed its needs for reserves to respond to a natural disaster or emergency?
- Does your LG have a comprehensive emergency operations plan?
- If your LG has suffered damage from past disasters, have steps been taken to reduce the potential of future damage in those areas (for example, restriction of development in flood zones)?
- Is your LG's insurance coverage adequate? Have its insurance needs been evaluated recently? If little insurance coverage is available, has this issue been discussed with appropriate officials?

POLITICAL CULTURE

Political culture refers to the LG's attitudes toward taxes and services. Of all the factors that affect financial condition, local political culture is perhaps the most difficult to analyze, primarily because it is influenced by the interaction of individuals and by their varying economic, ethnic, religious, and social backgrounds.

In addition to social and demographic characteristics, other issues to be considered are:

- The manner of political representation.
- The extent of citizen participation.
- The structure of the LG organization.
- The decision-making process.
- The content of political issues.
- The age, size, and density of the LG.

Because political culture is highly subjective, this chapter does not include indicators or evaluation questions for measuring it. However, a careful assessment

of these issues, based on your own knowledge, is valuable in relating this factor to an evaluation of financial condition.

PRACTICES AND POLICIES THAT JEOPARDIZE FINANCIAL CONDITION

Management practices and governing body policies are often regarded as the most critical influences on financial condition because a LG can theoretically adjust to environmental changes by changing its expenditure pattern. This assumes that the LG will have enough notice of problems, that it understands their nature and extent, that it knows what to do, and that it is willing to do it. While these assumptions may be optimistic, practices and policies are the factors over which a LG should have control. It is through practices and policies that a LG can exert leverage when wrestling with financial problems.

When international credit rating firms evaluate the financial condition of LGs, they consider management practices and governing body policies to be very important. For example, they assess the “professionalism” of management by examining the quality of financial reporting and capital planning, and by checking to see whether the LG has used any financial “gimmicks” or tricks. They determine the responsiveness of the governing body by considering whether elected officials have been willing to raise tax rates when needed. In short, sound financial practices and policies enable a LG to maintain good financial condition and to avoid financial emergencies.

EVALUATING FINANCIAL MANAGEMENT PRACTICES

It is possible to assess fairly quickly whether your LG is relying on practices that, while not inherently bad, can damage its financial condition if they are used for too long. These practices fall into three categories:

- Repeated use of one-time revenue sources, such as prior years' reserves or proceeds from the sale of assets, to balance the budget.
- Deferring a large amount of current costs to the future: deciding, for example, to postpone maintenance of capital assets or to defer pension liabilities.
- Ignoring long-range or full-life costs of a liability: deciding, for example, to purchase a capital asset without calculating the full-life costs of owning, operating, and maintaining that asset.

Most LG officials recognize the danger of such practices and would not ordinarily use them. In times of stress caused by financial problems or political pressures, however, local officials may find themselves tempted or even forced to use them.

As interim strategies, these practices can resolve temporary problems and provide time to find long-run solutions to financial troubles. For example, deferring maintenance costs for one year may allow the initiation of new cost-cutting programs

and adjustments in service. But continued use of such practices can harm a LG's financial condition in three ways.

- First, these practices can create problems. A LG may already have a few financial problems, but if it does not take into account the full-life cost of a new program or project, it may commit itself to future expenditure obligations that it cannot meet. This can happen, for example, if the LG grants employees additional employee benefits without first costing out the benefits in dollars and projecting their impact on future budgets.
- Second, these practices may compound existing problems. For example, when a LG defers a current expenditure by postponing maintenance on capital equipment, the effectiveness and efficiency of operations may go down, thereby causing service delivery costs to go up. Moreover, the equipment may deteriorate until it becomes more expensive to repair or replace than if it had been regularly maintained.
- Finally, these practices may delay recognition of existing problems. This is the most dangerous result, because it permits problems to persist and to grow to serious proportions. Eventually, solving the problem may be much more costly and difficult than it would have been at an earlier phase. For example, if over several years a LG does not fund accrued pension liabilities, pension costs can eventually become a large percentage of fixed costs at a time when revenues are no longer growing, forcing an ill-timed and disruptive reduction in services.

Discovering how or to what extent these practices may be jeopardizing a LG's financial health is not always easy. To evaluate whether such practices are harming your LG's financial condition, read the description of the practices below; if an indicator is associated with the practice, examine the indicator to see whether it shows a reliance on the financial management practice in question.

PRACTICES THAT SUSTAIN AN OPERATING DEFICIT

An operating deficit occurs when current expenditures exceed current revenues. This may occur even though the annual budget is balanced, because one-time revenue sources (such as a surplus from a previous year) can be used to supplement current revenues. An operating deficit in any one-year may not be cause for concern, but frequent and increasing deficits can be a warning sign. If an operating deficit is allowed to continue or grow, two questions should be asked:

- Is the LG continuing a level of services and expenditures that it may not be able to afford in the long run?
- Is the LG ignoring the underlying cause of the deficit, such as a declining revenue base or decreased productivity, and thereby compounding the problem?

Local officials may have trouble spotting an operating deficit because most LG accounting systems do not provide information that would make an operating deficit obvious. That is, LG accounting systems do not use cost accounting, nor are revenues and expenditures fully accrued in most countries. These two circumstances prevent officials from obtaining precise information on the LG's operating position. Nevertheless, telltale signs can point to the existence of an operating deficit. These signs are the repeated use of the following practices: using reserves (fund balances) from prior years, short-term borrowing, internal borrowing, selling assets, and one-time accounting changes.

