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PARTICIPANT WORKBOOK

FOUNDATION COURSE FOR LOCAL CREDIT IN ROMANIA

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Session 1
Getting Involved in Municipal Credit

Think about entering into the muni1cipal credit market, what you imagine it will be like or what your experience has been so far. What thoughts and feelings do you have about entering this process?

Session 1
Framework for Training in Municipal Credit

Understanding Borrowing

1. What is borrowing and how does it work?
   - Basic calculations in financing (estimating loan payments)
   - Legal framework -- how the new laws create opportunity and responsibility
   - Alternative means of borrowing (project finance, general obligation)
   - External and internal sources -- capital markets and international investors

2. Why should I borrow?
   - Benefits
   - Risks

Preparing to Borrow

3. How do I determine how much I can borrow?
   - Financial analysis
   - Debt carrying capacity

4. How do I select what I borrow for?
   - Capital investment planning -- economic development over the long term
   - Choosing the right project -- criteria for prioritization of projects
   - Role of citizen participation -- how to inform and engage the citizens

5. How do I design a technically and financially sound project?
   - Feasibility studies
   - Role of engineering and financial consultants
   - Role of the local service provider

The Borrowing Process

6. How do I approach a lender?
   - Preparing a prospectus - presenting a sound project package
   - Developing a business plan
   - Choosing from among lenders

7. What does a financing deal look like?
   - Loan application process - steps involved
   - Laws to attend to at this stage

8. How do I negotiate a loan?
   - Protecting the interests of the city
   - Negotiating terms the city can live with
   - Facilities banks can and cannot offer

Post Borrowing

9. How do I communicate the loan to all stakeholders?

10. How do I monitor the loan?
    - Relationship with the local service provider
    - Compliance with terms and conditions
    - Project monitoring

11. How do I ensure that I will have the continuing capacity to meet loan repayment obligations?
    - Preparing a multi-year financial strategy
    - Financial policies - what they are, how they can help me

Session 1
Course Goals

- ✧ Provide an overall understanding of borrowing including the benefits and risks.
- ✧ Review the key steps in preparing to borrow-- determining how much you can afford to borrow and how to choose the right project.
- ✧ Discuss how to arrange for credit financing with a lender.
- ✧ Determine what is required after the loan is secured.
- ✧ Develop a plan to continue learning about local credit and to apply what you have learned.

Session 1
Schedule

Day One	Day Two	Day Three
11:00 am Open/Welcome Getting Started Activity Overview of Credit Financing Framework Course Objectives Agenda Guidelines for Working Together	8:30 am Open/Agenda Session 3: Preparing to Borrow Debt Carrying Analysis Capital Investment Planning	Session 5: Post Borrowing Communicating about the Loan Monitoring the Loan Terms and Conditions
Lunch	Lunch	Lunch
Session 2: Understanding Borrowing Case Study Work	Session 4: The Borrowing Process Presenting to a Bank Negotiating a Loan	Session 6: Lessons Learned and Application Planning

Session 2
The Enabling Environment

In your small group, discuss the benefits and limits of each of the following laws:

- Law on Local Public Finance
- Patrimony Law
- Law on Concessions

Make some notes so you can be prepared to share what you have discussed with the full group in 15 minutes.

Session 2
Case Study: Part One

Read the case study, and record your responses to the questions at the end.

The municipality of Raisa is an industrial town, located in the Northeast with a population of 75,000. The local council has worked hard to ensure adequate services to its residents in the midst of a rapidly deteriorating infrastructure, focusing initially on road maintenance and urgent repairs to the water treatment plant.

The mayor of Raisa, Dmitri Suvitch, has developed a close working relationship with the Water Regia, and its General Manager, Philip Ionescu. Together they have great visions for the future of Raisa and for improving the quality of life for its residents. The Finance Director for the city, Mrs. Cristiana Calin, and the Technical Director, Victor Nicolescu, have been working with the local council to establish a development agenda for the municipality. They are frustrated by what they perceive to be reactive decisions, taken in the moment, rather than a focus on a long term strategy.

In addition to pressing infrastructure needs, the city is facing other budgetary pressures. The amount of revenues from local taxes and its share of wage taxes is uncertain. It also has yearly expenditures for education, social assistance, and housing that must be funded. There are also a range of infrastructure needs. The water distribution system is aging. Roads are in bad shape and are in need of more than minor maintenance. The city also needs a new landfill for its solid waste. The wastewater system also needs upgrading.

At this moment, the Town Council is meeting and its agenda this week includes a presentation from Mr. Ionescu of the Water Regia. He is asking the city to support a proposal to get financing for an upgrade in the wastewater system in Raisa. He makes some compelling arguments to support his proposal "The Regia has the technical capability to provide efficient wastewater service to the citizens of Raisa, but we are limited by the aging collection system and our treatment plant which has only the capacity to treat 50% of our waste. If we can upgrade our system, we will be able to increase the number of people we can serve and the volume of wastewater the system can treat. We will also be able to stop discharging raw sewage into the river and improve our water pollution problem. Our proposal is that the local council take out a loan so we can get the resources needed to make improvements for the citizens of Raisa."

The Council voted on the Regia proposal and agreed, in principal, to support the wastewater system upgrade and move to the next step in the process.

Analysis questions:

Why did the city make a yes decision?

What more did they need to know in order to come to a more informed decision?

Session 2
Credit Financing Considerations

Key Points

Notes

✓Has a cost - interest on the money used

✓Scarce resource -- the law says the repayment on all your outstanding loans cannot be greater than 20% of your current revenues

✓Long term commitment

✓First and most important decision is that you need and want to borrow - not automatically given

✓Given it's costly and limited, need to make careful and good decisions about whether and how much to borrow.

Session 2
Reasons to Borrow

Key Points | **Notes**

You borrow to finance investments. You do not borrow to pay for current expenditures. For example, you borrow to pay for a new water treatment plant or new trams. You do not borrow to pay for the staff of your local or county council.

