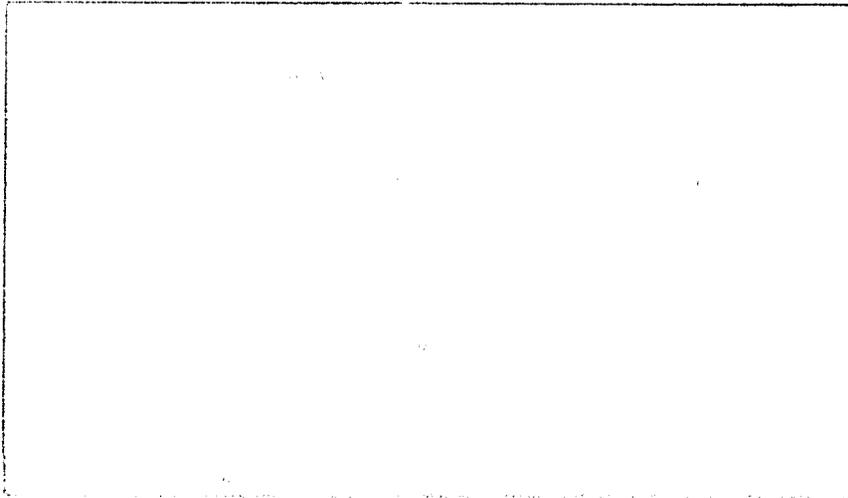


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# Central and Eastern Europe Local Government and Housing Privatization



Prepared for the Office of Housing and Urban Programs  
Agency for International Development



ICMA  
Consortium Report

Consortium Members

International City/County Management Association  
Urban Institute  
Urban Land Institute  
National League of Cities

PD-ABF-696

**LOCAL GOVERNMENT INVESTMENT IN  
THE CZECH AND SLOVAK REPUBLICS:  
A STRATEGY FOR ASSISTANCE**

March 1993

Prepared for the Office of Housing and Urban Programs  
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

Prepared by

G. Thomas Kingsley, George E. Peterson,  
and David A. Grossman

The Urban Institute

INTERNATIONAL CITY/COUNTY MANAGEMENT ASSOCIATION  
USAID Project No. 180-0034  
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A.I.D. Local Government and Housing Privatization Contract

**ABSTRACT**

This report presents the strategy for implementing the USAID supported Local Government and Housing Privatization Contract in the Czech and Slovak Republics. Missions to both Republics in late 1992 found that local governments there have been given enormous new responsibilities under national reforms but their financial resource base and institutional capacity remains weak. In particular, needs and opportunities in urban physical development are substantial. The strategy for assistance (accepted by both Republics and A.I.D.) will focus on helping cities develop cost-effective capital investment strategies (building skills in project preparation and capital budgeting) and working at the Republic level to develop market-oriented municipal credit systems to finance those strategies. The work will specifically entail: (1) technical assistance to individual municipalities on infrastructure provision, land development and management, housing privatization and management, and financing and financial management pertaining to urban physical development; (2) work at the Republic level to develop market-oriented municipal credit systems and provide guidelines for local government finance; and (3) broader training and dissemination of technical information through conferences and publications.

## **EXECUTIVE SUMMARY**

The U.S. Agency for International Development (AID) has initiated a three-year Local Government and Housing Privatization Contract (LGHP) as a part of its program of technical assistance and training to support the reform agendas of the countries of Eastern Europe. This contract was awarded to the ICMA Consortium, which is composed of the International City Managers Association (ICMA) as prime contractor, three major subcontractors (The Urban Institute, The Urban Land Institute, and the National League of Cities), and several supporting subcontractors.

This report presents the strategy for implementing the LGHP in the Czech and Slovak Republics. The aim of the program in these Republics is to contribute to the goals of economic restructuring and capital market development by helping to develop strong and self-reliant local governments. Assistance focuses on four substantive areas: (1) infrastructure provision; (2) land development and management; (3) housing privatization and management; and (4) financing and financial management pertaining to urban physical development.

## **FINDINGS OF PREPARATORY MISSIONS**

Missions to both Republics during the last quarter of 1992 entailed meetings with relevant Republic Ministries, Associations of Towns and Cities, the Mayors and staffs of 19 cities, other donors, and a number of indigenous training institutions. These discussions support the following conclusions:

1. The commitment to decentralization remains strong in both Republics. Municipalities have a critical role to play as change agents in the economic and social transformations now underway nationwide.
2. Municipalities lack the skills and the systems needed to perform the many governmental functions being devolved to them. The need to strengthen their capacity is enormous.
3. Legislation totally restructuring public revenues was passed in 1992 implying that municipal revenues from central budgets will decline substantially next year. Municipalities will have to become much more efficient and self-reliant.

4. Municipalities in both Republics generally recognize that the four substantive themes assigned by AID to the LGHP contract warrant highest priority attention. In particular, their needs for investment in infrastructure improvements are enormous.

5. Almost all Mayors we talked to requested AID technical assistance under the LGHP and have definite, relevant projects for us to work on that they regard as top priorities. All indicated a willingness to try market-oriented approaches that are far from conventional in the CSFR.

6. Virtually all Mayors highlighted the lack of finance for infrastructure improvements as one of their most severe constraints at present. They expressed strong interest in the possibility of USAID technical assistance to help develop a credit system to finance municipal infrastructure.

## **STRATEGY**

To address these findings, the technical assistance and training strategy should incorporate a mix of related activities, on one hand providing direct assistance to selected cities to help them resolve their priority problems but, on the other, also working to develop central support for effective municipal governance and to provide broader training and dissemination that will spread the lessons of individual city experiences so they will have nation-wide impact.

Cities need assistance in many areas but this program cannot do everything. The findings above warrant a *substantive focus on helping cities develop cost-effective capital investment strategies (building skills in project preparation and capital budgeting) and working at the Republic level to develop market-oriented municipal credit systems to finance those strategies*. Separate but related programs for the two countries are proposed with the following elements.

### **Work With Individual Cities**

**Intensive Assignments.** Work intensively with a few cities on interrelated investment programming issues (probably no more than two cities at a time in each Republic for a six to twelve month period, up to six cities per Republic in total). These activities would begin with assistance on one or two topics (e.g., developing strategies for water supply, sanitation, or land development with associated plans for financing) and then move out to other priorities and more general guidance in project preparation and appraisal and capital improvement programming.

**Short-Term Assignments.** Work with a broader range of cities and regions (ten to twelve) in a series of short-term assignments (around two weeks). In most cases, these would focus on the central themes: developing local infrastructure investment strategies and preparing and appraising projects (that could be financed by the new credit system) consistent with those strategies.

### **Work at the Republic Level**

**The Municipal Credit System and a Housing Guaranty Program.** As Republic budgets can no longer be relied upon as a major source for infrastructure financing, the only alternative may be for local governments to leverage the recurring revenue streams they will receive under the new tax law into capital financing, which can then be used to pay for infrastructure investments. Technical assistance will be provided in developing municipal credit finance systems built on this approach. An AID Housing Guaranty (HG) Loan, now offered on terms that should be attractive to both Republics, presents one way to partially capitalize such a fund, and analysis and planning for HG development shall be a part of this assistance.

**Guidelines for Municipal Finance.** The new national revenue systems represent a traumatic change. Officials in both Republics believe it would be wisest to monitor experience under the new system over the coming year and then, based on lessons learned, draft appropriate laws and guidelines. They have asked for LGHP assistance in monitoring and analyzing change, and then in preparing relevant laws, guidelines, and training for municipalities.

### **Training and Dissemination**

This entails working with and through indigenous institutions in: (1) proposing, designing, and participating in conferences and seminars; (2) designing training curricula and training trainers in their use in ongoing staff training programs for municipalities; (3) translating and disseminating key documents (reports on city projects, more general policy reports, etc.) to large numbers of municipalities; (4) working with universities and other training institutions to build our themes into their curricula. All of this will be coordinated through the Associations of Towns and Cities in each Republic.

### **INITIAL WORK PROGRAM**

The first four months of the program in each Republic will emphasize: (a) more detailed planning for the municipal credit system and HG Loan; and (b) intensive city assistance projects (the training and dissemination component will be phased in later during the year). Two cities in each Republic have been selected for the first intensive assignments.

These cities, and priority topics for assistance, in the Czech Republic are: Hradec Kralove (water supply system improvements, land development) and Liberec (housing privatization, and sanitation system improvements). In the Slovak Republic, the choices are: Banska Bystrica (sanitation system improvement, land development) and Trencin (sanitation system improvement, land development).

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## **INTRODUCTION**

This document presents a proposed strategy for the ICMA Consortium in providing technical assistance (TA) and training under Local Government and Housing Privatization (LGHP) Contract in the Czech and Slovak Republics (CR and SR, see Figure 1). Since Czechoslovakia was split into two separate countries in January 1993, this is the strategy for two independent, though related, programs. The contract is being operated by the U.S. Agency for International Development's (AID) Office of Housing and Urban Programs (PRE/H). The strategy is based on the findings of a mission to the two Republics in October 1992 as well as lessons learned from earlier AID assistance provided in the CSFR since mid-1991.

We first present background information (on the substantive elements assigned to this contract and the steps taken to prepare for strategy development). The second section reviews the main findings from the October mission and the third presents the strategy. The fourth, describes the proposed organization and staffing for the program and an approach to operating (preparing RFSs within it and making mid-course corrections). Section five discusses our approach to city selection and characteristics of individual cities in relation to that approach. The sixth section suggests an approach to issuing RFSs under this program.

Several annexes contain relevant background information and more detailed descriptions of the program elements: (A) a description of possible municipal credit system development (including the possible role for a Housing Guaranty (HG) Loan program; (B) a description of the current structure and function of local governments and the systems of local government finance in the CR and SR; (C) a more complete description of the characteristics and interests of the prime-candidate cities we have visited; (D) a review of candidate training institutions with which the program might be affiliated; (E) a review of other programs designed to strengthen local governments being operated by AID and other donors.

## **1. BACKGROUND**

### **Substantive Scope**

An important element of AID's program in Eastern Europe is providing technical assistance and training that will help popularly elected local governments become more self-reliant and, thereby, play strong and positive roles in the economic and societal transformations presently underway in the region.

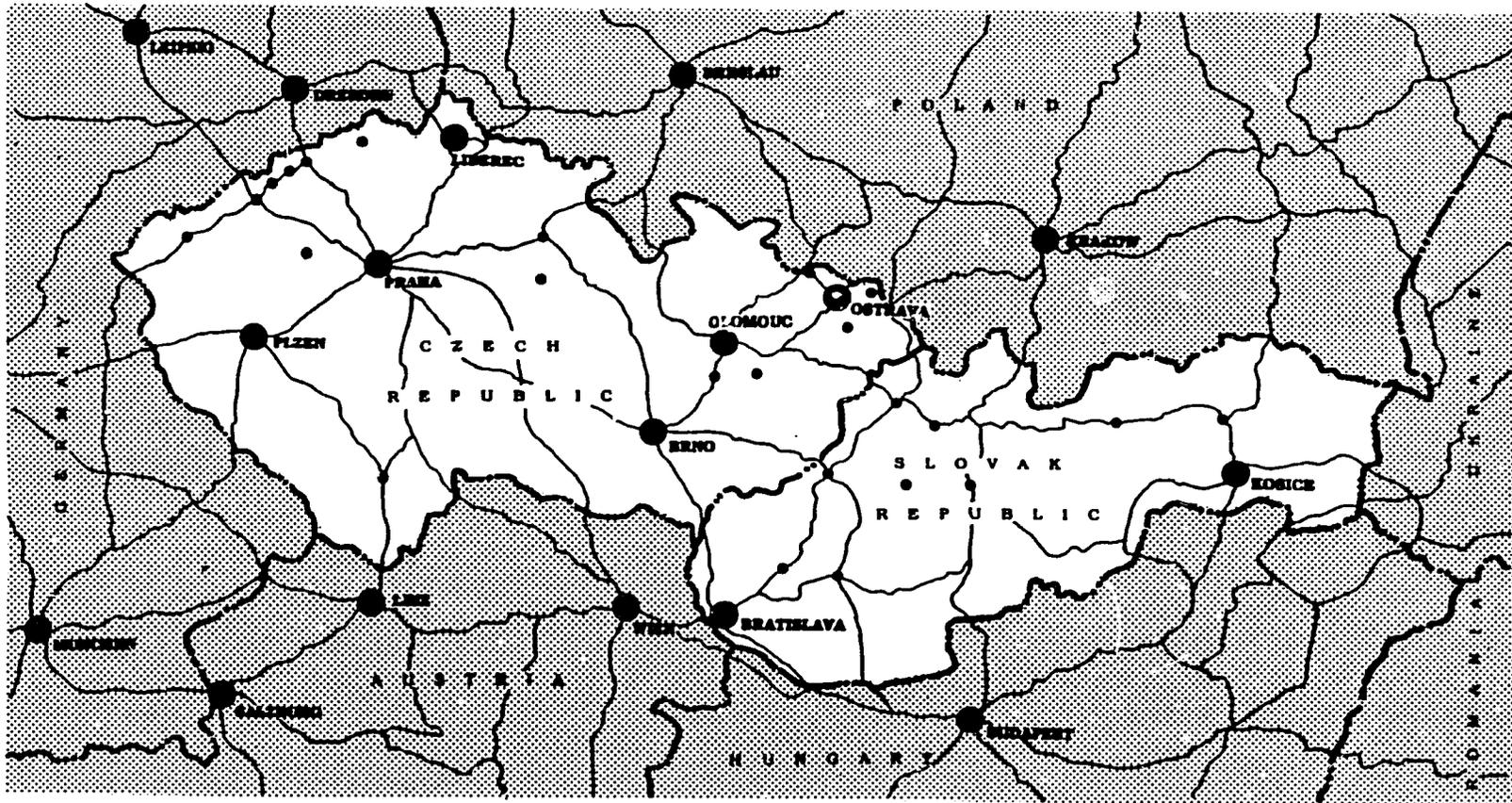
Another AID project (Democratic Initiatives) is providing broader assistance toward this end, addressing needs to improve the institutional structure and overall management practices of local government. The LGHP program is to provide more focused assistance in topics that have been the functional specialties of PRE/H, all related to urban physical development. Specifically, LGHP will provide assistance to local governments in four areas:

1. Infrastructure provision
2. Land development and management
3. Housing privatization and management
4. Financing and financial management pertaining to urban physical development

### **Preparing for the Strategy**

Representatives from ICMA, the Urban Institute, and other Consortium members met in August, 1991, to develop a basic approach. These ideas were discussed with RHUDO/EE and the approach (explained below) was accepted as a guide to field work. During late August and September, local consultants (Urban Research Inc.) completed a number of tasks in both Republics in preparation: (1) visited (or interviewed Mayors from) 19 towns and cities to find out about their TA/training needs and their commitment to reform and innovation; (2) documented the nature and extent of other donor assistance programs affecting municipalities; and (3) identified and met with indigenous institutions (private and public) that might serve as counterparts in an ongoing TA/training associated with LGHP.

With this background, the October mission entailed meetings with: (1) top officials of the Ministries in both Republics responsible for relations with municipalities (to describe our thoughts about the approach and gain their suggestions and approval to proceed); (2) cities that seemed to be the most promising candidates for more intensive work (meetings were held with Mayors or Deputy Mayors from 10 cities to discuss their TA/training needs); (3) the Associations of Towns and Cities (ATC's) in both Republics (to gain their suggestions on our approach and discuss collaboration in implementing it); (4) representatives of indigenous training institutions (to discuss possible collaboration); (5) officials of the Ministries of Finance in both Republics (to discuss the outlook for municipal revenues and interest in a



**Figure 1**  
**CZECH AND SLOVAK REPUBLICS**

HG program); (6) representatives of other related donor programs (e.g., Center for Clean Air Policy, other AID environmental initiatives--to learn more about their activities and discuss opportunities for collaboration); and (7) the AID Missions in both Republics (to review findings and recommendations). Following this mission, similar discussions have been held with four additional cities, bringing the total to 14.

Another mission, in December, yielded more detailed planning for an action agenda and discussions with Mayors and other officials on schedules for the next phases of the program.

## 2. MAIN FINDINGS OF THE STRATEGY ASSESSMENT

This preparatory work has indicated both a strong need and an extremely promising opportunity for sizeable LGHP programs in both the CR and SR over the next few years.

1. The **commitment to decentralization remains strong** in both Republics. Ministries in the SR as well as the CR stressed the need to "move government decision making down closer to the people". With this devolution, **municipalities have a critical role to play as change agents** in the economic and social transformations now underway nationwide. To take advantage of that position, they will have to see themselves as primarily responsible for their own destinies, be willing to innovate in the best interests of their citizens, and largely relinquish their traditional dependence on guidance from central officials.

2. **Municipalities lack the skills and the systems** needed to perform the many governmental functions being devolved to them, particularly with regard to the new approaches required to support a market-oriented economy. The **need to strengthen their capacity is enormous**. Republic level officials responsible for local government seem to recognize that the best approach will be to help the municipalities build capacity for themselves by their own designs rather than trying to control the process in detail from the center.

