

CHAPTER I

INTRODUCTION

1.1. Background of the Study

Decentralization is one of the most important tools to reduce poverty and inequality in both rural and urban sector. Furthermore, the local government should be more functional, for that, devolution of function to local government with more tax authority. The local government should be given a share of revenue generated from extraction of resources within their area (World Bank, 2000).

Decentralization, or decentralizing governance, refers to the restructuring or reorganization of authority so that there is a system of co-responsibility between institutions of governance at the central, regional and local levels according to the principle of subsidiary, thus increasing the overall quality and effectiveness of the system of governance, while increasing the authority and capacities of sub-national levels. Decentralization could also be expected to contribute to key elements of good governance, such as increasing people's opportunities for participation in economic, social and political decisions; assisting in developing people's capacities; and enhancing government responsiveness, transparency and accountability (UNDP, 1997).

It is also taken as a democratic process to make access of people to governance, rule, and resources. The decisions of higher levels, managerial and financial rights are transferred to local levels according to the abilities of local levels. Decentralization is also a way to increase to the effectiveness of services of government to the people. It is a process of empowering local people for enriching governing power. And it is also a way to increasing participation of local people in governance system in

accordance with equal treatment to every member of society. It is a medium of making public service easy, fast, economical, effective and efficient (Regmi, 2014).

Decentralization is a process of transferring of authority, recourses, rights and accountability from central level to the local level with clear vision to implement from local level.

Fiscal decentralization is understood as inter-governmental fiscal relations that study how different level of government act and interact with each other on fiscal issues with reference to their function and responsibilities... fiscal decentralization is a process of devolving fiscal decision-making power and management responsibilities to local level of government (Adhikari, 2006).

The main goal of fiscal decentralization is to move governance closer to the people and this does require strengthening local governance finances. It means local fiscal decentralization requires local government with some autonomy (Lamichhane, 2012).

The basic economic arguments in favor of fiscal decentralization rest on two assumption (1) that decentralization will increase economic efficiency as local governments are capable of providing better services due to proximately and in formational advantages, and (2) that competition and population mobility across local governments for the delivery of public services will ensure the right matching of preferences between local communities and local government (Tiebout, 1956).

Fiscal decentralization tends to be a relatively recent phenomenon in developed and developing countries. In these countries the two main reasons for the emergence of decentralization is either the failure in economic planning by central government and on changing international economic and political condition.

Argument in favor of fiscal decentralization originally centered around the work of

Tiebout (1956), Musgrove (1959) and Oates (1972) Claim it promotes higher efficiency, better public service, greater transparency and eventually economic growth. First it is often argued that decentralization increases economic efficiency because local governments are better positioned than the National government to deliver public services as a result of proximity and informational advantage.

The strongest argument in support of fiscal decentralization and federation rest on the allocation of quasi-national and non-national public goods. There is little, if any, economic justification to allocate non national public goods at the coordination by the central government may be desirable as states and localities supply certain quasi-national public goods... decentralization government is also advocated on the ground that state and local government allow the recognition of regional and local values rather than an across the board application of uniform standards on a national basis (Herber, 2004).

The fiscal independence has transferred to the local levels from higher level with legal basis is called fiscal decentralization. It is a system where local authority formulation it own fiscal policy, tax collects, utilize and spends revenue and as well manages public debts confirming within legal basis. Legal provisions, accountability, people participation, transparency and answerability are also kept in mind while practicing fiscal independence (Gyawaly, 2014).

Fiscal decentralization is also a better medium to increase economic capability and independence, politically it makes nearer government to people, to increase in participation, to make maximum utilization of public expenditure and effective way to mobilization of public revenues (LBFC, 2013).

It is fiscal freedom and independence which has given to local authority to actualize democratic process and practices.

Regmi (2014) says fiscal decentralization is mainly a concept of delivering a work function with clear responsibility, financial support and resources to fulfill those functions and responsibilities. As well it transfers the rights and authority to receive resource, to do financial decision and work responsibility to the local level. It can be understood in the following points; (1) To transfer responsibility with provision of expenditure, (2) Revenues rights, (3) Transference of intergovernmental finance and (4) Loan management.

Fiscal decentralization enhances the capability of local body, capitalizes financial resources, and it also reasonably maintains the local services and increases effectiveness of public services delivery and through participation of each and every member of local level, it makes access of people to government services and creates ownership among people to the government activities.

Fiscal decentralization, or devolving the revenue resource and expenditure functions to lower tiers of government, it is seen as part of a reform package to improve efficiency in the public sector, to increase composition among local governments in delivering the public service. By bringing the government closer to the people, fiscal decentralization is expected to boost public sector efficiency, as well as accountability and transparency in policy-making. It has become a clear trend in government reform in both developed and developing countries including Nepal (Devkota, 2013).

Local government is an important institution to mobilize the local resources. More and more local government units carry out new roles in mobilizing resources for development. Basically, local resource mobilization is the concern of fiscal issue determined by the degree of fiscal decentralization, a system of governance relating to fiscal power which focuses on how the local government generates the revenue

measured in monetary unit to meet the local level of expenditure incurred to provide services to the local people (Shrestha, 2009).

Nepal is located on the southern slopes of the Himalayas and bound by the two big countries of Asia - the people of republic of China & republic of India with an area of 147,181 square kilometers.

Nepal has followed a planned development system to improve the living conditions of its people since 1956. When it launched its first periodic plan of five year (1956-61). Thus so far, Nepal has implemented twelve periodic plans and the 13th is in the offing.

In the 4th plane (1970-75), the country was divided into five development regions with purpose of allocating the national budget and undertaking development programs in all regions. The other mechanism established by the government at the local level to associate and engage people in decision making process, especially in planning and development of the areas concerned. There were 36 municipalities before 2053; in 2053 Magh 21 by adding 15 municipalities, similarly 2053 Chaitra 4 declaring 7 municipalities, and total number of municipalities was 58. In 2071 Baisakh 25 government of Nepal added 72 municipalities, 2071 Mangsir 16, 61 municipalities and 2071 Ashoj 1 added 26 municipalities. Now the total numbers of municipalities are 217 (1 metropolitan, 12 sub-metropolitan and 204 municipalities). Remaining VDCs are 3157 and 75 DDCs such as altogether; there are 3449 local bodies (LBs) in the country. Since the beginning of the 1960s, the two-tire LBs have been involved in planning and development at the local level. Decentralization was adopted as the policy in the third plan period (1965-70) to associate and engage the people in the decision making process with specific reference to planning and development in the areas within the territorial boundary of the local body (LB).

After restoration of the multiparty democratic system in 1990, especially after 1999, LBs managed this responsibility per the Local Self Governance Act, 2055 (LSGA, 1999) and Local Self Governance Regulation, 2056 (LSGR, 1999), Local Body (Financial Administration) Regulations, 2007 as well as related rules and operational manuals (Dhungel, Sapkota, Hang & Regmi, 2011).

1.2. Statement of Problem

This paper tries to explore relationship between local resource mobilization and fiscal decentralization of municipalities in Nepal. Fiscal decentralization tends to be a recent phenomenon in transitional and developing countries in these countries the two main reasons for the emergence of decentralization are either the failure in economic planning by central government on the changing international economic and political condition in this circumstance decentralization has been sled as a means to achieve economic gains. There is relationship between fiscal decentralization and local resource mobilization. Fiscal decentralization promotes higher efficiency, better public services, greater transparency, economic growth often argued that decentralization increase economic efficiency because local government are better to central government. The study attempts to reach to the effect of fiscal decentralization on local resource mobilization. Local resource mobilization is the major issue; it's most non- debated topic after the fiscal decentralization.

The following are the preliminary research questions:

- i. How the local bodies generate revenue?
- ii. What is the pattern of income and expenditure of local entities in Nepal?

1.3. Rational of the Study

There are many researches and studies about the fiscal decentralization, economic growth and local resources mobilization from 3rd plan period (1965-70) but there is very less study about nexus between fiscal decentralization policy and local resource mobilization in Nepal. This study will analyze nexus between fiscal decentralization policy and local resource mobilization of municipalities in Nepal. This research has been carrying out to fill the information gap that accrues in the previous research. This study might be-useful for the researches; moreover this research will very much fruitful for the development studied, social workers, political leaders, other national international organization and stake holders, working in the field.

1.4. Objectives of the Study

This research has following objectives:

General objective is to examine Fiscal Decentralization Policy and Local Resource Mobilization Nexus in Nepal.

And, following are the specific objectives:

- i) To examine the revenue generation by the local bodies.
- ii) To analyze their income and expenditure pattern.

1.5. Limitations of the Study

This study is set for finding out nexus between fiscal decentralization policy and local resource mobilization in Nepal. It may have many shortcomings: financial, geographical, technical, statistical as well as time and resource limitations. The limitations are listed below:

- i. This paper is confined on nexus between fiscal decentralization policy and local resource mobilization of Nepal. No other magnitudes have taken into consideration.

- ii. The study is confined on the secondary data only.
- iii. This study is focusing on the especially case of Municipalities and only two municipalities are taken as sample municipalities.
- iv. This study is covering the secondary data relation fiscal decentralization of the period FY 2051/52 – 2070/71, only of 20 years.

1.6. Organization of the Study

This study has divided into 5 chapters. Prior to the body of the thesis several pages of preliminary materials such as title page, approval sheet, viva sheet, acknowledgements, table of contents, list of table, abbreviation used etc have been presented.

Chapter I: Introduction: The first chapter consists on introduction of the study, background of the study, statement of the problems, rational of the study, objectives of the study, limitation of the study.

Chapter II: Review of Literature: This chapter includes review of the literature. Review of literature will be taken into consideration through relevant books, articles, journals, reports and other concerned materials.

Chapter III: Research Methodology: This chapter deals on research design, nature and sources of data collection and processing techniques, analyze of tools.

Chapter IV: Presentation of Data, Analysis and Findings: This chapter encompasses presentation of data, analysis and findings.

Chapter V: Major Findings, Conclusion & Recommendations: This chapter covers summary and conclusion of the research. This chapter also encompasses recommendations made as per the findings of research and analysis.

CHAPTER II

REVIEW OF LITERATURE

2.1. Review of Literature

Fiscal decentralization is a new phenomenon in both developed and developing countries. It is especially in developing countries like Nepal. There is limited literature on fiscal decentralization and relationship between local resource mobilization and fiscal decentralization in Nepal. Due to limited literature and its availability in Nepalese context this study has also used the literature relating operational research and reports. This chapter seeks to make review of literature on the conceptual and theoretical framework of decentralization and fiscal decentralization; the historical perspective of local governance in Nepal and related to the subject in brief.

A. Conceptual and Theoretical Framework Global Context

Decentralization: Decentralization- the transfer of authority and responsibility for public function from the central government to intermediate and local government or quasi-independent government organizations and or private sector in a complex multifactor concept different types of decentralization should be distinguished because they have different characteristics policy implication and condition for success (World Bank, 1999) (Cited: Lamichhane, 2012).

Decentralization referred to as a transfer of authority and responsibility (service delivery and finance in order to become effective) of public functions from the Central Government to Local Government (LGs). Decentralization is a long term process that involves/needs mainly three components such as political decentralization, administrative decentralization and fiscal decentralization.

The case for decentralization government fiscal activity, and hence for federation rest on the following grounds: (1) The allocation of non-national goods., (2) Coordinating the allocation of certain quasi-national public goods., (3) Spatial mobility., (4) Allows the meeting of sub national preference where these may vary far from national preference., (5) Allows greater individual freedom and political responsibility (Herber, 2004).

If principal of decentralization translate into reality, establish of local authorities with clearly laid functions, duties and powers so that people could be able to participate in decision-process of those matters that affect their day-to-day lives.

Decentralization, the assignment of fiscal, political and administrative responsibilities to lower levels of government is occurring world-wide for different reasons at different paces and through different means. The ‘why’ of decentralization is as varied as the how the decentralization. The complexity inherent in the decentralization process is further aggravated by its cross cutting impact. The perfect combination of political, fiscal and administrative decentralization is very critical in designing decentralized government system (Subedi, 2014).

Subedi presented mainly four elements of decentralization: 1. Legal infrastructure and political commitment, 2. Fiscal resources and management, 3. Organizational capability and 4. Public Service /Satisfaction.

Decentralization essentially is a matter of the devolution of power, authority and responsibility (structurally politically, administratively and financially) from the center to the local level of government.

Fiscal Decentralization: Fiscal decentralization generally refers to the devolution of taxing and spending powers from the control of central government authorities to

government authorities either at sub-national levels (regional, provincial, municipal, etc). In a very decentralized system, local governments have considerable power to mobilize resources, through taxing authorities accompanied by strong tax bases (Boschmann, 2009).

Fiscal decentralization transfer power for revenue collection, resource mobilization and expenditure authority from central to local level government and promotes LBs strong.

Fiscal decentralization—who sets and collects what taxes, who makes what expenditures, and how any "vertical imbalance" is rectified—has been especially prominent in recent discussions in many countries, but as just indicated many of the more fundamental questions relate to political and administrative decentralization.

Political decentralization refers at one level to the extent to which political institutions map the multiplicity of citizen interests onto policy decisions (Inman and Rubinfeld, 1997). Administrative decentralization is concerned with how political institutions, once determined, turn policy decisions into allocative (and distributive) outcomes through both fiscal and regulatory actions. The political decision to devolve powers from central government, for example, can only get translated into actual powers being shifted if sub-national governments have the fiscal, political, and administrative capacity to manage this responsibility (Litvack, Ahmad, & Bird, 1999), (Cited:Working paper of UNDP,1999).

DDSMS and UNDP report of the 'United Nations in Global Forum on Innovative Policies and Practices in Local Governance' in 1996 stated that the basic characteristics of a system for decentralized financial management should include: (a) transparency of allocation (b) predictability of the amounts available to local institutions and (c) local autonomy of decision making on resource utilization. In

contrast with the widespread practice of ad hoc grants driven by politics, the allocation of resources should be based on transparent formulas. Also, unlike the typical unpredictability of most central-to-local transfer mechanisms prevailing in developing countries, the process should provide local institutions with an up-front indication of how much money will be available in the next multi-year planning cycle. This makes local strategic planning possible and provides a financial ceiling that makes such planning a meaningful exercise and an opportunity for local communities to take autonomous decisions on the use of limited resources.

Fiscal decentralization is associated with enhanced quality of government as measured by citizen participation, political and bureaucratic accountability, social justice, improved economic management and reduced corruption (Subedi, 2014).

Fiscal decentralization has been an integral part of overall public sector reform in a number of countries, both developed and developing, and consists primarily of re-assigning expenditure functions and revenue sources to lower tiers of government. Among the merits of fiscal decentralization, policy-makers have stressed efficiency gains, reduction in operational costs, and improved public sector performance in service delivery. The pitfalls of decentralized provision and fiscal policy-making consist, in general, of loss of control over sub national finances and coordination failures in fiscal policy-making, often leading to pressures on sub national finances and, ultimately, macroeconomic stability (De Mello, 2000).

