

Bulgarian subnational authorities in the process of decentralization of the government

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Introduction

Bulgaria is an ex-communistic country, located in Southeastern Europe. The date November 10th, 1989 marked the beginning of the democratic changes in the country. A new Constitution was adopted and Bulgaria chose the way of democratic development and market economy.

Nowadays Bulgaria is a parliamentary republic and conforms to the Constitution of the Republic passed by the Grand National Assembly in July 1991. The Constitution of the Republic of Bulgaria is the supreme law of the country and no other law may contravene it. All international treaties, which are ratified pursuant to the constitutional procedure, are considered part of the domestic legislation.

The National Assembly is a one-chamber parliament. It consists of 240 Members of Parliament who are directly elected every four years. The National Assembly is a permanent acting body, directed by a board of Chairmen including a Chairman of the National Assembly.

The head of the state is the President, who embodies the unity of the nation and represents the Republic of Bulgaria in its international relations.

The Council of Ministers is the executive state body and directs the domestic and foreign policy of the country. The government manages the implementation of the state budget, organizes the management of state property and approves or rescinds certain categories of international treaties pointed out in the Constitution.

Bulgaria's foreign policy is oriented to cohesion with the European structures. The country has been a member of the Council of Europe since 1991. In 2004, Bulgaria joined NATO. In 1995, the country started the process of accession to the European Union (EU). On 25 April 25th 2005, in Luxembourg was signed the Treaty of Accession of Republic of Bulgaria to the European Union. According to European Commission's opinion, announced a few days ago¹: *"...As a result of the progress made, Bulgaria will be in a position to take on the rights and obligations of EU membership on January 1st, 2007..."*

Many attempts at reorganizing the structure of subnational system of government recently have been made in Bulgaria. The predominant trend today is to strengthen the decentralization in the country.

¹ European monitoring report on the state of preparedness for EU membership, published on September 26th, 2006.

Current reforms are viewed as a way to bring together the efforts of the electorate and the elected, assuring correspondence between national, regional and local interests. The achievements of legal stability also guarantee prosperity on both the subnational and national level and encourage the desired direction of the development of local government and self-government.

Generally, the administrative organization of the modern state exhibits the combination and sequencing of two principles: centralization and decentralization. Within the framework of its legal and political unity, the state defines administrative division of the national territory in order to govern efficiently and effectively. The latter expresses the tendency of modern democracies towards decentralization—the recognition of self-governance rights for the administrative divisions, which as a level of government are closest to individual citizens, while the highest authority rests with the state, ensuring the rule of law and the pursuit of common national interests.

1. Legislative framework

1.1. Constitution of the Republic of Bulgaria (RoB)

The structure and functions of local and regional authorities are provided in the Constitution of RoB. According to the Constitution, the Republic of Bulgaria is a unitary state with local self-government.

The territory of Bulgaria is divided into municipalities (obshtini) and regions (oblasti). The current legal regulation defines the regions and the municipalities as constituent administrative-territorial formations.

The region is an administrative-territorial unit that carries out the regional policy, executes the state government locally, and ensures conformity between the national and local interests.

The municipality is the basic administrative-territorial unit, where the local self-government is carried out. The realization of this government is an element of the organization of the state power. The local self-government is a decentralized form of state authority and has independent competencies. The municipalities have their territory, borders, population, name, and an administrative center. They include one or more neighboring settlements. Constituent administrative-territorial units in the municipalities are the mayoralties and the districts, established to fulfill the functions and competencies entrusted to them by law or with a decision of the Municipal Council.

The citizens participate in the government of the municipalities through the local self-government bodies elected by them, as well as directly through referendum and the general assembly of the population. The municipalities are juridical bodies separate from the state.

The Constitution affirms the model of the modern democratic state and outlines the principle of decentralization, admitting the right of self-government to the basic administrative-territorial units and preserves its supremacy and its control over the defending of the common national interests.

1.2. Additional legal texts

The main piece of legislation with regard to subnational authorities is the *Local Self-Government and Local Administration Act (LSfLAA)* adopted in 1991. This Act, in conjunction with the *Administration Act* and with the *Civil Servants Acts*, regulates the implementation of local self-government in municipalities and the functions of local administration.

The LsfLAA specifies primarily the area of competencies of local self-government on municipal level, defined as the right of the people and the elected by them bodies to make decisions, related to differentiated set of issues, like:

- the sphere of action of municipal self-government,
- the powers and duties of the mayors of municipalities and mayoralties, and the secretary of the municipality, the status of the personnel of municipal administration;
- the powers of municipal councils, the organization of their activities, the powers and status of municipal councilors.

The financial resources of Bulgarian municipalities and the transfer payments from the state budget are regulated in *Local Taxes and Charges Act*, *Municipal Budgets Act*, *Organization of the State Budget Act*, and the *Annual State Budget Act*.

In addition to the above mentioned laws, *the Administration Act* regulates the structure and main organisational principles of national and subnational administration and administrative positions, and charges regional governors and municipal mayors with executive power and specifies their competences and functions.

As a whole the legislative base is stable, although practices during the last ten years indicate that it should be further developed and improved. The main source of instability can be found in the area of the relations between the central executive power and the bodies of local self-government, which according to the political situation, often develop into conflicts. These are the situations that reveal the deficiencies of the legislative guarantees for the implementation of the constitutional principle of local self-government.

