IMPROVING LOCAL GOVERNANCE AND SERVICE DELIVERY IN BANGLADESH: THE ROLE OF LOCAL GOVERNMENT FINANCE

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Preface

[Preface by LGD Senior Secretary to be inserted here.]

IMPROVING LOCAL GOVERNANCE AND SERVICE DELIVERY IN BANGLADESH: THE ROLE OF LOCAL GOVERNMENT FINANCE

Executive Summary

Context and objective. Local government institutions at different levels (Zila, Upazila and Union) play an important—but sometimes overlooked—role in public service delivery and sustainable development in Bangladesh. While these LGIs do not play a leading role in delivering key public services—such as primary education or basic health services—local governments are nonetheless an important partner in ensuring effective and inclusive service delivery. Although there is a recognition that local government institutions are generally under-resourced to perform the functions assigned to them, relatively little is known about the exact size, composition and distribution of intergovernmental finances in Bangladesh.

This report, as the first analysis of its kind, provides a “big picture” overview of local government revenues and expenditures for UPs, Upazila Parishads, Pourashavas, and City Corporations. It focuses on providing a basic quantitative overview of the expenditures, revenues and transfers of different types of LGIs. Rather than relying on sample analysis and case studies, the current document aims to represent as comprehensive and as accurate a view as possible of expenditures for all local government institutions in Bangladesh. As such, the analysis is based on data for all 4538 Union Parishads; financial data for all pourashavas for which complete and consistent financial reports were available (175 out of 329 pourashavas); financial data for all 11 City Corporations; and well as financial data (albeit incomplete) for all 492 Upazila Parishads. Where necessary, total expenditures, revenues and transfers were extrapolated to ensure a complete picture of the full universe of LGIs (Annex A).

For each local government type, the analysis in this report examines (i) the total volume of expenditures, revenues and transfers for each local government type based on an aggregation of actual available local government expenditure data; (ii) where possible, the composition of local expenditures, revenues and transfers (e.g. between recurrent versus capital expenditures); and (iii) the distribution of expenditures, revenues and transfers across local government jurisdictions. Given the fact that different LGIs have different population sizes, the comparison of LGI expenditures, revenues and transfers across LGIs is done in per capita terms.

The analysis in this section generally focuses on FY 2017/18, the latest year for which comprehensive data is available. Population data for each LGI was drawn from the Census 2011 (whenever possible) and adjusted for population growth up to 2018.

Findings. Figure ES-1 (at the end of the Executive Summary) provides a visual overview of the basic empirical findings of the analysis with respect to LGI expenditures, revenues, and transfers. A summary of the main findings includes:

- ***The current distribution of resources among LGIs appears imbalanced and inequitable***. The scale of increase in the levels of per capita expenditures, revenues and transfers from UPs to Pourashavas up to City Corporations suggests that smaller, rural LGIs as well as many pourashavas are possibly well underfunded. For instance, while Union Parishads spend slightly over BDT 500 per residents, City Corporations are able to spend BDT 3,750 per resident. It is highly unlikely that UPs or under-resourced pourashavas can deliver a similar level or quality of local services with the resources provided to them. The service deficit in these LGIs will continue to stimulate rural-urban migration.

- ***By contrast, there is generally relatively little variation in (per capita) expenditures within each category or type of LGI.*** To the extent that such variation exists, differences in resource availability appear to be driven largely by differences in special grants or earmarked project grant allocations rather than by variation in own source revenues.
- ***Despite the perception that LGIs should raise more own source revenue, the contribution made by own source revenue funding—especially in pourashavas—is quite high by global standards***. In most countries, rural local governments (which typically have a weak economic base) rely 90% or more on intergovernmental fiscal transfers. In countries around the world, even urban areas frequently receive considerable grant funding. By contrast, pourashavas in Bangladesh actually collect a higher share of resources from own sources than City Corporations. The high level of OSR contributions made by local taxpayers in urban LGIs is like to bias urban LGIs spending towards local public infrastructure and services demanded by local taxpayers, while causing them to focus less on other important urban functions (such as pro-poor urban services, or support infrastructure expansion for in-migrants due to urban expansion).
- ***The role of formula-based (block) grants as a share of revenues is relatively minor.*** Like in other countries, the bulk of LGI funding in Bangladesh is provided through the grant system. This is appropriate. However, to the extent that LGD tends to see LGIs through the lens of the formula-based block grants that it provides itself, it is missing the vast majority of funding that is flowing towards LGIs. The imbalance in the grant system in favor of special grants and earmarked project grants limits the spending discretion of LGIs and may result in non-LGD resources not being tracked with optimal detail by the budget and financial reporting formats prescribed by LGD.
- ***The combination of under-funding and reliance on earmarked grants limits the ability of local governments to be responsive to local priorities.*** Even through LGIs are receiving formula-based development grants, in practice, most transfer funding received by LGIs comes to them in the form of special grants and project grants, which are earmarked for the spending priorities of the central ministries that provide the funding. In addition, own source revenues could be seen as “conceptually earmarked” for the spending priorities of local businesses and other local taxpayers, who would otherwise resist paying local taxes were the money not spent on matters important to them. In addition, LGIs are expected to fund local administration from their own (often meagre) discretionary own resources. This means that, in practice, LGIs in Bangladesh have extremely little funding discretion to be responsive to the needs and priorities of the local community.

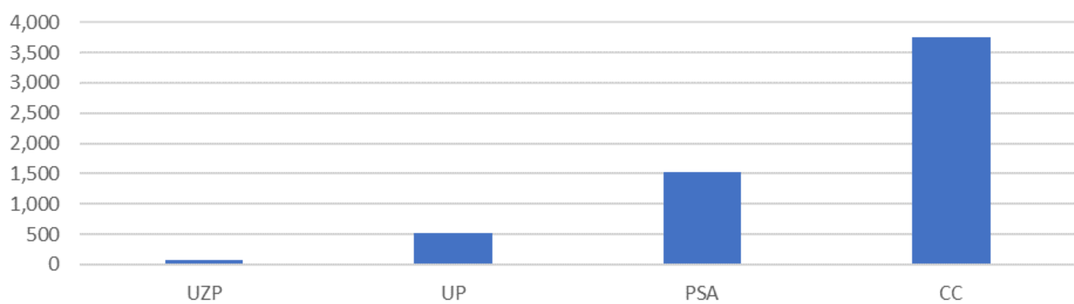
Implications. Policy implications of the analysis (explored further in Section 7) include the following:

1. Local government institutions will play an increasingly important role in Bangladesh.
2. Systematic monitoring local government finances should inform policies and reforms.
3. More effective deconcentration will be the key to localization and sustainable development.
4. Institutional capacity of LGIs is a binding constraint on the ability of LGIs to be a catalyst for better local planning, public services and achieving sustainable development. LGI funding is a binding constraint on the institutional capacity of LGIs.
5. The volume and nature of local government financing should distinguish between local priorities to be pursued by LGIs from own source revenues, and programs that leverage LGIs in pursuit of national objectives.
6. There is a need to elevate the intergovernmental fiscal transfer system.
7. Strengthening local budgeting, local public financial management and local revenue administration.

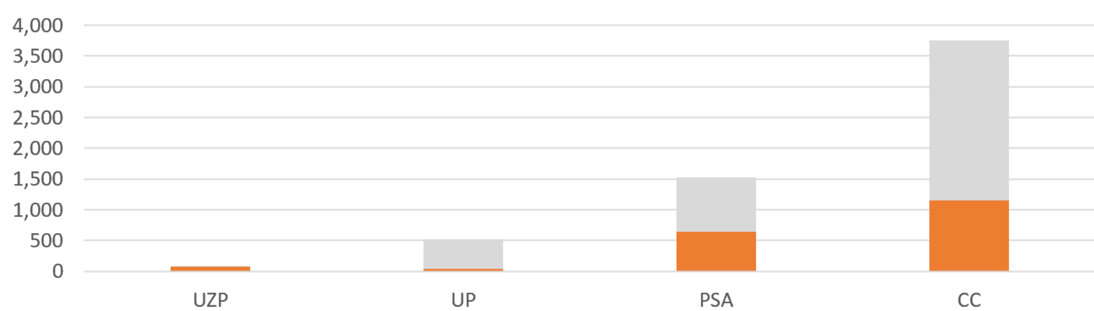
The analysis in this report suggests that improved and more systematic monitoring of LGI finances and operations is “low-hanging fruit” in terms of ensuring that LGIs become effective platforms for inclusion and the promoting of sustainable development at the local level. In fact, it would not be difficult to update the budget preparation and financial reporting formats for LGIs so that their budgets and finances are presented in organizational/functional (sectoral) manner, which would (a) allow citizens to more effectively scrutinize local budgets and finances, and (b) would allow LGD to analyze the distribution and sectoral breakdown of expenditures and transfers for each LGI in a more detailed manner. This would allow each central line ministry (and other sectoral stakeholders) to see the level of sectoral resources being spent across LGIs, and identify where these resources are being spent.

Table ES.1 Overview of LGI Finances, FY 2017-18

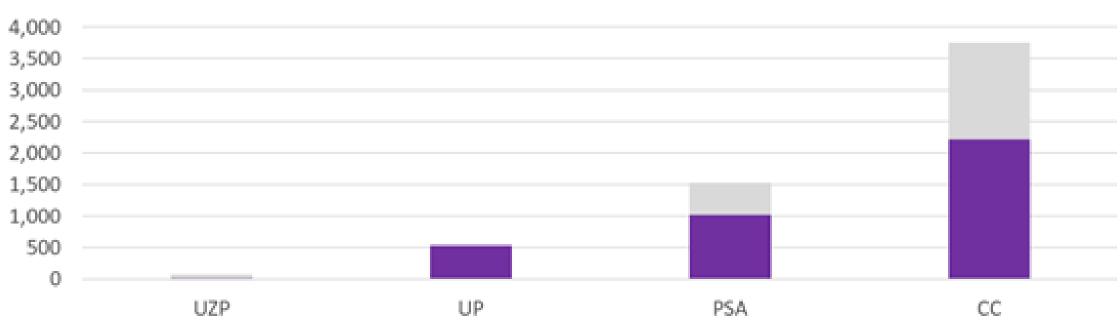
Panel A – Average per capita expenditures, by LGI type (FY 2017/18)



Panel B – Average per capita own source revenues, by LGI type (FY 2017/18)



Panel C – Average per capita intergovernmental fiscal transfers, by LGI type (FY 2017/18)



Note: In Panels B and C, the orange and purple bars reflects average per capita own source revenues and per capita transfers, respectively. For comparative purposes, the grey bar indicates the per capita level of LGI expenditures.

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Acronyms

ADP	-	Annual Development Program
BBG	-	Basic Block Grant
BDT	-	Bangladeshi Taka
CC	-	City Corporation
LGI	-	Local Government Institution
LGSP (1-3)	-	Local Governance Support Project (1-3)
PSA	-	Pourashava
UGDP	-	Upazila Governance and Development Project
UP	-	Union Parishad
UZP	-	Upazila Parishad
WASA	-	Water Supply and Sewerage Authority

Note: At the time of writing (April 2020), the approximate exchange rate was US$ 1.00 = BDT 85.

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PART I – INTRODUCTION AND OVERVIEW

IMPROVING LOCAL GOVERNANCE AND SERVICE DELIVERY IN BANGLADESH: THE ROLE OF LOCAL GOVERNMENT FINANCE

1. Background

Bangladesh has experienced a major social and economic transformation. The social and economic transformation of Bangladesh over the past half century—including rapid economic growth and increased productivity—has been closely related to important demographic changes and territorial developments, such as rapid urbanization of the country's growing population. While a large share of the country's economic and population growth has centered around Dhaka and Chittagong, much of this growth has taken place on the periphery of the metropolitan areas, rapidly transforming previously rural areas into peri-urban industrial zones that are a vital part of the country's ambitions to achieve middle-income status. In addition, whereas 25 years ago, Bangladesh had fewer than 100 urban local government jurisdictions, the country now has almost 350 urban jurisdictions (pourashavas and City Corporations).

Urban and rural local governments—as well as local administrations—are key players in achieving inclusive and sustainable social and economic development. While urban areas in Bangladesh—as in countries around the world—have been the engines of the country's economic growth, both urban and rural local governments have the potential to be important partners to the national government in achieving inclusive and sustainable social and economic development—including in the context of 2030 Agenda for Sustainable Development.

Within the context of the country's rapid economic and demographic transformation, considerable efforts have been made by the Government of Bangladesh and its partners to ensure an effective, inclusive and responsive public sector structure and to ensure that the benefits of economic progress are shared across the national territory. National efforts to achieve urban and rural development have been pursued using a combination of different approaches to "localize" public services and sustainable development, including through the effective deconcentration of public administration at different levels; the implementation of national or "vertical" sector programs; the mobilization of NGO partners and parastatal agencies; as well as by strengthening local government institutions as platforms for inclusion and transformation.

For instance, building on long-running efforts to transform Union Parishads into inclusive entry-points for rural residents into a modern and responsive public sector, the Government's "My village, my town" initiative provides a next step in the country's ambitious rural development efforts.

Different LGIs may play a different role in the ongoing social and economic transformation of Bangladesh. Naturally, the roles that different types of local government institutions (LGIs) might play in promoting the ongoing social and economic transformation of Bangladesh will differ by their type and nature.

Urban local governments are important mechanisms for inclusive collective decision-making for urban constituents and self-funded provision of urban services, including the paving of roads and streets, solid waste management, "greening and cleaning" and ensuring the provision of water and sanitation services. In addition, however, Pourashavas and City Corporations are natural partners to national government in pursuing national policy objectives in urban development, such as ensuring the operation and maintenance of existing urban infrastructure; ensuring climate resilience/disaster risk reduction; as well as providing social protection and public services to the urban poor (who often originate from outside the urban areas). Similarly, given the urban-rural linkages in the economic system, investments in urban infrastructure and services often known to have a positive impact on economic growth well beyond the urban government's own jurisdiction.

Likewise, rural local government institutions at different levels (Zila, Upazila and Union) play an important—but sometimes overlooked—role in public service delivery and sustainable development in Bangladesh. While these LGIs do not play a leading role in delivering key public services—such as primary education or basic health services—local governments are nonetheless recognized as an important partner in ensuring effective and inclusive service delivery. For instance, as the level closest to the people in rural areas, Union Parishads are able to support national ministries in identifying poor households in need of social security; are well-positioned to mobilize local residents to access local health programs; are able to help identify areas and households at risk of climate-related disasters; and so on.

Similarly, Upazila Parishads are uniquely positioned to not only monitor the performance of public services being provided by in their respective jurisdictions, but also to support the services being delivered through Upazila-level local administration. As such, as small contribution by LGIs can have an important impact on sustainable development outcomes.

Local governments appear to be under-resourced, but by how much? Although there is a recognition that local government institutions are generally under-resourced to perform the functions assigned to them, relatively little is known about the exact size, composition and distribution of intergovernmental finances in Bangladesh.[1] For instance, what share of national public finances flows to the different local government institutions as opposed to other channels of localization? As a result, how much are local governments able to spend? What is the resulting financing gap of local government institutions?

Objective and structure of this report. This report is the first analysis of its kind providing a "big picture" overview of local government revenues and expenditures for UPs, Upazila Parishads, Pourashavas, and City Corporations.[2] Rather than repeating what is already known about the structure of local government finances and local public financial management practices in Bangladesh, the analysis focuses on providing a quantitative overview of the expenditures, revenues and transfers of different types of LGIs.

Part I of this document provides an introduction and background analyses needed as context before moving on the more detailed analysis of LGI finances in Part II. As such, Section 2 provides an overview of public sector finances in Bangladesh, including a discussion on the nature and extent to which public expenditures are being localized. Section 3 presents a high-level estimate of the expenditure needs of LGIs in Bangladesh, along with a high-level overview of local government finances in Bangladesh.

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[1] The strengths and weaknesses of local governance institutions and local financial management at the local level are relatively well-documented. For instance, a series of high-quality policy papers was produced by LGD/UNDP (2015) on various institutional, legal and fiscal aspects of local governance in Bangladesh. Furthermore, with the support of SDC PROLOG, World Bank (2019) prepared an excellent review of local government financial management. LGD has prepared National Strategies for Local Governance Improvement for Pourashavas (as well as other LGIs).

[2] To the extent possible, LGI finances will also be contrasted to the level of deconcentrated (local administration) expenditures at the Upazila level.

Subsequently, Part II presents detailed quantitative analyses of the level, distribution and composition of local expenditures, revenues and intergovernmental fiscal transfers for LGIs in Bangladesh. Local expenditures, revenues and transfers are dealt with in Sections 4, 5 and 6, respectively. The discussion in each of these sections is further broken down by different types of local government institutions (i.e., Union Parishad; Upazila Parishad; Pourashavas and City Corporations).

Part III (Section 7) draws lessons and policy implications from the analysis.

The policy implications of this analysis will be relevant for many stakeholders. Policy analysis of local government finances leads to important policy implications that are relevant to the Government of Bangladesh and development partners alike. As the Government of Bangladesh seeks to pursue the Sustainable Development Goals as the country moves towards middle-income status, the Government of Bangladesh will be keen to identify the value-added that local governments can provide in their role as catalysts and change-agents in achieving inclusive, sustainable development. As such, the Local Government Division should be considered the main champion and owner of the analysis in this report.

Other stakeholders—both within the Government of Bangladesh, as well as its international partners—will have a keen interest in the analysis and implications of this study. The list of interested stakeholders would most likely include local government institutions themselves (along with their associations); civil society organizations operating at the local level; sector ministries; as well as development partners and international financial institutions.

2. Overview of Localization and Local Public Finances in Bangladesh

Before engaging in an in-depth analysis of local government expenditures, revenues and intergovernmental fiscal transfers in Bangladesh, an overview of local public finances is presented below.

This overview section presents an overview of the subnational public sector structure (Section 2.1); explores different approaches with which sustainable development can be "localized" (Section 2.2); presents an overview of national-level public sector finances in Bangladesh (Section 2.3); and analyzes the extent to which central public sector spending is distributed to different administrative tiers (Section 2.4). Next, Section 3 presents a high-level overview of local expenditure needs and local government finances in Bangladesh.

2.1 A brief overview of the subnational public sector structure in Bangladesh

The Constitution of the People's Republic of Bangladesh formally defines the subnational governance and administrative structure of the country's public sector. [3] Section 11 of the Constitution states that "[t]he Republic shall be a democracy in which fundamental human rights and freedoms and respect for the dignity and worth of the human person shall be guaranteed, and in which effective participation by the people through their elected representatives in administration at all levels shall be ensured." Furthermore, "Local Government in every administrative unit of the Republic shall be entrusted to bodies, composed of persons elected in accordance with law" (Section 59, Clause 1). In addition, Section 59 further states that everybody referred to in Clause 1 "… shall, subject to this Constitution and any other law, perform within the appropriate administrative unit such functions as shall be prescribed by Act of Parliament, which may include functions relating to (a) Administration and the work of public officers; (b) the maintenance of public order; (c) the preparation and implementation of plans relating to public services and economic development."

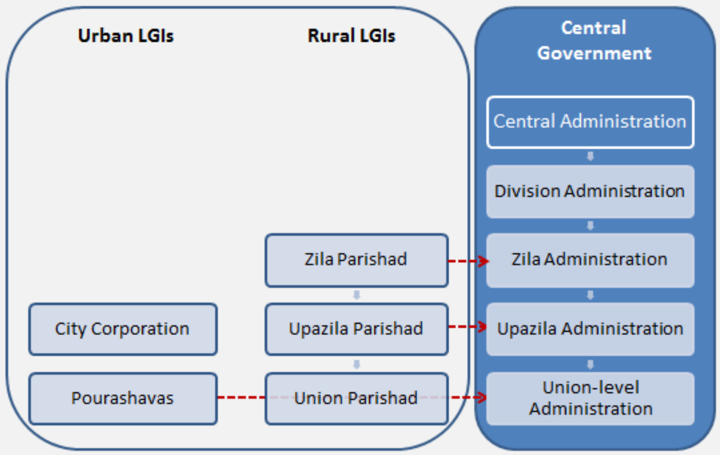
It should be noted that the term '*Sthanio Shashon'* used in the Bengali version of the Constitution is not synonymous with the term 'local government' used in the English version. The term in Bangla means 'local administration', which is in consonance with the term 'administration at all levels" of Article 11, but not in any way indicative of local self-government as has been envisioned in the English version of Article 59.

Over time, five types of Local Governments Institutions have been codified by law, including Zila Parishads, Upazila Parishad, Union Parishads, Pourashavas (municipalities) and City Corporations.[4] These five types of LGIs function alongside four subnational levels of tiers of local administration of the central government, also referred to as the "field administration" (Figure 2.1). At the time of writing, Bangladesh is divided into 8 Divisions; 64 Zilas, 492 Upazilas, 4,554 Union Parishads; 329 Pourashavas and 11 City Corporations.[5]

[3] This section is based on *The Local Government System In Bangladesh: A Comparative Analysis Of Perspectives And Practices* (Ahmed et al 2014). See this publication for a more extensive discussion of the local government institutional structure in Bangladesh.
[4] Several districts in the Chittagong Hill Tracts area have different local governance arrangements.
[5] Given the periodic increase in the number of administrative and governance sub-divisions, the number of subdivisions reflected in practice may lag. For instance, Mymensingh Division—which was split off from Dhaka Division in 2015—is not always reflected in official tabulation. In 2015, the process was started to create two more

In general, each of the five types of LGIs serves as a hybrid institution that covers both roles implied in the Constitution: in part, they function like local self-government institutions (managing and implementing some of their own affairs within their jurisdiction), and in part, they function as elected bodies supervising the functioning of the national government's field administration within their jurisdiction.

