April 2014

# City Creditworthiness Academy
# Self-Assessment Tool
# User Guide

## TABLE OF CONTENTS

## What is a sub-national finances Self Assessment and why is it important for general and special purpose sub-national government entities interested in improving their creditworthiness?

The World Bank has developed over the years a framework for Local Governments Assessments. The Self-Assessment Tool is an introductory version of this framework developed specifically for use in regional City Creditworthiness Academies. Although it is relatively brief, the Self-Assessment Tool has proven to be a thought-provoking instrument for jump-starting the systematic planning of steps needed to be taken by nations and individual sub-national entities to improve creditworthiness.

### Assessment Method

Representatives of each sub-national entity admitted for participation in a week-long Creditworthiness Academy will use the Self-Assessment Tool to:

**A)** Roughly assess their entity's own financial health and the national environment for financing in five key dimensions;

**B)** Identify specific actions needed at both the national and local levels to improve their entity's creditworthiness to the point of obtaining a first credit rating or improving an existing credit rating and mobilizing local market financing for climate friendly infrastructure projects; and

**C)** Identify some of the short- and long-term technical assistance and training activities that can most expeditiously facilitate these improvements in creditworthiness.

The Self-Assessment Tool assists each sub-national entity's representative to examine their entity's own readiness for debt financing of climate smart investments, including:

1. Fundamental Information, including demographic indicators, status of regional development planning, status of climate-related self-analysis, size of the public workforce, and the entity's degree of autonomy within the country's intergovernmental finance system;

2. Sub-National Mandate, i.e. the scope its responsibility for providing specific public services, as well as the degree to which that responsibility is shared with another governmental layer;

3. Sub-National Finances, including major sources of both recurring and non-recurring operating and/or capital revenue, major categories of both operating and capital expenditure, operating margins as well as short- and/or long-term debt profile;

4. Sub-National Financial Management, including experience repaying short- and/or long-term debt on time, management of managing liquidity and operating margins, the quality and effectiveness of financial information systems, including operating and capital budget planning and execution, accounting and audit systems; and

5. The Enabling Environment for subnational borrowing, including the current status of the domestic debt markets with respect to short and long term corporate and sub-national infrastructure finance, the availability of key forms of technical assistance and training from higher levels of government, the availability of financial advisory, credit rating, legal, engineering and other forms of expertise needed for the planning, financing, construction and operation of climate friendly infrastructure.

The following sections of this User Guide provide brief notes to help users understand those sections/subsections which may not be fully self-explanatory.

## 1. The Sub-National Profile

The Sub-National Profile provides a simple introduction of the sub-national entity.

- Please insert a map showing the administrative boundaries of the sub-national entity in .jpeg or .pdf form. In case of existing subdivisions (sub-city) or metropolitan entity, show the different levels of administrations.

- This section also asks three questions regarding the size of the population served by the general purpose subnational government or service entity. It is well-recognized that even in the most well-organized and managed sub-national jurisdictions, the measurement of population characteristics is an inexact science and respondents are asked to answer them in that spirit.

- This section also asks for the number of staff employed by the sub-national entity and that the answer be expressed in 'Full Time Equivalents," so that entities which make heavy use of part-time personnel can be compared more easily with those which make little use of part-time personnel. An FTE of 1.0 means that the employee is equivalent to a full-time employee, while an FTE of 0.5 signals that the worker is only half-time.

- This section also seeks information through an number of questions concerning the subnational entity's use of a 'development plan' which can best be described as a comprehensive strategic document which integrates physical and economic development planning in ways which are mutually reinforcing.

- Note that this section also seeks to elicit information about whether the entity's carbon footprint has been measured and goes on to ask whether the development plan being used by the entity includes ways and means of reducing that footprint. We recognize that some jurisdictions may have proceeded to develop capital projects designed to reduce their carbon footprints without having performed this measurement.

- Governmental decentralization is a highly complex area and yet very little space is provided in this section to answer the single question 'How would you describe the degree of autonomy of your municipality in terms of responsibility/authority/ availability of resources?' In Section 1 (line 1.13), respondents are asked to use just a few words here (e.g. 'great autonomy,' 'little autonomy,' 'amount of autonomy varies by sector,' etc.) to summarize the essence of their jurisdiction's self-perceived degree of actual financial autonomy within each country's intergovernmental finance system.

- Later sections of this self-assessment will request information which 'unpacks' this question in a variety of ways, including through exploration of the intergovernmental transfers system, the degree of local reliance on 'own source' revenues, etc. Therefore respondents may want to wait to give their highly summarized answer in line 1.13 until after they have completed all other sections.

## 2. Sub-National Entity's Governmental Mandates

This section covers the scope of the subnational entity's responsibility for providing specific public services, as well as the degree to which that responsibility is shared with another governmental layer.

