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## Tanzania – The Case of Dar es Salaam

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This chapter considers the state of municipal finances in Tanzania, focusing in particular on municipal infrastructure finance in Dar es Salaam. It first sets out the country or macro-economic context, then provides the background on the framework for decentralisation and local government finances. The chapter goes on to analyse the municipal finance situation and the approach to infrastructure financing in Dar es Salaam, concluding with a summary of the key findings of the case study.

### **Macro-economic context**

Tanzania is located in Eastern Africa bordering the Indian Ocean and covers a land area of 945,000 square kilometres. The current population of 39 million is projected to reach almost 60 million by 2025. The country's economic growth has averaged 6 per cent in the period of 2000 to 2006 and the economic outlook remains robust, with growth projections of 6–7 per cent of gross domestic product (GDP) for 2007 and 2008. Notwithstanding the recent economic surge, with a GDP per capita of less than US\$340 in 2005, half of Tanzania's population remains poor.<sup>1</sup>

Tanzania's development vision aims for a high quality of life for all people by 2025. Among the principal macro-economic policies to sustain growth, price stability is a central objective of the Bank of Tanzania. The inflation rate is expected to be 6 per cent in 2007. The Tanzanian Shilling (TSh) is now freely floating at an exchange rate of TSh1,275 to the US\$.<sup>2</sup> With macroeconomic stability and growth, the levels of public and private sector investment are gradually increasing.<sup>3</sup>

### ***Urbanisation and underlying economic trends***

A quarter of Tanzania's population live in urban areas. However, with urban growth rates twice the rural ones, UN projections estimate that the urbanisation rate will increase from 24 per cent in 2005 to 38 per cent by 2030, with more than 20 million Tanzanians living in urban areas.<sup>4</sup>

Depending on different estimates, Dar es Salaam accommodates about 30–40 per cent of the national urban population and functions as the locus of economic activities. Urbanisation is expected to drive the country's economic transformation. While 46 per cent of economic activity continues to be based on agricultural activities, industrial and services sectors are growing at a rapid pace. Tanzania's development vision anticipates a transfer to a more knowledge based, semi-industrialised economy, with particular focus on investing in sound infrastructure as an economic underpinning.<sup>5</sup> The main contributors to economic expansion are the manufacturing and construction sectors with growth rates of about 12 per cent and 9 per cent in 2006. The service sector grew at 7 per cent in 2006, with tourism leading the growth.<sup>6</sup>

## **Decentralisation framework**

The government's policy agenda recognises the local government's critical role in providing an environment conducive to economic growth and poverty reduction. In this context, decentralisation ranks high on the national policy agenda.

### ***Local government legislation and organisation structure***

The Local Government Act of 1982, setting out the framework of functional and fiscal decentralisation, has become a central theme of government policy. The government's vision of the local government system, based on 'decentralisation by devolution', is set forth in the Policy Paper on Local Government Reform of 1998. A number of amendments to the Local Government Act in 1999 gave more authority to district and urban councils to approve their plans and budgets.<sup>7</sup> In accordance with the Public Finance Act 2001, the Ministry of Finance (MoF) is responsible for co-ordinating intergovernmental fiscal relations. The Prime Minister's Office – Regional Administration and Local Government (PMO-RALG) oversees the local government system and the decentralisation process, and the line ministries are responsible for regulatory and sectoral policies.

Tanzania has adopted a two-tier structure of decentralisation – through both central government and local government authorities (LGAs). The LGAs have been awarded legal status enabling them to contract services and, subject to ministerial approval, raise borrowing. LGAs are comprised of 22 urban councils and 92 (rural) district councils that have autonomy in their geographic area. The urban councils comprise two city, twelve municipal and eight town councils. District councils co-ordinate activities of township authorities and village councils.<sup>8</sup>

### ***Functional and fiscal devolution of powers***

The devolution policy of local government functions and expenditures to the LGAs is enshrined in the Local Government Act and is based on the principles of subsidiary and that 'finance should follow function'. LGA activities include a list of public

services including general administration, education, social welfare, public health, housing and town planning, transport, environment, culture and economic affairs. The expenditure responsibilities range from concurrent functions, subject to central government policy, to purely local government services. It is expected that each of these will be funded through different identified sources of financing.<sup>9</sup> Table 3.1 below sets out, at a high level, the detailed expenditure assignments, and their planned source(s) of financing. These are described in further detail in the following sections.

**Table 3.1.** Assignment of LGA expenditure responsibilities and financing sources

<i>Type of local government function</i>	<i>Local government activity</i>	<i>Planned source of financing</i>
Concurrent functions (locally provided 'national' public services)*	<ul style="list-style-type: none"> <li>• Primary education</li> <li>• Local health services</li> <li>• Water supply</li> <li>• Local roads and works</li> <li>• Agriculture extension and livestock</li> </ul>	<ul style="list-style-type: none"> <li>• Sectoral block grants</li> </ul>
Exclusive local government functions	<ul style="list-style-type: none"> <li>• Land use planning</li> <li>• Sewage and sanitary services (including solid waste collection and street cleaning)</li> <li>• Local parks and markets</li> <li>• Community centres</li> <li>• Other local amenities</li> </ul>	<ul style="list-style-type: none"> <li>• General purpose grants</li> <li>• Own-source revenues</li> </ul>
Delegated central government functions	<ul style="list-style-type: none"> <li>• Outbreak of infectious diseases</li> </ul>	<ul style="list-style-type: none"> <li>• Ministerial subventions</li> </ul>
Local government administration	<ul style="list-style-type: none"> <li>• Council operations</li> <li>• Local planning</li> <li>• Local financial management</li> <li>• Village and street neighbourhood (<i>Mtaa</i>) administration</li> </ul>	<ul style="list-style-type: none"> <li>• General purpose grants</li> </ul>
Local capital development activities	<ul style="list-style-type: none"> <li>• Construction of new and rehabilitation of existing infrastructure in various sectors including education, health, water, roads, etc.</li> </ul>	<ul style="list-style-type: none"> <li>• Own-source revenues</li> <li>• Local borrowing</li> <li>• Capital development grants</li> </ul>