You borrow to finance investments that provide tangible benefits that are important to your community. For example, you borrow to pay for the expansion of the water system serving your community. You do not borrow to pay for land that has no immediate use.

You borrow when the useful life of the investment exceeds the term of the loan, that is, when you will still receive benefits from the investment after you have finished paying off the loan. For example, you can agree to a repay a loan over five years to pay for a new heating plant that will operate for fifteen years. You do not agree to repay a loan over ten years to pay for equipment that you will have to replace after five years.

You borrow when your debt service on all outstanding loans is 20 percent or less of your current revenues, as required by the Law on Local Public Finances.

You borrow in the international markets only after obtaining prior approval from the special commission created by the Law on Local Public Finances.

Session 2
Reasons Not to Borrow

Regarding the needs of your community, you should not borrow if:

Notes

✓ you have not ranked all pending investments according to their importance to your community

✓ you are not sure that you will be able to finance other investments that are more important to your community

✓ you have not determined that the investment is the least costly option available to address an outstanding need or problem in your community

Regarding the loan itself, you should not borrow if:

✓ you have not explored the use of less expensive means of financing the investment

✓ you do not know if the project itself can generate revenues to repay all or part of the cost of the investment

✓ you do not know your debt carrying capacity

✓ you do not know or do not understand all the terms of the loan

Session 2
Lessons Learned I
Making Borrowing Decisions

What do you want to pay more attention to in future discussions about borrowing decisions?

Session 3
Debt Carrying Capacity

Looking at your financial information

Currently, local and judets councils present the overall financial results in the format shown in Table 1. It first lists all the sources of funds, then all the expenditures, arranged by key sectors or chapters. As we will see below, this presentation does not provide the information that local officials need to determine their debt carrying capacity. Fortunately, all the information they will need is available to them. They simply need to rearrange the data as shown in Table 2.

The key differences between the two tables are as follows:

✓ In Table 2 the revenues have been separated into three groups labeled ***current revenues***, ***other sources of financing for current expenditures*** and ***other sources of financing for capital expenditures***. As you can see in the sheet called definitions, these three groups include all the sources of funds available to local and judet councils at this time.

✓ In Table 2 expenditures have been separated into two groups labeled ***operating*** and ***capital expenditures***. It is quite easy to construct these two groups using data as presented in Annex 14 of the annual financial statements.

✓ There are two new partial results in Table 2 labeled ***operating surplus (deficit) before debt service*** and ***net operating surplus (deficit)***. The overall surplus (deficit), as currently shown, remains at the bottom of the table.

The numbers in Tables 1 and 2 are the same, only organized differently. For example

	Table 1 1994		Table 2 1994
		Other Sources of financing for capital expenditures	
State Subsidies	114,078	- From other sources	114,078
Shared national tax revenues	2,841,836	Shared national tax revenues	2,841,836

		Local taxes and fees	1,167,342
		Other sources - operating	647,347
		Other sources capital - own	688,074
Own Revenues	2,502,763	Total	2,502,763

With the data as shown in Table 2, you are now ready to estimate your debt carrying capacity.

How do you determine the debt carrying capacity of our local or judet council?

Key Concepts

- Annual debt service
- Recurring or current revenues
- Debt service ratio
- Current expenditures
- Operating or current surplus (deficit)
- Operating or current surplus ratio
- Debt carrying capacity

A typical loan contract will require that you make periodic payments of principal and interest until you have repaid the full amount you borrowed. Since you budget on a yearly basis, you will be most interested in the sum of all the payments you must make each year. This is the ***annual debt service***. How much you pay each year will depend on the terms included in the loan contract. Among the most important terms are the time you have to repay the loan and the interest rate.

The example in Table 3 illustrates the concept of ***annual debt service***.

Amount of the loan in thousands of lei - 7,500,000 Years to pay - 3 Interest rate - 50%

	Year 1	Year 2	Year 3	Total
Annual debt service	5,328,947	5,328,947	5,328,947	15,986,842
Of which you will pay in:				
Principal	1,578,947	2,368,421	3,552,632	7,500,000
Interest	3,750,000	2,960,526	1,776,315	8,486,842

Note that the annual debt service remains the same in each of the three years. This is typically the case. Note also that the amount you pay in principal goes up each year. The reverse is true for interest payments because each year you are paying interest only on the portion of the loan that you still owe. Finally, note that the total interest payments after three years are greater than the amount you borrowed. This will not always be true. Generally, the higher the interest rate and longer the time to repay the loan, the more you will pay in interest. As you can see, borrowing can be costly.

When you sign a loan contract you agree to make annual debt service payments over several years. You will need to make sure that you have the funds each year to make these payments. The safest and most prudent approach is to rely only on those funds that you know will be available. In Romania today (in 1999) these include the funds you obtain from local taxes, shared wage taxes and the equalization grants provided from the State budget. These are your ***recurring or current revenues***, as shown in Table 2.

Note:

Other sources of financing for ***operating*** and ***capital expenditures*** include those funds that may or may not be available to you in a given year. For example, the local regia may not always show a profit in which you would share. Or, you may not sell local property or obtain a loan in every year. Excluding these from the calculation of your debt carrying capacity is a sound and prudent financial practice. This does not mean, however, that you may not rely on these to tide you over a difficult period when there is an unusual or unexpected decrease in revenues or increase in expenditures.

The ***debt service ratio*** is simply the annual debt service divided by total current revenues, as shown in the following formula:

debt service ratio = annual debt service ÷ total current revenues

You can express the result as a percentage.

The following example taken from Tables 2 and 3 illustrates the concept of ***debt service ratio***.

