

Fact Sheets on Fiscal Decentralisation in the Western Balkans*

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Fiscal Decentralisation in Albania

Legal Basis: Law on Organisation and Functioning of Local Governments, July 2000

Local Government Financing

The scope of local government discretion in financial matters has increased significantly during the last few years. The major changes include the introduction of an unconditional transfer in 2001, which has increased every year by substituting former conditional transfers, and has been based on a distribution formula since 2002. This has had an equalisation impact since the local tax reform implemented in 2003. Local budget expenditures reached 23 per cent of public expenditure in 2003, with the prospect of further increases. Recent reforms have greatly increased local discretion and transparency. The contribution of earmarked grants to local budget revenue has been reduced from 85 per cent in 1998 to 20 per cent, replaced by a combination of unconditional grants, local taxes and revenue shares over which local governments have full spending discretion. Unconditional grants and revenue shares are distributed by transparent formulae. Government ministries still exercise considerable discretion over the funding of the delegated services, education, healthcare, social welfare and public order, and the distribution of grants for capital investment.

Locally Derived Revenue

According to the Law on Organisation and Functioning of Local Governments (July 2000), communes and municipalities are authorized to derive revenues from

- a. *local taxes and levies* (such as on movable and immovable property, or the economic activity of small businesses)
- b. *local fees* (such as for public services offered by them, or the issuance of licenses, permits, authorizations and issuance of other documentation, at the discretion of local government),

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- c. *borrowing*: communes and municipalities shall be authorized to borrow funds for public purposes in a manner that is consistent with the conditions established by law
- d. *all revenues generated from their economic activities*: rents and sale of property and from donations, interest income and penalties.

Revenue Derived from National Sources

Communes and municipalities are entitled to receive funds from national sources, including:

- a. *Shared taxes*, consisting of a portion of certain central government taxes, such as the personal income tax and the company profit tax. These taxes shall be collected and distributed to communes and municipalities by the central government on a regular basis not less than three times a year during the fiscal year.
- b. *Unconditional transfers* from the central government to commune and municipality governments based on the ratio of exclusive and shared functions performed by the local governments and for the purpose of achieving equalization of resources among local governments.
- c. *Conditional transfers* from the central government. Among conditional transfers, so-called “pass-through” transfers are as high as half the total local government revenues. These transfers are for the payment of wages in pre-university education and primary health sectors, and for the payment of social benefits to poor households. However, for national accounts, they are ascribed to the respective ministry budgets. This means that the payment of these wages by local governments is a pure agency function.

The following table¹ summarises the situation of local government finances in Albania in recent years (in millions of leks).

	2000	2001	2002	2003
Total local expenditures (TLE)	32,846	38,177	40,724	46,654
Total local expenditures (per cent GDP)	6.19	6.25	6.01	6.24
Total local government current revenues without conditional pass-through transfers and earmarked grants	10,199	12,289	15,834	19,425
Conditional pass-through transfers (per cent TLE)	59.6	61.0	56.1	49.7
Earmarked grants (per cent TLE)	31.1	11.8	7.6	9.6
General purpose grant (per cent TLE)	0.0	18.0	25.7	17.0
Own taxes (rates set by LG) (per cent TLE)	2.5	3.2	3.0	12.2
Shared taxes (per cent TLE)	0.1	0.1	0.1	5.6
User charges and fees (per cent TLE)	2.7	3.1	3.9	2.6
Other revenues (per cent TLE)	4.0	2.8	3.6	3.3

Source: Based on data provided by A. Hoxha (with J.H. Pigey), *Fiscal decentralisation in SEE countries. Case of Albania*, Stability Pact Conference, September 2004.

Local Government Functions and Competences

The Law distinguishes exclusive functions (art.10), shared functions (art.11) and delegated functions (art.12), and for each category gives a definition and a list of matters

¹ Source : Gérard MARCOU “The State of Local and Regional Democracy in South-Eastern Europe”, published in *Proceedings of the South-Eastern Europe Regional Ministerial Conference [Effective Democratic Governance at Local and Regional Level](#)* (Budapest: LGI/OSI, 2005), p.56.



Exclusive Functions of Communes and Municipalities: The commune and municipality have full administrative, service, investment and regulatory powers for their exclusive functions. However, the central government may issue national standards in relation to exclusive functions for the sole purpose of achieving a clear and specific national interest, provided that the national standard does not limit local governments' discretion in areas of clear local interest. Exclusive functions include: (1) infrastructure and public services; (2) social cultural and recreational functions; (3) local economic development; and (4) civil security.