3. Legislation totally restructuring public revenues was passed in 1992. Both Republics have moved ahead to implement it as scheduled on January 1, 1993. That legislation introduced new taxes (e.g., VAT, property tax) and substantially reduced prior reliance on the payroll tax. Local governments are to receive sizeable shares of the new taxes but it is certain that the absolute level of **municipal revenues from central budgets will decline substantially next year** (see discussion in Annex B). There is a growing recognition at all levels that **municipalities will have to become much more efficient and self-reliant as well as more responsive to the demands of local citizens, but most local leaders do not have a full understanding of what that implies or how it can best be achieved**.

4. **Municipalities in both Republics generally recognize that the four substantive themes assigned by AID to the LGHP contract warrant highest priority attention** and that, although they focus directly only on physical development, they may be the most important tools available to them to achieve broader objectives. For example, both the privatization of their communal housing stocks and the disposition of their land resources will be critical in enhancing a municipality's overall fiscal position, and appropriate strategies for land development may be central to stimulating economic growth. These aspects of municipal development have an instrumental role to play in national economic restructuring.

5. Based on our descriptions of the options and their descriptions of their needs **almost all Mayors we talked to requested AID technical assistance under the LGHP and have definite, relevant projects for us to work on that they regard as top priorities. All indicated a willingness to try market-oriented approaches that are far from conventional in the CSFR. Republic officials and the Associations of Towns and Cities were also strongly supportive of our basic approach.** We did not assume this would necessarily be the case since these officials have been exposed to many offers of consulting assistance over the past year and have become skeptical about much of it. We believe the positive response we received is due to three factors: (1) the four substantive areas selected for this contract are indeed high priorities for them; (2) they regarded the way we talked about approaching them as realistic; and (3) prior AID assistance in this field has a good reputation for following through (most of the officials we met knew about our prior work with the condominium law, housing allowance program design, and accomplishments in housing privatization and management work with Prague Districts 2 and 6).

6. Virtually all Mayors mentioned the lack of finance for infrastructure improvements as one of their most severe constraints at present. Funds for local public works from the upcoming Republic budgets have either been sharply cut back or eliminated altogether depending on the category. No other alternatives exist at present. Most Mayors are disappointed in the lack of attention to this issue by the Republic banks and may have been attempting to set up their own Municipal Banks, either independently or in conjunction with other municipalities in their regions. When we informed them of the nature of the HG instrument and its possibilities, **Republic officials and Mayors uniformly expressed strong interest in the possibility of USAID technical assistance to help them develop a market-oriented credit system to finance municipal infrastructure and in using a Housing Guaranty Loan in conjunction with that system.** In both Republics, it appears that this system can be integrated with the banking system (which is now being privatized) thus reinforcing privatization of the financial sector and bringing municipal capital financing within the privatized framework.

### **3. PROPOSED STRATEGY**

#### **Program Goal**

We believe that these findings present an unusually promising opportunity for AID's program to have a marked influence in establishing innovative strategies for local governments in the CSFR and, thereby, on their long term effectiveness. They justify mounting two sizeable programs under the LGHP; one for each Republic. Considering both needs and circumstances, the goal should be to:

*Strengthen local governments to act as self-reliant change agents in transforming the development and management of the physical city so as to best contribute to economic restructuring, capital market development, and other societal objectives.*

The link between local government performance and overall economic and capital market development in these countries has become vital as so many of the critical functions of all governments have been transferred to the local level. Municipalities now control many of the factors that are essential to all private enterprise; e.g., the provision of adequate infrastructure, the process by which land can be developed for business use, regulations that affect business entry and ongoing activities. The way the Mayors perform these functions can do much to either constrain or enhance private market activity.

Furthermore, it is expected that the local share of all government expenditures will increase markedly over the coming years, thus the behavior of the Municipalities will have a great deal to say about the effectiveness of national fiscal policy. In many areas, they are now the key actors in the reform process. For example, given their inheritance of all state communal housing with its enormous continuing operating deficits, the Mayors have the responsibility for ending (through privatization) one of the most formidable remaining public-sector drains on national economic performance.

Finally, severe existing deficiencies in local public infrastructure imply that such infrastructure should receive a high priority for capital financing in the decade ahead. Given this (and also their role in housing), Municipalities are sure to play an important role in the institutional development needed for the evolution of effective capital markets. Again, their behavior in this regard can either further or constrain sensible restructuring.

#### **Overall Strategy**

While the opportunity for influence is substantial so is the opportunity for failure--at least the possibility that substantial sums will be spent without having much real impact. We have been attentive to this concern in the design of the strategy, which has four basic tenets.

**The first is that the programs should offer technical assistance and training in all four of the substantive areas defined for the LGHP.** These four are a natural constellation, heavily interrelated. For example, there is no way for a Mayor to develop a sensible capital budgeting strategy without looking at the potentials (problems, needs, and opportunities) in housing and land development, as well as infrastructure. Clearly, CR and SR Mayors see them as interrelated and express needs for technical assistance in all of these areas.

**The second is that the program should offer a mix of direct technical assistance (to individual cities), assistance in setting up intergovernmental institutions and financing systems, and broader training and dissemination of ideas,** but that each must be carefully designed if we are to avoid serious risk of failure.

Performing training and dissemination alone would be to risk lack of impact. The field is replete with training programs offering well attended seminars and conferences whose participants are appreciative but go back afterwards to do their work exactly as they did it before. Also, training alone would mean the program could never claim concrete achievements (like infrastructure system improvements, public land marketed to and developed by the private sector, housing units privatized). Finally, without learning about local circumstances from direct TA on real problems in-country, it is likely that the training sessions would themselves be at least somewhat off the mark for their intended audiences.

On the other hand, performing local technical assistance alone would, because of its cost, limit us to involvement in only a few cities. Those cities would benefit, but lessons learned from them would not be transmitted. The opportunity we have to have a significant impact on local government practices and performance nationwide would be lost.

Finally, direct work with individual cities and broader training and dissemination together, will not have the required impact if key reform themes and policies are not supported at the Republic level. In several cases, it will be imperative for us to work with Republic authorities to modify central government programs or legislation so that local governments can function efficiently. We expect to assist in designing intermediate financing institutions or grant-in-aid programs that can more effectively support local initiatives. The program will address these constraints directly, as it did in assisting in preparation of the condominium law. Wherever possible, it will work through the Associations of Towns and Cities to strengthen their role as technical representatives of the cities in influencing central level regulation and policies.

We propose starting immediately with work with individual cities and with Republic officials on factors that constrain local governments (particularly infrastructure finance), and beginning broader training and dissemination soon thereafter; i.e., we do not propose to wait until our first city projects are complete before we begin dialogues with a larger number of

cities. In fact, if we are attentive, those dialogues, built around conferences and broader training experiences in the relatively near term, should make us more effective in our direct TA experiences with individual cities and help us understand how best to generalize from them.

**The third is that the program should support and encourage local government strategies that are consistent with principles for effective urban development developed over the years by AID-PRE/H—most important here, that cities should be self-reliant, entrepreneurial, and efficient, promote market-oriented development processes, and retain focus on improving conditions for the poor.** This means the LGHP should avoid assistance that runs counter to the philosophy of restructuring now being followed in these Republics. We should be helping local governments *replace* "old structure" institutions rather than providing TA that will strengthen such institutions. We should be encouraging land disposition, cost recovery, and alternative financing mechanisms (e.g., credit) that will help to break the traditional reliance of local governments on central grants to fund their capital projects. We should be helping municipalities privatize communal housing rather than strengthening the old bureaucracies that traditionally managed it, we should be encouraging them to facilitate the development of land by the private sector (under appropriate local government guidelines) rather than to create or strengthen government agencies to do so.

**The fourth is that the program should attempt to support the development of a Housing Guaranty loan, structured in a manner that will facilitate the development of a market-oriented system of credit for financing the capital needs of local governments.** Technical assistance should be designed to support the objectives of the HG program.

Consistent with these tenets, we propose a program with three major components:

1. Work with individual cities (both intensive and short term assignments).
2. Work with Republic level authorities and financial institutions (to assist in developing a credit finance system for local infrastructure investment and to develop effective rules and guidelines to govern municipal finance and intergovernmental financial relations).
3. Broader training and dissemination.

### **Work With Individual Cities**

We propose direct work with individual cities at two levels: (1) intensive assignments, where teams would work closely with municipal officials for up to one year on their overall investment strategy and two to three concrete projects; (2) short-term assignments, where our advisors would work for a shorter period on one specific assignment (most often relating to

assistance in the preparation and appraisal of projects to be funded under the proposed municipal credit system--see further discussion below).

**Intensive Assignments.** In the intensive assignments, there is a need to establish definite work plans to assure concrete objectives will be achieved, but at the same time, retain enough flexibility so that both our consultants and municipal officials can shift to higher-payoff options as they jointly discover them.

We expect that this might run something like the following: In the first stage, our team would complete a specific assignment at the request of the Mayor (e.g., perform analyses to help the city select an effective strategy for developing its sanitation system). As that work is underway, the LGHP team will be learning more about the city and its broader problems and opportunities. By the time the first assignment is complete, the Mayor should have developed more confidence in the team and other priorities assignments would be motivated; e.g., review of physical, financing, and staging plans for a major land development project; design of an economic development strategy for the city; design and initiation of an infrastructure maintenance program and/or and infrastructure financing plan. In line with the basic tenets of the strategy noted earlier, emphasis in work with individual cities will be given to topics that support the proposed HG program (see discussion below).

Each city we work with would have to make a commitment up front to take the work seriously: for example, by clear commitments of staff time to work with us, time of the Mayor and other top officials to review and act on results and recommendations, provision of office space, etc. In each case, the city would be expected to set up a special steering committee for the ICMA work.

Given budget constraints (see discussion below) it is likely that we can support no more than two small teams working directly with cities in each Republic at any one time. We expect that an intensive assignment with a specific city might last for up to one year. Our teams would always be on the alert in looking for high-payoff project opportunities in other cities as the work proceeds--opportunities that might not be visible today. At this level over a three year project period, it would be possible to complete intensive assignments with about 6 cities in each Republic, phasing out of some and into others as opportunities suggest themselves as the work proceeds. (All proposed shifts in work priorities within cities, or shifts to new cities, would be of course reviewed and approved by AID before they are initiated).

This approach suggests an emphasis on projects with cities that will accomplish priority development objectives rather than just "building equipment" to help them do so in the future. For example, we would concentrate first on helping the city (A) privatize its housing stock, accomplish an efficient private-public collaboration in land development, or initiate a water system upgrading and maintenance program, rather than (B) restructure its budget formats and planning procedures, or build a housing information system. Clearly,

such equipment-building efforts (category B) might be a natural outgrowth of our projects, but our first priority should be in helping the cities achieve concrete developmental objectives.

**Short-Term Assignments.** At the same time, we would work with a broader range of cities around specific activities in a series of short-term assignments. In most cases, these would focus on the central themes of this program: developing local infrastructure investment strategies and preparing and appraising capital investment projects consistent with those strategies. By furthering the development of a large number of well thought out and economically feasible infrastructure investment projects, this would make a direct contribution to the success of the proposed municipal credit system (see discussion below).

### **Work With Republic Level Institutions**

**The Municipal Credit System and a Housing Guaranty Program.** As noted, the lack of finance for local infrastructure improvements is one of the most severe constraints on urban development in both Republics. As Republic budgets can no longer be relied upon as a major source for such funds, the only alternative may be for local governments to leverage the recurring revenue streams they will receive under the new tax law into capital financing, which can then be used to pay for infrastructure investments. We propose under the LGHP to provide assistance to both Republics in developing municipal credit finance systems that will make this possible.

Our suggested approach is described in Annex A. We argue that municipal lending should be oriented to market interest rates, rather than enjoying across-the-board subsidies, and that municipal loans should be made through standard banking institutions rather than through any permanently separate government channels. Liens on inter-governmental transfers are likely to offer the most practical form of security to limit municipal credit risk. Several institutional options are possible, including the establishment of a temporary Republic level municipal fund which could lend to banks and other financial institution which, in turn, would onlend to municipalities (or alternatively act as a secondary purchaser of municipal loans initiated by banks).

An AID Housing Guaranty (HG) Loan, now offered on terms that should be attractive to both Republics, presents one way to partially capitalize such a fund. We propose that technical assistance under the LGHP be applied to assist in the overall design and start-up of the new municipal credit finance system and in structuring HG loan arrangement should the Republics decide to make use of that opportunity (although, we expect that additional AID technical assistance outside of the LGHP would be required after start-up). As noted earlier, priority would be given in both intensive and limited technical assistance assignments with individual cities to the local preparation and appraisal of projects to be funded under the new system.

**Guidelines for Municipal Finance.** New municipal finance laws and regulations have not been drafted in either Republic. The new national revenue systems which went into effect in January 1993 will represent a traumatic change. Officials in both Republics believe it would be wisest to monitor experience under the new system over the coming year and then, based on lessons learned, draft appropriate laws and guidelines. They have asked for experts under this program to assist them in monitoring and analyzing change, and then in preparing relevant laws, guidelines, and training for municipalities.

### **Training and Dissemination**

In this component of the program, we are guided first by the reality that expatriate trainers cannot permanently change the system nationwide in just three years. Our main objective, therefore, should be to help build and restructure and the country's indigenous training and technical assistance system for local governments in areas related to our substantive focus--not just to provide direct training and TA ourselves.

This means we should be working with and through indigenous institutions in each of the elements of this component, which include: (1) proposing, designing, and participating in conferences and seminars; (2) designing training curricula and training trainers in the use of the curricula in ongoing staff training programs for municipalities; (3) translating and disseminating key documents (reports on city projects, more general policy reports, etc.) to large numbers of municipalities; (4) working with universities and other training institutions to build our themes into their curricula.

The CR and the SR each have one Association of Towns and Cities (ATC) and we propose working closely with these associations in all elements of the program. This represents a substantial advantage. Circumstances in other Eastern European countries are not yet as settled (e.g., in Hungary there are several competing associations, in Bulgaria no strong association has yet emerged). In the CR and SR we can go farther to design our work in a manner that will strengthen the ATCs (even though that is not a primary objective of this program).

Each of the ATCs has established a separate Foundation to provide training (with support from the European Community's PHARE program) and both are enthusiastic about our developing conferences, seminars and training courses that can be offered as a part of the overall programs of these Foundations. Offering training under the auspices of the ATC foundations (rather than any Republic Ministry) will help assure that the program will remain "demand driven"; i.e., the Mayors will have a strong say in assuring that the directions taken remain consistent with their true priorities.

Conferences and seminars would be designed around key substantive elements of the program. For example, one is certain to focus on developing infrastructure improvement and

maintenance strategies and techniques for financing them. This conference would open with presentations on general principles, followed by case studies offered by our city-team consultants and/or the Mayors of the cities in which we are doing direct work. Plenty of time would be left for discussion and sharing of experiences. Other conferences would focus on, for example, techniques of developing municipal lands consistent with economic restructuring goals, and updates on housing privatization and management strategies. Mayors and their key staff would dominate the lists of participants in all such conferences, but ATC and Ministry staff would also attend. In some cases we might hold one Republic level conferences in the capital city--in others we might offer the same event in several regional centers.

Training programs (all developed to be offered by indigenous training institutions on an ongoing basis) would focus more on lower level staff: A training curriculum on housing privatization and management for the CSFR has already been developed by the Urban Institute and OKM Associates under a prior contract. We expect to develop similar programs related to land development (including technical courses on market analysis, real estate project financial analysis, and local impact analysis), and infrastructure planning and financing (including courses on strategic capital planning, cost analysis, alternative financing techniques).

The work of developing conferences, seminars, and training programs for the LGHP in any Eastern European country will be made most efficient by planning to offer the same events, with adaptation as needed, in other countries. In other words, the ICMA Consortium plans to develop one basic set of seminars and courses (with associated training materials) on municipal land development and disposition strategies and techniques, and then offer them, with adaptation, in all countries in the region (in contrast to trying to "reinvent the wheel" in each country). This approach will also allow ICMA and AID the opportunity to better control quality and assure that the substance being offered remains consistent with PRE/H development philosophy.

### **Program Clients**

Since PRE/H assistance began in the CSFR, the overall program has reported directly to the Ministries in each Republic designated as being responsible for housing and municipal policy, but it has not worked *solely* for them. While we have regularly sought and gained the approval of those two Ministries for our approach (and kept them up to date on our progress), they have encouraged us to work with and for other clients on a day to day basis; e.g., the office of the Deputy Prime Minister for Legislation, the ATCs, and individual cities.

We assume the same working relationships for the LGHP. The designated Ministerial level counterparts for this contract are the Ministry of the Economy in the Czech Republic (Jiri Mejstrik, Director for Local Government) and the Ministry of Finance in the Slovak

Republic (Jozef Miks, Director of Local Government Budgets). We will involve the two Ministries in planning our approach and will regularly review progress with them and be responsive to their suggestions, but the approach itself calls for our working with other clients more directly without detailed review and approval by the Ministries.