Figure 2.1 An overview of local government and local administration of Bangladesh



Different legislative acts regulate the establishment, functions and operation of different types of LGIs (Box 2.1). As a result of the fragmented legal framework, there is considerable lack of clarity and duplication in the assignment of functional responsibilities, where different local government levels are assigned (seemingly) duplicative responsibility over concurrent functions (e.g., in health and education). Similarly, there is considerable overlap in the functional assignments of LGIs and deconcentrated field administrations. These issues were explored in greater detail by Osman et al (2014).

To the extent that the "de facto" assignment of public sector functions is reflected by the level of public expenditures, the analysis below will show that, in reality, the national government—through the local administration at different levels—is responsible for the vast majority of public service provision and investment in development activities in Bangladesh. Local government institutions—as local self-government institutions—are only responsible for a tiny fragment of public service provision and development expenditures.

Box 2.1 Functional assignment of different LGIs

There is considerable lack of clarity and duplication in the assignment of functional responsibilities, where different local government levels are assigned (seemingly) duplicative responsibility over concurrent functions (e.g., in health and education). Similarly, there is considerable overlap in the functional assignments of LGIs and deconcentrated field administrations.

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divisions: Comilla Division and Faridpur Division. Similarly, City Corporations that were recently establish (i.e., upgraded from Municipality status)—such as Mymensingh City Corporation, established in 2018—may be reflected under their previous status in the current report.

Union Parishad legal function assignments. The UP Act of 2009 (Section 47) prescribes four main categories of functions or activities to be undertaken by the UP: administration and establishment, maintenance of public order, services related to public welfare activities, and preparation and implementation of plans that relate to local economic and social welfare activities.

In addition to these broad areas of functional responsibility, a long list of specific activities (39) has been prescribed for the UP in Second Schedule of the UP Act. Among the UP functions listed are general functions, such as the " Preparation of five years and various time limited development plan" and the "Development, protection and maintenance of rural infrastructure." In addition, the list includes typical "local" functions", such as the "maintenance of public places, open spaces, gardens and play grounds", "Lightening the Union Parishad roads and public places" and "Tree plantation and caretaking."

Pourashava legal functional assignments. Pourashavas are legally empowered to perform a variety of social, economic and civic functions. These functions and activities are described in Local Government (Pourashava) Act 2009, Sections 50, 51 and Second Schedule. Although the distinction is not clearly made, the Act provides for 'mandatory' 'optional', or 'assigned' municipal functions. Most Pourashavas fail to deliver on their assigned functions due to acute financial stress, manpower shortages and other structural weaknesses that persist (Bhattacharya 2013).

Given the limited own revenue base and the limited financial support that the central government provides to municipalities, financial resources are simply inadequate for most municipalities to perform even their so-called mandatory functions. In particular, municipalities appear to face difficulties providing public services that require substantial investments, such as municipal piped water or major road infrastructure. In many cases, central government ministries or agencies (such as LGED and DPHE) step in to provide the functions which are assigned to the municipal government, but which cannot be funded from municipal revenues.

City Corporation legal functional assignments. City Corporations in Bangladesh have been vested with a long list of functions delegated to them by the central government under the Local Government (City Corporation) Act, 2009. The Local Government (City Corporation) Act, 2009 allows every city corporation to undertake any development plan and its implementation under the approval of the Government's Local Government Division. The third schedule of the Act lists 28 types of functions and activity of the Corporation, which can be broadly grouped into:

- Public health (water supply, sewerage and sanitation, etc.)
- Public welfare (public facilities for education, recreation, etc.)
- Regulation (enforcing building by laws, encroachment on public land, etc.)
- Public safety (fire protection, street lighting, etc.)
- Public works (construction and maintenance of roads, culverts and drainage systems, etc.)
- Development activities (town planning and development of commercial markets, etc.)

Upazila Parishad (UZP) legal functional assignments. For a long period of time, the UZP (previously known as the Thana Parishad) did not have any executive responsibility; its main task was to coordinate the activities of various departments working at that level. Unlike the UP, the UZP's status as an elected local body has swung back and forth over the past half century. The most significant change in this regard was the adoption of the Upazila Parishad Act of 2009. Although coordination still is seen as one of its main functions, in the 2009 Act, the Upazila Parishad was given better scope to play an executive role in providing different local services, including the preparation of development plans, including Five-Years Plans, to be implemented in different periods of time along with 17 additional functions.

The Act implies that these Upazila Parishad functions are executive in nature, as Section 23 states that Upazila Parishads "shall execute these functions in accordance with the capacities of their funds." On one hand, this suggests that these functions are executive (not just supervisory) responsibilities of the UZP. On the other hand, this clause delimits the functional responsibly of the Upazila Parishad by the resources available to it, rather than making sure that “finance follows function”.

Concerns about lack of clarity and duplication. Although the various legal documents may (or may not) delimit the detailed functional responsibilities of different LGIs and/or clarify under what circumstances different local government institutions are actually responsible for the management of health facilities, it is clear that under the current legal arrangements, even a well-informed citizen would have great difficult in holding any particular local government entity accountable for its failure to deliver effective public services. Similarly, given the fragmentation and duplication of responsibilities, it is essentially impossible for actors at any one level to achieve meaningful improvements in service delivery outcomes on their own.

Because improved service delivery outcomes often require coordination between three or more different administrative levels, the current situation limits the incentives felt at any one level to bring “quality services to the people’s doorsteps”. Furthermore, the vertical fragmentation results in a situation where no elected local leader at any level will be able to realistically claim credit for meaningfully improving health services in his or her jurisdiction. This means that the lack of clarity in functional assignments and the resulting fragmentation of the de facto responsibility (a) presents a major vertical coordination challenge to improving local services, (b) prevents meaningful accountability of local officials at all levels, and (c) prevents meaningful incentives for local leaders to improve local services.

Source: Ahmed et al (2014).

2.2 Different approaches to localizing sustainable development

Bangladesh was an active participant in the global process leading to the preparation of the post-2015 Development Agenda, and the starting time of the SDGs (2016-2030) enabled the country to integrate the SDGs into the 7th Five Year Plan (2016-2020). Nonetheless, knowledge, resources, skills and partnerships will need to be mobilized on an unprecedented scale to implement all the 17 Sustainable Development Goals (SDGs). In fact, the ultimate success of the 2030 Agenda for Sustainable Development hinges on the ability of the Government of Bangladesh to ensure that public services and sustainable development interventions reach the grassroots level across the entire national territory. In other words, there is a need to “localize” the Sustainable Development Goals in order to make sure that the benefits of sustainable development reach all citizens.[6]

Different countries follow different approaches to decentralization and localization of public services. In many countries, the most common way for the public sector to interact with people at the local level is through elected local governments. When local government officials are made responsible for the delivery of key public services in a way that is responsive to the needs of their constituents, ***devolution*** can increase the responsiveness, effectiveness and accountability of the public sector.[7]

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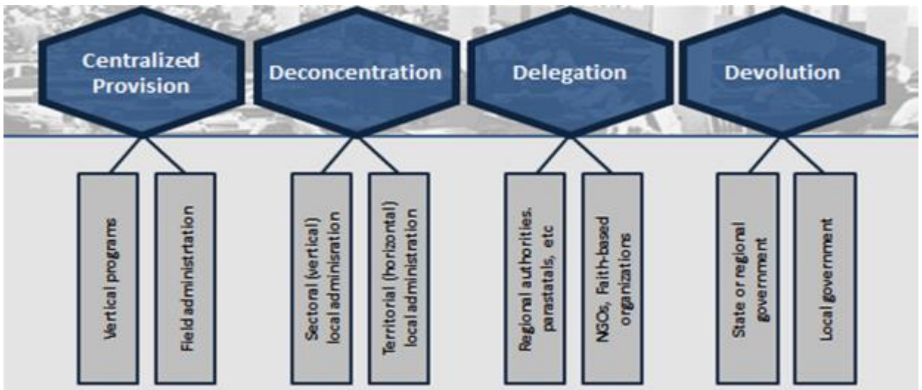
[6] In fact, the recognition of the importance of “localization” proceeded the SDGs in Bangladesh, as the Government’s commitment to bring “quality services to the people’s doorsteps” was already contained in the Sixth Five-Year Plan (Planning Commission, 2011: 218). Similarly, the “My village, my town” initiative recognizes that there is a need to upscale the nature of public services to be provided in the country’s rural areas.

[7] Dennis Rondinelli (1986) considered three different types of decentralization, notable (i) devolution, (ii) deconcentration, and (iii) delegation. Rondinelli noted that these different forms of decentralization had different degrees power, authority and autonomy associated with them. An important distinction should be made in particular between devolution and deconcentration. In short, devolution is the transfer of power and authority for planning, management, resource-raising and allocation, and other functions from the central government to semi-

In addition to providing services and localizing sustainable development through local governments, there are several other ways in which the public sector interacts with people and provides—or supports— public services and development at the local level. These non-devolved approaches to decentralization and localization are part and parcel of the local public sector (Figure 2.2).

Figure 2.2. Mechanisms for decentralization and localization



Source: Boex (2015).

For instance, in many countries, local administrative units or local departments of central line ministries provide public services in a ***deconcentrated*** manner. In addition, central authorities often provide grants or subsidies to para-statal organizations, semi-autonomous corporations, non-governmental organizations (NGOs) or faith-based organizations (FBOs) in order to deliver certain public services on behalf of the central government in a ***delegated*** manner. Likewise, central government line ministries sometimes provide direct support to local public services. For instance, ***centralized provision*** or direct support for localized services takes place when central line ministries supply schoolbooks or medicines that are used in local schools and clinics, or when a central agency directly funds the construction of classrooms or other local infrastructure.

Not all approaches to decentralization or localization are equal in terms of their potential impact on the empowerment of people over the public sector. As noted by UN HABITAT (2007), "[p]olitical decentralization to the local level is an essential component of democratization, good governance and citizen engagement; it should involve an appropriate combination of representative and participatory democracy". Similarly, not all approaches to decentralization or localization are equal with regard to their potential impact on sustainable development.

Although experiences differ from country to country, it is often difficult for central governments to effectively implement development interventions at the grassroots level in a sustainable manner through centralized mechanisms, such as vertical (sectoral) programs. Since devolved local government systems have a considerably greater potential degree of autonomy, accountability and responsiveness, this

autonomous local (or regional) government units. In contrast, deconcentration is the transfer of responsibility for public sector functions from the central government to field units or lower administrative levels of the central government.

approach offers the potential for more effective localization of public services and development interventions than deconcentration, delegation to direct centralized interventions. However, devolved local governments need to meet many preconditions—with respect to inclusive and responsive governance; administrative capacity; and adequacy of financial resources—in order to be suitable and efficient mechanism for localizing sustainable development.

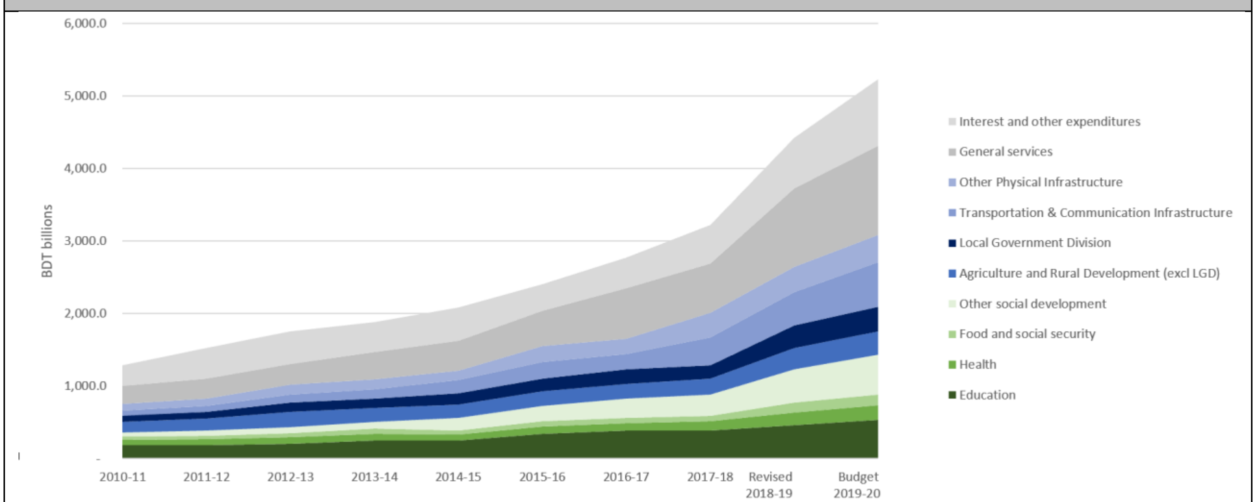
In fact, most countries do not rely exclusively on one approach or the other. Instead, many countries rely on a collaborative multi-level governance system where local public services are provided—and sustainable development goals are pursued—through a combination of different mechanisms (devolution, deconcentration and delegation) at the same time.

As such, in order to ensure that sustainable development outcomes are localized in the most effective manner, it is important to recognize that subnational authorities and central governments are mutually dependent, rather than isolated actors, and that the ability of local government institutions and local administrations to contribute to effective localization of development interventions is largely enshrined in their institutional background. As noted by Charbit (2011), the key underlying question is not whether to "decentralize or not" or even to opt for a specific decentralization model, but rather, to look at ways to ***improve capacity and co-ordination among public stakeholders at different levels of government to increase efficiency, equity and sustainability of public spending***.

2.3 An overview of public expenditures in Bangladesh

While the main focus of this policy study is the finances of local government institutions, it is important to place this discussion in the context of an overview of public sector finances in Bangladesh. As such, Figure 2.3 presents an overview of the level and functional composition of public expenditures in Bangladesh from 2010/11 through 2019/20.

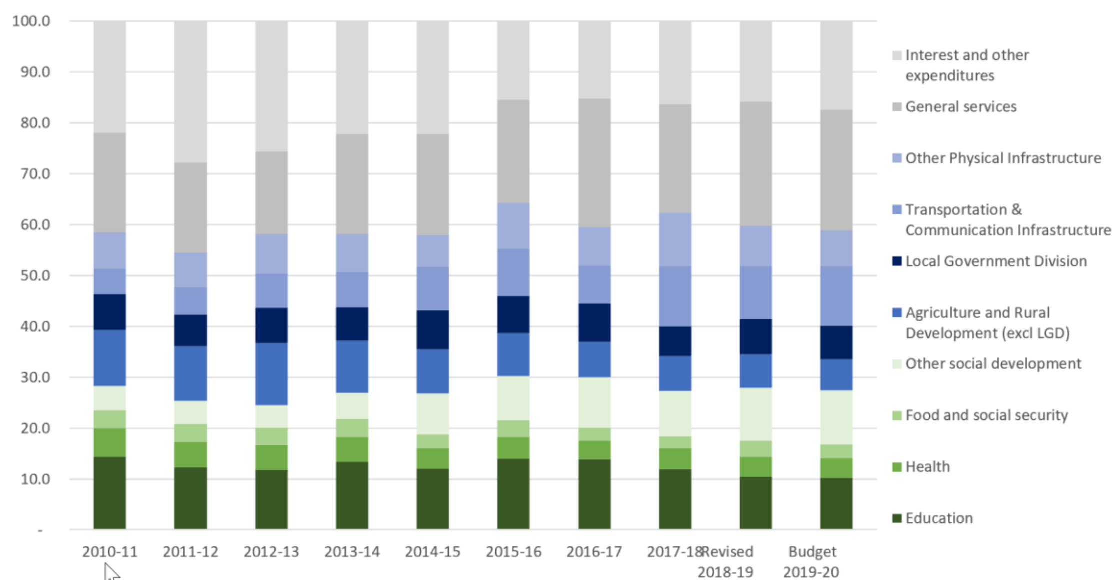
Figure 2.3. Public expenditures in Bangladesh: functional composition, 2010/11 – 2019/20 (BDT billions)



Source: Prepared by authors based on Ministry of Finance data (various years)

The first pattern on public spending in Bangladesh that is clearly visible in the figure is the overall size and steady increase over time: whereas in FY 2010/11, the Government of Bangladesh spent BDT 1.2 trillion (roughly US$ 19 billion), total national budget increased to BDT 5.3 trillion (roughly US$ 61 billion) by FY 2019/20. Although this increase partially reflects the impact of inflation, the increase in public sector spending is still substantial when considered in real terms (reflecting more than a doubling—and increased by a factor 2.3).

Figure 2.4. Public expenditures in Bangladesh: functional composition, 2010/11 – 2019/20 (as percent of total)



Source: Prepared by authors based on Ministry of Finance data (various years)

As per the functional composition of the Government's budget, the green area reflects spending on "social investment" functions, blue reflects "physical investment" functions, whereas gray reflects general services (including law and order) and other public spending, including interest payments.

According to the Government's functional classification, all spending by LGD is categorized as spending on physical infrastructure. LGD spending increased from BDT 90 billion (US$ 1.3 billion) in FY 2010/11 up to BDT 324 billion (US$ 4 billion) budgeted for FY 2019/20. Over this period, LGD spending has fluctuated between 5.8 percent and 7.7 percent of total Government expenditures (Figure 2.4).

2.4 An analysis of localized public sector spending

As discussed in Section 2.1, it is important to recognize that there are different ways for any country to transform public finances into sustainable development outcomes. As such, "localizing public services and development" should not be equated with devolved spending alone (i.e., spending by LGIs), nor should the measurement of "localization" be limited to the amount of resources spent by LGD. Instead, it is important to take into account all different mechanisms by which the Government of Bangladesh reaches the grassroots. In doing so, it is important to recognize that the most important mechanism for localization used by the Government of Bangladesh include vertical (sectoral) programs and deconcentrated spending.

Table 2.1 considers the vertical profile of public expenditures in Bangladesh, revealing the extent to which the Government relies on deconcentrated spending by function.

Table 2.1 Vertical profile of public expenditures, by function, FY 2017/18
Core budget expenditures; Taka billions

	Total	Central spending	Deconc. Spending	Upazila level Spending	As percent of total		
					Central spending	Deconc. Spending	Upazila level spending
Agriculture	191.3	151.8	39.5	19.0	79.4	20.6	9.9
Defense Services	211.5	209.6	1.9	0.3	99.1	0.9	0.1
Educ. / Technology	474.2	274.6	199.6	120.1	57.9	42.1	25.3
Energy and Power	285.6	285.6	0.1	0.0	100.0	0.0	0.0
Health	168.4	75.4	93.1	37.6	44.7	55.3	22.3
Housing	34.6	23.6	10.9	0.0	68.4	31.6	0.0
Industrial / Econ Svc	27.2	24.0	3.2	0.3	88.2	11.8	1.2
LG / Rural Dev	215.7	60.2	155.6	23.8	27.9	72.1	11.0
Public Order / Safety	220.7	109.3	111.4	19.5	49.5	50.5	8.8
Public Services	731.5	331.8	399.8	71.6	45.4	54.6	9.8
Rec., Culture / Relig.	30.9	21.8	9.1	5.2	70.5	29.5	16.7
Social Sec. / Welfare	184.5	92.0	92.6	45.5	49.8	50.2	24.7
Transport / Comm.	394.4	287.2	107.2	0.0	72.8	27.2	0.0
Total	**3,170.7**	**1,946.8**	**1,223.9**	**343.0**	**61.4**	**38.6**	**10.8**

Source: Computed by authors based on BOOST data.

This vertical expenditure profile shows that most public expenditures are concentrated at the central government level. The majority of public sector resources in Bangladesh are executed at the national (headquarters) level of the various ministries, with 61 percent of public spending being executed through national ministries, departments and agencies. Second, while almost 40 percent of public spending is being done in a deconcentrated manner, the vast majority of these resources are executed (or coded) at the Division of District (Zila) level, rather than at the sub-district (Upazila) level: Out of the 38.6 percent of spending that is geo-coded as subnational, only 10.8 percent of core budget expenditures are actually being coded to the Upazila level. Although Upazila-level spending is slightly higher for "front-line" functions and services such as education, health and social security, the overall percentage of sectoral resources that is managed at the Upazila-level is quite low.

While the percentage is quite low, compared to other resources making their way to the local level, the amount of deconcentrated spending that takes place at the Upazila level—around BDT 343 billion—is still quite considerable. By comparison, for instance, the total amount of grants budgeted to be provided by LGD to all LGIs in the same financial year was only BDT 7.1 billion – a fraction of this total.[8]

[8] For reference, according to the BOOST data set, LGD spending for FY 2017/18 was BDT 186 billion, of which BDT 163.3 billion (87.9 percent) was spent at national level. Deconcentrated LGD spending largely takes place at the Upazila level, with BDT 21 billion (11.3 percent) coded as Upazila-level spending and only BDT 1.6 billion as Division and District-level spending (0.85 percent).