Source: United Republic of Tanzania (2006)

\* Central government sets policies, regulation and norms and controls financing

## **Overview of the provision of municipal services**

This section provides an overview of the state of the key municipal services in Tanzania, including education, healthcare, roads, water supply and sanitation services, based on desk-based research. The combination of rapid urbanisation, unplanned settlements and pervasive urban poverty has confronted the central government, as well as LGAs, with serious challenges in public service provision:

- Among concurrent local government responsibilities, primary education stands out as the only public service rated as satisfactory. This is seen as a result of strong growth in school enrolment in recent years, following the abolition of school fees in 2001 and the launch of the Primary Education Development Plan, which aimed to increase the affordability and accessibility of primary schooling.<sup>10</sup>
- In contrast, the majority of citizens are not satisfied with health services, as accessibility and affordability remaining serious problems.<sup>11</sup>
- Roads, both urban and rural, remain under-funded and are generally in poor condition. Municipalities in Tanzania manage more than 56,000 kilometres of local roads with funding from sectoral block grants as well as from a 30 per cent share of the separate road fund financed by the proceeds of a fuel surcharge.<sup>12</sup>
- Water supply is largely operated by 19 urban water and sewerage authorities (UWSAs), established as autonomous bodies under the Urban Works Order of 1998. The water sector suffers from several issues, including low, non-cost-reflective tariffs, poor governance, and lack of resources for maintenance and capital investments. Fifty-four per cent of people in rural and 74 per cent in urban areas had access to safe drinking water in 2005. However, to meet the country's development vision's target of a countrywide 90 per cent coverage by 2025, a further 24.6 million will need improved water supply.<sup>13</sup>
- Sewerage operations, to the extent they exist, are under the control of the UWSAs. Due to poor maintenance, few wastewater treatment facilities are functioning. Seventeen per cent of the urban population is connected to an improved sewerage system and an estimated 50 per cent of the households have access to basic sanitation services. The government's objective is to increase the proportion of the urban population with improved sewerage services to 30 per cent and to allow for 95 per cent of the population to have access to basic sanitation by 2010.<sup>14</sup>

Urbanisation has contributed to the rapid growth of informal and unplanned settlements that make up 60 per cent of the total urban housing stock in Tanzania. This has aggravated the municipal infrastructure financing gap.<sup>15</sup>

## Local government revenues

Local governments in Tanzania finance their assigned expenditures from three main sources:

- intergovernmental transfers,
- own-source local revenues, and
- borrowing.

Table 3.2 provides an overview of the revenues across local governments in Tanzania for the period 2002–06. The key points to note are:

- The total amount of local government revenues has doubled since 2002, with the increase primarily driven by growth in intergovernmental transfers.
- Government transfers or grants account for nearly 90 per cent of local government revenues.
- Own-source revenues have declined in absolute and relative terms since 2002.
- Local borrowing, although provided for in the law, remains negligible.

**Table 3.2.** Local government revenues in Tanzania, 2002–2005/06 in TSh million

Revenues	2002 *	%	2003 *	%	2004/05	%	2005/06	%
Local grants (transfers)	247,027	81.0	313,873	86.5	386,768	89.9	452,831	89.9
Own-source revenues	57,740	18.9	48,344	13.4	42,871	10.0	49,291	9.8
Local borrowing	225	0.1	443	0.1	549	0.1	1,496	0.3
Total	304,992		362,660		430,188		503,618	

Source: United Republic of Tanzania (2007b)

\*Prior to 2004, revenue collections were reported based on calendar years and not fiscal years

## Intergovernmental transfers

Transfers from the central government currently amount to around 90 per cent of local government revenues. Following from the detailed expenditure responsibilities, these transfers include:

- Formula-based *recurrent (conditional) block grants* for grant-aided sectors, including primary education, local health services, water, local road maintenance, and agricultural extension.
- Formula-based, *equalising general-purpose grants (GPG)*. Such grants combine the former ‘current administration grant’ and the ‘compensation grant’

(provided in compensation of own-source revenues abolished in 2003/04). The size of GPG is largely dependent on population and the number of rural residents.

In total, recurrent block grants account for about two-thirds of all intergovernmental transfers. It is worth noting that 75 per cent of the total recurrent government transfers in 2005/06 were allocated to the health and education sectors, 18 per cent to administrative expenses and 7 per cent to roads, water and agriculture.

In addition to formula-based grants, local governments receive two additional sources of transfers:<sup>16</sup>

- Formula-based ‘local government capital development grants’ (LGCDGs). LGCDGs have been implemented since 2005/06 and provide discretionary funds to LGAs. Funding is linked to local government performance in key areas of financial management, participatory planning and issues of transparency and accountability. LGCDGs have become the main funding modality for local capital infrastructure and amounted to about TSh100 billion in 2005/06.<sup>17</sup>
- Ministerial subventions. These are routed around the available formula-based grant allocation modalities.<sup>18</sup> In 2005/06, LGAs reported receiving TSh77 billion in recurrent subventions from line ministries.