We anticipate a similar relationship with the ATCs; i.e., seeking their involvement in strategy development and keeping them informed of progress, with the understanding that we will also have direct working relationships with the Ministries, individual cities, and perhaps other institutions as may be appropriate. If the HG program moves ahead along the lines suggested here, substantial direct work will be required with the Ministries of Finance in each Republic as well as several financial institutions.

However, most of the direct work in this program will be with individual cities. Although as noted, we will maintain close collaborative relationships with many institutions, it is probably reasonable to say that *the primary clients in this program will be the Mayors of Czech and Slovak cities.*

### **End of Project Indicators**

It is impossible to quantify the outputs that will be yielded by a program of this kind. Specifying the types of outputs expected, however, should be a useful way to summarize what AID should expect to get for its money.

#### *Municipal Credit System and Housing Guaranty Loan*

- System of credit finance for municipal infrastructure established and operating in accord with principles jointly established with LGHP advisors.
- Local currency equivalent of HG Loan resources invested in shelter related infrastructure benefiting below-median income households.

#### *TA Projects in Selected Cities*

- Infrastructure maintenance projects initiated and having effects (e.g., unaccounted for water reduced)
- Municipal infrastructure improvements (development and major renovations) initiated consistent with LGHP proposed strategies.
- Public-private land development projects initiated (hectares of land sold, square meters of business floor space and housing units produced, jobs created)
- Hectares of public land sold to private owners
- Housing units privatized (sold to tenants or other private owners)
- Housing units brought under private management

- Demonstration cities continuing to implement strategies developed jointly with LGHP advisors (housing, land development, infrastructure maintenance, infrastructure planning and finance, economic development)

#### *Training and Dissemination*

- Significant share of all municipal officials exposed to LGHP proposed concepts, strategies, and techniques through conferences, seminars, and receipt of written reports and training materials.
- Significant number of municipal officials received training under LGHP and taking advantage of training in subsequent work.
- One or more indigenous institutions providing training in accord with LGHP developed curricula on ongoing, self-financing basis.
- Principles, approaches, techniques of LGHP built into curricula of universities, the ATC foundation, and other institutions providing professional training for local government officials.

## **4. PROPOSED ORGANIZATION AND STAFFING**

### **Staffing Arrangements**

We judge that this program can best be accomplished with two related teams for each Republic: a central Program Management and Training team (PMT) and a City TA team (CTA) which would work under the guidance and supervision of the PMT. Because there are similar legal and other traditions in the two Republics and because the Consortium has promising candidates for the PMT staff who already have substantial work experience in both Republics, substantial efficiencies can be gained if the same PMT is appointed to serve that function in both Republics.

### **The Program Management and Training Team (PMT)**

The PMT would be composed of three continuing (but part-time) staff plus a number of others used from time to time. The first continuing position would be that of Program Coordinator. We believe that AID and ICMA will need to rely on one individual to be responsible for the overall development and operation of the program in these countries--one individual who knows country conditions (political and substantive) in some detail, who will be responsible for spotting key problems and opportunities ahead of time and proposing the adjustments that are sure to be needed as the work proceeds, and who they can call on at any time for a full and knowledgeable accounting of where the program stands in these countries and what mid-course corrections should be made next to assure it will be implemented effectively. Along with guiding the work in individual cities, the Program

Coordinator will also have primary responsibility for the design and implementation of all training and dissemination activities and will play a major role in monitoring and guiding the work of the CTA teams. For this position, we propose Tom Kingsley of the Urban Institute, who has served as the Contractor's Director for the PRE/H housing program in Czechoslovakia since it began in March 1991.

The second continuing position will be that of Infrastructure Finance Advisor. This individual will have primary responsibility for designing the municipal credit finance system and related HG program and for managing continuing implementation of these initiatives. He will also have major responsibilities for training development and guiding and managing the work of the CTA teams. It is understood that AID will be placing a PSC in each Republic to handle overall PRE/H program coordination, and these individuals will no doubt be responsible for AID internal HG administration if those programs are implemented. Nonetheless, this does not diminish the need for the separate Infrastructure Finance Advisor to provide continuing substantive advice and guidance in support of the HG and alternative infrastructure finance systems. We propose George Peterson, of the Urban Institute, for this position. He has been responsible for studies of urban infrastructure problems and finance opportunities in Czechoslovakia CSFR since December 1991.

The third continuing position is that of Field Coordinator who will be responsible for managing all logistical arrangements for the program in both Republics and will also contribute to substantive guidance and CTA management. For this position we propose Peter Tajčman, of Urban Research Inc., who has had similar responsibilities related to all PRE/H programs in the CSFR since they began.

All three of these continuing staff will also be responsible for writing substantive reports and case studies that will be used as the basis for dissemination program. Each will also devote some time to participating in direct city projects with the CTA teams. Other personnel charged to the PMT will be mostly short-term staff used in developing and delivering conferences, seminars and training programs and arranging for their logistics.

### **City Technical Assistance Teams (CTAs)**

As noted earlier, these teams, will provide technical assistance to individual cities along the lines already described. Each team would probably complete intensive work with three cities over the three year program implementation period and perform short term assignments in a considerably larger number. These teams will be composed of primary substantive experts in the areas most suited to city physical development priorities and the substantive orientation of this program; e.g., municipal finance, water supply, sanitation, solid waste, land development, and housing privatization.

## **Staffing Recruitment**

Although we have a number of ideas about them, staff and consultants in addition to the three leadership positions for which we have proposed candidates remain to be recruited. These additional personnel will be drawn from lists of candidates proposed by the various institutions in the ICMA Consortium with selections made under the guidance of ICMA.

## **5. SELECTING CITIES FOR INTENSIVE TECHNICAL ASSISTANCE**

### **Criteria for City Selection**

The purpose of technical assistance in selected cities is not only to provide concrete benefits to those cities, but also to complete projects that will serve as good examples for other municipalities to emulate in line with PRE/H principles. With this understanding, we have chosen several criteria for city selection:

1. The Mayor and other top officials should have developed a clear understanding of their TA needs and have exhibited a willingness to innovate consistent with PRE/H endorsed principles and approaches for reform.
2. The city should be large enough to make our assistance worthwhile (international research suggests that very small cities are not as important to the national economy as larger ones and they do not have the same problems and opportunities warranting the kind of assistance we can best provide). Also, successful projects in larger cities are more likely to be emulated by cities of all sizes.
3. The city should not be facing such severe economic or political problems that it will be unable to give sufficient attention to the reform agenda.
4. Over time, cities should be selected from a variety of regional circumstances to show how reforms we work on can be implemented in different settings ("regional development" is not one of the goals of this contract and, given the type of assistance we will be providing, focusing on several cities in only one region would not contribute substantially to that goal).

Table 1 shows recent population trends for cities of different sizes in both Republics. In both, cities with populations above 20,000 accounted for *all* of the 1980-90 population growth (smaller towns and rural areas have lost population). Cities over 20,000 account for 47 percent of the total population in the CR and for 41 percent in the SR. We have restricted

**Table 1**  
**CITY POPULATION GROWTH, CZECHOSLOVAKIA**

	No. of Cities	Population (000)		1980-90	Change
		1980	1990	(000)	%/yr.
<b>CZECH REPUBLIC</b>					
<b>CITIES OVER 20,000</b>					
Over 100,000	6	2,252	2,308	56	0.25
50,000-100,000	18	1,235	1,273	39	0.31
20,000-50,000	40	1,104	1,177	73	0.64
Subtotal	64	4,591	4,759	168	0.36
OTHER CR		5,701	5,540	(161)	-0.29
TOTAL CR		10,292	10,299	7	0.01
<b>SLOVAK REPUBLIC</b>					
<b>CITIES OVER 20,000</b>					
Over 100,000	2	583	676	94	1.50
50,000-100,000	9	544	640	95	1.63
20,000-50,000	29	686	836	149	1.99
Subtotal	40	1,813	2,152	338	1.73
OTHER SR		3,178	3,117	(60)	-0.19
TOTAL SR		4,991	5,269	278	0.54

our choice of candidates almost totally to cities above 20,000 (a complete list of them is provided in Annex C) and given even more focus to those above 50,000.

### **Candidate Cities**

To develop a list of candidates, Urban Research staff interviewed ATC representatives and other knowledgeable individuals, and reviewed data, all relative to the criteria noted above. In the CR, they reviewed the results from about 200 responses to a survey on Municipalities expressed TA needs conducted by the Ministry of the Economy. The selections of candidate cities are listed below (Note: numbers in parens are 1990 populations in thousands; \*\*\* indicates those where the strategy team has held discussions with the Mayor or Deputy Mayor during October and early November) (See also, Republic maps in Annex C).

#### Czech Republic

- Praha (1,212) \*\*\*
- Brno (388) \*\*\*
- Plzen (173)
- Olomouc (106) \*\*\*
- Liberec (102) \*\*\*
- Hradec-Kralove (99) \*\*\*
- Usti nad Labem (99)
- Jihlava (52) \*\*\*
- Tabor (36) \*\*\*
- Pisek (30) \*\*\*

#### Slovak Republic

- Bratislava (442) \*\*\*
- Kosice (235) \*\*\*
- Banska Bystrica (85) \*\*\*
- Zilina (84) \*\*\*
- Trnava (72) \*\*\*
- Trencin (57) \*\*\*
- Levice (34)
- Dolni Kubin (19)
- Kysucke Nove Mesto (17)

## **Initial Selections**

Based on the strategy as stated, the need at present is to select just two cities in each Republic as starting points. We identify below the initial selections that have been made. These selections are the product discussions with counterpart Ministries (Ministry of the Economy in the CR and Ministry of Finance in the SR) and AID Directors in each Republic. In earlier discussions, we reached general agreement on criteria. In December, we reviewed the results of our field work in the cities, discussed comparative advantages and disadvantages, and jointly agreed on the four cities noted below as starting points.

Annex C provides a more complete discussion of characteristics, and issues to be addressed, in each of these cities. It should be noted that all four of these cities identified the establishment of a credit system to finance municipal investment as a very high priority--this will be addressed separately by the activities of the PMT in both Republics.

**Czech Republic.** Almost all cities on the list offer promise as counterparts in this program. Some, however, have immediate problems that might make it difficult to begin an assignment with them at this point (e.g., political uncertainties surrounding changes in leadership, priorities not clearly formulated as yet, economic problems that would prevent them from giving enough focus to the LGHP agenda). The following cities appear to be most appropriate for initial assignments.

1. *Liberec.* Mayor Jiří Drda is well organized and has been noted already for many innovations. He is eager for AID technical assistance. The issues that best fit program emphases and his priorities are: (1) analysis of housing conditions as a basis for forming a housing strategy; (2) working out a strategy for providing adequate sewage collection in areas now not well served in a manner that will link effectively to the new regional trunk sewer extensions being provided by the Republic; (3) developing a strategy for take advantage of immediate land development opportunities and structuring a process for the managing the marketing and disposition of city owned lands over the longer term (they have analyzed a few sites but need help with others).

2. *Hradec-Kralove.* Mayor Martin Dvořák, an economist, is also attempting major reforms in several areas. His priority concerns include: (1) developing a strategy for improvements to the city's water supply system focusing on fringe areas where service is now seriously deficient and working out institutional relationships with the recently privatized water company that serves the area; (2) preparing an approach and longer term process and strategy for the management of city lands, emphasizing early development of sites with strong market potentials whose development could most enhance job generation and municipal revenues; (3) an approach to valuing municipal owned properties for sale and in devising a disposition schedule; (4) improving local property records and, if possible, developing a

computer based GIS system. (The first two of these priorities are likely to be the most appropriate starting points under this program.)

**Slovak Republic.** As was the case in the CR, almost all cities on the SR list offer good potentials, but (for similar reasons) several are not at the point where a program of this type would be appropriate in the near term. Initial selections are:

1. *Banska Bystrica.* The city is also noted for progressive leadership under Stanislav Mika. Their highest priority for assistance is in designing (financing, scheduling, procedures, etc.) a program for upgrading their sewerage system which has suffered from undermaintenance, and for dealing with problems of pollution arising from inadequate wastewater treatment in upstream communities. Other priorities include: (1) the preparation of a strategy for solid waste disposal; (2) formulating a long term process and program to create income-earning land development projects; and (3) in developing a housing privatization and management strategy.

2. *Trencin.* Mayor Stefan Rehak and his staff have earned the city a reputation for innovation and self-reliant activity. The Mayor's priority assistance needs that match this program's themes are: (1) developing a strategy for extending the city's sewage system--the area of the city on the left bank of the Vah River has considerable residential (family housing) development and offers good potential for future growth but it was neglected in state investment planning during the communist era; (2) evaluation of land development project opportunities and building in a process for the ongoing management and development of the city's land resources.

## **PROGRAM START-UP**

Designing concrete work plans for starting up the program is challenging. Obviously, there is too much uncertainty about the content of the work to provide detailed tasks and staffing allocations even a year ahead. On the other hand, without some sense of commitment beyond month to month decision making, it will be impossible to recruit good staff and consultants who will make this work a top priority (i.e., so that they will plan ahead so as to be available when this program needs them). We suggest a compromise, as follows, with the general idea that both AID and the ICMA Consortium would try to work toward a six-month cycle of work assessment and revision of assignments:

1. A six-month allocation would be made initially to cover program coordination and logistics activities of the PMT.

2. At the start, three to four month allocations would be made to cover the next stages in designing the municipal credit systems in each Republic and the development of HG programs to support them.
3. Primary technical assistance at the beginning of the program would be focused on specific development activities that respond to the needs of the four selected cities as a part of the intensive city assistance component of the work. Individual work programs would be designed at the outset to cover one or more of the following priorities in these cities: (Short term assistance to additional cities--focusing on identifying projects that could be financed under the new credit system and providing guidance on developing local investment programs--would be phased in soon thereafter).
  - a. *Liberec*. Sanitation system development, housing privatization, land development.
  - b. *Hradec Kralove*. Water system development, land development.
  - c. *Banska Bystrica*. Sanitation system development, land development, solid waste management.
  - d. *Trencin*. Sanitation system development, land development.
4. Definite plans to cover broader training and dissemination would be phased in later as results from the initial city projects began to flow in to form a basis for this work. The ICMA Consortium would do much more detailed planning for training and dissemination in the short term so that solid six-month work allocations could be made at the end of the first half-year of experience.

Over the first half-year, AID would of course receive frequent and regular updates on the progress of the work in all areas and have the chance to review specific work areas in depth as short-term work plans are designed. At the end of the 5th month the PMT would prepare a more detailed progress document on all aspects of the program and a draft proposed work plan for the next six months. The plan would be detailed enough so that after AID review, the next set of definite work allocations could be made easily.

**ANNEX A**

**PRELIMINARY PROPOSAL  
FOR USE OF HOUSING GUARANTY (HG) LOANS  
TO SUPPORT MUNICIPAL LENDING SYSTEMS  
IN THE CZECH AND SLOVAK REPUBLICS**

**1. PURPOSE**

To strengthen the self-reliance and fiscal independence of local governments in a way that supports economic re-structuring and is consistent with a private-sector, market oriented financial sector.

**2. GOAL**

To use a USAID Housing Guaranty loan and associated technical assistance to help establish a municipal lending system that can finance a substantial part of local governments' infrastructure investment needs.

**3. PARTICULAR CONSTRAINTS THAT ARE BEING ADDRESSED**

Local governments in both republics now have no reliable source of capital financing. In the past, most local capital investment was carried out by the central government, which built capital facilities, then turned them over to state enterprises or local authorities. For the past two years a combination of direct state funding and capital grants to local governments has partially sustained local capital investment. However, separate capital grants now have been abolished. The federal and republic governments are rapidly withdrawing from direct construction for municipalities.

The result of these shifts has been a drastic decline in local capital investment. For example, in Trencin in 1992 planned capital expenditures were cut back by 72 percent as compared to a reduction of 56 percent in general recurrent spending and a 26 percent reduction in subsidies to municipal enterprises. A similar picture is found elsewhere.

There is at present no mechanism for long-term lending to local governments. Even short-to-intermediate term lending (two years or longer) is extremely rare. Banks normally only provide municipalities month-to-month loans to cover cash flow shortfalls.

Yet the capital needs of local governments are very large. Municipalities have aging, under-maintained capital systems. They are gaining control of water and wastewater systems that have a large backlog of capital investment requirements. Environmental conditions are extremely poor, and many of the most urgent investments--ranging from completion of sewage treatment plants to replacement of coal furnaces with local gas networks--will fall upon local authorities to finance. Municipalities also must invest to support local economic development strategies.

Some municipalities have been able to support part of their capital investment budgets through sales of land, housing, and other municipally owned assets. Even when successful, this obviously is only an interim financing device. Moreover, it adds to pressure to dispose of municipal assets quickly, often without considering alternative strategies for fully realizing the economic value of assets.