Shared Functions of Communes and Municipalities: Communes and municipalities may undertake any of the shared functions separately or jointly with then central government. To the extent that the central government requires a local government to perform any shared function or meet a national standard in the performance of a shared function the central government shall provide financial support of the requirement. Communes and municipalities may undertake any of the following shared functions: (1) pre school and pre university education; (2) priority health service and protection of public health; (3) social assistance and poverty alleviation and ensuring of the functioning of relevant institutions; (4) public order and civil protection; (5) environmental protection; (6) other shared functions as described by law.

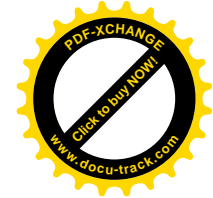
Delegated Functions of Communes and Municipalities: The central government institutions, when allowed by law, may authorize the commune, municipality or region to undertake a function under their [central government institution] jurisdiction. The Local Government units may be authorized to undertake other functions or competencies of the central government which are non-mandatory [optional]. This should be done solely by an agreement between the central government representative and the local government unit. In any case, the central government guarantees necessary financial support to the local government units to exercise delegated functions and powers.

Fiscal Decentralisation in Bosnia and Herzegovina

Legal Basis:

The basis and organization of the system of local self-government in Bosnia and Herzegovina is regulated by the Constitutions of the Entities and their laws. In an attempt to simplify local governance, new laws were drafted at the Entity level in late 2004. Until these are passed, local government is overseen in Republika Srpska (RS) at the Entity level, whereas in the Federation of Bosnia and Herzegovina (FBiH) H a general framework law left cantons to define the specific competencies (and funding) at the municipal level. Both entities outline general principles of local self-government in their constitutions. In March 2005, a new Federation draft Law on the Principles of Local Self-Government began its journey through the Federation's Parliament but has not yet been adopted. In RS, a new Law on Local Self-Government has entered in force, but implementation is at an early stage.

Local Government Financing



In BiH the funding of local governments is not done through government transfers, it is done through sharing tax revenues in set percentages. Firstly, the VAT, excise tax and customs are collected at BiH level and are used for 1) the BiH State budget, 2) foreign debt repayment, and the residual (quite significant) is shared between RS, FBiH and Brcko District in accordance with a formula.

Further, according to a report published by the Support for Improvement in Governance and Management Programme (SIGMA), "all other tax powers rest with the Entities. The FBiH and the RS have two distinct tax and finance systems.

Both Entities contribute to financing the State-level on the basis of 2/3 from the FBiH, and 1/3 from the RS. In both Entities, the tax administration is centralised; lower government levels have very limited taxing powers. However, FBiH tax revenue goes mainly to the Cantons; a mechanism to transfer resources from richer to poorer Cantons is not foreseen.

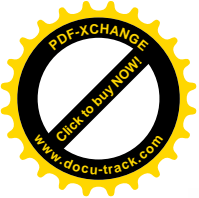
In the FBiH, Cantons legislate on a few cantonal taxes and municipal taxes (property tax, property transfer tax, some fees), and on tax-sharing with their respective municipalities. However, Cantons have control over neither rates nor bases of the most important taxes (sales tax, personal income taxes, profit tax), which are subject to Federal legislation. In the FBiH, the tax sharing between Cantons and Municipalities is based on the following taxes (average sharing rates between brackets: canton/municipalities): payroll tax (place of work: 80/20), citizen income tax (place of residence: 20/80), sales tax (on turnover: 70- 80/30- 20), property tax (20/80), property transfer tax (20/80), road tax (motor vehicles: 55/45). Cantons have the power to regulate the two property taxes and partly the citizen income tax.

The tax sharing between RS and its municipalities is based on the following taxes (sharing rates between brackets: Republic/municipalities): payroll tax (74/26), citizen income tax (74/26), sales tax (74/26), property tax (0/100), property transfer tax (0/100). According to the new RS *Local Government Act* (Art.68), city resources are derived from taxes, duties and fees assigned by the law to municipalities. A city receives 45% of the total revenue obtained by its component Municipalities. In the case of a city containing only one municipality (at present this concerns uniquely the City of Banja Luka) the city receives only 35% of this revenue."²

The distribution of expenditure across all levels of government in BiH shows that the level of Cantons and RS are most important. As can be seen from the following table³, the share of expenditure by municipalities is relatively low by comparison to that of the Entities themselves and, in the FBiH, of Cantons.

² Support for Improvement in Governance and Management Programme (SIGMA), [Assessment Report: Bosnia and Herzegovina - Decentralisation Process](#) (SIGMA, 2004), p.5.

