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CASE STUDY 5

Enhancing the financial position of cities: evidence from Mzuzu

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About this initiative

Supporting the urban dimension of development cooperation: *Enhancing the financial positions of cities in developing countries to achieve sustainable urban development*

This initiative has been requested by the European Parliament. It is implemented by European Commission and UN-Habitat, supported by the International Growth Centre. These partners are working to identify relevant measures to help mobilise financing for urban development at all levels of government. The work has been undertaken through case studies conducted in Dakar (Senegal), Hargeisa (Somaliland, Somalia), Kampala (Uganda), Kisumu (Kenya), Mzuzu (Malawi), meetings with experts and practitioners, and empirical literature. The initiative works with an Advisory Group, chaired by Professor Sir Paul Collier from the University of Oxford, and consisting of representatives from the European Investment Bank, African Development Bank, UN Capital Development Fund, UN Economic Commission for Africa, and United Cities and Local Governments.

CASE STUDY 5

Enhancing the financial position of cities: evidence from Mzuzu

Author: Victoria Delbridge, Oliver Harman, Dyson Jangia, with Astrid Haas and Tony Venables

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Acknowledgements

The following city case study has been developed as part of the initiative 'Supporting the Urban Dimension of Development Cooperation: Increasing financial capacities of cities from developing countries to deliver productive and sustainable urban development' requested by the European Parliament as a pilot project and funded by the European Union.

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Summary

The case of Mzuzu illustrates how secondary cities, where revenues are often incredibly low and capacity is minimal, can innovate and lead the way on municipal finance reform. Mzuzu is Malawi's third largest city. The focus of this case study is a simple and fit-for-capacity property valuation system that increased realised revenues seven-fold between 2013 and 2018:[1] The Revenue Mobilisation Programme (REMOP).

Although the programme was initially seen to be a success, several serious misgivings continue to inhibit further progress. These centre on legal barriers in the current property valuation process in Malawi. More broadly, issues such as revenue pilferage, lack of capacity for financial management, land ownership disputes between spheres of government, and national rural bias continue to prevent Mzuzu from achieving a sustainable financial position.

For development partners, the example of Mzuzu provides a stark reminder of the vital importance of widespread stakeholder engagement and caution for legal obstacles in order to achieve sustainable project success. It also illustrates the potential of using smaller cities, with more flexibility and somewhat strong incentives for reform, as a useful starting point to trial new revenue enhancement innovations. The Development Fund for Local Authorities (DFLA), a special entity set up for small and low-cost loans to local governments in Malawi, also presents an interesting model for further exploration. By helping local authorities through the process of lending, they are building local government creditworthiness and enabling them to develop systems for future debt finance.

Malawi's cities, being some of the poorest in the world and in a country with relatively low level of urbanisation, are still at the beginning of the development curve. This early stage brings numerous challenges that are yet to be faced as well as an enormous opportunity to learn from the mistakes and successes of other cities in similar contexts. The cities are still at the critical juncture where they can invest in the urban infrastructure essential for livability and productivity before mass settlement takes place.

Key messages:

- Secondary cities, with more flexibility and strong incentive for reform, can be useful places for innovation and experimentation of new revenue models.
- Automated points-based property valuation works well as a low-cost, and fit-for capacity way to increase property tax revenues and keep valuation rolls up to date.
- However, widespread stakeholder engagement and co-generation is essential to ensure buy-in, understand vested interests and achieve long term success.
- The use of Geographical Information Systems (GIS) has far reaching benefits beyond improving property tax, including the identification of informal properties, as well as improved urban planning and management.
- Development partners tend to work through the national government, reinforcing the national rural bias in policy-making and investment.
- The DFLA can be a useful model for local governments to smooth cashflow and demonstrate creditworthiness for additional debt financing.