Use of reserves—The accumulation of operating surpluses builds reserves, which provide a financial cushion against the: loss of a revenue source, an economic downturn, unanticipated expenditures required by natural disasters, insurance loss, and the like, unexpected large-scale capital expenditures or other nonrecurring expenses, an uneven cash flow, and similar events.

For most governments, surpluses from prior years are a cushion that allows them to meet current cash flow needs, temporary revenue shortfalls, or unexpected expenditure demands—without suddenly adjusting tax rates or user fees or cutting expenditures during the budget year. Positive fund balances can also help LGs avoid short-term borrowing, thereby saving interest costs (although the opportunity to earn interest on a fund balance is lost).

Reserves may be budgeted in a contingency account or carried as a part of one or more fund balances. If they are carried as an unappropriated part of a fund balance, they may never appear in a LG's budget or be discussed during budget deliberations.

A consistent decline in fund balances over several years is one indication that the LG may be sustaining an operating deficit. Relying on reserves to sustain the deficit can be damaging in two ways: first, the LG is left with fewer resources to cope with a financial emergency; second, relying on reserves may affect the LG's credit rating, because credit rating firms examine the history of fund balances.

To determine whether your LG is using reserves to balance the budget, see Indicator 14, Operating Deficits, and Indicator 16, Fund Balances.

Short-term borrowing—In short-term borrowing, the LG incurs a debt that it must pay back within twelve months. When revenues and previous surpluses (fund balances) do not provide enough cash to meet expenditures during the fiscal year, your country may provide the following options:

- Some countries allow LGs to tax anticipation notes (TANs) to be issued to obtain cash. When the taxes are collected, these notes are redeemed.
- Some countries allow LGs to borrow from the central government bank.
- Some countries allow LGs to borrow from local banks.

Lending institutions and the LG generally regard such borrowing as an acceptable fiscal procedure as long as it is temporary and tax collections or some other known source of revenues will be received that are clearly large enough to repay the debt within the fiscal year.

At times, however, revenue shortfalls or over expenditures may render a LG unable to repay short-term borrowing within this time period. In this event, the LG may

choose to repay the loan and then re-borrow the money, or simply to pay only the interest on the loan and not the principal. This practice, called “rolling over” short-term debt, can in effect turn short-term debt into long-term debt. Some analysts spot financial troubles by looking at the level of short-term debt outstanding at the end of the fiscal year as a percentage of revenues. Rolling over short-term debt can create several problems for a LG:

- Interest rates are added for the time the debt remains outstanding.
- The LG's credit rating may be affected; when assessing the investment worthiness of a LG, investors and international bond rating firms look more and more closely at short-term debt.
- Unless revenues increase or the debt is rolled over yet another year, the LG is forced to reduce service levels or raise revenues in the next fiscal year to pay off the debt.

To determine whether your LG is using short-term borrowing to balance the budget, see Indicator 14, Operating Deficits, and Indicator 18, Current Liabilities.

USE OF INTERNAL BORROWING (IF YOUR COUNTRY USES FUND ACCOUNTING)

Internal borrowing occurs when one LG accounting fund runs out of money and the fund “borrows” from other LG funds rather than from an outside source. In private business, the entire business is treated as a single entity so there is not a comparable practice in private sector accounting. But in some countries, LGs use “fund accounting,” in which revenues and expenditures are recorded in different funds, each with its own balance sheet and operating statement; money can therefore be transferred from one fund to another. To find out more about fund accounting see the Accounting⁵ chapter in this series. Because borrowing internally is usually less expensive than borrowing externally, internal borrowing can save a LG money. Internal borrowing can also be easier and quicker because it involves fewer actors.

Not all inter-fund transfers are “borrowing,” some occur regularly as a matter of explicit policy. For example, if an enterprise activity such as the water utility is generating a surplus, the surplus may be transferred periodically to the LG's operating fund to subsidize other expenditures; there is no intention of repaying the money later. Similarly, a LG may shift money into an internal service fund to reflect the value of services provided by one LG department to another. Interfund “borrowing” occurs when money is transferred from a fund that has been accumulating money for a special purpose, such as capital investments, to another fund, and there is an intention to repay at a later date.

Repeated use of internal borrowing, however, can create a future liability that the LG may not have the resources to meet—which can in turn force a disruptive reduction in services or cause a shortage in the fund from which the money was borrowed. If, for example, money borrowed from a capital investment fund cannot be repaid, improvements may have to be delayed or forgone. If money is borrowed from a self-insurance fund, the LG jeopardizes its ability to absorb large losses from

liabilities. To determine whether your LG is relying on internal borrowing to balance the budget, see Indicator 14, Operating Deficits, and Indicator 16, Fund Balances.