³ SIGMA, [Assessment Report: Bosnia and Herzegovina - Decentralisation Process](#) (SIGMA, 2004), p. 4.



<i>Government levels</i>	<i>FBiH (in %)</i>	<i>RS (in %)</i>
Entity level	25.2	60.4
Cantons	34.2	--
Municipalities	7.9	8.0
Public funds (pensions, unemployment ins. health ins.,)	32.6	31.6
TOTAL	100	100

(Source: World Bank, "Bosnia and Herzegovina: creating an efficient decentralized fiscal system", June 2003).

More up to date information follows: in Republika Srpska, in 2004, transfers from the entity government to municipalities were: 2 mIn KM (1 mil euro), or 0,20 % of RS budget for 2006, (or 0,01% of GDP). Other, non- budget funds are 122.4 mIn KM (61 mil euro). In total, Entity transfers are transfers 124.4 mIn KM (62 mil euro). In Federation BiH, inter- budgetary transfers from the Federal budget totalled KM 23.9 million (12 mil euro) in 2004, of which KM 12.4 (6.2 mil euro) was to cantons and municipalities. It should be noted that local governments have a different set of competencies in two Entities, which has an obvious impact on their revenues. Furthermore, the low level of inter- budgetary transfers reflects the reliance placed on revenue assignment and sharing arrangements for financing the expenditure programmes of both federal and sub- entity governments.

Local Government Functions and Competences

According to a USAID Local Governance Assessment, "the distribution of functions, and the administrative autonomy necessary, is not adjusted to the capabilities of the municipalities, and does not reflect true demand for services imposed by the population. Municipalities cannot adequately fund mandatory services from shared and own- source revenues, cannot reject delegated tasks from the entity or the canton, nor can they decide upon the most efficient and accountable form of delivering their services. Entity local government laws, as well as cantonal local government laws, were not designed taking into account which services could be optimally performed at each level of public administration, and the funding necessary for an optimal, or even for the current construct, is clearly inadequate, and beyond the control of the municipal level

The number of delegated functions varies canton by canton, as do the sharing formulae and the tax bases. In neither entity is there an explicitly logical connection between the cost of mandated and delegated tasks, the sharing formulae, and the use and availability of local taxes and non- tax revenues."⁴

According to the SIGMA report, "in both Entities, municipalities are only in charge of assigned responsibilities; there is no general competence of local self- government for local affairs. Responsibilities of municipalities include child care, primary and secondary school

⁴ USAID, [Local Governance Assessment and Policy Recommendations](#) (USAID, 2003), p. 7- 8.



buildings, employment agencies, social care, culture, sports; housing and urban planning; municipal utilities (sanitation, sewage treatment, water supply) usually performed by own enterprises; public order; tourism; management of municipal properties.

However, in a number of Cantons of the FBiH other tasks are assigned or devolved to municipalities: local roads, health care supplies; ambulance services. In several Cantons social welfare functions are left under-funded by the authorities of the Canton, shifting the burden onto municipalities in charge of the execution of these functions, on the assumption that those municipalities could raise resources to fill the gap. It is also usual that capital spending is left to municipalities.

In the new *Local Government Law* of the RS, the following tasks are added: health care, general and detailed land use planning; local roads and streets; regulating construction and business premises; other tasks as determined by laws and the statute of the municipality – this provision could authorize the municipality to extend its activities, provided that it would not infringe on the competence of other authorities. However a specific difficulty in the RS is the number of very small municipalities. The new *Local Government Law* provides that municipalities with under 1,000 inhabitants need not form an administration; the RS Government will designate a neighbouring municipality to discharge its administrative tasks (Art.28).⁵

Fiscal Decentralisation in Kosovo

Legal Basis: UNMIK Regulation No. 2000/45, On Self-Government of Municipalities in Kosovo, August 2000
UNMIK Regulation No. 2001/09, Constitutional Framework for Provisional Self-Government, May 2000

Local Government Financing:

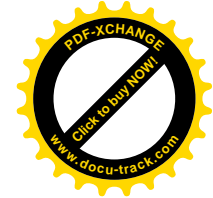
Kosovo municipalities have two sources of finance available to them: own-source revenues and intergovernmental transfers. Municipalities are mainly funded through transfers from the Central Authority and are thus very much dependent on intergovernmental transfers from the Kosovo Consolidated Budget. Generally, the own-source revenues they are able to raise are not sufficient to meet their needs. The legal basis for the financial resources for municipalities is UNMIK regulation 2000/45, which provides that municipalities are responsible for preparing balanced, transparent budgets, preparing and executing a budget plan.