2. Territorial structure, functions of the subnational administration and associations of the municipalities in Bulgaria

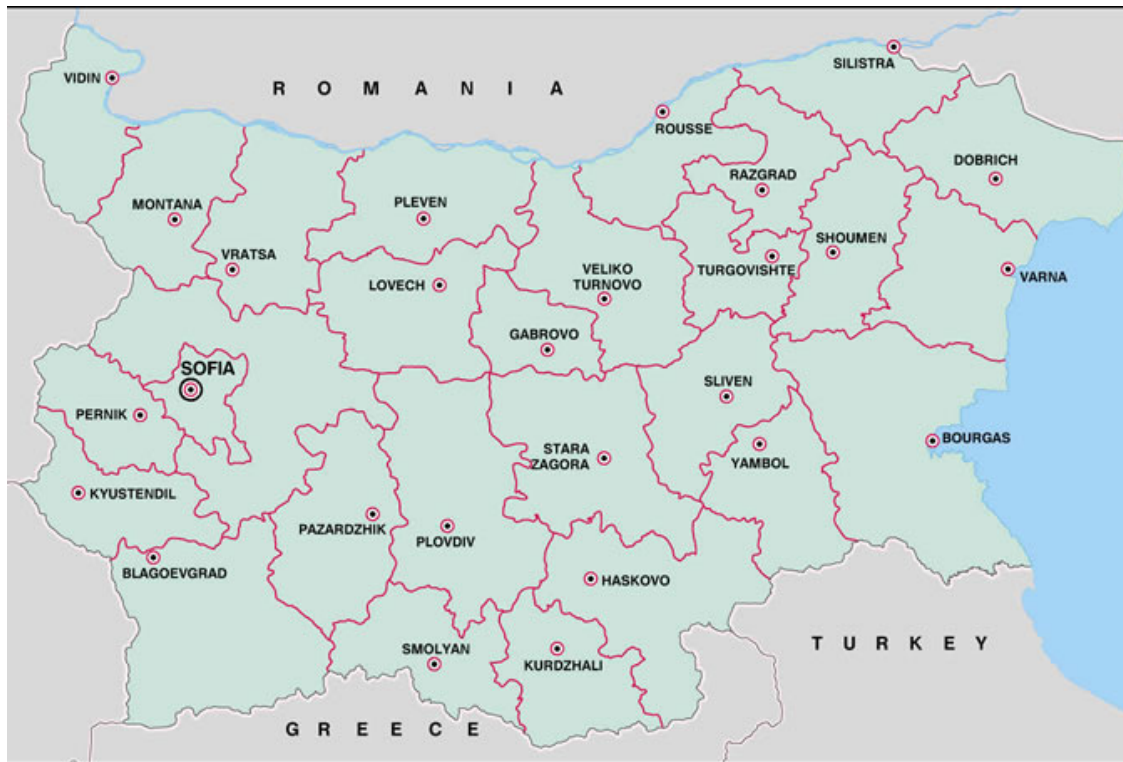
The territorial structure of Bulgaria is regulated by the Constitution and *Territorial-Administrative Division of the Republic of Bulgaria Act* (adopted in 1995), which confirm the two territorial levels: regions and municipalities.

2.1. Regions

By amendments to the Act of 1998, Bulgaria is subdivided into **28 regions** (*Sofia city, Sofia region, Plovdiv, Haskovo, Varna, Bourgas, Rouse, Lovetch Montana, Vidin, Vratza, Pernik, Kyustendil, Blagoevgrad, Pleven, Pazardjik, Smolyan, Kurdjali, Yambol, Gabrovo, Veliko Turnovo, Stara Zagora, Sliven, Turgovishte, Razgrad, Shoumen, Dobritch, Silistra – Figure 1.*), replacing the previously existing nine regions. The regional boundaries and their administrative centers are defined by a presidential decree.

In spite of the two-level division of the territory of the country – municipalities and regions, only the municipality is a territory of self-government. The Constitutional provision in this respect is explicit and not subject to interpretation. Article 142 specifies: “...*The region is an administrative territorial unit, which conducts regional policy, executes the policy of the state on local level, and provides for the balance between the local and state interests*”.

Figure 1: Bulgarian regions:



The region (oblast) is an instrument of deconcentrated state administration represented by a governor. This means, however, that a possible development of the regions as territories of self-government with elected institutions will require amendments of the Constitution itself.

Each region consists of one or more municipalities and its territory covers the territory of the included in it municipalities. In fact, all regions consist of more than one municipality. The case of the capital city is somewhat specific - the town of Sofia is divided into districts (which after the latest legislative amendments are not bodies of self government and the district structures are not elected by direct vote). However, the functions of the districts combine aspects of the level of self-government with aspects of regional policies. The town of Sofia has the legal status of a region, and at the same time both, the mayor of the town and the municipal council, are elected by direct vote.

The governor is the official representative of the government in the regions and is appointed directly by the Council of Ministers. The governor is assisted by a regional administration including a department for regional development. Under Article 31 of the *Administration Act*, the regional governor:

- Conducts state policies in the region, coordinates the work of the executive bodies and their respective administration within the territory of the region and their relations with the local power;
- Ensures compliance of national and sub-national interests, organizes the drafting and implementation of regional strategies and programs for regional development, implements coordination with the structures of local self-government and local administration;
- Is responsible for the protection of state property within the region;
- Ensures the observance of the law within the region and implements administrative control for the observance of legislation and administrative acts;
- Controls the implementation of administrative acts and the activities of self-government structures and local administration;
- Coordinates and controls the implementation of administrative acts by the executives of the territorial units of central administration and the executive power within the region;
- Organizes local civil defense, ensures the protection of the population in cases of natural disasters and is responsible for the maintenance of public order;
- Implements international contacts at regional level.