The transparency, efficiency, equity and responsiveness of public sector spending in Bangladesh could most likely be enhanced by pursuing more effective budgetary deconcentration of national budget resources directly at the Upazila level. As the bulk of public sector spending is spent at the national level and/or contained in vertical sectoral programs makes it difficult to track resources to the front line, front-line service delivery staff have limited ability to make efficient spending decisions, as these would have to be administered through multiple layers of bureaucracy.

Table 2.2 considers the horizontal profile of public expenditures in Bangladesh, revealing the manner in which deconcentrated spending is distributed across administrative Divisions.[9]

Table 2.2 Horizontal profile of public expenditures, by function, FY 2017/18
Core budget expenditures; Taka billions

Taka Billion	Total Government Spending	*Percent of Total*	Upazila Administration	*Upazila Admin. (Percent of Division Total)*	*Upazila Admin. (Percent of Grand Total)*
Barisal	71.3	*2.2*	29.6	*41.5*	*0.9*
Chittagong	198.5	*6.3*	74.9	*37.7*	*2.4*
Dhaka	426.7	*13.5*	93.9	*22.0*	*3.0*
Khulna	112.7	*3.6*	37.2	*33.0*	*1.2*
Rajshahi	116.2	*3.7*	45.4	*39.1*	*1.4*
Rangpur	93.3	*2.9*	38.7	*41.5*	*1.2*
Sylhet	53.8	*1.7*	23.3	*43.4*	*0.7*
Central*	**2,098.4**	***66.2***	**-**	**-**	**-**
Total	3,170.7	*100.0*	343.0		*10.8*

Source: Computed by authors based on BOOST data.

Although a detailed analysis of horizontal allocation of resources is beyond the scope of this analysis, it is clear from this bird's-eye view that the country's two most populous divisions—Dhaka Division and Chittagong Division, which together have more than half of the country's population—receive more than half of the deconcentrated resources. Per capital allocations—both at the division/district level as well as at the Upazila level—vary considerably between divisions.

In addition to some analysis of deconcentrated spending, relatively limited information about the localized allocation of spending in national budget documents is available. The LGD budget does break down the allocation of transfers to different types of LGIs (Table 2.3). However, the overall amount of information contained in the budget with regard to local government grants is limited. For example, data on the composition into formula-based block grants and more discretionary special grants, as well as regarding their horizontal distribution—is unevenly available.

[9] Note that in the source data, Mymensingh Division is still considered part of Dhaka Division.

Table 2.3 Medium Term Expenditure Estimates (MTEE) by Institutional Unit, Schemes and Projects						
	Actual	Budget	Revised	MTEE		
BDT Thousands	2017/18	2018/19	2018/19	2019/20	2020/21	2021/22
Transfer to LGIs						
City Corps.	592,750	100,000	1,018,500	125,000	250,000	350,000
Zila Parishad	17,612	10,000	25,000	12,000	15,000	18,000
Municipality	95,856	200,000	220,000	250,000	5,649,117	1,331,535
Upazila Parishad	539,299	700,000	704,500	750,000	925,750	1,064,612
Union Parishad	3,017,060	5,100,000	5,100,000	4,908,500	509,900	5,299,500
Total: Transfer to LGIs	**4,262,577**	**6,110,000**	**7,068,000**	**6,045,500**	**7,349,767**	**8,063,647**
Source: Government of Bangladesh Budget. 2019/2020, Table 6.1.3.						

3. A high-level overview of LGI expenditure needs and local government finances

Within the context of the overall picture of public finances in Bangladesh, Part II of this report presents a detailed analysis of the finances of local government institutions in the country. This analysis focuses on the four most relevant types of local government institutions: Union Parishads and Upazila Parishads in rural areas, and Pourashavas and City Corporations in urban areas. The analysis focuses on LGI expenditures (Section 4), own source revenues (Section 5) and intergovernmental fiscal transfers (Section 6).

Before considering the detailed quantitative analysis, however, it is useful to consider two things. First, based on the functional responsibilities assigned to LGIs, what is the size of expenditure needs of LGIs? An upfront estimate of LGI expenditure needs (Section 3.1) will provide a reference point for the subsequent analysis of actual expenditures, revenues and transfers. Second, before considering the detailed analysis, Section 3.2 provides a high-level overview of LGI finances, which again can provide a reference point for contextualizing the subsequent discussions. Section 3.3 considers the gap between expenditure needs and the existing LGI expenditure levels (which are in turn determined by the availability of LGI fiscal resources).

3.1 What is the size of LGI expenditure needs in Bangladesh?

It is notoriously difficult, however, to accurately estimate LGI expenditure needs. This is especially true in Bangladesh where the assignment of functional responsibilities is not always clear, and where there are duplicative assignments of functional responsibility, both among LGIs, as well as between LGIs and the deconcentrated administrative apparatus.

These limitations notwithstanding, it is possible to get a general sense of the scale of the funding required by different LGIs by considering (a) the requirement for local infrastructure funding; (b) the funding requirement for local operation and maintenance; and (c) the funding required for local government administration. By starting with detailed expenditure needs for local/urban infrastructure, a rough estimate can be developed for overall LGI expenditure needs in Bangladesh.

The need for local government infrastructure development for pourashavas. There are numerous approaches to computing the expenditure needs of municipalities and local governments.[10] One of the most obvious of these approaches is to compute the infrastructure and service delivery needs of municipalities by establishing a variety of municipal service delivery norms for different urban services, and by computing the capital and recurrent implications of attaining these norms vis-à-vis the existing stock of municipal infrastructure. While this approach might provide an estimate of local expenditure needs with greater objectivity and accuracy, this is an extremely data-intensive measurement approach for which the necessary data is not available for Bangladesh at the current time. The absence of such data makes it difficult to determine—even in aggregate—which local services or urban infrastructure needs are under-funded relative to other local functions.

Even in the absence of a detailed study of LGI expenditure needs, it is clear that the level of unmet urban infrastructure needs is considerable given the disproportionate population growth of urban areas in

[10] See, for instance, Boex and Jorge Martinez-Vazquez (2007).

Bangladesh. When rural residents migrate to urban areas, they impose an additional demand on the stock of urban infrastructure without taking their previous stock of public infrastructure with them. Urban local governments quickly become overloaded with additional demand; without expanding the level of urban infrastructure in a corresponding amount, roads become congested, transportation networks become overloaded, solid waste piles up in unmanaged locations, informal markets sprout up where population growth occurs, and so on. Additional infrastructure is required both within the central business district—which serves an increasingly large daytime population—as well as across the rest of the urban area –which witnesses increases in population and population density- and on the urban fringes, where the footprint of the urban area is expanding on lands that were previously unserved in terms of municipal services.

Considering that existing levels of urban infrastructure and services are already inadequate for the non-migrant population that they are already serving, what is the unmet need for urban infrastructure solely based on urban population growth? Population growth projections (BBS 2015) suggest on increase in urban population of almost 1.5 million residents per year over the next 10-20 years, which means that urban infrastructure is needed for approximately 1.5 million new urban residents each year. Of course, the per-resident or per-household cost of municipal infrastructure needs varies from municipality to municipality, based on the level and quality of infrastructure put in place. As a rough estimate, it is not unreasonable to suggest that cost of additional infrastructure needs (for the functions that municipalities currently deliver, such as the preparation of residential plots, road access, water supply and sanitation infrastructure, and basic solid waste management infrastructure requirements) at a minimum would fall in the range of at least $250-$750 per person. Based on these assumptions, then the mid-point estimate of the total annual requirement for new urban infrastructure for municipalities in Bangladesh (based exclusively on infrastructure needs for in-migration) would equal approximately $700 million per year. This roughly equals US$20 per capita (per urban resident), which is sometimes used as a "rule-of-thumb" for rough estimates of general urban infrastructure needs in the design of urban infrastructure projects.

This estimate is likely to provide a considerable under-estimate of true municipal infrastructure needs in Bangladesh. For instance, it does not include the current backlog of unmet urban infrastructure needs in urban jurisdictions, nor does it account for the urban infrastructure required to alleviate congestion costs associated with high-density urbanization. Smaller, financially weaker municipalities—especially those that were upgraded from rural status over the past twenty years—often have substantial deficits in basic urban infrastructure, and effectively provide little more in terms of infrastructure and urban services than a rural Union Parishad.

Rough estimate of LGI Expenditure Needs. The basic estimate for urban capital infrastructure needs of US$ 20 per urban resident per year can be used as the basis for a rough approximation of LGI expenditure needs for different types of LGIs. Although the methodology is admittedly not very precise, for the time being, it is helpful to have an idea of the rough expenditure needs of different types of LGIs.[11]

In terms of local/urban infrastructure costs, the basic analysis above suggests that for a typical pourashava, capital infrastructure needs might approximately equal US$ 20 per resident. By comparison, the infrastructure needs for UPs are likely to be less. For instance, it is possible that UPs have infrastructure needs roughly equal to half of that of a typical pourashava (i.e., US$10 per resident); which

[11] In fact, it would be possible to refine the estimates at a subsequent stage to get a more precise estimate of LGI expenditure needs by function, in order to ensure that different types of LGIs are in a good position to support the localization of sustainable development in different functional areas (e.g., climate resilience; health service provision; disaster response; etc.).

is most likely an under-estimate given the extensive infrastructure gaps identified as part of the "My Village, My Town" program. At the other end of the spectrum, City Corporations are likely to face considerably higher constructions costs and land prices than secondary and tertiary towns, and therefore, it is not unreasonable to expect that City Corporations are facing infrastructure needs of US$30 per person per year. These estimates, of course, would have to be multiplied by the relevant numbers of residents in each local government type in order to arrive at an estimate of total expenditure needs for local infrastructure.[12]

Recurrent costs need to be included in expenditure estimates. An important shift has taken place in the global development community over the past 20 years regarding the nature of development. Where development was previously seen as a one-off activity (such as the construction of a capital infrastructure project) or as a time-limited program needed to shift the *status quo* from one level of development to another, current development thinking (such as the collective thinking behind the SDGs) recognizes development as an integrated effort to improve the human condition by comprehensively promoting economic, social, spatial, environment and institutional development. Rather than merely seeing development as an increase in capital infrastructure to be provided by the public sector, the development philosophy underlying the SDGs recognizes that a sustainable development agenda needs to provide the means for sustained progress, in the form of continued economic growth, innovation, job opportunities, and livelihoods. As such, "development" is not just a matter of capital development, but a matter of improved recurrent service provision—in diverse areas such as education, health, and so on—in order to achieve sustainable human development.

This means that the recurrent activities of LGIs should be explicitly recognized and costed in order to achieve an initial estimate of overall LGI expenditure needs. At the simplest level, in order to prevent the pitfall of the "build, neglect and rebuild" development approach, one might set a per-resident spending requirement for the operation and maintenance of the LGI's infrastructure equal to 20% of the LGI's annual capital infrastructure needs.[13] In order to arrive at an overall recurrent expenditure needs estimate, an additional amount should further be set aside for the funding needs of local administration.[14]

Table 3.1 captures an overview of estimated LGU Expenditure Needs. Subject to all the caveats already noted, Table 3.1 suggests that LGIs in Bangladesh have an aggregate annual expenditure need of roughly BDT 330 billion.

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[12] For Upazila Parishads, a small set-aside of US$ 5 per person was equally divided between Upazila-level infrastructure needs and support of recurrent Upazila-level services.

[13] This is an extremely low estimate, as the infrastructure in need of operation and maintenance is cumulative over time.

[14] The minimum operating cost estimate (for staffing and other administrative cost) was based on a total staff of 10 per UP; 10 staff per UZP; and 1 LGI staff per 1000 residents for urban LGIs.

Table 3.1 Estimated LGI Expenditure Needs					
	UP	**Pourashavas**	**CC**	**Upazila**	**Total**
Number	4538	329	11	492	--
Population (mn)	115.4	20.2	19.7	132.8	--
Avg pop	25,433	61,406	1,794,892	270,020	--
Per Capita Exp. Needs					
Admin	2.12	8.79	8.79	0.33	--
O&M	2.00	4.00	6.00	2.50	--
Capital	10.00	20.00	30.00	2.50	--
Per Capita (US$)	14.12	32.79	44.79	5.33	--
Per Capita (BDT)	1,200.47	2,787.49	3,807.49	453.33	--
Total Exp. Needs (BDT mn)					
Expenditure Needs	138,554.6	56,314.1	75,174.3	60,225.0	**330,268.1**

3.2 A high-level overview of local government finances

Table 3.2 presents a high-level overview of LGI finances in Bangladesh, based on the detailed analysis of local government finances in the subsequent sections of this report. The top-level overview suggests that, in aggregate, local government spending in Bangladesh is substantial: across the four main types of LGIs, a total of BDT 175.5 billion was spent in FY 2017/18 (the latest year for which comprehensive data is available). Local government revenues account approximately BDT 47.7 billion, or roughly one-quarter of local government funding. In turn, intergovernmental fiscal transfers account for BDT 137.6 billion, or close to three-quarters of LGI spending.

Table 3.2 Overview of LGI Finances, 2017-18					
	Unit	**UP**	**PSA**	**CC**	**UZP**
Total Expenditures	**Tk million**	**59,677.3**	**30,934.2**	**74,191.7**	**10,651.7**
Total OSR	Tk million	3,877.6	13,061.1	22,649.3	8,151.7
Total Transfers	Tk million	61,498.9	20,633.8	53,010.7	2,500.0
Per Capita Expenditures	**Tk per person**	**517.1**	**1,531.2**	**3,757.7**	**80.2**
Share funded by OSR	Percent	6.5	42.2	30.5	76.5
Share funded by block grant	Percent	13.9	23.8	4.0	23.5
Share funded by other transfers	Percent	89.2	42.9	67.4	-
Units	LGI	4,538	329	11	492
Population	million	115.4	20.2	19.7	132.8

Source: Prepared by authors (drawing on Table 4.5; Table 5.5; Table 6.5; and Table 7.1).

However, Table 3.2 suggests that local government expenditures are not distributed evenly among local government types, and that their funding mix can also be quite different. For instance, Union Parishads represent about BDT 60 billion in spending, or roughly BDT 500 per person. Pourashavas accounted for BDT 31 billion in spending, or roughly BDT 2000 per person, while City Corporation spending amounted to BDT 74 billion in the same year, which is close to BDT 3800 per person. Upazila Parishads contributed about BDT 10.7 billion in public spending (or only about 80 Taka per person). These issues are analyzed in greater detail in the analytical sections in Part II of this report.

3.3 What is the size of LGIs' fiscal gap?

Table 3.2 suggests that in FY 2017/18, a total of BDT 175.5 billion was spent by LGIs. However, when compared to total Government of Bangladesh spending for the same year (BDT 3,171 billion), LGI spending only accounts for roughly 5 percent of public sector spending. Internationally, and even among this LDCs, this places Bangladesh among the least devolved countries (OECD/UCLG 2019).

The perspective changes when LGI spending is compared to the amount of spending that is deconcentrated to the Upazila-level administration as shown in Table 2.2 (BDT 343 billion). Compared to this localized deconcentrated spending, local government spending is substantial: in fact, LGI spending represents close to 50 percent of Upazila-level administration spending.[15] This fact should not be taken as evidence of adequate local government funding; as discussed earlier this high ratio is due to the fact that the Bangladeshi public sector is highly reliant on vertical sectoral programs, rather than on deconcentration.

Comparing the current picture of local government finances to the estimated LGI fiscal needs will show the extent of the fiscal gap. Although the costing methodology is admittedly rough, if anything, the assumptions used for the purpose of developing the LGI expenditure needs estimate in Table 3.2 are generally quite conservative.

Table 3.3 compares the difference between the estimate expenditure needs and the actual expenditure levels for FY 2017/18. The table shows an overall fiscal gap for LGIs of 46.9 percent, suggesting that almost of half of LGI expenditure needs currently go unfunded. These estimates provide an initial idea of the scale of LGI expenditure needs and confirm the perception that LGIs in Bangladesh are currently (considerably) underfunded.[16] Based on the underlying assumptions made in order to arrive at this figure, it appears that the funding gap is generally larger for rural local governments and for pourashavas than it is for City Corporations.[17]

Table 3.3 Estimated LGI Fiscal Gap

	UP	Pourashavas	CC	Upazila	Total
Number	4538	329	11	492	--
Population (mn)	115.4	20.2	19.7	132.8	--
Avg pop	25,433	61,406	1,794,892	270,020	--
Total Exp. Needs (BDT mn)					
Expenditure Needs	138,554.6	56,314.1	75,174.3	60,225.0	**330,268.1**
Expenditures (2017/18)	59,677.3	30,934.2	74,191.7	10,651.7	**175,454.9**
Fiscal Gap (percent)	56.9	45.1	1.3	82.3	**46.9**

[15] Note the difference between Upazila administration spending (spending by the deconcentrated administrative unit) and the spending done by the Upazila Parishad (the LGI unit).
[16] A more granular and detailed estimate of LGI expenditure needs would better reveal the types and extent of different expenditure needs,
[17] The fiscal gap for Upazilas may be overstated due to incomplete available of data for Upazila Parishad finances.

There are three avenues available for filling this fiscal gap at the local level; i) enhanced own source local revenue mobilization; ii) intergovernmental fiscal transfers; and iii) local borrowing and other financing mechanisms. The “correct” answer on how to fill the local fiscal gap may differ for different types of local government institutions and depends on the nature and mix of the functions that they provide or support.

The explanation of the size of the local funding gap—and potential options on how to fill this gap—should be informed by concerns about the institutional weaknesses at the local level related to their budgeting and financial management capacity, their limited capacity with respect to inclusive and participatory local decision-making; weak spatial and capital investment planning; and other weaknesses in local administration (e.g., weak procurement; limited transparency and weak accountability). When LGIs are weak, it may be more appropriate for central government institutions to act on their behalf.

At the same time, however, central government interventions are not likely to be as inclusive or responsive as more localized decisions. As such, it is important for LGD to consider on an ongoing basis how to strengthen the institutional capacity of LGIs, so that they can best support the achievement of sustainable development goals in their local communities.

PART II – ANALYSIS OF LOCAL PUBLIC FINANCES

4. Local Expenditures

4.0 Overview

Little comprehensive analysis of local government expenditures in Bangladesh has been done. While there are numerous studies that rely on sample analysis and case studies, the ambition of the current document was to represent as accurate a view as possible of expenditures for all local government institutions in Bangladesh.

As such, for each local government type, the analysis in this section examines:

- The total volume of expenditures, based on an aggregation of actual available local government expenditure data;
- The composition of local expenditures: recurrent versus capital expenditures, the amount of local spending directed towards different sectors or functions.
- The distribution of expenditures across local government jurisdictions. Given the fact that different LGIs have different population sizes, the comparison of expenditures is done in per capita terms.

The analysis in this section generally focuses on FY 2017/18, the latest year for which comprehensive data is available. Population data for each LGI was drawn from the Census 2011 (whenever possible) and adjusted for population growth up to 2018.

The analysis below finds that Union Parishads engaged in about BDT 60 billion in spending in FY 2017/18, or roughly 500 Taka per person. In the same year, Pourashavas accounted for close to BDT 31 billion in spending (roughly 1500 Taka per person), while City Corporations accounted for BDT 74 billion in spending per year (close to 3800 Taka per person). In addition, Upazila Parishads engaged in an additional BDT 10.7 billion in spending (BDT 80 per person). In aggregate, across the four main types of LGIs, a total of BDT 175.5 billion was spent in FY 2017/18.

4.1 UP Expenditures

In 2011, there were 4543 Union Parishads (UPs) in Bangladesh (BBS 2014).[18] Although there is a mismatch between the extensive responsibilities assigned to UPs by the legal framework and the actual situation on the ground, the role played by the UP in the government structure and in terms of delivering services to the community should not be underestimated. People turn to the UP as an entry point into accessing public sector and request a variety of services that are not otherwise available. Construction and maintenance of rural infrastructures such as roads, bridges and culverts is *de facto* the most important role of UPs, and most of the UPs perform remarkably well with respect to the implementation of schemes (especially those funded by LGSP). The involvement of UPs in the delivery of social services, if any, is extremely limited. For instance, UP support to public health services is so limited that building a footpath to a community clinic is considered by some UPs as a public health expenditure (Ahmed et al 2014).

The most comprehensive data source on UP finances is the data collected from UPs through the Local Government Support Project 3 (LGSP3) under LGD. The LGSP3 data set contains basic information

[18] The exact number of UPs fluctuates slightly from year to year, as new UPs are created (thus increasing the number) while others are combined and/or converted into Pourashavas (thus decreasing the number).

(including total expenditures; total own source revenue collections; and block grant allocations) for 4,538 Union Parishads. While these figures do not reflect audited local government accounts, for all intents and purposes, this data set should be understood to present a reasonable reflection of UPs finances for the entire universe of UP in Bangladesh. When adjusted for the estimated rural population growth from 2011-2018, these 4,538 UPs had a population of 115.4 million residents.[19,20]

Volume. Table 4.1 presents the basic volume of UP expenditures based on the data collected by the LGSP3 team in total; on average (per UP); and in per capita terms.

Table 4.1 Union Parishad Expenditures

Union Parishads	Unit	Expenditures (Tk)	Expenditures (USD)
Total	million	59,677.3	702.1
Average	million per UP	13.2	0.2
Per Capita	Per person	517.1	6.1

Note: N=4538; Population: 115,416,796.
Source: Prepared by authors based on LGSP3 data.