Locally Derived Revenue

According to Section 39 of Regulation 2000/45, municipalities are authorized to collect own-source revenues in the form of

- a. Licenses and fees assessed and levied by the municipality;

⁵ SIGMA, [Assessment Report: Bosnia and Herzegovina - Decentralisation Process](#) (SIGMA, 2004), p. 4.



- b. Income from municipal assets; and
- c. Fines or a proportion of fines.

Revenue Derived from the Central Authority

According to Section 38 of Regulation 2000/45, municipalities are also entitled to funding from the Central Authority. Such intergovernmental transfers must be calculated on an objective basis (e.g., on population size, number of students, number of health workers, etc) and include an assessment of the financial needs and resources of each municipality and the spending priorities established by the Central Authority. A portion of the transfer is unconditional with the balance being conditional, that is, with spending designated for specific activities. The Central Authority is supposed to notify municipalities in advance of the forthcoming fiscal year as to the amount of the planned transfers.

The Working Group on Local Government's Framework for the Reform of Local Self-Government in Kosovo

In 2004, the Working Group on Local Government, chaired by UNMIK and the PISG, developed a *Framework for the Reform of Local Self-Government in Kosovo*, which was endorsed by the government. With regard to local government financing, the Framework "recommends the adoption, as soon as possible, of a comprehensive law on Local Government Finance. The new Law should be prepared if possible concurrently with the Law on Local Self-Government or as soon as possible thereafter. It should contain or be based on the following principles:

- Municipalities should have the authority to manage their own budgets;
- All municipal services should be financed through municipal budgets which include own source revenues, central to local budgetary transfers, and extra budgetary funds;
- The authority to set rates and exemptions for local taxes, fees, tariffs and fines should be guaranteed as a municipal prerogative although central authorities may set allowable rate ranges;
- Criteria that determine allocation of grants to municipalities should be set by law;
- Municipal grant calculations should include measures to mitigate disparities among municipalities;
- A mandatory and consistent format for municipal budgets should be set by law;
- Municipalities should have the right to borrow in internal and external capital markets in conformity with the law on Public Financial Management and Accountability;
- Ensure that there is regular and structured consultation between local and central government on municipal finance issues; legislation should designate a forum in which local government representatives and central ministries will meet expressly to discuss these issues."⁶

Local Government Functions and Competences:

⁶ Working Group on Local Government, [*Framework for the Reform of Local Self-Government in Kosovo*](#) (UNMIK, 2004).



Concerning the functions and competences of the different levels of government, the USAID Assessment concluded that “because the roles and responsibilities and relationships between municipalities and other governmental and international authorities – UNMIK, central government ministries and agencies – are not clearly defined in law, regulations, policy or practices, municipal officials do not fully understand the scope of their roles, responsibilities and competences. [In addition] many of the responsibilities that municipalities would normally exercise are in the hands of UNMIK, which is responsible for exercising powers reserved to it, and supervising and monitoring municipal activities and decisions. UNMIK currently retains the authority to approve all expenditures and can overrule any local assembly decision ... This shared and inadequately- defined responsibility creates numerous conflicts and ambiguities.”⁷

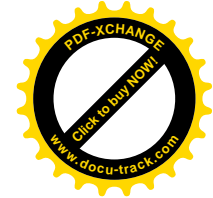
According to the UNMIK regulation 2000/45 (section 3.1) the “*responsibilities and powers of the municipalities*” are as follows:

- a. Providing basic local conditions for sustainable economic development;
- b. Urban and rural planning and land use;
- c. Licensing of building and other development;
- d. Local environmental protection;
- e. The implementation of building regulations and building control standards;
- f. Service provision in relation to local public utilities and infrastructure including water supply, sewers and drains, sewage treatment, waste management, local roads, local transport and local heating schemes;
- g. Public services including fire and emergency services;
- h. Management of municipal property;
- i. Pre- primary, primary and secondary education;
- j. Primary health care;
- k. Social services and housing;
- l. Consumer protection and public health;
- m. Licensing of services and facilities, including entertainment, food, markets, street vendors, local public transport and taxis, hunting and fishing and restaurants and hotels;
- n. Fairs and markets;
- o. Naming and renaming of roads, streets and other public places;
- p. The provision and maintenance of public parks and open spaces and cemeteries; and
- q. Such other activities as are necessary for the proper administration of the municipality and which are not assigned elsewhere by law.

Additionally, Section 3.2 identifies other matters with regard to which municipalities may take action within their territories, including:

- a. Tourism;
- b. Cultural activities;
- c. Sports and leisure;
- d. Youth activities;

⁷ Local Government Assessment Team, [Limited Scope Assessment of Local Governance in Kosovo](#) (USAID, 2003), p. 8, p. 10.