The activities of the regions and regional administration are entirely financed from the state budget, while the municipal budgets are composed of transfer payments from the state (differing in percentage) and own resources.

2.2. Municipalities

The current administrative territorial division of the country comprises **265 municipalities**. The administrative territorial subdivisions are the mayoralties and districts (rayons). There are 3 840 mayoralties, 24 districts in the capital (Sofia), 6 districts in Plovdiv and 5 districts in Varna. The municipality is an institution of self-government. Its managing authorities are the council and the mayor. The Municipal Council is a body of local self-government, and is elected by the residents in the municipality.

At the municipal level the deliberative body is the municipal council. Pursuant to the *Local Self-Government and Local Administration Act* the composition of the municipal council is determined according to the population of the respective municipality:

up to a population of 5 000:	11 councilors
up to a population of 10 000:	13 councilors
up to a population of 20 000:	17 councilors
up to a population of 30 000:	21 councilors
up to a population of 50 000:	29 councilors
up to a population of 75 000:	33 councilors
up to a population of 100 000:	37 councilors
up to a population of 160 000	41 councilors
a population of more than 160 000:	51 councilors
The capital municipality (Sofia):	61 councilors

The Territorial-Administrative Division of the Republic of Bulgaria Act stipulates that the population of a newly established municipality should be 6,000 people or more, the distance of its administrative centre from all belonging to the municipalities' settlements is not to exceed 40 km.

The Council as well as the mayor is elected separately by the population for a four-year term of office by direct universal suffrage. Separate direct elections are held and the mayor and the political majority in the council may well be from different parties.

The competencies of the municipal council are specified in detail separately, as well as the competencies of the mayor of the municipality and they are presented briefly in *Table 2*.

The Mayor is a body of the executive branch of government in the municipality. The Mayor of the municipality and the mayors of the mayoralities are elected directly. According to *LSfGLAA* citizens participate in local self-government by resolving directly - through general meetings, referendums, or in another manner - on local issues, or through the bodies they elect which formulate and implement the local policy in the interests of the community. Mayors and deputy mayors are banned from participation in the governing bodies of political parties, are banned from undertaking commercial activities and from sitting on boards for the time of their four-year term of office. The mayor appoints for an unlimited term of office a secretary, who organizes the activities of the administration.

Table 2: Competencies of municipal council and mayors in Bulgaria

The Municipal Council:	The Mayor of the municipality:
<ul style="list-style-type: none"> - establish the structure of the municipal administration and allocate funds from the municipal budget for staff wages; - elect and remove its Chairman. - elect and remove Vice Mayors and Mayoral delegates on the advice of the Mayor of the Municipality and in Sofia Municipality and the cities of district composition - the District Mayors as well; - determine the remuneration of Mayors within the existing regulations; - adopt the budget of the municipality, exercise control over its implementation and approve the relevant report; - set the size of local taxes and charges within the statutory limits; - make decisions on the acquisition, management, and disposal of municipal property, and define the Mayor's powers, and those of the District Mayors and other Mayors; - make decisions on the formation, reorganization, and termination of municipal companies, and designate its representatives in such companies; - make decisions on bank borrowing, interest-free lending, and municipal bond issues under terms and procedure provided by law; - make decisions on the design and approval of general and detailed territorial development plans for the 	<ul style="list-style-type: none"> - manages the entire executive activities of the municipality; - guides and coordinates the activities of the specialized executive bodies; - appoints and removes from office the senior management and the staff of the municipal administration, imposes the disciplinary penalties provided by law; - is responsible for the keeping of public order, and in order to ensure it, he shall issue ordinances binding the chiefs of the respective police departments; - organizes the implementation of the municipal budget; - organizes the implementation of long-term programs; - organizes the implementation of the Municipal Council decisions and reports to the Council accordingly; - organizes the performance of tasks deriving from Acts of Parliament, decrees of the President of the Republic, and of the Council of Ministers; - delegates his functions to mayoral and district mayors; coordinates and exercises control over the lawfulness and appropriateness of actions taken for that

<p>municipality or parts thereof;</p> <ul style="list-style-type: none"> - adopt municipal development strategies, projections, programs and plans; - define such requirements governing the activities of natural and legal persons within municipal boundaries as arise from the environmental, historical, social, etc., characteristics of the inhabited places, and from the condition of the existing technical and social infrastructure; - make decisions on the establishment and termination of municipal foundations, and on the management of donated property; - make decisions on the municipality's participation in local authority associations in this country and abroad, and designate its delegates to such associations; - create districts and mayoralties under terms and procedure provided by law; - make proposals respecting changes in the administrative and territorial division, such as affect the territory and the boundaries of the municipality; - make decisions to name or rename streets, squares, parks, engineering facilities, zones, recreation areas, etc., of local importance; - make decisions on the holding of referendums and general meetings on issues within its terms of reference. 	<p>purpose; exercises control over the lawfulness of the acts and actions of mayors in pursuance of their powers;</p> <ul style="list-style-type: none"> - keeps contacts with political parties, public organizations and movements, as well as with other bodies of local self-government in this country and abroad; - organizes and implements activities relating to defense from disasters and accidents; - signs general and detailed development plans as approved by the Municipal Council; organizes their implementation and enforcement; approves amendments and addenda thereto; - performs the functions of civil registrar; or delegates such functions by a written order to the mayors of mayoralties, which maintain civil status files or to other officials of the municipal administration; - represent the municipality before natural and legal persons, and the courts; - ensures the technical support of the Municipal Council.
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2.3. Planning regions

In compliance with the *Regional Development Act* and in addition to the formal territorial-administrative units, two complementary territorial divisions have been tasked to implement regional policy: planning regions and areas for targeted intervention. Regional development in Bulgaria is regulated by the *Regional Development Act*, promulgated in State Gazette No.14/20.02.2004. According to the Act stated above six planning regions are set up on the territory of the Republic of Bulgaria. The Planning Regions are formed on the basis of regions depending on their geographical location, economic development, number of population and prospects for development.