### ***Own-source revenues***

Besides intergovernmental transfers, own-source revenues raised by local governments are limited and include:

- property taxes and rent,
- charges from solid waste collection, vehicles, markets etc.,
- fees, including taxi registration, bus stands etc. and
- licences, including road and liquor.

Various amendments to the Local Government Acts in 2003 and 2004 significantly reduced the revenue-raising authority of local governments.<sup>19</sup> In 2003, the Ministry of Finance announced the abolition of the development levy, as well as a number of additional ‘minor’ local revenue sources, while also limiting the local rate-setting discretion for other local revenue sources. To compensate for the fall in own-source revenues, the general-purpose grant was introduced. Consequently, local revenue collection declined since 2003, and has only recovered since 2005/06 with a number of reform measures instituted to transform the current system of local government revenues. These include measures to strengthen administration of revenue collection and improved revenue mobilisation.<sup>20</sup>

Table 3.3 presents a summary of own-source revenues across local governments in Tanzania. The key observations are:

- Licences and permits, user fees and charges constitute about 28 per cent of own-source revenues.
- Local rates on business-related activities in form of service levies and agricultural cesses are further significant revenue sources.
- Local rates on property and land, although gradually growing as a source of revenue, are a minor component of local revenues.<sup>21</sup>
- The development levy, an earlier significant revenue source, was abolished in 2003. As a result, local revenue sources are yet to reach pre-2003 levels.

**Table 3.3.** Local government own-source revenues, 2002–2005/06, in TSh million

<i>Revenues</i>	2002 *	%	2003 *	%	2004/05	%	2005/06	%
Licenses, fees and charges	17,174	29.7	17,313	35.8	11,801	27.5	13,621	27.6
Service levy	9,261	16.0	7,787	16.1	10,682	24.9	11,734	23.8
Agricultural cesses	9,251	16.0	9,018	18.7	11,376	26.5	10,862	22.0
Other revenues	6,570	11.4	7,232	15.0	4,234	9.9	7,447	15.1
Property tax	3,548	6.1	3,135	6.5	4,208	9.8	4,857	9.9
Land rent	567	1.0	655	1.4	572	1.3	771	1.6
Development levy	11,369	19.7	3,205	6.6	0	0	0	0
Total revenues	57,740		48,345		42,873		49,292	

*Source:* United Republic of Tanzania (2007b)

\*Prior to 2004 revenue collections were reported based on calendar years

### ***Local government borrowing***

As shown in table 3.2, borrowing currently accounts for a negligible 0.3 per cent of local funds and is primarily from the Local Government Loans Board (LGLB), a government-supported financial intermediary.

The LGLB is largely funded from contributions of LGAs and grants from the central government. LGAs are requested to contribute a minimum compulsory reserve equal to 10 per cent of own-source revenues, which serves as a reserve with the LGLB. LGAs are eligible for borrowing only if the requested reserve is maintained. However, with own-source revenues remaining weak and many LGA being unable to contribute their minimum reserve requirement, the LGLB has been unable to cater to the level of loan applications. The level of new loans issued in 2006/07 amounted to only TSh598 million, with loan applications being much higher at TSh1,144 million.<sup>22</sup>

## **Local government financial management**

A series of reforms to strengthen local government financial management have been implemented in order to improve the spending effectiveness of the limited local revenues.<sup>23</sup> These include the following:

- A local government finance statistics reporting system was set up in 2006 to provide regular, detailed reports on local government finances for urban and district councils in mainland Tanzania.
- Recent actions were taken to improve the local government planning and budgeting process, particularly related to the operations and maintenance cost for infrastructure investments. Since 2006/07, all local governments in mainland Tanzania use PlanRep software to prepare their budget plans.
- LGAs in Tanzania are required to prepare their budget plans in a medium-term budget framework, consistent with the national strategy for economic growth and poverty reduction. Recent reforms include the training of local government officials in the medium-term expenditure framework processes, as well as the harmonisation of budget classifications and codes.

## **The case of Dar es Salaam**

Having outlined the decentralisation framework in Tanzania, including a description of local government finances, this section studies the municipal finances and service delivery in Dar es Salaam. It sets out the city context and describes the administrative framework of municipal finances in the city. The section also presents the municipal revenues and expenditures of the city, and goes on to discuss private sector participation in the city's service provision, finally reviewing the current state of and potential for alternate financing sources.

### **City context**

One of the fastest growing cities in sub-Saharan Africa, Dar es Salaam is Tanzania's industrial, commercial and governmental centre. With an estimated 3 million people, Dar es Salaam is seven times larger than the country's second largest city. Some estimates place the population as high as 5 million at daytime. Dar es Salaam comprises three municipalities, Ilala, Kinondoni and Temeke, which are in parallel districts of the Dar es Salaam region. Based on the 2002 Population and Housing Census, Kinondoni had the highest population, followed by Temeke and Ilala. Population figures and recent urban growth estimates are shown in table 3.4 below.<sup>24</sup>

The city population is growing at about 4 per cent and attracts 100,000 migrants annually. Although there is a strategy aiming to achieve 'a city without slums' by 2015, some 70 per cent of the population currently live in unplanned and

**Table 3.4.** Municipalities in the Dar es Salaam region, current and projected population

Municipality	2002	2003	2005*	2007*
Kinondoni	1,083,913	1,130,520	1,229,835	1,337,875
Ilala	634,924	662,225	720,401	783,687
Temeke	768,451	801,493	871,904	948,498
<b>Dar es Salaam</b>	<b>2,487,288</b>	<b>2,594,238</b>	<b>2,822,140</b>	<b>3,070,060</b>

Source: DSM CC (2004)

\*Projected population figures

un-serviced settlements.<sup>25</sup> The urban sprawl in the city as a result of this unplanned growth increases the burden of providing infrastructure services.