- e. Economic promotion; and
- f. Civic promotion.

In terms of local government functions and competences, *the Framework for the Reform of Local Self-Government in Kosovo* proposes a distinction between *own competences* and *delegated competences*, as follows:

Own competences are divided into “regulatory competences” (art. 2.1) and “other own responsibilities” (art. 2.2). Municipalities may adopt regulations in the following areas

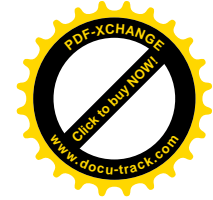
- a. spatial plans for urban and rural areas, as regards i.e. housing, roads, etc.
- b. rates and conditions of access for the use of municipal services and facilities
- c. local tax rates, the manner of their collection and persons and entities obliged to pay these taxes
- d. maintenance of public order and use of public spaces
- e. functioning of the organs of the municipality

For “other own responsibilities”, a fairly long list is proposed which includes, among others, the competence to

- a. determine local economic development priorities;
- b. collect local taxes as determined by applicable law;
- c. identify features of natural, historic and environmental interest on their territory, ensure their protection and try to obtain funding including from international sources;
- d. establish and operate facilities for the social welfare of the people including orphanages, homes for single mothers and the elderly and disabled, shelters for the homeless, childcare facilities;
- e. establish and operate public utilities in particular with respect to drinking water, sewage, canalisation, water treatment, drainage, waste collection and disposal, and heating;
- f. build and maintain buildings for pre- primary, primary and secondary education, provide nursery education and employ the teaching and technical staff of schools including the director, the latter being selected by the Municipal Assembly from a shortlist provided by the Ministry of Education, Science and Technology;
- g. establish and operate public areas such as parks, green areas and recreational spaces, playgrounds, public parking areas;
- h. establish and operate primary and, in the framework of inter- municipal co- operation, also secondary health care facilities and promote health education;
- i. carry out any other public tasks of a local nature not assigned by law to other public bodies.

The *Framework* identifies the following areas as *delegated competences* (which are to be carried out provided that commensurate resources are made available to the municipality):

- a. civil registration and providing civil documents;
- b. business registration;
- c. granting business licenses;
- d. providing social assistance payments to the inhabitants of the municipality;
- e. allocating financial means to schools and supervising their spending;
- f. controlling standards of construction;



- g. taking measures for the protection of water, soil, air and other resources against pollution;
- h. managing the forests situated on the municipal territory within the authority delegated by the central authority, including the granting of licenses for the felling of trees on the basis of rules adopted by the Government;
- i. granting other licenses for the use of natural resources such as quarries;
- j. other tasks delegated by the central authorities

Fiscal Decentralisation in Macedonia

Legal Basis: Law on Local Self- Government, January 2002
Law on Financing of the Units of Local Self- Government, July 2004

Local Government Financing

As the relevant legislation was only passed in 2004, and is being implemented gradually, information on the (new) system of local government financing is not yet fully available. The Law on Local Self- Government and the Local Government Finance Law identify local government responsibilities and the means to fund these. However, at the time of the preparation of the 2005 budget, complete identification of movement of resources for devolved activities to the local level has not been completed, thus transferred amounts are not shown here. Municipalities are financed by their own sources of revenues, by grants from the national budget, loans and other funds.

Locally Derived Revenue

According to the Law on Financing of Units of Local Self- Government, municipalities are authorized to derive revenues from

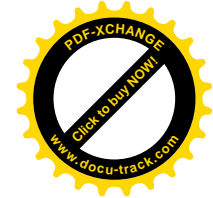
- a. *local taxes* (such as property tax, or tax on inheritances and gifts)
- b. *local fees* (such as utilities fees, or administrative fees)
- c. *local charges* (such as charges for urbanization of construction land or charges for communal activities)
- d. *ownership* (such as revenues from leasing or from interests)
- e. *other sources, such as donations, fines, self- contribution, other revenues established in accordance with law.*

Revenue from Income Taxes

Additionally, the municipalities collect a portion of the personal income taxes in the amount of a) 3% of the personal income tax from salaries of persons who reside and permanently live in that municipality and b) 100% of the personal income tax from persons who are performing a "craft activity".