Planning regions are not territorial-administrative units according to the *Administrative-Territorial Division Act*. They are established for the purpose of regional development and regional statistics. They are to compensate for the shortcomings of the administrative regions (oblast) and to serve as a basis for drafting integrated plans and programs for regional development on a large territorial scale transcending the regions. They can also be seen as a response to the EU requirements for the implementation of regional policy, which designate regions of the NUTS-2 type as the main frame for planning, programming, implementation and monitoring, particularly as regards Objective 1 of the EU structure funds.

The six planning regions do indeed correspond in size to regions of the NUTS-2 type in the EU. They bring together between three and six of the 28 administrative regions (*Table 3*):

Table 3: Data on planning regions in Bulgaria²

Planning regions	Area (km ²)	% of the total area of the country	Population 2003 (persons)	% of the national total	Population density (persons / km ²)	Number of regions	Number of municipalities
Republic of Bulgaria	111001.9	100.0	7801273	100.0	70.3	28	265
Northwestern	10288.2	9.3	512593	6.6	49.8	3	33
North Central	18320.0	16.5	1165806	14.9	63.6	5	41
Northeastern	19923.4	17.9	1285803	16.5	64.5	6	49
Southeastern	14647.6	13.2	782653	10.0	53.4	3	22
South Central	27516.2	24.8	1944382	24.9	70.7	6	68
Southwestern	20306.5	18.3	2110036	27.0	103.9	5	52

2.4. National and regional associations of the municipalities in Bulgaria

- *National Association of Municipalities in the Republic of Bulgaria (NAMRB).*

The National Association of Municipalities was established in 1996 by one third of the Bulgarian municipalities. As a result of its active work more municipalities gradually started joining the association. Since the end of the year 1999 all Bulgarian municipalities have been members of NAMRB. Thus, the association has the power of being the only nationally representative local government organization and nowadays is the “voice” of local governments. Being united in their National association Bulgarian municipalities jointly stand up for their common interests. All mayors, municipal councilors, and experts in the various fields of municipal activity have the opportunity to contribute to the implementation of the initiatives of the various commissions, contact groups and working groups of NAMRB.

The General Assembly of NAMRB is the highest leadership body, and each municipality is entitled to one vote in this Assembly. The Board of Directors is comprised of 19 members, who are elected by the General Assembly for a period of four years. They elect the Chair and Vice Chairs of the Board. The Control Council is comprised of 5 members, who are elected by the General Assembly.

NARMB representatives in consultative councils and bodies (to the Council of Ministers or certain ministries) take part in the solution of problems, related to regional development, demographic issues and social integration, healthcare, development of small and medium-sized enterprises, culture, tourism, protection of the environment, European integration, child protection, as well as absorption of funds under the ISPA and SAPARD Programs.

Every year the Association holds negotiations with the Ministry of Finance on the framework of the municipal budgets where we stand up for the interests of our members. The association's position of the draft State budget is based on the multitude of proposals made by the municipalities and the expert working groups.

² *Sources: Cadastre Agency; NSI, current demographic statistics*

NAMRB is working together with more than 46 other organizations under different projects and programs. Those are the Foundation for Local Government Reform, the regional municipal associations, United States Agency for International Development (USAID), Local Government Initiative and lots of other nongovernmental organizations. Our association has been receiving since the very beginning of its establishment substantial assistance and support from the USAID, as well as by the municipal associations of Denmark, the Netherlands and other European countries. Since 1998 NAMRB has been a member of the International Union of Local Authorities and its European branch, the Council of European Municipalities and Regions. NAMRB is taking part in the work the European Union's Committee of the Regions.

- Regional associations of the municipalities

Under the Constitution of Bulgaria municipalities enjoy the right to form voluntary associations in order to solve problems and accomplish tasks of common interest. Based on this right, the following regional associations have been established:

- Association of Rodopi Municipalities;
- Association of the Danube River Municipalities;
- Association of the Black Sea Region Municipalities;
- Regional Association of Municipalities “Maritsa”;
- Regional Association of Municipalities “Trakia”;
- Regional Association of Municipalities “Podbalkanski obštini”;
- Regional Association of Municipalities “Central Balkans”;
- Regional Association of Municipalities “Hebar”;
- Regional Association of South West Municipalities.

Most of the regional associations of municipalities in Bulgaria were established in the late 1990s (1996-98), as independent voluntary non governmental organizations. Their mission is to take an active part in:

- Improving the local self-government and the legal framework of the local authorities;
- Increasing the efficiency and the transparency of the activities of the municipalities in implementing their individual and collective responsibilities and creating opportunities for a wide citizen participation in the local self-government;
- Economical development of the region.