	1998
Local taxes	28,104,945
Shared wage taxes	18,905,190
State Operating Subsidies	18,584,025

A	Total Current Revenues	65,594,159
B	Annual debt service	5,328,947
B/A	***Debt service ratio***	8.1%

Did you know that the Law on Local Public Finance limits your debt service ratio to 20%?[1]

Remember that you should plan to pay the annual debt service from your recurring or current revenues. These are the same revenues that pay for the services that you provide to your community, such as maintenance of streets, schools and parks. These also are the revenues you use to pay your own administrative costs, such as the salaries of your employees. These are your ***operating expenditures***, as shown in Table 2. In effect you pay the annual debt service from the surplus of recurring or current revenues over operating expenditures. This is the ***operating surplus***. The ***ratio of operating surplus (deficit) to current revenues*** is simply the operating surplus divided by total current revenues, as shown in the following formula:

operating surplus ratio = operating surplus ÷ total current revenues

You can express the result as a percentage.

The following example taken from Table 2 illustrates the concepts of ***operating surplus*** and of the ***ratio of operating surplus (deficit) to current revenues***.

		1998
A	Total Current Revenues	65,594,159
B	Total Operating Expenditures	65,348,391
B - A	***Operating Surplus (Deficit)***	***245,768***
B/A	***Operating Surplus (Deficit) ratio***	***0.4%***

[1] Law 189/98 Article 51 (1)

Note: If you have an operating deficit you may want to defer any decision to borrow until you have analyzed the causes. An operating deficit shows that you cannot pay for the services you provide to your community with recurring or current revenues. If this persists for more than one year, you may be facing serious financial problems at some point in the near future. You should understand and address the causes of the deficit before entering into a loan. This will require measures to increase your current revenues, decrease your operating expenditures or some combination of the two.

In its simplest expression, the ***debt carrying capacity*** of the local or judet council is determined by how much you can set aside from your recurring revenues each year over the next several years in order to make annual debt service payments. Since any projection is uncertain, you want to plan your borrowing so that the annual debt service is less than the projected operating surplus over the life of the loan. That is, the planned or expected debt service ratio should be less than the planned or projected ratio of operating surplus to current revenues.

Note that the debt carrying capacity is defined by how much the local or judet council can pay annually. It is not defined as the maximum amount you can borrow. The reason for this is that usually you will not know in advance the terms at which you can obtain financing. As you know from the example in Table 3, the years you have to repay the loan and the interest rate are some of the factors that determine what part of the annual debt service is for payment of principal and what part for interest. As you enter into specific loans, the terms of those loans will determine your annual debt service. As long as the debt service as a percent of recurring revenues is within the limits you have set for yourself in conformance with existing legislation, you can continue to seek additional credit financing. It is only when the total debt service on all your outstanding loans reaches the limit that you will know for sure the actual amount you were able to borrow.

What factors affect my debt carrying capacity?

The key factors are:

✓ Your willingness and ability to limit funding for services for your community so that you can pay for investments and for credit to finance those investments

✓ Your willingness and ability to accept risk

There is no simple mathematical formula that will calculate your debt carrying capacity. There are quantitative methods that can help you in the process. However, eventually you will have to make difficult choices that depend largely on your judgement. These choices always will be present when you make a decision about a loan. It is important to make sure you are aware of the choices and agree with the decisions before proceeding with any loan.

Does my debt carrying capacity determine how much we can afford to invest in our community?

Not necessarily. The debt carrying capacity tells you how much your local or judet council can borrow to pay for investments while relying exclusively on its own revenues. Often, it will be the case that one or more of the projects you have in mind will generate their own revenues once they have been completed. This is the case, for example, of a water system. Once it has been completed, the consumers will pay a fee for the water they consume. The income from these fees paid by the consumers also can be used to pay the debt service on a loan. This loan would provide additional funding to pay for investments. In this case, the borrower would be the *regia* or company that will implement the project.

> ***A note of caution***: If the local or judet council is not the borrower, it might seem that this does not affect your debt carrying capacity. However, the lender or an investor may ask the local or judet council to guarantee the loan provided to the company or regia that will implement the project and be the actual borrower. This guarantee will reduce your debt carrying capacity in one of several ways. Lenders will take the guarantee into account when they decide how much they think you can afford to borrow to finance other investments. Also, if the borrower fails to pay and your guarantee becomes effective, this will count against the 20% limit established by law.

The ability of a specific investment project to generate its own revenues to pay for debt service on a loan is determined by an analysis of the ***financial feasibility*** of the project. This type of analysis should be completed as part of the process of preparing the capital investment plan, as discussed in the second part of this session.

Session 3
Case Study: Part Two
Debt Carrying Capacity

The local council has asked Mayor Suvitch to determine if the city can afford the loan. Mayor Suvitch has asked Christiana Calin, the finance director to help in making this determination. Christiana decides to consider three scenarios, each with different assumptions.

Tables 4, 5 and 6 illustrate one way for Raisa to analyze its debt carrying capacity. These are three scenarios of the finances of Raisa as they might develop over the next three years. They were prepared in 1998 by the city to evaluate its debt carrying capacity in the period from 1999 to 2001. Based on the analysis, the city decided to go ahead with the planned loan. The three scenarios all assume the city would borrow 7,500,000,000 lei in 1999, with the debt service to begin in 2000. The difference in the scenarios is in the assumptions regarding the future of an existing state enterprise that is the major tax payer and employer in the community. This will have a big impact on current revenues, which in turn affects future operating and capital expenditures.

The following table summarizes the assumptions made for each scenario.

Scenario A	The state enterprise is privatized and restructured successfully. Activity and employment at the plant grows, adding to local taxes and to the share of wage taxes.
Scenario B	The state enterprise is privatized but there are delays in the restructuring which stall the growth in activity at the plant and lead to some loss in jobs. Both local taxes and the share of wage taxes stagnate.
Scenario C	The privatization fails to materialize. The state enterprise receives a limited credit from the Government that keeps it open. Economic activity at the plant is greatly reduced. A large number of current workers are let go. This reduces revenues from local taxes and the share of wage taxes dramatically. Because of the financial distress the city qualifies for equalization grants, but these fail to make up for lost revenues.

Analysis questions:

Look at Tables 4, 5, and 6 that represent three different scenarios.

What is the operating surplus for each scenario for 1999-2001?

