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**TECHNICAL ASSISTANCE TO THE
CZECH MINISTRY OF ECONOMY:**

Compilation of Informational Memoranda

Prepared by

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PREFACE

In response to a request from Dr. Karel Dyba, Minister of Economy of the Czech Republic, Dr. Ludwig O. Dittrich served as an advisor to the Ministry from July, 1992 through December 1992. This Technical Assistance project was funded by the United States Agency for International Development under the program for Privatization and Enterprise Restructuring in Central and Eastern Europe. During the six-month term of this effort, Dr. Dittrich provided advice to the Ministry in a variety of areas related to privatization, economic reform, municipal finance and intergovernmental relations. This document presents a compilation of the information provided to Czech Ministry officials in the form of memorandums, briefing papers and other forms of correspondence during the course of the project.

In addition to the information presented in this document, and the day-to-day advice provided by Dr. Dittrich to Ministry officials during the course of the project, a seminar was organized and conducted on the topic of "Municipal Finance and Intergovernmental Relations." This two-day seminar was attended by officials from the Ministry of Economy, the Ministry of Finance, the Czech Parliament, and numerous municipalities. A briefing booklet for this seminar was prepared under separate cover.

Information for Mr. Prikryl, Deputy Minister

MAIN FEATURES OF US PUBLIC POLICY AT THE STATE AND LOCAL LEVEL

Numbers and Types of American Government Administrative Entities

According to census from 1987, there were 83,217 governmental entities in United States. These include 50 state entities and the Federal administration.

Figures for 1987 and 1982 are given in Table 1.

	Table 1	
Government type	1987	1982
Federal government	1	1
State government	50	50
Local governments total	83,166	81,780
out of that		
"County"	3,042	3,041
Municipality	19,205	19,076
Town	16,691	16,734
School district	14,741	14,851
Special district	29,487	28,078

The average number of "local governments" in each State is 1,663, the distribution among States is very uneven. E.g. in State Illinois there are 6,626 local governments, but State Hawaii has only 18 local governments. From 50 states of the United States of America, ten States concentrate almost 50 % out of total number of local governments, i.e. around 41,000 administrative entities.

Sources and Uses of Funds on the Federal, State, and Local Level

On the federal level in 1988-89, the total revenues amounted to 1,093 billion dollars. Out of that number, tax revenues accounted for 56 %, social security insurance for 31 %, other incomes from insurance 1 %, fees 7 %, miscellaneous other revenues 5%.

During the same period, the expenditures of the federal

government amounted to 1,270 billion dollars. Out of this sum, expenditures for defense and international relations accounted for 27 %, subsidies to States and local governments 10 %, interests on federal debt 14 %, social security payments 25 %, other federal expenditures 21 %, and other payments of federal insurance 3 %.

Distribution of tax revenues in 1989 according to tax types on the federal level was as follows: tax from individual incomes accounted for 72.3 %, corporate income tax 16.77 %, sale taxes (e.g. payments of duties and gasoline tax) 8.53 %, other taxes 2.33 %.

On the level of States, the total revenues in 1989 amounted to 482.4 billion dollars. Out of that sum, intergovernmental transfers account for 24 %, tax revenues 58.9 %, fees 8.7 %, other returns (e.g. from lottery) 9.1 %.

In the same year, the expenditures of States amounted to 469.3 billion dollars. Out of that, subsidies and other intergovernmental transfers accounted for 35.2 %, expenditures for elementary schools 0.3 %, for universities° system 11.9 %, social support 15.6 %, hospitals and health care programs 6.9 %, costs of road network 7.5 %, state police 0.9 % and miscellaneous expenditures 21.6 %.

Allocation of tax revenues of state administration, which represented 284.1 billion dollars, is as follows: Tax from land 2 %, tax from sale 33 %, tax from individual incomes 31 %, tax from corporate profit 8.3 %, and miscellaneous other taxes such as selective taxes from sales at 25.6 %.

On the level of local governments, the total revenues for 1989 were 468.5 billion dollars. Out of that sum, intergovernmental transfers from the federal government

account for 3.8, and from the State administration 3.6 %. Tax revenues represent 39.4 %, fees 14.1 % and other returns 9.1 %.

In the same year, the expenditures of local governments amounted to 460.4 billion dollars. Out of that, transfers to the State budget represented only 1.1 %, expenditures for elementary education 39.9 %, for universities° program 7.7 %, costs of road network 4.9 %, local police 5.1 % and other expenditures 34 %.

Allocation of tax revenues of local governments, which represented 184.5 billion dollars in 1989, is as follows: tax from land 74 %, tax from sale 10 %, tax from individual incomes 5 %, tax from corporate profit 1 %, and miscellaneous other taxes 9 %.

Variability of state and local sources and expenditures excluding the states Hawaii and Alaska for 1989

In Tables is given a range as an indicator of variability of state and local sources and expenditures as a percentage of individual sources or expenditures in the sum total.

Table 2
Variability of revenues on the State level for 1989
range of range of revenues
shares (%) per head (\$)

intergovernmental transfers	17,6-35,6	291-1023
tax from real property	0,0- 9,8	0- 211
tax from sales	0,0-39,6	0- 822
tax from individual income	0,0-31,7	0- 771
corporate profit tax	0,0-10,2	0- 247
selective taxes	8,7-32,0	162- 813
fees for services	4,6-20,2	75- 481

MEMORANDUM

Date: August 27, 1992

To: Dr. Karel Dyba, Minister

From: Ludwig O. Dittrich Ph.D.

Subject: PRINCIPLES AND EXPERIENCE WITH MUNICIPAL FINANCING AND
GRANT SYSTEMS

This document is not intended as an exhausting description of the problematic of financing costs of management of municipalities and localities and re-allocation of funds from the central budget, but rather a sketch of important question for construction of intergovernmental fiscal relations.

General Problems of Relations Between Central Budget and Budget of Localities

Experience shows that almost without exception the central government requires from localities provision of services calling for higher expenditures than the localities are able to provide from their sources (vertical imbalance). This situation almost always leads to a transfer from central sources to localities.

Another problem linked with local finance situation is the so-called "horizontal imbalance". This means that localities have very differing capabilities in the sense of tax capacity.

Local governments bear main responsibility for effective allocation of funds producing public and social services and creating conditions for private investments.

This means that the role of local governments in issues of social redistribution and macroeconomic stability is of secondary importance.

From this viewpoint, a theoretical guideline for allocation of responsibility for services among various degrees of governmental level should be a principle that the responsibility is to be allocated to the lowest governmental level consistent with effectiveness of lad out sources.

A higher degree of government would be theoretically more effective only in cases where demand for a service is equal among localities, where the positive (or negative) contribution of the service provided "spreads out" beyond administrative borderlines of the locality and when

administrative costs of the locality for providing the service would be excessively high.