Under the new tax and intergovernmental financing law, which takes effect in 1993, municipal governments will for the first time have substantial own sources of recurring revenue. The law confers on municipalities the revenues from the new real property tax, as well as a share of wage tax collections. It is widely expected that, as water and sewer systems are privatized or otherwise turned over to greater local control, the present restrictions on tariffs will be relaxed, allowing these enterprises to raise rates. The intergovernmental grant system is being revised so that, for the first time, municipalities have fixed entitlements to transfers, established by transparent grant formulas. It is expected that between 50 and 60 percent of municipal budgets will be financed from own-source revenues, with the rest coming from formula-driven intergovernmental transfers.

Although the revenue-raising capacity of the new tax system will remain uncertain until there has been experience with implementation, the new system greatly lessens local authorities' dependence on discretionary funding from central government, while strengthening local sources of recurring revenue. A major difficulty remains, however. Since there are no capital grant programs, how will municipalities finance their capital needs?

#### **4. CAPITAL FINANCING AND THE ROLE OF CREDIT**

Local government authorities must find ways to capitalize their new income streams if they are to adequately finance infrastructure investment. That is, they must leverage their recurring revenue streams into capital financing, which can then be used to pay for

infrastructure investments. There are essentially two options for doing this. Both should be vigorously pursued.

(a) Infrastructure services that can generate their own revenues through fees and charges can be privatized. The new owners can finance needed investment through infusions of equity capital, or by facilitating access to international and domestic lending, in return for control of the revenue streams these projects generate. Such an approach is being pursued for water and sewer enterprises, and for some local economic development projects.

(b) A more difficult challenge is posed by capital investment that does not yield direct financial returns, or where these returns are presently too uncertain (for economic or political reasons) to attract equity capital or qualify for project loan financing. A more general system of municipal credit is needed for these cases. Essentially, local governments' tax and transfer income has to be used as security for loan repayment.

Neither of these mechanisms provides a "magic" way to finance capital investment. Both have costs. Investors in water utilities or economic development projects must be able to raise prices to recover a return on their investment, and these higher tariffs are borne by consumers. General tax revenues that are used to repay capital borrowing are not available to finance other activities in a municipality's operating budget. Nonetheless, the importance of local capital investment is so great, especially at this juncture, that a mechanism that allows local authorities to convert future revenue streams into financial capital for investment has great value. It allows local authorities to strike the budget balance they and local taxpayer-voters desire between current services and investment, given the overall local budget constraint.

## **5. THE ESSENTIAL ELEMENTS OF A MUNICIPAL CREDIT SYSTEM**

A municipal credit system introduced in either the Czech or Slovak Republics should adhere to certain basic principles.

■ It should be consistent with other financial sector reforms that are being carried out, and be integrated into the overall banking system. Specifically, this means: (a) municipal lending should be oriented to market interest rates, rather than enjoy across-the-board subsidies; (b) municipal loans should be made through standard banking institutions rather than through permanently separate governmental funds. Any special municipal lending mechanism that is established should be designed to be transitional; that is, it should serve as a bridge to market-oriented lending to local governments by regular financial institutions.

- It needs to identify, clarify, and limit municipal credit risk. The reason that there is virtually no lending to local governments for capital investment purposes at present is that there is no way to measure or limit municipal credit risk. Since there is almost no experience with intermediate or longer-term lending to local governments, there is no empirical basis on which to assess repayment risk. Part of the purpose of a transitional system is to establish a track record for municipal lending, and to demonstrate that the system can be designed in such a way as to make credit risk extremely low.
  
- It should move away from real property as collateral. There is a natural inclination to secure loans with tangible property--such as land or buildings. This will be appropriate for some commercially oriented development projects. However, the legal procedures for foreclosing on municipally owned property are, to say the least, unclear. The political and practical difficulties of a commercial lender foreclosing on a water system or municipal building are still more profound. (Even in the United States, the impediments to municipal bond holders' actually claiming school buildings or other public property that has been offered as security for municipal loans have proved almost insurmountable in some states.)
  
- Instead, liens on inter-governmental transfers offer the most practical form of security. Under such a system, a municipality or other local governmental authority that borrows capital funds must enter into a contractual agreement that authorizes the Republic government to divert transfer payments directly to the lender in the event the municipality does not repay its loan on a timely basis. A system of this type can eliminate credit risk completely for the lender. It also eliminates credit risk for the Republic-level government, which may (legally or practically) have residual responsibility for local loan repayment. Since all loan payments on behalf of delinquent municipalities would be made by the Republic government from local transfer entitlements, and subtracted from the payments made to the locality, there would be no financial risk for the central authority, as long as local borrowing is limited to amounts that can be adequately secured by transfer entitlements. Liens on inter-governmental transfers have been used in many other countries to solve the problem of municipal credit risk. For example, municipal lending programs in Brazil and Colombia have totally eliminated problems of municipal re-payment through such means. In the United States, approximately half the state governments use some variant of this approach for lending to high-risk central city governments or central-city school districts. There have been no instances of default under such programs.
  
- In the Czech and Slovak Republics, the most suitable instrument to offer as security would be liens on local property tax receipts or local wage tax transfers. In the former case, the Republic government will collect the property tax on behalf of municipalities, returning revenues collected to the point of collection. In the latter case, localities are by law entitled to a fixed share of national tax collections. In both cases, borrowing municipalities would be providing as security tax revenue streams to which they are unambiguously

entitled, but which must be paid to them by agencies of the Republic. Thus withholding is administratively straightforward. Local borrowing would be limited to an amount that could be repaid, with some margin, by liens on these tax sources.

Note that the lien on "transfers" from the Republic government is a guarantee only. Local authorities are expected to budget debt repayments, and to adjust local fees and charges or other revenue and expenditure items under local control to ensure that debt payments can be made in full and on time. Only if this system fails would the lien on entitlement payments, as guarantee, be exercised.

## **6. MECHANICS OF LENDING**

A variety of institutional arrangements is possible under this system. Banks can lend their own funds to municipal authorities, secured by the intergovernmental guarantee. Or, to accelerate implementation of municipal lending, a special Municipal Fund can be established at the Republic level.

Under one option, the Municipal Fund could lend to banks or other financial institutions willing to make municipal loans. The Municipal Fund thus would inject capital funds into the banking system for the specific purpose of municipal lending. Banks or other lenders to municipalities would charge an interest rate that covers their own cost of capital from the Municipal Fund plus a margin to cover administrative costs and profit. Both the loans to municipalities, and the Municipal Fund's loans to banks, would be covered by the intergovernmental guarantee.

Alternatively, the Municipal Fund could act as a secondary purchaser of municipal loans initiated by banks. That is, all or part of authorized municipal loans could be sold at face value by the banks initiating the loans to the Municipal Fund. This mechanism guarantees banks a way to replenish capital committed to municipal lending.

Any funding provided by the Municipal Fund would, of course, be limited to authorized loans. The original bank lenders should retain partial exposure any loans they make, to ensure that the intergovernmental guarantee is not abused.

A number of banking institutions in the Czech and Slovak Republics have expressed interest in making municipal loans, if credit risk can be controlled. These include the Communal Banks being established with the Savings Bank system, the new municipal and regional banks being created in some parts of the two republics, and other specialized institutions within the current banking system. In principle, a Municipal Fund could on-lend on equal terms to all of these financial intermediaries. It is the municipal sector's interest not to become fully dependent upon a single source of credit financing.

## **7. THE ROLE OF A HOUSING GUARANTY LOAN (HGL) AND INTERNATIONAL FINANCING**

The Housing Guaranty Loan (HGL) offers one way that a Municipal Fund could be capitalized. The HGL involves borrowing from the United States private capital market, with a United States government guarantee of repayment. The guarantee results in the lowest possible market rate of interest. At present, 30-year loans with five-year grace periods on principal repayment carry interest rates in the range of 8.00%, with an additional 0.5% for administrative and guarantee costs, for a total interest-rate cost in the range of 8.5%. Variable-rate loans, tied to LIBOR, now carry initial interest-rate costs in the range of 4.5%. Housing Guaranty Loans have been authorized for Eastern Europe. Annual loans between US\$5 and US\$20 million for each Republic are possible, depending upon the scale of municipal on-lending that has been identified, and the extent of HGL demand in other Eastern European countries.

There are both potential advantages and potential disadvantages to using a HGL to capitalize the Municipal Fund.

Among the advantages:

- Borrowing at this rate is potentially less costly than other marginal sources of funds. The 30-year loan period also is potentially attractive.
- The loan can serve as a valuable precedent for accessing international capital markets for municipal capital finance.
- Depending upon a Republic's financial situation, access to foreign exchange may be valuable. The Housing Guaranty Loan is made in US dollars.
- A Housing Guaranty Loan would be accompanied by a substantial technical assistance commitment, financed from grants, to help the host republic establish a Municipal Fund and to work with the Fund, individual municipalities, and the Association of Cities and Towns, to establish procedures for project appraisal and capital budgeting.

Among the disadvantages of HGL capitalization of the Municipal Fund:

- The borrowing republic takes on foreign exchange risk. The Housing Guaranty Loan requires that the host republic guarantee loan repayment. The projected foreign exchange risk, if any, can be incorporated into the municipal lending rate.
- Depending upon each republic's macro-economic situation, additional foreign indebtedness may or may not be advisable.

*It needs to be emphasized that Housing Guaranty Loan financing, or other external financing, is not crucial to operation of the Municipal Fund system outlined above. This is essentially a domestic credit system. Initial capitalization through a HGL, with associated technical assistance, is one option for launching a Municipal Fund.*

## **8. ISSUES**

*Question: How much technical appraisal of projects should there be?*

Most Municipal Funds in the developing world have gotten into trouble by demanding that the Fund itself take on too much responsibility for project identification and project appraisal. In a decentralized governmental system, of the type that both the Czech and Slovak Republics are attempting to establish, it is appropriate that the principal responsibility for project identification, project appraisal, and project preparation lie with local government. Especially at the outset, the Municipal Fund can facilitate local governments in accessing technical assistance for project design and economic appraisal. Projects would have to meet Fund guidelines in order to qualify for Fund financing. However, the lending system should be designed so that as much project assessment as possible is carried out by the municipality, on the one hand, and by the direct lender, on the other. The lender's interest, in turn, lies primarily in the financial security for its loan. In a decentralized system of municipal finance, municipal authorities must take the ultimate responsibility for project selection, by recognizing that even if a project goes bad, the loan costs must be serviced in full.

*Question: How much modification to current law governing local taxes and intergovernmental transfers is necessary to implement a system of the type proposed?*

It is not clear how much modification to existing law would be required. That is one issue to clarify in the next trip. However, the objective would be to make the system as simple as possible, by having municipalities enter into voluntary contractual agreements to have their tax revenue entitlements withheld, and diverted to the lender, in the event of late payment of municipal loan amounts due.

*Question: How can a lending system of this kind be targeted to subsidize capital investments where there is a national priority or a national interest for investment to take place?*

It is probable that at some point national priorities will make the Republic governments want to subsidize certain types of local investment. All developed countries have mechanisms for reducing the costs of preferred infrastructure investment. One mechanism for targeting investment priorities is up-front capital grants. Republic-level

grants for certain types of investment (e.g., wastewater treatment plants that have large external benefits, or road investments that carry benefits beyond the local area) could easily be blended with market-rate lending through the Municipal Fund and associated banks. This procedure has the advantage of identifying and funding the capital subsidy at the outset.

Alternatively, the Republic governments could add low-cost or zero-cost capital to the Municipal Funds' financing mix, and the Fund could pass on its lower costs of capital for certain types of investment projects, by lowering interest rates to municipalities. Although similar mechanisms are employed in a large number of developed countries, and in most environmental revolving funds in the United States, this approach tends to obscure the cost of capital subsidies and has greater potential for permanently separating municipal lending from market institutions.

*Question: What would be the normal interest-rate policy for municipal lending under the system?*

The Municipal Fund would lend to banks or other financial intermediaries making municipal loans at its true cost of capital. That is, the interest rate the Municipal Fund charged would cover the dollar interest-rate of the external loan, the estimated costs of foreign exchange risk (i.e., any projected devaluation of local currency with respect to the US dollar), and the administrative costs of operating the Municipal Fund. Technical assistance costs for helping municipalities develop and appraise projects could be funded separately, through external technical assistance financing, the central government budget, or charges for services.

Participating banks or other municipal lenders would charge interest rates that recover the cost of capital to them from the Municipal Fund, plus their administrative costs and any residual risk that is perceived to exist after the intergovernmental guarantee.

At recent rates of inflation, this procedure would yield strongly positive real interest rates. Since there is no current market for longer-term municipal loans, it is impossible to compare the municipal lending rate that would result with "market" rates. However, the interest rate should be well below what municipalities currently would have to pay for much shorter-term loans. A lower interest rate will be necessary to introduce local authorities to capital borrowing. Once the system has been in operation for a time, and has demonstrated that credit risks in the municipal sector can be minimized, banks should be willing to use their own capital funds for municipal lending. At that time, the lending rate would move to a true "market" rate, comparable to rates that lenders charge other borrowers for loans of comparable risk and terms.

*Question: What relationship would exist between the Municipal Fund and other vehicles that have been suggested such as an Environmental Revolving Fund in the Slovak Republic?*

These mechanisms can easily be reconciled in principle. In fact, it would be highly desirable to segregate into a separate fund those capital investments--mostly, environmental investments--that national and international policy says should be subsidized. This Fund could receive grants and below-market loans from the Republic government and international aid agencies, passing on its subsidized cost of capital for the targeted investment projects. The Municipal Fund, in contrast, would raise its funds from international and domestic sources at market rates of interest, or at only modestly subsidized rates. It would lend to local governments for projects where cost recovery is feasible, or where the benefits of investment are local and thus it is appropriate for municipalities to bear the full cost of capital. Administratively, the two institutions should be designed to work in parallel with one another. The upcoming conference in Bratislava on the proposed Environmental Fund will provide an opportunity for comparing design approaches.

*Question: How much of a project backlog is there in the two Republics?*

The answer to this question is not known at present. As a result of the next trip, specific project proposals from Liberec, Trentin, and selected other cities should be identified for study. If this preliminary project description is received favorably, a follow-up trip in January would concentrate primarily on local project identification and project development. As a general observation: the capital needs of local governments are known to be very large, and the engineering capacity for project design is high. Most localities will require some assistance in the financial and economic analysis of projects, particularly in realistically forecasting market demand. However, the standards of financial analysis at the local level are also impressively high in many municipalities. All of this suggests that the capacity to design, appraise, and implement projects is likely to be much higher than in the typical countries receiving USAID assistance. Nonetheless, it is impossible to state at this time a probable magnitude of aggregate project financing.

*Question: What kind of technical assistance will be needed to make the project succeed?*

Technical assistance will be needed at three levels. Local governments and municipal authorities will require assistance in capital budgeting and capital planning, as well as in economic and financial project appraisal. These tasks fit fully into the draft strategy statement for municipal priorities in the USAID programs for the two republics. Additional technical assistance will be required in setting up the Municipal Fund and establishing its on-lending arrangements with participating banks, as well as in establishing the project appraisal process for the banks and Municipal Fund to follow. Finally, a modest amount of

technical assistance probably will be required at the Republic level to set up relations between the Municipal Fund and Republic-level agencies and to design the contractual agreements to be used as loan guarantees.

The great majority of this technical assistance is already contemplated in the country technical assistance strategies. The Municipal Fund and municipal lending arrangements would merely give this technical assistance greater institutional focus.

*Question: Where would the Municipal Fund be housed at the Republic level?*

The Municipal Fund's closest connections will be with the Ministry of Finance. It will need to use revenue collections by the Ministry of Finance as loan security, and will need to work out a simple way for municipal revenue entitlements to be withheld and transferred to creditors when required. Most of the macro-economic considerations regarding external borrowing lie within the province of the Ministry of Finance. Local grants will be disbursed through the Ministry of Finance, making this the appropriate locus for coordinating grant and loan policy. For all these reasons, the local government offices of the Ministry of Finance seem the most appropriate institutional home for the Municipal Fund.

\* \* \* \* \*

In this summary program description, we have attempted to anticipate and answer some specific questions about how the Municipal Fund could operate. There are, however, numerous design possibilities. We have not held any specific discussions with Czech or Slovak authorities about the institutional design of such a program. Obviously, these authorities would make any institutional determinations. They also are in position to take into account many other factors besides those identified here. Therefore, full discussion with these authorities is the appropriate next step in defining how such a program could in fact operate in practice, and whether there is substantial interest in proceeding with the general approach.

## **ANNEX B**

### **LOCAL GOVERNMENT AND MUNICIPAL FINANCE IN THE CZECH AND SLOVAK REPUBLICS**

This Annex describes the structure of local government in the two Republics and also reviews the current status of municipal finance and expected changes in the short term.

#### **LOCAL GOVERNMENT AND FINANCE IN THE CZECH REPUBLIC**

##### **Governmental Structure**

There are two basic levels of government in the Czech Republic, each with legislatures democratically elected by the constituents: (1) the central (Republic) government with its seat in Prague and (2) the more than 6,000 municipalities whose individual territories together fill the entire boundaries of the nation. Formerly, there were regional units of government but these no longer exist (although there is some current talk of re-creating some type of intermediate level government units). One important feature of local governance is that municipal officials have two types of responsibilities: "self-administration" where they carry out functions under the direction of their own local legislatures; and "state-administration", where they carry out other functions in the locality on behalf of, and under direction from, Republic level ministries.