The objectives of the associations are in the sphere of:

- Representation and defense of the member interests before the central authorities and their regional structures, before Bulgarian and foreign public organizations and other institutions for civil society development through support and assistance for a strong and open at the citizens local self-government;
- Cooperation and mediation between the municipalities in common strategies elaboration and realization of programs for a strong local self-government and civil society and for the sustainable development of the settlements in the region;
- Improving the knowledge and skills of the municipal councilors and officers for a stronger and open at the citizens local self-government;

- Survey and multiplication of the Bulgarian and foreign experience in the sphere of the local self-government;
- Enlarging and enriching the public understanding of the role and the importance of the local self-government and the citizen participation;
- Cooperation with related organizations in Bulgaria and abroad.

Regional associations are mediators between the member municipalities in providing information and exchanging positive practices. They stimulate the assistance between their members in developing projects, supporting the local self-government, civil society and the sustainable development of the settlements in a certain region.

3. Responsibilities and financial resources of subnational authorities

As was mentioned, the Republic of Bulgaria has a one-tier subnational budget system and only municipalities possess full powers of self-government. The 28 administrative regions do not form budgets on the basis of their own local taxes and charges and do not make expenditures for the corresponding territory and its population. As bodies of the central executive power, they receive subsidies from the central budget for the operation of their own administrations. Planning regions do not have any fiscal powers.

As a basic administrative and territorial unit of self-government, according to the Constitution of Bulgaria, the municipality is a legal entity and has many responsibilities, related to a various set of tasks, like:

- physical planning and territorial structure;
- municipal property, municipal enterprises, municipal finances, taxes and charges, municipal administration
- environment and rational use of natural resources of municipal significance;
- water supply and sewage treatment;
- street cleaning, refuse collection and waste disposal;
- local public transport;
- street lighting;
- maintenance and construction of local roads;
- health care (outpatient and hospital care, prophylactic and sanitation activities);
- maintenance of green areas;
- municipal housing;
- education (preschool, primary and secondary school);
- culture, including local libraries, theatres, museums and leisure centers.

The financial resources of local self-government are a vital guarantee for fulfillment of all mentioned tasks and activities. That is why this matter is also defined in general terms in the Constitution of the Republic of Bulgaria. According to Article 141 paragraph 1, every municipality is allocated an independent budget. The permanent financial sources of the municipalities are specified by the law and the state contributes to the effective functioning of the municipalities via the state budget and otherwise. The provisions of Article 140 have to be added to the constitutional guarantees of the resources of local self-government: “...*The municipality has the right to property, which is exploited in the interest of the territorial community*”.

Besides the Constitution, legal regulation of the municipal budgets is also specified in the *Local Self-Government and Local Administration Act*. On the other hand, the approved by Parliament annual state budget includes mandatory for the municipalities norms for adoption of their budgets. A special *Municipal Budgets Act* was adopted in 1998.

The constitutional, as well as the other legal norms on municipal budgets follow Article 9 of the *European Charter of Local Self-government*, which requires:

1. Intensification and expansion of the process of decentralization of power;
2. Correspondence between the financial resources of the municipalities and their competencies;
3. Right of the local authorities to sufficient independent resources in the frame of the national policy, which they can use freely for the effective performance of their competencies.

The independence of local authorities is determined by the amount of their own revenues. Financial decentralization requires that municipalities are delegated significant powers to generate revenues with which they could guarantee the local decisions on the amount, quality and type of locally delivered public services. In other words, municipalities should have real own revenues with levels defined locally and not centrally.

The autonomous of municipal budgets within the State budget was acknowledged in 1993. This means, in essence, that the State abandons the centralization of local budget surplus and the financing of local deficit. In the first years of decentralization process a great deal of attention was given to issues of revenue sharing and government transfers. Much less attention was given to an efficient and stable assignment of expenditure responsibilities to particular levels of government.

Despite the positive changes and the legislative amendments, made in the first years after the period of centralized economy and governance, the subnational financial system stayed almost unchanged. Like most countries in transition, one of the most severe problems that Bulgarian local governments were facing was the discrepancy between the responsibilities and powers of municipalities.

3.1. The reform of subnational financial system

Since the end of 2001 there was no clear distinction between local governments' responsibilities and responsibilities delegated from central government tasks. The financial system was highly centralized, with complete control over expenditures in municipal budgets, limits on local revenues and priorities of local governance regulated by the State Budget. Municipalities could not determine the local taxes and charges on their own. Local taxes were determined by law, and constraints were set for local charges. According to reported data for 1999, Bulgarian municipalities were free to influence in some way about to 18% of their total revenue base.

On 11th March 2002 the Council of Ministers established a joint Working group on Financial Decentralization with members: the Deputy Prime Ministers (of finance and of regional development and public works), representatives of other ministries (of education and science, labor and social policy, healthcare), the Audit Office, the Council of Ministers, the National Association of Municipalities in the Republic of Bulgaria, the Foundation for Local Government Reform. In June 2002 the working group developed and the Council of Ministers adopted a Concept and a Program for Financial Decentralization. Financial Decentralization Concept and the Program for its

implementation marked the start of the reform of local finance system with the purpose to increase the financial independence of municipalities and redefine the regulatory framework of intergovernmental relations.

