



**Ministry of Local Government, Rural Development & Cooperatives  
Local Government Division  
Local Government Engineering Department (LGED)**

## **4.6 Guidelines for all due debts to GoB and other entities fully repaid according the schedule**

**Project Coordination Office (PCO)  
City Governance Project (CGP)**

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**Assisted by  
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## 1. Introduction

Rapid urbanization accelerated by industry led economic growth has been taking place in Bangladesh. Potential of economic growth in urban areas is worthy of notice. There are 335 Local Government Institutions which cover 8% of total geographical area of Bangladesh and 30% of total population, while accounting for 60% of total national growth. On the other hand, the negative impact of dramatic change in urban areas is observed. The negative impacts are because the functions of municipalities and city corporations prescribed in Local Government (Pourashava) Act 2009 and Local Government (City Corporation) Act 2009, which are very relevant to the demand of city dwellers and urban development, are not implemented in an appropriate manner. In order to improve the public services provided by urban local governments, several urban development projects are being or were implemented by Local Government Divisions (LGD) and local government and engineering departments (LGED) with financial assistance of different development partners and government's own funds. Based on the experiences gained through implemented projects, effective activities for improvement of urban governance have been formulated as a program that has been well accepted. The urban governance improvement programs have been implemented to ensure good governance of those urban local government institutions namely Paurashava for equal, social harmony and planned development. Initiating urban governance improvement, LGD and LGED with financial support of JICA commenced a project named City Government Project (CGP) in 5 City Corporations.

## 2. Justifications

Any growing urban area requires substantial investments in infrastructure, and there are very few CCs which receive enough in capital grants from national government to finance all their requirements. This shortfall requires that municipalities look for alternative funding sources, or face the prospect that infrastructure backlogs become insurmountable, with seriously negative implications for the quality of life and the economic productivity of the urban area.

Municipalities wishing to finance capital infrastructure in principle have a limited range of possibilities: *external resources*, such as, government capital grants, and *own resources*, such as any accumulated cash savings, annual operating surpluses, and borrowing, whether from state or private lenders. Borrowing is classified as own resources because the municipality must repay the loan from its own resources.

Municipality must honour all its loan obligations according to the schedule. Failure to effect prompt payment will adversely affect the raising of future loans at favourable costs of borrowing. In addition to the timely payment of the loans, the City Corporation must adhere to the covenants stipulated in the loan agreements.

To avoid problems meeting loan obligations, it is necessary to establish a balance between CCs' financial strength and repayment schedule of debt to GoB and other entities. In the context of the City Governance Project (CGP), one of the activities of the Inclusive City Governance Improvement Action Program (ICGIAP) is that "all due debts to GoB and other entities fully repaid according to the schedule."

### **3. Relevant Issues of ICGIAP**

#### **3.1 Tasks**

To strengthen the financial discipline in CC, it is necessary for CC to make repayments for all debts to GOB/other entities by complying with repayment conditions. CC should conduct the following steps:

Task 1: Review documents related to all debts with the Government of Bangladesh and other entities, and make budget provisions for full repayment according to schedule.

Task 2: Inform PCO about debt repayments due on a quarterly basis.

#### **3.2 Action by**

- Mayor
- CEO
- Accounts officer

#### **3.3 Indicators**

- 1<sup>st</sup> PR: Complied with
- 2<sup>nd</sup> PR: Complied with

### **4. Objectives**

To make the City Corporation authority capable of timely repayment of its debts to Government and other entities.

It has been found that in many instances, municipalities have failed to meet their statutory financial commitments and also the requirement to pay creditors on time, including repayments of loan installments and payments to other creditors. Municipalities should be aware that the practice of prolonging payments to creditors beyond the stipulated timeframe contravenes provisions of the financing agreements. As a means of boosting available working capital, the practice is unsustainable and therefore, not recommended, being contrary to sound principles of cash management and investment, which should be examined and put in place to effectively manage liquidity and working capital through a range of other means, including regular reviews of cash flow projections.

This Guideline presents tasks and procedures that should indeed be followed by the CC aiming to achieve the above ICGIAP activity, and consequently to establish strong financial management.