The goal of this fiscal and financial decentralization policy is not only to pursue efficiency in the provision of services at the local level, but also sustainable development, economic growth and the reduction of poverty. Indeed, sustainable development implies efficient management of resources and the environment and a dynamic economic growth process, all based upon a partnership between the public

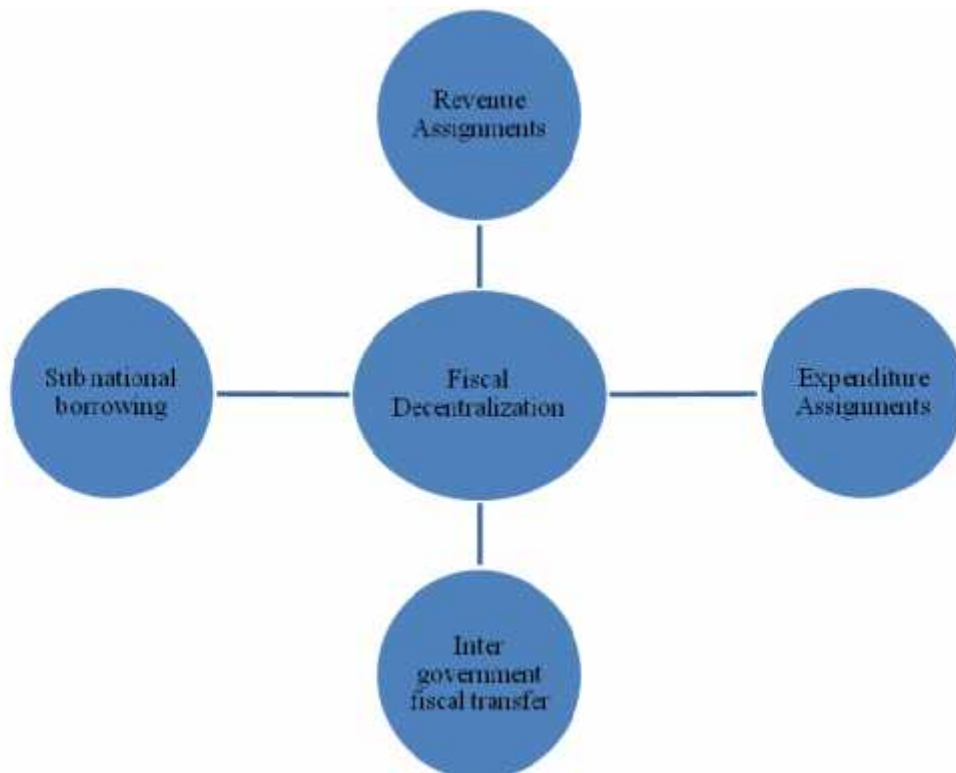
sector, the private sector and civil society. Fiscal and financial decentralization can promote efficiency, innovation, human resource development, entrepreneurship, and dynamism at the local level. Indeed, these are the key elements of a poverty reduction policy (Ministry of Finance and Economic Planning, 2006).

The core theme of fiscal decentralization are some basic principles, including funding to responsibility, equity, transparency, accountability, effectiveness, incentives and enforcement. It includes participative approach, which promotes balanced development process at the local level and decision-making process by local body.

Pillars of Fiscal Decentralization

There are 'four pillars' or 'building blocks' of fiscal decentralization. They are (i) expenditure assignments, (ii) revenue assignments, (iii) Inter-governmental fiscal transfer, and (iv) sub-national borrowing (Boex, 2001)(Cited: Lamichhane, 2012).

The four pillars are explained very briefly in the following ways.



(i) Revenue Assignments

Revenue assignment is the second pillar or building block of fiscal decentralization. Revenue assignment is also known as revenue sharing between central and local level government.

Once the assignment of expenditure responsibility has been determined the second key question is: Who gets what revenue sources? Obviously, an important determinant of the assignment of revenue sources to sub-national governments is the assignment of expenditure responsibilities, giving rise to the adage; finance should follow function (Subedi, 2014).

The sub-national governments have the authority and responsibility to own-finance local services at the margin. There is no ideal assignment of revenue sources between central and lower levels of government. Nevertheless, the three major functions need to be determined as revenue assignment (Musgrave, 1959). (Cited: Lamichhane)

It is important to understand the five core issues with respect to intergovernmental finance (Neumann and Robinson, 2006). The first issue is about expenditure assignments (**Who should do what?**). The second is about revenue assignment (**Who should levy what taxes?**). The third is in relation to fiscal transfer to address the imbalance between revenue and expenditure (**How should any imbalance between revenue and expenditure of sub-national governments be addressed?**). Similarly, the fourth concern is regarding the horizontal fiscal imbalance that occurs when different units of the same order of government, with similar expenditure responsibilities, have significantly differing fiscal capacities (**How are any horizontal imbalances addressed?**) Finally, the issue is about the legal provision of borrowing of sub-national governments (**How to address the issue of sub-national borrowing?**). (Cited: Lamichhane, 2012)

Generally the resources of local government are: Tax (property/house tax, professional tax, vehicle tax, tax on agricultural land, pilgrim tax, tax on animal, fees and other non-tax revenue etc), assigned/Shared Revenue (inter-governmental transfer), Grants (conditional and un-conditional).

Taxes are the most important component of government revenue. User charges and borrowing can't provide all that is needed. Federal aid is unlikely to fill the gap. Taxes must produce enough revenue to fund necessary services. The principles of taxation are specific tax measures up in terms of simplicity, horizontal equity, vertical equity, and distortion of economic decisions, volatility and revenue adequacy (John, 2002). Tax is one of the major sources of internal revenue of government. Taxation is most important financial resource.

Regarding the tax assignment among different tiers of government, international experience suggests that some taxes are better suited for local government than others. Maintaining efficiency is often emphasized for the assignment of local taxes. However, commonly emphasized criteria of tax assignment are as follows: (1) Local taxes should be independent from national policy goals such as income redistribution objectives and economic stability. (2) The local tax base should exhibit low mobility between jurisdictions. (3) Benefit taxes and user charges are appropriate to local taxes (Lamichhane, 2012).

(ii) Expenditure Assignments

The expenditure assignment is the main step in designing an inter-government fiscal system. It is the base of fiscal decentralization. There is no need of revenue without expenditure responsibility.

Expenditure assignment is the first step in designing an inter-government fiscal system. Designing revenue and transfer components of a decentralized inter-

governmental fiscal system without concert expenditure responsibilities would weaken decentralization process. Subedi, (2014) said that the lack of clarity in the definition of sub national responsibilities, there will be confusion whether sub national expenditures represent local priorities or centrally determined program.

The assignment should be based on economies of scale, benefits/cost spillovers, consumer sovereignty and political proximity. The principle of finance should follow function must be practiced properly. Moreover, revenue should match with expenditure needs. It indicates the fiscal deficit must be addressed. The major objectives of revenue allocation are to provide sufficient revenue for macroeconomic stabilization functions, redistribution functions, essential government goods and services (Lamichhane, 2012).

In general, there are two different approaches in expenditure assignment such as "Expenditure-led" and the "Revenue-led" approaches. In expenditure led approach, functions are first designed with clear responsibility based on "subsidiary" principle. Likewise, in revenue-led approach, public revenue resources are first allocated in general way between levels of governments. This approach is regarded as politically sensitive rather than cleaning up the confusion and ambiguity due to overlapping of functions at different level of government (Ligal et al, 2004). (Cited: Lamichhane, 2012)

A stable and meaningful decentralization requires a well-defined institutional framework in the assignment of expenditure responsibilities among the different levels of government together with the sufficient budgetary autonomy to carry out the assigned responsibilities at each level of government (Boschmann, 2009).

(iii) Inter-governmental fiscal transfer

Another pillar of fiscal decentralization is inter-government fiscal transfer. It has many names such as grants, subsidies, subventions etc. Inter-government fiscal transfers are the dominant sources of revenues. It has two dimensions of the transfer: horizontal and vertical.

Since revenue assignment often does not provide regional and local governments with sufficient revenues of fund their expenditure functions, inter-governmental transfers are often necessary to assure revenue adequacy. Transfers are grants from one level of government to another for the purpose of funding government activities. The term “Transfer” is often used interchangeably with the term ‘grant’. In some countries transfers may also be known under different names, such as “subventions” or “subsidies” (Subedi, 2014).

The intergovernmental fiscal transfers are important tool of public sector finance in both industrial and developing countries in three major reasons (Shrivastave, 2002). First, the central government will have opportunity to raise more revenue and maintain good relationship with the sub-national governments and on the other hand, sub-national governments will have advantages to deliver quality services as required by the people in transparent and efficient manner. Second, in most cases, there are considerable differences in revenue-raising capacity between sub-national governments. If they were fully autonomous to mobilize revenue and solely depend on their own revenue, richer jurisdictions would be capable to spend more on public service as compare to the lower income jurisdictions. Third, resource transferred from central to sub-national level helps to address the national priorities areas such as health, education, sanitation, drinking water etc. through the initiation of sub-national government. It is more helpful to promote equity and efficiency of sub-

national governments and be supportive for poverty reduction agendas at grass root level (Lamichhane, 2012).

(iv) Sub-national borrowing

Sub-national borrowing is the fourth and final pillar of fiscal decentralization. Sub-national governments are entitled to receive borrow/debt from the finance company in the development activities of the jurisdiction. However, this provision is applied or not applied in practice depending upon the state law of the respective countries (Lamichhane, 2012).

If any local government expenditure needs are not properly balanced with the resources available to it this could result in sub national deficits and incurrence of debt, of course, just like central government debt, the incurrence of sub national debts by sub-national governments would have the potential of driving up interest rates and crowding out private sector investments (Subedi, 2014).

B. Empirical Study

International Experience in Fiscal Decentralization

Ullah and Pongquan (2010) had conducted a research topic on 'Financial Resource Mobilization Performance of Rural Local Government: Case Study of Three Union Parishad in Bahgladesh'. The main objective of their study was examine the trend and performance of UPs own financial resources mobilization. The research of their study was based upon descriptive analysis and it was an empirical research based on field work and case study approach. The study in summary, it is evident from findings that the local resources mobilization performance of UPs do not lie in lack of commitment, but rather a pragmatic fiscal devolution policy of central authority to induce UP in strengthening revenue efforts which is confirmed by the stated

hypothesis. Fiscal devolution policy adopted by the government is still, in its infant that requires continuous central commitment as well as local efforts and strategies.

This study concluded that the changes in the rural housing pattern and literacy rate have better possibility of increase generation of holding tax revenue of UPs. The regression presents estimation results for a posited relationship between households' ability to pay and other explanatory variables. The regression result suggests that households housing pattern and literacy rate can be used as major determinants of annual average holding tax revenue and for this accomplishment, the regression result also suggests that household ability to pay can be based on last years actual per capita households holding tax, foreign and domestic remittances, agricultural land ownership and household having electricity connection. Since complicated taxation system is not understood by the rural commoners, link of visible benefit of tax is weak and non-compliance become a hurdle in harnessing property and community tax, easy and transparent method will help in increasing tax revenue collection. But there are still arguments that some conditions need to be fulfilled for ability to pay based criteria, such as accurate households statistics, a clear commitment of local representatives, transparency and ability to mobilize local resources by addressing all constraining factors that may derived from existing social, economic, political and administrative and legal factors.

Sareen (2000) conducted a research topic on 'Fiscal Decentralization and Revenue Mobilization: Case of Olongapo City, Philippines'. The main objective of her study was to evaluate the performance of different key source of revenue, identify the problems associated with valuation of the revenue base and the collection of revenue, and suggest recommendations that would improve the fiscal and administrative performance of the Local Government and render generation more

efficient and predictable. It was an empirical research based on primary and secondary data analyzing stated objectives.

Her study funded that from the existing sector and tax base, business tax and property tax will remain major sources of tax revenue for Olongapo city. Increasing revenue will largely depend on the performance of these two taxes. Secondly, public enterprises demonstrate reasonable collection efficiency but have poor costing and pricing mechanisms. Lastly, the local capacity to undertake the new decentralization role is limited because management and financial control system are often deficient. There is little co-ordination between different levels of the decentralization system. In addition, however well designed system might be, they cannot achieve the desired results unless the local government have the capacity to undertake administration, implementation and enforcement of policies in an efficient and effective management. Unless local government improve and streamline their revenue generation mechanisms and expenditure decisions, fiscal decentralization will not be successful.

Vazquez & Mc Nab (1997) had examined research topic on 'Fiscal Decentralization, Economic Growth and Democratic Governance'. The main objective of their study focused exclusively as fiscal decentralization and its separate impact on growth and governance. The study summarized that the positive impact of decentralization on the efficient allocation of economic resources and democratic governance. Policy makers and international aid providers need to have a balanced view of the importance of growth vis-a-vis other economic policy objectives. The concern of policy makers in developing countries and economies in transition is probably wider than economic growth per se. The wider concerns are about economic development which includes growth in per capita income, of course, but it also includes other

things such as preservation of the economic environment, a balanced distribution of resources, higher individual welfare as provided by a more efficient provision of public services, democratic governance and so on.

In their paper, there were strong reasons a priori to argue that there should be a symbiotic relationship between fiscal decentralization and democratic governance. Explicitly, and more often implicitly, democratic governance is widely acknowledged in the economic literature as a necessary condition for effective fiscal decentralization. But clearly, there is wide consensus that the relationship also works the other ways. Greater fiscal decentralization, especially the devolution or delegation of tax and financing and spending powers to sub national governments and promotes democratic governance through representation and accountability. The strongest evidence for this comes from country studies and general evaluations of fiscal decentralization experiments in Latin America.

Asatryan, Feld, & Geys, (2012) had studied a research topic on 'Partial Fiscal Decentralization and Sub-National Government Fiscal Discipline: Empirical Evidence from OECD Countries'. The main objective of their paper was to find the role of SNG revenue independence for local-level budgetary (im)balances and role of revenue decentralization for sub-national fiscal discipline, and their results remain somewhat mixed. That was theoretical and empirical research. Based on a new panel dataset including 23 OECD countries from 1975 to 2000, the study results indicate that greater fiscal autonomy is indeed associated with higher SNG budget discipline. This suggests that, while a broader constellation of political, market and fiscal institutions should be considered for sustaining sound fiscal policies, the availability of own revenue sources may be a component allowing SNG to maintain a healthy fiscal balance. Yet, even when assuming that causality runs from revenue autonomy

to fiscal discipline (which, as mentioned, could not be conclusively demonstrated here), one should keep in mind that raising SNG revenue autonomy may face institutional constraints (such as the capacity of SNG tax administration) as well as economic challenges (e.g., increased scope for horizontal and vertical tax competition, fiscal disparities and/or adverse distributive effects across regions). Careful consideration of such effects is essential to generate the right policy decision regarding the need and/or benefits of (further) revenue decentralization.

Smoke (2001) mentioned that "As Economic & political pressure for fiscal decentralization continue to escalate & as forces driving democratization continue to dollop many countries will feel an increasing urgency to decentralize."