Revenue Derived from National Sources

Grants from the Budget of the Republic of Macedonia provide additional revenues for the municipalities for financing their competencies. These grants are allocated as follows:



- a. *Revenues from the value added tax.* These to be used by municipalities for the financing of their activities but within this framework municipalities can autonomously decide how to use the revenues from the VAT. Three percent of the total value added tax income of the previous fiscal year should be divided in proportion to the total number of inhabitants and in accordance with other criteria regulated by decree.
- a. *Earmarked grant.* These are to be used for financing a specific activity. The Line Ministries and the Funds shall propose to the Ministry of Finance the distribution of the earmarked grants per Municipality, project, institution and/or program with a budget calculation for the following budget year and shall monitor the execution of the earmarked grant.
- b. *Capital grant.* The capital grant is allocated for financing investment projects, on the basis of a programme approved by the Government. The municipalities need to draft quality projects - complete with a comprehensive financial breakdown of project activities - for capital investments that exceed the financial capabilities of the municipality.
- c. *Block grant.* These are to be used for financing specific local government responsibilities (culture, social welfare and child protection, primary and secondary education and primary healthcare) through concrete programs. The criteria for distribution of block grants are to be formula-based and using appropriate need indicators for each program.
- d. *Grant for delegated competency.* These grants are to be used for financing a delegated competency from a body of Mayor's state management. The Minister who manages the state administration body and the Mayor of the municipality shall conclude an agreement for regulation of mutual relations regarding the grant for delegated competency.

Local Government Functions and Competences

In 2004 a number of legal acts were prepared and enacted to delegate competencies to the local governments. Some of the delegation involves a phased approach, such as in the case of the devolution of primary and secondary education, child care and part of the activities in the area of culture. Some involve the shifting of administrative functions and responsibilities as soon as decentralization acts become effective. According to the Law, municipalities, within the legal framework, and in accordance with the principle of subsidiarity, have the right to perform activities of local importance that are not excluded from their competency or are not under the competency of the organs of the state administration (art. 20). Municipalities shall independently regulate and perform these activities, and are responsible for their performance (art. 21).

Municipal competencies include the following (art. 22):

- a. *Urban and rural planning*
- b. *Protection of the environment, nature and space regulation*
- c. *Local economic development*
- d. *Communal activities* (i.e. water supply; regulation and organization of public local transportation of passengers reconstruction)
- e. *Culture*
- f. *Sport and recreation*



- g. *Social welfare and child protection* (i.e. kindergartens and homes for the elderly; exercising of social care for disabled persons, children without parents and parental care, children with educational and social problems, etc)
- h. *Education* (i.e. establishing, and financing, and administering of primary and secondary schools, in cooperation with the central government)
- i. *Healthcare* (i.e. health improvement; preventive activities; protection of health of workers and protection at work)
- j. Execution of preparations and undertaking of activities for *protection and rescuing* of citizens and goods at their territory against war destructions, natural and other disasters as well as against the consequences caused by them in the state of war
- k. *Firefighting* activities performed by the territorial firefighting brigades.

The Law also refers to *delegated competencies*. In these cases a public administration body may delegate the execution of certain tasks from its competency to the mayor, in accordance with law. In these cases the funds from the budget of the Republic of Macedonia anticipated for the performance of these tasks shall also be transferred. The way of performing these tasks may be adjusted to local conditions, respecting the standards determined by law.

Fiscal Decentralisation in Serbia and Montenegro

Legal Basis: Law on Local Self Government, February 2002 (Serbia)
Law on Public Revenues and Expenditures, 2001 (Serbia)
Law on Local Government, 1995 (Montenegro)

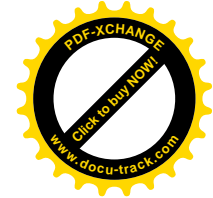
Local Government Financing

Serbia: Local governments are financed by own revenues, shared revenues and transfers from the Republic of Serbia government.

Own revenues of local units

According to the UNDP Assessment of Fiscal Decentralisation in Serbia, "starting in 2001, local units were given the right to introduce many new forms of their own revenues. They include tax and non- tax revenues, and are follows:

- a. *fees*: administrative fees, local communal fees, tourism fees,
- b. *charges* for: using building plots, arranging building plots, protection and improvement of the environment,
- c. *revenues* from: renting and using republic property used by the local unit, the sale of republic movable property used by the local unit, the concession charge for communal services and revenues from other concession jobs concluded by the local unit, the interest on local- unit funds saved in the banks,
- d. fines,
- e. revenues from the activities of the local unit authorities,
- f. self contribution fee
- g. donations,



h. other local revenues ...