Basic economic role of local governments is to provide public services for which the local inhabitants are willing to pay. An important element for successful implementation of this role is existence of a mechanism for monitoring the outcomes of the work of local governments by the inhabitants of localities for such part of services the inhabitants of localities pay for and by the central government for such work which was finance by transfer of funds from the central budget. This mechanism for "accounts rendering" in public sector is a functional version of "economic result" (profit) in private sector.

For proper function of this mechanism, the local governments should in most cases collect fees for provided services and where this is not practicable, finance the provided services from taxes on local inhabitants. Local governments should be supported in using such funds in a largest scale possible, but also held responsible for using these funds. Essential principle is that the local governments ought to have right of a free access to local sources even assuming that there will be mistakes in their use. When sources are used to providing local services, the mistakes of the local government can be corrected by the election system (via election of other representatives). When services are connected with national interest, e.g. research or programs for poverty restriction, they should be at least partly financed from the central budget and the result monitored centrally.

Principles of Intergovernmental Financing Redistribution

Type and system of financing redistribution can be assessed only from the viewpoint of their impact on principles of effective use of funds, macroeconomic stability and distributional balance.

Main tasks of financing redistribution are as follows:

1. To remove vertical imbalance, i.e. to ensure that revenues and expenditures on various governmental levels are relatively balanced.

This process can be characterized as follows. First, all transfers from a higher governmental level to a lower one help remove imbalance independently on the purpose of transfer. Second, independently on what are the transfers based on, i.e. on value per inhabitant or on a basis of contributions of values accrued in the locality to the

central budget, they should not be contradictory to other tasks of governmental policy, such as e.g. effectiveness of public sector, diminishing social inequalities and so on. Third, one can say that the vertical imbalance have been removed, when revenues and expenditures of the richest locality are balanced. Imbalance between revenues and expenditures remains for poorer localities, but this is then a problem of removing horizontal imbalance.

2. To remove horizontal imbalance, i.e. to ensure that economic conditions are if possible equal in all localities. The stress is on imbalance in economic conditions and it is not assumed that deficit of local administrative would be flatly compensated for from the central budget. The flat compensation would have no economic sense since it would ignore differences in preferences of local inhabitants, their needs, costs of providing public services and tax capacity. Therefore the systems aiming at removal of horizontal imbalance focus on balancing of tax capacity of a locality for provision of a specific "package" of public services or on equalizing the inhabitants of localities in the sense of ensuring certain level of services.
3. To stimulate tax effort of localities. This goal of governmental transfers of funds is controversial. Question is whether it is effective to use an intergovernmental transfer as a means for enhancing the effort of localities to widen the tax basis. The answer is by its character conditioned by the situation of the locality. In some cases there may be also dampening of the effort of the locality to mobilize tax basis.

Tax from real property together with user fees as an instrumentality of financial resource for municipalities (local level governments)

Tax From Real Property

Tax from real property is an important source of revenues for localities in many countries. Tax from real property, although relatively administratively demanding, has good qualities in view of allocative effectiveness and social neutrality especially in such case, when consumption of public services in a locality is strongly in proportion with the value of real property in the locality. Tax from real property is also very "visible" to local taxpayers and therefore leads to greater responsibility in management of local government.

On the other hand tax from real property has its disadvantages:

1. Tax from real property must be paid directly to the locality in periodical payments. This means that taxpayers are more aware of the amount of payment, not as in the case of income tax which is paid through regular deduction from their weekly or monthly salaries. The method of payment of the tax from real property increases sensitivity of taxpayers also to nominal increases of the tax.
2. Tax base of the tax from real property is not elastic in relation to price increases of the services provided by the locality. This in practice leads to increase of tax rate which is politically unpopular measure.
3. Tax from real property is in most cases the main source for provision of municipal services such as road maintenance, waste collection, removal of snow, public schools and so on. In case of problems with these services the inhabitants will easily make connection between these problems and a high tax from real property and may make more difficult or block the use of the tax for obtaining other sources.
4. Administration of the tax from real property has also its problems. Theoretically, assessment of real property for tax reasons should be equal to the market value of real property. In practice we can find big differences between market value and assessment for the same type of real property in a locality and between localities. This leads to consistent pressures from taxpayers for relief from taxes through individual changes in tax assessment.

User Fees

In general we may distinguish at least three kinds of users' fees.

1. Fees for services - e.g. license fees connected with ownership of a car, dog, entrance into marital status, obtaining copy of a document and so on, paid by a specific person or persons. These fees actually represent partial settlement of the private sector of costs of public sector.
2. Public prices - e.g. fees for entrance to recreational facilities, prices of gas and electricity provided by a city gasworks or power plant is the price for which the locality provides this goods to private persons. These prices should be determined on the basis of a market mechanism without subventions or a tax component.

3. Taxes from specific advantages - e.g. sewerage fees, fees for improvement of the locality, fees for street lighting and so on. Taxes from specific advantages differ from public prices, which are paid on the basis of a free decision of the buyer, but are similar to payments for services, which are in many cases commissions. Main difference is in that this source is not a result of providing services to a specific person. Most of these taxes are derived from a characteristic of real property such as assessment, where it is built, size of the area and so on.

Information for J. Prikryl, Deputy minister.

From : Ludwig O. Dittrich

CHARACTERISTICS OF MUNICIPAL BONDS AND THEIR ROLE IN LOCAL FINANCING

Municipal Short-Term and Long-Term Credit in USA in Figures

The following data outline the scope of use of municipal bonds in United States of America.

Value of municipal bonds in USA by the end of 1989 according to type of bonds (\$ million)

Total	Short-term	Long-term
502,855	15,714	487,141

Value of long-term municipal bonds in USA by the end of 1989 according to function of bond (\$ billions)

Total	Water	Electricity	Gas	Transport	Education	Industry	Others	
					A	B		
487	41	65	1	7	49	2	130	190

(A = Elementary and high schools, B = higher education)

For comparison, in 1989 revenue of municipalities from own sources was 293 billion dollars and together with intergovernmental transfers amounted to 468 billion dollars. This means, that debt/revenue ratio for municipalities in USA is roughly one to one. In 1989 municipal bonds in a total sum of 60 billion dollars were placed in the market and bonds at 35 billion dollars were paid, so that the total increment was 25 billion dollars.

The above figures show that in market economy the access of municipalities to capital markets is vital important for planning and implementation of investment programs which cannot (and/or should not) be financed from tax revenues and

governmental subsidies. It is also necessary to note that most municipal bonds (97%) are of long-term character, i.e. with payment period over 5 years.