Although UP expenditures represent a large sum of money in aggregate (close to BDT 60 billion, or roughly US$ 700 million), in per capita terms, UP spending per person is relatively little (around BDT 500 per person), especially when compared to other LGIs, as noted below.

Composition. Through the UP Operations Manual, LGD provides UPs guidance on the process of community involvement in prioritizing local spending.

To the extent that expenditures are funded from different grants or funding sources, UPs must adhere to limitations on how resources must be spent. For instance, Block Grants (BBG/PBG) provided under LGSP 3 can generally be used for any purpose or functions that are assigned to UPs as per the UP Act 2009, with exceptions of spending or schemes on a “negative list”.[21] As such, UPs are able to use their block grant allocations to finance a wide range of developmental expenditures / small-scale infrastructures across the sectors of transportation, water supply, health, education, etc., including construction and/or rehabilitation of rural roads, bridges, installation of community-managed tube wells, piped water supply, and rehabilitation of pre- and primary, secondary schools and colleges, etc. Anecdotal evidence suggests that in practice, 75 percent of block grants are spent on physical infrastructure.

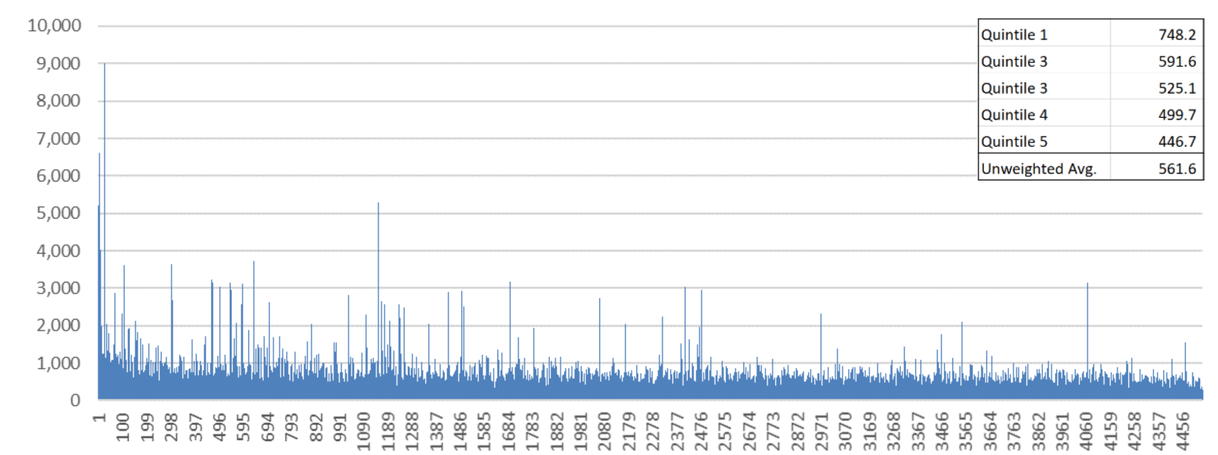
However, the LGD/LGSP3 data collection and reporting efforts at the UP level do not provide a detailed analysis of the sectoral composition of UP expenditures. In fact, the available data does not allow us to even consider recurrent spending versus capital spending being done at the UP level. The absence of annual reports on sectoral spending by UPs makes it incredibility difficult to sensitize central ministries (other than LGD) to the potential that UPs offer as a platform for community engagement and front-line service delivery coordination in support of localizing the SDGs, or disaster/emergency response.

[19] This is less than the projected national population, as it does not include the population living in urban areas (pourashavas and City Corporations).
[20] The rural growth rate was determined based on BBS (2015: Table 4.9).
[21] There is a list of schemes that will not be implemented by BBG/PBG, e.g., salaries, wages and benefits for UP Members or staff, schemes that are linked with any religious institutions, and schemes that have negative environmental/social impacts.

Distribution/incidence. Figure 4.1 ranks all UPs from least populous (number 1) to most populous (number 4538) on the horizontal axis and presents the per capita expenditures for each UP in Bangladesh.

The pattern revealed in Figure 4.1 reflects an even distribution of UP expenditures, with an (unweighted) average expenditure of BDT 561 per capita. Although there are some UPs that spend considerably more per person than average (i.e., the "peaks" in the graph), relatively speaking, there are few of these outliers.[22] In total, 95 percent of UPs have spending below BDT 1000 per person, with only 5 percent of UPs having an expenditure level exceed twice the average.

Figure 4.1 Per Capita UP Expenditures, 2017/18 (BDT per person)



Source: Prepared by authors based on LGSP3 data.

The distribution further shows that smaller (less populous) UPs have slightly higher per capita expenditure level across each of the five quintiles (see inset), which may be reflective of scale economies in UP administration and service delivery. This finding is a bit surprising, however, because we would expect more populous UPs—all else equal—to be more urban in nature, and therefore, have both a larger tax base as well as a higher demand for public services. The overall decline in per capita spending (as population increases) seems expected, however, with the smallest UPs in the first quintile (population between 1,000-17,400 residents) on average receiving roughly 150 percent of the per capita allocation received by the largest UPs in the fifth quintile (population ranging from 32,000 – 310,000).

4.2 Pourashava Expenditures

While fewer in number than UPs, Pourashavas tend to be more populous and have stronger economic bases. They should be in a better position to perform effectively as a local government institution as compared to the rural UPs. Unfortunately, however, development partner support to urban development has been much more fragmented over the past 20 years, with individual development partners typically selecting a subset of urban local governments to support, rather than providing support across the universe of urban local government institutions as a whole (as has been the case under LGSP1-3 for UPs). This has resulted in a dearth of consistent local government finance data on urban local governments.

[22] Naturally, these outliers require further detailed investigation. Doing so, however, is beyond the scope of this exploration.

As such, from January-March 2020, LGD and the study team worked with a range of stakeholders and local officials to collect budget documents from as many pourashavas as possible. Budget documents for FY 2019/2020 generally report actual (rather than budgeted) revenue and expenditure figures for two years prior (i.e., 2017/18). While the data collection efforts were hindered somewhat by the global outbreak of COVID-19, the team was able to collect local government finance data for 175 out of 329 pourashavas. When adjusted for the estimated urban population growth from 2011-2018, these 175 pourashavas had a population of 12.7 million residents.[23]

Based on this sample of pourashavas, total pourashava expenditures (as well as revenues and transfers) were extrapolated for the full universe of 329 pourashavas, representing an estimated urban population of 20.2 million. Extrapolations were done separately for each category of municipalities (A, B or C) to minimize the impact of sample selection bias. While the resulting aggregate figures are an estimate based on unaudited local government accounts, this data set should be understood to present a reasonable reflection of pourashavas finances in Bangladesh.

Volume. Table 4.2 presents the aggregate (estimated) volume of pourashavas expenditures based on the data collected by the study team in total; on average (per pourashava); and in per capita terms.

Table 4.2 Pourashava Expenditures

Union Parishads	Unit	Expenditures (Tk)	Expenditures (USD)
Total (Estimated)	million	30,934.2	363.9
Average	million per PSA	94.0	1.1
Per Capita	Per person	1,531.2	18.0

Note: N=329 (Sample: 175); Population: 20,202,466.
Source: Prepared by authors based on LGD/Pourashava data.

In aggregate, pourashava expenditures represent around BDT 30 billion in LGI spending. While this is only half as much as total UP spending, in per capita terms, pourashavas on average spend roughly BDT 1500 per resident, which is three times greater than the amount of UP spending per person.

Composition. Given that the format by which pourashavas report their budget summaries provides no functional breakdown of spending, the pourashava dataset does not allow a detailed analysis of the functional or sectoral composition of pourashava expenditures.

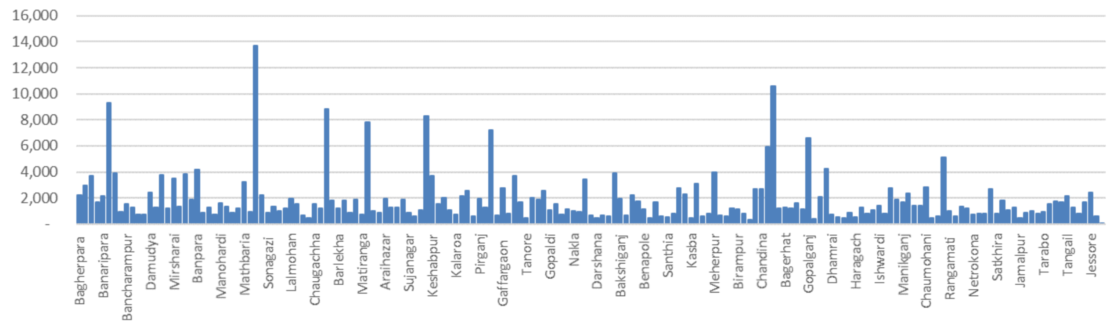
An analysis of the available data suggests that on average, 37.5 percent of pourashava spending is dedicated to recurrent expenditures versus 62.5 percent on development expenditures. It appears that Category A pourashavas tend to devote more of their budget on recurrent spending (operation and maintenance) than Category B or C pourashavas (38.0% versus 36.4% and 31.8%, respectively). The reason for this is not clear. It is possible that there is a greater need for operation and maintenance in larger, more established municipalities, or whether this breakdown is driven by the size and composition of the municipal funding mix of different types of municipalities.

Distribution/incidence. Figure 4.2 presents per-capita pourashava expenditures across Bangladesh. Individual pourashavas differ in their level and pattern of expenditures. Similar to the distributional

[23] The urban growth rate was determined based on BBS (2015: Table 4.9).

analysis of UP expenditures in the previous section, Figure 4.2 ranks the 175 pourashavas for which detailed information was available from least to most populous on the horizontal axis and presents the per capita expenditures for each pourashava.[24]

Figure 4.2 Per Capita Pourashava Expenditures, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/Pourashava data.

The expenditure distribution revealed in Figure 4.2 reflects a relatively even distribution of pourashava expenditures, with an (unweighted) average expenditure of BDT 1876 per capita. Although there are a handful of pourashavas that spend considerably more per person than average (i.e., the “peaks” in the graph), relatively speaking, there are few of these outliers. In contrast, two-thirds of pourashavas spend between BDT 500-2000 per person.

4.3 City Corporation Expenditures

City Corporations form a class of local government institutions that is separate from municipalities (Pourashavas). In the recent past, some Pourashavas (single or in combination of two or three) have been upgraded to the status of city corporations. As a result, there are now 11 City Corporations in Bangladesh, with a combined estimated population of 19.7 million residents (2018).[25]

As large, economically well-positioned local government authorities, one would expect that they are granted the most significant functional responsibilities. In practice, however, City Corporations actually have fewer powers than pourashavas. Despite the fact that the City Corporation Act assigns the responsibility for development planning and master planning to the City Corporation, special development authorities have been created by the central government for four of the city corporations for the purpose of providing urban planning services relating to infrastructure and site development for housing, commercial and industrial use.[26] They are semi-autonomous and autonomous bodies run by their

[24] The most populous is Bagherpara municipality, estimated 2018 population: 11,632 residents, least populous Bagura municipality: estimated 2018 population 562,635

[25] These include: Barishal CC (460,620); Comilla CC (475,851); Rajshahi CC (631,070); Sylhet CC (673,278); Khulna CC (930,761); Gazipur CC (967,340); Narayangonj CC (995,360); Rangpur CC (1,117,679); Chittagong CC (3,623,468); Dhaka South CC (4,489,405) and Dhaka North CC (5,378,979).

[26] These four special development authorities form the Rajdhani Unnayan Kartripakkha (RAJUK) for Dhaka City Corporation, the Chittagong Development Authority (CDA), the Khulna Development Authority (KDA) and the Rajshahi Development Authority (RDA).

respective chairmen and boards, with most members of these boards appointed by (central) government. Similarly, water and sanitation services in City Corporations tend to be provided by Water Supply and Sewerage Authorities (WASA), which are also run by chairmen and boards who are deputed by the central government to carry out their assigned responsibilities. Given the relatively small number of City Corporations, the study team was able to collect budget documents from each of them.

Volume. Table 4.3 presents the basic volume of City Corporation expenditures based on the data collected by the study team in total; on average (per CC); and in per capita terms.

Table 4.3 City Corporation Expenditures

Union Parishads	Unit	Expenditures (Tk)	Expenditures (USD)
Total	million	74,191.7	872.8
Average	million per CC	6,744.7	79.3
Per Capita	Per person	3,757.7	44.2

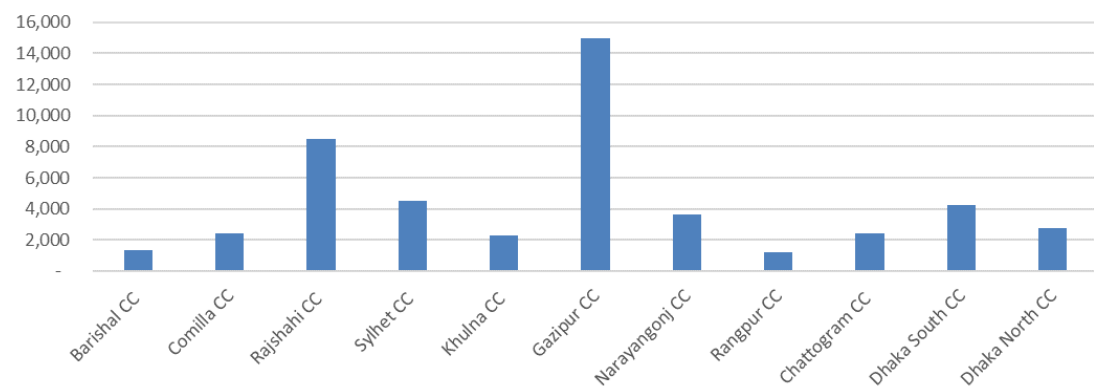
Note: N=11; Population: 19,743,811.
Source: Prepared by authors based on LGD/CC data.

City corporation expenditures represent the largest amount of total spending relative to than any other type of LGI: CCs spend in excess of BDT 74 billion. This is the case even though a far greater number of people reside in rural areas than in the largest urban centers of Bangladesh (115.4 million versus 19.7 million). As a result, in average per capita terms, City Corporation spending far exceeds spending in other types of LGI, with an average CC spending close to 3,800 Taka per resident.

Composition. The available data does not readily allow a detailed analysis of the sectoral/functional composition of CC expenditures. Furthermore, it should be noted that the statistics presented here do not include spending by any of the WASAs, not of the RAJUK/CC Development Authorities. It should be noted that 21.8 percent of total CC spending reflects “revenue expenditures” (i.e., recurrent expenditures), whereas 78.2 percent of CC is spending reflect development costs.

Distribution/incidence. Figure 4.3 shows per capita expenditures for each of the 11 CCs, with the CCs ranked by population size (from smallest to largest). It shows a fairly unequal expenditure pattern among city corporations, with Rajshahi CC (BDT 8,465) and Gazipur CC (BDT 14,964) spending considerably more in per capita terms than other CCs (unweighted average of all CCs: BDT 4,383 per person). While some of these differences can be explained by greater own source revenue collections (as further explored in Section 5.3), own source revenues are *not* the main driver for these expenditure differences.

Figure 4.3 Per Capita City Corporation Expenditures, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/CC data.

In per capita terms, the expenditure differences between Dhaka North and Dhaka South (BDT 2,742 versus 4,212, respectively) are substantial—especially given the fact that Dhaka was a single CC until 2011.

4.4 Upazila Parishad Expenditures

In contrast to UPs, Pourashavas and City Corporations, the Upazila Parishad (UZP) is an intermediate tier local government. The Upazila Parishad (UZP), which stands midway between the UP and the (non-elected) Zila Parishad, is effectively the newest of all elected local government institutions, having been re-activated as an elected local government body in 2009.[27] In addition to a directly elected Chairperson, the Upazila Parishad Act, as revised in 2009, now provides for two popularly elected vice-chairs - one male and one female. UP chairs as well as chairs of municipalities falling within the jurisdiction of an Upazila hold ex-officio membership of the UZP. Provisions have also been made for indirectly elected women members.

In 2011, there were 545 Upazila and Thana jurisdictions in Bangladesh (BBS 2014). Since Thanas (the subdivision within City Corporations) do not have elected Upazila Parishads, the number of Upazila Parishads is slightly lower. The exact number of Upazila Parishads in Bangladesh fluctuates slightly from year to year, as new Upazilas are created from time to time (thus increasing the number) while others are combined and/or converted into City Corporations (thus decreasing the number). Bangladesh these 492 UZPs had a population of 132.8 million residents.[28]

The Upazila Parishad is legally responsible for planning, promotion and execution of a wide range of development programs/projects/schemes, although its *de facto* responsibilities are limited by the resources at its disposal (Ahmed 2015; LGD 2019). Many of the development interventions pursued by

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[27] Sometimes, Upazila Parishads are referred to as a rural local government institution, and therefore presented under the same "umbrella" as Union Parishads. While Upazila Parishads tend to be dominated by the rural elected officials in each Upazila jurisdiction, in theory (and by law), UZPs cover both rural and urban areas within their territorial jurisdictions.

[28] This is less than the projected national population, as it does not include the population living in City Corporations.

the UZP are primarily implemented by the deconcentrated line departments. As such UZP projects and schemes can include a wide range of sectors. In this context, effective coordination—both with Upazila administrative departments as well as with the UPs and municipalities within its jurisdiction—will be critical for the Upazila Parishad to achieve its development goals.

Consistent fiscal data for Upazila Parishads is scarce. While LGD was able to provide data on annual ADP allocations for all 492 UZPs, it does not appear that LGD has a systematic approach for collecting UZP financial statements. In addition to the ADP allocations, the Upazila wing of LGD collected own source revenue data for a sample of 73 Upazila Parishads. The available data allowed an estimate of Upazila Parishad expenditures to be prepared as the sum of the ADP Block Grant spending for each Upazila plus the spending of the (extrapolated) Upazila own revenues.

The estimation procedure used for this analysis produces an under-estimate of Upazila Parishad expenditures, as Upazila Parishads spend resources from UGDP (Box 4.1) as well as potentially from other development projects. While these estimates are less solid than the expenditure information available for other LGIs, the estimated expenditure levels nonetheless give some insight into the relative role of Upazila Parishads compared to other LGIs in Bangladesh. This caveat should be noted throughout this report in interpreting all UZP-related financial figures.

Box 4.1 Upazila Governance and Development Project (UGDP)

The Upazila Parishad (UZP) Act was enacted in 1998; elections of Upazila Parishad (UZP) were properly carried out in 2009, 2014 and 2019. The Annual Development Program (ADP) has been gradually enhanced for the Upazilas. Line departments at Upazila level were formally transferred under Upazila Parishad by the Local Government (Upazila Parishad) Act amended in 2011 (although in reality, line departments continue to be part of their respective ministries, with only limited deference being paid to their subordination under the Upazila Parishad). Compared to the Union Parishads, the process of decentralization and governance improvement at the Upazila level had many challenges. At the same time, linkage between Union Parishad and UZP remains weak particularly in development coordination. Considering the above-mentioned situation of local governance at Union and Upazila levels, the Government of Bangaldesh with support from JICA initiated a comprehensive and integrated project, named Upazila Governance and Development Project (UGDP), worth of BDT 10.59 billion BDT (i.e., around US$ 144 million), to strengthen local governance, focusing particularly on Upazila as a pivotal institution to enhance the capacity of Upazila Parishads to deliver more effective and responsive public services to citizens by providing additional development funds, and a series of capacity development opportunities to concerned stakeholders.

UGDP is designed to provide financial assistance to all 492 Upazilas as its target. However, it is being done in phases. The fund allocation under UGDP is carried out based on the performance assessment of all Upazilas as per selection criteria to be selected for UGDP. In other words, only selected Upazilas can submit proposal of sub-projects, and will receive financial assistance. In the first year, 104 Upazilas were selected, whereas in the second year 200 Upazilas, third year 300 Upazilas, and in the current year i.e., financial year 2019-2020, total 357 Upazilas were selected for UGDP. Each selected Upazila receives 50 Lakhs BDT annually from UGDP in addition to their regular budget from ADP. Maximum 40 Lakhs BDT is being used for improving services and good governance; whereas, maximum 10 Lakhs BDT is being utilized for capacity building of Upazila stakeholders. This will nearly double the present government ADP grant to any Upazila per year. The learning of UGDP implementation will support LGD for revisiting policies in regard to Upazila Parishad as necessary.

Volume. Table 4.4 presents the basic volume of UZP expenditures based on the data and estimation process as described above. As with the other expenditure tables in this section, the table shows aggregate expenditures, as well as average spending (per UZP); and overall Upazila Parishad spending in per capita terms.

Table 4.4 Upazila Parishad Expenditures

Union Parishads	Unit	Expenditures (Tk)	Expenditures (USD)
Total	million	10,651.74	125.3
Average	million per UZP	21.6	0.3
Per Capita	Per person	80.2	0.9

Note: N=492; Population: 132,849,989.
Source: Prepared by authors.

Although the total amount of UZP expenditures (BDT 10.6 billion) is roughly half of total pourashava spending, when the amount is considered in per capita terms, this spending only amounts to BDT 80 per person, which is considerably less than the other LGI types.