### **City administration and allocation of responsibilities**

Dar es Salaam has a regional administration headed by the Dar es Salaam regional commissioner. In addition, Dar es Salaam has a city council, headed by a mayor. Each of the three municipal councils has been given an administrative jurisdiction area in the city.

Table 3.5 sets out the split of responsibilities between the city council and the three municipalities. Dar es Salaam City Council (DSM CC) only performs a co-ordinating role and attends to issues cutting across the three municipalities. In contrast, each of the three municipal councils is responsible for providing the bulk of infrastructure and public services outlined below.

**Table 3.5.** Responsibilities of Dar es Salaam City Council and municipalities

<i>Dar es Salaam City Council (DSM CC)</i>	<i>Municipalities of Ilala, Temeke and Kinondoni</i>
<ul style="list-style-type: none"> <li>• Co-ordinate the functions of the three municipalities regarding infrastructure.</li> <li>• Prepare a coherent citywide framework for the purpose of enhancing sustainable development.</li> <li>• Deal with matters of interdependency among the municipalities – such as inter-district roads.</li> <li>• Provide peace, security and emergency services such as fire prevention, and control ambulance and auxiliary police.</li> </ul>	<ul style="list-style-type: none"> <li>• Primary education</li> <li>• Local health services</li> <li>• Solid-waste management</li> <li>• Transport infrastructure including roads</li> <li>• Informal sector development</li> <li>• Culture and community development</li> <li>• Water supply – municipal councils are responsible for supporting the construction of wells on demand<sup>26</sup></li> </ul>

Source: DSM CC (2004); Interview DSM City Council

## ***Municipal revenues***

Based on the devolution of powers and responsibilities to the municipalities, this section describes the revenues of the city council and the municipalities. Overall, own-source revenues in the Dar es Salaam region amounted to a total of TSh17,300 million in 2005/06, equal to 30 per cent of total local government revenues. A further increase to about TSh21,000 million is expected in 2006/07.

### ***Dar es Salaam City Council***

The Dar es Salaam City Council has limited revenue powers, given its role as a primarily co-ordinating institution, and limited expenditure responsibilities. Table 3.6 describes the composition of its revenues.

- The city council does not raise its own taxes like the municipalities. The bulk of its own-source revenues are from parking and bus stand fees.
- Intergovernmental transfers comprise the majority of the council's revenues and are mostly general purpose grants for recurrent expenditures. The 2006/07 budget indicates a nearly three-fold increase in general purpose grants to the city council.
- The city council has not raised any borrowing.

**Table 3.6.** Revenues of Dar es Salaam City Council, in TSh million

<i>Revenues</i>	<i>2005/06 actuals</i>	<i>%</i>	<i>2006/07 budget</i>	<i>%</i>
<b>Own-source revenues, of which</b>	<b>2,004</b>	<b>47.1</b>	<b>2,371</b>	<b>29.9</b>
Fees and charges	1,607	37.8	1,892	23.9
Service levy	99	2.3	80	1.0
Other revenues	298	7.0	399	5.0
<b>Intergovernmental transfers, of which</b>	<b>2,249</b>	<b>52.9</b>	<b>5,553</b>	<b>70.1</b>
Total recurrent grants	2,219	52.2	5,297	66.9
General purpose grants	1,634	38.4	5,031	63.5
Roads	246	5.8	146	1.8
Health	75	1.8	120	1.5
Local admin	264	6.2	0	0
Development grants	30	0.7	256	3.2
Local borrowing	—	—	—	—
<b>Total revenues</b>	<b>4,253</b>	<b>100.0</b>	<b>7,924</b>	<b>100.0</b>

*Source:* United Republic of Tanzania (2007c) and Local Government Information, Monitor Local Government Finances, Budgets 2006/07

## Municipalities in Dar es Salaam region

The core revenue raising powers and expenditure responsibilities at city level are assigned to the three municipalities of Ilala, Kinondoni and Temeke. Table 3.7 sets out the aggregate revenue sources of the three municipalities. The key lessons are described further below.

**Table 3.7.** Revenue sources, municipalities in Dar es Salaam region, in TSh million

Revenues	2005/06 actuals	%	2006/07 budget	%
<b>Own-source revenues, of which</b>	<b>15,383</b>	<b>28.7</b>	<b>18,820</b>	<b>22.3</b>
Service levy	8,201	15.3	8,361	9.9
Property taxes	2,723	5.1	5,031	5.9
Fees and charges**	3,095	5.8	3,005	3.6
Hotel levy	187	0.3	212	0.3
Licenses	76	0.1	101	0.1
Produce cess*	30	0.1	2	0.0
Land rent	0	0.0	50	0.1
Other revenues	1,071	2.0	2,058	2.4
<b>Intergovernmental transfers, of which</b>	<b>38,298</b>	<b>71.3</b>	<b>65,736</b>	<b>77.7</b>
Total recurrent grants	29,215	54.4	41,407	47.3
Education	15,536	28.9	21,954	26.0
General purpose grants	4,842	9.0	8,996	10.6
Health	5,066	9.4	7,824	9.3
Local admin	900	1.7	1,390	1.6
Agriculture	1,147	2.1	592	0.7
Water	496	0.9	359	0.4
Roads	1,229	2.3	292	0.3
Subventions and basket funds	4,995	9.3	9,192	10.9
Development grants	4,088	7.6	16,528	19.5
Local borrowing***	—	—	—	—
<b>Total revenues</b>	<b>53,681</b>	<b>100.0</b>	<b>84,556</b>	<b>100.0</b>

