

## Meeting during the “Africities” Summit of the Chief Financial Officers (CFOs) of large African cities

### I. Context:

#### 1.1 Urban Growth and Investment Needs

Faced with unprecedented urban growth, African cities must prepare to welcome more than 300 million additional people in the next twenty five years. The investment needs enabling African cities to accommodate these populations must be added to the funds already required in order to compensate for the accumulated delays in most cities in terms of infrastructure, and essential equipment and services.

Different estimates indicate that the funds collected today to finance urban investment are largely insufficient to allow the cities to develop their full potential, whether in terms of economic growth or poverty reduction.

Indeed, while the needs are estimated to over 90 billion USD per year, Africa currently spends only 45 billion USD per year on its infrastructures, and obtains an additional 8 billion USD from donors. The capacity of urban investment of local authorities is valued at 25 billion USD.

#### 1.2 Decentralization and Local Finances

In this context, there is a need for a drastic change of scale in the amounts of funding mobilized for the cities. Among the different options available, improving the financial capacities of local authorities appears to be the most sustainable way to reduce the gap between financial needs and secured funding.

To meet this objective, the four main sources of funding for local authorities must be optimized.

*1.2.1. The legal and financial frameworks of decentralization* in different countries define the rules regarding the sharing of expertise and resources between the central and local levels (mainly transfers and local taxes). The coherence of these components largely determines the financial health of the local authorities.

*1.2.2. The practice of borrowing* is particularly well adapted to local investment. It spreads over time the reimbursement of infrastructures and equipments that, in the context of rapid demographic expansion, will benefit a growing number of people in cities whose capacities will be multiplied due to the expansion of the financial base. Moreover, borrowing is sometimes credited with enhancing the management of local authorities as the latter seek to optimize their lending capacity by presenting credit institutions or credit rating institutions with evidence of their management capacity and good governance.

*1.2.3 Urban land*, and the ability for local authorities to reap the benefits of its added value, is an endogenous source of funding enabling the city to finance itself. While Western cities, and more recently China, have largely financed their growth using these techniques (taxation or planning), the majority of African countries have so far neglected this opportunity.

1.2.4. Local investments may also be funded through the framework of Public-Private Partnerships (PPP). However, this model has failed to attract investors on the African continent, especially in the urban sector, due to its poor financial profitability. Nevertheless, this concept is worth exploring further, especially with regards to the evolution of “management contracts” of public services or joint venture companies.

### **1.3 United Cities and Local Governments (UCLG)**

The United Cities and Local Governments (UCLG) is a political platform that brings together local authorities from around the world, and promotes decentralization as a form of social organization that promotes and strengthens democracy. Through its activities, the organization seeks for its members to be recognized as full-fledged actors by their national governments as well as international organizations. By promoting exchanges and developing tools that support regional development, the organization encourages and participates significantly in the capacity building of an extensive network of local actors.

In the past decades, the process of decentralization has seen great strides in terms of the devolution of capacity building, which has enabled local governments to play a key role in addressing current global challenges. These challenges affect, to varying degrees, most countries around the world, whether in terms of food crises or energy, environmental, financial or political policies in the fight against poverty and the fulfillment of the Millennium Development Goals.

However, a study on the financial systems of local authorities indicates that the process of decentralization is now facing a number of difficulties, such as poorly developed financial systems, lack of capacities of local authorities, and insufficient resources. While many factors account for the paucity of local governments, a look at the national income allocated to local authorities in Africa is very telling: 6.2% to 8.3% on average against 25% in Europe.

Under these conditions, the improvement of living conditions of populations is slow to materialize and the strengthening of fiscal decentralization is essential in order to concertize the process of decentralization. Indeed, the process of decentralization may appear as an unrealizable goal if the transfer of skills to local governments does not ameliorate the quality of life of citizens, and if local authorities do not have the financial resources with which to assume the responsibilities that are assigned to them by law.