Pilot Program for Enabling Access of Municipalities to Capital Market in the Czech Republic

When we assume a transient period of instability in revenues of municipalities and increased demandingness of operating and investment expenditures at least in the next 4 years, the municipalities must have access to financial sources of long-term character with no binding to rendering these funds from central government and from funds of current accounts

From this reason and for support of independence of municipalities in their performance of self-government and creating conditions for development of private activities, municipalities cannot wait for stabilization of the situation before launching long-term investments.

The pilot project would focus on the following:

- a. Analysis of municipal projects in financially prospective municipalities.
- b. Definition and preparation of capacity of a Czech financial institution for securing issue and administration of municipal credits.
- c. Providing technical aid to the Czech financial institutions for securing managerial and operating group.
- d. Active cooperation with municipal administration at structuralization of financial part of the project and legal security.

e. Elaboration of a method in selection of private enterprises for technical realisation of the project with focus on minimalization of risk.

COMMENTARY ON NOTES ON "PRINCIPLES OF BUDGETING FOR MUNICIPALITIES IN 1993", ON MINISTRY TOP MANAGEMENT OPERATIONAL MEETING HELD ON 27. JULY.

- has no characterized objective

increase in effectiveness of providing local services through stress on combination of expenditures and financial sources of municipalities.

Creation of conditions for development of private sector through increased effort at making localities attractive for domestic and foreign capital.

to prepare effective intergovernmental cooperation between the central government and local governments.

Making transparent the impact of financing and investment actions of the municipality and private sector on current and future financial balance of the locality.

- has not elaborated analysis of the hitherto state and described practice at allocation of the budget in 1992

Information for Minister.

L. O. Dittrich

MUNICIPAL BUDGETING AND THE INTERGOVERNMENTAL TRANSFERS
Letter to Minister of Finance, P. Kocárník.

21. August, 1992

Pavel Kocárník, Minister
Ministry of Finance of Czech Republic

Dear Mr Minister:

It is obvious, that the development and implementation of a system of financing municipalities and intergovernmental relations is not a short-term affair and will go through an evolutionary process. Any system which will be used will go through changes in the next years on the basis of gained experience.

Experience shows, that localities are mostly not able to finance all their expenditures on activities in their competences from their own sources. Therefore subsidizing policy is important for reaching social stability, economic growth, macroeconomic stability and microeconomic effectiveness.

For a successful system it is necessary to realistically define the tax base of municipalities, their expenditures for provided services and also to ensure monitoring of results. Success of the system of municipal finances and intergovernmental transfers must be measured in reaching the goals of effectiveness, stability, growth and security of basic social standards. Therefore monitoring of results in reaching these goals is inseparable part of the whole process.

In my opinion, the expert position of the Ministry of Finance of the Czech Republic in revenues area would be effectively completed by an active participation of the MHPR in preparation and monitoring of the system of financing municipalities and intergovernmental transfers from the following reasons:

1. MHPR is in a position to monitor reached results of the system of intergovernmental transfers based upon work directed to development of the region and to provide continuous link between intended results and reality, which is a precondition for rational and rapid modification of the subsidizing system.
2. MHPR is in a favorable position for interpretation of the interests of municipalities and the central government, which creates condition for continuous cooperation of localities on the development of intergovernmental relations. This continuous cooperation foregoes potential risk that local governments would feel alienated from the policy of the centre.
3. MHPR has conditions to gather data on localities. These data are important for construction and assessment of subsidizing schemes.

Information for minister.

L.O.Dittrich

PRELIMINARY COMMENTS ON "PRINCIPLES OF LOCAL BUDGETS".

I presume that this material focuses on the issue of revenues deliberately, leaving a more detailed solution of expenditures issues for a further discussion. Especially in this transient period the expenditures may show considerable instability.

I believe, that the paragraph "Preconditions" describes a set of stylized truths, which should be a philosophical basis for proposed measures.

All which is sad up to the section "c" is generally accepted as a stylized truth in the area of public finances" (see my Memorandum to Mr. P²ikryl as of June 27, 92).

I do not understand the section "d", because it is improbable that localities would associate on principle of mutual subsidizing current expenditures. In the section "e" there is an implicit precondition, that for preparation of budget the revenue side is primarily important. I believe that for completeness and transparency of the budgetary reality, the expenditure items should also be prepared in several variants depending on external preconditions on change of structure and amount of local expenditures. Sections "f" through "h" can be accepted on the basis of a principle of compensation of "horizontal and vertical" imbalance.

Paragraph "Plans" sets directives to the financial system. The main problem of this section is a general indefiniteness (vagueness) in terms, such as "to a largest possible extent, to avoid too big changes etc., to compensate for differences to an extent which will not impair the interest of citizens etc."

Without more detailed analysis these concepts cannot be given a quantitative value even though the effectiveness of the system is directly dependent on this quantification.

From section "Target solution" a potential item of revenue from tax from sales (turnover tax) is left out. Tax from sales complies with the requirements that local expenditures be financed from local sources. Participation on income of natural and legal entities has its logic, although it is not clear whether allocation of the tax into localities on the basis of where is the residence or site of the enterprise will not lead to destabilization of revenue basis of localities due to considerable concentration of creation of GNP in the Czech Republic.

The problem with numeric data in the table of revenue items of local budgets is that materials used for preparation of these estimates are not made transparent. Therefore it is hard to comment on these figures.

Also, nowhere is elaborated the problematic of this new system on localizing decisions of private sector which will actually form the tax base and the scope of necessary services in each locality in the next years.

MEMORANDUM TO MINISTER

Date: September 8, 1992

To: Dr. K. Dyba, Minister for Economy Policy and Development.

From: L.O.Dittrich

Subject: CHAMBERS OF COMMERCE IN USA.

In the USA the chambers of commerce are organized as non-profit organizations. Membership is non-obligatory while the members' basis does not significantly differ from proportional representation of economic sectors and distribution of small, medium-sized and large firms in the American economy.

Top organization of chambers of commerce is "U.S. chamber of commerce" which collects fees from economic chambers on the level of States, which collect fees from local chambers. Important is that firms may become members in chambers on all three levels and then pay fees to all economic chambers to which they are members. In proportion of total funds of economic chambers, membership fees represent for U.S. Chamber of Commerce, state chambers and local chambers roughly 60 %, 80 %, 95 % respectively of the total incomes. Membership fees are scaled with regard to size of a firm (e.g. number of employees, amount of sales etc.). Additional incomes are from fee for conferences, income from publishing activity, advertising and others.

The main function of chambers of commerce is in protection of interests of business circles on federal, state and local government level (lobby).

From this reason the chambers of commerce in USA do not have funds from state to avoid conflict of interests. From the viewpoint of firms the chambers of commerce would become "prisoners" of governmental interests which would decrease attractiveness of membership.