The basic long-term objective of the Concept is “*to provide public services in quantities, of quality, and at prices corresponding to the needs of and affordable to the people, on the basis of long-term balancing of municipal expenditure responsibilities with stable revenue sources and effective civil control*”. Bulgarian municipalities and the Government agreed that this objective requires observation of the following principles:

- Creating a system of incentives which target higher local revenues, consolidated financial management potential, and the maximum level of local autonomy to determine the type, scope and provision of municipal services;
- Adopting simple financial relationship structure;
- Strict financial discipline followed by central and local governance;
- Monitoring and assessing the decentralization process by central governance;
- Considering municipal differences in terms of financial resources and management competence, and enabling municipalities with different potential to develop in accordance with their characteristics;
- Generating conditions suitable effective civil control.

The first steps towards financial decentralization in Bulgaria brought to division of all municipal-budget-financed public services into 3 groups:

- *State-delegated* services refer to those of the education, healthcare, and social establishment sectors, as well as, to some degree, services in the cultural sector. Operating expenses of State-delegated activities are calculated according to standards including personnel number, amount of salaries and insurance payments, and cost amount. The State serves to provide necessary financial resources for this group of activities, utilizing two sources: shared taxes and complementary subsidies. According to implemented changes, municipalities are deprived of revenues from corporate profit taxation at the expense of receiving 100% of the revenues from the Individual income tax (IIT). Additionally, the financing of State-delegated activities expenditures is determined by calculating their amount according to standards. Where revenues from IIT exceed the amount of expenditures, the municipality receives a percentage of IIT up to this amount and does not receive any complementary subsidies.
- *Local activities* include public works, maintenance of country roads, cost of kindergartens and nursery homes, and most activities in the cultural sector. Municipalities incur expenses for local activities up to the amount of their own revenues, which formed by local taxes, local charges and other non-tax revenues (municipal property management, fines, and so on).
- *Activities having mixed financing* include kindergartens and nursery homes. The cost of such establishments is financed from municipal revenues, whereas salary and social security expenditures are financed from government transfers.

After the implementation of the financial reform Bulgarian municipal governments have four sources of revenue: own revenues, state transfers, municipal property, and issuance of debt. The Constitution requires the Parliament to approve all taxes and tax rates, including at the local level. Data from the NAMRB indicate that between 7 and 10 percent of all tax revenues are devoted

strictly to local governments. Once the municipalities receive their subsidies from the central government, they have complete control over their own budgets. The only exception applies to money received for targeted national programs.

3.2. Municipalities' own revenues

Municipalities' own revenues are generated by:

- *local taxes*: property tax; donations tax; tax on the purchase of property for value; death-duty; other local taxes as regulated by law; and
- *local charges*: for domestic waste; for the use of markets, marketplaces, fairs, sidewalks, and roadbeds; for the use of nursery homes, kindergartens, social care homes, camps, hostels, and other municipal social services; for extraction of quarried materials; for technical services; for administrative services; for purchase of grave plots; tourist charges; and other local charges as regulated by law.

Currently, opportunities to increase local revenues relate to local tax rate fixing. However, the Constitution prohibits Bulgarian municipalities to fix rates and taxation bases. This conflicts with Art. 9.3 of *the European Chart of Local Self-Government*, signed by Bulgaria in 1995. Consequently, there is a need to find political consensus to amend the Constitution with a view to amend local tax rate levels by delegating powers to local authorities.

In 2004 the *Local Taxes and Charges Act* was amended especially in the area of local charges aiming at providing some financial advantages for the municipalities. Positive changes include the possibilities for the municipalities to impose, on their own, the rates of charges enumerated in the act, up to covering of the actual cost of local services provision, and to decide for what services prices will be required and how the revenues they yield will be utilized. Municipal council defines the level of each kind of charges, without any restrictions to minimum or maximum rates boundaries, keeping the principles as indicated by the law:

- covering the total cost of municipal service provision;
- creating conditions for enlargement of the provided services and increasing their quality; and,
- obtaining higher justice in defining and paying local charges.

Despite these possibilities, the gains from local charges are still very small in comparison with other budget revenues like taxes and government transfers. At the discretion of the municipal council for some of the services it is possible to set charges under the actual cost of provision. In this case the difference between expenditure and revenues is on the account of municipal budget. First of all, the matter in hand is the social services in relation to which the municipalities usually apply minimal charges.

For now Bulgarian local governments are not motivated to increase local charges and most of them are set at a quite low rate. Local charges are viewed by local governments only as an additional source of revenue for the budget. The significance of local charges, however, lies in the fact that they represent a small, but important part of the independence of local governments. Of course, there are other additional preconditions necessary for Bulgarian municipalities to enjoy the greater revenues they so much need. The charging policy at local level in Bulgaria should be designed in a

way to achieve in addition a broadened scope of using charges, an efficient use of resources and fair distribution of costs among users of services.