- Please note that, for each possible type of basic public service, respondents are asked to indicate whether revenues fail to cover costs, only just cover costs, or exceed costs. The 'revenues' to be included in respondents' consideration of this question should be only those funds which are produced by the service itself, e.g. through user fees/charges or through taxes specifically dedicated by law (or long-standing tradition/practice) to paying for the provision of that service.

- The 'costs' to be included in respondents' consideration of this question should be all of those expenses which are incurred by the sub-national entity to provide the specific public service being discussed, including operations, maintenance and capital acquisition (including both annual direct outlays and total annual debt service for any debt taken on by the subnational entity to finance capital equipment, major maintenance and repair, or new facilities).

- Re: use of 2.2, 'Shared responsibility' – please use this section instead of section 2.1 for a specific service, if responsibility is shared with another level of government (or another service entity at the same level of government). The same service should not be included in both 2.1 and 2.2

## 3. Sub-National Entity's Finances

This section provides a basic overview of the subnational entity's financial status, including its major sources of both recurring and non-recurring operating and capital revenue, the major categories of both operating and capital expenditure, as well as the short- and/or long-term debt profile.

The objective is to evaluate at a glance the financial position of the sub-national entity and to assess its:

- Ability to self-finance part of its capital investment budget, directly or through additional debt (borrowing);

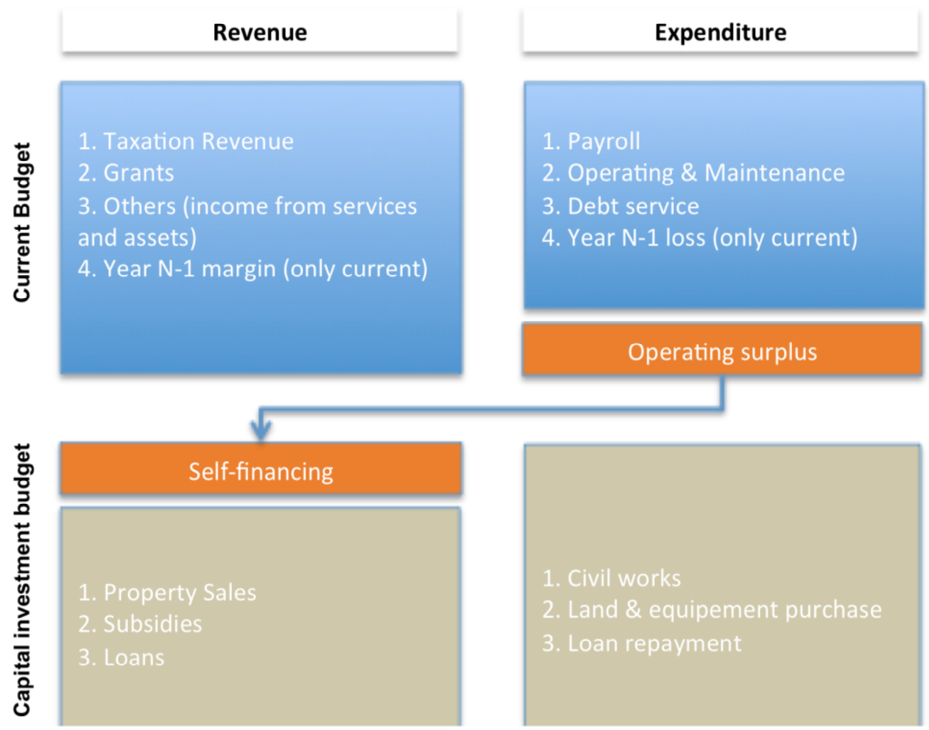
- Financial capacity to cover existing and contemplated future debt service requirements;

- Level of capital investment effort compared with operating budget;

- Degree of dependency  on grants coming from higher levels of government;  and

- General surplus/deficit at the end of the year so that the general surplus /deficit coming from the previous year ('N-1') can be factored into the actual budget of the current year ('N').

The following graphic representation can help respondents visualize these relationships:




The following definitions should be helpful in filling out this section (especially the table in sub-section 3.7.3):

- 'Capital expenditures' are expenditures for the acquisition of fixed or movable capital assets. 'Capital revenues' and 'capital expenditures' flow in (e.g. through sale) or out (e.g. through acquisition) that increase or reduce the capital assets of the local authority (acquisitions or sales, civil works).  Most sub-national public accounting systems are cash-based and thus do not include depreciation of the assets owned by the sub-national entity, although these concepts will often be used in administrative accounting, (e.g. in governmental asset valuation and management systems).

- ‘Investment Balance’ is the amount of the unfunded capital expenditure budget which must be funded through some form of investment (i.e. debt or equity) from outside the sub-national entity.

- ‘Operating’ expenses should include the expenses used to provide for operations. They are often considered as mandatory and repeat themselves relatively predictably and typically include salaries (payroll including social insurance and other charges connected to staff management), running costs, maintenance, and debt service paid by the subnational entity.

- ‘Operating revenue’ is revenue dedicated to operating uses of any kind. ‘Capital revenue’ is revenue dedicated to use for acquisition of fixed or movable capital assets.