Calculate the debt service ratio for each scenario. (As a percentage)

What is the relationship between the operating surplus and debt service ratio?

What measures has the city taken under each scenario to maintain its ability to borrow?

What risks does the city face in each scenario?

Table 1
Current Version
Statement of Income and Expenditures

	1994	1995	1996	1997	1998
TOTAL REVENUES	5,458,677	15,128,624	27,217,531	62,286,920	75,519,015
Own Revenues	2,502,763	8,595,382	10,733,176	17,381,612	32,700,300
Shared National Tax Revenues	2,841,836	6,097,192	9,643,488	21,458,505	18,905,190
State Subsidies	114,078	436,050	6,840,867	23,446,803	23,913,525
Donations	0	0	0	0	0
Loan Proceeds	0	0	0	0	0
TOTAL EXPENDITURES	5,352,311	15,113,410	26,927,600	62,214,114	74,937,615
Of which:					
- *General Administration*	263,891	657,360	1,182,933	2,991,638	5,478,726
- *Education*	0	2,326,357	3,550,050	6,665,223	10,465,200
- *Health*	2,726,494	4,015,148	6,142,711	10,776,733	996,132
- *Culture & Sports*	0	24,322	15,392	12,209	41,667
- *Social Assistance*	394,375	730,090	985,352	1,885,178	3,099,831
- *Public Works & Housing*	1,953,163	7,240,199	13,682,272	36,200,953	52,148,673
- *Transportation & Communication*	14,083	116,498	1,276,412	3,624,060	2,688,006
- *Other Economic Activities*	0	0	0	0	0
- *Other Activities*	305	3,435	92,478	58,120	19,380
Set Aside for Reserves	53,184	7,607	289,931	72,806	581,400
Loan Payments (Interest/Principal)	0	0	0	0	0
Surplus (Deficit)	53,183	7,608	0	0	0
Distribution of Surplus	53,183	7,608	0	0	0

Table 2
Modified Version
Statement of Income and Expenditures

	1994	1995	1996	1997	1998
Current Revenues Total	4,009,177	13,404,320	24,265,947	56,221,661	65,594,159
Of which:					
- Local Taxes and Fees	1,167,342	7,307,128	9,209,250	15,189,356	28,104,945
- Shared National Tax Revenues	2,841,836	6,097,192	9,643,488	21,458,505	18,905,190
- State Operating Subsidies	0	0	5,413,209	19,573,800	18,584,025
- Equalization grant (new law)					
Operating Expenditures Total	5,218,853	11,952,238	24,007,793	55,506,142	65,348,391
Of which:					
- General Administration	263,891	535,843	1,105,413	2,701,249	5,211,282
- Education	0	2,326,357	3,550,050	6,665,223	10,465,200
- Health	2,726,494	4,015,148	6,142,711	10,776,733	996,132
- Culture & Sports	0	24,322	15,392	12,209	41,667
- Social Assistance	394,375	720,530	985,352	1,885,178	3,099,831
- Public Works & Housing	1,833,788	4,327,571	11,112,047	30,117,655	42,832,707
- Transportation & Communication	0	0	1,004,350	3,333,360	2,688,006
- Other Economic Activities	0	0	0	0	0
- Other Activities	305	2,466	92,478	14,535	13,566
Operating Surplus (Deficit) - Before Debt Service	(1,209,675)	1,452,082	258,154	715,519	245,768
Net Operating Surplus as a percent of total current revenues	-30 2%	10.8%	1.1%	1 3%	0.4%
Total Debt Service	0	0	0	0	0
Interest Payments Current Debt	0	0	0	0	0
Principal Payments	0	0	0	0	0
Other Sources of Financing for Current Expenditures	647,347	468,338	694,822	1,450,117	3,858,237
Of which:					
- Varioius Local Extraordinary Income	647,347	468,338	694,822	1,450,117	3,858,237
Net Operating Surplus (Deficit)	(562,328)	1,920,420	952,977	2,165,637	4,104,006
Other Sources of Financing for Capital Expenditures	802,153	1,255,965	2,256,761	4,615,142	6,066,618
Of which:					
- From Own Sources	688,074	819,915	829,104	742,139	737,118
- From Other Sources	114,078	436,050	1,427,658	3,873,003	5,329,500
Total Funds Available for Investments	239,825	3,176,386	3,209,738	6,780,778	10,170,624
Capital Expenditures Total by Chapter	133,458	3,161,172	2,919,807	6,707,972	9,589,224
- General Administration	0	121,516	77,520	290,389	267,444
- Education	0	0	0	0	0
- Health	0	0	0	0	0
- Culture & Sports	0	0	0	0	0
- Social Assistance	0	9,560	0	0	0
- Public Works & Housing	119,375	2,912,628	2,570,225	6,083,299	9,315,966
- Transportation & Communication	14,083	116,498	272,062	290,700	0
- Other Economic Activities	0	0	0	0	0
- Other Investmens	0	969	0	43,585	5,814
Overall Surplus (Deficit)	106,366	15,214	289,931	72,806	581,400
Set Aside for Reserves	53,184	7,607	289,931	72,806	581,400
Distribution of Surplus to Others	53,183	7,608	0	0	0
Total Other Payments	106,366	15,214	289,931	72,806	581,400
Net Transfer To (From) Accumulated Surplus	0	0	0	0	0

Table 3
Debt Service Schedule

Loan Terms

Amount	7,500,000
Interest rate	50%
Term	3

Debt Service Schedule

	Year 1	Year 2	Year 3	Total
Principal	1,578,947	2,368,421	3,552,632	7,500,000
Interest	3,750,000	2,960,526	1,776,316	8,486,842
Total	5,328,947	5,328,947	5,328,947	15,986,842
Balance	5,921,053	3,552,632	0	

