
The Strategic Reforms in Budapest, 1990-2000

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THE HUNGARIAN LOCAL GOVERNMENT SYSTEM

The 1990. Hungarian Act on Local Governments was created on the basis of the major values and principles of the Council of Europe's European Charter of Local Self-Governments. The locally elected governments have their own assets and their own revenues that are supplemented by revenues from the central government. They are basically public service entities to which obligatory tasks are assigned, while they can also undertake voluntary tasks. They have the right to associate. They have considerable decision-making power. Decisions of local governments can be overridden only by the decision of a court in the case of violation of law or by the Constitutional Court.

Table 1: Expenditure of the Public Sector in Hungary

YEAR	PUBLIC EXPENDITURE (as % of GDP)	LOCAL EXPENDITURES (as % of GDP)	LOCAL EXPENDITURES (as % of Public expenditure)
1994	54.0	16.8	26.7
1995	44.7	14.1	26.6
1996	40.5	13.3	27.2
1997	39.0	12.0	25.5

Source: Hermann, Horváth, Péteri, Ungvári, Önkormányzatok feladattelepítésének szempontjai és feltételei, 1998

In Hungary the local governments are organized by settlements. They have the general responsibility for the basic local public services. Beside this, as a weak middle tier, county governments are also elected for subsidiary functions. I.e. for services that the settlements are not capable to perform or are of regional character. Local governments have mandatory services and can overtake by choice any optional services as long as they do not endanger the supply of mandatory services. The parliament defines the mandatory services and it has to allocate the necessary financial resources for their fulfillment. As local government sizes and capabilities strongly differ, there is a sub-group of mandatory services that must be supplied by all local governments, and there are some other services that are assigned to governments with greater capacities.

Table 2: Rights and Responsibilities of Local Governments in Hungary

RESPONSIBILITIES	RIGHTS
Development planning, Master Planning and urban regulation	Political independence
Protection of the natural and built environment	Property transferred
Transport and Public works	Annual revenue transfer
Cemeteries, fire brigades and public security	Shared revenues
Management of housing	Normative grants
Education and Culture	Targeted- and aimed revenues
Social and Health Care	Own-source revenues:
Others	Local tax and user charges
	Other incomes
	Loans and bond issuing

Local governments can freely select the forms of their service delivery. They can provide services by their own budgetary institutions, they can contract the private sector or utilize any alternative form of service delivery. (i.e. privatization, out sourcing, concessions, etc)

The rights and responsibilities of local governments are exercised by the elected body of representatives. The local government has an office as well who is responsible for preparatory and administrative tasks. The government can autonomously decide about the organizational structures and rules of procedures.

Operation of local governments is financed by own revenues, shared revenues (PIT and vehicle tax) and normative grants. Own revenues are the local tax revenues, user charges and fees collected by the local governments. Municipal governments can levy taxes on property, tourism and turnover of businesses. They can set tax and other revenue rates within the limits given by the central government.

Other own revenues of local governments are from profits, dividend yield, leasing fees and sale of assets. For capital investments aimed and targeted subsidies can also be tendered from the central government.

The Act on Local Governments includes the right of borrowing and bond issuing, but at the same time sets the limit of annual commitment of debt service. The borrowing limit is pegged to a specific portion of own-source revenues.

Table 3: Distribution of Local Government revenues in Hungary (%)

REVENUES	1997	1998
Own source revenues	23.4	22.6
Shared revenues	12.1	14.6
Grants	29.2	31.7
Capital Investment Financing	15.5	10.3
Transfers from Social Security Fund	16.9	17.5
Others	2.9	3.3
TOTAL	100	100

Source: Edit Nyitrai Kuzstosné, ed.: A helyi önkormányzatok és pénzügyeik, 1998

THE REFORM PROCESS IN BUDAPEST

1990 Act on Local Governments stipulated strong decentralization, creating the possibilities for independence of local governments. During the 1990s the major challenge facing the newly elected local leadership was to use the frame created by the Act to transform the inherited, socialist type local council into an autonomously functioning local government.

The old era meant a hierarchical structure, with the local council functioning as a de-concentrated unit of the state. Different fields of local activities were vertically connected to line ministries and local planning was more functioning as a tool of lobbying for central subsidies, than a comprehensive activity. The new era gave the possibility for real local planning, i.e. local aggregation of policies for better synergy of activities and for improved developmental outcomes. To exploit the possibility given by the new, decentralized framework for the benefit of the city a comprehensive process of interior reforms had to be conducted to make the local government capable to independently plan, elaborate and implement strategies.