Urbanisation trends, challenges and financial needs

Malawi, the 'warm heart of Africa', is one of the poorest countries in the world, with a gross domestic product (GDP) per capita of around US$290 and 51 per cent of the population living in poverty.[2] Furthermore, it has a Human Development Index (HDI) of 0.418, ranking 170 out of 187 countries measured. The country also has a low life expectancy of 55 years. Apart from the unrest surrounding the recent elections, Malawi has been predominantly peaceful, with mostly stable governments since gaining independence in 1964. However, many of Malawi's indicators are similar to those of fragile states or war-torn countries.

The land-locked economy is heavily dependent on agriculture, which employs almost 80 per cent of the population, contributes almost 30 per cent to GDP, and is highly vulnerable to climatic shocks.[3] Manufacturing, such as food processing, construction, and cigarette production, contribute around 11 per cent to GDP; while the services sector, such as tourism, transport, health services, and banking, dominates the economy at 52 per cent. Despite its fragile economic state, Malawi has a real GDP growth rate of around 5 per cent and an unemployment rate of just six per cent (this is mostly due to subsistence farming). Given the challenging context, the national tax to GDP ratio is also reasonable, at 17 per cent in 2018.[4]

Malawi's population of 17.5 million is primarily rural, with only 17 per cent of people currently living in urban areas. However, estimates show Malawi as one of the most rapidly urbanising countries in the world, at over 5 per cent per annum.[5] The National Urbanisation Policy was published in response to this. It highlights that "past national development strategies have viewed urbanisation as a constraint to development rather than an opportunity that needs to be harnessed". Malawi's early stage of urbanisation gives it a unique opportunity to learn from the mistakes of cities further along the development trajectory. In particular, to actively plan ahead of urban settlement, investing in the necessary infrastructure required to ensure the maximum benefits of urban agglomeration.

The four urban centres in Malawi are Lilongwe, Blantyre, Mzuzu, and Zomba. Lilongwe was declared the capital city in 1975, and is the largest city in terms of population, at 989,318 people in 2018. Blantyre is the second largest city and is still the commercial and industrial centre of Malawi. It is located near to Zomba, the fourth largest city and the former political capital of Malawi, as established during the colonial era. Mzuzu, the focus of our case study, is the third largest city in Malawi, with a population of only around 221,272 residents in 2018, and with a further 1.7 million living on its outskirts. Although a small city, recent reforms have substantially increased its revenue collections, accountability and transparency – in some cases beyond that of the larger cities in the country.

Mzuzu's key urban challenge is its under-developed economy. There is much potential to leverage, with the city serving as a key gateway to the Tanzanian border, being home to well-known coffee production, and offering room for further processing of other agricultural products, such as fish, rice, and tobacco. Mzuzu is also home to one of the best universities in the country. As a secondary city run by an opposition party, it is often not prioritised for critical infrastructure investment and has gaps in terms of major roads as well as vital water, sanitation, and electricity infrastructure. However, the small city at preliminary stages of expansion is still able to make these investments before mass settlement takes place.

Stadium in Lilongwe, Malawi © Oliver Harman, IGC

Municipal finance and urban governance structure

Urban governance structure and mandate

Malawi has two spheres of government: National and local. While the classification of local governments can be as a city, town, municipality, or district, there is no stipulated institutional hierarchy between them. Together, the National Decentralisation Policy and Local Government Act of 1998, provide the legal framework for decentralisation in the country. The Act has been continuously reviewed and amended (most recently in 2017) to ensure that local governments are empowered to promote infrastructure and economic development within their area. The National Decentralisation Policy aims to eliminate dual administrations, as well as to promote accountability and participatory governance at the local level.

In urban areas, governance takes the form of a city council, made up of two parts: A political arm composed of elected councillors and led by a Mayor; and an administrative arm called the Council Secretariat, led by the Chief Executive Officer (CEO).[6] The Ministry of Local Government and Rural Development has oversight and responsibility for all local governments. For city councils, the Ministry of Lands, Housing and Urban Development also assists with strategic planning and urban policy.