Composition. The UZP data does not allow a detailed analysis of the composition of UZP expenditures. With respect to the utilization of its ADP resource, however, the Upazila Operational Manual gives following indicative sectoral allocation:

Sector	Allocation
1. Agriculture and small-scale irrigation:	
(a) Agriculture	10%
(b) Fishery and Livestock	5%
(c) Small and Cottage industries	5%
2. Physical Infrastructure:	
(a) Transport and Communication	15%
(b) Public Health	15%
3. Socio-economic infrastructure:	
(a) Improvement of quality of education	10%
(b) Health and Social Welfare	15%
(c) Youth, Sports and Culture	10%
(d) Other	5%

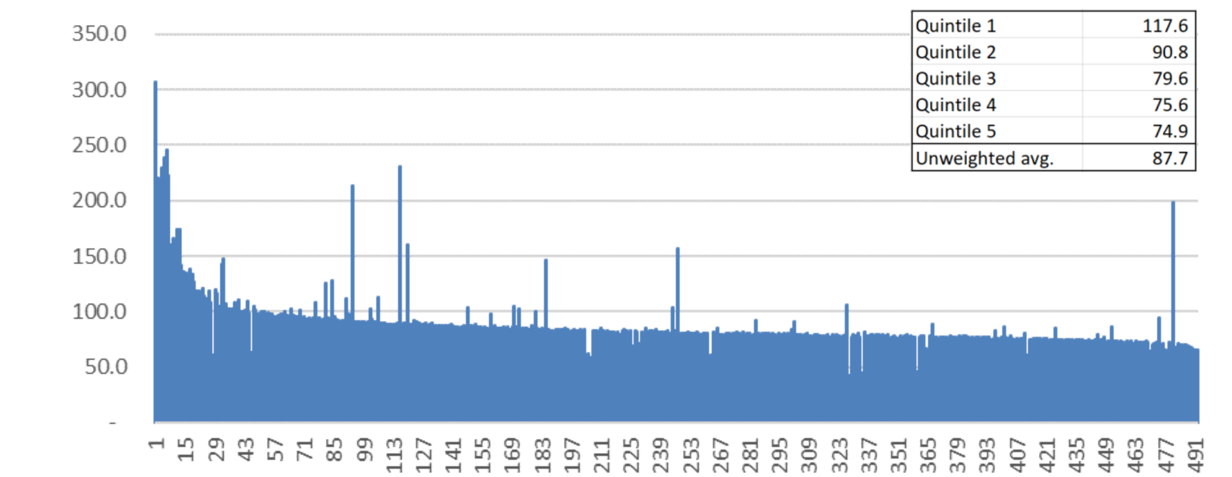
Anecdotal evidence as well as case studies suggest that planning and budgeting guidelines issued by LGD are often not being followed by local officials (e.g., LGD/JICA 2015). In the absence of systematic reporting and monitoring of Upazila finances, LGD is not in a good position to enforce its regulations.

In practice, it appears that rather than spending their resources on larger-scale Upazila-wide plans and priorities, most Upazila Parishads simply divide up their budget resources among their respective UPs. Analysis of Upazila Parishads budgets further suggests that some, if not most, of the Upazilas currently spend their ADP resources without considering indicative sector-wise ceilings given by the guidelines, with the vast majority of ADP resources being allocated towards road infrastructure and educational scholarships (LGD/JICA 2015).

Distribution/incidence. As with the previous distributional analyses, Figure 4.4 ranks all Upazilas from least populous (number 1) to most populous (number 492) on the horizontal axis and presents the per capita expenditures for each UZP in Bangladesh.

The pattern revealed in the figure reflects an even distribution of UZP expenditures, with an (unweighted) average expenditure of BDT 88 per capita. Although there are some UZPs that spend up to four times more per person than average, this variation is relatively modest. However, the limited variation in estimated Upazila expenditures may be driven in part by the relatively crude method for estimating Upazila expenditures (as more detailed data for Upazila Parishad expenditures were unavailable).

Figure 4.4 Per Capita UZP Expenditures, 2017/18 (BDT per person)



Source: Prepared by authors based on LGSP3 data.

4.5 Summary and Tentative Conclusions

Having a "big picture" overview of LGI expenditures in Bangladesh—as well as having a detailed understanding of the composition and distribution of expenditures for each local government type—is critical to understanding the role of each type of local government institution in the overall local government system, and in understanding how each type of local government institution might be better contribute to Bangladesh's ambition to achieve sustainable development at the frontlines in every village, town and city. In fact, merely presenting the volume, composition and distribution of LGI expenditures in basic bar diagrams—as done above—allows nation-level policy makers to readily see the levels and distributions of LGI expenditures—both within and across different LGI types.

Based on the preceding analyses of expenditures for Union Parishads, Pourashavas, City Corporations, and Upazila Parishads, Table 4.5 presents a comparative overview of LGI expenditures. The table suggests that in total, across all four LGI types analyzes, total LGI spending for FY 2017/18 amounted to BDT 171.5 billion, with Union Parishads and City Corporations contributing the largest shares of spending.

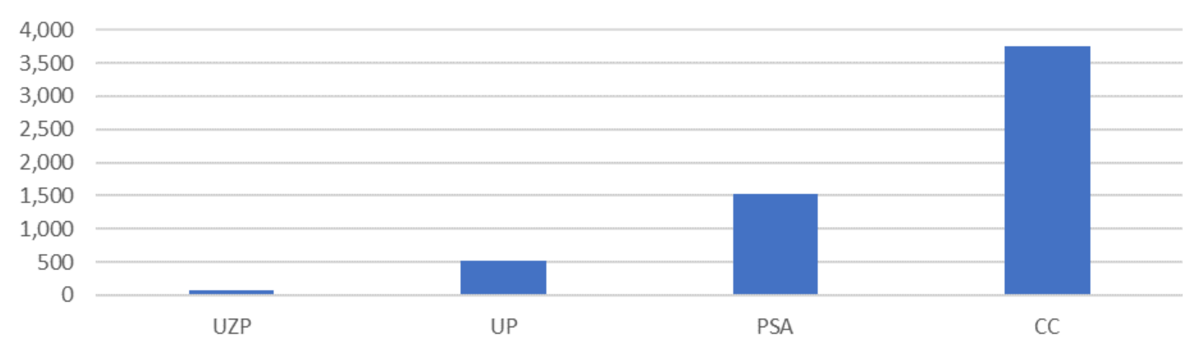
Table 4.5 LGI Expenditures, 2017-18

	Unit	UP	PSA	CC	UZP
Total	Tk million	59,677.3	30,934.2	74,191.7	10,651.7
Average	Tk million per LGI	13.2	94.0	6,744.7	21.6
Per Capita	Tk per person	517.1	1,531.2	3,757.7	80.2
Percent of Total LGI Exp.	Percent	34.0	17.6	42.3	6.1
Units	LGI	4,538	329	11	492
Population	million	115.4	20.2	19.7	132.8

Source: Prepared by authors based on data sources cited in previous tables.

Figure 4.5 presents a comparative overview of LGI expenditures in per capita terms. It is important to consider not only the total (aggregate) amount of these expenditures for each type of LGI, but also to consider the amount in per capita (per person) terms: after all, the per capita amount reflects the average amount of resources used by each local government type to provide services to their residents. In the per capita analysis of expenditures, it is striking that Union Parishads—on average—only spend little more than BDT 500 per resident, whereas City Corporations—on average—spend almost eight times as much per resident.

Figure 4.5 Average per capita expenditures, by LGI type (FY 2017/18)



Source: Prepared by authors based on data sources cited in previous tables.

In a way, this finding should come as no surprise. The Government of Bangladesh has acknowledged that rural areas are lagging behind urban areas, and is seeking to rapidly upgrade service delivery coverage and quality in rural areas through the "My Village, My Town" initiative.

However, the above finding raises an important question about rural LGIs spending: why do they spend so much less per person than larger urban LGIs. It is not clear if City Corporations really have a per-capita expenditure need that is ten times higher than rural LGIs, or if the difference may be due to variation in own source revenue collections. Another possibility is that populous LGIs could receive more grant resources per person. Finally, the link between the variation in LGI expenditures and their respective institutional capacities and abilities to spend is also not clear. These questions are explored in Sections 5 and 6 as well as in the concluding section of this report.

5. Local Own Source Revenues

5.0 Overview

Local government revenues in Bangladesh are extensively studied in Bangladesh as part of individual case studies and through analyses of samples. For instance, a recent overview of local government revenues (Musleh 2017) notes that LGIs in Bangladesh are provided with several types of own revenue sources, but that they are yet to achieve adequate revenue raising capacity and performance. Musleh (ibid) summarizes the existing literature by noting that local revenue performance is limited due to a lack of commitment to meaningful revenue decentralization by both central as well as local governments. As a result of this lack of commitment, the tax structure is highly centralized with LGIs being assigned narrow tax bases, while local officials generally lack a strong political incentive to collect own source revenues. This makes it difficult for LGIs to collect considerable own source revenues (OSR). This is particularly true for many rural LGIs, as many Union Parishads tend to have a limited economic activity and a small tax base. Furthermore, there are instances of tax competition between governments at different levels, including between Upazila Parishads and Pourashavas.

The overview of local government revenues recognizes, however, that these conclusions are actually being drawn in the absence of a comprehensive quantitative analysis of LGI revenues, as at the national level, there is no overall record of local revenue performance (Musleh 2017). It is in this regard that this report seeks to contribute.

The analysis below finds that only roughly a quarter of all LGI spending is funded from own source revenues. As expected, however, revenue collection patterns vary greatly between different types of LGIs. Based on the latest year for which data are consistently available (2017/18), Union Parishads collected less than BDT 4 billion in OSR in FY 2017/18, or which represents BDT 34 per person. In the same year, Pourashavas accounted for close to BDT 13 billion in local revenue collections (roughly BDT 650 per person), while City Corporations accounted for BDT 22.6 billion in own source revenues (close to BDT 1150 per person). Upazila Parishads accounted for an additional BDT 8.1 billion in local revenues (BDT 76.5 per person). In aggregate, across the four main types of LGIs, a total of BDT 47.7 billion was collected in local own source revenues in FY 2017/18.

5.1 UP Own Source Revenues

Data on Union Parishad own source revenues for each UP (FY 2017/18) is contained in the data set prepared by LGSP3 (see Annex).

Volume. Table 5.1 presents the basic volume of UP revenues based on the data collected by the LGSP3 team in total; on average (per UP); and in per capita terms. The table also expressed UP own source revenues as a share of UP expenditures.

Compared to UP expenditures (which amounted to around BDT 60 billion), UP own source revenues reflect a much more modest sum: UP revenues amount to only BDT 3.9 billion, or only BDT 34 per person. In other words, UP OSR is only adequate to fund about 6.5 percent of UP expenditures.

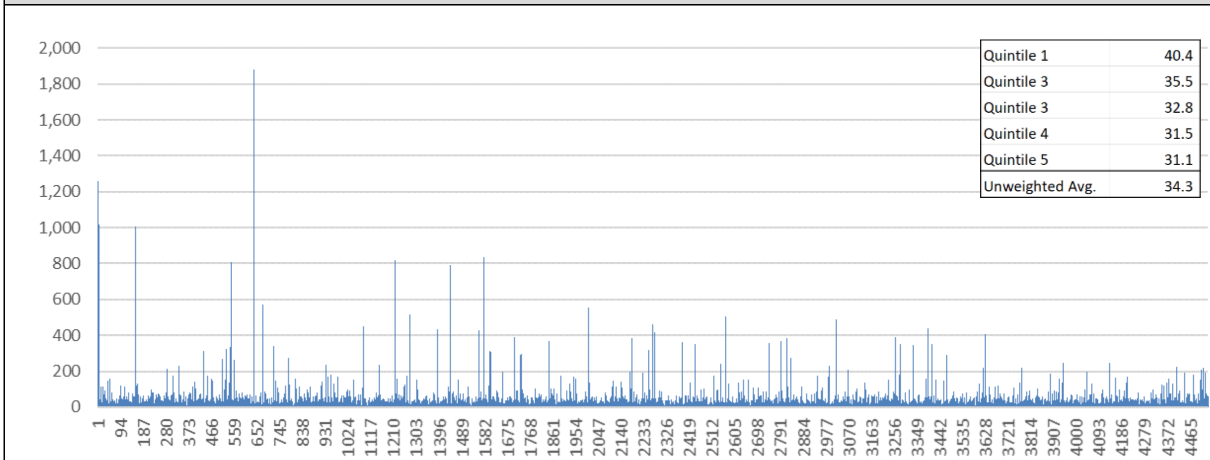
Table 5.1 Union Parishad Own Source Revenues			
Union Parishads	**Unit**	**Revenues (Tk)**	**Revenues (USD)**
Total	million	3,877.6	45.6
Average	million per UP	0.9	0.0
Per Capita	Per person	33.6	0.4
Share of expenditures	Percent	6.5	6.5
Note: N=4538; Population: 115,416,796. Source: Prepared by authors based on LGSP3 data.			

It is important not to prejudge the reasons for low revenue collections by UPs. It is not uncommon to blame low UP revenue collections on the lack of political will at the local level. While limited revenue effort by local officials may be contributing to low own source revenue collections, other contributing factors may be at play. For example, the economic basis of the rural areas tends to be much smaller compared to more urban areas, which lowers the overall amount of potential revenue to be collected, while UPs are generally not assigned high-yielding or easy-to-collect revenue sources.

Composition. The LGD/LGSP3 dataset does not allow a detailed analysis of the composition of UP revenues. A discussion of the composition of UP revenues—and the specific challenges faced in revenue administration at the UP level—are dealt with in the existing literature and fall beyond the scope of the current review.

Distribution/incidence. As with the analysis of local expenditures, there is no reason to expect that different UPs would collect the same—average—amount of own source revenues per capita. After all, neither economic activity nor the taxable bases are distributed equally across the national territory. Furthermore, revenue collection efforts are not identical across different UP jurisdictions. While a detailed analysis of revenue capacity and revenue effort is beyond the scope of this review, Figure 5.1 ranks all UPs from least populous (number 1) to most populous (number 4538) on the horizontal axis and presents the per capita revenues for each UP in Bangladesh.

Figure 5.1 Per Capita UP Own Source Revenues, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/LGSP3 data.

The pattern revealed in Figure 5.1 reflects an uneven distribution of UP revenues. Although the (unweighted) average revenue collections equal only BDT 34 in OSR per person, there are a few dozen UPs that collect a greater amount of revenue per person than average. Most UPs (85 percent) collect between BDT 1-50 per person in own source revenues. Even within the range of UPs collecting below BDT 50 per person, there is considerable variation in UP revenue collections, resulting in a relatively high overall Coefficient of Variation for per capita UP revenue collections (CoV = 1.8). Were the distribution of revenue collection among UPs more equal, we would otherwise expect the CoV value to be closer to zero.

The distribution further suggests that smaller (less populous) UPs collect slightly greater revenue per capita than more populous UPs across each of the five quintiles (see inset). While the decrease is only minor (from BDT 40.4 per person in the lowest population quintile to BDT 31.1 per person in the highest population quintile), the distribution is a bit surprising: as a rule, more populous UPs tend to have disproportionately greater economic activity and tend to be more urban in nature. The absence of an increasing distributional pattern suggests that UPs perform more or less the same in terms of revenue collections regardless of local economic conditions, and possibly indicates that smaller UPs exert somewhat higher revenue collection effort.

5.2 Pourashava Own Source Revenues

The analysis of Pourashava own source revenues relies on the budget reports collected from a sample of 175 Pourashavas, which reflected actual local revenue collections for FY 2017/18.

Volume. Table 5.1 presents the total estimated volume of UP revenues based on available data, according to extrapolation by municipal classification (A, B and C). In addition, the table presents average revenue per pourashava as well as local revenue collections in per capita terms. For comparative purposes, the table also expressed pourashava own source revenues as a share of pourashava expenditures.

Table 5.2 Pourashava Own Source Revenues

Union Parishads	Unit	Revenues (Tk)	Revenues (USD)
Total (Estimate)	million	13,061.1	153.7
Average	million per PSA	39.7	0.5
Per Capita	Per person	646.5	7.6
Share of expenditures	Percent	42.2	42.2

Note: N=329 (Sample: 175); Population: 20,202,466.
Source: Prepared by authors based on LGD/Pourashava data.

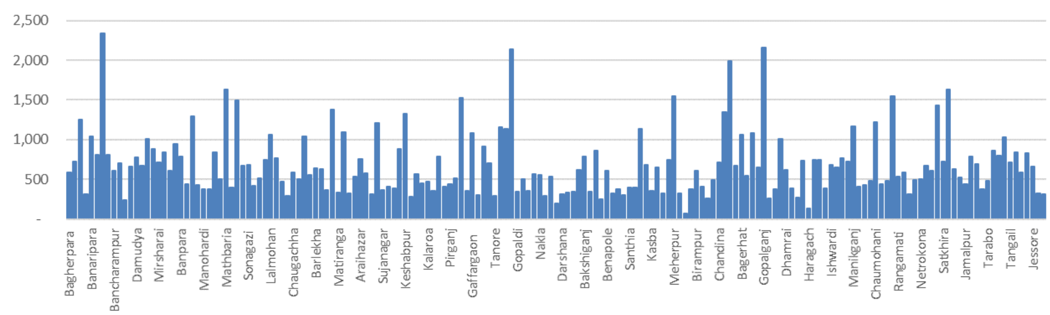
Compared to UP revenues (which amounted to around BDT 3.8 billion), pourashava own source revenues reflect a much more substantial sum: pourashavas collected a total of BDT 13.1 billion in own source revenues in 2017/18. Pourashavas on average collected close to 650 Taka per resident. In per capita terms, this reflects close to a 20-fold greater level of OSR collection in pourashavas when compared to UPs. Pourashava own source revenues in total reflect 42 percent of pourashava spending.

There are a few caveats for the interpretation of the local revenue collection levels identified here. For example, much of the difference in revenue collections between pourashavas and UPs may be explained by the fact that municipalities have a much stronger tax base than rural areas. Unfortunately, no accurate data are available for the local taxable bases of different pourashavas (or UPs). In fact, Bangladesh is no exception in this regard: international experience suggests that data availability on local tax bases is extremely limited.

Composition. A discussion of the composition of pourashava revenues—and the specific challenges faced in municipal revenue administration—are dealt with in the existing studies and fall beyond the scope of the current review.

Distribution/incidence. Figure 5.2 considers municipal revenue collections across the sample of 175 pourashava for which OSR collection data are available. Pourashavas are again ranked from least populous (on the left) to most populous (on the right).

Figure 5.2 Per Capita Pourashava Own Source Revenues, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/Pourashava data.

When compared to the variation in municipal expenditures as well as when compared to variation in UP revenues, Figure 5.2 reflects relatively less variation in per capita pourashava own source revenues. While some pourashavas collect greater revenues (per capita) than others, these differences in performance among pourashavas cannot be objectively compared because each municipality's revenue base is currently unknown.

5.3 City Corporation Own Source Revenues

Volume. Table 5.3 presents the volume of City Corporation revenues based on the data collected by the research team for each of the 11 City Corporation. The level of own source revenues is presented in total (in BDT millions); the overall average per City Corporation); in per capita terms; as well as reflecting CC own source revenues as a share of CC expenditures.

Table 5.3 City Corporation Own Source Revenues

Union Parishads	Unit	Revenues (Tk)	Revenues (USD)
Total	million	22,649.3	266.5
Average	million per CC	2,059.0	24.2
Per Capita	Per person	1,147.2	13.5
Share of expenditures	Percent	30.5	30.5

Note: N=11; Population: 19,743,811.
Source: Prepared by authors based on LGD/CC data.

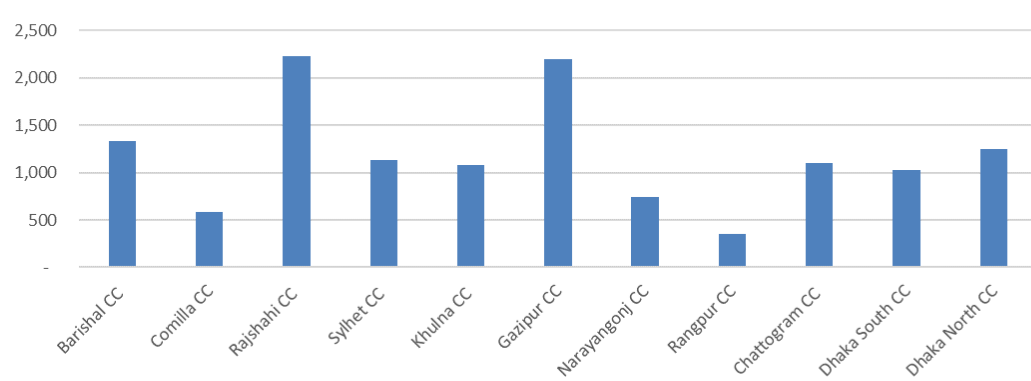
Even though there are few City Corporations (11 CCs, versus 329 pourashavas and 4538 UPs), they represent the majority of local OSR collections, as City Corporations collectively collect BDT 22.6 billion in own source revenues. In per capita terms, City Corporation revenues are twice as high as pourashavas revenues. As noted before, it is difficult to make any judgements about whether the amount of revenue collected is appropriate without knowing the underlying distribution of economic activity.