- ‘Recurring’ revenue sources are any revenue sources the respondent believes with a high degree of confidence will come to the sub-national entity year after year with no foreseeable interruptions; for example, property tax revenues.

- ‘Non-recurring’ revenue sources are all other revenue sources, e.g. all sources of revenue that the respondent does not believe with a high degree of confidence will come to the sub-national entity year after year with no foreseeable interruptions; for example asset sale proceeds.

- ‘Operating Margin’ is defined as the Total Current Revenue minus Total Operating Expenses while ‘Net Margin’ is defined as the Operating Margin minus Debt Repayment. Reliably calculating these two amounts is central to the analysis of any subnational entity’s ability to incur first-time or additional multi-year debt intended for capital acquisition.

## 4. Sub-National Financial Management

This section asks respondents to assess their organization on a small number of key indicators of financial management quality, including:

- The sub-national entity’s current or prior experience repaying debt. Please note that **‘short-term’ debt** (typically used by public sector managers for cash-flow management purposes and repaid within the same fiscal year as it was borrowed) is defined here as any form of debt of less than 365 days’ final maturity.

- ‘Liquidity’ means easily accessible money in the form of cash and ‘equivalents to cash.’

- Public sector financial managers should be extremely conservative in defining 'equivalents to cash' as even the safest of short-term fixed income securities from a credit quality perspective, (e.g. locally-denominated national Treasury notes, highly-rated bank Certificates of Deposit, etc.) can lose principal value due to even normal market conditions or early redemption penalties if they must be cashed-in before maturity, in order to pay expenses.

- Please remember that **'Short-term' debt** can take a variety of forms, including:
    - use of over-draft privileges granted by banks on checking accounts;
    - loans from banks and other commercial financial institutions, other public agencies, and international development finance institutions;
    - vendor financing, e.g. 'time payment' terms in the purchase of goods and services, leases of less than one year duration, etc.; and
    - notes or other fixed income securities issued in the local capital markets.

- Please also remember that **'Long-term' debt** can also take a variety of forms, e.g. bank loans, bonds, lease-purchase transactions, etc.

- Several questions (Section 4.3) ask respondents to reflect objectively on the quality of financial information and monitoring; in reflecting on this vital area of financial management, respondents are asked to also think rigorously about how well various types of financial information are provided to both appointed and elected decision-makers.

- Independent **'credit ratings'** are provided by independent credit rating agencies. Independent **'credit ratings'** are given in two forms: to the entity itself as a measure of the entire entity's ability and willingness to pay debt service in full from all sources over which it has control ('general obligation' or 'GO' rating) and to each issuance of debt by the entity, as each issuance may have credit characteristics which differ from the GO structure in which the entity's full faith and credit is being pledged to investors.

- One or more rating agencies have established **'national rating scales'** for debt issued as notes or bonds in most countries' local capital markets. These scales – on which the local 'risk free' rating of AAA is typically granted to the national government's locally denominated Treasury bonds and sometimes to very high quality corporations - are used by local capital market participants and regulators in securities sales, trading, and fiduciary activities.

- Concerning the planning of **'capital expenditures'** (Section 4.4), respondents are asked to think of all forms of spending for any form of capital assets, including land, new buildings, improvements to existing buildings, fixed and moveable equipment, and major maintenance and repair.

- Respondents are asked to keep in mind that best practice capital expenditure planning systems, e.g. capital budgeting and similarly-named processes, should cover a significant number of years in the future, typically at least 3 to 5 years and have a 'rolling' character, i.e. be updated annually with the addition of another year in the future.

- Section 4.5.3 asks respondents whether **'climate change adaptation'** and/or **'Greenhouse Gas (GHG) reduction'** projects have been included in capital expenditure plans. Please use a broad definition of each of each of these terms.
    - Examples of **'climate change adaptation'** capital projects can range from improvements to sewerage and drainage in flood prone areas, to water supply leak detection/repair projects and increased use of rainwater collection/storage in places with heightened vulnerability to drought, to increasing the height of seawalls in coastal ports in places at increased risk due to rising sea-levels, and improving the resilience of vital public facilities to higher wind speeds in places vulnerable to more powerful cyclones.
    - Examples of **'Greenhouse Gas (GHG) reduction**' capital projects can range from installation of solar power and/or heating systems on public facilities land and/or buildings, capture and use of methane from sewerage treatment plants or landfills to generate heat or power, to energy efficiency or low emissions fuel improvements for mass transit systems or vehicle fleets.

## 5. SUB-NATIONAL FINANCE ENABLING ENVIRONMENT

The questions in this section refer to the legal, regulatory and other national, regional and local frameworks – as well as the financial and professional human resource market conditions -- within which sub-national entities must conduct their financial affairs.

- Respondents are asked to make their own best judgments in answering questions 5.1 through 5.6 most of which are substantially subjective in nature.

- Questions 5.7 – 5.12 seek judgments about the availability of professionally qualified consultants or staff.