SELLING ASSETS

Most LGs own property or facilities, such as vacant land or unused buildings, which would be valuable to private interests or possibly to an adjacent LG. Selling such assets can bring in one-time revenue. For example, a LG might sell its sewer system to an independent authority and use the proceeds for general operating expenditures. When one-time revenues are used for current operating expenditures instead of for one-time needs, they are sustaining an operating deficit. Aside from sustaining an operating deficit, selling an asset may harm the LG's long-run financial condition in the following ways:

- Flexibility in service delivery capacity may be reduced because the LG loses control of how service is provided.
- If it sells under the pressure of immediate revenue needs, the LG may accept a lower price than it would otherwise have received for the property.
- If the LG decides to re-acquire the asset, doing so may be more expensive at a future date.
- The sale of a utility (e.g. water, sewer, electric) or recreational facilities may make the LG dependent on someone else for prices and availability.

To determine whether your LG is relying on the sale of assets to balance its budget, see Indicator 5, One-time revenues, and Indicator 14, Operating deficits.

ONE-TIME ACCOUNTING CHANGES

Accounting methods can be manipulated to make a budget appear balanced. For example, if a payroll day falls on the last day of a fiscal year, the LG may be tempted to wait one day to record that expense, thus making expenses for the current year appear smaller. An end-of-year surplus could thereby be made to look larger or a deficit smaller (or nonexistent).

Three commonly used one-time accounting changes are (1) postponing current costs to future periods, (2) accruing revenues from a future fiscal year to the current fiscal year (to make the current revenues appear higher), and (3) extending the length of the fiscal year—for example, from twelve to thirteen months—so that revenues in the thirteenth month can be counted as revenues for the current year.

Many LGs that have had financial problems have relied on one-time accounting changes to balance their budgets, but these techniques do not solve underlying problems; they only disguise them. Credit rating firms and other analysts look unfavourably on such practices. Even if they do not violate the letter of accounting standards and laws, one-time accounting changes are considered unsound because they almost always violate the intent of these laws and standards.

PRACTICES THAT DEFER CURRENT COSTS

A LG is deferring current costs when it does not meet all its expenditure needs in the current budget. Two examples of the kinds of costs that can be postponed are contributions to employee pension funds and expenditures for the maintenance of capital plant. Deferring current costs has several general drawbacks:

- It sustains a level of services and expenditures that the LG may not be able to afford in the long run.
- It can affect a LG's bond rating. Credit rating organizations consider unfunded liabilities an unfavourable sign.
- Because these costs do not ordinarily show up on LG financial records, their effect may not be recognized until the problem is serious.

Two kinds of deferred costs will be considered here: deferred pension liabilities and deferred maintenance of capital assets.

DEFERRED PENSION LIABILITIES

A pension liability is a legal commitment a LG has made to pay benefits to its employees at some point in the future. There are two basic ways to fund this liability. The first way is "full funding," which means reserving money in a special fund as benefits are accrued. This "pay-as-you-go" method requires that current pension payments be made from the general fund as benefits become due.

Many LGs choose the "pay-as-you-use" method because it requires less spending from the current budget. This method is successful as long as the money is available when needed. The problem created by deferral, however, may be more serious than the problem it was intended to avoid, especially if accrued benefits increase rapidly while revenues remain stable or decline. As more employees become entitled to benefits, and as inflation increases the cost of benefits, pension costs can become a large fixed cost in the operating budget.

The analysis of unfunded pension liability is highly technical. Developing Indicator 22, Unfunded pension liability, can help you to determine whether and to what extent your LG is deferring pension liability.

DEFERRED MAINTENANCE EXPENDITURES

A LG's capital assets include its land, infrastructure (e.g. streets, bridges, street lights, traffic signals, sidewalks, etc.) buildings, utility networks, vehicles, and equipment. If these assets are not adequately maintained or if they are allowed to become obsolete, efficiency drops, maintenance and replacement costs go up, and the LG becomes a less attractive place to live and do business.

In times of financial strain, local officials often see deferred maintenance as a relatively painless, short-run way to reduce expenditures. Continued deferral, however, can create serious problems because of the huge sums of money invested in capital facilities. Following are some of the potential problems created by deferral:

- Safety hazards and other liability risks created, for example, by an unrepaired street.
- Decline in residential and business property values, which can lead to a decline in tax revenues.
- Loss of efficiency of equipment if; for example, an obsolete truck spends more time in the garage than on the street.
- An increase in the cost of repairing a capital asset (for instance, when street repair is postponed so long that the street has to be completely reconstructed).

To check on your LG's deferral of maintenance expenditures, see Indicator 25, Maintenance effort.

PRACTICES THAT IGNORE FULL-LIFE COSTS

A LG that fails to consider the long-range costs of a liability can jeopardize its financial condition by building a future imbalance between revenues and expenditures. Many communities do this by granting labour agreements without costing out non-salary benefits, or by arranging to construct or purchase a capital asset without calculating the full-life operating and maintenance costs.

NON-SALARY EMPLOYEE BENEFITS

Non-salary benefits include pension plans, health and life insurance, vacation, sick and holiday leave, deferred compensation, disability insurance, educational provisions, or other similar types of benefits. The cost of these benefits is difficult to assess because their value often varies from one employee or group of employees to another. Benefits depend on variables such as occupation and length of employment. Translating the costs into budget dollars requires a special analysis. But if non-salary benefits are not calculated, a LG may face the following problems:

- It may not be able to accurately budget enough money for benefit costs in the current budget.
- It may have trouble making long-range expenditure forecasts, and thus will be unable to anticipate and prepare for increases as they occur.
- It may find itself in a weak position in negotiating with labour unions; without good information on the exact cost of a proposal, it is difficult to judge competing proposals.
- It may not be able to predict the budget impact of increases or decreases in personnel.