Davoodi, Xie, & Zou, (1998) studied topic on 'Fiscal Decentralization and Economic Growth: A Cross-Country Study'. The main objective of their paper had to provide theory and evidence on the relationship between fiscal decentralization and growth. In a simple model of endogenous growth with public spending by different levels of government, they have demonstrated how fiscal decentralization affects the long-run growth rate of the economy. Applying the model to the U.S. economy, they found that the existing spending shares for local and state governments are consistent with growth maximization. That finding holds for two as well as three levels of government. Their empirical examination is highly relevant for current policy debates on the allocation of federal grants and the assignment of expenditure responsibilities among the three levels of government in the United States. If efficiency gains and growth are the main objectives for further fiscal decentralization in the United States, the empirical results of their study seem to suggest that this move may be harmful for growth.

Vazquez, (2011) studied the topic on 'The impact of fiscal decentralization: Issues in theory and challenges in practice.' The goal of his study to explored (i) why countries choose to decentralize their governance; (ii) what economic theory expects from decentralization; and (iii) what is known about the impact of decentralization on a relevant list of economic and political variables, as well as what conclusions are appropriate. His study attempted to study many questions on the impact of fiscal decentralization not certain even with the additional research that was needed. However, these were grounds to be positive & optimistic about the overall impact of decentralization system, especially when they are will design & implemented much work still needs to be done to discover how to improve the design the implementation of fiscal decentralization system.

Greco (2003) under asymmetric information, local governments are always as efficient as central government in providing the efficient allocation of the local public good.

Rodríguez-Pose & Krøijer, (2009) had studied research topic on 'Fiscal Decentralization and Economic Growth in Central and Eastern Europe'. His paper discussed the relationship between fiscal decentralization and economic growth in Central and Eastern Europe (CEE) and tested the relationship between a decentralized fiscal structure and economic growth rates at national level. His study had tested for the effect of fiscal decentralization on the rate of economic growth across a sample of 16 Central and Eastern European countries for the years 1990-2004. His findings suggested that fiscal decentralization is operating in the opposite direction than what is predicted by the 'economic growth through fiscal decentralization' hypothesis. The results conclude that expenditure at, and transfers to, the sub national level have had negative correlation with national growth rates in

CEE, while locally imposed taxation has achieved some mildly positive economic benefits over time.

Overall of his study, fiscal decentralization is a multifaceted process and the inverse relationship between growth and sub-national expenditure assignment and fiscal transfers, and the in time, positive correlation between growth and sub-national taxation, as implied in this study, is just one facet to consider. Within the fiscal sphere, all the fiscal decentralization indicators examined in his study are intertwined. Meaning is that if one of these elements is poorly designed, the entire fiscal structure may be compromised. As indicated by Bird (2000), the design of each pillar of the intergovernmental system must be very well linked to broader decentralization reform goals and intergovernmental fiscal policy objectives. The importance of his study is therefore not only to isolate the significant influence of any individual fiscal decentralization indicator, but also to underline the complex nature of the interaction between different indicators and the importance of understanding this interaction when undertaking further reforms towards fiscal decentralization.

Although, decentralization is often associated with increased degrees of policy innovation, greater transparency, and better capacity of governments to adapt policies to local needs, it can be difficult to connect these factors with increased economic performance.

Fiscal Decentralization in Nepal

Devkota (n.d.) demonstrated an article topic on 'Effect of Fiscal Decentralization on Economic Growth in Districts of Nepal: An Econometric Analysis'. The key objective of his article was to analyze the effect of fiscal decentralization on economic growth in districts of Nepal on using the cross section district level data

for the period of three years (2007-2009). That was an empirical research on secondary data based on 20 districts data set for the panel regression model; the finding was that, *ceteris paribus* fiscal decentralization enhances the district economic growth.

Devkota's theory suggested that a close match between expenditure and revenue assignments at Local Governments level benefit allocative efficiency, production efficiency, and fiscal efficiency and hence enhances to economic growth...process of fiscal decentralization is beneficial to the economy of Nepal. It points out that it is conducive for economic growth. The overall conclusion was that, fiscal decentralization is supportive to district per capita agriculture growth; i.e. the proxy of district per capita GDP growth of Nepal and it is a crucial step towards economic growth in aggregate.

Dhungel, Sapkota, Renmi & Haug (2011) concluded a research topic on 'Decentralization in Nepal: Laws and Practices'. The prime objective of the research was to focus on the workings of existing mechanisms of decentralized local governance in the context of the LSGA with the objectives of analyzing whether or not there had been: (i) Increase in participation (including representation) in the planning process with focus on women, Janajatis and Dalits, especially after the promulgation of the Interim Constitution of Nepal in 2007; (ii) Resource allocation systems more sensitive to demands of marginalized groups; (iii) Increase in the mobilization of local resources by the LBs (DDC/VDC); (iv) More autonomy to the LBs in decision making, service delivery and benefit sharing; and (v) Increase in responsiveness and accountability in both the LBs and the centre in the planning process; and decrease in conflict in benefit sharing at the local level. It was an

empirical study. The study used qualitative methods based on both a desk study and fieldwork.

The study concluded that to overcome the absence of elected representative, the all party mechanism was institutionalized as an advisory body for the village development committee (VDC) secretary his/her team & the local development officer (LDO) who were assigned the responsibility of operating & managing the VDC & DDC. Even in the absence of elected representatives, the LSGA's implementation experience could very well form the basis of framing a new law on LBs in Federal Nepal.

In reality, however, decisions are made in closed sessions that follow the open meetings in VDC/DDC level to discuss development plan, to which only a few influential people are invited, and decisions are made by a more constricted circle of politicians and civil servants. However, popular participation is neither inclusive nor effective and decision making is largely in the hands of politicians whose power has become institutionalized through the all-party mechanism (APM).

Resource mobilization by local bodies varies across local bodies depending on economic development in the area. In the more developed Tarai area, local bodies have been able to mobilize 10 per cent to 15 per cent of their resource requirements, whereas in the hills, less than 5 per cent of financial resources are raised by local bodies. Consequently, the autonomy of local bodies is severely circumscribed because they rely heavily on central government grants for recurrent expenditures as well as development initiatives.

Shrestha, (2009) studied article topic on 'Fiscal Decentralization and Local Resource Mobilization in Nepal'. The main objectives of his paper were: a) to identify the current local resource mobilization practices of District Development Committees

(DDCs) and Village Development Committees (VDCs) of Nepal, b) to elucidate the scope and challenges of local bodies as regards to the local resource mobilization at the local level. The research of his study was based upon primary data and that was an empirical research.

His research concluded that fiscal decentralization is an important means of system of governance to mobilize the local resources. The suggestions are made in the following bullets in the context of Nepal. Present nominated local government needs to change into local elected representative, which could have more power for the effective and efficient mobilization of local resources. The technical manpower at the local level is the felt need of the local government, which has to be fulfilled. Locally available resources should be monetized to be measure in unit and divisibility of factors, which help enhance the productivity by exchanging the goods and services. Local resources should integrate as productive unit and determine the distribution mechanism to equalize the marginal social benefit and marginal social cost. Several alternatives should be explored to make the local bodies self-sufficient in terms of resources by using the given fiscal power. Current tax base and tax rate provision of LSGA should be reviewed in the changed context. The local bodies should be made responsible and accountable to the local people to focus in the capacity development to improve the quality service delivery system.

Adhikari (2006) summarized that the planning, administrative and management capacity of the local bodies must be strengthened aggressively (with high priority) to be able to accomplish their increased functions and tap the opportunities offered by the decentralization train. As discussed above, the central authority, generally doubt and blame the local bodies and local level agencies for their weak capacity and use this as good excuse to limit decentralization rather than helping them to strong then

their capacities. The central level has to take responsibility to render them strong, ready and capable of achieving the objectives of decentralization...furthermore; the central level institutions have to have the responsibility of supervising local bodies on a result based manner. Continuous policy monitoring, review and policy adjustment is enough for the central-level agencies.

Nepal (2007) studied topic on 'Fiscal Decentralization and Size of Local Government: A case of Nepal'. He summarized that it is worth mentioning that fiscal decentralization should get sufficient attention in an effort to improve governance as well as public service delivery in the country. Stimulation of local taxes and charges is an important part of the activities of local self-government bodies in the performance of local financial management. Efficient implementation of a policy of local taxing and spending will increase the local efficiency and there by improve the whole governance, while will fulfill the political promises.

Communication and Management Institute (2010) concluded that the Himalayan districts are very diverse in terms of generating internal revenue attributed mainly by geography, accessibility and state of the development. The revenue potentials are not the same within the region as well. The existing policy of GoN also doesn't favor equitably to all districts (e.g. revenue sharing from tourism and electricity). Hence, most of the districts are heavily dependent on the GoN grant for their expenditure needs. Even with the improvement and reformation of internal revenue mobilization policy and practice, the dependency of these districts on central grant cannot be expected to reduce substantially.

Lamichhane, (2012) studied a research topic on 'Fiscal Federalism and Local Government Finance in Nepal'. His study focused on the theoretical perspective of fiscal federalism and its practice in some selected countries. The main objective was

to review the theories of fiscal federalism, fiscal decentralization and local government finances in Nepal. It is an empirical research on the secondary data analyzing stated objectives. His study said that expenditure decentralization is given more priority rather than revenue decentralization in many countries of the world. For effective implementation of fiscal decentralization, authorities on fixing the bases and rates of taxes should be devolved to sub-national governments. The financial dependency of local government bodies in Nepal on central government has increased year by year. For stabilization and fiscal equalization/redistribution purposes, general practice is that the central government should collect 50% or more of total taxes, and those taxes should be from a broad-based elastic tax bases (such as income or value added).

Lamichhane concluded that there is provision of carrying out the study on revenue potentiality by local government bodies in Nepal, no effective and practical efforts are made so far. The legal provision of horizontal revenue sharing and revenue transfer from one local government to another is not appropriately practiced in Nepal. The total national revenue is found very powerful factor to determine the local government expenditure in Nepal. It is clear that very limited power and authorities are devolved to the VDCs in order to mobilize internal revenue to meet the local expenditure at rural area. There is practice to obtain loan and borrowings by the municipalities that covers about 1.43% of the total income. The share of tax and non-tax revenue (internal revenue) plays very insignificant role in total revenue mobilization by DDC. However, the share of internal revenue to total revenue of local governments is about 31.40%.

On an average, of the total expenditure, about 78% is directly spent by central government whereas 22% is spent by local government bodies, district and village

level line agencies. The share of central government grant to municipalities is very low as compared to DDCs and VDCs. This point explains that municipalities have been exercising more fiscal autonomy as compared to DDCs and VDCs in Nepal. On the other hand, VDCs are more dependent to the central government grant among the three local bodies in Nepal. Although municipalities are relatively more autonomous than VDCs and DDCs in resource mobilization, in totality, local government in Nepal deeply rely on the central government grant to deliver services at local level. The tax collection authority is not devolved appropriately to the local government especially to DDCs in Nepal. Therefore it can be said that the dependency of DDCs on central government revenue is substantially high. It is the fact that of the total revenue, the share of grant and revenue sharing is about 75% of DDCs revenue.

LSGA, (2055) provides independent rights and responsibility with accountability to the local institutions for the enjoyment of the fruits of democracy through the utmost participation of the sovereign people in the process of governance by way of decentralization, Institutionalize the process of development by enhancing the participation of all the people including the ethnic communities, indigenous people and down-trodden as well as socially and economically backward groups in bringing out social equality in mobilizing and allocating means for the development of their own region and in the balanced and equal distribution of the fruits of development, by handling all the responsibility of local level by local people. This Act has the provision of institutional development of local bodies capable of bearing responsibility, by providing such responsibility and power at the local level as is necessary to formulate and carry out plans, and Constitute local bodies for the development of the local self-governance system in a manner that they are able to

make decisions on the matters affecting the day-to-date needs and lives of the people, by developing local leadership. Long term plans should be made in local level to make people and country side developed and the long term plan should be implemented in village area.

The Interim Constitution 2063 recognizes this fact and says: There shall be mobilization and allocation of responsibilities and revenue between the Government of Nepal and the local self-governance related authorities as provided by law in order to make the local self-governance related authorities accountable for the identification, formulation and implementation of local level plans, while maintaining equality in the mobilization, appropriation of means and resources and in the balanced and equitable distribution of the fruits of development with a view to strengthening the local self-governance related authorities for local development (Article 140.1). While mobilizing and allocating revenues... special attention shall be accorded to the overall upliftment of those classes and communities who are backward socially and economically in such a manner as to have a balanced and equal development of the country (Article 140.2).

Based on the review of major earlier studies, it is realized that there is a specific research gap in the area of comparative study about fiscal decentralization policy and local resource mobilization nexus between all municipalities and better performing municipality as well as relatively poorly performed municipality.

CHAPTER III

RESEARCH METHODOLOGY

3.1. Research Methodology

Research methodology is a way to systematically solve the research problem. It may be understood as a science of studying how research is done scientifically (Pant, 1975). This study is use secondary data and information and use qualitative and quantitative variables in nature. Secondary data is collected from various published and unpublished government and non-government sources such as books, report, journals and articles and from internet also.

3.2. Research Design

This research is descriptive and quantitative research which is describing the nexus between fiscal decentralization policy and local resource mobilization in Nepal. The purpose of research is to achieve new insights into the phenomenon of relationship between fiscal decentralization policy and local resource mobilization in Nepal.

3.3. Nature and Sources of Data

The research is using both qualitative and quantitative nature of data. This study is mainly based on the secondary data. To fulfill the purpose of study this, there are some of municipality were take as sample and compared with over all municipalities.

3.3.1. Selection of Municipality

This study mainly based on the income and expenditure pattern of all municipalities as well sample municipality to identify the actual situation. For this purpose the two municipalities are selected as sample municipality. In my study area 58 municipalities, out of them two municipality Bhaktapur municipality of Bhaktapur

district and Bhimdatta municipality of Kanchanpur district are selected on the basis of geographical diversity, revenue generation potential and diversity in terms of city or legal of development and cultural variations as well as connivance of the research.

3.3.2. Source of Data

The secondary data is collected through various published and unpublished sources regarding fiscal decentralization and local resource mobilization in Nepal.

Secondary sources of Data:

-) Data from Ministry of Finance (MOF)
-) Data from Ministry of Federal Affairs and Local Development(MOFALD)
-) Data from Financial Management Discipline of gtz/udle
-) Data from Local Body Fiscal Commission Secretariat (LBFCS)
-) Data from Office of Bhaktapur Municipality
-) Data from Office of Bhimdatta Municipality
-) National Planning Commission (NPC)
-) Central Bureau of Statistics (CBS)
-) Financial Comptroller General Office(FCGO)
-) Human Development Report of UNDP
-) World Development Report
-) Asian Development Bank Report
-) Central Library of TU, Kirtipur
-) Data from the published journals, books, research reports and survey.
-) Other data from website/web-portals and internet also will be analyzed.