Apart from active "lobby", the chambers of commerce provide information on the development of tax laws, development of legislation, they organize workshops and specialized courses for their members.

MEMORANDUM TO MINISTER

Date: September 22, 1992
To: K. Dyba, Minister for Economy Policy and Development
From: L.O.Dittrich
Subject: RESTRUCTURING OF THE COAL INDUSTRY AND RESPECTIVE
STANDPOINTS OF KOO, OKR AND MSS FOS.

References in "opinion" to the report relate mainly to black coal. Section on problematic of lignite is referred to only once on page 6, namely in the sense of "imbalance" of the proposal on compensation of mining damage for both sectors and on page 4 in connection with the concept of "inner competition".

On a general level, the "opinion" comments on objective, implementation and financing of restructuralization.

Page 1. I do not have sufficient materials and information to comment on the statement in the "opinion" that the Czech republic has not elaborated a long-term raw materials and energy study.

On the other hand, absolutely wrong is the conclusion that "one cannot speak of unprofitability of mining, when the energy sector has CSK 20 billion of profit".

Page 2. The commentary of the "opinion" on quality of privatization projects which were submitted to evaluation by the privatization committee of the MHPR CR before solving the issue of timing of the price liberalization and of statutory standing of KUS in its relations to the state has its merit. Demands on the state budget will become a function of the variant of price liberalization, as it is finally mentioned in restructurizing document (for black coal on Page 10). Comments on adequacy of contribution from the state budget to various items which follow on Page 2 and

on first half of Page 3 and after all in the whole "opinion" are directed toward making doubts on distribution of financial responsibility between the state and KUS. With regard to non-decision on progress of price liberalization, the position of the "opinion" is almost without exception defensive.

Page 3. Here the whole logic of selection and construction of new KUS is attacked. Without more detailed knowledge of attributes of each plant it is difficult to comment on the view, that district OKD including CSM a Hermanice, which as I understand it was the subject of privatization project No.2, would be more able to carry out dampening operation, carry out transfer of personnel and soften social and political impacts.

Page 4. Reference to inner competition as a result of three entities in lignite industry can be commented from the viewpoint of an alternative non-creation of KUS. One can say that decrease in production at new price conditions and "all in cost" operation would go on at least as rapidly or even more rapidly with all social and political impacts.

Payment liabilities from the past have two dimensions. First, the total volume of sums depends on inflation, which may be different for other sectors. For example, stabilization of prices of black coal due to international competition does not have to have a parallel in price development of costs for closing of mines, removal of environmental damages and indexation of pensions, and similar. Second, distribution of expenditures is a function of the dynamics of start of various items. If for example process of consolidation accelerated against the anticipated time period, the financial burden of KUS could compress on the beginning of the consolidation period.

Page 6. Costs on closing mines are commented on the Page 6. The period of four years in the "opinion" is contradictory to proposed budget for two years in Restructuralization Project. In this case, I would adhere to the statement of the "opinion".

**FOREIGN AID AND COOPERATION IN THE DEVELOPMENT OF THE
LONG-TERM MUNICIPAL CREDIT SYSTEM**

Introduction to Problem

Investments into local infrastructure are of a long-term character and have considerable demands on amount of funds. Currently a financial mechanism is lacking which would enable municipalities to invest into infrastructure in required scope. Current possibilities which exist do not by far cover the real need. Municipalities are dependent on funds from current revenues, subsidies and funds gained by sale of municipal property. The last mentioned source is of temporary character and a question also arises of its suitability for these purposes.

Experience of states with advanced market economy corroborate that for successful introduction of a market economy it is necessary to create conditions for enterprise on a local level. Economic and administrative decentralization of the economy, which is a prerequisite of a successful transformation of our economy, calls for flexible response of local governments to needs of small, medium and large enterprise. Therefore it is necessary to enable municipalities an access to sufficient mechanism for financing of municipal projects through a functioning system of municipal credits.

But it is improbable that in a situation of absolute shortage of funds of a long-term character and lack of experience with municipal credit the existing financial institutions could react to requirements of the municipalities.

Therefore it seems desired, that in compliance with experience from abroad the access of municipalities to long-term credit would be enabled with using foreign funds and technical assistance. We must however stress, that the final municipal credit system is conceived as a system using predominantly domestic sources and does not rely on foreign capital.

The objective of the proposed project is mobilization of capital from various foreign and domestic sources and creation of conditions for integration of municipal demand for capital into newly emerging capital market.

Proposed Mechanism and Process Enabling Municipalities Access to Funds for Investments in Infrastructure

First it must be taken into account, that proposed institutions and institutional relations and stress on various components of the project will gradually change, as final objective is a mechanism of crediting municipalities on a commercial basis.

With regard to available sources and in order to secure successful start of the concept we propose to conceive the project as pilot. This means, that for the beginning we propose selection of a group of municipalities (3 up to 6) for including into a program of financing their investment programs.

Municipalities

As it has already been stated, municipalities are at the same time in conditions of a bigger responsibility for economy and they are also given a larger possibility to determine and decide on composition of future revenues. The

fact, that future revenues can be realized only on conditions where municipalities have possibility to capitalize these revenues, stresses the necessity of developing a credit system.

Given the low procedural equipment and experience of local governments with estimates of financial and economic return of long-term investment in conditions of market economy and their connection and impact on local budgets, an intensive technical assistance is necessary, which will be provided by foreign and trained domestic experts in this field and financed from foreign sources intended for these purposes. Evaluation of intended investments and their connection with future revenues of localities will be in the course of time and in correspondence with strengthening of decentralization process predominantly in the hands of local governments.

Municipalities included in the pilot project should be medium-sized, with initiative board (management) and a well-thought technical concept of investment. From external view, the selection of municipalities seeks to respect regional development preferences, but not to the detriment of commercial quality of proposed investments.

The most important element in the selection will be a clear conception of representatives of a municipality that it is a case of credit funds, which will be reimbursed with interests to the creditor.

Financial Institutions and Credit Mechanism

The variant of a municipal credit system, which appears prospective especially in the initial period and on condition, that the initial capitalization of the program will be realized using foreign sources is establishment of

a Municipal Fund (MF). In one version of the program, the MF would be capitalized from foreign sources, which would via existing network of commercial financial institutions be offered to local governments for investment into infrastructure. The financial institutions would grant credits on such terms and with such interest rates which would cover their profit, administrative costs and costs for funds from MF. The MF grants sources in such a way so as to cover its commercial margin and costs of financial funds from foreign creditors.

In the next phase of the development of the municipal credit system it can be expected that MF would be able to issue own bonds intended for domestic and foreign capital market and thus guarantee for liquidity to financial institutions granting the municipal credit. Financial parameters of the bonds should enable their participation in a secondary capital market. Composition of demand for bonds would develop in connection with the development of the capital market and it can be assumed that in the set of clients will be both households and banking institutions as well as insurance companies.