CAPITAL ASSETS

A LG's capital assets are long-term investments with high initial costs. During the capital planning and budgeting process, local officials usually consider carefully how to finance assets. Often overlooked, however, are the long-range costs of owning and maintaining the asset—the “full-life costs.” These costs may be overlooked if capital and operating budgets are developed separately, and the operating costs of owning and using the asset are not planned for. These costs can also change over time. For example, the cost of using an older asset may be much less than the cost of using its replacement; the higher cost of the new asset might not be anticipated when the old asset is replaced.

Here are some disadvantages of not calculating total costs:

- The LG may not be able to budget accurately the operating costs of the asset.
- The LG may have incomplete information when choosing which capital asset to obtain. For example, since the cost of owning and maintaining a fleet of garbage trucks is high, it may be cheaper to contract for solid waste services.
- The LG may have trouble forecasting long-range expenditure needs.

INTERNET RESOURCES

Preparing an Economic and Strategic Vision for a City. Nigel Harris (1999).

In analyzing the implications of globalization and decentralization for city management, this presentation also attempts to answer the question: What do we need to know about trends and the city economy? Its main argument is that city managers have to need to know much more about the economic strengths and weaknesses of their city to make its economic management and the political consensus underlying policy increasingly better informed, more precisely targeted, and more effective.

<http://www.worldbank.org/wbi/urbancitymgt/toronto/assets/t-harris-mod02.ppt>

PART TWO—MANAGEMENT TOOLS

PURPOSE

Financial condition refers to the ability of a LG to pay its bills without going into debt and without sacrificing the level of public services needed for the health, safety, and welfare of its citizens. Financially healthy governments are systematic in anticipating and evaluating factors that could erode their financial health. And LGs with existing or emerging financial problems benefit from evaluation as a way to locate causes of trouble and to become increasingly alert to possible future problems. This workshop is to acquaint local officials with the benefits of a system for evaluating financial condition and an opportunity for skill practice in analyzing financial data and monitoring trends.

Don't forget to look back at the Learning Applications! Many of them can be easily adapted for group exercises and may be more appropriate for persons who are just being introduced to the concepts of evaluating financial condition.

CONTENTS

A brief description of each learning activity is shown below with an approximation of the amount of time required. If you wish to change the order, to omit something, or to add training material of your own, feel free to do so.

4.1 WARM-UP EXERCISE: TO YOUR FINANCIAL HEALTH!

Participants choose a category of financial health which seems to fit their respective LGs and discuss the rationale for their choice of categories. (45 minutes)

4.2 TRAINER PRESENTATION

Brief concept presentation based on the preceding essay that describes the importance of monitoring financial condition and the use of quantifiable indicators to measure trends that could influence financial condition. (30 minutes)

4.3 GUIDED DISCUSSION: ANALYZING INDICATORS

Participants learn to analyze trends that serve as indicators of financial condition and the relationship of these trends. (60 minutes)

4.4 EXERCISE: LEARNING TRANSFER

Participants reflect individually on what they have learned and make commitments to put it to use back home after the workshop. (30 -45 minutes)

4.1 WARM-UP EXERCISE: TO YOUR FINANCIAL HEALTH!

TIME REQUIRED

45 minutes

PURPOSE

This exercise is to help participants think about and decide which of three financial health conditions applies to their LGs.

PROCESS

Before the workshop begins, write on a chart pad sheet three statements (in large, readable letters), each describing a condition of financial health that might apply to a LG. The three statements are:

My LG is under the strain of a few identifiable financial problems and is in need of a broader perspective on these problems.

My LG senses that financial problems are emerging but is having difficulty pinpointing their origin or developing a strategy for coping with them.

My LG is in good financial condition but needs a systematic way to monitor changes and anticipate future problems.

Begin the exercise by explaining that few LGs face such severe financial problems that they are likely to default on loans or fail to meet current obligations. On the other hand, financial health is perishable. It can slip quickly away from a healthy LG that has become complacent or lacks the tools to spot the danger signs.

Continue your comments by saying that this workshop can benefit any LG that finds itself in any of the following situations. At this point, reveal the three statements on the chart pad sheet. Ask participants to read each of the three statements and to choose one of the three that most closely applies to their respective LGs. Also ask participants to be prepared to explain any events or conditions that led to their individual choices. Give participants several minutes to make their choices.

After a few minutes, ask participants to introduce themselves by name, title and organization. As they introduce themselves, ask participants to tell other participants which of the three statements they feel is closest to the situation of their LG and why.

4.2 TRAINER PRESENTATION

TIME REQUIRED

60 minutes

PURPOSE

This presentation is to provide participants with a concept and rationale for evaluating the financial condition of a LG. It is also to prepare participants for an exercise on how to use indicators to assess trends in financial performance.

PROCESS

Prepare the presentation based on information covered by the preceding essay on evaluating financial condition. Focus the general presentation on the meaning of financial condition. Give particular attention to the practice of financial trend monitoring as a useful way to compare a LG's financial condition with the vital factors that influence financial condition.