3.4. Presentation of Data and Analysis

It is both descriptive as well as analytical study. The simple percentage method is used to calculate the share of own source/ internal revenue in total revenue and expenditure of local bodies (municipalities) in Nepal. Revenue pattern of local body reviewed and calculated the ratio between internal revenue and external revenue (grants, lone) for our study time period. Internal revenue mobilization, share of internal sources in expenditure also reviewed. The recurrent and capital expenditure reviewed and calculated the ratio between recurrent and capital expenditure in total expenditure. This analysis has shown the detail status of revenue generation and expenditure pattern of the local bodies. All the descriptive analyses are presented in table, bar-diagram, pie chart and figure in the chapter-four of the study.

CHAPTER IV

PRESENTATION OF DATA, ANALYSIS AND FINDINGS

The government of Nepal has been practicing different forms of decentralization ranging from delegation, de-concentration and devolution of authority (MLD, 2006:8). In the Panchayat (non-party system of government) period, various laws were enacted including financial regulation. However, the promulgated law and rule could not stand for a long time which was changed from time to time. There are various laws concerning decentralization such as Village Panchayat Act 1962, District Panchayat Act 1962, Local Administration Arrangements Act 1966, Decentralization Act 1979, etc. The working approaches of these laws were characterized by top down approach. Generally, in the context of financial regulation, the central government mobilized almost all of the resources through the district office line ministries.

After the restoration of democracy in 1990, at first, three laws were enacted with regard to local bodies named as Village Development Committee Act 1992, Municipality Act 1992, and District Development Committee Act 1992. Due to contradiction between the central and local governments as well as in between the local governments (DDC and VDC) with regards to power and sharing of resources and duplication of role and responsibilities, the government of Nepal has enacted "Local Self- Governance Act-1999" and "Regulations 2000" by integrating the then three Acts as mentioned above. Promulgation of Act and Regulations is a landmark decision of the government of Nepal to practice the fiscal decentralization principle democratically. The major aim of present financial regulations is to clarify the

functions, duties and responsibilities of the local bodies to collect and mobilize resources and making them accountable and responsible (Shrestha, 2009).

In Nepal there are two level local bodies according to concept of decentralization. In first level there are Village Development Committees (VDCs) and Municipalities, and in second level or higher level there is District Development Committees (DDCs). DDCs work as the bridge between central and local level government. In Nepal, structure of local bodies is in the form of 3,176 VDC's, 217 municipalities (1 metropolitan and 12 sub-metropolitan) and 75 DDCs organized and functioning. These bodies are controlled and supervised in accordance with Local Self Governance Act (LSGA), 1999(2055) and Local Self Governance Regulation (LSGR), 2000(2056).

4.1. Revenue Generation of Local Bodies in Nepal

The Local Self Governance Act (LSGA), 2055 has been made provision for tax, fees and fines, and revenue sources for VDCs, Municipality and DDCs. The Local Self Governance Regulation (LSGR), 2056 has fixed the rates of sources of revenue of local bodies (VDCs, Municipality and DDCs). The detail source of revenue of the local bodies as per LSGA, 2055 and LSGR, 2056 are given in Annex 4.1. The Clause 60, 125 and 221 of LSGA, 2055 has determined revenues area respectively for the VDCs, Municipalities and DDCs, which are following:

-) Taxes, Fees and Fines, Levies, etc
-) Revenues from self construction and management.
-) Income achieved from Revenue Sharing and Field Registration Fees.
-) Conditional and Unconditional aid given by central level.
-) Help from donor organizations.
-) Legal based debt and other helps.

) Municipalities earn their extra income from fees to pass house maps and integrated property tax whereas extra income of DDCs comes from selling stones, sands, and other natural sources, etc.

4.2. Classification of Municipality

According to LSGA, 2055 under Section 88, (1) Government of Nepal may classify the Municipalities constituted under Section 80, on the basis of population, sources of income and other urban facilities, as follows: -

- (a) Municipal Corporation,
- (b) Sub-municipal Corporation,
- (c) Municipality.

(2) The following Municipalities classified under Sub-section (1) shall have the population and urban facilities as follows: -

(a) Municipal Corporation: With the population of at least three hundred thousand and annual income source of minimum four hundred million rupees, having the facilities of electricity, drinking water and communications, having the main road and accessory roads of the town pitched, availability of highly sophisticated nature of service in respect of health services, having the necessary infrastructures as required for international sports program, availability of adequate opportunities for higher education in different subjects and having at least one university established and other similar adequate urban facilities and having already been existed as a Sub-municipal Corporation.

(b) Sub-municipal Corporation: With the population of at least one hundred thousand and annual income source of minimum one hundred million rupees, having the facilities of electricity, drinking water and communications, having the main roads of the town already pitched, having the facilities of higher level education and

health services, ordinary facilities for national as well as international level sports program, having the provisions of public gardens and city halls and other similar necessary urban facilities and having already been existed as a Municipality.

(c) Municipality: A semi-urban area with a population of at least twenty thousand, and annual source of income of minimum five million rupees and with electricity, roads, drinking water, communications and similar other minimum urban facilities. Provided that in the cases of mountainous and hilly areas, a population of at least ten thousand and annual source of income of minimum five hundred thousand rupees shall be sufficient even if there is no road facility.

Details of all other municipalities are in annex 4.2.

4.3. Revenue Generation and Income Pattern of Municipality

Clause 136 to 145 of LSGA, 2055 includes the provision of income and expenditure area of Municipalities has been included such as; land revenue and house and land tax, rent tax, enterprise tax, vehicle tax, property tax, entertainment tax, commercial video tax, advertisement tax, parking charge, service charge, etc. And according to Clause 148 of LSGA, 2055, Municipalities can Borrow loan and debt and it can also get grants from external sources according to the same clause as well as non expenditure of previous year also included as income of current fiscal year. The data on overall income from Fiscal Year (FY) 2051/52 to FY2070/71 of all Municipalities is presented in table 4.1.

Table 4.1: Revenue Generation Pattern of Municipality in Nepal

Fiscal Year	Revenue of Municipality (In 00)										
	Local Taxes(a)	Fees and Fines(b)	Property Rental ©	Other Revenue (d)	Own Source Revenue(a+b+C+d)	Miscellaneous Income	Grants	Loans	Balance Forward	Total Revenue	Share of Own source Revenue in Total Revenue
51/52	6115137	455519	232038	83774	6886468	88958	551878	301381	1185556	7828686	87.96
52/53	6580222	471037	265289	105352	7421900	116430	689622	986954	1034294	10249199	72.41
53/54	6860953	652413	349355	199298	8062019	184307	849435	222081	1147366	10465207	77.04
54/55	9843444	786254	396504	223831	11250034	163565	2618022	195560	1637048	15864229	70.91
55/56	8727099	904485	460593	330839	10423017	164353	2486871	509526	1869695	15453462	67.45
56/57	10531943	1417638	502139	278619	12730338	227971	2430924	1541664	1338153	18269049	69.68
57/58	11664474	2560381	571811	327973	15124638	262148	2543352	1356185	2338205	21624528	69.94
58/59	13681684	2465234	675890	824555	17647363	263960	3702677	92248	2071359	23777607	74.22
59/60	12484126	3237023	786485	573460	17081094	3651488	2333395	261437	1614628	21653728	78.88
60/61	12374355	3595493	826657	858407	17654911	633697	2889863	263460	3753683	25195615	70.07
61/62	13473498	4088279	901479	872115	19335370	734436	7056972	239845	3688762	31055385	62.26
62/63	13311774	3852879	790590	723698	18678940	919718	6556533	398442	1941154	28494787	65.55
63/64	13716259	4431612	862984	435473	19446328	2584916	11006094	477784	2462120	35977242	54.05
64/65	14393177	5100939	1070722	509412	21074250	1140473	12000884	284907	6261536	40762050	51.70
65/66	24475889	6439692	975555	731675	32622810	3141956	23757472	234810	1818745	61575793	52.98
66/67	18637532	5382545	987735	687648	25695460	3534240	28142210	997620	16381050	74750580	34.37
67/68	12699420	10898500	995600	6526730	31120250	5180580	38155620	821050	6484040	81761540	38.06
68/69	9271980	9103610	516300	3706290	22598180	NA	53412510	NA	NA	76010690	29.73
69/70	12775040	13575540	935020	6370540	33656140	2672850	42333540	507950	NA	76497630	44.00
70/71	15270550	12931640	1058500	8564810	37825500	2713920	33501880	NA	NA	74041300	51.09
Average	12344428	4617536	708062	1646725	19316751	1418998	13850988	484645	2851370	37565415	61.1

Source: UDLE/LBFCS,(2055,2057,2066,2068,2069,2070,2071)

Table 4.1 shows the revenue pattern of all Municipalities in Nepal. The table depicts the total revenue, own source revenue (internal income), total grants, loan, miscellaneous income, balance forward and percent of internal income in total revenue. In fiscal year 2051/52 the contribution of internal income (with revenue sharing) in total revenue is 87.96 percent, which is 72.41 percent in FY 2052/53, 77.04 percent in FY 2053/54, 70.91 percent in FY 2054/55, 67.45 percent in FY 2055/56, 69.68 percent in FY 2056/57, 69.94 percent in FY 2057/58, 74.22 percent in FY 2058/59, 78.88 percent in FY 2059/60 and which is 70.07 percent in FY 2060/61.

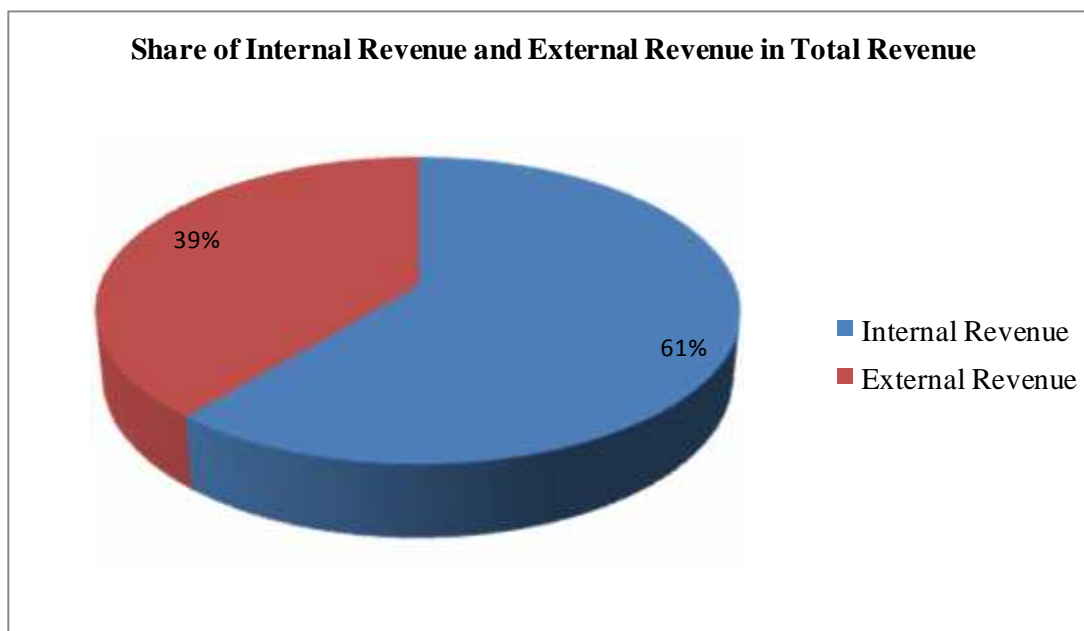
Here, the share of internal revenue in total revenue from FY 2051/52 to FY 2060/61 contributing in larger portion which is approximately 74 percent.

The trend of share of internal revenue after FY 2061/62 is decreasing. In FY 2061/62 contribution of internal revenue in total revenue is 62.26 percent, which is 65.55 percent in FY 2062/63, 54.05 percent in FY 2063/64, 51.70 percent in FY 2064/65, 52.98 percent in FY 2065/66. In FY 2066/67 it is 34.37 percent. Same wise, it is 38.06 percent in FY 2067/68, 29.73 percent in FY 2068/69. In FY 2069/70 internal revenue is 44.00 percent and 49.23 percent in FY 2070/71. Here, the share of internal revenue after FY 2068/69 was in increasing trend.

Initial 10 years, the contribution of internal revenue in total revenue of municipality was relatively high that may be the cause of presence of elected representative of local bodies (i. e they are legally authorized representative persons). But, trend is decreasing after FY 2061/62 to FY 2068/69, which may be the cause of political instability and intervention of political parties. Similarly, *CHANDA AATANKA* different unusual activities of different groups, such as threat to life, abduction and other negative activity creates problem to security, lack of business environment etc.

in Terai and eastern hilly area. So that there should be created conducive environment.

Figure 4.1: Share of Internal Revenue and External Revenue in Municipalities



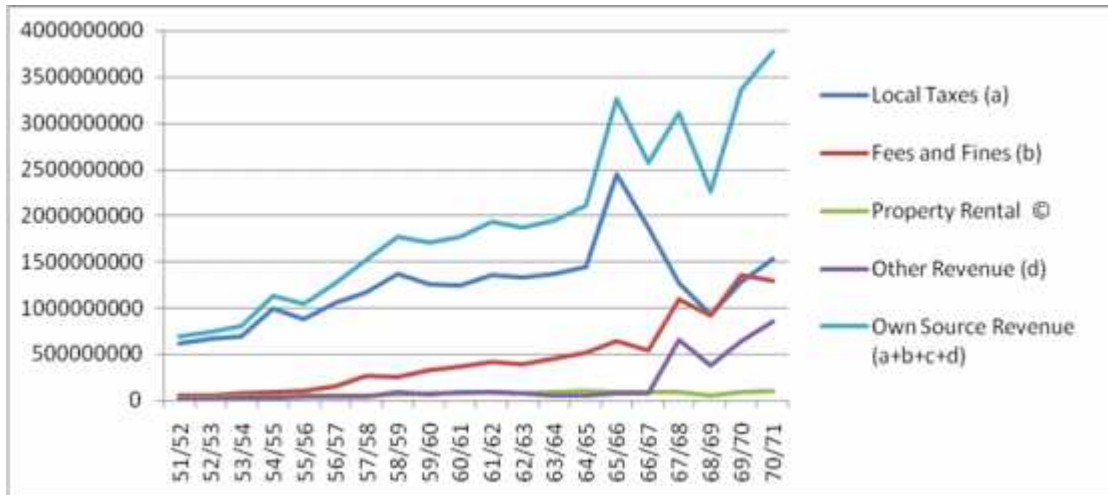
Source: UDLE/LBFCS, (2055, 2057, 2066, 2068, 2069, 2070, 2071)

The average contribution of internal revenue in last twenty year is about 60.56 percent out of total revenue of municipality. This shows that, 39.44 percent revenue is contributed by central level (External sources: Grand, Loan, Balance forward, etc.). The state of revenue generation capacity of municipality shows there is low dependency of municipality to central level, which is the good indicator for fiscal decentralization.

4.4. Revenue Generation (Own Source) by Municipalities

Municipalities generate income from various sources like local tax, fee and fines, property rent, royalty and other various sources. The detail analysis of revenue generation for the last 20 years is included in annex 4.4 and average summary of revenue generation of all municipalities can be shown in following figure.