Currently a possibility is considered that for the pilot project, primary financial source for capitalization of the Municipal Fund will be "Housing Guaranty Program" (HGP). In such case the U.S. government guarantees commercial and exchange rate risk to American investors and requires equal guarantees from the Czech government.

In the process of establishment of the municipal credit system will thus apart from municipalities domestic financial institutes, the municipal fund, MHCR, Ministry of Finance and the Czech Government be involved through allocation of reserves to cover commercial and exchange raterisk.

For covering commercial risk and thus neutrality of this part towards the state budget, it is proposed that municipalities will grant a pledge in the form of to them appurtenant transfers of taxes from income of natural entities, tax from real property and as the case may be their own real property. It is necessary to realize that it is the case only of guarantees and the municipalities have responsibility for payment of credit through modification of their revenues and expenditures and the guarantees would be used only in case of municipal insolvency.

Also in the case of the exchange rate risk there is a possibility of a partial insulation of the budget in such a way, that part of the risk will reflect itself in the interest rate of municipal credit, or it will be covered b an investment of part of the reserve fund into financial instruments denominated in corresponding foreign exchange orboth.

Time schedule of the pilot project:

- selection of municipalities which have shown interest in the project and which meet criterions of needs of capital investments, potential for fulfilment of payment liabilities and which accept terms of guarantees from the funds of transfers appurtenant to them and as the case may be by pledging real property. Selection is made by MHCR in cooperation with Ministry of Finance. Deadline: End of March 1993.
- Precision of administrative demandingness and legal correctness of guarantees with Ministry of Finance and MHCR and relating quantification thus burdened municipal sources. Deadline: end of March 1993.
- Provision of technical assistance to municipalities in

preparation of budgets and their modification in connection with prepared projects. This assistance is not conditioned with participation in the pilot project even though the long-term technical assistance should predominantly be directed to municipalities which will take part in the pilot project. Deadline: start by the beginning of March 1993 with an open deadline of completion.

- Selection of an institution serving as a site o MF and provision of technical assistance for its establishment. CMZRB appears to be prospective institutions. In this connection it is expected a technical assistance to financial institutions, which have shown interest in cooperation in the form of training of their workers in the field of municipal credit and its administration. Equal assistance will be provided to the workers of the MF with sufficient stress on ev aluation of results and development of institutional capabilities of the MF in mobilization of domestic and foreign financial sources. Deadline: start by the end of February 1993 with an open deadline of completion.

COMPARISON OF THE PROPOSED PILOT CREDIT PROGRAM WITH THE FULL DEVELOPED CREDIT SYSTEM: INFORMATION FOR MINISTER

Partners in the proposed program are municipalities, financial institutions (FI), municipal fund (MF), central governmental institutions and of course foreign investors.

The program presupposes that during the next years the participation of partners will change in relation to shift of the character of the program to a normally functioning municipal credit system (MCS).

The final MCS should meet a condition that instruments offered to investors are an attractive alternative at construction of their portfolio. This means that combination of risk and return of municipal instruments must complete the range of existing possibilities for the investor. Whereas municipality is by its nature a political entity, capital is in most cases offered by commercially oriented private entities, which do not have any reason except commercial advantage, to prefer political entities to private entities.

It follows that the final MCS must have a) low administrative costs, b) information effectiveness, c) sufficient liquidity and d) range, in addition to e) definable return on investment and f) risk components.

The proposed program must be designed in such a way to enable as quick as possible an access of municipalities to capital, but also a stimulative element enabling development and integrating of MCS into the regular financial market.

In a functioning financial market the MCS would represent a set of alternative instruments with transparent and definable characteristics.

Following is a proposal of a description of the program and of transformational process to MCS according to individual criterions.

a) Administrative costs.

PROGRAM: For all participants to the program, administrative costs will be considerable. In most cases however these will be initial investment costs for introduction of analytic, information and operational system. What is meant is financial and economic analysis of projects on the level of

municipalities, evaluating and operational system MF and FI and last but not least solution of legal frame for providing guarantees and accurate terms of granted credits. No less important is preparation of employees of MF and FI and their training in all aspects of the program.

During the launching time these costs will be from major part covered from technical assistance financed from the funds of USAID.

MCS: In the process of transformation of the program it is supposed that standardization of information and operations connected with financing of municipalities will lead to lowering of costs. Financial institutions and MF will be able to offer a forming of an offer in the form of percentage fee from the total amount of required financing.

b) Information effectiveness.

PROGRAM: Heterogeneity of projects, unstable price relations and uncertainties about tax return on the level of municipalities will call for direct participation of FI and MF in evaluation of projects of municipalities. Important will be in this phase the participation of foreign and domestic experts, specifically in the field of evaluation of economic and financial return of offered projects. It is assumed that financing of this technical assistance will be from funds of USAID.

MCS: It is assumed a lower participation of MF and FI in analysis of individual projects. MF and FI will more rely on general information on financial value of a municipality. By this the MCS will transform into a form which is in compliance with commercial principles. This phase will take a longer time depending on collection of time information, stabilization of tax base and standardization of accounting and auditing system of municipalities.

c) Liquidity.

PROGRAM: In initial phases of the program the liquidity of municipal credit is very low, almost equal to zero. Purchase of municipal bonds or participation on loan, which within the program the FI prepared from the side of MF, is an in advance agreed characteristic of the program and therefore limited to participating FI. This means, that the condition for a real liquidity, i.e. to find a buyer for a financial liability in a short time, is not met. Nevertheless, it would be possible to introduce from the beginning a certain percentual range, in which MF and FI would agree to take

over part of their position in the municipal credit at predefined terms.

MCS: Liquidity of instruments of the municipal sector, just as of every other sector, is dependent primarily on the development of the capital market. Provided that the capital market will develop successfully, standardization of credit instruments, credit history of the market, tax conditions and innovative constructions of municipal credit appealing to a wide range of investors will be decisive elements of a degree of liquidity of municipal credit. Municipal bonds financing investments of larger volume should become a common instrument on the market with securities.

d) Range.

PROGRAM: By range a heterogeneity of standardized offers of municipalities to potential investors is meant. In the first phase of the program, the character of the credit and its term will be determined depending on the initial investor, i.e. by terms of credit granted within Housing Guaranty Program, a specific need of municipalities and by terms of MF. But also from the beginning it is however supposed that the structure of loans or bonds will as much as possible approximate to a common standard.