Table 4
Scenario A

	1998	1999	2000	2001	2002
Current Revenues Total	65,594,159	86,046,600	101,055,777	110,590,842	121,415,584
Of which:					
- Local Taxes and Fees	28,104,945	42,157,417	56,069,365	64,479,770	74,151,735
- Shared National Tax Revenues	18,905,190	43,889,183	44,986,412	46,111,072	47,263,849
- State Operating Subsidies	18,584,025	n/a	n/a	n/a	n/a
- Equalization grant (new law)					
Operating Expenditures Total	65,348,391	74,674,992	90,791,797	103,275,117	117,725,670
Of which:					
- General Administration	5,211,282	5,732,410	6,305,651	6,936,216	7,629,838
- Education	10,465,200	12,034,980	13,840,227	15,916,261	18,303,700
- Health	996,132	896,519	806,867	726,180	653,562
- Culture & Sports	41,667	42,709	43,136	44,214	45,320
- Social Assistance	3,099,831	3,874,789	4,843,486	6,054,357	7,567,947
- Public Works & Housing	42,832,707	49,257,613	56,646,255	65,143,193	74,914,672
- Transportation & Communication	2,688,006	2,822,406	2,963,527	3,111,703	3,267,288
- Other Economic Activities	0	0	0	0	0
- Other Activities	13,566	13,566	13,702	14,044	14,395
Operating Surplus (Deficit) - Before debt service		11,371,608	10,263,979	7,315,725	3,689,915
Operating Surplus before debt service as a percent of total current revenues		13 2%	10 2%	6 6%	3.0%
Total Debt Service	0	0	5,328,947	5,328,947	5,328,947
Of which:					
Interest Payments Projected New Debt	0	0	3,750,000	2,960,526	1,776,316
Principal Repayments Projected New Debt	0	0	1,578,947	2,368,421	3,552,632
Net Operating Surplus (Deficit)	4,104,006	11,371,608	4,935,032	1,986,778	(1,639,033)
Other Sources of Financing for Capital Expenditures	6,066,618	5,000,000	2,500,000	0	0
Of which:					
- From projected new loan		5,000,000	2,500,000	0	0
Total Funds Available for Investments	10,170,624	16,371,608	7,435,032	1,986,778	(1,639,033)
Capital Expenditures Total by Chapter	9,589,224	11,500,000	7,000,000	1,500,000	0
- General Administration	267,444	0	0	0	0
- Education	0	0	0	0	0
- Health	0	0	0	0	0
- Culture & Sports	0	0	0	0	0
- Social Assistance	0	0	0	0	0
- Public Works & Housing	9,315,966	12,500,000	10,000,000	7,500,000	7,500,000
- Transportation & Communication	0	0	0	0	0
- Other Economic Activities	0	0	0	0	0
- Other Investmens	5,814	0	0	0	0
Overall Surplus (Deficit)	581,400	4,871,608	435,032	486,778	(1,639,033)

Table 5
Scenario B

	1998	1999	2000	2001
Current Revenues Total	65,594,159	71,593,218	74,684,762	75,941,714
Of which:				
- *Local Taxes and Fees*	28,104,945	30,915,439	34,006,983	34,857,158
- *Shared National Tax Revenues*	18,905,190	40,677,779	40,677,779	41,084,557
- *State Operating Subsidies*	18,584,025	n/a	n/a	n/a
- *Equalization grant (new law)*				
Operating Expenditures Total	65,348,391	65,542,143	68,857,932	70,080,874
Of which:				
- *General Administration*	5,211,282	5,341,564	5,394,980	5,529,854
- *Education*	10,465,200	10,569,852	10,675,551	11,209,328
- *Health*	996,132	896,519	806,867	726,180
- *Culture & Sports*	41,667	42,084	42,505	43,567
- *Social Assistance*	3,099,831	3,130,829	3,162,138	3,320,244
- *Public Works & Housing*	42,832,707	42,832,707	40,691,072	41,097,982
- *Transportation & Communication*	2,688,006	2,714,886	2,742,035	2,810,586
- *Other Economic Activities*	0	0	0	0
- *Other Activities*	13,566	13,702	13,839	14,185
Operating Surplus (Deficit) - Before debt service		6,051,076	5,826,830	5,860,840
Operating Surplus before debt service as a percent of total current revenues		8 5%	7.8%	7 7%
Total Debt Service	0	0	5,328,947	5,328,947
Of which:				
Interest Payments Projected New Debt	0	0	3,750,000	2,960,526
Principal Repayments Projected New Debt	0	0	1,578,947	2,368,421
Net Operating Surplus (Deficit)	4,104,006	6,051,076	497,883	531,893
Other Sources of Financing for Capital Expenditures	6,066,618	5,000,000	2,500,000	0
Of which:				
- From projected new loan		5,000,000	2,500,000	0
Total Funds Available for Investments	10,170,624	11,051,076	2,997,883	531,893
Capital Expenditures Total by Chapter	9,589,224	10,000,000	2,500,000	500,000
- *General Administration*	267,444	0	0	0
- *Education*	0	0	0	0
- *Health*	0	0	0	0
- *Culture & Sports*	0	0	0	0
- *Social Assistance*	0	0	0	0
- *Public Works & Housing*	9,315,966	10,000,000	2,500,000	500,000
- *Transportation & Communication*	0	0	0	0
- *Other Economic Activities*	0	0	0	0
- *Other Investmens*	5,814	0	0	0
Overall Surplus (Deficit)	581,400	1,051,076	497,883	31,893