Source: United Republic of Tanzania (2007c) and Local Government Information, Monitor Local Government Finances, Budgets 2006/07

\*Charges on agricultural and livestock produce, \*\*includes parking fees, billboard fees, bus stand fees, \*\*\*no municipal borrowing, other than a small loan to Ilala municipality from the LGLB has been reported

In contrast to other local governments, the urban municipalities in Dar es Salaam mobilise greater levels of own-source revenues. These constitute 29 per cent of local revenues, and are relatively three times higher than the national average. The key factors determining own-source revenues are outlined below:

- The primary source of revenue in the three municipalities is service levy, which constitutes more than 40 per cent of own-source revenues. The service levy, raised as a 0.3 per cent charge on business turnover, has risen from TSh3,000 million in 2000 to more than TSh8,000 million in 2006/07.<sup>27</sup>
- Property taxes are collected by each municipality.<sup>28</sup> Properties in Dar es Salaam were however last fully valued in 1994 and there is a need to strengthen administration of local property rates in order to improve local resource mobilisation.
- Similar to the national trend, the three municipalities have lower own-source revenues following the abolition of the development levy and other 'nuisance' taxes in 2003.
- Miscellaneous fees and charges are a growing source of own revenues, with parking and billboard fees being a significant source of income.

With respect to intergovernmental transfers, similar to the countrywide level, recurrent grants constitute about 50 per cent of total local government revenues and are largely sector specific. Education and health are the sectors that receive most of the funding.

As for capital investments, all three municipalities fulfilled the eligibility criteria for development grants in 2006/07. These grants are largely discretionary and are the main sources of finance for infrastructure investments.<sup>29</sup> Funding amounted to more than 7 per cent of local revenues in 2005/06 and is expected to increase to about 20 per cent of total local revenues (TSh16,500 million) in 2006/07. The grants include funds from the community infrastructure-upgrading window of the World Bank's Local Government Support Project.<sup>30</sup>

### ***Revenue enhancement plans***

As part of the ongoing Local Government Support Project, Dar es Salaam is implementing a revenue enhancement plan to strengthen its own-source revenues. The city aims to increase its own-source revenues by TSh28,900 million in the coming years from the current level of TSh21,000 million. A major focus is on widening the revenue base. Key strategies for revenue enhancement aim at:<sup>31</sup>

- *Strengthening the tax administration system.* A tax increase of TSh12,000 million is expected from improved tax administration. Reform measures include a wider identification of taxpayers and improved assessment of tax liability, capacity building of councillors and staff, better enforcement of tax collection, and follow up on debtors. It is also proposed to better utilise technology for tax administration and undertake a public awareness campaign on taxpayers' responsibilities.
- *Realising the potential of property related taxes.* The total potential increase from property taxes is estimated at about TSh20,000 million by 2011 from a level

of about TSh5,000 million in 2006/07. The project aims at the valuation of all taxable properties in Dar es Salaam, including using aerial mapping to identify unassessed properties. This includes a large number of high-value properties not captured under the current valuation. Furthermore, reform will include improvements in the techniques of valuation and assessment of properties, as well as improved enforcement and collections of property taxes.

### *Municipal expenditures*

This section outlines the expenditure patterns of Dar es Salaam LGAs. Tables 3.8 and 3.9 show the expenditures of the DSM CC and the three municipalities (aggregated) respectively. Since the city council mainly plays a co-ordinating role, its expenses are limited and essentially comprise recurrent expenditure such as salaries and local administrative expenses.

The aggregate expenditure of the municipalities is much higher in comparison. With municipalities being autonomous, their expenditure control makes up more than 90 per cent of the local government funds in the Dar es Salam region. The main observations that can be drawn from their budgets are:

- Development expenditures, including funds for infrastructure developments and rehabilitation, constituted only about 15 per cent of the 2005/06 expenditure.<sup>32</sup> However, for 2006/07 a strong rise in the absolute and relative share of capital expenditures is expected, as the modalities and process of the new capital development grant system become established and the capacity of financial management further improves.<sup>33</sup>
- Recurrent expenditure accounts for the majority of the municipalities' expenditure. Since responsibility for most municipal functions are devolved, the bulk of recurrent funds are allocated to payment of salaries in the education and health sectors (in addition to local administration expenses).

**Table 3.8.** Local government expenditures, Dar es Salaam City Council, in million TSh

<i>Expenditure</i>	2005/06 <i>actuals</i>	%	2006/07 <i>budget</i>	%
<b>Recurrent expenditures, of which</b>	<b>3,512</b>	<b>87.2</b>	<b>6,263</b>	<b>79.3</b>
Local admin.	365	9.1	3,241	41.0
Roads	47	1.2	146	1.8
Health	121	3.0	120	1.5
Water	290	7.2	0	0.0
Other local spending*	2,689	66.8	2,756	34.9
<b>Development expenditure</b>	<b>514</b>	<b>12.8</b>	<b>1,638</b>	<b>20.7</b>
<b>Total expenditure</b>	<b>4,026</b>	<b>100.0</b>	<b>7,901</b>	<b>100.0</b>

*Source:* United Republic of Tanzania (2007c) and Local Government Information, Monitor Local Government Finances