MCS: The goal of a developed system is an offer of heterogeneous but standard financial instruments which would find place in portfolio of FI and other institutional and individual investors. What is meant is heterogeneity in terms of payment, coupon value, methods of amortization and classification of demands on revenues of municipalities.

e) Return

PROGRAM: Return of nominal invested capital and nominal return on such capital is for foreign investors secured by governmental guarantees. As was said elsewhere, in the first phase of the program it is calculated with general tax revenues of municipalities which complete demands for returns from financed projects. Apart from it it is assumed that municipalities will guarantee loans by abandoning possibility of interception of MF revenues from tax from real property and other revenues and demand for own real property. It is thus a temporary situation substantiated by the need of quick start of long-term credit for municipalities.

MCS: Full developed system assumes that the market mechanism determines the required return rate. Investor requires a return rate which is attainable on investment instruments

of equal characteristics and quality. It is assumed that municipal instruments will have different quality and characteristic which will determine the required return rate. MF in this phase can develop into a financial institution which stabilizes the market with municipal bonds through purchase when there is a supply overhang and through sale on overhang of demand.

f) Risk

Relevant risk for each investor granting credit is the risk of non-payment, risk due to change in market interest rate, risk of illiquidity, risk of premature withdrawal of credit or withdrawal of bond. In the case when use of foreign funds is supposed there is also an exchange rate risk.

PROGRAM: The risk of non-payment is fully covered by guarantees mentioned in the foregoing paragraph and is therefore transferred to municipality.

Risk of change in market interest rate either bears MF and FI in case of a fixed interest rate, or in case of a variable interest rate this risk is transferred to municipality.

Risk of illiquidity cannot be defined in this case, since in the pilot phase of the project there exists an agreement on repurchase of loans or bonds by the Municipal Fund (MF).

Risk of premature withdrawal of credit or withdrawal of bond will be solved by terms of financing which will not allow to shorten the term of the loan or prepayment of bond.

Risk of change in exchange rate may leave the main guarantor of the loan, i.e. governmental guarantor, or part of the risk will be transferred to municipalities through indexed interest rate.

MCS: Risk of non-payment corresponds to credit value of a municipality and reflects itself in the required return rate. MF can "improve the quality" of the municipal credit by spreading the risk through holding a diversified portfolio and financing it by issuing its own bonds.

Risk of change in market interest rates is borne by investors.

Risk of illiquidity so will diminish with the development of a secondary market, with range of supply and with activity of brokers.

Risk of premature payment of bond or credit is regulated by terms of contract and reflects itself in

required interest rate or return on bond.

Risk of change in exchange rate will diminish as it is assumed that financing of municipalities will be predominantly matter of domestic investors. Foreign investors in case of a free convertibility of koruna can limit their risks by means of standard financial operations.

Appendix 1

Information for Minister

NUMERICAL EXAMPLE OF THE FUNDING PROCESS

In this appendix typical steps are described leading to realization of municipal loans or issue of municipal bonds with participation of Municipal Fund (MF). MF is a proposed financial institution aiming at support of long-term investments into municipal sphere on a commercial basis.

Provided that establishment of MF and goals of program are in compliance with conditions of foreign investors and price and terms of loan are acceptable to the Czech government as a guarantor of the loan, concrete steps towards realization of municipal loans or bonds may be as follows:

1. Financial sources placed in MF will be divided among commercial and financial institutions which agreed with conditions for participation in the municipal credit system. (in the following description we use an example of a loan. The procedure in case of bonds is similar).

Positions on accounts of financial institutions and MF is as follows:

Assets	Liabilities
MF	
Advance payment of fin. instr. 1000	Funds from foreign credit 1000
FINANCIAL INSTITUTIONS	
Monetary instruments 1000	Advance payment MF 1000

2. Financial institutions announce that they are able to accept applications for credit and provide information on conditions of the loan.
3. Municipalities will prepare materials for the financial institution including description of project, financial standing of the municipality, guarantees of payment and other information required by the financial institution and by MF.
4. Financial institutions and MF will agree on a pledge,

which can have form of a transfer of tax from real property or interception of the share of tax from incomes appurtenant to municipality in case of its insolvency.

5. Financial institutions and MF will evaluate quality of required credit from the viewpoint of financial risk and other criterions.
6. Final conditions of the loan are agreed upon and the loan is approved by the financial institution and by MF.
7. The funds are transferred to municipality.

Positions on accounts of municipality, financial institution and Mf is as follows:

Assets:		Liabilities	
MF			
Advance fin. instr.	1000	Funds from foreign credit	1000
FINANCIAL INSTITUTION			
Municipal loan	100	Advance payment from MF	1000
Monetary instrument	900		
MUNICIPALITY			
Investment	100	Loan from fin.institution	100

8. In accordance with an agreement of the financial institution and the MF, part of loan is purchased by MF. It is probable that the financial institution would continue (for e fee) in administration of the loan in the interest of MF.

Positions of accounts of municipality, financial institution and MF in case that MF purchases 80 % of the loan is as follows:

Assets		Liabilities	
MF			
Municipal loan	80	Funds from foreign credit	1000
Advance fin. inst.	920		
FINANCIAL INSTITUTIONS			
Municipal loan	20	Own funds	20
Monetary instruments	920	Advance from fin. inst.	920

MUNICIPALITY

Investment	100	Loan from fin. inst	100
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This process would continue with new loans (or issue of bonds) up to exhausting of advance payments. In this example 1000 monetary units could theoretically support credits in a total value of 1250.

With the development of a secondary market one may expect that other investors would participate in financing, either directly through purchase of loan or bond from financial institutions, or by purchase of bonds of MF issued for this purpose.

An important aspect for the development of the secondary market is standardization of legal norms of mu, cd is applies primarily for standardization of forms and conditions of municipal credit, standardization of financial guarantees, standardization of required information on financial situation of municipalities and amount of risk of projects during the term of the credit.

MEMORANDUM

Date: 3/12/1992

To: Dr. K. Dyba, Minister of Economy

From: Dr. Ludwig O. Dittrich

Subject: Visit to Sumava with Ing. Ladislav Macka, Director of CMZRB on 3.12.1992, with preliminary evaluation

Elaboration of municipal credit system via pilot project with participation of CMZRB, technical and financial support of AID, or other institution

For a successful development of municipalities able to support private activity it is necessary to complete the funds from the state budgets and common tax revenues by funds predominantly of a long-term nature, acquired on the capital market on conditions nearing to demands of the commercial sector.

Pilot project or projects, unlike a flat introduction of the municipal credit system, are due to the amount of available funds and lack of experience from the side of municipalities and financial institutions a necessary interlink.