Table 6
Scenario C

	1998	1999	2000	2001
Current Revenues Total	65,594,159	63,421,604	58,448,687	51,296,910
Of which:				
- *Local Taxes and Fees*	28,104,945	28,807,568	23,046,055	17,284,541
- *Shared National Tax Revenues*	18,905,190	32,114,036	28,902,632	26,012,369
- *State Operating Subsidies*	18,584,025	n/a	n/a	n/a
- *Equalization grant (new law)*	n/a	2,500,000	6,500,000	8,000,000
Operating Expenditures Total	65,348,391	62,196,098	52,476,931	45,654,062
Of which:				
- *General Administration*	5,211,282	5,263,395	5,316,029	5,369,189
- *Education*	10,465,200	8,895,420	6,671,565	6,838,354
- *Health*	996,132	498,066	298,840	179,304
- *Culture & Sports*	41,667	42,084	42,505	43,567
- *Social Assistance*	3,099,831	2,634,856	2,239,628	1,903,684
- *Public Works & Housing*	42,832,707	42,832,707	31,053,713	24,842,970
- *Transportation & Communication*	2,688,006	2,016,005	1,512,003	1,134,003
- *Other Economic Activities*	0	0	0	0
- *Other Activities*	13,566	13,566	13,702	14,044
Operating Surplus (Deficit) - Before debt service		1,225,506	5,971,756	5,642,848
Operating Surplus before debt service as a percent of total current revenues		1.9%	10.2%	11.0%
Total Debt Service	0	0	5,328,947	5,328,947
Of which:				
Interest Payments Projected New Debt	0	0	3,750,000	2,960,526
Principal Repayments Projected New Debt	0	0	1,578,947	2,368,421
Net Operating Surplus (Deficit)	4,104,006	1,225,506	642,809	313,901
Other Sources of Financing for Capital Expenditures	6,066,618	5,000,000	2,500,000	0
Of which:				
- From projected new loan		5,000,000	2,500,000	0
Total Funds Available for Investments	10,170,624	6,225,506	3,142,809	313,901
Capital Expenditures Total by Chapter	9,589,224	6,225,000	3,050,000	225,000
- *General Administration*	267,444	0	0	0
- *Education*	0	0	0	0
- *Health*	0	0	0	0
- *Culture & Sports*	0	0	0	0
- *Social Assistance*	0	0	0	0
- *Public Works & Housing*	9,315,966	6,225,000	3,050,000	225,000
- *Transportation & Communication*	0	0	0	0
- *Other Economic Activities*	0	0	0	0
- *Other Investmens*	5,814	0	0	0
Overall Surplus (Deficit)	581,400	506	92,809	88,901

Definitions

Code	1996 Category/Sub Category
	Current Revenues
	of which:
	Local Taxes and Fees
	Shared National Salary Tax Revenues
	State Operating Subsidies
	Equalization Grant - New Law
	Local Taxes and Fees
	of which:
01.02.	Taxes on Profits of Regii
03.02.	Taxes and Fees on Individuals
04.02.	Fees for Use of State Property
05.02.	Corporate Property Tax
06.02.	Corporate Vehicle Fees
07.02.	Tax on Revenues from Agriculture
08.02.	Other Direct Taxes
15.02.	Entertainment Fees
17.02.	Other Indirect Taxes
21.02.06	Driving Exam & License Fees
	Tax on Personal Income, other than from wages (1998>)
	Shared National Tax Revenues
	of which:
34.02.	Shared National Salary Tax Revenues
	State Operating Subsidies
	of which:
37.02.01	Subsidies for Socal Assistance, Heating & Public Transport
	Other Sources of Financing
	of which:
	Other Sources of Financing for Operating Expenditures
	Own Sources of Financing for Capital Expenditures
	External Sources of Financing for Capital Expenditures
	Other Sources of Financing for Operating Expenditures
	of which:
20.02.	Distribution from Profits of Regii
21.02.	Revenues from Public Institutions
22.02.	Other Various Revenues
40.02.	Donations
Minus	
21.02.06	Driving Exam and License Fees
	Own Sources of Financing for Capital Expenditures
	of which:
30.02.	Proceeds from the Sale of Public Property & Housing
45.02.	Proceeds of Short-term Loans
	External Sources of Financing for Capital Expenditures
	of which:
37.02.02	State Capital Investment Subsidies
37.02.03	Capital Investment Subsidies from External Loans
46.02.	Proceeds of Loans from Revolving Funds

Session 3
Capital Investment Planning

Key Points

Notes

Provides a comprehensive view of your needs and possibilities: A basic function of the CIP is to bring together both representatives from City Hall and the *Regia* to plan and budget for all your capital investment needs. Together, they can consider what to buy, what to build, what to repair, when to build or repair and how to finance these costs.

Serves as a financial management tool: A key concern in developing the CIP is to prioritize current and future needs to fit within the financial constraints of the local government. Capital investment planning considers not only what a community needs but, equally important, what it can afford. Developing a CIP is very different than developing a "wish list" of projects that cannot be fully implemented. The CIP puts you in control of all your investment decisions.

Serves as a Reporting Document: The document that is produced following the CIP process provides a clear description of the proposed projects that will be undertaken over the course of the planning period. This document communicates to citizens, businesses and other interested parties the local government's capital priorities and plans for carrying out projects. The community has a better understanding of the government's plan for capital spending and can make more informed decisions.

Advantages:

✓A CIP focuses attention a local government's goals, needs and financial capability considering all possible sources of financing.

✓A CIP builds broad scale public awareness of the need for effective local planning

✓A CIP improves cooperation and communication between City Hall and the *Regia*.

✓A CIP can help local governments avoid costly infrastructure mistakes.

✓A CIP helps local governments enhance their financial stability.

Session 3
Case Study: Part Three

Read the next part of the case study and answer the questions at the end.

Since the vote to support the Regia's wastewater system improvement project, the Raisa Council members have been curious about what's involved in moving the project forward. A couple of the members privately wondered if they had made the right decision. They want the wastewater system improved but are asking if this is this the right way to get it done. The next Council meeting had many residents coming to ask for road improvements. They were not happy that nothing could be done right away.

The Mayor has been receiving phone calls from various members asking questions that lead him to believe there is some doubt among the Council as to the wisdom of the decision to go ahead. Meanwhile, Philip Ionescu has been showing up daily in the Mayor's office, giving him updates on progress and lobbying hard for a financing decision. "We're ready to start," he says, "We've even got a lender all lined up to negotiate with us."