Figure 4.2: Revenue generation by municipalities



Source: UDLE/LBFCS (2055, 2057, 2066, 2068, 2069, 2070, 2071)

Above figure shows that the share of property rental and other revenue in own source revenue is very small in portion, which is in average of twenty year is about 4 percent, 8 percent respectively. The share of fee and fine is medium and the share of local tax in own source revenue in very high which is in average of twenty year is about 24 percent and 64 percent respectively. In conclusion most of the part of own source revenue is generated through the local taxes and fee and fines.

Revenue Generation Pattern of Bhaktapur and Bhimdatta Municipality

Generally, Municipalities revenue sources are a combination of tax and non-tax charges that are internally generated and grant, borrowing from the central level government. Tax revenues include local tax such as property tax, land tax, roof top tax, house rent tax, unclaimed land tax, industrial tax, vehicle tax, road permit tax, entertainment tax, advertisement tax, etc. Non-tax revenue includes fees and fines, service charge fee, sale income, property rental, local development fee, etc.

The detail revenue generation structure of sample municipality: Bhaktapur and Bhimdatta Municipality of fiscal year 2065/66 are shows in following table.

Table 4.2: Revenue of Bhaktapur and Bhimdatta Municipality of fiscal year 2065/66

INTERNAL REVENUE	Bhaktapur Municipality	Share in Total Revenue	Bhimdatta Municipality	Share in Total Revenue
<i>Tax Revenue</i>	12146872	7.05	5335887	11.71
LOCAL TAX	12146872	7.05	5335887	11.71
House Rent Tax	3642221	2.11	200485	0.44
Roof Top Tax	2865489	1.66		0.00
Land Tax	1489184	0.86		0.00
Unclaimed Land Tax	978886	0.57		0.00
PATAKE Business Tax	0	0.00	258260	0.57
Business Tax	1758218	1.02	620645	1.36
Vehicle Tax	413733	0.24	174143	0.38
Industrial Tax	863671	0.50		0.00
Property Tax	0	0.00	3726807	8.18
Vehicle Registration and Annual Tax	0	0.00	12657	0.03
Road Permit Tax	10805	0.01	342890	0.75
Entertainment Tax	117665	0.07		0.00
Advertisement Tax	7000	0.00		0.00
<i>Non-Tax Revenue</i>	160177397	92.95	40246054	88.29
FEES AND FINES	108888824	63.19	8250621	18.10
Parking Fee	495195	0.29	70710	0.16
Bills and Service Fee	0	0.00		0.00
Electricity	80579	0.05	38195	0.08
Recommendation Fee				
Telephone	0	0.00	150	0.00

Recommendation Fee				
Appraisal Fee of Fixed Assets	172154	0.10	379170	0.83
Local Development Fee	26611000	15.44	7404000	16.24
Sanitation Service Fee	69450	0.04	139393	0.31
Toilet Use Service Fee	4835	0.00	104164	0.23
Park Entry Fee		0.00	23456	0.05
Tourism Service Fee	80302531	46.60		0.00
Village Partnership Development Fund		0.00	91383	0.20
Other Service Fee	1153080	0.67		0.00
FEES	5568006	3.23	1131846	2.48
Registration and Renew Fee	83230	0.05		0.00
Building Permit Fee	3542676	2.06	606670	1.33
Recommendation Fee	1911305	1.11	470381	1.03
Relationship Certified Fee	12100	0.01	6520	0.01
Citizenship Recommendation Fee		0.00	21400	0.05
Animal House Fee		0.00	26875	0.06
Other Fee	18695	0.01		0.00
SALES	10972	0.01	656890	1.44
Auction of Property Sale	9942	0.01	28700	0.06
Tender Sale		0.00	126690	0.28
PRASAD Sale		0.00	501500	1.10
Other Sale	1030	0.00		0.00

OTHER REVENUE	11849909	6.88	6741168	14.79
Fine	1020088	0.59	172548	0.38
Property Rental	2910002	1.69	2845521	6.24
Contingency		0.00	70026	0.15
Last Year Advance Refund	246607	0.14		0.00
Other Income	7673212	4.45	146064	0.32
Balance Forward		0.00	3507009	7.69
Total	138464583	80.35	22116412	48.52
EXTERNAL REVENUE		19.65		51.48
Grand from Government	27926046	16.21	18785950	41.21
Grand from DDC	838640	0.49	69779	0.15
Retained Fund		0.00	4431000	9.72
Public Partnership Cost Heritage	5095000	2.96		0.00
Governance Reform Program		0.00	178800	0.39
Total	33859686	19.65	23465529	51.48
Grand Total	172324269		45581941	

Source: Bhaktapur/Bhimdatta Municipality, 2065/66

The total revenue of Bhaktapur Municipality is 172324269 and total revenue of Bhimdatta Municipality is 45581941 which show revenue of Bhaktapur municipality is about 4 times greater than to revenue of Bhimdatta municipality.

The contribution of tax revenue in total revenue of Bhaktapur and Bhimdatta municipality are 7.05 percent and 11.71 percent respectively. Similarly share of non-tax revenue in total revenue are 92.95 percent and 88.29 percent respectively.

The contribution of internal revenue in total revenue of Bhaktapur and Bhimdatta municipality are 80.35 percent and 48.52 percent respectively. The share internal revenue in total revenue of Bhaktapur municipality is higher than Bhimdatta municipality. That is Bhaktapur municipality is performing betterly and performance of Bhamdatta municipality is poor in comparision with Bhaktapur municipality. Bhaktapur municipality generate revenue from tourism service fee about 47 percent in total revenue which as in this heading has not income of Bhimdatta municipality. Similarly, Bhaktapur municapility collact revenue from house rent tax, roof top tax, building permit fee approximately higher than Bhimdatta municipality. Which causes may be high population, more economic and industrial activity identified other possibility sector which can contribute to local resources like as tourism sector, mine, cultural heritage, etc. Which shows that the some of municipalities are getting more advantaces from the fiscal decentralization policy whare as some of other municipality are getteing little benefits from this policy.

Bhaktapur municipality generate revenue from local tax, fees and fines(service charge), fees, sale income, other internal revenue and transfare from higher level(grants) are 7.07, 63.19, 3.23, 0.01, 6.88 and 19.65 percent of total revenue respectively where as Bhimdatta municipality are 11.71, 18.10, 2.48, 1.44, 14.79 and 51.48 percent of total revenue respectively.

Tax Revenue

The municipal taxation is one of the most important sources of revenue in municipalities. In Nepal, municipal tax bases are defined by LSGA,2055 and rate are defined by LSGR, 2056. House rent tax, roof top tax, land tax, business tax, vehicle tax, property tax, road permit tax, advertisement tax, etc are the major taxes assigned

to the municipalities. The structure of municipal tax revenue is as in the following table.

Table 4.3: The Structure of Tax Revenue of Bhaktapur and Bhimdatta Municipality of fiscal year 2065/66

Tax Head	Bhaktapur Municipality		Bhimdatta Municipality	
	Amount	Share in Total Tax	Amount	Share in Total Tax
House Rent Tax	3642221	29.98	200485	3.76
Roof Top Tax	2865489	23.59	0	0.00
Land Tax	1489184	12.26	0	0.00
Unclaimed Land Tax	978886	8.06	0	0.00
PATAKE Business Tax	0	0.00	258260	4.84
Business Tax	1758218	14.47	620645	11.63
Vehicle Tax	413733	3.41	174143	3.26
Industrial Tax	863671	7.11	0	0.00
Property Tax	0	0.00	3726807	69.84
Vehicle Registration and Annual Tax	0	0.00	12657	0.24
Road Permit Tax	10805	0.09	342890	6.43
Entertainment Tax	117665	0.97	0	0
Advertisement Tax	7000	0.06	0	0
Total Tax Revenue	12146872		5335887	

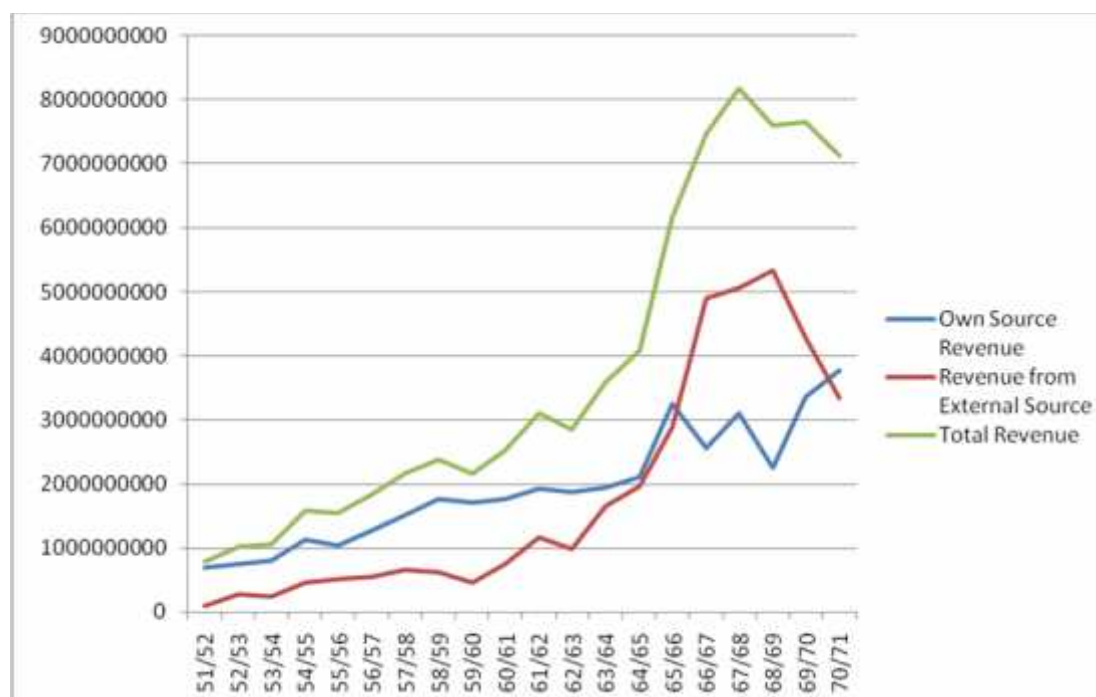
Source: Bhaktapur/Bhimdatta Municipality, 2065/66

The above table shows Bhaktapur municipality collect revenue from house rent tax (29.98 percent), roof top tax (23.59 percent) in total tax revenue are more than other tax and Bhimdatta municipality collect revenue from property tax (69.84 percent), business tax (11.63 percent) in total tax revenue are more than other taxes. Bhaktapur municipality collect tax revenue more than about 2 times from Bhimdatta municipality. It shows that Bhaktapur municipality is more strgenthness to mobilization of local resources than Bhimdatta municipality.

Share of Own Source Revenue and External Revenue in Total Revenue of All Municipalities

Total revenue is the sum of own source revenue and external revenue. The share of own source revenue and external revenue in total revenue of all municipalities is shown in figure below.

Figure 4.3: Share of Own Source Revenue and External Revenue in Total Revenue



Source: UDLE/LBFCS, (2055,2057,2066,2068,2069,2070,2071)

In above figure the trend of own source revenue of municipality increases smoothly up to fiscal year 2065/66 and beyond it revenue fluctuated. The revenue of municipality from external source is less than own source revenue up to F.Y. 2065/66 and beyond this the external revenue increased rapidly and exceed the own source revenue of municipalities. But after F.Y. 2068/69 external revenue starts to fall continuously and become less than own source revenue at F.Y. 2070/71.

The trend of total revenue of municipalities is increasing up to F.Y. 2067/68 and stars to fall beyond this. Up to fiscal year 2064/65 the total revenue increases smoothly when own source revenue also increases smoothly. Total revenue of municipalities increases rapidly from F.Y. 2064/65 to 2067/68 when the external revenue of municipalities increases rapidly i.e. the rapid increase in total revenue is due to the rapid increase in external revenue. Similarly the fall in total revenue is also to result of fall in external revenue of municipalities.

Here, when external revenue increased rapidly, it is seems that the own source revenue start to fall and become fluctuated. This is the serious phenomenon of this study. The reason behind this inverse relationship between the rapid increase in external revenue and fluctuate in own source revenue may be high grand provided by central body increases the dependency of local body to central they need not to collect revenue efficiently from their own source.

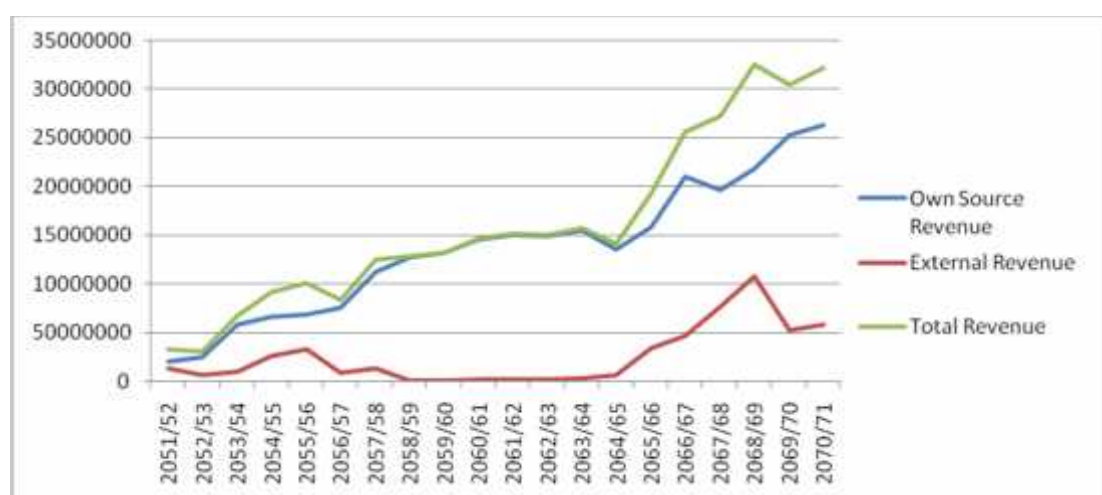
Above evidences shows that the fiscal decentralization can only work efficiently when all right of revenue collection and expenditure given to the local bodies rather than to provide the grand by central body to local bodies.

Share of Own Source Revenue and External Revenue in Total Revenue of Sample Municipalities

Case of Bhaktapur Municipality:

Bhaktapur Municipalities generated income from various internal sources like local tax, fee and fines, tourist service charge, land sale, property rent, royalty and other various sources similarly it generated income from external sources. The detail analysis of revenue generation for the last 20 years is included in annex 4.5 and average summary of revenue generation can be shown in following figure.