The goal of reforms was clear from the beginning: (1) financial independence had to be strengthened by the increase of own revenues to create the basis for decision making independence, (2) the service delivery and management had to be reorganized to create a sustainable and planable system and (3) the administrative and decision making procedures had to be renewed to create a system conducive to the elaboration and implementation of coordinated, strategic policies. The goals for the reforms were set relatively early and clearly. The process of the implementation of the reforms was less foreseeable than the goals, as possible timing of the introduction of different reform elements has always been dependent on the maturity of the existing system and the actual political context.

In Budapest the leading force of the whole reform process was the financial reform. It was the restructuring of financing that led the reorganization of procedures and supplied better understanding of the capabilities of the Municipality. Results of the financial forecasting and planning and the realization of the limited margin of maneuverability was twofold: (1) it helped to clarify public roles and focus local government activities to these roles; (2) it pushed sectoral and development thinking towards strategic policies and towards more active and demand oriented policies.

In 1990 the Municipality inherited the institutions and development plans of the socialist council. The institutions had problematic infrastructure and the traditional "base financing"

system, the development concepts were mostly individual sector plans with extensive lists of all possible interventions. The council discussed new projects when elaborated and after approval the new project could be added to the existing list. This procedure was logical during the old communist regime, as a larger local "wish list" could increase the possibility to get financing from different parts of the centralized budget.

In the new situation aggregation and decision had to happen at the local level. For this a comprehensive budget and its comparison to forecasted financial capacities had to be elaborated. The reorganization of the capital budget was the first, decisive step to better local planning in Budapest. The Municipality could elaborate the first Two-Years Capital Investment Plan (CIP) in 1993 after long negotiations and revisions on earlier sector plans and established a gradual and adjusted decision making process for the elaboration of new projects. Thus capital expenditure planning became better regulated, but reform capabilities and political conditions were not mature yet to the more complicated task of reforming the financing of operation.

The second election term (1994-98) brought the more comprehensive reform. Through the introduction of a seven-years financial forecasting and planning model the structural deficit of the budget could be demonstrated and wider understanding could be developed for a financial strategy leading to sustainable stability. Then, in 1995, a short-term financial crisis could be exploited by the leadership of the Municipality to build the necessary coalition for launching major privatization transactions and for the acceptance of undertaking the political costs of a thorough institutional restructuring. The intergovernmental fiscal pressure balanced by the increase of own current revenues (user charges, fees and local taxes) increased financial independence of the Municipality, and the privatization revenues could be turned into the up grading of infrastructure.

Increasing charges supplied better information on demand and improving financial forecasting and planning supplied better assessment of future investment needs and capabilities. On the basis of this new information the revision of the earlier sectoral development concepts could continue to establish the balance of targeted investments and financing capabilities and on the basis of financing plans and better programming of interventions could be elaborated.

The restructuring of operation and financing of institutions was the most complicated and conflicting part of the financial reform. When it started in 1996 its acceptance could already be built on the increased belief in the results of forecasting, the widening understanding of the basics of financial management, on the credibility of the enduring leadership and on incentives and rewards balancing restrictions.

The restructuring of operation had to tackle three tasks: (1) reconsideration of the responsibilities that had started earlier by the revision of sectoral task concepts, (2) introduction of zero based task financing as an effective method to increase efficiency of institutional management and (3) establishment of a Rationalization Fund to cover the one time investment needed for long-term cost saving on operation.

Reforms of operation and development, creditworthiness and a sustainable balance created the basis for the harmonization of operation and development activities and the base for the elaboration of a comprehensive strategic plan. The elaboration of a new Urban Development Concept started in 1997 and still it is in the process. Hopefully it will be finished and accepted soon. At that time all elements for a comprehensive strategic plan will be there, and can be synchronized so as Budapest can enter to a period of continuous strategic planning process.

Table 3: Summary table of the reforms in the Municipality of Budapest

1990 – 1994 CONSOLIDATION	1994 – 1998 START OF MAJOR REFORMS	Further Targets ACCOMPLISHMENT
External and internal conditions		
Uncertainty of the new system, fiscal pressure and initially un-experienced leadership.	Continuing fiscal pressure, more certainty of the context, experienced leadership. Short-term financial crisis.	Re-centralizing tendencies of central government and politicised intergovernmental relations.
Elements of the financial reform		
Renewal of decision processes and procedures for new projects. Two years CIP.	Forecasting and medium term planning of capital budgets. Increase of financial independence / own revenues. (privatization, tax, fees)	Reform of operation and long term financial planning of operation and development. Active borrowing policy
Planning of sectors and development		
First Urban Policy Concept First revision of previous plans (water, traffic, human sector services, etc)	Elaboration of new sector concepts and plans adapted to the new conditions. Steps in agreement on financing and implementation programs of sector plans.	Harmonization of urban management and development, shift to continuous strategic planning process.
Results in development planning		
Coexistence of old and new elements and routines	Coalition could be built for major structural reforms and restrictive policies.	Sustainable balance. Survival in alien conditions.

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