The mayor knows there are other needs. The municipality's infrastructure is deteriorating around him. The earlier decision by the Council to go ahead with the improvements to the wastewater system seems to have limited Raisa's ability to invest in other projects. The mayor wonders if there is any way to pay for the wastewater project and also for other important projects, such as the road improvements. He is hesitant to allow Mr. Ionescu to make any commitment with the possible lenders until he has a better sense of how to meet the needs of his community.

Analysis questions:

How would Capital Investment Planning help in this decision making process?

What are the potential implications of not doing CIP?

Who needs to be involved in this process?

Session 3
Steps In The CIP Process

Step 1. Establish the Organizational and Policy Framework
* Establish the CIP Organizational Structure
* Develop Programmatic Policies
* Develop Financial Policies

Step 2: Identify Possible Projects
* Review Status of Previously Approved Projects
* Identify and Develop Information for New Projects
* Examine Capital Project Alternatives

Step 3: Identify all potential sources of financing for investments
*Evaluate the debt carrying capacity of the local or judet council
*Perform an initial financial analysis for each project to see what part of the investment can be paid for with revenues generated by the projects themselves
* Identify other funding options

Step 4: Rank and Prioritize Projects
* Review Total Project Opportunities
* Prioritize Capital Projects
* Select and schedule projects and assign funding source(s) for each project

Step 5: Implement and Monitor the Capital Program
* Review Project Milestones and Costs
* Monitor External Environment
* Monitor the Planning Process

Session 3
Lessons Learned II
Preparing to Borrow

What have you learned about Debt Carrying Capacity?

What have you learned about Capital Investment Planning?

What do you plan to do when you return to your local or judet council with respect to Capital Investment Planning?

Session 4
Project Plan Development

❖Must conduct a technical feasibility study that looks at the final design, confirms that there are no technical design options that are less costly or more efficient, and considers how the choice of technical solutions affects the financial feasibility of the project

❖Must conduct a financial feasibility study that looks at what it will cost to build the project and to operate and maintain it, to what extent revenues generated by the project once completed can pay for all or part of the financing, operating and maintenance costs, what subsidies are required, if any, and whether all this is affordable

❖Use outside experts to get an impartial, objective analysis

❖Final document reviewed by technical and financial directors

Notes:

Session 4
Negotiating a Loan

Key steps:

1. Establish contact with one or more interested lenders or investors
2. Apply for the financing -- meet the requirements of the lender or investor
3. Receive one or more offers of financing
4. Evaluate the offer(s)
5. Select an offer and agree to the terms of the financing
6. Execute the contract(s) required to formalize the financing

Notes

Key points

✓Make sure to obtain in writing from the lender or investor all the terms and conditions of the proposed loan or investment, including the period of time during which the offer will remain valid. Make sure you have information on what contracts or other legal documents you will have to sign. Obtain complete written drafts of all documents well in advance so you have time to evaluate them.

✓Ask the lender or investor to explain any terms or conditions in their offer that you do not understand. Consider obtaining advice from experts outside your local or county council if you are not sure you understand or can evaluate the offer.

✓ Terms and conditions that you should be careful with:

- Fixed versus variable rates: Will the interest rate be fixed for the life of the loan or will it vary? If it will vary, how often will it change, how will the new interest rate be determined, will it be negotiable?

- Loans in *lei* versus loans in a foreign currency: In what currency will you have to repay the loan? It is extremely difficult to evaluate the cost and risks involved in a foreign currency loan.

- Other fees: What fees do you have to pay, if any, to whom and at what point? Fees can add significantly to the total cost of a loan.

- Disbursements: When will you receive the funds? What conditions, if any, must you meet before obtaining a disbursement? Are there any penalties if you do not follow an agreed upon disbursement schedule?

- Payment of interest and principal: When do you begin to owe interest on the funds? When do you have to begin repaying the principal? This becomes especially important if you will be financing the construction of a project over more than one year. It is especially important if you will be relying on revenues generated by the completed project to repay the loan.

Notes:

✓Comparison of offers can be complicated. If you succeeded in obtaining more than one offer of financing, the terms and conditions may differ from one offer to another. All the items listed above - fixed vs. variable rates, loans in different currencies, fees, schedule and conditions of disbursement, and so on - have a direct impact on the total cost to you of a particular offer of financing. If you are not sure how to evaluate such costs, obtain expert advice of your own.

✓If you are guaranteeing a loan, be sure to understand the extent of your liability. What is the trigger for the guarantee? That is, at what point do you become responsible for repaying the loan? What remedies do you have? What can you do to protect yourself from poor financial management by the original borrower? Will you have a clear right to obtain timely information on the financial condition of the borrower over the life of the loan? Can you take action before you are forced to assume responsibility for repaying the loan? At least some of these issues will be between you and the borrower. Sign a formal agreement or contract with the borrower that protects your financial interests. Make sure the lender is aware of this agreement and agrees to it as part of the terms and conditions of the loan.

✓Finally, terms usually are negotiable. Do not be afraid to ask for alternatives to particular terms you do not like or do not understand. Explore with the lender what guarantees you could offer that might improve the terms and conditions of the loan or investment. For example, in Romania today you can offer to guarantee the loan by pledging part of your revenues. In exchange for new or additional guarantees you should receive an offer of improved terms and conditions from the lender or investor.

Session Four
Case Study: Part Four

Read Part Four of the Case Study and answer the questions at the end.

When Raisa prepared its CIP it became evident that the Water Regia could afford to repay half the costs of the waste water project from future revenues once the project had been completed. This made it possible for the municipality to use part of its debt carrying capacity to borrow funds for some of the other priority projects, notably the road improvements that were so important to the members of the Council.

Raisa will borrow 7,500,000,000 directly from the banks to pay for half of the cost of the waste water system and other projects. The Water Regia will obtain a loan to pay for the other half of the costs of the waste water project. The Council supports this solution, and now they must prepare to enter the loan negotiation process.