Figure 4.4: Share of Own Source Revenue and External Revenue in Total Revenue of Bhaktapur Municipality



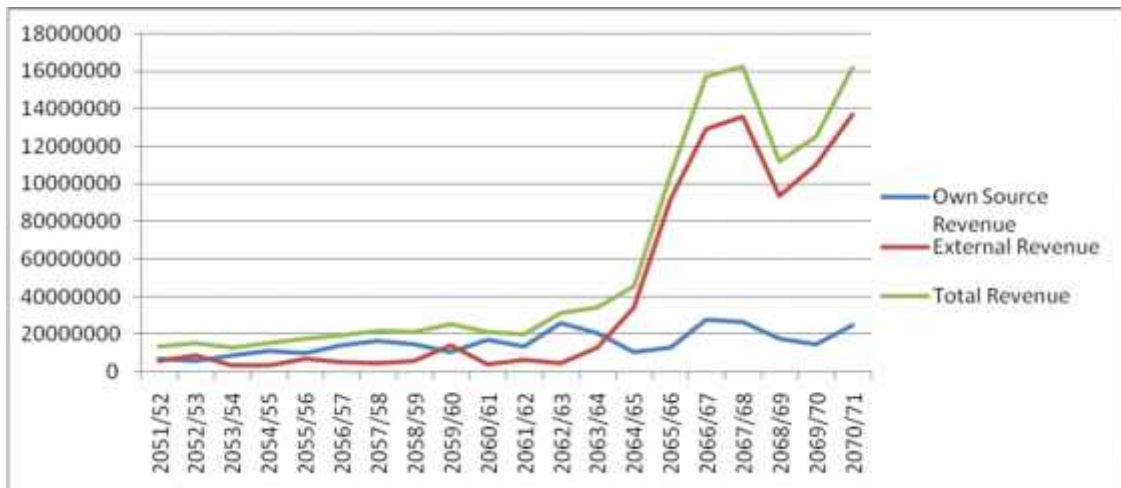
Source: UDLE/Bhaktapur Municipality

In above figure the total External revenue of Bhaktapur municipality is negligible level and nearly the total revenue is generated by the internal source. The average performance of twenty year shows that the most of the part of total revenue is covered by own source revenue which is about 89 percent in average and rest of 11 percent is covered by external sources. This indicates that Bhaktapur municipality is self sustained. The decentralization is effectively work in the Bhaktapur municipality.

Case of Bhimdatta Municipality:

Bhimdatt Municipalities generated income from various internal sources like local tax, fee and fines, property rent, tourist service charge, royalty and other various sources similarly it generated income from external sources. The detail analysis of revenue generation for the last 20 years is included in annex 4.6 and average summary of revenue generation of all municipalities can be shown in following figure.

Figure 4.5: Share of Own Source Revenue and External Revenue in Total Revenue of Bhimdatta Municipality



Source: UDLE/Bhimdatta Municipality

In above figure the own source revenue of Bhimdatta municipality up to F.Y. 2063/64 is higher than external revenue. The majority of total revenue is generated by own source revenue, which indicate that the effect of fiscal decentralization is positive. Beyond the F.Y. 2063/64 the share of internal revenue in total revenue is very low in comparison to the share of external revenue. The rapid increase in total revenue is all because of rapid increase in external revenue. The average performance of twenty year shows that the less than half part of total revenue is

covered by own source revenue which is about 49 percent in average and rest of 51 percent is covered by external sources.

Comparitive Study of Share of Own Source Revenue in Total Revenue

The comparative study of share of own source revenue in total revenue of all municipality, Bhaktapur municipality and Bhimdatta municipality is presented in the following figure.

Figure 4.6: Comparitive Study of Share of Own Source Revenue in Total Revenue



Source: UDLE/LBFCS/Bhaktapur & Bhimdatta Municipality

While we compare the share of own source revenue in total revenue, the share of own source revenue in total revenue of Bhaktapur municipality is higher than all municipality as well as Bhimdatta municipality. That is Bhaktapur municipality is performing betterly. The share of own source revenue in total revenue of Bhimdatta municipality is relatively lower than all municipality. That is performance of Bhimdatta municipality is poor in comparison to all municipality as well as Bhaktapur municipality. The some of municipalities are getting more advantages

from the fiscal decentralization policy where as some of other municipality are getting little benefits from this policy.

4.5. Expenditure Pattern of Local Bodies in Nepal

Local Bodies have assigned different expenditure responsibilities along with tax and non tax financial resources. The Local Self Governance Act, 2055 and Regulation, 2056 and Local Bodies Financial Administration Regulation (LBFAR), 2064 has provides task, function responsibilities and fiscal authorities to the VDCs, Municipality and DDCs for development activities and service delivery in local level. The Power, function and responsibilities of local bodies as per the LSGA, 2055 is presented in Annex 3

4.5.1. Expenditure Pattern of Municipality of Nepal

LSGA, 2055 provides of Functions, Duty, Power and responsibility of Municipalities. According to this Act, Regulation and timely to Nepal governments directives, municipalities are delivering public services and functioning development activities. Expenditure of municipalities is Capital Expenditure and Recurrent Expenditure. To perform development activities and to maintain those two expenditures, the main resources are; internal sources, revenue sharing, and grants from central level as well as non expenditure of previous year also included in these expenditures and it is maintaining current fiscal year plans and development through these expenditure. Total Expenditure of municipalities of all districts from fiscal year 2051/52 to 2070/71 included in table below:

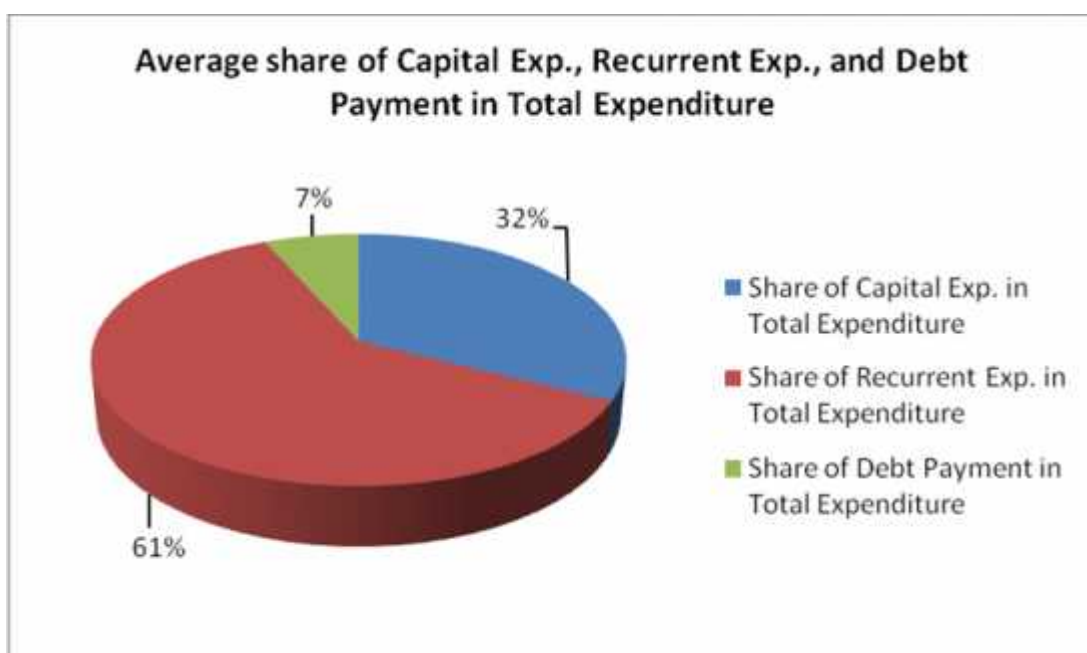
Table 4.4: Expenditure Patten of Municipality

Fiscal Year	Expenditure of municipality							
	Capital Expenditure	Recurrent Expenditure	Debt Payment	Internal Revenue	Total Expenditure	Share of Internal Revenue in Total Expenditure	Share of Capital Exp. in Total Expenditure	Share of Recurrent Exp. in Total Expenditure
51/52	277533454	501193001	1535775	688646829	780262230	88.26	35.57	64.23
52/53	325031283	567887720	18152102	742190013	911071105	81.46	35.68	62.33
53/54	363546300	514001732	26352769	806201849	903900801	89.19	40.22	56.86
54/55	576231765	762982710	44241707	1125003399	1383456182	81.32	41.65	55.15
55/56	619021824	737702206	34883913	1042301688	1391607943	74.90	44.48	53.01
56/57	683252332	912464511	37585897	1273033842	1633302740	77.94	41.83	55.87
57/58	801195745	1037116891	63716618	1512463821	1902029254	79.52	42.12	54.53
58/59	888346648	1210555909	62658910	1764736276	2161561467	81.64	41.10	56.00
59/60	783598889	916658241	66915746	1708109397	1767172876	96.66	44.34	51.87
60/61	835010503	1262663998	62478978	1765491127	2160153479	81.73	38.66	58.45
61/62	811450811	1838050418	76626536	1933536948	2726127765	70.93	29.77	67.42
62/63	843356247	1504154839	57780766	1867894020	2405291852	77.66	35.06	62.54
63/64	845620455	2216582540	68718786	1944632789	3130921781	62.11	27.01	70.80
64/65	947911573	2536107395	63533730	2107424945	3547552698	59.41	26.72	71.49
65/66	1192740152	3871244780	69960321	3262280986	5133945253	63.54	23.23	75.40
66/67	1473915000	4538217000	28196000	2569546000	6040328000	42.54	24.40	75.13
67/68	1534954000	5465549000	72757000	3112025000	7073260000	44.00	21.70	77.27
68/69	1902240000	4891475000	NA	2259818000	6793715000	33.26	28.00	72.00
69/70	1085472000	2471502000	NA	3365614000	6768701000	49.72	16.04	36.51
70/71	746195000	2589984000	NA	3782550000	6199924000	61.01	12.04	41.77
Average	876831199	2017304695	42804778	1931675046	3240714271	69.84	32.48	60.93

Source: UDLE/LBCFS, (2055,2057,2066,2068,2069,2070,2071)

Table 4.4 shows the expenditure pattern of municipality in Nepal. The total expenditure is divided into recurrent and capital expenditure. Salaries, allowances, travel and per diem, services, rent, repair and maintenance, office supplies, fuel, health supplies, financial asst. /donation, contingencies, other material, etc. are included in recurrent expenditure. Social programs (education, health, forestry, cultural /sports, disaster relief, financial assistance, miscellaneous), ordinary capital (furniture, vehicle, machinery equipment), capital investment (land/building purchase, building construction, town level projects, other development/construction) are included in capital expenditure. The data analysis from FY 2051/52 to 2070/71 shows that, the average capital expenditure is Rs 876831199.1 which is 32.48 percent of total expenditure. The highest capital expenditure is 44.48 percent in the FY 2055/56 and the lowest capital expenditure is 21.70 in FY 2067/68. The average recurrent expenditure is Rs 2017304695, which is 60.93 percent of total expenditure. The highest recurrent expenditure is 77.27 in FY 2067/68 and the lowest recurrent expenditure is 51.87 in FY 2059/60. Similarly, the share of internal revenue in total expenditure is 69.62 percent in average.

Figure 4.7: Share of capital exp., recurrent exp. and debt payment in Total expenditure



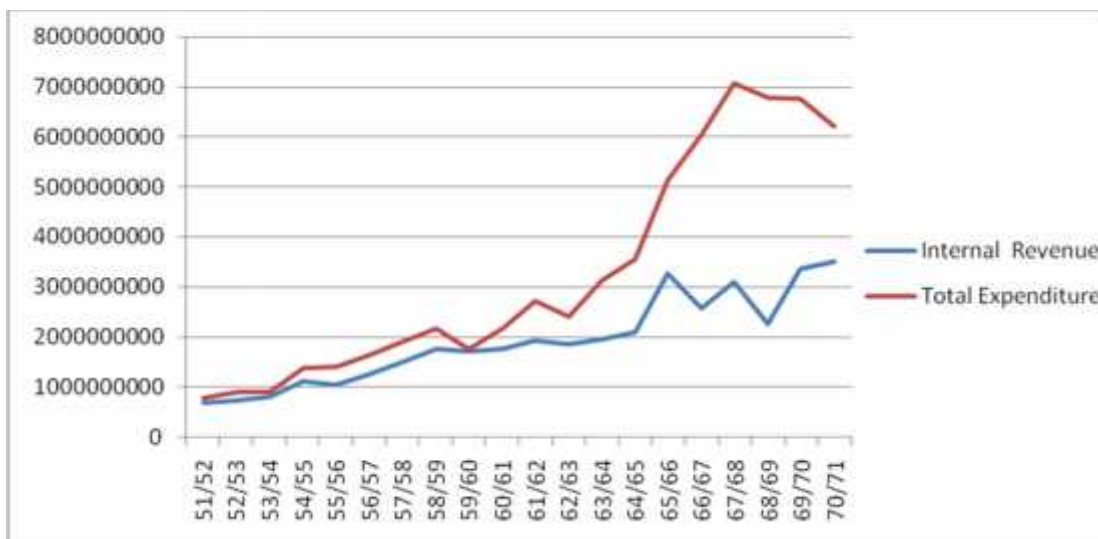
Source: UDLE/LBFCS, (2055,2057,2066,2068,2069,2070,2071)

The above figure shows that an average 61 percent expenditure in recurrent and 32 percent expenditure in capital expenditure and 9 percent in debt payment from total expenditure of municipalities in Nepal.

Share of Own Source Revenue to Total Expenditure of All Municipalities

The share of own source revenue in total expenditure is another important component to find out that whether municipalities are able to meet the expenditure or not. The share of own source revenue in total expenditure of all municipalities can be shown in the following figure.

Figure 4.8: The share of own source revenue in total expenditure of all municipalities



Source: UDLE/LBFCS, (2055,2057,2066,2068,2069,2070,2071)

Figure 4.8 shows that in initial years up to F.Y. 2064/65 municipalities are able to cover the large part of their total expenditure by their own source revenue. After F.Y. 2064/65 the gap between total expenditure and own source revenue increases rapidly. The average share of own source revenue in total expenditure of twenty year is about 70 percent, and rest of 30 percent share is of external revenue.

That is the large part of total expenditure is fulfilled by external source rather than own source revenue. The cause behind that may the central body increases grant to local level and also the local bodies are unable to collect own source revenue.

Share of Own Source Revenue in Total Expenditure of Bhaktapur Municipality

The share of own source revenue in total expenditure of Bhaktapur Municipality to find out that wither municipality is able to meet the expenditure or not. The share of own source revenue in total expenditure can be shown in the following figure.

Figure 4.9: The share of own source revenue in total expenditure of Bhaktapur municipality



Source: UDLE/Bhaktapur Municipality

Above figure of Bhaktapur municipality is depicts relatively better scenario. Up to fiscal year 2065/66 there seems the own source revenue alone is greater than the total expenditure. After F.Y. 2065/66 the total expenditure exceed by little portion to the own source revenue.