OSR revenues fund 30 percent of City Corporation expenditures, which is a smaller percentage than pourashavas (42 percent). Given the difference in population, economic diversity and tax base, it may seem that city corporations have the potential to have a greater reliance on self-funding. Global experience is inconsistent on this topic. For example, the City of London, which most likely has the second-largest concentration of financial institutions and wealth in the world actually funds merely 31.2 percent of its expenditures from own sources, while relying on intergovernmental fiscal transfers for 68.8 percent of its expenditures (Slack 2016). For Berlin, the comparable figure is 30.3 percent.[29]

Composition. The available revenue data for OSRs allows no detailed analysis of the composition of CC revenues.

Distribution/incidence. Similarly, it is difficult to interpret the differences in the distribution of revenue collections highlighted in Figure 5.3 without knowing the economic/tax base of each city.

Figure 5.3 Per Capita City Corporation Own Source Revenues, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/CC data.

Figure 5.3 shows per-capita City Corporation OSRs, with City Corporations arranged according to population (less populous on the left to more populous on the right). As economic activity tends to be concentrated in more populous and more densely populated urban areas, we would expect City Corporation revenues to increase from left to right. However, the data do not show this pattern, suggesting that either that some of the smaller cities have a more robust economy than the larger

[29] Other major cities, such as Paris, Tokyo, Madrid and New York collect tend to be more reliant on own source revenues (around 75-85 percent). However, many of these cities have been assigned major revenue powers, such as the collection of local taxes on corporate income and personal income.

metropolitan areas, or that some of the smaller cities exert a higher degree of collection effort (or possibly both).

5.4 Upazila Parishad Own Source Revenues

There is little systematic documentation and analysis (other than studies based on small samples) about the collection and utilization of Upazila own source resources. Data on Upazila Parishad own source revenues was available for a sample of 73 UZP (FY 2017/18). For analytical purposes, the total amount of UZP own source revenues was imputed for the remaining UZPs based on the sample average of per capita OSR.

Volume. Based on these computations, Table 5.4 presents the estimated volume of UZP revenues (in BDT millions); the average estimated revenue per Upazila; and Upazila Parishad revenues expressed in per capita terms. The table also presents UZP own source revenues as a share of total UZP expenditures.

Table 5.4 Upazila Parishad Own Source Revenues

Upazila Parishads	Unit	Revenues (Tk)	Revenues (USD)
Total	million	8,151.7	95.9
Average	million per UZP	16.6	0.2
Per Capita	Per person	61.4	0.7
Share of expenditures	Percent	76.5	76.5

Note: N=492; Population: 132,849,989.
Source: Prepared by authors.

The estimation suggests that UZP revenue collections amount to almost BDT 8.2 billion overall, or BDT 61.4 per person. While this is higher than the level of UP revenue collections per person (BDT 34), this amount is well below the amount of OSR collected by urban local governments.

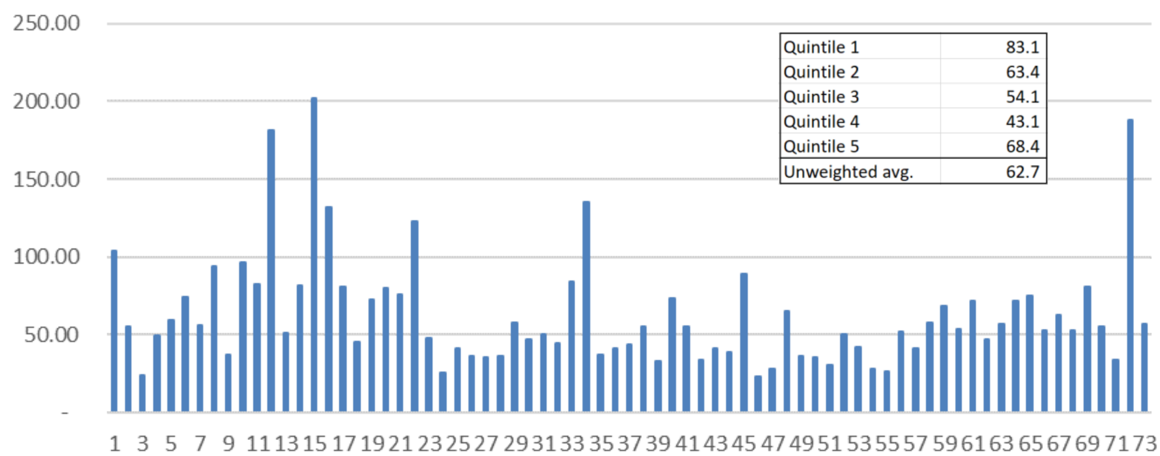
Nonetheless, the table suggests that this relatively small UZP OSR sum is a major funding source for UZPs, funding almost exactly three-quarter of UZP expenditures.[30]. Given the limited and contested revenue base of UZPs, it is not clear whether this high ratio reflects inadequate funding of Upazila Parishads through other funding mechanisms (i.e., transfers).

Composition. The available revenue data for UZPs unfortunately does not allow a detailed analysis of the composition of UZP revenues.

Distribution/incidence. As with the analysis of revenue collections by other LGIs, we should not expect to find every UZP collecting the same amount of own source revenues per capita. Figure 5.4 shows the variation in revenue collections at the Upazila level based on the 73 Upazila Parishads for which OSR data were available, presenting per capita revenues for each of these UZPs ranked from least populous to most populous.

[30] This share may be overstated due the limited availability of accurate financial data for UZPs, which may underestimate grant funding received by UZPs

Figure 5.4 Per Capita UZP Own Source Revenues, 2017/18 (BDT per person)



Source: Prepared by authors based on revenue data for a sample of 73 UZPs.

The pattern revealed in Figure 5.4 reveals considerable variation in UZP revenues (per person) around an (unweighted) average of BDT 67 per person in OSR. It shows a reasonable amount of variation in revenue collections, with some Upazila Parishads collecting up to 4-6 times more per person than others. There does not appear to be a strong correlation between OSR collections and population, although it appears that less populous UZPs generally collect somewhat more per person than more populous UZPs. Future studies should examine the exact cause for this variation.

5.5 Summary and Tentative Conclusions

The findings about OSR collections by the four different types of LGIs are summarized in Table 5.5.

As expected, the table shows that the larger and more urban local government institutions collect disproportionately greater own source revenues. As noted previously, however, it is difficult to assess the extent to which this progression reveals an increase in the actual local tax burden vis-à-vis an increase in the taxable base of different types of LGIs.

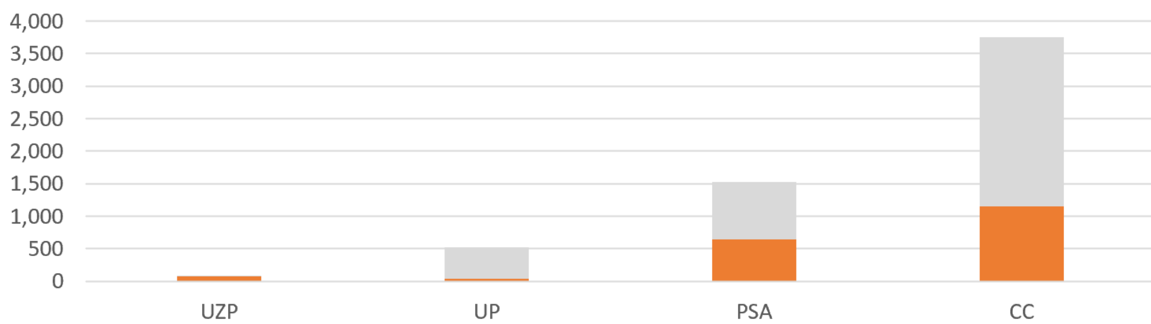
Table 5.5 LGI Revenues, 2017-18

	Unit	UP	PSA	CC	UZP
Total	Tk million	3,877.6	13,061.1	22,649.3	8,151.7
Average	Tk million per LGI	0.9	39.7	2,059.0	61.4
Per Capita	Tk per person	33.6	646.5	1,147.2	76.5
OSR as Percent of Exp.	Percent	6.5	42.2	30.5	76.5
Percent of Total LGI Rev.	Percent	8.1	27.4	47.4	17.1
Units	LGI	4,538	329	11	492
Population	million	115.4	20.2	19.7	132.8

Source: Prepared by authors based on data sources cited in previous tables.

An additional concern is raised by the comparison is the position of Upazila Parishads: to the extent that tax base of Upazila Parishads overlaps with the tax base of Pourashavas (and the UPs), the tax burden on pourashavas taxpayers may be even higher due to this administrative coverage.

Figure 5.5 Average per capita own source revenues, by LGI type (FY 2017/18)



Note: The orange bar reflects average per capita own source revenues. For comparative purposes, the grey bar indicates the per capita level of LGI expenditures.
Source: Prepared by authors based on data sources cited in previous tables.

Finally, the increase in per capita own source revenues between different local government types is actually *smaller* than the increase in per capita expenditures. This suggests that the intergovernmental fiscal transfer system plays a critical role in the observed resource distribution patterns. Earlier, in the section on local expenditures, Table 4.5 indicated that UP expenditures per person are considerably smaller than pourashava expenditures, while in turn, per capita pourashava expenditures are at least twice as small as those of City Corporations (with per capita expenditure levels of BDT 517, BDT 1,531 and BDT 3,757, respectively). As shown in Figure 5.5, own source revenues only provide a partial explanation for the pattern: whereas Pourashavas spend BDT 1000 more per person, the average revenue increase between these two types of local governments is only BDT 600 per person. Similarly, whereas City Corporations on average spend BDT 2,000 more per resident than pourashavas, they only collect BDT 500 more per resident in own revenues. For these LGIs, fiscal transfers are an important means to fill the expenditure gap.

6. Local Intergovernmental Fiscal Transfers

6.0 Overview

Intergovernmental fiscal transfers are often referred to as the third pillar of local government finance: after all, transfers (or grants) are the primary source of funding to fill the gap between a locality's expenditure needs on one hand and the locality's own revenue sources on the other hand. In many countries around the world, intergovernmental fiscal transfers provide the majority of funding for local governments (OECD/UCLG, 2019). This is clearly also the case in Bangladesh.

The most commonly known source of LGI Transfers are ADP Block Grants and Special Grants to LGIs provided by LGD (see Table 2.3). However, in addition, other central ministries provide different types of other transfers to LGIs in order to support specific interventions within their respective sectors. While there are some basic similarities in the way that transfers fund the four different types of LGIs, there are some important differences, which are discussed below.

6.1 UP Transfers

Over the past 20 years, UP transfers have seen considerable reform. Whereas previously, the ADP Block Grant was channeled to UPs through the administrative apparatus at the Upazila level (which often caused block grants to be received in a delayed and incomplete manner), an important innovation of LGSP1-3 was the direct transfer of UP Block Grants from LGD to the UPs bank account (Box 6.1).

Box 6.1 Formula-based UP Block Grants

Prior to LGSP, the intergovernmental fiscal transfers to UPs had been made in a conventional way that lacked transparency, predictability and efficiency: (i) transfers were made through intermediate administrative levels, i.e., Upazila Parishads, in the absence of any direct link established between UPs and the central government; (ii) the grant funding pool was determined by the central government in an ad hoc and opaque manner; (iii) rules/conditions that govern the allocation of funds among the eligible UPs were not equitable, and were not used as an instrument to incentivize improved governance and accountability performance; and (iv) degree of discretion for utilization of funds often was conditional or funds were ear-marked. The drawbacks of such a system included a cumbersome process resulting in delays in the transfer of funds, and the potential for manipulation of fund flows by political and institutional interference, which in turn resulted in unpredictability in the receipt of funds at the local level.

Building on the UNCDF/UNDP-supported Sirajganj Local Governance Development Funds Project, consecutive phases of LGSP have successfully established a formula-based intergovernmental fiscal transfer system to UPs that ensures enhanced transparency and predictability. The key features of the system are: (i) formula-based BBGs, based on population and area, transferred directly to UP bank accounts from the central government in two tranches/year; (ii) consistency with GoB's Medium Term Budgetary Framework (MTBF) by announcing in advance three years' indicative BBG ceilings to facilitate forward planning; (iii) annual financial audits and performance assessments of all 4,550 UPs conducted by private audit firms, as a condition for access to funds; (iv) performance-based grants to incentivize UPs for better performance in governance, accountability, and financial management; (v) full discretion in the use of funds that allows local expenditure and investment priorities to be determined by communities, within the parameters of their legal mandate; and (vi) the flexibility to rollover unspent balances of BBGs/Performance Based Grants (PBGs) to subsequent fiscal years.

Source: World Bank (2017).

Data on the transfers received by Union Parishad for FY 2017/18 is contained in the data set on UP finances collected by LGSP3, as described in the Annex. Although the LGSP3 data identifies the disbursement of Basic Block Grant allocations, it does not provide a detailed breakdown of other transfers. As such, the allocation of Other UP Transfers is estimated as Total Income excluding Own Source Revenues and the BBG Allocation.

Volume. Table 6.1 presents the basic volume of UP transfers received by UPs—for Basic Block Grants; other grant; and total grants—in aggregate; on average (per UP); and in per capita terms. The table also expressed UP transfers as a share of UP expenditures.

Table 6.1 Union Parishad Transfers

UP BBG Allocation	Unit	Transfers (Tk)	Transfers (USD)
Total	million	8,287.7	97.5
Average	million per UP	1.8	0.0
Per Capita	Per person	71.8	0.8
Share of expenditures	Percent	13.9	13.9
Other UP Transfers			
Total	million	53,211.22	626.0
Average	million per UP	11,725.70	137.9
Per Capita	Per person	461.04	5.4
Share of expenditures	Percent	89.2	89.2
Total transfers			
Total	million	61,498.90	723.5
Average	million per UP	13,551.98	159.4
Per Capita	Per person	532.84	6.3
Share of expenditures	Percent	103.1	103.1

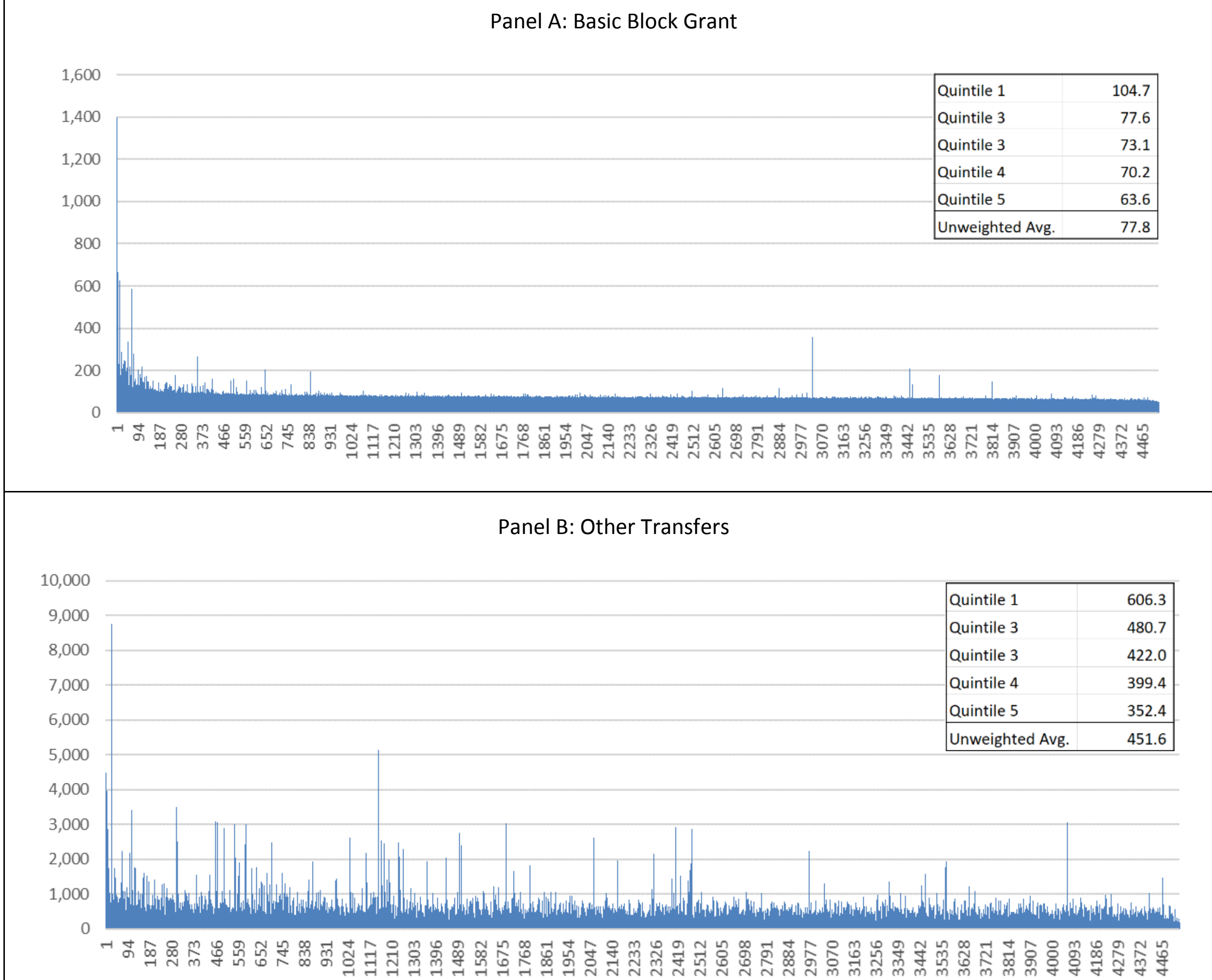
Note: N=4538; Population: 115,416,796.
Source: Prepared by authors based on LGSP3 data.

In aggregate, UP transfers for the latest year available amount to BDT 61.5 billion. Surprisingly, Total UP Transfers slightly *exceed* reported UP expenditures (which amounted to around BDT 60 billion). There are two possible reasons for this. First, the estimate for "Other UP Transfers" likely over-estimates transfers, as the estimate may also include balances carried forward from previous years. Second, it is possible that not all transfers are spent in the year in which they were received, resulting in a carry-forward of 10-, 20- or more percent of transfers and revenue into the subsequent financial year.

Composition. The LGSP3 dataset provides some detail on the composition of UP Transfers, as the data set reports BBG separate from the (estimate of) "Other UP Transfers." The main observation here is that the BBG—while receiving most attention from LGD, DPs, local officials and in the media—only represents a very small share of transfers received by UPs (around 15 percent).

Distribution/incidence. As with the previous graphs, Figure 6.1 ranks all UPs from least populous to most populous on the horizontal axis and presents the per capita transfers for each UP in Bangladesh. Panel A of the Figure presents the Basic Block Grant (BBG) allocations for FY 2017/18, while Panel B presents the allocation of all other transfers. Per capita averages by population quintile are reported in the insets.

Figure 6.1 Per Capita UP Transfers, 2017/18 (BDT per person)



Source: Prepared by authors based on LGSP3 data.

The pattern revealed in Panel A of Figure 6.1 reflects an extremely even distribution of the UP Basic Block Grant. This results from the fact that the BBG allocation is done consistently on a formula basis, thus limiting the ability of officials to provide arbitrary allocations—for instance, based on political influence or administrative favoritism—to different UPs. The slight decline in average per capita BBG allocations is due to inclusion of land area as an allocation factor (weighted 10 percent) in addition to population (90 percent) in the allocation formula.

By contrast, the pattern revealed in Panel B of Figure 6.1 reflects (a) that "Other UP Transfers" account for the major share of UP funding, and (b) that "Other UP Transfers" are distributed with considerably greater variation than BBG allocations.

It should be noted that many Other UP Transfer are discretionary, earmarked, sectoral allocations made by different central ministries through the hierarchical budget process, much in the same was that ADP Block Grants were allocated to UPs under the previous system (Box 6.1). While the discretionary nature of these grants allows different central ministries to be responsive to the specific needs of different UPs, it is (virtually) impossible for central officials to determine the relative expenditure needs of over 4,500 Union Parishads. Yet, because many of these funds are not formula-based; they do not flow directly from the center to the UP bank account; and are not given the same level of social and external scrutiny as block grants. Due to this, the greater variation of allocations—including due to potential political influence or administrative favoritism—should come as no surprise.

6.2 Pourashava Transfers

Volume. Table 6.2 presents the volume of transfers received by pourashavas, indicating that (on average) municipalities receive two-thirds of the funding needed for their expenditures from intergovernmental transfers.

Table 6.2 Pourashava Transfers

BBG Allocation	Unit	Transfers (Tk)	Transfers (USD)
Total (Estimated)	million	7,372.0	86.7
Average	millions per PSA	22.4	0.3
Per Capita	Per person	364.9	4.3
Share of expenditures	Percent	23.8	23.8
Other Transfers*			
Total (Estimated)	million	13,261.7	156.0
Average	millions per PSA	40.3	0.5
Per Capita	Per person	656.4	7.7
Share of expenditures	Percent	42.9	42.9
Total Transfers*			
Total (Estimated)	million	20,633.8	242.8
Average	millions per PSA	62.7	0.7
Per Capita	Per person	1,021.3	12.0
Share of expenditures	Percent	66.7	66.7

Note: N=329 (Sample: 175); Population: 20,202,466.
Source: Prepared by authors based on LGD/Pourashava data.