\*Including part of the salaries of administrative staff

**Table 3.9.** Local expenditures, municipalities of Dar es Salaam region, in TSh million

<i>Expenditure</i>	2005/06 <i>actuals</i>	%	2006/07 <i>budget</i>	%
<b>Recurrent expenditures, of which</b>	<b>34,274</b>	85.3	<b>59,498</b>	64.8
Education	17,013	42.3	25,257	27.5
Local admin.	8,728	21.7	16,461	17.9
Health	5,454	13.6	8,647	9.4
Roads	513	1.3	742	0.8
Agriculture	231	0.6	669	0.7
Water	313	0.8	497	0.5
Other local spending	2,022	5.0	7,225	7.9
<b>Development expenditures, of which</b>	<b>5,908</b>	14.7	<b>32,306</b>	35.2
Education	1,778	4.4	7,314	8.0
Admin.	92	0.2	5,841	6.4
Roads	2,130	5.3	4,060	4.4
Health	464	1.2	2,836	3.1
Water	29	0.1	100	0.1
Agriculture	11	0.0	96	0.1
Other	1,404	3.5	12,059	13.1
<b>Total expenditure</b>	<b>40,182</b>	100.0	<b>91,804</b>	100.0

*Source:* United Republic of Tanzania (2007c) and Local Government Information, Monitor Local Government Finances

### ***Municipal infrastructure services and the framework for PSP***

As with other rapidly urbanising cities facing an infrastructure financing gap, Dar es Salaam also faces the following key challenges in delivering an adequate level of municipal infrastructure:<sup>34</sup>

- *Rapid urban migration and unplanned settlements:* The backlog in infrastructure service provision is evident in Dar es Salaam, as infrastructure investments cannot cope with rapid urban growth. The urbanisation process, coupled with the spread of informal settlements, is not co-ordinated with the capacity of the respective utility systems.
- *Lack of co-ordination across stakeholders:* Studies show a lack of co-ordination among the different urban institutions and stakeholders. Sector-focused planning and implementation has led to overall unco-ordinated city development and investments.
- *Land tenure system further constrains infrastructure development:* While there is progress at the municipal level with geographic information systems and

land use plans,<sup>35</sup> the existing land tenure system constrains the acquisition of land for infrastructure development.

The municipalities in Dar es Salaam are trying to attract private sector participation to bridge the gap for infrastructure financing.

### ***National PSP environment***

The local governments' attempts to mobilise private sector participation (PSP) in infrastructure is to be examined in the context of the fairly nascent PSP activity at the national level in Tanzania. As a step towards more vibrant private sector development, the government is making efforts to strengthen the overall enabling environment. These include reforms in the banking sector and the commercial courts, a credit guarantee scheme for small and medium-sized enterprises (SMEs), and a privatisation programme to facilitate development of local capital markets. The Public Sector Reform Commission is in the process of completing the privatisation of the remaining 36 public enterprises in 2007.<sup>36</sup> However, poor physical infrastructure and investors' perception of local government efficiency are still bottlenecks inhibiting private investments.<sup>37</sup>

The government is currently examining new options of private sector provisioning of public infrastructure, particularly in the transport sector. For example, a study exploring options for PSP in the road sectors has been commissioned.<sup>38</sup> Some recent examples of successful PSP activities include a concession contract awarded by the Dar es Salaam port authority for a container terminal,<sup>39</sup> and a 25-year concession contract awarded to operate the Tanzania National Railway.

### ***PSP at sub-national level***

At the sub-national level, successful practices of private sector activities in infrastructure provision have so far been limited to contracting out specific municipal services. The most notable examples of contracting out municipal services include solid waste management, parking services, a bus terminal and the operation of local markets. However, an attempt to operate the local water supply system under a leasing agreement was terminated with the management of water services reverting back to the state-owned operator DAWASCO.

These experiences with outsourcing municipal services are discussed in turn below.

- Since 1992, the city's solid waste management system has been reformed and contracted out to private sector operators. The programme, focusing on the privatisation of waste disposal and community waste collection, is considered a notable success. Solid waste collection has been fully contracted out by the municipalities and is tendered competitively. There are currently 23 different operators and the collection rate of solid waste has increased from

2–4 per cent in 1992 to currently 45 per cent of the city area. The DSM CC monitors the quality of services and manages the disposal facilities.<sup>40</sup>

- Similarly, the city's central bus terminal is managed by a private operator. Not only does the bus terminal raise more than TSh600 million from fees annually but it creates more than 1,000 jobs. In addition, parking services in Dar es Salaam are privately operated, and the city council receives a certain percentage from fees collected. The operation of local markets is also tendered on an annual basis and successful contractors pay the council a fee.<sup>41</sup>
- On the contrary, the city's experience with PSP for water and sanitation services was not successful. This sector in Dar es Salaam has been particularly constrained with limited capital investments for 30 years. In 2002, a British-German-Tanzanian joint venture – 'City Water Services' – was awarded the tender for a 10-year lease contract to manage the technical and commercial operation of the water and sewerage system in the city. The infrastructure assets remained in government hands and the consortium entered the contract for the implementation of the 'Dar es Salaam Water Supply and Sanitation Project' with DAWASA. The World Bank and other donors awarded US\$143 million for repairs, upgrades and expansion of the water and sewerage infrastructure. However, in May 2005, the government, accusing the operator of failure to deliver on its contractual investment obligations and settle the lease fee, terminated the contract and transferred the responsibilities back into the public sphere. The city's water supply and sewerage has since then been managed by DAWASCO.<sup>42</sup>

Going forward, the city is planning some of its future new infrastructure developments in the form of public–private partnerships:

- Urban transport in Dar es Salaam is generally considered inefficient, and of poor quality and safety. Public sector operators only hold a 10 per cent stake in the market, while transport is largely run by private bus operators on an ad hoc basis. The World Bank is currently spearheading the implementation of the Dar es Salaam Rapid Transport Project to improve public transport in the city. Under the auspices of the Dar es Salaam Rapid Transit Agency, a separate lane rapid bus system modelled after the successful Bogotá TransMilenio<sup>43</sup> project is being envisioned. Key project characteristics are:<sup>44</sup>
  - o Total planned investments are US\$125 million and operation should start in 2009.
  - o Funding for infrastructure investments will be co-ordinated by the city council, and investments in vehicles to operate the system will be largely privately financed. Two operators are expected to invest US\$15 million.
  - o The private sector operator will run the fare collection, management and operation. The project will be operated under a 10-year concession

contract awarded to the operator with ticket prices similar to those of private operators who will be banned from the market. Small subsidy payments are budgeted for the introductory phase.

- Similarly, several new properties are being developed for commercial and residential purposes, with the explicit objective of attracting private sector developers and financiers. Box 3.1 provides a summary of a new property development planned in Kinondoni municipality.

**Box 3.1: New property development in Kinondoni municipality**

Kinondoni, one of the three municipalities in Dar es Salaam, has attracted private sector developers to invest on a joint venture basis with the municipality, in the development of a new business district accommodating office and residential buildings. As one of the main financiers, the National Social Security Fund will provide seed capital for the project. The plan is that the municipality contributes the plot of land and the investors shall bear the construction cost. While the exact share and management of the development project are still to be agreed, it is expected that the revenues from rents and sales of units will be shared between the municipality and the investor.<sup>45</sup> The rapid urbanisation and tourism potential are driving up land prices in priority areas of the city, which is anticipated to attract private property developers and other financiers seeking to invest in long-term, high-return avenues.

### ***Alternative sources of municipal financing***

As noted, the budgets of Dar es Salaam municipalities are largely supported by inter-governmental transfers. The revenue enhancement plans largely focus on strengthening own-source revenues such as property tax and improving financial management.

Currently, the municipalities do not access any alternative financing to the traditional revenue sources. There are several demand and supply side issues constraining the development of market-based financing.

The Local Government Finance Act of 1982 allows LGAs to borrow with ministerial permission. However, borrowing has been negligible. Given the limited resources and financial strength of the municipalities, lenders are not confident to provide financing to the municipalities, unless supported by bankable projects, and/or guarantees from the government or donors. Private sector financiers perceive local government authorities as not being creditworthy and hence highly risky. Also, the PMO-RALG and the Ministry of Finance currently oppose providing loan guarantees for local government borrowing.<sup>46</sup> Hence, despite a substantial level of liquidity in the market, no market lending activities on the sub-national level have evolved.

There appears to be an interest within the Government of Tanzania to expand the possibilities for LGAs to use borrowing as a tool to finance local capital

infrastructure, as long as the framework ensures prudent borrowing in the context of a 'hard budget constraint'. Several measures have been proposed to reform the existing Local Government Loan Board.<sup>47</sup>

As regards the sources of financing, the Tanzanian financial sector is evolving but remains nascent.<sup>48</sup> With the ongoing macro-economic and financial sector reforms, the overall business climate is expected to improve substantially, resulting in the growth of local capital markets and new corporate listings.

The general observation is that there is a lot of liquidity in the economy, but a shortage of local investment-grade and long-tenor assets. Pension funds and insurance companies have excess liquidity and are not allowed to invest offshore. In prior studies, pension funds and insurance companies indicated that they would welcome alternative investment options, like creditworthy infrastructure bonds.<sup>49</sup> There continues to be a strong demand for government securities and bond issues are usually oversubscribed.<sup>50</sup>

## Summary

Tanzania has experienced strong economic growth over the last decade. Urbanisation drives the country's economic transformation, with 30–40 per cent of the urban population living in the commercial and industrial capital Dar es Salaam, a city of 3 million. Decentralisation is high on the government agenda, and municipalities are responsible for providing the bulk of infrastructure and municipal services. Dar es Salaam comprises three municipalities, to which the core of revenue raising powers and expenditure responsibilities have been assigned. Overall, the municipalities control 90 per cent of expenditures in Dar es Salaam. The city council only performs a co-ordinating role.

While other local governments in Tanzania depend almost exclusively on government transfers (90 per cent), Dar es Salaam municipalities mobilise a greater level of own-source revenues (about 30 per cent of their budgets) than at the national level. The main sources of own revenues are service levies and property taxes. Revenue enhancement plans are being implemented that aim to strengthen own revenue sources, largely business service levies and property taxes, which are expected to double by 2011. Nonetheless, budgets are still largely supported by government transfers, including the discretionary capital development grants that are expected to increase significantly. An increase in capital investments is very much needed, since the city's infrastructure provision is found to be inadequate and 70 per cent of the population continue to live in informal settlements.

As regards alternate provision and financing of municipal infrastructure, PSP activity is fairly nascent both at the national and municipal level. PSP has so far been limited to contracting out of specific municipal services like solid waste management system, bus terminals and parking services. An attempt at PSP in the water and

sanitation sector failed in 2005. Future projects to attract private participation include a World Bank funded mass urban transit system with private operators and large-scale property developments for commercial purposes, for example, in Kinondoni municipality in the Dar es Salaam region.