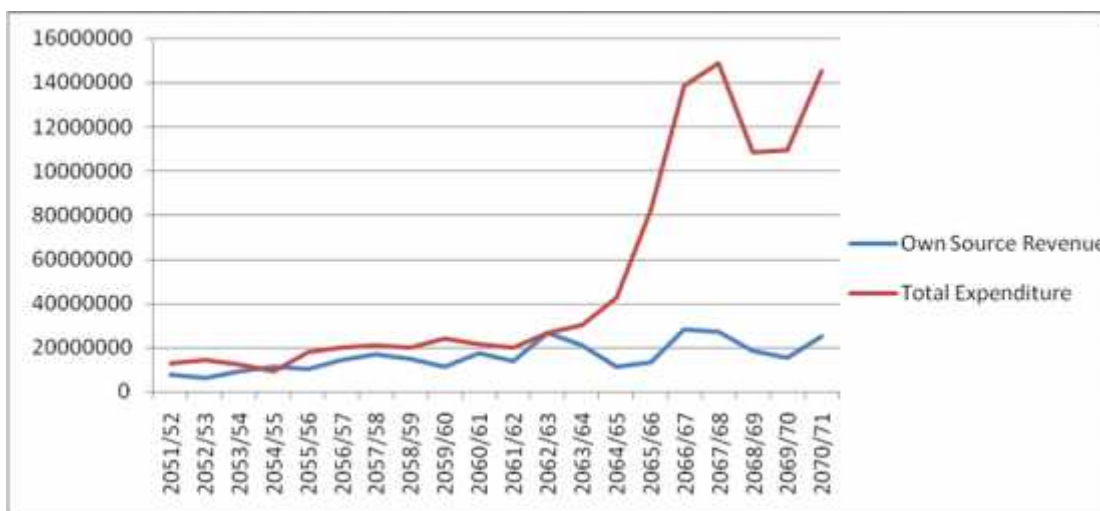
The average share of own source revenue in total expenditure of twenty year of Bhaktapur municipality is about 97 percent, and rest of 3 percent share is of external revenue.

Data presented above shows that the local resource is mobilized effectively. In case of Bhaktapur municipality the fiscal decentralization policy play the vital role in local resource mobilization.

Share of Own Source Revenue in Total Expenditure of Bhimdatta Municipality

The share of own source revenue in total expenditure of Bhimdatta Municipality to find out that wither municipality is able to meet the expenditure or not. The share of own source revenue in total expenditure can be shown in the following figure.

Figure 4.10: The share of own source revenue in total expenditure of Bhimdatta municipality



Source: UDLE/Bhimdatta Municipality

The above figure shows that total expenditure of Bhimdatta municipality is greater than own source revenue but the own source revenue is near to total revenue up to fiscal year 2064/65 and beyond this total expenditure increases rapidly but the own source revenue remains same as previous. The average share of own source revenue in total expenditure of twenty year of Bhimdatta municipality is about 31 percent, and rest of 69 percent share is of external revenue. This makes large gap between the total expenditure and own source revenue. In general the aggregate performance of Bhimdatta municipality is not satisfactory.

Expenditure Pattern of Bhaktapur and Bhimdatta Municipality

The expenditure of municipalities is included in capital expenditure and recurrent expenditure to perform development activities and to delivering public services and functioning. Recurrent expenditure includes salary, welfare fund, allowance, travel and per diem, uniform, stationary, maintains office supplies, etc. Capital expenditure includes land and building purchases exp., furniture, vehicle, machinery tools and

other equipment, building construction, investment in education, health, cultural, road, disaster, grants, etc. The expenditure in these sectors of Bhaktapur and Bhimdatta municipality in fiscal year 2065/66 are detail in the following table.

Table 4.5: Expenditure of Bhaktapur and Bhimdatta municipality of fiscal year 2065/66

Heading	Bhaktapur Municipality	Share in Total Expenditure	Bhimdatta Municipality	Share in Total Expenditure
RECURRENT EXPENDITURE	96292730	55.48	13350044	36.52
Staff Salary	23539223	13.56	8761955	23.97
Member Salary		0.00	27075	0.07
Welfare Fund	4000000	2.30	700000	1.91
Insurance Premium Expenditure	804000	0.46	279559	0.76
Staff Allowance	3350579	1.93	41327	0.11
Meeting Allowance	45000	0.03	82600	0.23
Travel and Per Diem	157693	0.09	227690	0.62
Uniform	1757940	1.01	184489	0.50
Food Allowance		0.00	103600	0.28
Health Treatment	86681	0.05	387184	1.06
Training Program		0.00	32699	0.09
Water and Electricity Expenditure	850345	0.49	167438	0.46
Telephone Expenditure	671457	0.39	96872	0.26
Office Supplies	817197	0.47	734753	2.01
Rent	30000	0.02		0.00

Repair and Maintains	777185	0.45	174001	0.48
Fuel	590013	0.34	248353	0.68
Councillng Fee	161000	0.09		0.00
Contingences		0.00	172947	0.47
Membership Fee		0.00	50000	0.14
Economic Aid	19175	0.01	65823	0.18
Grant to Public Organization		0.00	699650	1.91
Other Expenditure	386253	0.22	77399	0.21
Stationary	153591	0.09	34630	0.09
Sanitation and Other Service Expenditure	58095398	33.47		0.00
CAPITAL EXPENDITURE	77258783	44.52	23208702	63.48
Land Purchases Expenditure	2248681	1.30		0.00
Building Purchases Expenditure		0.00		0.00
Furniture	28225	0.02		0.00
Vehicle	738149	0.43	36670	0.10
Machinary Tools and Other Equipment	50850	0.03	102630	0.28
Building Construction	1500000	0.86	3622000	9.91
Public Construction Expenditure	20006762	11.53		0.00
Ward Budget		0.00	2864165	7.83

Expenditure				
Investment	10000000	5.76		0.00
Education	38254165	22.04	150260	0.41
Health Treatment	2171951	1.25	1996627	5.46
Road	2000000	1.15	14436350	39.49
Administration Grant	260000	0.15		0.00
Governance Reform Program		0.00	196453	0.54
Other Expenditure		0.00	5107481	13.97
Total	173551513		36558746	

Source: Bhaktapur/Bhimdatta Municipality, 2065/66

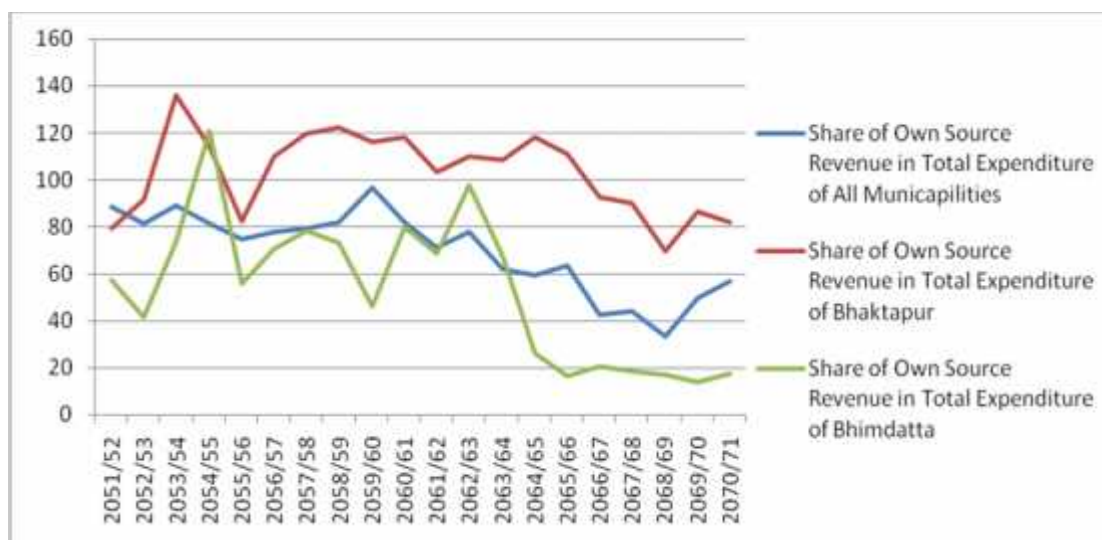
The recurrent expenditure of Bhaktapur municipality is about 55 percent in total expenditure and Bhimdatta municipality is about 37 percent in total expenditure. The recurrent expenditure of Bhaktapur municipality is quite higher than Bhimdatta municipality, which is not good for Bhaktapur municipality. The maximum expenditure is goes on salary for the both municipality.

Similarly, capital expenditure of Bhaktapur and Bhimdatta municipality is about 45 percent and 63 percent of total expenditure. Capital expenditure of Bhimdatta municipality is higher than Bhaktapur municipality, which is good for Bhimdatta municipality to build capital formation. Bhaktapur municipality should be reducing recurrent expenditure and increase capital expenditure.

Comparitive Study of Share of Own Source Revenue in Total Expenditure

The comparitive study of share of own source revenue in total expenditure of all municipality, Bhaktapur municipality and Bhimdatta municipality is presented in the following figure.

Figure 4.11: Comparative study of share of own source revenue in total expenditure



Source: UDLE/LBFCS/Bhaktapur & Bhimdatta Municipality

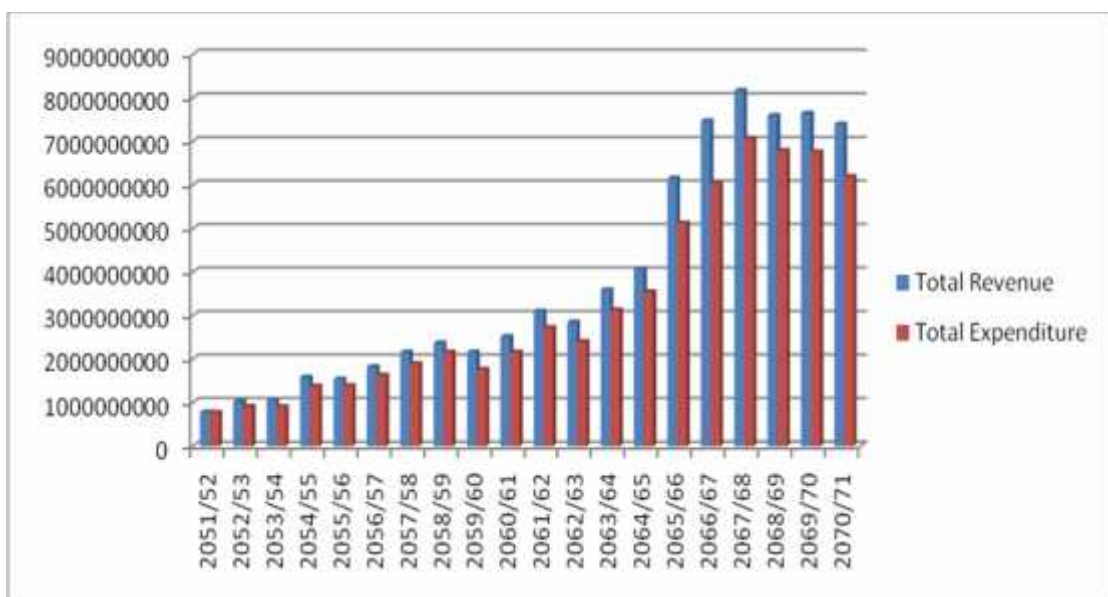
While we compare the share of own source revenue in total expenditure, the share of own source revenue in total expenditure of Bhaktapur municipality is higher than all municipality as well as Bhimdatta municipality. That is Bhaktapur municipality is performing betterly. The share of own source revenue in total expenditure of Bhimdatta municipality is relatively lower than all municipality. That is performance of Bhamdatta municipality is poor in comparision to all municipality as well as Bhaktapur municipality. The some of municipalities are getting more advantages from the fiscal decentralization policy whare as some of other municipality are getteing little benefits from this policy.

Data presented above shows that the local resource is mobilized effectively in some of the municipality but in some of others is not effective. In case of Bhaktapur municipality the fiscal decentralization policy play the vital role in local resource mobilization, where as in case of Bhimdatta municipality the fiscal decentralization policy is not much effective in overall.

Comparison between Total Revenue and Total Expenditure of All Municipalities

What is the status of total revenue and total expenditure? It is another important part of the study. The status of total income and total expenditure is shown in following figure.

Figure 4.12: Comparison between Total Revenue and Total Expenditure of All Municipalities



Source: UDLE/LBFCS,(2055,2057,2066,2068,2069,2070,2071)

Above figure shows that in all fiscal year, the total revenue is greater than total expenditure. Municipalities are able to spend about 86 percent of total revenue and rest of 14 percent is unable to spend. This indicates that municipalities are unable to expend all revenue generated from various sources. That is, municipalities are unable to full utilize their resources, which made the speed of development slower.

CHAPTER V

MAJOR FINDING, CONCLUSION AND RECOMANDATIONS

5.1. Findings

This paper focuses on fiscal decentralization policy and local resource mobilization nexus in Nepal. Moreover, it identifies the revenue generation pattern and trend as well as expenditure pattern of local bodies.

Based on the secondary data, two sample municipalities are selected in order to exploit the objectives. The approach is descriptive and analytical as well. Findings of this paper are listed in the table below:

Major Findings

More than half (about 61 per cent) of total revenue of local bodies is generated themselves and the rest portion (39 per cent) is attributed by external sources such as grants, borrowing etc. The majority of the local revenue incorporates local taxes which is 64 per cent of total revenue generated by the local bodies whereas 24 per cent revenue depends on fees and fines. On the other hand, property rental tax contributes approximately 4 per cent in total revenue generated by the local bodies and approximately 8 per cent share depends on other sources.

In the case of Bhaktapur municipality, most share of locally generated revenue is about 89 percent in average and rest portion depends on external sources. In case of Bhimdatta municipality, less than the half part of total revenue internally created and out sourcing revenue is more than half of total revenue approximately 49 per cent and 51 per cent respectively.

Total revenue Bhaktapur municipality is about 4 times greater than to revenue of Bhimdatta municipality. Similarly, Bhaktapur municipality collect tax revenue more than about 2 times from Bhimdatta municipality.

The comparative study shows that Bhaktapru municipality's performance is better than that of Bhimdatta municipality. The share of recurrent expenditure in total expenditure of all municipalities is about 61 percent, share of capital expenditure is about 32 percent and rest of share 7 percent is of debt payment.

The average share of own source revenue in total expenditure of twenty year of all municipalities is about 70 percent, and rest of 30 percent share is of external revenue.

The average share of own source revenue in total expenditure of twenty year of Bhaktapur municipality is about 97 percent, and rest of 3 percent share is of external revenue.

The average share of own source revenue in total expenditure of twenty year of Bhimdatta municipality is about 31 percent, and rest of 69 percent share is of external revenue.

The comparative study shows that Bhaktapru municipality's covering all most all expenditure which is better than that of Bhimdatta municipality.

Municipalities are able to spend about 86 percent of total revenue and rest of 14 percent is remained unspent.

5.2. Conclusion

Fiscal decentralization enhances the capability of local body, capitalizes financial resources, and also promotes local services as well as increases effectiveness of public services delivery through participatory approach. It betters the access of

general public to the government entities and services which ultimately develops ownership of development agendas by the local people.

Fiscal decentralization, or devolving the revenue resource and expenditure functions to lower tiers of government. It is seen as part of a reform package to improve efficiency in the public sector, to increase composition among local governments in delivering the public service. By bringing the government closer to the people, fiscal decentralization is expected to boost public sector efficiency, as well as accountability and transparency in policy-making.