Shared revenues

Formally, the system of shared revenues exists only in relations between the republic and local units, because shares of PIT and CIT allocated to the autonomous province are considered as general grants. All revenue shared between the republic and local units come from taxes introduced by the republic. These include several tax instruments (property tax, tax on the transfer of property rights, inheritance and gift tax), which are fully allocated to local budgets. Also, local units were given the authority to collect these latter revenues. Other shared revenues include several charges for using public resources. These are the following:

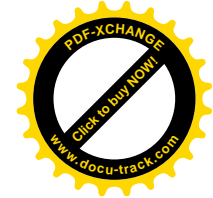
- a. charge for using mineral springs;
- b. charge for water exploitation;
- c. charge for exploitation of the forests;
- d. charge for reclassification of agricultural land;
- e. charge for building, maintenance, and using local roads;
- f. charge for environmental exploitation;
- g. concessions.

These revenues are allocated to municipalities and cities in certain percentages. Only funds collected from the charges for building and maintenance, use of local roads and environmental exploitation belong to the local budgets in total ...

Intergovernmental transfers

Each year the republic transfers a fixed amount of revenues from its budget to budgets of local units and to the budget of the autonomous province. Local units get these funds according to the rules stipulated in the annual law on the distribution of transferred funds from the budget of the republic and sharing the tax on salaries with municipalities, cities and the city of Belgrade (starting in 2005). Transfer of funds from the budget of the republic to the autonomous province of Vojvodina is based on the norms stipulated in the law on the annual budget of the Republic of Serbia. Until 2005, the major form of transfer from the republic to the local level and the largest revenue source for the local budgets was the retail sales tax ... The retail sales tax was abolished on 31 December 2004 and from 1 January 2005 the VAT has been implemented in its place in the fiscal system of Serbia. Because revenues collected from VAT cannot be shared on the derivation basis, it was necessary to find another source for transferring funds to local units. As a consequence of abolishing the retail sales tax, local units are now financed with a larger share of PIT (40 per cent compared with 5 per cent till 1 July 2004 and 30 per cent in the period of 1 July 2004 till 31 December 2004) and with a general revenue grant from the budget of the republic. General grants are distributed with certain criteria that were formerly used for sharing the retail sales tax. These criteria are as follows:

- a. area of the municipality or city's territory;
- b. number of inhabitants;
- c. number of classes and number of primary and secondary schools;
- d. number of children in social care and number of social care buildings;
- e. position of the environment in the municipality or city;



f. level of development.”⁸

The following table⁹ indicates the share of expenditures by level of government:

	2003	2004	2005
S&M Union	23.02	16.25	12.65
Republic (Net of Transfer)	51.79	61.98	64.97
Vojvodina	7.55	4.80	5.01
Local units	17.64	16.97	17.36
Total Government (excluding social funds)	100.00	100.00	100.00

Source: Ministry of finance of the Republic of Serbia and Budget Laws of the Republic of Serbia for 2003, 2004 and 2005

Montenegro: According to a report published by the Support for Improvement in Governance and Management Programme (SIGMA), “less information is available on Montenegro. A reform of local finance is pending. The present system is regulated by the Law on Local Government of 1995 and the Government Revenues Act of 1996. The basic structure of the present system is close to the Serbian model. Own revenues result from a number of taxes, fees and property revenues: a communal tax, a local administrative tax, self-imposed contributions, compensations for the use of municipal property, fees.

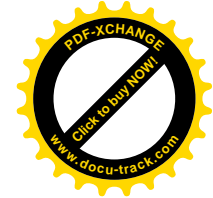
Own revenues are in excess of 43% of total revenues (data of 1998). Municipalities receive shares of the following taxes controlled by the state: property tax (50%), property transfer tax, residence tax, inheritance duties and gift tax, personal income tax (15% of the local yield). Other revenues ceded to municipalities are: revenues collected out of compensations for construction, maintenance and use of local roads and other objects of public importance, revenues from interests collected on bank deposits. Altogether these revenues amount to 49% of total revenues; the main source of revenue is the income tax share (78%), followed by the property tax (17.3%). Lastly, there is a government support grant that is allocated to 11 underdeveloped municipalities (7.7% of total revenues of these municipalities). Otherwise there is no budgetary grant in the local finance system ...

The draft Local Government Finance Bill is aimed at increasing the share of own tax revenues and diminishing the weight of self-imposed contributions and of tax shares. According to the bill, 10% of the local yield of the income tax should go to the municipality, but the municipality would be allowed to add a surtax at a maximum rate of 13% (15% in Podgorica and Cetinje), and 10% of the national yield would be channelled to an equalisation fund.”¹⁰

⁸ UNDP, [Country Report: An Assessment of Fiscal Decentralisation Reform in Serbia](#). In *Fiscal Decentralization in Transition Economies: Case Studies from the Balkans and Caucasus* (UNDP, 2005), p. 182- 185.

⁹ Ibid, p. 172.