- Compares LG trends over time
- Also review briefly how to use indicators to:
- Examine trends in multi-year perspective (i.e., what direction? how fast? compared to what national trends?)
- Identify potential problems (i.e., existing; emerging)
- Breakdown problems into component parts (i.e., causes; solutions)

Outlined information on note cards may help you cover the information systematically and stay on schedule. Ask questions from time to time during the presentation as a check on participant comprehension and to hold their attention. Augment the presentation with visual aids including pre-printed newsprint sheets and overhead transparencies as a further aid to comprehension.

4.3 GUIDED DISCUSSION: ANALYZING INDICATORS

TIME REQUIRED

45 minutes

PURPOSE

Give participants experience analyzing financial trends based on key indicators and observing how these trends relate to one another.

PROCESS

Tell participants that the focus of the exercise is how to analyze financial trend indicators and to observe how these trends are related to one another. Explain that for local officials to be effective in evaluating the financial condition of their LGs, they must understand how to “read” trend indicators and to recognize the patterns created by the relationship among these trends. They also must be able to effectively communicate this information to elected officials in an easy-to-understand manner. Continue by telling participants that we will be spending a few minutes analyzing five trend indicators and then discussing what these indicators together reveal about the financial health of a hypothetical LG.

Handout six graphs which have been photocopied prior to the workshop (see the following pages). Explain that each of the first five graphs refers to a separate financial condition indicator and shows a trend line that describes the actual situation facing a LG. Explain that the LG in our example is small (population increasing from 17,000 to 20,000) with an annual budget of US 5 million in 1996 and increasing to US 6 million in 2006.

Trainers note: The effectiveness of this exercise can be enhanced greatly either by creating overhead transparencies (will require an overhead projector) from the six graphs to use during the discussion or by drawing facsimiles of the six graphs on sheets of chart pad paper.

Ask participants to look at the first graph: Indicator 19–Long-term debt as a percent of assessed valuation. Lead a discussion of the indicator using the following comments to focus the discussion.

Trainer’s Comment: Long-term debt is compared to assessed valuation because, for many communities, the property tax is the major source for repayment of debt. Therefore, assessed valuation becomes a measure of LG’s ability to repay.

In our example, we see that from 1996-2006 the amount of debt for the LG is relatively modest. Between 1996 and 1999, debt is approximately 2% of assessed valuation; then from 2000-2006 debt is ap-

proximately 4% of assessed valuation. The projection for 2007-2011 shows debt going to 5.5% of assessed valuation and is based on the assumption that this LG intends to borrow money to construct a new street.

How would local officials analyze this trend? The first thing is to look at benchmarks used by credit rating or other similar types of organizations.

One benchmark is that overall debt that exceeds 10% of assessed valuation is a potential sign of problem. In our example, the amounts of 2% and 4% are well within the limit.

Another benchmark is whether or not overall debt as a percent of assessed valuation exceeds 20% of the previous year. Looking at our example, in 1999 and in the projections for 2008, this benchmark is exceeded. However, the amounts are small. Therefore, the situation need not be viewed as serious.

In looking at this indicator, the important thing is knowing how much additional debt the jurisdiction is projecting in the next three to five years and what impact the debt will have on the budget. For example, can the LG afford the additional debt service and maintenance costs of new facilities.

Ask participants to look at the second graph: Indicator 17–Liquidity, which refers to the flow of cash in and out of a LG's treasury. Lead a discussion of the indicator using the following comments to focus the discussion.

Trainer's Note: Liquidity is an indicator that is seldom examined, but it should be for some good reasons. First, it is a good short-run indicator. That is, it points to a very immediate problem. Second, it is often the first sign of other problems. For example, if a LG is short of cash to pay current obligations, it may be necessary to borrow money on a short-term basis, and studies show that short-term borrowing is one of the early signs of a more serious underlying problem.

In the example, liquidity is steadily declining from roughly 200% in 1996 to 150% in 2006. If the drop continues, liquidity will be down to almost 100% in 2011. Liquidity of 200% means that a LG has roughly twice the cash on hand that it needs to meet its short-term commitments. As it moves to 100%, the LG has exactly what it needs to meet its payments but no surpluses to rely upon for unanticipated needs. If this ration drops to less than one-to-one (in our example to less than 100%) it is considered a negative factor. However, it could be offset if, for three consecutive years, there is a trend indicating that in the following year a one-to-one ratio will be exceeded.

In analyzing this indicator we can conclude that there is not yet a serious problem. However, local officials would be wise to watch their cash management procedures closely. They might want to assure that: 1) there is a good system for generating invoices for money owed to the LG, 2) money that is owed to the LG is collected promptly, 3)

shared-revenues and other inter-governmental payments are received promptly, 4) departmental needs are being anticipated in sufficient time to acquire the needed items, 5) projected revenues are matched routinely with projected expenditures.

Ask participants to look at the third graph: Indicator 14—Operating deficits which occur when revenues generated during the current year are not sufficient to cover expenditures generated during the year.. Lead a discussion of the indicator using the following comments to focus the discussion.

Trainer's Notes—Having an operating deficit is not the same as having a budget deficit. The budget may be balanced by such an action as using reserves funds, but an operating deficit still exists. While the use of reserves provides for a balanced budget, an operating deficit exists because current expenditures will exceed current revenues.