### **5. Relevant Organizations, Stakeholders and their roles and Responsibility**

#### **5.1 Role of City Corporation**

Section 79 of the Local Government (City Corporation) Act, 2009 provides that subject to the provisions of this act, rules, the Local Authorities Loans Act, 1914 (Act No. IX of 1914), and any other law in force at the time, the Corporation may, with the previous sanction of the Government, raise loans in the prescribed manner, and make suitable arrangements, to the satisfaction of the Government, for the repayment of the loans in such installments as may be

fixed.

(2) The Corporation may, and if required by the Government shall, establish and maintain such separate funds as may be necessary for the repayment of loans, and the Government may, among other things, require that any specified item of income of the Corporation shall wholly or in part be earmarked for and apply in the repayment of loans.

## **5.2 The Municipality may incur two types of debt, namely short-term and long-term debt**

### **5.2.1 Short Term Debt**

The Municipality may incur short-term debt only when necessary to bridge:

- (a) Shortfalls within a financial year during which the debt is incurred, in expectation of specific and realistically anticipated income to be received within that financial year; or
- (b) Capital needs within a financial year, to be repaid from specific funds to be received from enforceable allocations or long-term debt commitments.

The Municipality:

- (a) Must pay off short-term debt within a financial year; and
- (b) May not renew or refinance its short-term debt.

### **5.2.2 Long Term Debt**

The Municipality may incur long-term debt for purposes of financing its long-term strategic objectives to:

- (a) Provide democratic and accountable government for local communities;
- (b) Ensure the provision of services to communities in a sustainable manner;
- (c) Promote social and economic development;
- (d) Promote a safe and healthy environment; and
- (e) Encourage the involvement of communities and community organizations in the matters of local government.

## **5.3 Role of Local Government Division**

The Government may make rules consistent with Local Authorities Loans Act, 1914 (Act No. IX of 1914) as to which may include, inter-alia, the following:

- (i) the nature of the funds permitted to secure loans or against which money may be borrowed;
- (ii) the works for which money may be borrowed;
- (iii) the manner of making applications for permission to borrow money;
- (iv) the inquiries to be made in relation to such loans, and the manner of conducting such inquiries;
- (v) the cases and the forms in which particulars of applications and proceedings, and orders thereon, shall be published;
- (vi) the cases in which the Government may make loans;
- (vii) the cases in which local authorities may take loans from persons other than the Government;
- (viii) the manner of recording and enforcing the conditions on which money is to be borrowed;
- (ix) the manner and time of making or raising loans;
- (x) the inspection of any works carried out by means of loans;
- (xi) the installments, if any, by which loans shall be repaid, the interest to be charged on loans, and the manner and time of repaying loans and of paying the interest thereon;
- (xii) the sum to be charged against the funds which are to form the security for the loan, as costs

in effecting the loan;  
(xiii) the attachment of such funds, and the manner of disposing of or collecting them;  
(xiv) the accounts to be kept in respect of loans;  
(xv) the utilization of unexpended balances of loans either in the reduction in any way of the debt of the local authority, or in carrying out any works which that authority is legally authorized to carry out; and the sanction necessary to such utilization;

#### **5.4 Role of Potential lenders**

- Various Development Partners of GoB (JICA, WB, ADB etc.)

Creditworthiness means worthy of receiving credit. Essentially it is an opinion by third parties, mainly lenders, on whether debt service payments will be made fully and on time. A lender which has confidence in the long-term financial strength of the borrower, and in the ability and willingness of the City Corporation to pay its obligations in full and on time, will regard that City Corporation as creditworthy.

### **6. Necessary Tasks and Procedure**

To strengthen the financial discipline in CC, it is necessary for CC to make repayments for all debts due to GOB/other entities by complying with repayment conditions. CC should conduct the following steps:

#### **6.1 Review documents related to all debts due to the Government of Bangladesh and other entities, and make budget provision for making full repayment according to schedule. (Task-1 )**

Debt management is administratively relatively simple. It involves knowing the payments required per year over life of the loan, budgeting for the repayments every year, making the payments in full on the due dates, and keeping full records and documentation on all transactions. The administrative capacity required for this clearly depends on the number of loan agreements being maintained, but for small or medium sized City Corporations it will seldom be more than a part-time job for an appropriately skilled individual.