There are also two other geographic types of governmental jurisdictions. One is the district, a unit of state-administration: i.e., a geographic area that is utilized as the unit for many Republic ministry functions, including revenue collection and construction permit issuance. There are 72 such districts in the Czech Republic. Quasi-legislative bodies exist at the district level, consisting of assemblies of local elected officials from the municipalities in each district. These officials, with votes proportional to the number of inhabitants of their municipality, make decisions on how to allocate district-collected revenues from certain taxes among the municipalities. In at least one district this assembly has divided itself into two bodies, one composed of the largest city's representatives and the other from all other localities; by mutual agreement, both bodies have to concur on any allocation of funds.

The other local unit, which exists only in the largest cities such as Prague and Plzen, is the Community District (so-called to distinguish it from the similarly-translated term for

the districts described above). Community Districts (CD's) are geographic sub-units which have elected boards and officials closely parallel to those of the municipalities of which they are a part. They carry out a number of governmental service delivery responsibilities, including operation of kindergartens and elementary and secondary schools and provision of social welfare. Prague's 13 CD's have also been given title to the governmentally-owned housing which elsewhere is generally the property of the municipalities. CD's have minor revenue-raising authority, such as imposing fees and obtaining rents from their property. Most of their budgetary support, however, comes from the government of their primary city.

### **Municipal Structure and Authority**

In the larger municipalities basic legislative power is lodged in an elected Board of Representatives which can have as many as 50 members. The Boards are organized along political party lines, much as is the national government. Board legislative functions include adoption of the annual budget.

The Board of Representatives in turn elects a Municipal Council (consisting of about 12 members in the large cities) from which are selected the Mayor and Deputy Mayors. Generally, Deputy Mayors are assigned as "super-commissioners" with responsibility over a number of municipal functions. In Plzen, for example, there are three such deputies. One oversees "economic" functions such as public enterprises, tourism and municipal finance and accounting. Another is responsible for "technical offices" such as planning, engineering, development control and public works construction, plus the management of city-owned housing and not-yet-privatized energy production. The third deputy covers "cultural" functions such as education, social welfare and public health. In Plzen, there is also a Secretary (sometimes referred to as the "city manager") with responsibility for environmental activities, roads and street lighting, legal services and audit. Several other municipal functions, such as the police and the fire protection service, report directly to the Mayor. The Municipal Council is viewed as a collective executive, roughly comparable to the cabinet in a parliamentary government.

Municipal responsibilities are divided in various ways in different cities. Also, the structures of city governments tend to be fluid, because there are still many decisions being made on how authority and responsibility ought to be allocated in the post-Communist era. Elementary and secondary education, for example, is now a local responsibility but with considerable Republic involvement and direction. This also is the case with regard to social welfare and health functions. These are viewed as national responsibilities administratively delegated to Municipal Councils (and not subject to policy control by the Boards of Representatives).

Municipalities enjoy a broad range of powers, including the right to contract with other public or private entities, to establish subsidiaries or enterprises of various kinds, to buy and

sell property and to borrow. Many municipalities are already substantial owners of land and structures of various types, although data on just what they own and what its value is cannot readily be obtained in some cases because of the poor state of property records.

### **The Municipal Role in Public Expenditure**

In the Czech Republic, an estimated 25 percent of total public sector spending currently takes place at the municipal level. This estimate is derived from a statement by a spokesperson from the Ministry of Finance that some 17 percent of the national budget goes to local government and estimates by several mayors that cities raise only about 30 percent of their total revenues from their own sources.

This places the Czech Republic well up on a world scale of total public spending that takes place at the local (or sub-national) level. For example, in the United States about half of the total public expenditure is by state and local government. The central/local relationship is similar to that in the U.S. in most other industrialized countries. By contrast, there tends to be a much smaller non-central share in developing countries. In a recent book on urban finance in the developing world, Bahl and Linn (1992) presented data for a number of developing countries indicating that only about 15 percent of total public spending takes place at the local level. In a recent survey of five Central American countries, the author found that local governments only accounted for between 4 and 10 percent of total public sector spending. While this is only a rough measure, it does suggest the substantial importance of the local government role in the Czech Republic.

The own-source share of municipal revenues appears likely to increase. While at present local own-source revenues account for less than a third of total local resources, the Ministry of Finance expects this to increase to around 50 percent in the coming year (largely as a result of gains in centrally-collected local revenues such as the real property tax). Some central government officials have even discussed a target for the own-source share of revenues in local budgets of as much as 70 percent. The Czech government's intentions in this regard were clearly stated in a recent article by Vera Kamenickova of the Ministry of Finance's local government unit (*Ekonom* 38/1992; pp. 48-9). The article notes that the government objective is to increase local decision-making through expanding municipal revenue-raising power as well as through reducing regulatory controls over municipalities.

### **Intergovernmental Fiscal Relationships**

The sharing of revenues and service delivery responsibilities between the Czech Republic and its municipalities is in a state of rapid change at present, as privatization and other basic changes in the role of government proceed.

Much of the financial aid that central government provides is in the form of shared taxes such as the national wage tax. Other intergovernmental aid comes in the form of subsidy payments for the operation of public housing, for teachers' salaries and for the costs of social welfare programs. Formerly, there were also substantial amounts of intergovernmental aid available for capital investment in infrastructure by localities. Among these were funds for water pollution control facilities and for electric power generation. At present, there are no specific capital grant programs and the only loan program for which localities are eligible is one for energy conservation.

Intergovernmental aid to local governments, starting in 1993, is anticipated to take the following form:

- Local property taxes will be collected by the district offices and then redistributed among municipalities on the basis of their origins. At present, there is no local discretion with regard to the nationally-mandated tax rates except to lower them, nor is any planned for the near future. Assessments will be set in a general law that fixes values by the area of land and structure and its location. In the absence of any market-based assessment process, the real property tax appears likely to encounter the same problems now confronting municipalities as they try to set prices for land sales.
- Municipalities will receive a share of the national personal and corporate income taxes (referred to in translations as taxes on the income of "physical and legal entities"). The plan is to share about half of the revenue from these taxes with municipalities. Distribution of income tax revenues is to be on the basis of the location of the taxpayer, unlike the situation at present when the distribution is decided on by the District Assemblies.
- Payments will continue to be made to local governments to defray part or all of the costs of what are considered centrally-delegated (state administration) functions. Generally, these are education, health and social welfare services.
- In addition, the central government appears likely to make available some general subsidies to local governments. There are no set formulas for such payments, however, and the decision on how much each gets will apparently be based on specific local circumstances.

### **Municipal Revenues**

The principal fiscal problem facing Czech municipalities is perceived by their mayors as the same as that cited by local public officials across the world: insufficient revenue to met the many demands upon them. Their sources of revenue, at least at the present time,

are severely constrained by such factors as central controls over the scope and rate of local taxes. The principal sources of revenue available to local government are:

- The "house tax" (soon to be replaced by the real property tax) which is collected centrally and then redistributed.
- Income from municipal enterprises. This includes income from publicly-owned housing (which generally also requires a substantial subsidy because of the low controlled rents). In most cases, municipalities do not yet own their water and sewer systems, but where they do the fees on these municipal services are included in the budget. Most cities operate other businesses and enterprises as well.
- Income from the sale or rental of municipal property.

SOURCE	AMOUNT (in Kcs. m.)	PERCENT (of Total)
<b>Central Government</b>		
Fixed Subsidies	17.6	8.9
Other Subsidies	67.0	33.9
<b>Own-Source Revenues</b>		
Taxes and Fees	37.2	18.8
Sale or Rental of Property	45.0	22.8
Enterprise Income	18.9	9.6
Transfer from Reserves	10.9	5.5
Miscellaneous	1.2	0.6
<b>TOTAL</b>	<b>197.8</b>	<b>100.0</b>

**Table B.2**  
**HRADICE KRALOVE: SOURCES OF REVENUE (1991)**

SOURCE	AMOUNT (In Kcs. m.)	PERCENT (of Total)
<b>Central Government</b>		
Subsidies	251.6	63.3
<b>Own-Source Revenues</b>		
Taxes and Fees	9.6	2.4
Enterprise Earnings	127.7	32.1
Miscellaneous	8.5	2.1
<b>TOTAL</b>	<b>397.4</b>	<b>100.0</b>

- Fees and charges for various public administrative services (issuance of licenses, certificates, etc.). The relative roles of these revenue sources in two city budgets can be seen in the data presented below from the cities of Frydek-Mistek (pop. 65,000) and Hradice Kralove (pop. 99,000).

Revenues patterns vary widely among the major cities. For example, the large industrial center of Plzen obtained fully 95 percent of its budgetary support from the central governments in 1991. This amounted to about Kcs 7,000 per person. Central government transfers to municipalities in 1991 ranged from Kcs 4,500 to Kcs 12,000.

### **Municipal Expenditures**

Czech cities utilize a unified budget to appropriate both recurrent expenditures for annual operating purposes and capital spending for investment purposes. Notations are shown in the budget to indicate whether an item is for investment or non-investment purposes.

Capital spending accounts for only about a quarter of local budgets. In Plzen, 17 percent of the 1991 budget of Kcs 1,100 million was allocated for investment; the bulk of this was used to complete housing owned by the city. In Frydek-Mistek, 23 percent of the 1992 budget of Kcs 197 million was allocated for investment; the largest items in this category were

for water supply and sewerage projects, followed by road work. Most of the mayors who were interviewed cited the extreme difficulties they faced in allocating a sufficient portion of their budgets for investment purposes in the absence of any source for long-term borrowing. Even without the ability to borrow, however, cities are beginning to think about their capital needs, although none of those interviewed had yet prepared long-range capital investment plans or multi-year capital budgets.

On the recurrent (or operating) side of the budget, education is consistently among the largest categories of expenditure, accounting for about a quarter of the total (22 percent in Plzen and 28 percent in Frydek-Mistek). Health spending is more variable, ranging from a very substantial 27 percent of Plzen's recurrent spending in 1991 to only 1.4 percent of Frydek-Mistek's 1992 budget (primarily for nurseries). Other items of significance in the Frydek-Mistek budget include "internal administration" and "general treasury administration"; these categories apparently include most municipal service function other than education, health and social welfare. Together they accounted for nearly 38 percent of recurrent spending in 1992. Comparable items, included in the "miscellaneous" category of Plzen's 1991 budget, accounted for less than a quarter of the total.

### **Financial Management**

Generally, the Czech cities visited during the October mission appeared to have basically sound budgeting systems. They utilize centrally-mandated approaches to categorizing revenues and expenditures; they were able to provide copies of current budgets on request; and they follow sound practices of modifying their budgets as conditions change (at times drastically) during the fiscal year.

The Mayors and Deputy Mayors interviewed were extremely aware of the need to balance their budgets, despite the great difficulties of doing so in times of rapid change such as the past few years. Their only resources for additional revenues are appeals to the Ministry of Finance (usually denied) or use of any local reserves.

There was less evidence immediately available about the state of other management systems to support the budgeting process, such as accounting, performance measurement and auditing, although there is apparently an annual financial audit done by central government. Other than this audit, there is no central monitoring of local finances.

In at least one city (Hradec Kralove), a number of local community organizations have been appointed by the mayor, with at least one of their functions being to review the annual budget before it is adopted by the Board of Representatives.

## **LOCAL GOVERNMENT AND FINANCE IN THE SLOVAK REPUBLIC**

### **Governmental Structure and Local Authority**

As in the CR, the Slovak Republic has the same two basic levels of government: (1) the central (Republic) government with its seat in Bratislava and (2) more than 2,800 municipalities, with similar functions and responsibilities to those in the CR. The SR also had districts (121 of them) to perform functions for state administration. However, unlike the CR, the SR also has 38 regional administrative offices that also perform functions for the Republic government.

The profusion of governmental bodies in the Slovak Republic has given rise to considerable citizen dissatisfaction, according to officials in the Ministry of Finance. An oft-repeated complaint is that you have to go from office to office to get anything resolved. A new design is being prepared to reduce the number of district and regional offices, with adoption contemplated in 1993 or 1994.

In the major cities such as Bratislava there are also Community Districts (like those in the larger CR cities). They also have elected boards and officials closely parallel to those of the municipalities.

The basic structure and authority of municipalities in the SR is also much the same as in the CR. A problem that appears more serious in Slovakia, however, is the continuing creation of additional small municipalities, despite the existing profusion. This occurs in part because of the Republic government's subsidy distribution formula--which offer a minimum grant no matter what the size of the municipality and, therefore, encourages the establishment of new units.

### **Local Government Finance in Slovakia**

In the Slovak Republic, an estimated 23 percent of total public sector spending currently takes place at the municipal level, very close to the 25 percent estimated for the CR. (This estimate is derived from statements by a spokesperson from the Ministry of Finance that about 9 percent of the national budget goes to local government and that cities raise about 60 percent of their revenues from their own sources).

Intergovernmental aid to local governments in Slovakia also takes the principal form of general revenue-sharing. Municipalities receive a share of the national government's total revenue, generally distributed on an unweighted per capita basis. These payments are made to local governments to defray part or all of the costs of what are considered centrally-delegated functions such as education, health and social welfare. In addition, the central government provides subsidies for the cost of public housing not covered by rents.

Table B.3

## TRENČIN: SOURCES OF REVENUE (1992)

SOURCE	ADOPTED BUDGET (Kcs. m.)	MID-YEAR ACTUAL (Kcs. m.)	MID-YEAR AS A % OF TOTAL
<b>Central Government Transfers</b>			
Housing and Other Subsidies	55.3	23.2	27.3%
Local Share of Wage Tax	47.0	19.0	22.4
<b>Own-Source Revenues</b>			
Fees	17.0	11.9	14.0
House Tax	1.3	1.4	1.6
Income Tax	14.0	11.4	13.4
Municipal Enterprise	18.4	8.8	10.4
Rents	1.0	0.4	0.4
Sale of Property	32.0	3.5	4.1
Miscellaneous	5.6	5.2	6.1
<b>TOTALS</b>	<b>191.5</b>	<b>85.0</b>	<b>100.0</b>

The elements of both revenues and expenditures in the budgets of Slovak municipalities are much the same as for their Czech counterparts. The relative roles of the various revenue sources in the 1992 budget of the city of Trenčín (pop. 57,000) can be seen in the data presented below. The table also underlines the difficulties faced by municipal officials in coping with the rapid pace of change in Slovakia at present. There was a drastic decline of 55 percent in Trenčín's budgetary resources from the time the budget was adopted at the end of 1991 to the middle of the fiscal year. This is a rate of change so rapid that it makes it extremely difficult to plan or control resource allocation.

The brunt of the cutback in Trenčín was taken in the half of the adopted budget that was allocated to capital investment. Planned capital expenditures were cut back by 72 percent as compared to a reduction of 56 percent in general recurrent spending and only a 26 percent reduction in subsidies to municipal enterprises. Even in the absence of sources of capital money, cities are beginning to think about their capital needs although none of those visited had yet completed long-range capital investment plans or multi-year capital budgets. The mayor of Trenčín, however, did state that the city planned to prepare a capital investment program with the aid of a consulting firm already under contract.

Nearly half of Trencin's budget was allocated for recurrent activities. Costs associated with the municipal workforce accounted for 52 percent, contract spending for 24 percent and subsidies to municipal enterprises came to 12 percent. The remainder went to a miscellaneous category entitled "monetary operations".

Generally, as was the case in the CR, the Slovak cities visited during the October mission also appeared to be following reasonably sound budgeting practices although many opportunities to improve their financial management practices were evident.

Slovak cities utilize a fiscal year that is the same as the calendar year, just as the central government does. This coincidence of fiscal periods was cited as an additional burden on hard-pressed municipalities: they have to adopt their budgets before they can obtain information on what the national parliament has decided with respect to the substantial part of local revenues that depends on intergovernmental aid.

## **PRINCIPAL FINDINGS**

Even on the basis of this initial survey of the state of municipal finance in the Czech and Slovak Republics, the findings presented below appear to be warranted. Because the findings were generally similar in the case of cities in both republics, only a single set are presented.

**1. There is a reasonably solid base of financial management practices to build on.** In all of the cities visited there was evidence of generally good budgetary discipline; this was an impressive achievement, given the rapidly changing fiscal environment. Some possible improvements appear obvious: none of the local budgets showed evidence of the availability of computers, an addition that would greatly improve staff ability to maintain records and undertake budgetary analysis. Other needs are less obvious: for example, little evidence was presented that multi-year capital planning was under way (hardly surprising given the speed at which conditions are changing in the municipal arena). Overall, however, it seems clear that the larger Czech and Slovak cities would be quite capable of utilizing technical assistance of a relatively sophisticated nature.. Most of the cities visited responded very positively to the prospect of such help.