Procedure:

- a. Selection of a municipal project proposed by a municipality with analysis carried out by an advisory group of foreign experts in cooperation with CMZRB.
- b. Simultaneously creation and training of a managerial and operational group in CMZRB for administration and analysis of potential projects and evaluation of quality of municipal guarantees (credit rating).
- c. Preparation of a financial instrument which would be offered to investors and which would meet timing of financial requirements of the project, terms set for participation in "Housing Guaranty Program" (HGP) or in other program of financing.

Regional municipal organizations in the μ umava region:

Regional association of municipalities is to function in the form of an associations of legal entities. The membership is composed of 40 municipalities having a total of 70 thousand

inhabitants on a territory with about 270,000 ha.

Projects:

The projects should meet financial return rate and in case of a supraregional interest an economic return rate. This means that the project will ensure return of paid-in capital and also return on capital.

The representatives of the association summarized the need of investments for infrastructure into following fields: sewage treatment plants, water supplies, energy networks, road networks, gas pipeline.

The general impression from the discussion on projects was very positive, as the representatives of the association had concrete and well thought-out financial aspects of investments. Financial demandingness of the project is in the range from 25 up to 800 million korunas.

It is assumed a technical assistance on evaluation of projects which will be provided in cooperation with the advisory company, the municipality and the financial institution.

Credit risk:

Commercial and exchange rate risk is to be, according to current conditions of HGP, eliminated to the satisfaction of the US government namely in such a way that the Czech government or other acceptable guarantor will grant guarantees to the American government. Commercial risk, i.e. the possibility of non-payment of the credit by municipalities, is dependent among others on the following:

1. Quality of provided guarantees

In case of regional project *μumava* the possibility of use of subsidy allocation must be investigated in its size in comparison with granted credit. In case of other guarantees such as in the form of a real property, legal and functional aspects must be investigated.

2. Experience with municipality at repayment of debt.

In this case it is hard to apply this criterion because the past system of financing municipalities and of granting credits was based on another, centralized system.

3. Possibilities of municipality legally and functionally raise tax assessments and fees.

Here is a question the result of currently introduced reform in administration of municipalities. The Sumava region has an advantage in that it has a potential of high tourism and therefore it can expect improvement in tax base, increase in amount of user fees and license revenues.

4. Sensitivity of the region to general economic conditions.

The region is a border area and it can be assumed that the region is influenced by economic conditions of the Czech republic but also by conditions in neighboring Austria and Germany. Which leads to a partial diversification between sources of economic influences on the region.

Exchange rate risk:

In given conditions the exchange rate risk cannot be removed completely as common mechanism for control of exchange rate risk cannot be applied in case of exposure of CSK versus dollar.

Partial protection could be provided by that the loan would have variable interest rate depending on inflational difference.

Information for Minister

From: L.O.Dittrich

Date: 15.12.1992

INFORMATION AND REPORT PREPARED AS ON 11.12.1992 ON BOTH AID AND URBAN INSTITUTE REPRESENTATIVES VISIT IN MHCR AND THE PROGRAM OF THE COOPERATION

On an informational meeting with the minister of economy Dr. Karel Dyba, representatives of AID and Urban Institute acquainted the minister with main points of proposed project on financing municipal infrastructure from credit funds provided within HG program.

It was set to elaborate a proposal for further procedure in construction and application of the credit. Since it is a loan calling for guarantees of the government, to hand over the information to the Ministry of Finance for evaluation.

It was also set to elaborate an information for the meeting of economic ministers.

After reception with the minister a narrower working group of workers of MHCR met with representation of AID and Urban Institute re more detailed work on procedure for granting technical assistance to municipalities and establishment of municipal credit system for long-term investments into infrastructure. Summary and conclusions are as follows:

Objectives: To support decentralization of the system of management of local governments

To mobilize participation of private sector in economy of municipalities.

To start and develop a credit system for long-term credits to municipalities based on commercial principle.

The discussion stated, that for fulfillment of the above objectives the project must ensure success of a pilot application. It was also stated that results and experience from the project should be generally applicable for solution of the problem of financing municipalities in the Czech Republic. Placement of the project and its content must take into account regional priorities, but not to the detriment of the success of the project.

The group agreed upon the following program before next

visit of the expert group planned by the end of January 1993:

MHCR, department of municipal policy and department of housing policy will ensure the following:

1. Informedness of municipalities which could be considered to be included in the pilot project provided that automatically those municipalities will be included which had been informed on the project during previous visits of the expert group and showed interest.
2. Contact with financial institutions, primarily with CMZRB and ěeská Spo²itelna for determination of an optimal mechanism for administration and allocation of financial credit sources. What is meant is determination of range and type of criterions on decision-making (credit value of municipality, project analysis or their combinations) on allocation of the credit a thus determination of predominant characteristic of an institution as a development or commercial one.
3. Elaboration of a more detailed analysis of guarantee component provided by municipalities with regard to its composition and scope. Selection and composition of the guarantee component must be solved from the viewpoint of administrative simplicity, legal correctness and overall size of needed guarantees.

AID and the expert group will provide the following:

1. A detailed material on linkage between technical assistance for engaged organizations and effective use of credit funds.
2. A detailed description of proposed variants of the mechanism of credit financing.
3. Concrete examples of existing programs and their legislative framework.
4. A detailed program of technical assistance of short-term and long-term nature for the need of project financial and economic analysis.
5. A set of documents and their elaboration for AID when submitting application fo financial funds within HG.
6. Preparation and development of a system for evaluation and monitoring of the quality of the credit program.

Present: AID: Ms. Lee Russell, Mr. Orlinger

Urban Institute: Mr. Kingsley, Mr. Peterson
Mr. Tajsman

MHCR: K. Dyba, V. Stepánek, J. Mejstřík, J. Wagner,
L. Dittrich

Information for Minister

From: L.O.Dittrich

To: Dr. Karel Dyba, Minister of Economy of Czech Republic

RE: Participation in "Housing Guaranty Program" (HGP),
administred by Agency for International Development
(AID), USA.

Dear Mr. Minister:

I would like to support the relatively attractive offer of AID to long-term financing of municipal investment projects with participation of private sector.

It is a long-term loan with payment period up to 30 years for favorable interests.

At least as far as flexibility of use of financial sources is concerned it seems to me, that this offer is attractive, as it does not limit the use of funds only to housing construction as would suggest the name, but it allows financing all projects which support private initiative in the field of housing and stimulate market economy of municipalities.

It is obvious, that the privat sector must take part in the complex housing construction and municipal development in a much larger scale than is the case up to now. Unfortunately, our banking system is at present time not able to offer adequate and effective financial mechanism for transfer of funds for these purposes and capital market for municipal bonds does not exist either.

Apart from direct investments into municipal infrastructure and rehabilitation projects very attractive appears the use of funds from HGP for pilot projects in

coordination with financial institutions either for direct financing of projects or for support of issues of municipal bonds.