### **1.4. Commission des Finances Locales pour le Développement/ Committee for Local Finance for Development**

In this context, the financing of local governments constitutes one of the key issues enabling local action. Within UCLG, the Committee for Local Finance for Development, founded in 2006, has for mission to facilitate the access that local communities have to financial resources (see points 1.2.1 to 1.2.4). The Committee operates through three main axes of intervention:

#### **1.4.1. Raise awareness of international, regional, and national institutions on the issues relating to fiscal decentralization**

During its first years of operation, the Committee for Local Finance for Development has produced a body of recommendations for financial decentralization, hosted several national debates on the issue of funding for local authorities, and supported several local government associations in deepening the dialogue with national authorities on the institutional framework

of local government finance. The Committee also participated in the preparation of the "GOLD (Global Observatory on Decentralization and Local Democracy) II" report regarding the situation of local finance in the world.

At a time when the financial crisis experienced by most countries in the world has exacerbated the already tense situation of local finance, and when economic and social issues related to territorial development are particularly acute in terms of unemployment and poverty reduction, the strengthening of international, regional, and national dialogue on the sharing of resources among different levels of government is an essential element for strengthening democracy and the rule of law.

#### 1.4.2 Promote trade, capitalization of experiences, and coordinate a network of experts in local finance

This network, comprised of academics and professionals of local finance, aims to provide the necessary expertise to locally elected officials and their associations allowing them to fully play their advocacy role on the political scene. Within this network, CFOs and directors of local authorities, who examine on a daily basis the weaknesses in financing schemes, play a central role. Through the exchange of information, experiences, deployment training, and production of methodological guides, the Committee for Local Finance for Development aims to facilitate:

1. their positioning in terms of aiding local officials in the development and implementation of financial policies of local authorities
2. their active participation in providing the expertise that associations of local authorities need to analyze the financial situation and develop their claims;
3. their input on specific topics that seem relevant;
4. their involvement in programs of capacity building in financial management of communities that will be developed in their country or sub-region.

#### 1.4.3. Facilitate the link between the needs of local stakeholders and potential funders

In a context where financial markets are able to raise funds to finance urban investments, and development assistance grants amount to over 100 billion USD per year, and local authorities constitute a potential "market" for these very large funders, how do we explain the lack of enthusiasm for these local authorities?

What are the criteria for gaining access to external financing, and the levers needed to break the structural backwardness that accumulates from year to year in urban investment?

Without reviewing all components of the risk assessment conducted by banks, several factors seem decisive here:

- At the national level, the quality and stability of the institutional, political, demographic and economic environment of a country constitute factors that are external to the local authority, but can influence its future development and are therefore taken into account in assessing the "country risk";
- Also at the national level, financial security provided by the legal and financial framework of decentralization also plays a role in the assessment of "risk," and local officials are thus quite justified in pressuring their governments to undertake the necessary reforms. Without recurring and reliable resources, and without the possibility to employ a specific tax to adapt its financial strategy to

public policies, it is impossible to secure a future repayment from a local authority. Moreover, the legal mechanisms to authorize borrowing, the prudential standards in force, and the reimbursement mechanisms are specifically valued by potential funders;

- At the local level, the performance of the financial management of the local authority, as well as the analysis of its accounts, is an essential component in the decision to lend. The quality of the preparation process in implementing the budget, the reliability of its accounting and internal controls, and the transparency of its management is heavily involved in the evaluation of the borrowing capacity of the local authority, as well as the retrospective and prospective analysis of its financial equilibrium.

Promoting access to lending for local authorities implies an intervention at different levels of decision-making in financial governance at central and local levels. The capacity building of national associations of local authorities and individual cities are closely linked.

## **II. Objectives of the Project**

### **2.1 Africities**

The "Africities" summits reunite every three years since 1998 up to 5000 actors from localities in Africa, as well as their African partners in other regions of the world including local authorities ministers, ministers responsible for local sustainable development and employment, local authorities and elected officials responsible for central and local governments, civil society organizations, associations and unions, economic operators in the public and private sector, and the social economy, traditional authorities, researchers and academics, and international cooperation agencies.

These meetings are essential in boosting the process of decentralization in Africa, and in considering the place and role of local communities in the governance and development of African countries. They are important moments in the assessment and implementation of policies and programs for cooperation in the field of decentralization.

The sixth edition of the Africities summit will be held in Dakar from 4 to 8 December 2012, and will be focused on the theme "Building Africa from its territories: What challenges for local governments?" The summit will examine the impact of the dynamics of urbanization, globalization and democratization with its corollary decentralization, the reorganization of the settlement and development of the continent, and its place in the world of today and tomorrow.