Far more important are the commitments and promises involved in managing debt, and on this, no mistakes should be made. Having promised to pay the CC should make payments on time and in full. The creditworthiness of a City Corporation will slip immediately if it fails to honor that commitment.

The City Corporation borrower should therefore ensure that nothing will prevent it from meeting its commitments in terms of the loan agreement. This will mean ensuring that audited financial statements are available on time each year; that key financial ratios are maintained; that debt service payments are protected when budgets are under pressure, and ensuring compliance with any other features of the loan agreement. Most of all, the loan agreement is a commitment to ensure that the municipality is financially well-managed, so that sustainable annual operating surpluses are achieved in order to provide for debt service payments.

Whilst the period for which loan/debt may be repaid will vary from time to time according to the requirements of the various lenders, cognizance is taken of the useful lives of the underlying assets to be financed by the debt, and, moreover, careful consideration is taken of the interest rates on the yield curve.

### **6.1.1 PROVISION FOR REDEMPTION OF LOANS**

CC may borrow from Institutions and set up sinking funds to facilitate loan repayments, especially when the repayment is to be met by a bullet payment on the maturity date of the loan. These sinking funds may also be invested. The maturity date and accumulated value of such investment must coincide with the maturity date and amount of the intended loan that is to be repaid.

### **6.1.2 Budgeted Financial Plan**

- On an annual basis, the Accounts officer must assess the City's financial requirements and determine the amount of funds that need to be raised from external service providers.
- Consideration must be taken of the limitations of the capital and operating budgets and the expected impact that any external debt raised may have on the budget.
- The City's standard budgeting process must be followed when assessing the funding requirements of the City and the need for long term funding from external sources.
- A cash flow statement should be prepared indicating the anticipated shortfalls and anticipated further income streams that will repay the short term and long term debt.
- Monthly cash flow reports should be used to indicate progress towards the repayment of the short term and long term debt.
- An operating budget reflecting the effect of the anticipated depreciation of the envisaged asset to be financed and /or capital costs on service charges is needed; and
- The impact of the financial plan on the capital and operating budgets must be considered and included in the budget.

### **6.2 Inform PCO about debt repayments due on a quarterly basis. (Task 2)**

City Corporation must make public an information statement setting out particulars of the debt, including the amount of the debt and the purposes for which the debt is to be incurred.

A copy of the information statement must be submitted to Council prior to the meeting on a quarterly basis to discuss loan status, together with particulars of –

- i. the essential repayment terms, including the debt repayment schedule; and
- ii. the total cost in connection with such debt over the repayment period.

The same debt repayment statement should be submitted to the PCO on a quarterly basis.

## **7. Responsible personnel for Implementation**

**Accounts Officer:** Following the loan/financial agreement with GoB and other entities, the Accounts Officer will take initiatives to ascertain the total debt outstanding and the yearly total tranche of loan repayments and accordingly make budget provisions in consultation with CEO.

**CEO & CC Mayor:** CEO will be aware of the provisions of the financial/loan agreements and timely repayment of loans taken from GoB and other entities and s/he will make sure a sufficient amount is provisioned in the budget to repay debts when due. CEO will follow up the repayment of installments and keep the Mayor informed of the repayment status.

## 8. Implementation Schedule

Necessary budget provision for yearly tranche of repayment of debts needs to be made following the loan/financial agreement with the GoB or other lenders and payment should be made as per loan/financial repayment schedule.

Activity	Task/TOR	1st Year				2nd Year				3rd Year				4th Year			
		1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
All debts due to GoB and other entities fully repaid according to the schedule	Task 1 Review documents related to all debts due to the Government of Bangladesh and any other entity, and make budget provision for making full repayment according to schedule																
	Task 2: Inform PCO about debt repayments due on a quarterly basis																

## 9. Cost of Implementation (if necessary)

CEO and Accounts Officer will consider the probable cost of implementation of the activity and prepare proposal for consideration of the Mayor and CC council.



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