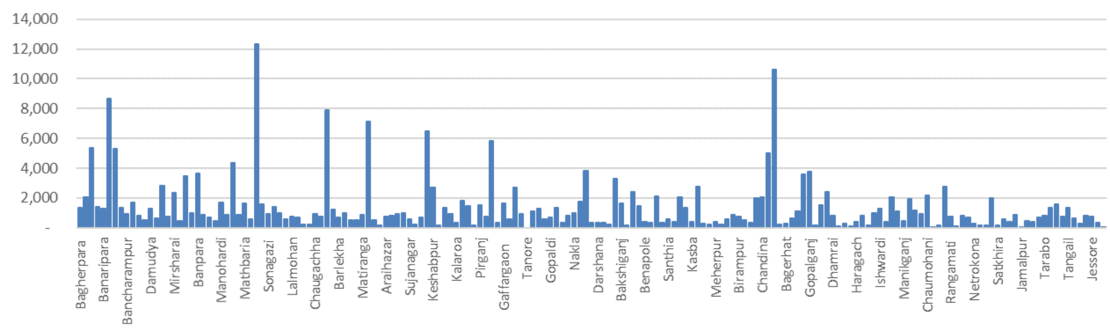
In per capita terms, pourashavas receive slightly over BDT 1,000 per resident in transfers from the central government, which is twice greater than the average grant allocation received by UPs. It is unclear what the cause of the greater per capita allocation is, given that UPs are known to have lower revenue potential. The greater per capital allocation may reflect a perception that municipal residents have higher expenditure needs, or the fact that development partners disproportionately support urban programs.

The greater allocation per person to municipal local governments could also simply be the result of the fact that there are many fewer urban residents than rural residents in Bangladesh. For example, even though the total grant pool for municipalities is only one-third of the size of the UP transfer pool (and thus looks smaller), the per person allocation is nonetheless greater in urban areas. The possible horizontal fiscal imbalance may persist because politicians from urban areas are often better connected, as well as a perception that urban local governments are more "deserving" because rural local governments tend to be administratively weak.

Composition. As with UPs (albeit perhaps to a slightly lesser extent), the category of “other transfers” plays a more important role than (block and general) government grants. In total, pourashavas report receiving twice more in “other transfers” than in block/general grants.

Distribution/incidence. Figure 6.2 presents he distribution of transfers to pourashavas, with pourashavas again sorted from least populous (left side) to most populous (right side) on the horizontal axis. The distribution of per capita transfers does not apper to follow any specific pattern, although there is considerable variation in the allocation of transfers among pourashavas. This is demonstrated by value of the Coeffient of Variation (where “0” represents more equality) computed for the per capita pourashava transfers from Table 6.2 is 1.31, which is greater than the variation in per capita pourashava expenditures or revenues (1.02 and 0.58, respectively). The variation in per capita pourashava transfers is also considerably greater than the variation in per capita UP transfers (CoV=0.69).

Figure 6.2 Per Capita Pourashava Transfers, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/Pourashava data.

6.3 City Corporation Transfers

Finally, the analysis considers intergovernmental fiscal transfers to City Corporations.

Volume. Table 6.4 presents the volume of transfers received by City Corporations. In total, these 11 local government institutions receive BDT 53 billion in transfers. This is not only much more in absolute terms than the other urban local bodies, but also in per capita terms: City Corporations receive more than twice the allocation per resident (BDT 2,223 per person) when compared to pourashavas (BDT 1,021 per resident).

Table 6.4 City Corporation Transfers			
Block Grants	**Unit**	**Transfers (Tk)**	**Transfers (USD)**
Total	million	2,992.4	35.2
Average	million per CC	272.0	3.2
Per Capita	Per person	151.6	1.8
Special Grants			
Total	million	6,129.5	72.1
Average	million per CC	557.2	6.6
Per Capita	Per person	310.5	3.7
Project Grants			
Total	million	43,888.84	516.3
Average	million per CC	3,989.9	46.9
Per Capita	Per person	2,222.9	26.2
Total Transfers			
Total	million	53,010.71	623.7
Average	million per CC	4,819.2	56.7
Per Capita	Per person	2,684.9	31.6
Note: N=11; Population: 19,743,811. Source: Prepared by authors based on LGD/CC data.			

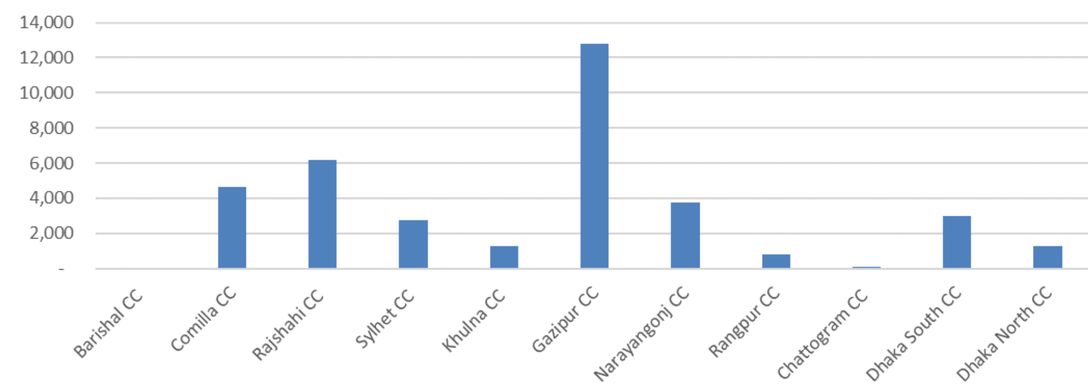
Composition. The breakdown in Table 6.4 suggests that projects grants are by far the main funding source for City Corporations. Even though these are institutionally the most well-positioned LGIs to determine how grants could be used —the central government determines the spending priorities within their jurisdiction based on earmarked project grants.[31]

Distribution/incidence. Figure 6.3 presents the distribution of transfers to each of the eleven City Corporations, with the City Corporations again listed from least populous to most populous from left to right. It shows major variations in the grant allocations received by different City Corporations. However, it is unclear whether the reporting of little of no transfers in Barishal CC and Chittagong CC reflects the actual situation, or whether this is the result of data reporting errors on the part of local officials.

It also not clear what the policy justifications are for one City Corporation to receive multiple times more in grant resources than other city corporations. It would be appropriate for an urban infrastructure financing strategy to inform the distribution of intergovernmental fiscal transfer resources among different types of urban local government institutions, and among the different City Corporations.

[31] These grant figures exclude financial support provided by central ministries to RAJUK/ City Development Authorities and city-level Water and Sewerage Authorities.

Figure 6.3 Per Capita City Corporation Transfers, 2017/18 (BDT per person)



Source: Prepared by authors based on LGD/CC data.

6.4 Upazila Parishad Transfers

Experience shows that much of what the UZP can raise from internal sources is used to for day-to-day expenditure. The main recurrent expenditure heads typically include the honorarium for UZ Chair and vice-chairmen, salary of UZP employees, office procurement, maintenance of UZP buildings and premise, servicing of vehicle of the Upazila Chair, and entertainment (Ahmed et al 2014). The major source of development funding is the block grant of the Annual Development Programme (ADP) from the government. The surplus of the revenue budget is another major source of the development budget (LGD 2019). It is unclear whether UZPs receive in earmarked transfers from sector ministries for specific development projects, and if so what the amount is.

Volume. Table 6.4 presents the basic volume of ADB block grants received by UZPs—in aggregate; on average (per Upazila); and in per capita terms. The table also expressed UZP transfers as a share of UZP expenditures. The table suggests that Upazilas received BDT 2.5 billion in funding in 2017/18, or roughly BDT 20 per person.

Table 6.4 Upazila Parishad Transfers

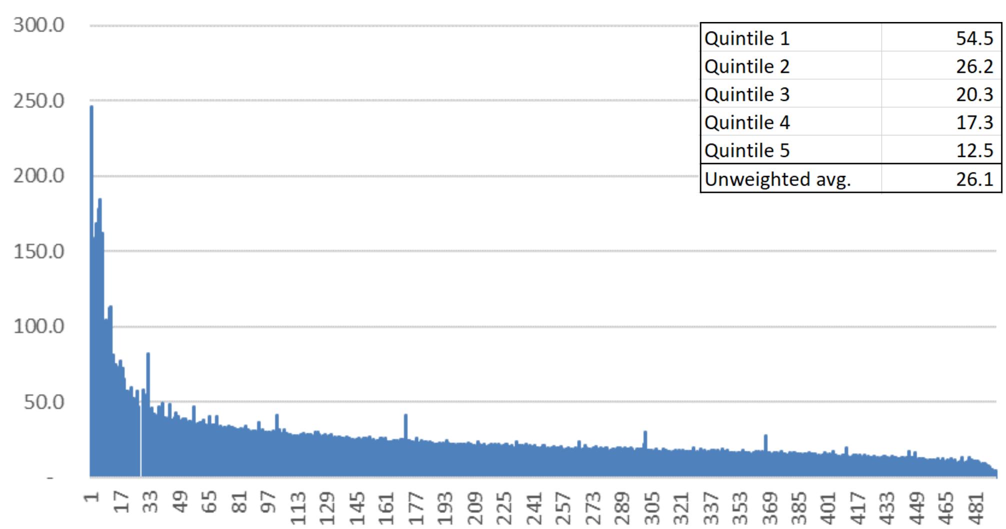
UP BBG Allocation	Unit	Transfers (Tk)	Transfers (USD)
Total	million	2,500.0	29.4
Average	million per UZP	5.1	0.1
Per Capita	Per person	18.8	0.2
Share of expenditures	Percent	23.5	23.5

Note: N=492; Population: 132,849,989.
Source: Prepared by authors.

Composition. Although the data limits the analysis, it appears that Upazila Parishads rely almost exclusively on formula-based block grants, with limited or no Special Grants or other development funding. This contrasts sharply with other LGIs.

Distribution/incidence. Figure 6.4 presents he distribution of ADP Block Grants to UZPs in the standards manner (with LGIs ranked from least populous to most populous on the horizontal axis). Per capita averages by population quintile are reported in the inset.

Figure 6.4 Per Capita UZP Transfers, 2017/18 (BDT per person)



Source: Prepared by authors.

The allocation of the ADP is managed by Upazila Wing of LGD (LGD/JICA 2015). The ADP allocation to the Upazila level is distributed according to a formula based on population (35 percent), land area (35 percent) and fixed amount (30 percent). As a result, the pattern revealed in Figure 6.4 reflects an extremely even distribution of the UP Basic Block Grant in per capita terms. The somewhat large per capita allocations for smaller (less populous) UZPs is because in addition to population and land area, the formula includes a fixed amount (or equal share) of 30 percent to ensure each Upazila receives a fixed minimum amount. As a result, less populous Upazilas receive a higher per capita amount.

6.5 Summary and Tentative Conclusions

Table 6.5 provides an overview of the transfer resources received by different types of LGIs. Perhaps the most consistent and unexpected finding across the different LGIs is the important role played by project grants vis-à-vis the limited role played by formula-based block grants.

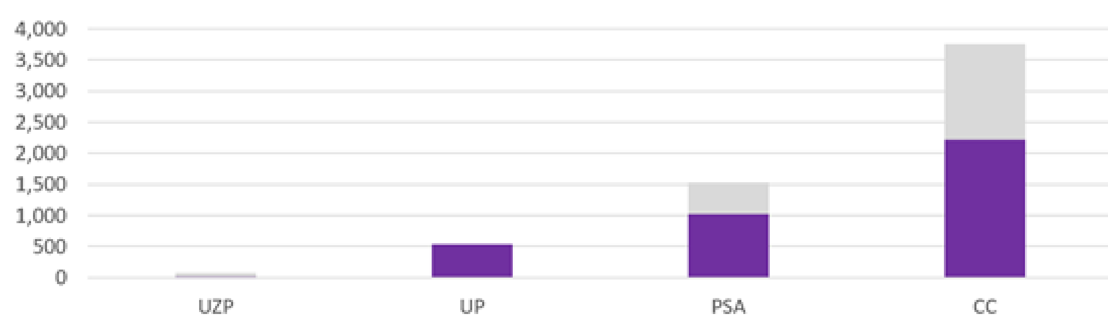
Table 6.5 LGI Transfers, 2017-18					
	Unit	UP	PSA	CC	UZP
Total	**Tk million**	**61,498.9**	**20,633.8**	**53,010.7**	**2,500.0**
o/w Block Grant	Tk million	8,287.7	7,372.0	2,992.4	2,500.0
o/w Other Transfers	Tk million	53,211.2	13,261.7	50,018.3	-
BBG as percent of total	Percent	13.5	35.7	5.6	100.0
Average	Tk million per LGI	13,552.0	62.7	3,989.9	5.1
Per Capita	Tk per person	532.8	1,021.3	2,222.9	18.8
Transfers as Pct. of Exp.	Percent	103.1	66.7	71.5	23.5
Pct. of Total LGI Transfers	Percent	44.7	15.0	38.5	1.8
Units	LGI	4,538	329	11	492
Population	million	115.4	20.2	19.7	132.8

Source: Prepared by authors based on data sources cited in previous tables.

The transfer system also lacks basic recurrent or operational grants to LGIs. Many countries provide a general-purpose grant to local government institutions that funds—among others—the basic operation and administration of the local government. Such general-purpose funding is typically provided to local governments on the implicit understanding that local governments are the level of government that is most visible and closest to the people and coordinates important public services, and therefore, should have adequate funding to manage local affairs in an efficient and responsive manner.

In addition, the practice of providing recurrent funding to local governments—for instance, through a municipal fund and municipal grant—recognizes that local governments (in Bangladesh, as well as elsewhere) are not just platforms for local self-government, but act as inclusive developmental entities and provide public services to the entire local community. Since poor households are unable to financially contribute to the recurrent provision of local public services (and since wealthier local taxpayers may object to their local taxes being diverted away from general local public services toward specific pro-poor local interventions), general-purpose (or recurrent) transfers to local governments can support funding local service delivery to the poor.

Figure 6.5 Average per capita intergovernmental fiscal transfers, by LGI type (FY 2017/18)



Note: The purple bar reflects average per capita transfers. For comparative purposes, the grey bar indicates the per capita level of LGI expenditures.
Source: Prepared by authors based on data sources cited in previous tables.

A final point revealed both Table 6.5 and in Figure 6.5 is that different types of local government receive vastly different levels of intergovernmental fiscal transfers in per capita terms. City Corporations receive multiple times the resources per person when compared to Union Parishads and even compared to pourashavas. Although it is possible that major urban centers have higher needs because infrastructure needs are greater and more costly, at the same time, this burden is shared by a greater number of residents. The pattern reflected in Table 6.5 suggests the possibility that expenditure needs in rural areas and in smaller urban areas are being under-funded.

PART III – FINDINGS AND IMPLICATIONS

7. Findings and implications

7.1 Overview of findings

The preceding sections have analyzed—with considerable detail—the volume, composition and distribution of LGI expenditure, revenues and transfers by type of local government. The main findings are summarized in Table 7.1.

Table 7.1 Overview of LGI Finances, 2017-18

	Unit	**UP**	**PSA**	**CC**	**UZP**
Total Expenditures	**Tk million**	**59,677.3**	**30,934.2**	**74,191.7**	**10,651.7**
Per Capita Expenditures	**Tk per person**	**517.1**	**1,531.2**	**3,757.7**	**80.2**
Share funded by OSR	Percent	6.5	42.2	30.5	76.5
Share funded by block grant	Percent	13.9	23.8	4.0	23.5
Share funded by other transfers	Percent	89.2	42.9	67.4	-
Units	LGI	4,538	329	11	492
Population	million	115.4	20.2	19.7	132.8

Source: Prepared by authors based on data sources cited in previous tables.

A summary of the main findings from the preceding analysis is below:

- ***The current distribution of resources among LGIs appears imbalanced and inequitable***. The scale of increase in the levels of per capita expenditures, revenues and transfers from UPs to Pourashavas up to City Corporations suggests that smaller, rural LGIs as well as many pourashavas are possibly well underfunded. It is highly unlikely that UPs or under-resources pourashavas can deliver a similar level or quality of local services with the resources provided to them. The service deficit in these LGIs will continue to stimulate rural-urban migration.
- ***Despite the perception that LGIs should raise more own source revenue, the contribution made by own source revenue funding—especially in pourashavas—is quite high by global standards***. Given the high level of OSR contributions made by local taxpayers in urban LGIs, we should expect urban LGIs to be oriented towards provided local public infrastructure and services demanded by local taxpayers, and focus less on other important urban functions (such as pro-poor urban services, or support infrastructure expansion for in-migrants due to urban expansion)
- ***The role of formula-based (block) grants is as a share of revenues is relatively minor.*** To the extent that LGD tends to see LGIs through the lens of the formula-based block grants that it provides, it is missing the vast majority of funding that is flowing towards LGIs. This limits the spending discretion of LGIs and may result in non-LGD resources not being tracked with optimal detail by the budget and financial reporting formats prescribed by LGD.
- ***The combination of under-funding and reliance on earmarked grants limits the ability of local governments to be responsive to local priorities.*** Even through LGIs are receiving formula-based development grants, in practice, most transfer funding received by LGIs comes to them in the form of special grants and project grants, which are earmarked for the spending priorities of the central ministries that provide the funding. In addition, own source revenues could be seen as "conceptually earmarked" for the spending priorities of local businesses and other local taxpayers, who would

otherwise resist paying local taxes were the money not spent on matters important to them. In addition, LGIs are expected to fund local administration from their own (often meagre) discretionary own resources. This means that, in practice, LGIs in Bangladesh have extremely little funding discretion to be responsive to the needs and priorities of the local community.

7.2 Implications

The analysis in this document has several implications for the structure and management of the local government system in Bangladesh (Table 7.2). The observations and implications focus on—but are not exclusively limited to—the local government finance system, as decentralized financing arrangements are closely tied to other (including institutional) aspects of local governance in Bangladesh.

Table 7.2 Findings and implications of the analysis

1.	Local government institutions will play an increasingly important role in Bangladesh
2.	Systematic monitoring local government finances should inform policies and reforms
3.	More effective deconcentration will be the key to localization and sustainable development
4.	Institutional capacity of LGIs is a binding constraint on the ability of LGIs to be a catalyst for better local planning, public services and achieving sustainable development. LGI funding is a binding constraint on the institutional capacity of LGIs.
5.	The volume and nature of local government financing should distinguish between local priorities to be pursued by LGIs from own source revenues, and programs that leverage LGIs in pursuit of national objectives
6.	There is a need to elevate the intergovernmental fiscal transfer system
7.	Strengthening local budgeting, local public financial management and local revenue administration

To a large extent, the implications and conclusions drawn from the quantitative analysis in this document are not new. In fact, the results of this analysis to a large extent reconfirm—and provide further support for—recommendations that have been made by earlier policy studies, and lend further support for recommendations contained in strategy documents already prepared by LGD for the development of local government institutions and system.

1. Local government institutions will play an increasingly important role in Bangladesh

Social and economic transformation is moving Bangladesh towards middle-income country status with an increasingly complex economy. While deconcentration surely will—for the time being—remain the main modality for localizing sustainable development (as discussed further below), inclusive and responsive local governance institutions will become increasingly important for the continued economic and social development of the country. However, the ability of LGIs to act as efficient, responsive, and accountable local self-government bodies is currently being hindered quite considerably by the segmentation of the local government system, as well as extensive reliance on earmarked transfers.

The analysis suggests that while the lowest tier of local governments institutions is divided into three types (UPs, Pourashavas and City Corporations), within each category, LGIs are largely managed based on a one-size-fits-all approach. While the binary segmentation into rural versus urban local governments may have been appropriate during the first half of the twentieth century, this segmentation ignores today's reality that information technology and improving transportation infrastructure are connecting even the most rural areas to the global economy; that some pre-urban UPs have a larger population and economic base than mid-size pourashavas; while many rural poor have now relocated to urban centers, thus requiring urban local governments to provide public services to the urban poor. This means that in today's reality, local governments form a continuum, with rural local government facing some of the challenges of urban areas, while urban areas are facing some of the challenges that were previously exclusively dealt with in rural areas. The implication of this finding is that it would be appropriate to consider integrating the legal foundation for local government institutions into a single legal framework, and to increasingly deal with LGIs as being on a continuum, recognizing the diversity of conditions at the local level.

While centrally planned and executed urban and local infrastructure will continue to be an important mechanism for enhancing the well-being of Bangladeshis and the communities where they live,[32] as local social and economic systems develop, it will be increasingly difficult for top-down interventions to respond to the self-generated social and economic dynamism of urban places. This is particularly true in City Corporations, which should have the socio-economic foundation to take on considerable responsibility in spatial and socio-economic development of their cities. Numerous good practices are emerging in Bangladesh where the youth, professional organizations and local business organizations are showing their eagerness to help shape urban spaces as productive and livable cities. There will be a need to foster good practices and experiences with respect to community involvement in planning and implementation, and to create greater space for strong and inclusive local leadership in the development of the country's largest urban areas.

The role of inclusion and greater civic engagement has not only been limited to the largest urban areas: in fact, the review of local government finances suggests that a relatively small amount of money at the UP level (the BBG) has been able to incentivize more inclusive and accountable planning and governance even in the smallest and more rural LGIs.