**2. The governments of both republics need to persevere in the revenue changes they now contemplate.** Local governments need a reasonably assured level of support from their national government. Plans now under way in both republics for a new form of real property tax appear sound in the long run, but it is likely to be some years before this tax becomes a reliable and substantial revenue source for municipalities. In addition, however, some continued level of national subsidy to local governments is almost certain to be required (although it appears to be time for the Slovak government to think of varying its

current per capita formula to introduce some weighting for the level of local need). It is also a positive sign that the Ministries of Finance in both republics support the development of a high level of own-source revenue for local government.

**3. There is a serious need for sources of loans to finance infrastructure investment.** Most of the cities interviewed are in the process of seeking sources of loans to finance infrastructure investment. In most cases this is taking the form of a "municipal bank". Some of these institutions are being designed by an individual city, others by regional groups of municipalities (for example, Trencin and the other 14 communities in its district), and in yet other cases by municipal associations. It is also possible that the private banking industry will become a source for municipal capital investment. Without some form of financing, however, it seems likely that municipalities will only be able to afford a modest level of investment from their recurrent budgets.

**4. The roles appropriate to municipal government need to be defined further.** In the post-Communist era the lines of appropriate municipal responsibility are still being explored. Many municipalities still own factories or retail businesses that should be privatized. The types and levels of service that should be delivered by municipalities also will need to be examined in relation to the levels of resources available to local government. Another aspect of public service delivery that needs further examination and experimentation is the degree of privatization that is desirable, and whether it should be in the form of contracting-out or load-shedding.

## ANNEX C

### **CHARACTERISTICS AND PRIORITIES OF CANDIDATE CITIES**

#### **INTRODUCTION**

In this annex, we describe characteristics of the four cities selected for initial intensive assignments and discuss their priorities for assistance and possible assistance tasks suited to the objectives of this program. Maps are provided to show the locations of all cities with populations of 50,000 or more in both Republics. Tables show 1980-1990 population change for all cities with populations in excess of 20,000.

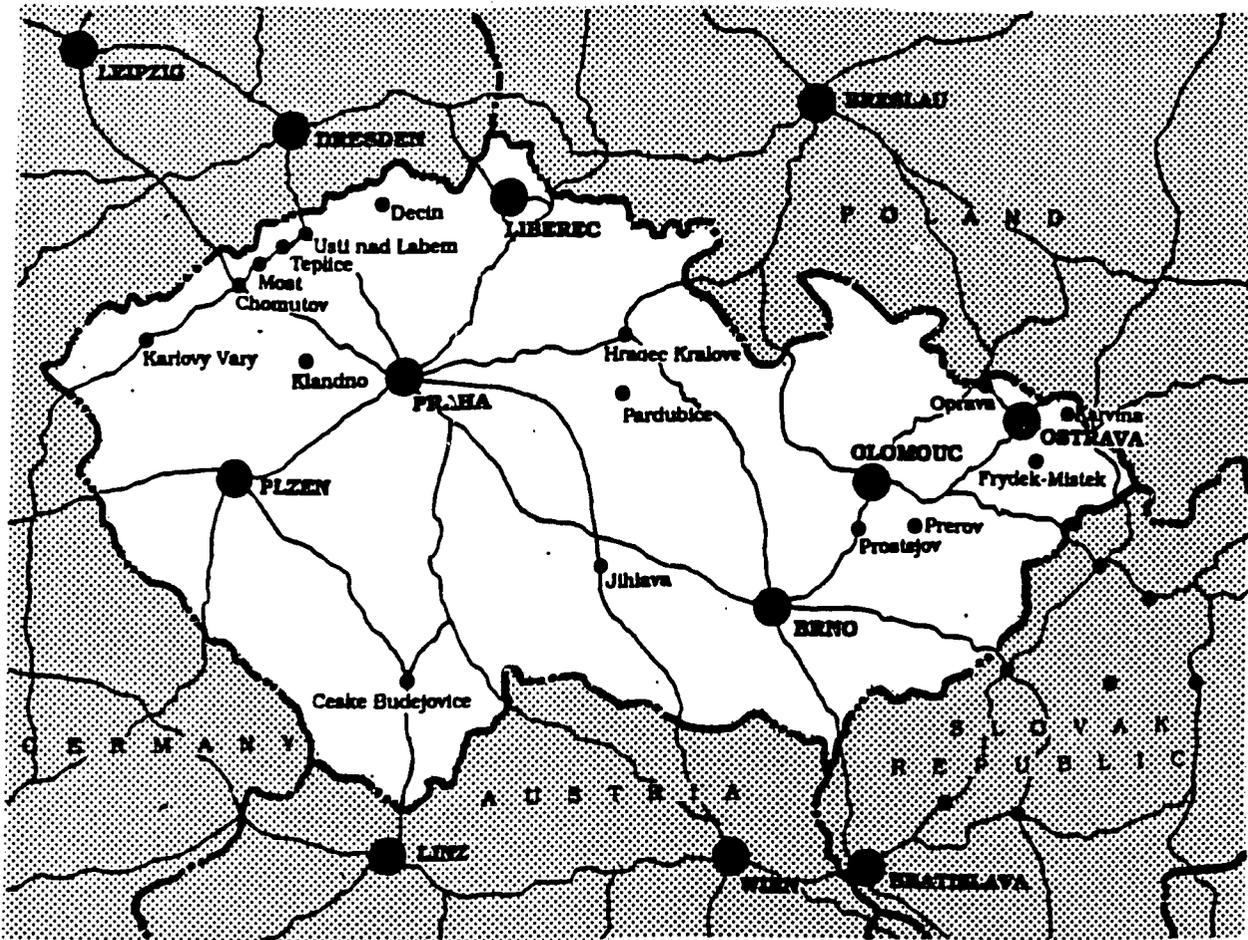
#### **HRADEC KRALOVE**

Hradice Kralove (HK) is a city of 100,000 people in eastern Bohemia, about an hour and a half due east of Prague, with an area of 105.6 square kilometers (only 27.1 percent of which is built up). The city is a substantial industrial center and is also the site of Charles University's medical college and hospital. Its most important industries include: the ZVU Works (5,000 employees--chemicals, agro-processing, production technology); the ČKD Works (2,200 employees--diesel engines); Tesla (1,924 employees--ceramic products, micro-electronic components); Foma (760 employees--photo-chemicals); and Vertex (360 employees--reinforced glass fibers, polyester-glass laminates).

#### **City Government and Mayoral Priorities**

In 1991, HK's municipal government had 219 employees and an operating budget of Kcs. 397.8 million. While HK does not have community Districts, the Mayor has appointed 23 area committees to do local planning; among other things, they comment on the city budget. There is no regional government or even association (because of rivalries between HK and the nearby city of Pardubice) but the mayor has good relations with the district secretary. The district assembly now operates with two houses, one for HK (which has 70 percent of the district population) and the other for all other communities. Both houses have to agree on fund allocations.

The team met with the Mayor, Martin Dvorak, an economist, and his staff. He identified his principal concern as the expected decrease in financial resources, not only for infrastructure investment but even for bare bones maintenance of the city. As to



**Figure 2**  
**CZECH REPUBLIC**

infrastructure finance, he has considered the idea of a municipal banks but has not had the resources to examine it seriously--he was most interested in the prospect of AID assistance in credit system development. He said the city would benefit from technical assistance in the following priority areas:

1. Improving and expanding the city's water supply system (see further discussion below).
2. Municipal land development. (He emphasized the problem of deciding whether to sell municipal property now when they do not really know what it is worth but need the money, or wait until they have some sense of the market and when values may be higher. He said the town council is split down the middle on this issue. See further discussion below).
3. Solid waste management. (The capacity of the current land-fill site at Smržov is virtually exhausted--additional sites and more efficient means of disposal will be essential).

Table C.1  
CITY POPULATION GROWTH: CZECH REPUBLIC

City	Population (000)		Gr.Rate %/year 1980-90
	1980	1990	
<b>ABOVE 100,000</b>			
Praha	1,182.9	1,212.0	0.24
Brno	371.0	388.0	0.45
Ostrava	327.9	327.6	-0.01
Pizen	170.7	173.1	0.14
Olomouc	102.2	105.7	0.34
Liberec	97.5	101.9	0.45
Subtotal	2,252.0	2,308.3	0.25
<b>50,000-100,000</b>			
Hradec Kralove	95.5	99.9	0.45
Usti nad Labem	87.9	99.7	1.27
Ceske Budejovice	90.3	97.3	0.74
Pardubice	91.9	94.9	0.32
Havirov	90.0	86.3	-0.42
Zin	84.0	84.6	0.07
Kladno	71.2	71.7	0.07
Most	60.0	70.7	1.66
Karvina	78.3	68.4	-1.35
Frydek-Mistek	59.4	65.1	0.91
Opava	59.4	63.6	0.69
Karlovy Vary	60.9	56.3	-0.78
Decin	49.6	55.1	1.06
Chomutov	51.8	53.2	0.27
Teplice	53.8	53.0	-0.15
Jihlava	51.1	52.3	0.23
Prerov	50.2	51.3	0.22
Prostejov	49.6	50.1	0.10
Subtotal	1,234.8	1,273.5	0.31
<b>20,000-50,000</b>			
Jablonec nad Nisou	42.2	45.9	0.85
Trinec	44.4	45.2	0.17
Mlada Boleslav	45.9	44.5	-0.32
Znojmo	39.3	39.9	0.17
Ceska Lipa	24.9	39.7	4.77
Trebic	30.2	39.3	2.67
Pribram	37.8	36.9	-0.26
Tabor	31.9	36.3	1.32

Table C.1 (Continued)  
CITY POPULATION GROWTH: CZECH REPUBLIC

City	Population (000)		Gr.Rate %/year 1980-90
	1980	1990	
Orlova	31.2	36.3	1.52
Trutnov	27.6	32.0	1.48
Cheb	31.0	31.8	0.28
Vsetin	29.9	31.6	0.54
Kolin	30.9	31.6	0.21
Hodonin	25.5	30.7	1.89
Sumperk	31.8	30.4	-0.45
Pisek	28.1	29.5	0.50
Litinov	22.6	29.1	2.56
Novy Jicin	31.5	29.0	-0.81
Kromeriz	25.9	29.0	1.12
Cesky Tesin	23.4	28.7	2.08
Valasske Mezirici	26.5	28.2	0.60
Uherske Hradiste	36.7	26.8	-3.10
Breclav	24.0	26.2	0.88
Litomerice	23.8	26.0	0.88
Zdar nad Sazavou	25.0	25.6	0.23
Krnov	25.6	25.6	-0.01
Sokolov	28.5	25.4	-1.14
Strakonice	22.6	25.0	1.00
Havlickuv Brod	24.5	24.9	0.12
Koprivnice	19.8	24.1	1.97
Bohumin	25.2	23.7	-0.61
Chrudim	20.5	23.6	1.42
Vyskov	18.3	23.1	2.35
Klatovy	27.8	23.1	-1.84
Louny	20.4	22.7	1.06
Jindrichuv Hradec	20.1	21.8	0.83
Kutna Hora	20.9	21.5	0.29
Blansko	19.5	21.4	0.91
Nachod	19.9	20.6	0.37
Otrokovice	18.1	20.3	1.16
Subtotal	1,104.0	1,177.0	0.64
CITIES ABOVE 20,000	4,590.8	4,758.7	0.36
OTHER CR	5,701.2	5,540.3	-0.29
TOTAL CR	10,292.0	10,299.0	0.01

4. Residential heating. Heating systems based on hot water, that now service a large portion of the city, are highly inefficient. Some progress has been made to convert to natural gas, but the work on this transition has been stalled. The city needs analyses to determine the most efficient technical options, a realistic phasing plan, and effective means to finance the conversion.

5. The communal housing stock. (There are 13,000 units now owned by the city: the city must operate and maintain this housing but rents from tenants--still strictly controlled at the Republic level--cover only a fraction of the costs).

6. The near-total absence of property records. (This means, among other things, that the city is not sure what it owns. HK is unusual in that it does have a detailed price map--approved by the Ministry of Finance. It was prepared with the help of a government organization named Geodesia which is now helping the city to develop a geo-coded cadastral system.)

7. The continued ownership of industrial firms by the city. (The question here is how to manage and phase out these relationships).

Discussion of these issues suggested that the best match between city priorities and LGHP capabilities initially would be assistance with the two issues described below.

#### **Hradec Kralove Strategy for Water System Development**

Hradec Kralove's existing water system is faced with deterioration due to undermaintenance and the system has not been extended to serve all existing developments on the urban fringe (both within and outside of the municipal boundary). The construction of new mains to address the need in some of the unserved areas had been started, but all work was terminated in 1990 due to cut-backs in Republic funding. It is also recognized that contamination of surface water sources in the surrounding area has increased significantly over the past few years (since the last planning study was completed) and that past planning did not adequately deal with the problem of the linkage between elements of the system within the municipality and service to nearby towns.

The water system is owned and operated by a recently privatized corporation that serves the city and the immediate region (this entity is much smaller than the previous state enterprise that served the city and the city will have a large influence over the policies of its Board).

The city has requested assistance with a study of planning options for the system that would rethink opportunities and priorities for the future given a realistic view of expected constraints on Republic funding and the water company's latitude for tariff increases. It

recognizes that a workable solution today may have to rely on a mix of several approaches, most of which represent a break with tradition: e.g., an expanded and more tightly run maintenance and repair strategy, the phasing in of higher water tariffs, reliance external credit rather than Republic grants. The city would like an initial study of options to help it form its own strategy, recognizing that this could lead into our providing further assistance directly to the corporation at a later stage and the possibility of tapping a new municipal credit system.

The Mayor understands that we do not have the resources to fund a full-fledged water system planning and design project, but believes that a sensible shorter term analysis (relying on available data and existing engineering studies) could establish a sound basic approach and offer guidance as to what further analysis and engineering work should be undertaken.

### **Hradec Kralove Land Development Strategy**

With the certainty of reductions in grants from the Republic government, Hradec Kralove has recognized that it must take steps to become more self reliant. City staff are aware that facilitating private sector development city owned and controlled land may be an important means for stimulating economic development as well as augmenting city revenues.

There are a number of city owned sites that the city's staff believes should have market development potential for commercial and mixed-use development. However, there have been differences of opinion as to whether the city should attempt to sell some of this land now (when the city does not really know what it is worth, but needs the money) or wait until they have some sense of the market and when values may be higher. The city's property records are extremely deficient, further complicating the task of implementing a sensible land development strategy.

The Mayor would like assistance in: (1) generally evaluating the advantages and disadvantages of rapid vs. slower marketing of municipal lands (including financial implications); (2) (to make this concrete) conducting assessments to identify one or more city owned sites that offer the greatest opportunity for private sector development in the city's interests; (3) developing land use options and a prototype planning/marketing/implementation process for those sites; (3) designing a longer-term city-wide strategy and process for the disposition and development of city owned lands (including guidance on an approach to improving land ownership records).

## **LIBEREC**

Liberec is a city of 100,000 in northern Bohemia, close to the point where the Polish-German border intersects the Czech border. The city has an area of 114.3 square kilometers. It has a comparatively strong and diversified industrial base, although it best known for a sizeable textile industry.

### **City Government and Mayoral Priorities**

Liberec had budgeted outlays of Kcs. 440.0 million in 1991, against anticipated revenues of Kcs. 443.9 million. Of total expenditures, education accounted for 19 percent, technical services (e.g., solid waste collection) accounted for 16 percent, housing management for 12 percent, and transportation services and cultural activities for 10 percent each).

Mayor Jiří Drda is widely regarded as a strong manager and is a member of the Board of the Association of Towns and Cities. He and his staff identified a number of priorities for technical assistance.

1. **Housing privatization and management.** Because outlays for housing management greatly exceed rental income from tenants, the operation of the communal housing stock implies a substantial ongoing financial loss for the city. The Mayor believes that rapid privatization is required and needs assistance in preparing a plan for privatization and subsequent management (see further discussion below).

2. **Sanitation.** The Republic government is completing new trunk sewer lines to serve Liberec and the surrounding region. Local collector systems are inadequate in several areas, however, and need to be developed to link to the new trunk lines. The city requires guidance on forming both a physical development and realistic financing plan for this work (see further discussion below).

3. **Land management.** The city is also aware that facilitating the private development of city owned lands will be important for the its revenue base as well as its economic development potential. They have identified several areas that would appear to have high potential for development but need assistance in market analysis and devising a process for engaging private sector entities in the development process.

The city has a number of other infrastructure projects and capital facilities it wishes to finance (e.g., transit system improvement, schools, a incinerator for solid waste disposal) and is most desirous of participating in the development of an effective system for municipal credit.

Our meetings with the Mayor indicated that the best match between city priorities and LGHP capabilities at the outset would be the two projects discussed below.

### **Liberec Strategy for Housing Privatization and Management**

Liberec now owns and operates 2,320 residential buildings, containing 16,900 communal housing units. In 1991, this housing was operated on a budget of Kcs 78 million, only Kcs. 55 million of which was covered by rental revenue from residential and commercial tenants. Beginning in 1993, there will be no state subsidy to cover the revenue shortfall. The city wants to privatize all but about 10 percent of this housing but needs help to work out a strategy and implementation plan. The issues to be addressed include: Which dwellings should be sold and which kept as low-income rental housing? How should the city choose among prospective buyers? How should sale prices be set? Should the city sell individual dwellings or only entire buildings? Should the land be sold along with the buildings, or only leased? What should the city do with revenue from privatization?