The different sessions that have been organized place a spotlight on the issue of funding for local authorities. During the first two days, seven thematic sessions deal directly or indirectly with local finances:

- local financial strategies;
- management strategies and local governance;
- financial institutions;
- professionals from the central and local administrations;
- academics and researchers (including research in local finances);
- participatory budgeting, the observatory for decentralization and local governance;
- fiscal decentralization

Special sessions organized on the following day have not yet been finalized but the theme of local finances is, again, the subject of numerous requests.

## **2.2 Chief Financial Officers (CFOs)**

While the arrival of many Mayors and representatives of their associations is expected at the summit, it seems that the delegations have very few close associates in regional administrations, such as general directors, directors of technical services or financial managers. However, improving the management of local authorities largely implies the involvement of these professionals in the field.

The training organized by the CEFEB (Centre d'Etudes Financière Economiques et Bancaires), from the French Development Agency/l'Agence Française de Développement (AFD), geared towards CFOs of local African authorities has demonstrated that the latter were still struggling to gain recognition for their role as financial strategists and in lending support in the decisions regarding elected officials. Enabling them to intervene and participate in sessions organized during Africities, and meet and build a network will likely strengthen their position and raise potential issues of financial management, resource mobilization, and access to loans, in particular with local officials.

In addition, this is a unique opportunity to bring together financial experts in this field to deal with issues surrounding the financing of local authorities, with regards to their "structural" revenue, their financial performance for accessing loans, or the valuation of land or the use of Public-Private Partnerships. These exchanges will result in the structure of working groups and the elaboration of capacity building programs, in conjunction with national and international management training programs and interested donors.

## **2.3 The organization of a special session for the PEFA (Public Expenditures and Financial Accountability) framework**

The PEFA framework was introduced in June 2005 to assess the performance of the Public Finance Management (PFM) of central governments and, since 2007, it is increasingly used by sub-national entities (around fifty assessments for such entities have been conducted in late 2010).

With its 32 indicators, the PEFA framework is currently the analytical tool of the Public Finance Management and the most widely used around the world. It introduces a novel approach by replacing many different diagnostic tools with a single framework.

With regards to local african authorities, three assessments have been conducted according to the PEFA framework: in Dakar (Senegal) in 2009, in Ouagadougou (Burkina Faso) in 2010, and in Cotonou (Benin) in 2012. These three assessments were all conducted with support from the PPIAF (Public-Private Infrastructure Advisory Facility), and have been used in the elaboration of a program for capacity building in connection with the establishment of a direct loan, without state warranty, and implemented by AFD. One of the great benefits of financing these early experiments with a multi-donor fund has been to enable various technical and financial partners to use a common tool for qualitative analysis of the local public financial system. Until now, each donor, depending on its financial instruments and mandates in its various sites of intervention, has used its own analytical frameworks.

The assessments of the financial performance of local authorities and the steps taken to improve their financial management were conducted according to a dual objective:

- to facilitate access to loans by reassuring potential lenders (including fiduciary risk measurement)
- to optimize the predictability and the mobilization of their revenue

During the workshop held in June 2011 in Rabat, under the aegis of the CFLD and UCLG Africa, many mayors were interested in the process, and it was decided that this framework should be spread across 10 countries, and cover 3 cities in each country.

The relevance of this project has been confirmed by a study published recently by the AFD titled "Methodologie PEFA et collectivités infranationales: quels enseignements pour l'AFD?"/ "PEFA methodology and subnational authorities: lessons for AFD," which indicates that the PEFA framework, when applied to subnational authorities, is a useful tool for operational opportunities that help develop a reform plan adapted to improve the financial management of local governments or to develop a national program to support fiscal decentralization in a given country.

Not only does it complement the classical approach to financial analysis and evaluation of the decentralization process, the PEFA framework "boosts" the different methods and will contribute to provide a common analysis grid for national and local governments, as well as technical and financial partners.