The role of different types of local government in future public sector interventions should also be considered to the extent that it would be desirable for Bangladesh to redirect and reduce the rate of rural-urban migration. Rapid migration is increasingly imposing congestion cost, pollution, and other hardships on the residents of the greater Dhaka metropolitan areas. Long-run economic growth is likely to benefit from a more balanced spatial-economic approach, which might prevent further overwhelming Dhaka and Chittagong. This points to the critical need for a coherent and proactive urban policy and strategy.

The findings suggest that the current approach to local government financing appears to be largely reactive rather than strategically-focused on development outcomes. For example, grant money is largely flowing to the primary urban areas where people are moving, thereby crowding out the resources flowing to secondary urban centers and rural areas that lack services and infrastructure. If the aim of a national urban policy would be to retain a greater share of the population in secondary and tertiary cities (division HQs and pourashavas) to ensure more balanced long-run economic growth across the country, this would require a reallocation of (financial and other) resources towards smaller urban and rural local government jurisdictions, as well as greater local discretion over those resources at the local level.

[32] For instance, through initiatives such as "My Village, My Town".

2. Systematic monitoring local government finances should inform policies and reforms

The analysis in this report suggests that improved and more systematic monitoring of LGI finances and operations is “low-hanging fruit” in terms of ensuring that LGIs become effective platforms for inclusion and the promoting of sustainable development at the local level. Figure ES.1 provides an overview of LGI finances and an overview of (per capita) LGI expenditure, revenues and transfers across LGI types that is extremely informative with regard to the distribution of LGI financial resources. Similarly, the other figures in this report present the distribution of (per capita) expenditures, revenues and transfers across UPs, pourashavas, City Corporations and Upazila Parishads in a way that is easy for stakeholders and policy makers to understand.

Some of the data used for the analyses in this report are already readily available to LGD, or was be collected with relatively limited effort. What this report has shown is the value-added of basic quantitative analysis of these data. In fact, LGD would no doubt benefit from producing such an analysis on an annual basis, allowing it to track improvements in LGI spending, revenue and transfer levels over time.

Basic improvements in LGI budget and reporting formats would further enhance the analysis provided here. One area where the current report was unable to shed a lot of light was the sectoral composition of local government expenditures. To a large extent, the absence of this information is due to the reporting format imposed on local governments by LGD. It would not be difficult to update the budget preparation and financial reporting formats for LGIs so that their budgets and finances are presented in organizational/functional (sectoral) manner, which would (a) allow citizens to more effectively scrutinize local budgets and finances, and (b) would allow LGD to analyze the distribution and sectoral breakdown of expenditures and transfers for each LGI in a more detailed manner. This would easily allow each sectoral ministry (and other sectoral stakeholders) to see the level of sectoral resources being spent across LGIs, and identify where these resources are being spent.

Accomplishing this improvement in LGI financial reporting would require upgrading the budget and reporting format used by LGIs in a coordinated manner, but doing so would significantly strengthen the link between “finances and functions”, as local governments increasingly become a platform for promoting localized sustainable development.

In fact, LGD could use the Digital Bangladesh / Bangladesh National Portal (https://bangladesh.gov.bd/) to the facilitate collection of budget and financial reports from LGIs by enabling LGIs to upload and share the required documents electronically in the prescribed form on the national portal. This would instantly make all necessary budget documents available not only to LGD staff, but also greatly enhance the transparency of the public sector as a whole by making these documents available to the citizens in each LGI.

3. More effective deconcentration will be the key to localization and sustainable development

Even though local government institutions play an important role in the localization of sustainable development in Bangladesh, the majority of public sector funding that flows to grassroots development and services flows alongside—rather than through—LGI accounts. Unfortunately, the national budget is not effectively structured or organized in manner that allows LGIs to monitor deconcentrated funding to their local jurisdiction: the vast majority of budgetary resources that are used for frontline service provision in Bangladesh is channeled through vertical programs, even in sectors such as education (recall

Table 2.1). Even to the extent that resources are deconcentrated, these resources are managed at the divisional or district (zila) levels, rather than at the Upazila level.

Resources that are managed by national sector ministries—or that flow through divisions and districts—are likely to achieve less value-for-money at the local level when compared to resources that are more directly under the authoritative control of Upazila administration, where front-line services are actually managed. It has been noted in earlier policy studies that Upazila-level jurisdictions have sufficient scale (with an average population of close to 300,000 residents) in order to perform most local service delivery functions efficiently. Indeed, when the subsidiarity principle is applied to the delivery of key public services (education, health services, social safety net program, and so on) in Bangladesh, it is difficult to avoid the conclusion that in the long run, the Upazila level is the lowest level of administration that would be able to administer these functions in an efficient manner (Ahmed 2014). As such, in the long run, it would be appropriate for the Upazila level to become the main platform for the administration of these services (most likely, for the foreseeable future, primarily through deconcentrated Upazila administration.

Here, the national budget structure can learn on important lesson from LGIs: rather than having resources flow hierarchically flow through several administrative levels, LGSP found that a more direct funding flow (combined with more effective management at the local level) is more responsive and efficient. This lesson is equally true for local administration: rather than letting funding trickle down within the national budget structure from the central level through divisions and zila administrations to the Upazila level (where front-line services in key sectors are managed), it would most likely be more effective to establish Upazila-level departments as deconcentrated entities within their respective ministries as budget sub-organizations in their own right, with administrative authority, with funding and front-line service delivery staff directly mapped to it. Modernizing the deconcentrated structure of the national budget in Bangladesh is certainly feasible given the state of technology, and is likely to make the public sector much more agile, more transparent, and reduce administrative waste and duplication.

More effective deconcentration will also increase the synergy between Upazila Parishad and Upazila Administration. First, it would allow the UZP to more effectively play the accountability role assigned to it by the Constitution. Second, if Upazila Administrations were more effectively deconcentrated, the Upazila Parishad would be able to have considerable impact on local service delivery outcomes and sustainable development by providing targeted funding to the Upazila Administration in areas where local circumstances or priorities require greater funding than is provided through the deconcentrated system.

4. Institutional capacity of LGIs is a binding constraint on the ability of LGIs to be a catalyst for better local planning, public services and achieving sustainable development. LGI funding is a binding constraint on the institutional capacity of LGIs.

It is easy to advocate for a stronger role for local government institutions as catalysts for better local planning, public services and achieve sustainable development in response to the social and economic transformation that is being experienced in Bangladesh. In practice, however, this argument cannot be made without simultaneously considering the need to gradually build the institutional capacity of LGIs to perform these functions.

Local government institutional capacity is a binding constraint in the ability of local government institutions to take on a more prevalent role in providing public services and localizing development. As such, there is an inescapable need to gradually build the institutional capacity of LGIs in order for them to become a catalyst for better local planning, public services and achieve sustainable development.

In fact, it appears Bangladesh is caught in a “Catch 22” problem where the approach conflicts with the ultimate goal. On the one hand, due to weak local institutions, LGED and other central government actors plan and implement local infrastructure and other local development interventions. On the other hand, the result of this approach is that local government institutions fail to develop their ability to plan and implement local development activities.

One major reason weak institutional capacity of LGIs continues is the current expectation how local government administrative capacity should be funded. The analysis in this document supports earlier findings that the practice of funding local administration as a “first charge” from local own source revenues—before spending the balance of local resources on development—is an outdated practice and an impediment and a binding constraint to local institutional development. Instead, re-structuring LGI budgets along a functional orientation—and recognizing that inclusive and accountable local administration is an important public sector function—will benefit not only the local government, but the entire public sector.

While local taxpayers (and the local politicians they help elect) are often happy to pay local taxes in return for specific local infrastructure and services as long as the benefits are immediately visible to them, few local taxpayers are interested in funding the salaries of local administrators whose benefit is less direct, or less visible and evident. As a result, many countries that seek to leverage local governments are part of an effective, inclusive responsive and accountable public sector therefore provide an unconditional general-purpose grant to local governments which covers the operating costs of local administration, thereby removing institutional capacity as “Catch 22” binding constraint. This is not (yet) the practice in Bangladesh.

In addition to the need for LGIs to have adequate (human and financial) resources to ensure appropriate local administration, there are other systemic obstacles to be overcome. In order for local governments to plan and work most effectively (and even for them to optimize local revenue collections), it is important that local governments are provided with some degree of fiscal discretion as well as clear budget constraints within which to plan. To the extent that local government finances in Bangladesh rely heavily on special grants and project grants (which have to be executed in a top-down manner) rather than on predictable formula-based block grants (which allow for local discretion and innovation), local government institutions will have a hard time retaining capable, motivated staff.[33]

5. The volume and nature of local government financing should distinguish between local priorities to be pursued by LGIs from own source revenues, and programs that leverage LGIs in pursuit of national objectives

Based on previous policy and legal reform agendas, there seems to be an assumption that local government institutions in Bangladesh—especially in urban areas—should be able to finance all their expenditure needs from own revenue sources. While this may have been a reasonable assumption during

[33] As noted further below, the large volumes of *ad hoc* grants also reduce local revenue effort—why would a local elected politician collect local taxes if it is easier to obtain funds by requesting support from central government officials?

colonial times and even up until the time of the country's founding—when urban local governments served as spatial "clubs" for economically productive urban dwellers—this is certainly no longer the case.[34]

The nature of urban development in Bangladesh has changed significantly over the past quarter century: industrial activity has shifted from the central city to peri-urban areas (where land and low-cost housing for factory workers was abundant), while the rural poor continue to migrate to the country's main urban areas. As a significant portion of the economic / tax base of urban areas has suburbanized, and the socio-economic burden of poverty in the country has urbanized, the assumption that "urban local governments can provide their own public services by taxing local business activity" is no longer conceptually true. In addition, the role of the national government has strengthened considerably over time (imposing a greater tax burden on local taxpayers), while the economic growth and changes in spatial distribution have also re-shaped the political and social relationships at the local level. Whereas rural landlords predominantly resided in their rural communities in the past, the wealthy are increasingly urbanized, thereby breaking the traditional spatial and social connections between the elites and the working class and poor at the local level. As a result, the traditional perception of urban local governments as local "clubs" that are able to self-fund their operations is simply no longer valid.

In reality, LGIs in Bangladesh (like local governments in other countries) provide many functions that have a positive (economic or social) impact beyond the local jurisdictions. This is especially true for urban local government institutions (Boex 2012). The public finance literature suggests that local governments should be funded by a mix of own source revenue and intergovernmental fiscal transfers, in line with the extent to which benefits from local functions exclusively flow to local residents only (which are to be funded in principle from own source revenues) versus local functions for which the benefits spill over (either horizontally or vertically) to residents outside the local jurisdiction (which are to be funded in principle from intergovernmental fiscal transfers).

For instance, effective urban local governments provide positive spillover effects for their surrounding regions—and in fact, for the nation as a whole—by serving as a regional economic hub for surrounding rural areas. Indeed, urban jurisdictions are typically the engines of national economic growth: while businesses rely on their local governments to provide the local infrastructure needed for them to operate efficiently and to connect them to national markets, these same businesses form most of the tax base for national government. Furthermore, to the extent that local governments form the interface between the central public sector on one hand and citizens and the private sector on the other hand, local governments perform an important governance function by ensuing inclusivity and legitimizing the public sector. Similarly, to the extent that municipalities deliver social sector services or pro-poor functions, such functions ought to conceptually be subsidized by a higher-level government, as poverty reduction is an

[34] In response to the question whether own revenue sources are adequate to finance municipal expenditure needs, the answer is quite clear: based on conceptual grounds as well as based on the available empirical estimates, own source revenue collections fall drastically short in funding the municipal infrastructure and services needed by municipal residents. The analyses suggest that most LGIs in Bangladesh—perhaps with the exception of some City Corporations—collect relatively limited own source revenues relative to their expenditure needs. This should not be a surprise. All high-yielding taxes and revenues (VAT, personal income taxes, corporate taxes, and so on) are assigned to the central government, as the central government is typically in a position to collect these revenues more efficiently than lower-level governments. By comparison, the revenue instruments assigned to LGIs are relatively low-yielding. Furthermore, because discretionary grants make up the bulk of the transfer system, local government leaders lack an incentive to collect own source revenues: it is often simpler (especially for a well-connected local politician) to receive a discretionary special grant or a project grant from a sympathetic central government official.

important national policy objective. Likewise, from an efficiency as well as from a fairness viewpoint, it would be inappropriate to force municipalities to fund the expansion of the urban infrastructure base required for newcomers to the urban area from own source revenues: doing so would essentially require municipalities to tax existing residents in an urban area in order to pay for the new infrastructure to be developed for the benefit of others (new in-migrants).

Based on this, it is critically important to make a distinction between the types of local government spending that should be funded from local own source revenues, versus spending that should in principle be funded (in part of in whole) from intergovernmental fiscal transfers.

Local own source revenues should in principle function as quasi-user fees for local public goods: for instance, to a large extent, local property taxes could be seen as user fee for the construction and maintenance of the street in front of the house or business; streetlighting; access to basic services (including solid waste management), and access to community amenities, such as local parks.

In contrast, local taxes are generally an inappropriate funding source for funding redistributive social programs (e.g., such as the upgrading of informal settlements or other pro-poor programs). Local revenues also are generally inadequate to fund major urban infrastructure programs, such as the expansion of road networks; water and sewerage networks; and other major urban infrastructure. To the extent that local administration spends a considerable amount of time and energy coordinating and supporting national programs, local administration should in fact also be seen as a national (not merely local) public good. As a result, it would be appropriate for all these local functions—including the cost of local administration; the expansion of local infrastructure needed to accommodate urban growth; as well as local support to pro-poor services—to be funded from intergovernmental fiscal transfers rather than from own revenue sources.

In line with international best practices and based on a comprehensive review of funding flows in Bangladesh (Kabir, 2014), three different types of intergovernmental fiscal transfers or grants could be included in a comprehensive approach to financing local government institutions in Bangladesh. First, since LGIs cannot spend the same Taka twice, many LGIs are confronted with the choice to either pay for the provision of basic local services and infrastructure from their meager own revenue sources or to fund adequate local government administration. In order to ensure that LGIs can afford to pay for basic (responsive and inclusive) local administration *and* the provision of basic local public services, LGIs could be provided with an unconditional (recurrent) grant to fund their ongoing operational costs, in addition to providing some funding to support the provision of basic local services to poor residents. Second, in line with the current ADP Block Grant, it would be appropriate for LGIs to receive a formula-based grant to support the development of capital infrastructure for the executive functions assigned to LGIs. Third, LGIs could receive sectoral grants or earmarked grants for the purpose of supporting the localized delivery of national programs and services within their local jurisdiction.

It would be important to ensure that even project grants—provided to LGIs to support specific national programs—are provided to the local level in an objective, transparent, formula-based and predictable manner. The reliance on *ad hoc* or discretionary grants (grants that are allocated and earmarked at the discretion of central government officials) should be minimized.

6. There is a need to elevate the intergovernmental fiscal transfer system

It is important to recognize that LGIs are systemically at a disadvantage in the national budget allocation process, as the vertical allocation of resources between the central government and local governments is exclusively decided by central government officials. Furthermore, the current location of LGI grants in the national budget—under the Local Government Division—may raise the impression that whenever LDG allocates an additional million Taka to LGI, that it takes away the same amount from any one of the different Departments that operate under LGD.

Of course, it is understood that LGIs are not merely an extension of a single division or ministry, but rather, that LGIs are semi-autonomous elected local government bodies that (a) represent the interest of their local constituents and (b) that serve the collective interests of the national government (not just LGD's) at the local level.

Some countries have sought to resolve the political economy pressures associated with intergovernmental transfers by separating the process of allocation local government grants from the regular central budget process. One approach—common in South Asia—has been to seek the guidance of an independent Grants Commission to determine the resource sharing between central and local governments. Other countries have resolved this concern by fixing the local government's (minimum) share of national government finances either by constitution (e.g., Kenya) or by law (e.g., Indonesia).

Another common practice is to isolate the funds which are set aside for local government institutions in a separate local government fund or account based on permanent legislation, separate from the annual budget formulation process which allocates central line ministry resources. Under this practice, the Ministry of Finance allocates and transfers local governments' share of national budgetary resources to LGIs in accordance with an allocation formula based on standing legislative authorization (i.e., without requiring further authorization from any administrative ministry or division).

For instance, it would be possible to fix the size of the two main grant windows in Bangladesh—a recurrent, unconditional LGI grant and the ADP Block Grant—as a share of the national budget (e.g., by setting the grant windows for each at 5 percent of the recurrent and development budget, respectively). Next, these resources could be distributed into four different grant pools; one for each of the main types of local government institutions (Upazila Parishads, Union Parishads, Pourashavas and City Corporations). Within each group of local governments, the resources would be distributed in accordance with a transparent allocation formula that is objective, efficient and equitable.

In order to ensure an efficient and timely flow of funds to the local level and to prevent any political interference in the release of funds, the Finance Division could distribute the unconditional LGI Grant and ADP Block Grant directly to LGIs in equal instalments during the budget year without any further requirement or impediment.

7. Strengthening local budgeting, local public financial management and local revenue administration

In order to be legitimate, responsive and responsible local governments, local government institutions need to adhere to participatory budget processes, follow transparent public financial management (PFM) practices, and engage in efficient and equitable revenue administration practices.

While much progress has already been made in recent years, most LGIs in Bangladesh still fall short from this ideal. As such, there is a need to strengthen local budgeting, public financial management and local revenue administration processes on an ongoing basis across all types of local government institutions in Bangladesh. In addition, there is a need to ensure that local government finances are planned, executed and monitored as an integral part of the country's public finance system.

Effective processes and procedures for local budgeting, PFM and local revenue administration seldom arise on their own accord. Indeed, regulations and guidelines from the central level are often required to ensure that local government finances are properly coordinated with the national budget cycle and with national government financial reporting. Although different local government institutions will have different requirements with respect to financial management, these regulations and guidelines should be coordinated across the different types of local governments in order for the local governance system in Bangladesh to be a coherent whole.

In line with the ambition for LGIs to contribute to the effective delivery of public services and the localization of sustainable development, it will be important to revisit the overall budget reporting structure for local governments in Bangladesh. The analysis conducted for this study uncovered that whereas national budgets and finances are reported in a consolidated manner by functional ministry and/or department (before being broken down into recurrent and capital spending), the budgets and financial reports prepared by LGIs are typically broken down into a recurrent budget and a development budget, with little reporting of local spending by department or functional classification. Without consistent reporting on the functional breakdown of local government spending, it is very hard to track (both for the center as well as to their own constituents) whether local government spending is allocated effectively in pursuit of the sustainable development goals that are being pursued by LGIs.

In addition, greater revenue space for local government institutions should be pursued where appropriate.

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Annex: Overview of data sources used

A.1 Key Union Parishad Data Sources

The analyses of UP finances is based on data collected from UPs through the Local Government Support Project 3 (LGSP3) under LGD. The LGSP3 data set contains basic information (including total expenditures; total own source revenue collections; and block grant allocations) for 4,538 Union Parishads. While these figures do not reflect audited local government accounts, for all intents and purposes, this data set should be understood to present a reasonable reflection of UPs finances for the entire universe of UP in Bangladesh.

A.2 Key Pourashava Data Sources

From January-March 2020, LGD and the study team worked with a range of stakeholders and local officials to collect budget documents from as many pourashavas as possible. Budget documents for FY 2019/2020 generally report actual (rather than budgeted) revenue and expenditure figures for two years prior (i.e., 2017/18). While the data collection efforts were hindered somewhat by the global outbreak of COVID-19, the team was able to collect complete local government finance data for 175 out of 329 pourashavas.

Based on this sample of pourashavas, total pourashava expenditures (as well as revenues and transfers) were extrapolated for the full universe of 329 pourashavas, representing an estimated urban population of 20.2 million. Extrapolations were done separately for each category of municipalities (A, B or C) to minimize the impact of sample selection bias. While the resulting aggregate figures are an estimate based on unaudited local government accounts, this data set should be understood to present a reasonable reflection of pourashavas finances in Bangladesh.

A.3 Key City Corporation Data Sources

Given the relatively small number of City Corporations, the study team was able to collect budget documents from each of the CCs. Similar to pourashava budgets, budget documents for FY 2019/2020 generally report actual (rather than budgeted) revenue and expenditure figures for two years prior (i.e., 2017/18).

The available CC data does not readily allow a detailed analysis of the sectoral/functional composition of CC expenditures. Furthermore, it should be noted that the statistics presented here do not include spending by any of the WASAs, not of the RAJUK/CC Development Authorities.

A.4 Key Upazila Parishad Data Sources

Consistent fiscal data for Upazila Parishads is difficult to obtain. While LGD was able to provide data on annual ADP allocations for all 492 UZPs, at this time, there does not appear to be a systematic effort by LGD to collect UZP financial statements. In addition to the ADP allocations, the Upazila wing of LGD collected own source revenue data for a sample of 73 Upazila Parishads. The available data allowed an estimate of Upazila Parishad expenditures to be prepared as the sum of the ADP Block Grant spending for each Upazila plus the spending of the (extrapolated) Upazila own revenues.

It should be noted that the estimation procedure relied on here produces an under-estimate of Upazila Parishad expenditures, as Upazila Parishads spend resources from UGDP (Box 4.1) as well as potentially from other development projects. While these estimates are less solid than the expenditure information available for other LGIs, the estimated expenditure levels nonetheless give some insight into the relative role of Upazila Parishads compared to other LGIs in Bangladesh. This caveat should be noted throughout this report in interpreting UZP-related financial figures.