The city has also requested guidance on how best to manage this communal housing inventory (the full inventory, now and then phasing down to a much smaller inventory through privatization). At present, government offices handle apartment allocation, rent collection, and routine maintenance, with larger repairs being the responsibility of five private management companies, each responsible for a separate group of buildings. The city has asked for guidance on how to redistribute responsibilities between city offices and private management companies, improve and standardize management procedures, and provide the private companies with stronger incentives for good performance.

### **Liberec Sanitation System Development**

The Czech Republic expects to complete major sewage trunk lines and treatment facilities in 1994 that will serve Liberec and the surrounding region. These works form the backbone of an adequate regional system, but collection systems within Liberec are woefully inadequate to meet present needs (in some cases existing systems are in bad repair, in others needed collectors have not been provided). The city recognizes the development of this internal collector systems, so that it can link effectively to the major works being provided by the Republic, as one of its highest infrastructure priorities.

The Mayor would like assistance in forming a strategy to address this problem. The approach should first consider what type of improvement plan would be feasible for its internal sewage collection system, considering needs for maintenance and rehabilitation as well as new construction. The study should also examine and compare options for financing system improvements given a realistic view of legal and other impediments.

## **BANSKA BYSTRICA**

Banska Bystrica is a city of 85,000 residents located near the geographical center of Slovakia, about four hours driving time from Bratislava. Situated in the Low Tatra mountains, the city is surrounded by picturesque hills and has a substantial river running through it. About half of the local work force is employed in manufacturing, but no single industry dominates. The city produces Ulpin beer, cement, electronic parts, textiles, and other items, mostly in small, modern-looking plants along the river. It is also the site of Mateja Bela University which has faculties in economics, education, and science. It has a substantial military sports facility and is a center of tourism (skiing and hiking, primarily, plus visits to the historic small towns in the district).

### **City Government and Mayoral Priorities**

Banska Bystrica's 1992 expenditure budget totaled Kcs. 343 million. A 30 percent increase in base budget costs is expected for 1993, but the city knows revenues under the new tax system are highly uncertain. Mayor Stanislav Mika recognizes this probable revenue shortfall as his most fundamental concern and sees that efforts must be made to focus on priorities and vastly improve the efficiency of service delivery.

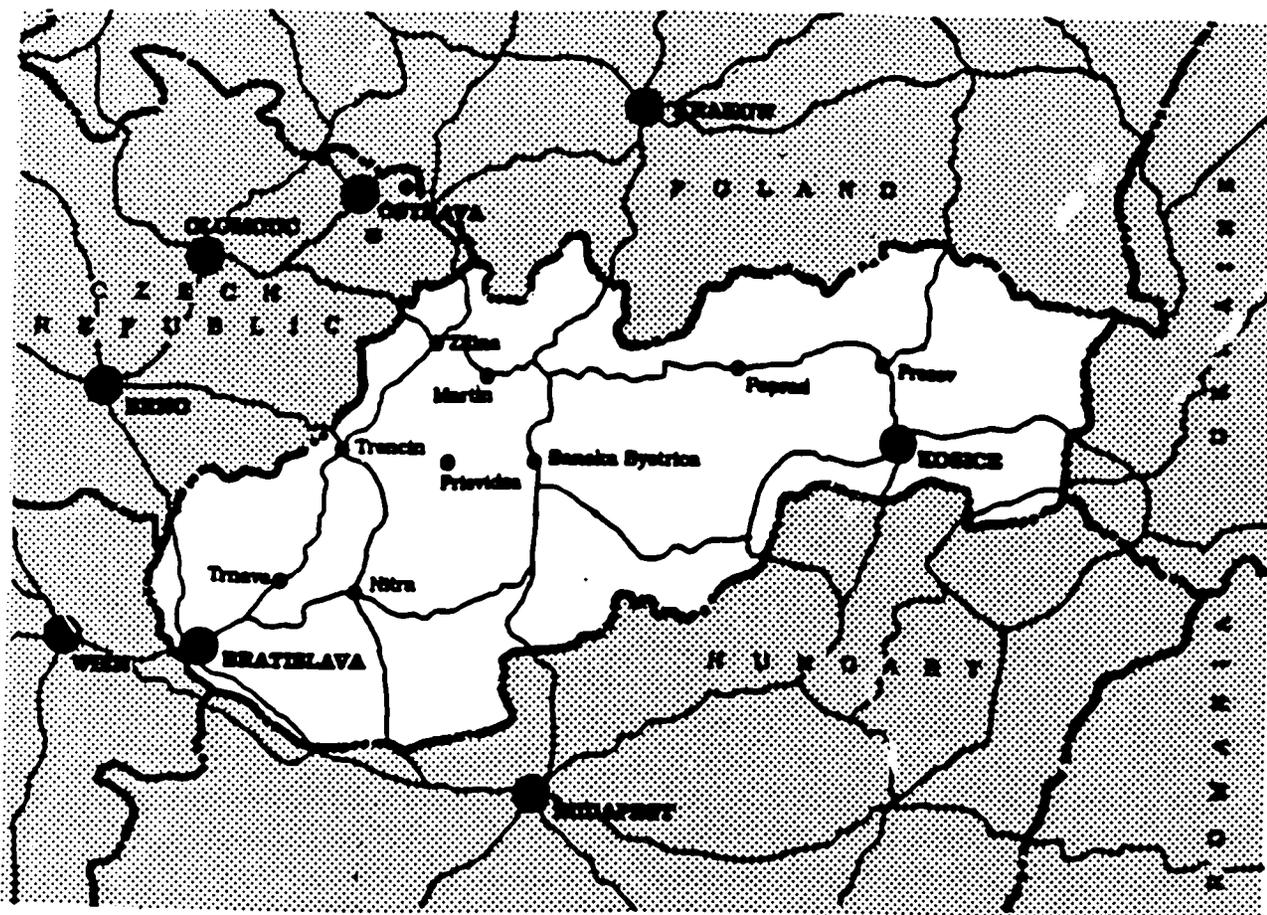
More specific priorities he identified were: upgrading the city's sewer system and water pollution control system; developing city owned land (including a 42 ha. site where infrastructure has been provided but the previously budgeted funds for development have been eliminated from the Republic budget); finding funds to finish two schools and a polyclinic on which construction has started; air pollution control (particularly with regard to the local cement plant); finding a new landfill site, and providing an incinerator, to handle solid waste disposal; securing funding for planned road improvements.

Our discussions with the Mayor and other officials resulted in the selection of the following two projects as the most promising starting points for LGHP assistance.

### **Banska Bystrica Strategy for Sanitation Systems Improvement**

Banska Bystrica wastewater treatment facilities are old and in bad repair. Capacity is inadequate to serve the needs of the existing population, let alone accommodate new growth. At the same time the city is concerned about that the inadequate treatment and disposal of growing volumes of liquid wastes by upstream activities in the surrounding region may lead to serious pollution of its own drinking water supply.

The Mayor would like assistance in forming a strategy to address these issues. The approach should first consider what type of improvement plan would be feasible for its own treatment facilities, given a realistic view of financial opportunities and constraints. It should



**Figure 3**  
**SLOVAK REPUBLIC**

then formulate and compare various options for reducing potential pollution from activity upstream. The study should consider how to create more efficient and effective approaches to system maintenance and repair as well as initially needed capital improvements.

The analysis should also consider institutional options. A Republic government enterprise now operates all wastewater collection and treatment operations in the region, but the Republic plans to break up and privatize these operations later this year. The Mayor would like guidance on institutional forms (including the city's role in them) that would best guard the city's interests over the long term.

### **Banska Bystrica Land Development Strategy**

Banska Bystrica has recently developed an overall zoning concept and is working with an Austrian firm to computerize (and correct) land ownership records. It owns a 42 hectare undeveloped site that was planned for panel housing under the CHC (infrastructure has been

**Table C.2**  
**CITY POPULATION GROWTH: SLOVAK REPUBLIC**

City	Population (000)		Gr.Rate %/year 1980-90
	1980	1990	
<b>ABOVE 100,000</b>			
Bratislava	380.2	441.5	1.50
Kosice	202.4	234.8	1.50
Subtotal	582.62	676.2	1.50
<b>50,000-100,000</b>			
Nitra	76.6	89.9	1.61
Presov	71.5	87.8	2.08
Banska Bystrica	66.3	85.0	2.52
Zilina	83.0	83.9	0.10
Trnava	64.1	71.6	1.12
Martin	56.2	58.3	0.38
Trencin	47.8	56.7	1.72
Prievidza	40.7	53.4	2.74
Poprad	38.0	52.9	3.36
Subtotal	544.2	639.5	1.63
<b>20,000-50,000</b>			
Nove Zamky	34.2	42.9	2.29
Zvolen	36.5	41.9	1.39
Povazska Bystrica	30.4	39.8	2.72
Spisska Nova Ves	31.6	39.2	2.17
Michalovce	29.7	38.9	2.72
Komarno	32.5	37.4	1.41
Humenne	27.3	34.7	2.42
Levice	26.1	34.0	2.67
Piestany	30.5	33.0	0.80
Topolcany	31.3	32.6	0.40
Liptovsky Mikulas	24.5	31.7	2.62
Bardejov	23.7	30.8	2.65
Ruzomberok	26.4	29.4	1.10
Lucenec	26.4	28.9	0.89
Partizanske	23.3	26.5	1.31
Cadca	19.3	25.2	2.69
Rimavska Sobota	19.7	24.8	2.31
Sala	19.2	24.7	2.59
Dubnica nad Vahom	15.6	24.4	4.62
Hlohovec	21.2	23.3	0.95
Dunajska Streda	18.7	23.2	2.18

**Table C.2 (Continued)**  
**CITY POPULATION GROWTH: SLOVAK REPUBLIC**

City	Population (000)		Gr.Rate %/year 1980-90
	1980	1990	
<b>ABOVE 100,000</b>			
Ziar nad Hronom	19.2	21.5	1.16
Nové Mesto nad Vahom	18.1	20.9	1.43
Trebišov	15.0	20.8	3.34
Pezinok	17.1	20.5	1.81
Kezmarok	17.6	20.2	1.41
Senica	15.4	20.0	2.64
Subtotal	686.5	835.9	1.99
<b>CITIES ABOVE 20,000</b>	<b>1,813.3</b>	<b>2,151.7</b>	<b>1.73</b>
<b>OTHER SR</b>	<b>3,177.7</b>	<b>3,117.3</b>	<b>-0.19</b>
<b>TOTAL SR</b>	<b>4,991.0</b>	<b>5,269.0</b>	<b>0.54</b>

already provided) but funds for the housing no longer exist and the city no longer wants to be locked into the original panel housing design. Since considerable investment has already been made in the infrastructure, the evaluation of realistic alternative possibilities for the development of this site is a priority for the Mayor.

More importantly, there are a number of other city owned sites (several in and near the downtown area) that the staff believes should have market development potential for commercial and mixed-use development. The Mayor would like assistance similar to that requested for Hradec Kralove, entailing: (1) further assessments to select one or more sites for priority development; (2) developing land use options and a development planning/marketing/implementation process for those sites; (3) designing a city-wide strategy and process for further disposition and development of city owned lands.

## **TRENCIN**

Trencin is a city of about 57,000 population, located about 150 kilometers north of Bratislava in the Vah River valley. It is on the rail line that runs north from Bratislava and is located at the planned intersection of main arterial roads between Bratislava and Prague.

### **City Government and Mayoral Priorities**

Trencin's adopted budget for 1992 anticipates Kcs. 191.5 million in revenues, 53 percent of which is to come from central government transfers (see further discussion in Annex B). Own source revenues include local taxes and fees (house tax, fog fees, etc.), income from municipally-owned property, the wage tax (collected, however, by the central government) and other sources. About half of the annual budget is spent for recurrent purposes (such as solid waste collection and disposal, road maintenance, cultural services, etc.) and the remainder for capital investments. The city has managed to balance its budget in each of the past few years, but with considerable difficulty. Primarily, they relied more on obtaining more revenue rather than cutting expenditures.

The Mayor, Stefan Rehak, has been developing a plan, in cooperation with the other municipalities in the surrounding region and local banks (the Mayor mentioned Tatra), to establish a municipal bank to finance capital investments by the cities in the region. The Mayor also noted that by the end of this year Trencin planned to complete a long-range capital improvement plan; an Austrian-Slovak firm is preparing the plan on a consulting basis.

The city is very investment-oriented. The Mayor said that they own a lot of land that they are prepared to sell or lease to generate private investment. The single project he talked of most is the reconstruction of an existing hotel located near the city center and just at the foot of the castle rock. The city is rehabilitating the historic structure with its own money and is in an advanced stage of negotiations with a Canadian firm (the lone bidder to an RFP) to operate it. The Canadians promise to bring in Best Western or Holiday Inn as the principal operator.

Other local activities of which the Mayor told us are: Trencin is setting up its own "university" to teach business administration and marketing in a building they bought for the purpose; they have a Swiss firm working on plans to convert the local airport from military to civilian use; and they have already signed contracts with investors to use municipal property. The Mayor complained that Slovak law doesn't allow them to give private firms tax exemption.

The city would also like to upgrade and expand its housing stock, but the Mayor appeared quite realistic on this score. He recognizes that the local population isn't growing and that this is not likely to change. He cited nearby cities in the surrounding 400,000 inhabitant region that already have vacant housing that they can't fill. Several times he stressed the strong relationship among the cities in the 400,000 inhabitant region of which Trencin is the center and he noted that this would be helpful in spreading the benefit of any assistance.

In terms of technical assistance priorities, the Mayor emphasized problems in the development of the left bank of the Vah River, across from the town center.

### **Trencin Land Development Strategy**

Trencin's downtown area is on the right bank of the Vah River, and most new investment in the city during the Communist era (including panel housing developments and related infrastructure) also took place on the right bank. The portion of the city on the left bank, which was neglected during this period, had considerable housing now and is seen as having great potential for future development. The new major expressways linking Trencin to the Czech Republic will be located on the left bank and their primary intersections will be points of high accessibility, creating important development opportunities for land around those points.

The city has no clear plans as yet to take advantage of these opportunities. The Mayor would like assistance in assessing the development potential of these areas and outlining a land use strategy for them. An important part of this work is considering the timing of potential development on the left bank in relation to other development sites on the right bank that may be important priorities for city investment in the short term. The city also requires assistance in developing a standardized process by which it reviews the characteristics of all land parcels it now owns or controls, and sets priorities and staging for facilitating private development of those sites.

### **Trencin Sanitation System Strategy**

A related problem is the imminent need for sewerage on the left bank of the Vah. Considerable family housing already exists on that bank, and as noted, the infrastructure needs of the area have been ignored for many years. A strategy for sanitation is needed in which short term projects designed to address today's unmet needs are sensibly linked to the longer term land development strategy for the left bank noted above.

The approach should first consider what type of improvement plan would be feasible for the sewage collection system on the left bank, considering needs for maintenance and rehabilitation as well as new construction. The study should also examine and compare options for financing system improvements given a realistic view of legal and other constraints that now apply.

The analysis should also consider institutional options. As in Banska Bystrica, a Republic government enterprise now operates all wastewater collection and treatment operations in the region, but the Republic plans to break up and privatize these operations later this year. The Mayor would like guidance on institutional forms (including the city's role in them) that would best guard the city's interests over the long term.

## **ANNEX D**

### **CANDIDATE LOCAL TRAINING INSTITUTIONS**

#### **APPROACH TO TRAINING**

The strategy calls for the PMT to develop training courses that will be implemented through indigenous training institutions. We expect to offer courses in at least four areas: housing privatization and management, strategic land development and management; infrastructure planning and management; capital budgeting and infrastructure finance. Course offerings in each area are substantively linked but are otherwise relatively independent of each other. They can be initiated under differing start-up schedules depending on priorities expressed in the two Republics and the ease of curriculum development in the topic at hand. The process of developing and implementing the training program will vary depending on the subject matter. In general, however, we see it proceeding as follows.

The first step will be the development of curriculum materials by the CSFR PMT and others working in the ICMA consortium. In some cases, (e.g., housing management) this work has for the most part already been completed under prior contracts. In others, thought has been given to curricula but more work remains (e.g., land management, infrastructure, financial planning and management, infrastructure finance).

As the second step, we would make a final selection of the local training institution to deliver the course on an ongoing basis (after consultation with the ATCc relevant Ministries). We would then negotiate a plan with that institution and familiarize them with the curriculum materials. The third step is for staff and consultants in the ICMA consortium to offer the course directly in each Republic on a pilot basis--staff from the selected training institution would observe and participate. Materials and approaches would then be revised as appropriate based on the experiences with these pilots. As the fourth step, the training institution would offer the course themselves with us as observers. Again, revisions would be made based on our joint views on this experience.

Finally, the training institutions would begin to offer the course on a regular, financially self sustaining basis. We would be working with the institution throughout the development and testing period to develop sound plans and guidelines for the ongoing program, including financial aspects.