3.3. State transfers

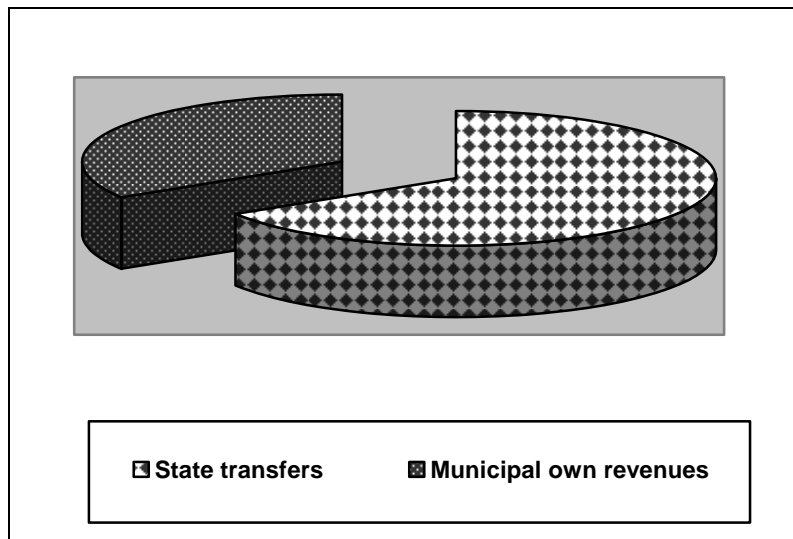
There are two types of transfers to municipalities:

- *Shared taxes*: Since 2003, municipalities receive 100% of proceeds from the Individual income tax. Percentages which secure revenues up to the amount spent for State-delegated activities are allocated for 35 municipalities with higher proceeds from this tax.
- *Government subsidies*: general complementary subsidy; general adjustment subsidy; and tied subsidies for investments.

All other taxes, not mentioned above (for example: Corporate income tax and VAT) are assigned to the national level of government.

Municipal resources of Bulgarian local authorities depend to a great extent on the transfers from the republican budget, as local taxes and charges are strictly specified and the income from public services is not sufficient to meet demand. The general conclusions on the part of the National Association of the Municipalities in the Republic of Bulgaria contain the grave statement that “...a completely wrong approach of underestimating and eliminating of the municipal sector as a factor in the process of development in the interest of the public has been adopted for the last ten years of transition to market economy”. Actually, the percentage of governmental transfers for the last 3 years, as a share in the total local budget, for most of Bulgarian municipalities is higher than 60%.

Figure 2: Share of state transfers and own revenues in the municioal budgets³:



³ Sources: Researches of NAMRB and LGI for 2004 and 2005.

The amount and the mechanism of allocating state transfers to municipalities are defined by the central government. The latter receive these revenues in three basic forms: shared taxes, general subsidies and tied subsidies. The total amount of state transfers is fixed in three basic ways:

- according to the source;
- on the basis of a formula;
- on a decision by the government.

The formula for the governmental subsidies in the case of Bulgaria is set in the annual State Budget Act and is calculated as follows:

$$\underline{S = S1 + S2 + S3}, \text{ where:}$$

- **S** is the total amount of the subsidy for a concrete municipality from the central budget;
- **S1** is the amount of the general complementary subsidy. It is calculated as a negative margin between the size of all State delegated activities and the size of shared taxes (for Bulgarian municipalities – the amount of revenues from Individual income tax.). *Where municipal revenues from IIT are less than expenditures or services, the municipality receives a complementary subsidy up to the difference;*
- **S2** is the amount of the general adjustment subsidy from the State budget for a concrete municipality. In Bulgaria only municipalities with low capacity to generate revenues receive *adjustment subsidies*. The size of the adjustment subsidy is calculated as follows:

$$\underline{S2 = (LTav - LT) \times P \times C}, \text{ where:}$$

- LTav is the average size of local taxes for the whole country per capita;
 - LT is the size of local taxes for a concrete municipality per capita;
 - P is the population of the concrete municipality;
 - C is a coefficient for distribution till the total size of the adjustment subsidy.
- **S3** is the amount of tied subsidies for investments.

Governmental transfers, as a part of municipal revenues, supplement own revenues. The equalization grants in Bulgaria try to bridge the difference between the fiscal capacity and the expenditure need of the municipalities.

The new system of municipal finance introduced in 2002 provided solutions to a number of issues. It solved the question of calculating the total amount of funds for the total complementary subsidy, i.e. the vertical allocation of financial resources between the central and the local authorities for State delegated activities. In general the division of the funding responsibilities for locally delivered services between the state and the local authorities, introduced with the start of the financial decentralization in Bulgaria, has allowed minimizing the transfer of responsibility for the inadequate funding of certain services. A powerful positive impetus was given to the issue of the clear and objective allocation of all types of state subsidies to municipalities. Clear and transparent rules are now in place for horizontal leveling of the capacity of municipalities to generate revenues. Still the fair distribution of the general complementary subsidy and the general adjustment subsidy remains a problem. In the current Bulgarian intergovernmental transfer system, the subsidies are negotiated

annually and are set in the State Budget Act. The amount of the subsidy affects the economic behavior of local governments. When Bulgarian local authorities do not succeed to maximize the size of subsidies they receive from the central government, they have to use another source for financing the provision of services. An example of a type of behavior is selling municipal property because of the lack of enough revenues (both from local taxes and governmental transfers).

To sum up, the major part of local tax revenues in Bulgaria comes from shared taxes and state transfers which are under full central government control. More local authorities have to rely directly or indirectly on reallocated funds and the more they need authorization on how to use own and reallocated funds, the higher is their financial dependence on the central government.

That is why there are still issues, which if implemented, will improve the balance of the central-local government financial relationship and these issues are connected with:

- Limiting the opportunities for the Ministry of Finance to set the expenditure standards and expenditure ceilings for state activities;
- Conservatism in drafting the state budget, which leads to chronic municipal deficit,
- Amending the Constitution of Republic of Bulgaria to allow municipalities to establish and administrate local taxes and charges,
- Delegating greater tax autonomy to the local authorities regarding the local taxes and charges,
- Placing under the administration of local authorities taxes like the business tax, the agricultural land tax, etc. and some national taxes, for example rental income tax, patent taxes, liberal profession income tax,
- Updating the rates of the property tax and/or changing the tax basis on the basis of the market value of real estates.