In addition, the study highlights some limitations of the exercise which must be taken into consideration before proceeding further with the process:

- the PEFA framework seems appropriate for communities that have both a sufficient critical size (200 000 or even 500 000) in Francophone Africa (level of resources to achieve a level of efficiency to finance investment management capacity), and a minimum level of financial autonomy
- despite the strong involvement of elected representatives and their teams in the assessment process and in setting priorities for improving municipal management (*management of local fieldwork, workshops, restitution, agenda and their calendar, ...*), programs for capacity building have proven difficult to fully implement. Beyond the support that can be offered in the assessment process, and the definition of a "roadmap" to access loans under favorable conditions, these initial experiments tend to show that the focus should also be placed on the implementation and monitoring of programs for capacity building;

The workshop will focus on the strengths and weaknesses that have been identified, and will involve CFOs who have participated in a PEFA assessment course, as well as those who attend the workshop through a process of self-evaluation. In addition, the intervention of training agencies for local managers will shed light on how they can help support the municipal teams in their efforts to improve their financial performance.

Based on these exchanges and preparation work, several national capacity building programs can be elaborated with donors on the ground of a diffusion of PEFA assessments, enabling a process of change.

#### **2.4 The organization of a special session on financing urban investment by valuing land**

Land has long played an important role in financing urban infrastructure. Cities like New York, London or Paris, and more recently cities in China, have made it a central component in financing their urban infrastructure. By producing substantial revenue that reduces dependency in terms of debt as well the budget risks associated with loans, the use of various techniques for financing land seem well suited for cities experiencing rapid urban growth.

The study published in 2008 by the World Bank and the PPIAF titled “Exploiter la valeur du foncier pour financer les infrastructures urbaines”/ “Harnessing land value to finance urban infrastructure” examines the different ways of using land value to finance urban infrastructure. Based on an analysis of experiences in developed countries as well as developing countries, George E. Peterson identifies key lessons in the implementation of these financing techniques.

According to the author, the potential benefits of using land go well beyond its revenue generation properties; as a component of investment financing, financing land loans improves the efficiency of urban land markets and helps to direct urban growth to areas that are most capable of accommodating it effectively.

It also highlights the opportunities this field opens for public policy to increase the effectiveness of the design and implementation of these instruments in the delineation of clear guidelines for the auction of public land, the development of strategies for land management, the definition of stable and equitable rules on expropriation, and adapting tax systems on land value.

However, this type of financing still arouses little interest on the African continent. A special session on this topic during Africities would raise the awareness of locally elected officials and their ministries to the use of these techniques as well as the underlying legal prerequisites (and therefore on the reforms to be implemented). The participation of CFOs will allow for an exchange of experiences on this subject, and will also implicate training organizations in the process of elaborating support programs that can be implemented.

In addition, the session will promote exchange programs between cities and their operators in order to facilitate the implementation of these techniques. This will complement the current study by CFLD on the legal and institutional prerequisites necessary regarding the creation of land value and its use in financing all or part of the urban infrastructure.

## **2.5 Other planned sessions and seances**

Aside from the participation and/or involvement of financial directors in different sessions addressing fiscal decentralization, several workshops will be organized in order to deepen the links between the network of experts. These involve:

- Support for structuring the pan-African network of CFOs
- Contributions from the CFOs on the study concerning the feasibility of a local finance observatory;
- Exchange sessions with technical and financial partners supporting the arrival and attendance of CFOs at the Africities summit:
  - PPIAF: presentation of the work done by the PPIAF on the Public-Private Partnership, methodological guides, exchange of experiences, and training needs;
  - AFD: presentation of the strategy for financing local authorities of AFD, its projects in Africa, and training programs

## *2.6 Financing the arrival and attendance of the CFOs*

One of the expected outcomes from the attendance of CFOs at the Africities summit is deepening the discussion regarding financial management issues in order to coordinate a network of experts as a long-term goal. The funding provided for their journey and their stay entails a form of commitment on their part to fuel the debate and, at the very least, to establish focal points of the network in their country. Consequently, they are asked:

- to provide data on fiscal decentralization in their country (in order to aliment the observatory on local finance, at least on the qualitative aspects), a questionnaire will be sent to this effect.
- to provide their assessment of the PEFA framework (in preparation for the workshop) as well as on the managers;
- following Africities, to commit to communicate to other CFOs in their respective countries, the information disseminated by the CFLD.