If a LG has a large fund balance and consciously chooses to draw it down for non-recurring expenses, then the existence of an operating deficit is not serious. However, frequent and increasing deficits can indicate that current revenues are not supporting current expenditures. When this happens, serious problems may lie ahead.

Looking at the graph, the LG had no operating deficits until 1999 at which time the deficit amounted to about 1% of total operating revenues. In 2000 and 2001, the operating budget was balanced, and then for 2002 there was a small surplus. In the subsequent years of 2004 and 2005 operating deficits again appear. A trend line for the years 2006-2011 show that, if the trend continues, operating deficits will continue to grow. So, on our graph, three of the last eight years resulted in an operating deficit, although a small one.

Turning again to the benchmarks, a current year operating deficit is considered a minor warning signal. An operating deficit is considered a negative factor under these conditions: 1) there is a current operating fund deficit greater than the previous year, and 2) there has been a current operating fund deficit in two or more of the last five years.

In our example, the LG violates each of these two benchmark criteria. However, the amounts are small.

In analyzing this indicator, local officials should ask themselves these questions: 1) Was the deficit anticipated during budget preparation? 2) Is the deficit being funded by borrowing from surpluses of other funds? 3) Can these other funds afford the loan without creating additional problems at a later date? 4) Was the deficit due to revenue shortfalls or was it due to expenditure overruns?

Ask participants to look at the fourth graph: Indicator 1—Revenues per capita. Lead a discussion of the indicator using the following comments to focus the discussion.

Trainer's Comment—In the example, revenues per capita run between \$4800 and \$6150. The per capita method is used to control for changes in population. To control for inflation, revenues are computed in constant figures.

In the example, revenues per capita are increasing, a probable sign of a healthy revenue base. However, this is not always true. Local officials may want to ask these additional questions:

- *Is the increase in revenues per capita a signal that costs will be increasing in future years? For example, new revenues may be due to an increase related to fees for new building construction. This increase may mean that expenditures will be increasing as the LG begins to service this new development.*
- *Is the increase in revenue per capita due to an increased tax burden? If this is true, are residents and businesses willing and able to pay?*

Ask participants to look at the fifth graph: Indicator 10—Expenditures per capita. Lead a discussion of the indicator using the following comments to focus the discussion.

Trainer's Comment—In the example, expenditures per capita range from \$4650 to \$6000 per capita. Expenditures per capita are increasing but are still exceeded by revenues per capita until 2009.

Local officials would still want to ask the following questions:

- *Is the increase due to the new services? If so, are there increased revenues to pay for these services?*
- *If the increase due to an increase in fixed costs, such as union contracts, debt service, or externally mandated services over which the LG has little control? Or is it due to increases in services which the LG can cut back at its own discretion?*
- *If the increase due to construction of capital facilities? If so, will the operating costs of the new facilities put additional strain on future years' budgets?*
- *If increases in per capita expenditures cannot be explained by the addition of new services, then, perhaps, is productivity or service efficiency declining?*

Ask participants to look at the sixth graph that is a composite analysis of the other five. Lead a discussion of the indicator using the following comments to focus the discussion.

Trainer's Comment—From an examination of the preceding five indicators we must conclude that no serious problems appear to exist.

However, we have yet to look at these indicators in relation to one another to determine if this might reveal any emerging problems.

Starting from the bottom of the graph we are reminded that operating deficits are small. However, we also see that they begin to occur in the same years that the gap between revenues per capita and expenditures per capita is narrowing.

(Remember, a LG can have an operating deficit even if total revenues exceed total expenditures. This is because operating deficits occur when current expenditures exceed current revenues. The revenues and expenditure lines on the composite refer to total revenues and total expenditures, including revenues such as prior year fund balances.)

As the gap between revenues and expenditures decreases, even higher operating deficits can be expected, and the trend line on the composite suggests that this may happen. (Operating deficits are going down in the trend line on the graph indicating a negative.)

Looking at liquidity, we see that is positive, but that it has been declining steadily. If we look back at operating deficits, we see there may be a relationship between the two, and we might come to the conclusion that the increase in the operating deficits has been reflected in declining liquidity. The LG may have used beginning balances or reserves to balance the budget and thereby reduced liquidity reserves.

As mentioned earlier, the projected trend for revenues and expenditures per capita shows that the gap between the two is narrowing. As we look to the future, it is evident that, if this trend continues, expenditures may actually exceed revenues in 2009. This may lead to the reconsideration of the growth and nature of LG expenditures. It may be necessary to think about long-term debt, which is the third line from the bottom. If LG is going to increase debt by 50% in 2008, it should consider the degree of strain this will place on the annual budget.

After completing the discussion of the five indicators and the composite, ask participants these questions to determine what they have learned from the discussion:

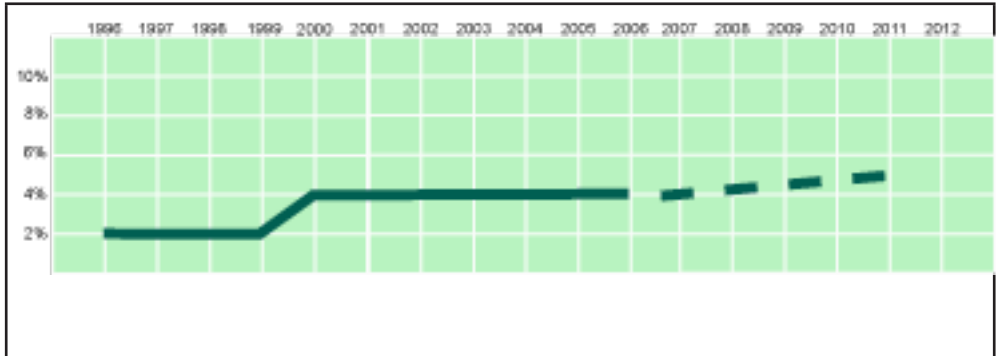
What might a local official learn from an analysis of individual indicators such as the five discussed? **Answer:** trends that point to existing financial problems or warn of problems in the future unless action is taken to reverse the trend.