3.4. Current amendments, aiming further improvements of the financial relations between the different levels of government

As in many other countries, in Bulgaria, the process of decentralizing powers and responsibilities to subnational authorities is ongoing. Implementation of the government's medium-term financial decentralization program continued in 2005, and already texts amending the Constitution regarding the ability of municipalities to define local tax rates are being discussed in a parliamentary working group. However, any actual changes are still pending.

A major new development is the *Municipal Debt Act*, adopted in April, 2005, which regulates the opportunity of municipalities to issue debt for financing infrastructure and other capital projects. This act regulates all three opportunities for financing local infrastructure projects and specifies that central government doesn't act as a guarantor of municipal debts and that a week and a half after the Municipal Council's decision for borrowing is taken, the mayor submits this decision with additional information to the Ministry of Finance.

The *Municipal Debt Act* has increased the access of municipalities to resources, but there is still a lack of sufficient resources to address local problems and provide quality public services. This situation makes some local governments dependent on a few strategic local economic actors. Additionally, local governments feel more pressure to be on good terms with the central government rather than accountable to the local public. Even though there are mechanisms for transparency, as well as public and media

control over local authorities, these measures are not particularly effective at this stage of Bulgarian local government reform.

Conclusions

Bulgarian municipalities are assigned responsibilities for expenditures, which are secured with revenues – both own and transferred. In most municipalities revenues from taxes and charges are insufficient to cover the costs of delivered municipal services. That is why sub-national government bodies (municipalities) receive governmental transfers. The reform in the financial system introduced in 2003:

- Defined strictly municipal and state expenditure responsibilities as a first step towards proper structuring of municipal budget balances and gradually overcoming the fiscal imbalance of municipalities formed over time.
- Provided solution to the problem of calculating the total amount of the funds for the total complementary subsidy, i.e. the vertical distribution of the financial resources between the central and local government in respect of State-delegated activities;
- Established clear and transparent rules for horizontal leveling of the capacity of municipalities to generate incomes.

At the same time 4 years after the reform in the sphere of the subnational finances and the start of the financial decentralization, the major part of local tax revenues in Bulgaria comes from shared taxes and state subsidies which are under full central government control. More local authorities have to rely directly or indirectly on reallocated funds and the more they need authorization on how to use own and reallocated funds, the higher is their financial dependence on the central government.

As Bulgaria is preparing to join the European Union, the attention is focused on the close link between decentralization, regional administration and regional development. Actually, in the whole process of the decentralization in Bulgaria roles of the regions and regional administrations were belittled. The concept for decentralization, till now, was based basically on the traditional understanding of the process as a transfer of power and resources from the national to the local level and in Bulgaria was given a priority to the institution building at the municipal level.

Nowadays, 17 years after the collapse of the communism and 4 years after the implementation of the Concept for Financial Decentralization, the division of the responsibilities only between two levels - central government and municipalities - brought strengthening of the centralization and increase of the real power of the ministries and agencies. Furthermore, as many Eastern European Countries, Bulgaria is plagued by the problems of fragmented state administrative organization at the regional level. So far the tasks of central government at the regional level are mainly fulfilled by the field offices of the respective ministries. This has resulted in the lack of coordination of central government policies at the regional level. In particular, regional policy considerations have received too little attention and there is unnecessary duplication of organizational structures at the regional level.

In fact, according to the European Commission, six different models for local and regional self-government are known in Europe. They are based on different degrees of independence of the regional authorities from the central government. In each of the models the regional authorities are directly or indirectly (through the local municipal councils) elected by the citizens.

There are a number of open questions related to a possible creation of a second tier of self-government in Bulgaria. The initial effort in the early 90's was targeted mainly at strengthening local self-government. In 1995 the Government adopted a concept for administrative territorial reform, one of the main directions of which was the introduction of regional self-government, however, it was not implemented due to the economic crisis of 1996-1997. The 2001 program of the government envisaged a wide public debate on this issue which has not taken place in practice. A similar goal was set in 2005 program of the government and in the Strategy for decentralization, adopted in the summer of 2006.

It is a serious problem that when discussing regional self-government issues in Bulgaria the emphasis is put on the election of regional governors as well as on boundaries and centers, and important issues are neglected such as the appropriate territorial level (the 28 regions or the 6 planning regions), functions and competencies of the regions, resources and their own sources etc. In that respect, in the adopted Strategy for decentralization, large researches and analyses are envisaged in Bulgaria on the following issues:

- Is it possible and how for Bulgaria to introduce one of these six models in order to replace the direct appointment of regional authorities by the central government?
- What supplementary institutions and mechanisms are needed at local and regional level in order to improve the democratic system and horizontal accountability of the municipalities and regions in Bulgaria?

The administrative-territorial system of 28 regions and 265 local authorities implemented in 1998 may be regarded as a first step towards decentralisation and regionalisation. While the local level municipalities enjoy self-government, the regional level represents deconcentrated state administration. Nowadays there are definite plans to develop the system further. Besides, as Bulgaria has established the national goal of becoming a member of the European Union, it faces numerous challenges regarding the roles and relationships of the different levels of government – national, regional and local. Current conditions require continuation of the decentralization process and strengthening the role and the capacity of subnational authorities for successful participation in EU programs and funds.

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