The Water Regia has identified a bank to approach for a loan that they believe will be a favorable lender. Mr. Ionescu has a verbal offer from the bank manager for a loan but has been told that he must obtain a guarantee from the municipality. Raisa, in turn, has received an offer for a loan of 7,500,000,000 at 50 percent annual interest to be repaid in three years.

The mayor is a bit anxious about this stage of the borrowing process. He's heard that the bank is helpful but at the same time, hard but fair negotiators. At this point, the terms and conditions they have put forth are appealing but he is not sure how to evaluate the offers and what he should be negotiating with the two potential lenders. He also is wondering about the guarantee to the Water Regia.

What does the Mayor (and the council) have to do to prepare?

How do they get ready to both protect the city's interests and negotiate a fair loan?

Lessons Learned III
Preparing to Borrow
Session 4

What is important to prepare to borrow?

What are the key elements of this process that you want to pay attention to the next time you borrow?

Session 5
Monitoring The Loan

✓ *Whether you are the borrower or a guarantor, monitor very carefully the progress in time and cost of the project you are financing with the loan.* If there are strict conditions regarding the schedule of disbursements there may be penalties to pay for a delay in drawing down the funds. Once the borrower begins to pay interest on the funds, construction delays will be very costly. The revenues from the completed project may be required to repay the loan or investment. Delays, or worse yet, a failure to complete the project can have serious consequences. If final costs exceed the original estimates, do you have access to other funds to complete the project?

✓ *If you are the guarantor, be sure to monitor the performance of the borrower.* Are they in compliance with all the terms and conditions of the various contracts and agreements? Obtain complete and timely information from the borrower so that you can anticipate their ability to meet their future obligations to the lender or investor. If there appear to be problems, ask the borrower to take corrective actions in time to avoid triggering your guarantee.

✓ *Monitor the debt service schedule*

on all your loan portfolio carefully. For the current year, be aware of the dates when payments are due. Monitor the rest of your budget very carefully. Look for expenditures that are higher than expected or for revenues that are lower than expected. Will you have sufficient cash on hand? What will you do if your revenues from taxes or other sources are delayed or are less than you anticipated? Look forward to anticipate potential problems. If you have a variable interest loan, how likely is it that interest payments may increase? If you are paying in a foreign currency, how likely is that it may become more expensive for you to buy that currency? Have a contingency plan. Determine in advance what other expenditures you can defer if necessary. Consider getting a line of credit with the State Treasury or with a local bank. At least once a year, probably when you are preparing the budget for the next year, look three or four years into the future. Consider the same questions as above. Plan what you can do today to minimize future risk and to prepare contingencies for unanticipated problems.

Session 5
Case Study: Part Five

Read this part of the case study and answer the questions at the end.

The two loans have been approved! The Regia is now in the position to move forward with its wastewater upgrading project. The project plan calls for work to begin in three months. The first thing they will do is dig up the streets where the wastewater system will be improved and begin to make preparations for those areas in which they will be working. Overall, the project will take two years to complete. Major portions of the downtown area will likely be closed off for a several month period once construction has begun. Service will be intermittently interrupted as new pipes are laid and old ones replaced. These seem to be, from the Council's perspective, a small burden to bear for an wastewater system.

The Council is quite pleased with itself and the Regia with this accomplishment. Relations between Philip and Dmitri have never been better, and they have often been overheard referring to one another as "my business partner." The most recent council meeting involved a review of the terms and conditions of the loans. Also, the General Manager of the Regia made a presentation to the Council of the current and projected water and waste water tariffs and of his plans to improve collections. This report is part of the requirements in the revised contract between the municipality and the Regia negotiated as part of the loan guarantee. "This loan will ensure Raisa residents improved wastewater service at fair rates. The bank has given us fair terms. The Council can rest assured that we will manage this project well, and keep our commitments to you, the bank and the citizens of Raisa."

Session 5
Small Group Work on the Case Study

If your group is doing the *Communication Task*, answer the following questions:

Who needs to know about the financing and the project?

What do they want to know about that would be important to communicate to them?

If your group is working on the *Monitoring task*, answer the following questions:

What do you need to monitor?

How will you get the information you need to monitor effectively?

Session 5
Lessons Learned IV
Post-Borrowing

What have you learned about the post-borrowing phase?

Session 6
Summary of Lessons Learned from this workshop

Think about all of the topics we have covered in this workshop. What are the most important insights you have gained in the past three days about municipal credit? Make a list of all the things you have learned below:

Session 6
Planning for Application

Review your course notes, and consider the other in-depth training that will be available in each of the topic areas we have covered. Answer the following questions:

1. Given your lessons learned on the previous page, what do you want to be sure to do the next time you and your council are faced with a borrowing opportunity?

2. What additional training do you want/need to take in order to be more comfortable with all aspects of the borrowing process?

Session 6
Evaluation

Part I: Objectives

Please indicate the degree to which the workshop has achieved its objectives:

1. Provide an overall understanding of borrowing including the benefits and risks.

1	2	3	4
very little	somewhat	Well	very well

2. Review the key steps in preparing to borrow-- determining how much you can afford to borrow and how to choose the right project.

1	2	3	4
very little	somewhat	Well	very well

3. Discuss how to arrange for credit financing with a lender.

1	2	3	4
very little	somewhat	Well	very well

4. Determine what is required after the loan is secured.

1	2	3	4
very little	somewhat	Well	very well

5. Develop a plan to continue learning about local credit and to apply what you have learned.

1	2	3	4
very little	somewhat	Well	very well

Part II: Comments

1. What did you like best about the workshop?

2. What did you like least about the workshop?

3. How would you rate the effectiveness of the trainers?

1	2	3	4
poor	fair	good	excellent

Comments:

4. Please rate the logistics and administrative support.

1	2	3	4
poor	fair	good	excellent

Comments:

5. Please evaluate the effectiveness of the following training techniques

	poor	fair	good	excellent
participant workbook				
case study				
presentation				
small group exercises				
full group discussions				

Comments:

6. Do you have any suggestions on how we could improve the workshop?