Another advantage is the fact, that the loan may become a load-bearing axis for various kinds of technical assistance so that for each dollar of the loan a fraction of subsidized dollar is assigned.

As said at the beginning, these funds have repayment terms up to 30 years and have a relatively low interest. At present, if I am not mistaken, funds with such a long term of repayment just for the field of municipal construction are not available through our financial institutions.

From the viewpoint of interest rate the advantages lie in the fact, that the interest rate in United States of America is relatively lower than in countries of European Community and revenue curve is relatively flat from 7 to 30 years of the repayment term.

HGP presupposes guarantees of the Czech government for commercial and exchange rate risk. Method of securing potential loans must be a topic of concrete discussions with AID. I believe that AID has sufficient interest to apply HGP in the Czech Republic and therefore will have a positive attitude to the process of allocation of risk from various risk sources.

I recommend to apply aggressively for allocation of funds under HGP and in this sense to inform the Ministry of Finance of the Czech Republic.

INFORMATION FOR MINISTER

From: L.O.Dittrich

A. VISIT TO "U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT" (HUD).

HUD has not its own foreign agency for financing projects or technical assistance. This goes via USAID. Experts of HUD can be obtained for participation in projects abroad.

Experience of HUD which could be a topic of discussion with regard to its importance for the Czech Republic relate to three fields.

1. Policy for socially weak classes, in relation lessee - lessor. Criteria, methods, who is subsidized and what are the results.

In this field HUD has many experience and credible statistical data.

2. Role of HUD in financing and insurance of financial liabilities on the market of existing housing fund, family homes and new housing construction. Two institutions have central importance here, Federal Housing Administration (FHA), which insures subsidized as well as not subsidized loans (mortgages) and Government National Mortgage Association (GNMA) which repurchases subsidized mortgages from private financial institutions. Both agencies are fully under control of HUD.

Special attention should be given also to "low rent public housing" program under control of FHA.

3. Role and support of HUD for development of municipalities and their financing.

Form, which is proposed in case of using HGP for establishment of the Municipal fund, is a hybrid of the so-called bond bank and revolving infrastructure fund. Whereas in the US the capital stock is provided by the state, under HGP the capital stock would be provided by foreign investors.

B. MHCR INITIATIVE STATUS RELATING TO FRAMEWORK OF GUARANTY PROGRAM (HGP) FOR FINANCING OF MUNICIPAL INFRASTRUCTURE. DESCRIPTION OF HGP IN APPENDIX.

- According to recent information, USAID is currently negotiating a specific variant of the program for CR.
- an expert group is at the same time in CR and continues in selection of concrete municipalities and projects.
- workers of MH contacted municipalities which can be considered by means of a letter describing the program and with a requirement on providing project and financial information.
- Czech financial institutions expressed their interest about participation in the program. A detailed discussion will be led with Czech financial institutions during the next two weeks.
- the Ministry of Finance is informed on the initiative of MH and a series of meetings will be started for detailing of the guarantee component of the program.

Appendix

Brief description of the Housing Guaranty Program

The Housing Guaranty funds may be used for following purposes:

Loans for construction and renovation of housing units, investments into municipal infrastructure such as sewage treatment plants, water supply, sewerage, gas pipeline, energy and road networks.

Objective of the program:

Support of decentralization of decision-making and financing of municipalities.
Creation of a credit system based on commercial principle.
Creation of conditions for private initiative within strengthening of market mechanism.

Interest terms:

Currently the interest of HGP is 8.75 % fixed for 30 years, or a variable interest with a basic interest rate 4.5 % and indexation to portfolio of financial instruments, or a variable interest with an interest "ceiling".

Volume of funds offered:

Yearly 20 million dollars during 5 years. Together 100 million dollars.

Governmental guarantees:

According to terms of HGP, the Czech government will grant guarantees to the American government on repayment of credit. Elimination of credit risk for the Czech government will be reached by the system of financial guarantees, lying in the possibility of automatic blocking of specific tax revenues of municipalities.

Characteristics of selected projects.

Municipal projects should meet the condition of adequate financial and economic return rate based upon increase in volume of future revenues of municipalities due to investment made.

Technical assistance financed from external sources.

- a. Provided to municipalities for enhancement of local budgetary administration and capital planning.
- b. Creation and training of a managerial and operational group of financial institutions and municipal boards for administration and analysis of potential projects and credit rating.
- c. For association of towns and municipalities and other organizations, introduction of a training program with this problematic.
- d. Assistance to central financial institutions and corresponding ministers at solution of legal and financial aspects of the system.

Information for Minister.

From: Ludwig O. Dittrich

INFORMATION ABOUT FOREIGN USA AID TO CZECH REPUBLIC

A. FOR NEGOTIATION WITH DIRECTOR OF TRADE DEVELOPMENT AGENCY (TDA) MR. MARTINEZ.

TDA is an agency of the US government whose main mission is to support export of American companies into "target countries" and to use expertise of American firms for economic development of these countries.

From the part of TDA so far funds for elaboration of the following studies in the telecommunication sector were released:

- in October 1990 USD 400 ths were provided for technical assistance at selection of technology and system for digital overlapping network. The study was elaborated by firms J.P.Morgan and Bell Atlantic.
- in September 1991 USD 240 ths were provided for elaboration of a study of rules and prescriptions system in telecommunication. The study was elaborated by firm Squire, Sanders & Dempsey.

Contracts have been closed with the then existing Federal Ministry of Posts and Telecommunication.

TDA has also provided funds for studies in the following fields: banking, energy, petrochemical industry, environment, railroad transport and management.

Topics for discussion from the last meeting with Mr. Martinez and which correspond to present interests of MHCR.

MHCR intends to continue in developing cooperation in telecommunication namely in the following form:

- providing assistance at introduction of new prescription basis into practice
- providing assistance at preparation of a new summarizing law on telecommunications
- training of workers of Telecommunications office
- consulting at incorporation, privatization, and license procedures and at preparation of decrees and other legal

documents

MH CR is also interested in providing assistance at preparation of prescription and regulation basis for public utilities.

MH CR does not at present time consider possible to develop cooperation as to the military territories Rálsko and Mladá.

B. FURTHER FIELDS OF COOPERATION OF MH CR WITH USAID.

- The housing policy and development of mortgage credit system, technical assistance and provision of seed capital. References in the report elaborated by the housing policy department (Wagner, Dittrich)
- Financing of municipalities with use of municipal credits and bonds. Technical assistance and seed capital provided via Housing Guaranty Loan Program (HGP). References in the report elaborated by the municipal policy department (Mejstřík, Dittrich)
- Support of social and economic development of regions. Possibility of establishment of Venture Capital project for the region North Bohemia.
(PEACE, American Enterprise Fund).