What is the principal value of the composite indicators? **Answer:** When the performance of several indicators are viewed together, problems are sometimes discovered that would not be apparent when viewing one indicator at a time.

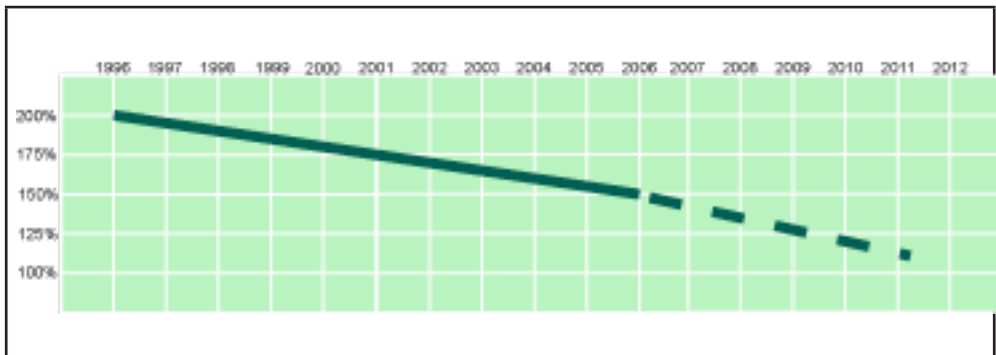
What action should be taken when the indicators disclose financial problems? **Answer:** Begin by searching for the cause of the problems. Then assess their significance or potential for harm. Finally, develop appropriate actions to resolve them.

Remind participants, to close, that financial trend monitoring is not meant to produce concrete answers. It is a tool that can be used to put financial issues and factors into their proper perspective.

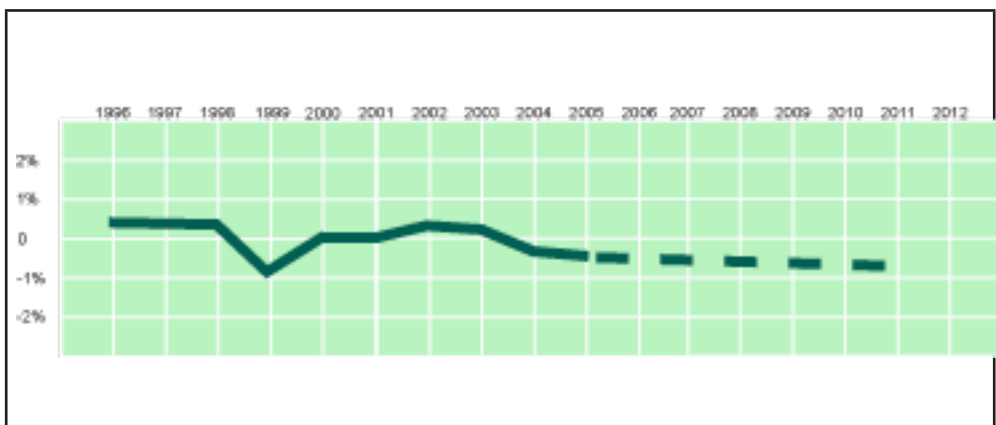
GRAPH 1: INDICATOR 19—LONG-TERM DEBT AS A PERCENT OF ASSESSED VALUATION



