

**Presentation
to
International Association
of
Development Funds
by
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National Enabling Framework
for
Municipal Finance**

October 1, 2004

Resource Mobilization Advisors

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Introduction

- **There is no perfect enabling framework for municipal finance in the world today.**
- **Local projects can be financed in an imperfect framework--in an emerging framework**
- **Don't wait until all the perceived necessary elements are in place before you advance a local financing initiative**
- **Best way to test the viability of an enabling framework and identify shortcomings and need for improvements is through a financial transaction (Romania, Estonia)**

Objectives of a More Perfect Framework

- **Lower risk profile of local governments**
 - **Improve transparency and accountability**
 - **Budgeting/ accounting**
 - **Reporting**
 - **Enforceable legal framework**
- **This will lower costs of capital**
- **Streamline financing process**
 - **Disclosure**
 - **Government approvals**
 - **Public participation**
- **This will lower transaction costs**

Framework Analysis

- **Legal audit**
- **Fiscal federalism review**
- **Commercial lending practices**

Legal Framework Analysis

- **Much like the laws of physics, the principles of municipal finance have universal application**
- **Investors in Mozambique are just as concerned about risk and rate of return as investors in Manhattan**
- **Similarly, financial structures and credit enhancements designed to reduce investor risk should result in reductions in cost of capital regardless of location of investment (Poland)**
- **Attempts to cut corners or design sub-standard financial programs in developing countries will fail to raise capital or result in unintended consequences**

Professional and Independent Judiciary

- **All debt instruments, including loans, bonds and debentures, are contractual agreements**
- **Capacity of the judiciary to effectively and fairly resolve disputes between contracting parties is a factor considered by investors (Indonesia)**
- **This analysis goes beyond the scope of legal audit**
- **Highly professional, independent judiciary will enhance development of municipal finance system**
- **Enforcement of contractual obligations of parties by an impartial judiciary is essential to viable municipal finance system**

Three Phases of Legal Analysis

- **Legal Audit – review all relevant laws for municipal finance and identify barriers to efficient and effective mobilization of private capital for public infrastructure development**
 - **Should be conducted by experienced bond counsel and local legal advisor.**
- **Remediation Strategy – address impediments on a triage basis –**
 - **Stipulation of parties**
 - **Financial structures**
 - **Administrative orders**
 - **Legislative initiatives**
- **Draft Standard Legal Documents**
 - **Bond Resolution**
 - **Trust Indenture**
 - **Disclosure Document**

Legal Audit

Laws to be Reviewed

Constitution

- **U.S. bond market is predicated on specific provisions in the U.S. Constitution**
- **Constitution does not need to authorize municipal debt, however, the federalism section may contain language that will have a direct impact on municipal finance**
- **Provisions defining local governments' entitlement to percentage of nationally collected revenues (Colombia, Argentina and Brazil)**

Local Governance Legislation

- **Legislation granting specific powers to sub-national government entities**
- **Authority to incur debt (Russia) and specific limitation on such authority, e.g. debt caps (Europe), state approval (Mexico), foreign currency (Mexico)**
- **Authority to raise revenue**
- **Authority to pledge assets (Zimbabwe)**
- **Authority to contract with the private sector for the provision of public services – PPP, concession, joint venture (Zimbabwe)**
- **Monitoring and oversight of local government financing**
- **Terms of office**

Local Governance Legislation (Continued)

- **Power of national or regional government to suspend actions of lower levels of government**
- **Power of national or regional government to dissolve municipal corporations or governments**
- **Public notice and hearings (U.S.)**
- **Taxes levied and collected by the national government but assigned to the states**

Local Governance Legislation (Continued)

- **Central registration of borrowing and collateral pledges**
- **Municipal accounting and budget standards (Do they meet private sector needs?)**
- **Audit procedures and requirements**

Financial Disclosure Legislation

- **Will govern public bond offerings not private placements**
- **Most countries' disclosure laws cover the issuance of stock and debt for private companies only (India)**
- **Very few countries have specific disclosure requirements for municipal securities**
- **Modification to disclosure laws to accommodate municipal securities will streamline financing process**

Municipal Enterprise Law

- **Governs activities of municipal utilities (Water Districts, Philippines)**
- **May have specific debt limit and other restrictions independent of local finance laws**
- **Will generally govern the issues of revenue bonds**
- **Will define powers of utility to contract with the private sector for delivery of public services**
- **Provides procedures for tariff setting and adjustments**

Trust Act

- **Municipal bond financing structures utilize trust and trustees**
- **Trust Act will specify what qualification an entity must meet to serve as a trustee (Indian Trust Act of 1882)**
- **Some legislation provides trustees with much broader authority than trustees are willing to assume (India)**
- **Trust Act is not always necessary**

Bankruptcy Law

- **Does it cover municipal bankruptcy? (Hungary)**
- **Who can file? Debtors and/or creditors?**
- **Remedies and procedures**
- **Inability of creditors to take local authorities into bankruptcy or insolvency proceedings is not fatal to a vibrant municipal finance system**

Municipal Charter

- **Elections and terms of office**
- **Provisions regarding validity of proceedings**
- **Obligatory and discretionary duties**
- **Power to execute contracts**
- **Acquisition and disposal of property**

Municipal Charter (Continued)

- **Municipal funds**
 - **deposits**
 - **draw against**
 - **restrictions on expenditures**
- **Audit of accounts**
- **Borrowing powers**
- **Taxing powers - taxes to be imposed and manner of recovery**

Fiscal Federalism Review I

- **Is there a clear/rational allocation of responsibility for the delivery of essential services among levels of government?**
- **Does the level of government responsible for delivery of a particular essential service have the capacity to deliver that service**
 - **management**
 - **accounting/ budget**
 - **interaction or relationship with public client**
 - **financial**

Fiscal Federalism Review II

- **Is there a clear/rational allocation of financial responsibilities for the delivery of essential services among levels of government?**
- **Are local governments able to mobilize private capital to fully assume responsibilities?**
- **Does the central government provide financial support to local government projects**
 - **Subsidy or cost sharing**
 - **Distortion or leverage**
 - **Deter private investment or incentivize private investment**

Commercial Lending Environment

- **Enabling framework analysis must involve consultation with private sector lenders and investors (Philippines)**
- **Private Sector - Ultimate decision makers on the viability of enabling framework**
- **What are general terms of finance?**
 - **maturities**
 - **interest rates**
 - **collateral requirements**
- **What are currently available financial structures? Balance Sheet/ Project Finance**
- **What are available internal credit enhancement options and external or third-party options?**
- **What role can central government play in this regard?**