The evidence supported by this study is that fiscal decentralization policy has positive impact on both revenue generation and resource mobilization process. The performance of some municipalities like Bhaktapur is so better; however, other municipalities have relatively poor performance. But, in average the performance of all municipalities is satisfactory.

When external revenue increased rapidly, it is seems that the own source revenue start to fall and become fluctuated. This is the serious phenomenon of this study. The reason behind this inverse relationship between the rapid increase in external revenue and fluctuate in own source revenue may be high grant provided by central body increases the dependency of local body to central they need not to collect revenue efficiently from their own source.

The evidence shows about 69 percent of total expenditure is covered by own source revenue and rest of 31 percent is envelops by external sources like grants, borrowing etc. But, municipalities are unable to fully utilize their revenue.

There are various constraints that disturb the municipalities to work efficiently. The election of local level has not held from 2054, so that local level is functioning without people's representatives. The full authorities have not given by central level

to local bodies. There is lack of capacity of planning and decision making of bureaucracy of local body. Various policies are still in favor of centralization even after LSGA, 2055 and LSGR 2056. There is lack of effective implementation and monitoring of development activities. Similarly there is lack of proper utilization of available resources and also lack of distribution of available resources in the basis of justice and equity.

Despite these constraints, overall performance of municipalities is indifferent. And, this assures relative success of fiscal decentralization policy in Nepal.

5.3. Recommendations

Theoretical decentralization is to make local decision and directives effective in local intuition through the representatives of local people. It is also effective way to deliver public services through the channels of representative. But practically in Nepal the election of local level has not held from 2054, so that local level is functioning without people's representatives from 2059, which violates the principle of no taxation without representatives. Hence, it is only need to organize election of local level as soon as possible and make it function through representatives of people.

There is no proper utilization of available resources so there is seems always income is greater than expenditure. There is need of proper and efficient utilization of available resources to lead the rural area to the way of development.

Local bodies are unable to generate sufficient revenue due to lack of tax rate and tax base authority given to them, central body provide them the authority so that they can increase or reduces tax rate and tax base. The expenditure needed to local level should be collected from local level itself through maximum and proper utilization of local resources. To do all proper mechanism should be made.

There is need to identify new source of revenue of local bodies to increase their own source revenue, so that they can able to meet their total expenditure form their own sources.

Still there is lack of authority to local bodies to make decision about various planning and allocation of resources. So, central body should have to provide the full authority to local bodies.

Fiscal decentralization can only work efficiently when all right of revenue collection and expenditure given to the local bodies rather than to provide the grand by central body to local bodies

Stakeholders of local bodies are unable to make proper plan and employment that. So, there is need of improvement the capacity of stakeholders.

Without people's representatives, local levels are functioning through parties' local structure. Nepalese political party's organization and functions are not transparent so that working of local level is not going smoothly. So that there should be created transparent party organization.

In Nepal, local bodies are not able to generate revenue; they are dependent on the central level government grant. For the strengthening of fiscal decentralization process, capacity building of the local body to enhance and internalize the role and responsibilities to collect local resources and make them accountable should be done.

Financial decentralization is mainly a concept of delivering a work function with clear responsibility, financial support and resources to fulfill those functions and responsibilities. As well it transfers the rights and authority to receive resource, to do financial decision and work responsibility to the local level. There is need to

provide following right by central body to local bodies so that they can perform
bitterly;

1. To transfer responsibility with provision of expenditure
2. Revenues rights.
3. Transference of intergovernmental finance.
4. Loan management
5. Service delivery etc.

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ANNEX 4.1

The Source of Revenue of VDCs, Municipalities and DDCs

Resource	VDCs	Municipalities	DDCs
Tax	<ul style="list-style-type: none"> -House and land tax -Land revenue and tax -Hat Bazaar Pasal tax -Rent tax -Vehicle tax -Entertainment tax -Professional tax -Advertisement tax -Natural resource utilization tax -Commercial video tax -Other tax 	<ul style="list-style-type: none"> -House and land tax -Vehicle tax -Entertainment tax -Rent tax -Advertisement tax -Professional tax -Property tax -Commercial video tax 	<ul style="list-style-type: none"> -Infrastructure (road, bridge, irrigation, etc) -Wool, solvent extraction, herbs dry grass (bankes), Kabadi (reusable solid waste) boulders, slate, sand, animal bone, horn, feather, hyde (export tax)
Service Charge	<ul style="list-style-type: none"> -Sanitation-use of drainage -Tourist site entrance fee -Park, garden, view tower -Fee for entertainment like magic, circus etc. -For recovering dues for others 	<ul style="list-style-type: none"> -Parking fees -Water supply, electricity, tap, public telephone fee -Solid waste, sanitation, sewerage fee -public lavatories, park, bathroom, 	<ul style="list-style-type: none"> -Road bridge, irrigation canal, pond -Guest house, library, medical centre, inn, community hall -Canal, water source (irrigation), embankment -Local development

		swimming pool, gymnasium, guest house, tourist site, hostel, haat bazaar. Slaughter house, crematorium, use of washing space, street light, road, drainage maintenance. -valuation of real estate (fixed assets)	fee
Fees	-Television, video and other equipment license fee -Approval fee -Recommendation fee	-Approval and recommendation fee -Approval of building design fee -Attestation of maps fee	-River rafting, boat, tuin, fishing permission, and renewal -Registration and renewal fee for water bank -Recommendation fee -Other
Sales	-Soil from fallow govt. land -Product from public pond-orchard		-River sand, aggregates, boulders, slate, soli, swept away wood

	<ul style="list-style-type: none"> -VDC property -Dry wood, fire wood, branches roots -Grass (khar) 		
Loan	-Loans from bank or other institution with approval from council, with or without collateral and on Government guarantee	-Loans from bank or other institution with approval from council, with or without collateral and on Government guarantee	-Borrowing from bank or other institutions with or without collateral with approval from District council and on Government guarantee

Sources: Government of Nepal, LSGA, 2055 and LSGR, 2056

ANNEX 4.2

List of Municipality in Nepal

Attariya	Gadhinmaee	Dhangadhi	Beltarbasaha	Lahan
Ananteshwar	Ghodaghodi	Dhangadhimai	Beshisahar	Lalbandi
Api	Ghorahi	Dhanusadham	Bhajanitrishakti	Laligunrasa
Amargadhi	Chandrapur	Dharan	Bhadrapur	Libanga
Aanbukhairenee	Chandragiri	Nagarjun	Bharatapur	Lekhanatha
Itahari	Charnath	Narayan	Bhanu	Letangabhagateni
Inaruwa	Changunarayan	Narayani	Bhimeshwar	Walin
Eelam	Chapakot	Nijgada	Bhimdatta	Biratnagar
Eeshwarpur	Chitrawan	Nilakantha	Bhirkota	Birgunja
Urlabari	Chainpru	Nepalgunja	Bhrikuti	Birendranagar
Katari	Chautara	Patharishanischare	Bheriganga	Beldandi
Kankaee	Chaurajahari	Parashuram	Bherimalika	Byasa
Kanchanpur	Janakpur	Panchakhal	Bhojpur	Shankharpur
Kapilbastu	Jayaprithbi	Pakhibasa	Mangasen	Shamvunatha
Kamalbajar	Jaleshwar	Patan	Madhyanepal	Shaniarjuna
Kamalamaee	Jiri	Palumtar	Madhyabindu	Sharada
Karaputar	Jhalariplari	Putalibajar	Manthali	Shivraj
Kalaiya	Tikapur	Punarbasa	Malanguwa	Shabasatakshi
Kageshwarim	Tokha	Pokhara	Mahagadhimaee	Shuklagandaki
Kathmandu	Tansen	Pokhariya	Mahamanjushree	Subhaghatagamala
Karyabinayak	Taplejunga	Pyuthan	Mahalakshmi	Sadananda
Kalika	Tarakeshwar	Phidim	Madi	Saptakoshi
Kawasoti	Tilottama	Bajrabarahi	Madi	Sabaila

Kashinkhada	Tulsiapur	Badhimalika	Mithila	Saphebagar
Kushma	Tripur	Bandipur	Michaiya	Sanoshreetaratal
Krishnanagar	Triyuga	Babaee	Mushikota	Siddharthanagar
Krishnapur	Thaha	Baeahathawa	Mechinagar	Siddhicharan
Kolhabi	Dakshinakali	Bardaghat	Melamchi	Simrongadha
Koshiharaicha	Damak	Bardibasa	Myanlunga	Siraha
Kohalpur	Dasharathchand	Bansagadhi	Rangeli	Sukhipur
Khandawari	Diktel	Bagachaura	Raeenasa	Sunwal
Khairahanee	Dipayalsilgadhi	Bagluna	Rajbiraj	Sundardulahi
Garuda	Dudhakunda	Banaganga	Rajapur	Sundarbajar
Gulariya	Dudhauri	Bidur	Rapti	Suryabianayak
Gaidakot	Dullu	Birtamod	Ramgram	Suryabianayak
Gokarneshwar	Duhawibhaluwa	Butawal	Ramdhunibhasi	Suryodaya
Godawari	Deumae	Budhanilkantha	Rampur	Sainamaina
Gorkha	Dewachuli	Buddhabatika	Ramechhap	Hanumanagar yoginimae
Golabajar	Debadaha	Bedkota	Resunga	Hetauda
Gaur	Dodharachadani	Beni	Lamahi	
Gauradaha	Dhankuta	Belwari	Lamkichuha	
Gaushala		Belauri	Lalitapur	

Source: Ministry of Federal Affairs and Local Development, 2016

ANNEX 4.3.

Functions and Responsibilities of Local Bodies

Village Development Committee (VDC)	Municipality	District Development Committee (DDC)
Agriculture	Finance	Agriculture
Rural drinking water	Physical Development	Rural Drinking Water and Habitation Development
Work and Transport	Water resource, Environment and Sanitation	Hydropower
Education and Sports	Education and Sports development	Work and Transport
Irrigation, Soil-erosion and River control	Culture	Land reform and Management
Physical development	Work and Transport	Women's development and Handicapped
Health services	Health services	Forest and Environment
Forest and environment	Social welfare	Education and Sports
Language and Culture	Industry and Tourism	Labour wage
Tourism and Cottage industry	Approval of building design	Irrigation, Soil-erosion and River control
Miscellaneous	Miscellaneous	Information and Communication

	Optional works	Language and Culture
		Cottage industries
		Health services
		Tourism
		Miscellaneous

Sources: Government of Nepal, LSGA, 2055

ANNEX 4.4

Revenue generate from own source revenue by Municipalities

Fiscal Year	Local Taxes (a)	Fees and Fines (b)	Property Rental ©	Other Revenue (d)	Own Source Revenue (a+b+c+d)
51/52	611513738	45551882	23203792	8377417	688646829
52/53	658022276	47103679	26528905	10535153	742190013
53/54	686095292	65241280	34935503	19929774	806201849
54/55	984344399	78625443	39650431	22383126	1125003399
55/56	872709942	90448496	46059314	33083936	1042301688
56/57	1053194316	141763777	50213898	27861851	1273033842
57/58	1166447435	256038082	57181050	32797254	1512463821
58/59	1368168356	246523419	67588959	82455542	1764736276
59/60	1248412577	323702339	78648465	57346016	1708109397
60/61	1237435519	359549258	82665692	85840658	1765491127
61/62	1347349751	408827853	90147893	87211451	1933536948
62/63	1331177444	385287858	79058971	72369747	1867894020
63/64	1371625883	443161211	86298380	43547315	1944632789
64/65	1439317720	510093850	107072157	50941218	2107424945
65/66	2447588857	643969207	97555450	73167472	3262280986
66/67	1863753180	538254475	98773528	68764817	2569546000
67/68	1269942000	1089850000	99560000	652673000	3112025000
68/69	927198000	910361000	51630000	370629000	2259818000
69/70	1277504000	1357554000	93502000	637054000	3365614000

70/71	1527055000	1293164000	105850000	856481000	3782550000
Average	1234442784	461753555	70806219	164672487	1931675046
In Percentage	63.91	23.90	3.67	8.52	

Source: UDLE/LBFCS,(2055,2057,2066,2068,2069,2070,2071)

ANNEX 4.5

Revenue and Expenditure of Bhaktapur Municipality

Bhaktapur Municipality					
Fiscal Year	Own Source Revenue	External Revenue	Total Revenue	Total Expenditure	Share of Own Source Revenue in Total Revenue
2051/52	20058685	13050327	33109012	25340487	60.58
2052/53	24615243	6157386	30772629	26808533	79.99
2053/54	58377597	9539375	67916972	42877002	85.95
2054/55	65904004	26068429	91972433	57611575	71.66
2055/56	68441316	32427512	100868828	83056623	67.85
2056/57	75743221	8439989	84183210	68769456	89.97
2057/58	112102782	13018824	125121606	93525636	89.60
2058/59	127296583	842014	128138597	103923528	99.34
2059/60	131671607	400000	132071607	113312290	99.70
2060/61	145318895	1454000	146772895	122884146	99.01
2061/62	149784915	1416700	151201615	144486064	99.06
2062/63	148472307	1362900	149835207	134785960	99.09
2063/64	154488217	2974683	157462900	142137500	98.11
2064/65	135073625	5711216	140784841	114387823	95.94
2065/66	158716118	33859686	192575804	143051513	82.42
2066/67	209439533	46391254	255830787	225863212	81.87
2067/68	195966160	76139166	272105326	216938938	72.02

2068/69	217485000	107585000	325070000	312090000	66.90
2069/70	252142000	52051000	304193000	291608000	82.89
2070/71	262902000	58410000	321312000	321290000	81.82
Average					85.19

Source: udle/Bhaktapur Municipality

ANNEX 4.6

Revenue and Expenditure of Bhimdatta Municipality

Bhimdatta Municipality					
Fiscal Year	Own Source Revenue	External Revenue	Total Revenue	Total Expenditure	Share of Own Source Revenue in Total Revenue
2051/52	7451505	5825269	13276774	13013801	56.12
2052/53	6078672	9010229	15088901	14690203	40.29
2053/54	9080396	3832803	12913199	12333995	70.32
2054/55	11404895	3656179	15061074	9443085	75.72
2055/56	10162863	7478724	17641587	18290355	57.61
2056/57	14167290	5178668	19345958	19994054	73.23
2057/58	16658309	4888172	21546481	21313988	77.31
2058/59	14766863	6245569	21012432	20118347	70.28
2059/60	11097193	14199236	25296429	24119571	43.87
2060/61	17200606	4311580	21512186	21503249	79.96
2061/62	13638127	6554227	20192354	19929232	67.54
2062/63	26461565	4571764	31033329	27011327	85.27
2063/64	20627322	13416178	34043500	30479347	60.59
2064/65	11114019	34467921	45581940	42405385	24.38
2065/66	13278467	91618518	104896985	82394025	12.66
2066/67	28018808	128871137	156889945	138576199	17.86
2067/68	26989601	135466723	162456324	148645314	16.61

2068/69	18115598	93691970	111807568	108426487	16.20
2069/70	15067000	109905000	124972000	109206000	12.06
2070/71	25014965	136816943	161831908	145104698	15.46
Average					48.67

Source: udle/Bhimdatta Municipality