The mandate of Malawi's local governments as stipulated by law includes the provision and maintenance of refuse and sewage disposal, city and feeder roads, water supplies, public amenities, as well as licencing and inspection of small and medium businesses. They are also assigned with managing healthcare centres, education, transport, agriculture, and the administration of land within their localities.

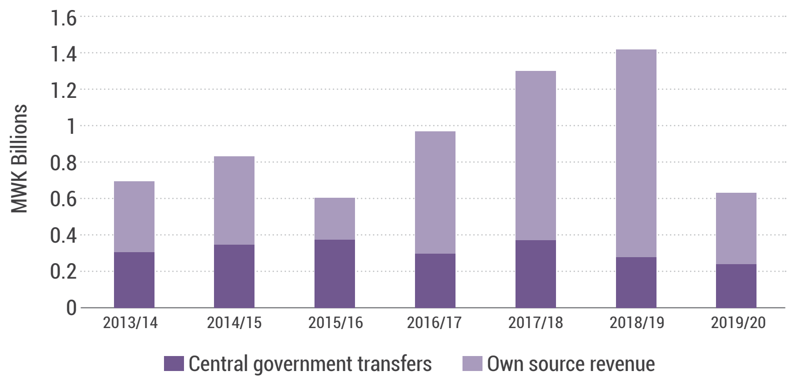
The law does not discern between urban and rural councils, but councils may request an exemption from functions that do not relate to their location. In reality, local governments often lack the resources to deliver on this mandate, requiring assistance from national government and development partners. Consequently, full devolution of powers, including land administration and fiscal decentralisation, is still not complete.

Municipal finance overview

Cities in Malawi struggle with a very narrow tax base, and low levels of collection. Because most of the Malawian population is rural, national government efforts focus primarily on uplifting the rural districts. This is reflected in the allocation of funds. For cities, central government transfers should make up less than 20 per cent of the total budget, given they have potential to raise revenues of their own. For rural local authorities this figure is 80 per cent. Development partners have provided some initial investments in necessary projects in an attempt to ameliorate particular urban challenges. However, there are often not enough resources in place to support the ongoing maintenance of these projects.

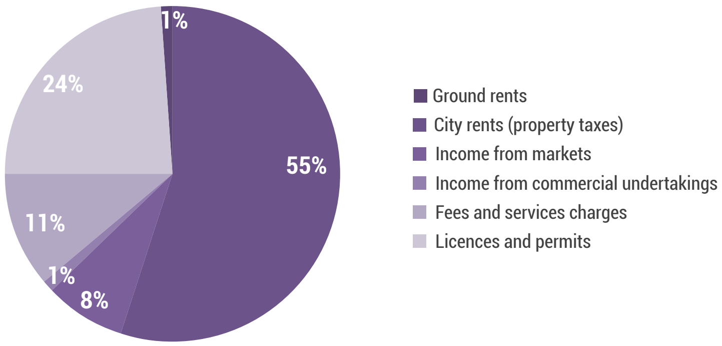
In Mzuzu, the 2019/20 budget is a total of Malawian kwacha (MWK) 2.4 billion (US$ 3.3 million), up 15 per cent from the previous year. Of this, MWK 414 million (US$ 563,000) or 17 per cent is due to come from central government, while own source revenues are due to account for MWK 2 billion (US$ 2.7million) or 83 per cent. However, the actual revenues are often much lower than predicted. Therefore, central governments typically end up contributing a far higher proportion of total revenue. The central transfers and own source revenue split over the last seven years is illustrated for Mzuzu in Figure 1 below. As the figure shows, there is wide variability and inconsistency of own source revenue collection.

Figure 1: Mzuzu total revenue breakdown by own source and central transfers from 2013 to 2020



Source: Data from the Mzuzu City Council.

Figure 2: Breakdown of own source revenues in Mzuzu for the year 2019/20



Source: Data from the Mzuzu City Council.