As noted in the main body of this report, we expect that, regardless of the training institution that actually presents the courses, all LGHP training will be offered under the auspices of the new PHARE supported foundations that have been set up by the ATCs in each Republic. These foundations will also be actively involved as direct participants in helping us plan the LGHP training program.

### **CANDIDATE INSTITUTIONS**

Urban Research Inc. was assigned the task of identifying training institutions with which the LGHP might affiliate in this manner. (They were able to complete the review only for the Czech Republic so far, but a similar review for Slovakia is now in process). In the CR, they began with a series of interviews, with the ATC and selected municipal officials. In these interviews, they asked for the names of relevant training institutions and for some assessment of the characteristics, skills, and capacities of each identified.

They discovered that a sizeable number of organizations, institutes, companies, foundations, associations, centers, etc. exist which have some involvement in training. Also, almost all Ministries and professional unions have some training capacity. After assessing information from the interviews, Urban Research made direct contact with eleven institutions:

- (1) Department of Local Administration, the University of Economics Prague;
- (2) Department of Local Administration, Chemical-Technological College at Pardubice;
- (3) CERGE (Center for Economic Research and Graduate Education), Taboritska 23, Prague 3;
- (4) Inorga, Prague 1, Letenska 17;
- (5) Institute of Management, Prague 1, Jungmannova 29;
- (6) Institute of Education of Construction Industry Workers, Prague 4, Klanova 62;

- (7) Institute for Education of Managing Scientific workers of the Ministry of Industry of the CR, Prague 1, Vaclavske Namesti 35;
- (8) Institute for Local Administration, Prague
- (9) Czechoslovak Management Center, Celakovice, 5. kvetna 2;
- (10) Inventa, spol s r.o. Prague, Rehorova 14, Prague 3;
- (11) Fund of Assistance to Local Administration in the CR, U radnice 2, Prague 1.

### **Assessment**

These institutions were assessed in two ways: (1) as to their general capacity, reliability, and reputation as training institutions (i.e., scope of subject matter offered; quality and capacity of staff, facilities, and equipment; past responsiveness to client institutions); and (2) as to their capacity to meet the particular needs of the LGHP in training local government staff in the four main topical areas of the program.

The assessment narrowed the choice down to four institutions which we believe would be best suited to address the needs of the LGHP. All of these institutions could be used under the program, at different times and in different ways.

- (1) Gradua-Institute for Education of Workers in Construction: rated top for technical training, probably best for first LGHP courses in housing management and land development.
- (2) Institute for Local Administration (Ministry of Interior): promising in areas of local administration and finance and could be used for courses in these fields.
- (3) College of Land Management of the Chemical-Technological College, Pardubice: main university level education in CR now focusing on local government management.
- (4) Fund of Assistance to Local Administration in the CR: this is the ATC foundation--all LGHP courses will be offered under the auspices of this institution, and as their own technical staff is enhanced in the future, they could eventually take over some of our courses and present them directly.

## **GRADUA--INSTITUTE FOR EDUCATION OF WORKERS IN CONSTRUCTION**

Address: Klanova 62, 147 09 Prague 4, telephone: 02 472 95 96; Fax: 02 472 73 27.  
Director: Adriena Hascynova  
Science Secretary: Vladislav Blecha  
Commercial Director: Marta Neumajerova  
Economic-operational Director: Petr Bohac

Gradua is a contributory (state) organization still under the jurisdiction of the Ministry of Industry, Trade and Tourism of the CR. In a short while, however, it will be privatized, most probably in accordance with the privatization plan submitted by workers the institute. It will then be Gradua, spol. s r.o., which would continue past activities with little change in substance. Its functions include offering seminars and training programs in the fields of business management, financial management and accounting, construction and the construction industry, computer technology.

Their own group of lecturers represents highly-qualified experts and this field, and they also hire top experts from colleges, research institutes and consulting firms. Gradua now has five departments: management preparation; construction techniques; social and personnel management; mechanization; computer technology. They have a staff of around 70, and appear to place great emphasis on satisfying the requirements and needs of their clients. They are known for flexibility and skill in rapid innovation with respect to new services. Gradua is oriented to long-term partnerlike relations with firms and institutions focused not only on the area of construction. Since 1990 it has given much more emphasis to management and finance.

Courses, seminars and consulting are run on a commercial basis. Prices of services provided are governed by the law on prices; i.e., by agreement between the supplier and customer. Included are schooling fees (comprising all costs associated with the preparation and implementation of the seminar or course, including costs for printed materials for participants), night accommodation fees in the hotel GARNI (80 Kcs per person per night), meals (70 Kcs per person per day).

Good conditions exist for the independent introduction of courses in the framework of our program-proof of this is a seminar organized by Urban Research in cooperation with the Construction Guild under the financial support of USAID in October 1992. Also, other positive features are leaders that appear to understand our interests, an open approach to modern methods and foreign experience, and their emphasis on self-financing, activities.

The training facility is situated in a historical building in the quiet surroundings of a villa quarter in Prague 4, relatively easily accessible by city public transportation. Courses and seminars are held in five classrooms and seminar rooms which are equipped with

interpreting facilities, didactic technology including video, personal computers. Serving or accommodation is the institute's own hotel GARNI.

### **INSTITUTE FOR LOCAL ADMINISTRATION**

Address: Na Perstýně 11, 110 00 Prague 1, telephone: 02 236 88 73; Fax: 02 236 87 88

Director: Evzen Sykora

Contact person: Mr. Pokorný, telephone: 02 26 93 61

Address of the schooling center: Ke Stadionu 1918, 256 01 Benesov; telephone: 0301 23 853.

This Institute was the traditional unit of the Ministry of the Interior that has provided training for local government officials. Until not long ago, it was in essence only a training facility for members of boards of representatives and town officials. The Institute, has not had a good reputation with the expert or lay public--through 1991, structures from the Communist era survived in its leadership. In the summer of 1992, however, dramatic changes in the activity occurred in association with the accession of a new leadership.

The Institute is financed from a combination of sources. Finances fall come from the budget of the Ministry of the Interior of the CR in the form of subsidies as well as from fees from trainees and other institutions who lease the center for meetings. A week-long stay in the schooling center for workers of the sector of the Ministry of the Interior costs around Kcs 1,000--others pay a much higher price. Besides training courses, the Institute offers the holding of seminars, conferences, conventions, international congresses, scientific symposia and with a wide thematic focus.

The clientele is formed above all by workers of state administration and self-administration at all levels of government. The schooling of workers of local governments has a very long tradition, with roots reaching back sixty years. Lecturers are 90 percent from the outside, recruited especially from teachers of select colleges (economic and legal focus) and top experts in state administration, of the sector of the Ministry of the Interior.

An advantage is the Institute's enormously long experience with the organization of educational courses and seminars. On the other hand, a disadvantage could be inertia and difficulty in adapting to new approaches. Regarding the fact that the technical outfitting and quality of the personnel corresponds to our requirements as well as regarding the good personal contacts with top management, future cooperation in LGHP seems attractive.

The Institute's facilities are at the edge of the town of Benesov in Central Bohemia on the main Prague-Tabor-Ceske Budejovice highway, 50 km from Prague. There are also good

train and bus links. Lying nearby is the castle Konopiste and a lovely park. The schooling center was built in 1966 and thoroughly renovated about ten years ago. Its facilities and equipment rate very high in quality, even in comparison with abroad. The congregation hall has a capacity of 200 persons, broadcast equipment, a projection booth--they are also preparing to install an interpreting booth. At one's disposition are seven negotiation rooms (classrooms) outfitted with modern didactic technology, blackboards, reverse projectors and projections screens, televisions sets, and video. One classroom is outfitted with personal computers.

The six-story hotel at the site accommodates 200 persons in 2-3 person bed rooms with baths. Day long eating facilities (self-service buffet) are also available. A sauna, exercise room, tennis courts, and swimming pool are also provided at no charge to trainees.

#### **FACULTY OF LAND MANAGEMENT, CHEMICAL-TECHNOLOGICAL COLLEGE**

Address: Studentska 84, 530 09, Pardubice

Dean of the College: Eng. Milos Vitak, CSc.

Secretary of the College: Pavel Pelak, LL.D.

The College of Land Management was founded in 1991, but it appears that is has already written itself into the subconscious of the public, because this year more than 100 students are beginning their studies at the college. The college has two departments: the Department of Regional Sciences and the Department of Information Science. The study is for now only three-year bachelor's but the college is attempting to gain accreditation for five-year study. Graduates should find application especially in institutions and authorities of state administration and self-administration (local, financial, labor offices, etc.).

Study in the first year is focused on the teaching of subjects of a more general type (history, philosophy, fundamentals of law, introduction to economics, mathematics, psychology) in order that the students gain basic knowledge, on which they then add in higher years more specialized subjects (e.g., city management, business management, personnel management).

Great emphasis is placed on the teaching of foreign languages. Students have two required languages (this year they are English, German and French). It is being considered that in the future foreign lecturers will teach a number of subjects directly in their tongues. Next January, extramural study will also be initiated for the education of employees of local and town offices.

The college works together with many foreign universities and institutions of a similar focus (for example, the University in Bayrouth). It has a good meeting hall and dormitory facilities and is well equipped with computer technology.

### **FUND FOR ASSISTANCE TO LOCAL ADMINISTRATION**

Address: U radnice 2.10, 110 00 Prague 1  
Chairman of the Board of the foundation: Borek Valvoda  
Secretary of the foundation: Oldrich Smotlacha  
Directory of the team of experts: Miroslav Cernik

This is the foundation, discussed earlier, that was established by the Association of Towns and Cities of the CR. Other sponsoring and affiliated institutions include the Committee of the Czech National Council for Land Management and National Communities, the Civil Administration Section of the Ministry of the Interior of the CR, the Institute for Democracy and a Unified Europe, and the Institute of the Capital City of Prague.

The foundation is creating an educational and consulting system of authorities of self-administration of the CR. This system is fixed for mayors, members of the municipal boards of representatives, general secretaries, and other officials of towns and municipalities. It is planned that the foundation will provide consultations and education in the following areas: self-administration, financing, land planning, public service, information science and the use of computers, housing policy, transportation and the maintenance of thoroughfares, the environment, schooling and care for youth, culture and protection of monuments, sport, recreation and free time, agricultural land, forest and water conservancy system, enterprising and management, international cooperation, health care, social care, regional cooperation, municipal and town police.

In order that it be flexible and that it be able to react well to local conditions, the provision of educational and consulting services is to be decentralized to the maximum extent possible. Beginning in September 1992, operations are to be initiated at regional centers in the following towns and cities: Prague (town), Prague (region), Ceske Budejovice, Cheb, Liberec, Pardubice, Plzen, Most, Brno, Jihlava, Olomouc, Ostrava, Zlin.

The Fund of Assistance to Local Administration has been created with the financial support of the European Community in the framework of the PHARE program, which provides modern technical equipment, top foreign experts for the educational process, and an extensive program of foreign internships. The government of the CR is taking part in financing for operating costs. Prices of educational and consulting services provided to workers of local administration are to be kept at reasonable levels.

Since the Fund of Assistance to Local Administration was founded only recently, it does not yet have a team of its own expert consultants, nor does it yet have much in the way of technical equipment. Just as modest are the results of its training activity so far. All this is in the fledgling stage. Nonetheless, financial coverage from the European Community as well as support from a top levels in government and other high level institutions (members of the Association of Towns and Cities are members of the Board of the foundation) would indicate good prospects for the future.

## **ANNEX E**

### **OTHER DONOR PROGRAMS ASSISTING MUNICIPALITIES**

#### **PHARE**

Phare is the European Community's particular effort to support the ongoing process of economic reconstruction in the countries of Central and Eastern Europe - Bulgaria, Czechoslovakia, Hungary, Poland, Romania and Yugoslavia - by providing financial and technical support in key areas to the governments in creating the conditions of a market-oriented economy based upon private ownership and initiative.

The EC Phare program is financed from funds which are specifically made available for this purpose in the annual Community budget. For 1990, ECU 300 million was provided for Poland and Hungary, and a further ECU 200 million was set aside for the other beneficiary countries (Bulgaria, Czechoslovakia, GDR, Romania and Yugoslavia). For 1991, budget allocations amounted to ECU 765 million. The same figure for 1992 is ECU 1,000 million. These funds are made available as non-reimbursable grants to finance reconstruction programs and not in form of loans for commercial activities.

Phare's objective is to contribute to creation of administrative, regulatory, financial and commercial environment in the following particular areas:

- abolition of state monopolies;
- restructuring and privatization of public enterprises;
- restructuring of the banking system to operate on a commercial basis, development of capital and securities markets, insurance systems and reformed credit, accounting and taxation systems, including the development of rural financial networks.
- promotion of the private sector, particularly small and medium-sized enterprises, together with the appropriate support services, including vocational training;
- development of the labor-market and social sector, including the reform of social security and welfare policies.

The EC Phare program funding for Czechoslovakia (in million ECU) in 1991 had the following structure:

1.	Industrial restructuring and privatization	20
2.	Development of SMEs	20
3.	Energy sector'	5
4.	Environment	5
5.	Telecommunications	6
6.	TEMPUS	9
7.	Labor market restructuring	15
8.	General technical assistance facility - GTAF	20
	Total	100

The GTAF is a multidisciplinary fund, a tool to help develop and implement reform measures which are complementary to the major cooperation programs and contribute to their successful implementation (costs in million ECU in 1991, Czechoslovakia):

1.	Trade and investment	4
1.1	Foreign investment support	1
1.2	Customs, standards, statistics	3
2.	Financial sector	7
2.1	Accounting	1.7
2.2	Tax reform	0.5
2.3	Banking and insurance	3.5
2.4	Capital market	0.7
2.5	Legal advice, general coordination	0.6
3.	Transport	2
4.	Social policy reform	3
4.1	Social security and wage determination	2
4.2	Health	0.5
4.3	Science and technology	0.5
5.	Public administration	4
5.1	Local government	1.6
5.2	Aid coordination	1.3
5.3	Miscellaneous and contingencies	1.1
	GTAF total	20

The EC Phare program is coordinated on the side of Czechoslovakia by the Interministerial Council for Foreign Assistance and Coöperation which has as its secretariat the Bureau for the Coordination of Foreign Assistance. The Bureau is headed by Dipl. Ing. Martineo and currently is located in the Federal Ministry of Economy.

### **EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT - EBRD**

The European Bank is an International Institution with ECU 10 billion of capital whose members comprise forty countries together with the European Economic Community and European Investment Bank.

The Bank's objectives are to provide advice, loans and equity investment and debt guarantees to qualified applicants designed to:

- foster the transition towards democracy and open market-oriented economies, and
- promote private and entrepreneurial initiative

The Bank lends and invests exclusively for projects or investment programs in Bulgaria, Czechoslovakia, Hungary, Poland, Romania, ex-Soviet Union and Yugoslavia.

The Bank's mandate gives it a particular concern for the promotion of democratic institutions and human rights in its countries of operation. The Bank is a combination of merchant bank and development bank. Not less than 60 percent of its funding will be directed either to:

- private sector enterprises, or to
- state-owned enterprises implementing a program to achieve private ownership and control.

Not more than 40 percent will be directed to public infrastructure or other projects. The Bank is committed to promoting environmentally sound and sustainable development. The Bank provides funds according to sound banking and investment principles and within commercial decisions-making time frames. The Bank seeks projects which will contribute to:

- developing the private sector,
- implementing privatization of state-owned enterprises,
- encouraging direct foreign investment,
- creating and strengthening financial institutions,
- restructuring the industrial sector,

- creating a modern infrastructure for private sector, development and transition to a market economy,
- promoting small and medium-size enterprise,
- improving the environment.

In Czechoslovakia, the Bank is a stockholder in companies like Cokoladovny (The Chocolate Works) Praha-Modrany, Czechoslovak Airlines, Telecom and other.

In selected cases the Bank can offer financial advice, and training and technical assistance, where this facilitates the achievement of its overall objectives, based on funds specifically provided for this purpose by certain of its member governments.

The Bank wishes to have contact with a wide range of consultants and financial advisors who are active in Central and Eastern Europe, and who may bring to its attention viable enterprises and projects in the commercial sector. The Bank also calls on the services of consultants and financial advisors from time to time to advise on projects or to provide technical assistance, and maintains a database of consultants. The Bank is also a subscriber to the Dacon system. The Bank opened its representative office in ulice 28. října S. Prague 1. The office is currently headed by Mr. Igor Tham.

The Bank develops Municipal Development Initiative (MDI), a program for the Bank's action in urban infrastructure and local government development. The MDI is being funded through the Bank's Cooperation Fund Program established through contributions from the bilateral donor community and special multilateral funds. In Czechoslovakia, the Bank organized a seminar on local government organization, and provides expert assistance to financial equalization. Other activities of the Bank in Czechoslovakia, together with the Association of Towns and Cities, include:

- study tour in Eastern Europe for town managers and elected officials,
- training for establishment of twinning arrangements,
- restructuring of Ostrava region,
- Bratislava Environmental Seminar for local governments,
- seminars on local autonomy and democracy.