Municipal borrowing for infrastructure investments has not taken hold, and local governments need central government permission to borrow. Although the Local Government Loans Board acts as a specialised public municipal lender, loans to local governments remain negligible at 0.3 per cent of total revenues. Several reform measures to expand lending have been proposed, but have not been implemented yet. At the same time, the financial sector is evolving and demand for government securities is strong. Private sector lenders, however, still perceive local governments as not creditworthy and, hence, lending too risky. Potential lenders could be insurance companies and pension funds, which have the appetite for long-term investments and have indicated potential willingness to invest in creditworthy municipal infrastructure bonds.

## Notes

1. Organisation for Economic Co-operation and Development (OECD, 2007); International Monetary Fund (IMF, 2007a); United Republic of Tanzania (2004).
2. Bank of Tanzania, 17 September 2007.
3. OECD (2007); IMF (2007a); United Republic of Tanzania (2004).
4. United Nations (2006).
5. United Republic of Tanzania (2004); OECD (2007).
6. World Bank (2006g).
7. See Tanzania - Local Government Laws Amendment Act 1999.
8. CLGF (2007a).
9. Function and expenditure responsibilities are assigned in the Local Government Acts.
10. Braathen et al. (2005).
11. Braathen et al. (2005).
12. Interview with World Bank Tanzania Office, transport specialist in July 2007. The current fuel surcharge is 16 US cents per litre and was doubled some years ago.
13. World Bank (2007a); OECD (2007). The total cost for improving access to safe drinking water and sanitation in accordance with the Millennium Development Targets is estimated at US\$2 billion. WaterAid (2005).
14. World Bank (2003); OECD (2007).
15. World Bank (2006a).
16. United Republic of Tanzania (2007b).
17. United Republic of Tanzania (2007a).
18. The allocation process is widely flagged for reform in order to develop the transfer system towards a more efficient, transparent and equitable one. United Republic of Tanzania (2007b).

19. Prior to 2003, each local government was generally allowed to define its own revenue structure, including determining its own tax base and rates. However, the system of local taxes and revenues was widely considered inefficient, inequitable and poorly administered. As a consequence, local discretion in setting own-source revenues was significantly constrained in 2003.
20. For an example, see the case of Dar es Salaam below. United Republic of Tanzania (2006b).
21. The specific case of Dar es Salaam, where a concerted effort is made to better tap into potential sources of property tax, is discussed further below.
22. Interview with PMO-RALG and Local Government Loan Board.
23. United Republic of Tanzania (2006b, 2007b). Interview with Dar es Salaam City Council.
24. DSM CC (2004).
25. Ibid.
26. The provision and management of water and sewerage services is in the responsibility of a separate entity – the Dar es Salaam Water and Sewerage Corporation (DAWASCO), which has been contracted by the Dar es Salaam Water and Sewerage Authority (DAWASA). Once the construction of wells by the municipality is complete, the responsibility is handed over to the water authority.
27. Business-related taxes have a stronger economic base in an urban context. In contrast to a national trend where own-source revenues constitute a mere 10 per cent of local government revenues, the Dar es Salaam region is better off and is able to tap on its more vibrant local economy and property market.
28. A current bill is due in parliament, which will centralise taxation power for local revenue sources like property tax and the service levy (Interviews DSM City Council, PMO-RALG).
29. United Republic of Tanzania (2007b); interview Dar es Salaam City Council, Kinondoni municipality.
30. Funds benefit 31 communities in basic infrastructure provision.
31. Interview with Dar es Salaam City Council.
32. This was much less than the 30 per cent budgeted for development expenditure.
33. Interview with Dar es Salaam City Council and Kinondoni Municipality.
34. Megacities (2007).
35. Interview with Kinondoni Municipality.
36. Some of the public enterprises to be privatised include the National Insurance Corporation, the Tanzania Zambia Railways Authority, commercial units of the Tanzania ports authority and the power utility TANESCO.
37. Infrastructure Finance Corporation Limited (INCA, 2005).
38. Interview with World Bank Transport Specialist. Road development is increasingly administered by TANROADS, which became an autonomous agency by 2005. Most new contracts for road construction and maintenance are performance based and awarded to private contractors.
39. Its main objective was to improve the efficiency of operation, which was successfully realised with decreased dwell time of containers and a doubling of container volumes since start of

operation in 2000. The private operator is responsible for the maintenance of the infrastructure and pays a fixed fee and royalties depending on the volume of containers.

40. Interview with Dar es Salaam City Council.
41. Ibid.
42. IPP Media (2005); World Bank (2003); WaterAid (2003).
43. See chapter 7 for details on the PSP arrangement of the TransMilenio project.
44. Interview with World Bank Office Tanzania (transport specialist) and DSM City Council (finance officer). The bus system shall operate with a total of 142 trunk and feeder buses and 20.9 km of special lanes will be set in place for the rapid transit system with 29 bus stops. The DSM CC will own one of the bus companies, but private operators are encouraged to compete for the second licence. The project further includes investments for five bus terminals and will bring positive externalities in terms of adjacent businesses.
45. Interview with Kinondoni Municipality and the National Social Security Fund.
46. United Republic of Tanzania (2006c, 2007b).
47. Interview with Local Government Loan Board.
48. INCA (2005); private sector demand for commercial lending has grown significantly in recent years.
49. INCA (2005).
50. United Republic of Tanzania (2006a); OECD (2007); interview with National Social Security Fund. Eight companies were listed at the Dar es Salaam Stock Exchange (DSE) by July 2007, of which two were foreign companies. There are still very few corporate bonds listed at the DSE, and trading volumes in corporate bonds are minimal.