¹⁰ SIGMA, [Assessment Report: Serbia and Montenegro - Decentralisation Process](#) (SIGMA, 2004), p. 9-10.



Local Government Functions and Competences

Serbia: Concerning local government functions and competences, the UNDP assessment points out that “considering the issue of local government functions and competences, it is very important to point out the specific situation faced by local governments. Because of the sequencing of the fiscal decentralization process in Serbia, the period from the end of 2000 (start of the fiscal reform and reform of revenue assignment) to 2002 (start of the responsibilities and expenditure assignment reform) was characterized by the existence of municipalities with high revenues that exceeded their expenditures. This situation changed when the reform of the expenditure assignment started with the adoption of a new Law on Local Self- Government in 2002. This Law introduced many new responsibilities for local government units. With the adoption of this Law, local government units were assigned two types of expenditure responsibilities: those financed with their own funds (own expenditures), and other responsibilities financed both from the local budget and the republic budget.

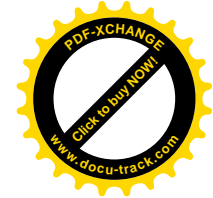
The Law on Local Self- Government enumerates 35 *own responsibilities* (art. 18) for the municipalities. These responsibilities include:

- a. adoption of the development programme;
- b. adoption of the urban plan;
- c. adoption of the budget and financial statement;
- d. regulation and provision of communal services;
- e. maintenance of housing and buildings and making them secure;
- f. regulation and provision of the use of building plots and business premises;
- g. environmental protection;
- h. establishment of institutions and organizations in the fields of primary education, culture, primary health care, recreation, sport, children and social care, tourism, etc.

The Law also allows for the *delegation of responsibilities* (art. 19, 20) from the level of the Republic. These responsibilities are financed from the Republic budget and mainly consist of inspection duties in the fields of products and services, agriculture, water supply, forestry, etc ...

Co- financed expenditures

Beside the expenditures mentioned as own responsibilities of each level of government, there are also expenditures shared between two or more levels of governments (shared expenditures, co- financed responsibilities). These are, mainly, responsibilities for the following public functions: education, health care, social care, environmental protection, tourism, sport and recreation, culture, public information. Usually, the republic finances the largest part of these expenditures and lower levels of government (the province and local units) finance expenditures on activities concerning their territories. It is notable that all these responsibilities are mainly given to lower levels of government via the process of managerial devolution. This means that local units are responsible for executing some tasks that were initially the responsibility of the republic, but for the sake of administrative simplicity and lower administrative costs they were transferred for execution to the lower level of government. The most important co- shared expenditures are social care, health care



and education. All levels of government provide these public goods, but each level produces the portion of them that benefits to the inhabitants of the broader or narrower territory.”¹¹

Montenegro: With regard to local government functions and competences: the SIGMA assessment writes that “the tasks of municipalities are regulated by the 1995 and the 1992 Law on the Transfer of Public Service Affairs to Municipalities. The latter delegated a number of tasks from the Republic to municipalities, on a ministry by ministry basis and provided for further transfers by subsequent laws. The Law on Local Government of 1995 enumerates particular rights and duties that municipalities have to exercise, by contrast with Serbian legislation, that enumerates fields in which municipalities have an authority, and refers to substantive legislation. Despite certain difference of approach in legislation, there is little difference between the Member States in the material competence of municipalities. The current interpretation of the law, despite the wording of article 16 of the Law on Local Government, of 1995, which includes a general clause, is that municipalities may not act in any matter without an explicit legal basis. Due to this interpretation, the lack of clarity of the distinction between own and delegated tasks becomes secondary, although it implies differences in the scope of state supervision. The new Law on Local Government includes a general clause (Art.30) but, unfortunately, it brings no clarity on the distinction between own and devolved and delegated activities.”¹²

¹¹ UNDP, [Country Report: An Assessment of Fiscal Decentralisation Reform in Serbia](#). In Fiscal Decentralization in Transition Economies: Case Studies from the Balkans and Caucasus (UNDP, 2005), p. 175- 178.

¹² SIGMA, [Assessment Report: Serbia and Montenegro - Decentralisation Process](#) (SIGMA, 2004), p.6.



For more information ...

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Emilia KANDEVA (ed), [Stabilization of Local Governments](#) (Local Government and Public Service Reform Initiative, Open Society Institute, 2001). Note: many of the articles in this book are not up to date with recent legislative changes, but they may still be of interest for providing a general background.

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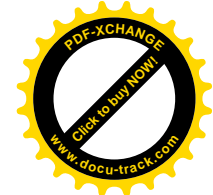
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