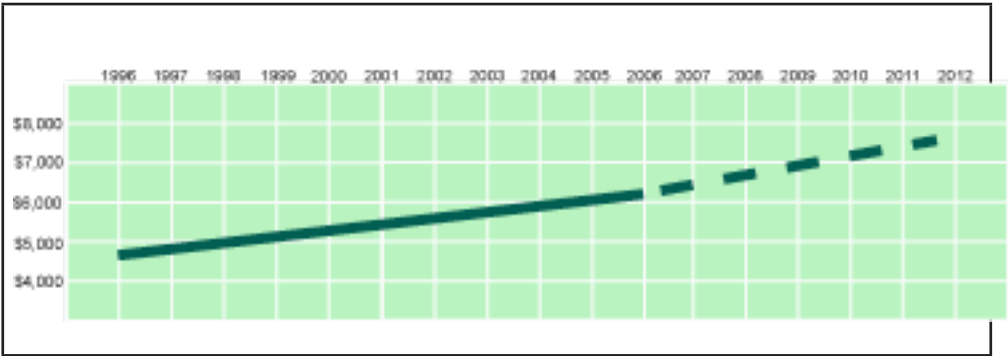
GRAPH 2: INDICATOR 17—LIQUIDITY



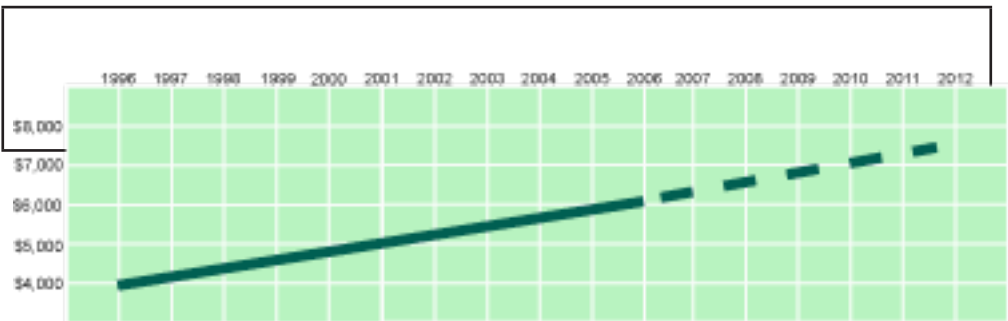
GRAPH 3: INDICATOR 14—OPERATING DEFICITS



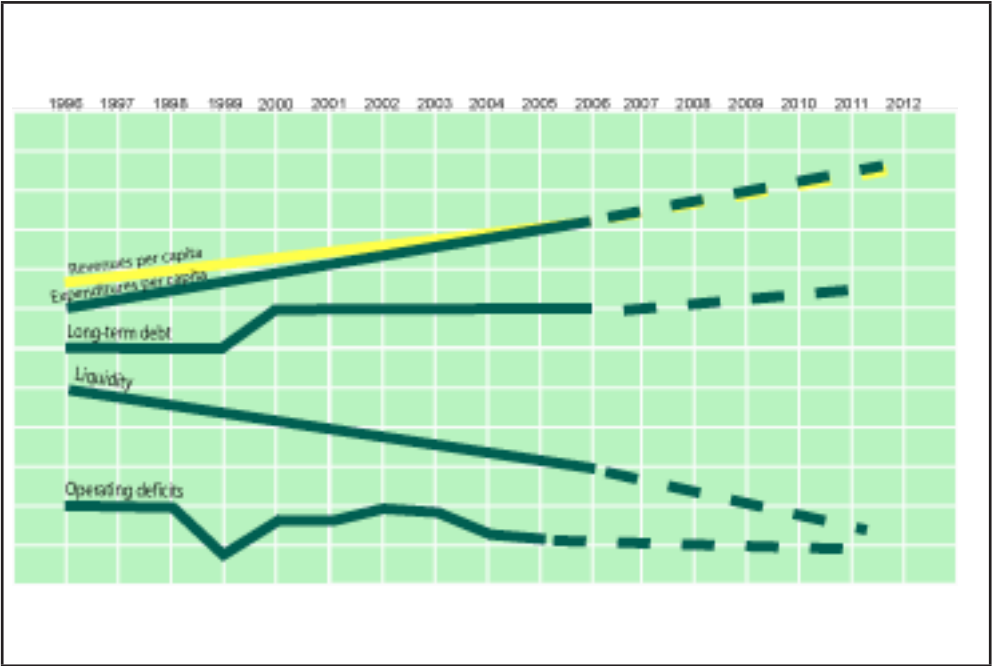
GRAPH 4: INDICATOR 1—REVENUES PER CAPITA



GRAPH 5 INDICATOR 10—EXPENDITURES PER CAPITA



GRAPH 6: COMPOSITE



4.4 CLOSING EXERCISE: LEARNING TRANSFER

TIME REQUIRED

30-45 minutes

PURPOSE

This exercise is to help participants transfer the learning experiences of the workshop into their real-world activities as finance directors. The focus of this exercise is on raising expectations, engaging in realistic planning and making personal commitments. Most of the work is done on a personal basis with some interpersonal sharing.

PROCESS

Spend at least half an hour at the end of the workshop to focus the attention of participants on important learnings and encourage them to continue experimenting with these learnings in their management activities. Begin by giving participants about fifteen minutes to work independently on a simple learning transfer questionnaire.

When participants have completed the questionnaire, ask them to share quickly with the group two or three things they intend to do differently in their roles with respect to evaluating financial condition to close the workshop.

Trainers note. It is generally agreed that the purpose of training is to improve the way people do things by showing them a better way. In fact, the success of a training experience can be measured by the amount of personal growth and change that takes place both during training and after the training is over.

Commitments to learning and change made at the close of a workshop can help participants overcome learning resistance in themselves and in the work environment. A trainer can help learners make a successful transition from the world of learning to the world of doing through a few simple planning exercises.

A LEARNING TRANSFER QUESTIONNAIRE

Take a few minutes to reflect on evaluating financial condition, the new ideas you encountered in this workshop, and how you feel about them. Then, in the space below, write a sentence or two to describe something interesting you have learned about yourself during this workshop.

Based on what you have learned about yourself and the many possibilities for change presented by this workshop, what two or three things do you intend to do differently that involves evaluating the financial condition of your LG?

Finally, what obstacles in yourself or in your work environment do you expect to experience during your efforts to implement these changes? What will you do to remove or minimize these obstacles?

Obstacle	Overcome obstacle
1. _____ _____	1. _____ _____
2. _____ _____	2. _____ _____
3. _____ _____	3. _____ _____