Section 68 of the Local Government Act empowers local governments to collect **own source revenues**. The principal sources of own source revenues include property rates (known as city rents in Malawi) and ground rents (a flat fee for rent of public land), business licences and market fees, service charges such as fumigation, and commercial entities such as city-owned guest houses and stadiums. The breakdown of actual own source revenues recieved in Mzuzu for the year 2019/20 is detailed in Figure 2, together making up a total of MWK 397 million (US$ 544,000).

The largest source of revenue for all local governments is property rates, as evidenced in Figure 2, at 55 per cent of all revenues. Cities in Malawi levy these property rates on the value of both land and improvements. According to the law, every property is rateable, but the cost of updating property registers as well as low levels of compliance means that achieving potential collection rarely occurs. Fees and service charges are the second most important revenue source, making up 24 per cent of revenues in Mzuzu, largely due to market fees.

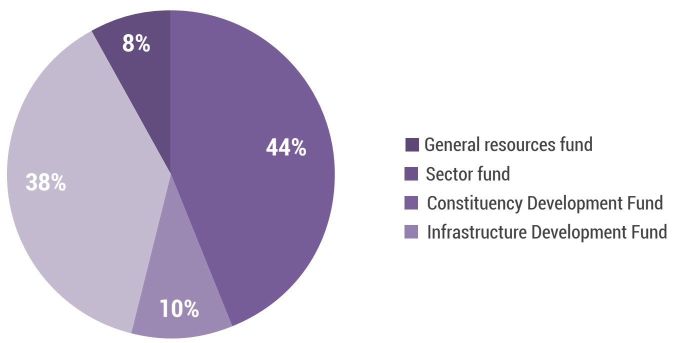
Some of the significant challenges faced in own source revenue collection are:

- City-owned property and infrastructure often require investment and maintenance before they can become revenue-generating, and the city councils do not have enough upfront capital to invest in this.
- Illegal vending prevents the city from collecting the required market fees. Also, the operational costs of many markets are much higher than the money coming in from them. Business licenses are better as the costs of collection are lower.
- Compliance with numerous fees and taxes is low. Most cities are severely lacking in by-laws to enforce this given the cost and technical expertise it requires.
- The tax base is constrained by the fact that 60-70 per cent of the urban population in Malawi live in low-income or informal settlements.[7]

Central government contribution and transfers come in several forms, both for capital investment and to cover operation costs. As is the case in many developing cities, the calculation of the amount transferred uses a formula based on population size and specific development indicators. However, it was asserted that it is also largely influenced by politics. Staff salaries, apart from those seconded to the council, are not covered by this transfer at the city level, while they are in their rural counterparts. In the cities, salaries must be paid from local revenues, which has resulted in a number of periods where city council workers have gone unpaid, in some cases for up to four months.[8]

The central government contribution to urban councils is often lower per-capita than for rural councils. A UNICEF report highlights that Blantyre and Lilongwe City Councils get the lowest per capita allocations[9], partly due to the majority of the population still being rural, and partly due to the presumption that urban councils have the means to raise sufficient own source revenues. The National Local Government Financing Committee (NLGFC) makes transfers and is mandated to disperse and manage operational and development resources for Local Councils in Malawi. It helps with improving financial management, budgeting, accounting, and auditing of local government finances. In Mzuzu, the relative allocation of all central government funding for the 2019/20 financial year is shown in Figure 3. The total amount transferred was MWK 241 million (US$ 328,000).

Figure 3: Breakdown of central government transfers to Mzuzu for the year 2019/20



Source: Data from the Mzuzu City Council.

Central government funds relevant to cities:

- **The General Resource Fund (GRF)** provides an unconditional grant that central government transfers to local governments every month, with an expectation that a minimum of a quarter will be used for service delivery. It is relatively small and usually used for operational expenditure. The Constitution stipulates that the central government should be contributing at least 5 per cent of national revenues to the local councils. However, councils profess that even though the national government collects significant revenues, they rarely end up transferring the legislated amount – currently averaging only 1.5 per cent.

- **The Infrastructure Development Fund (IDF)** helps to finance various infrastructure projects, such as the development of markets. It is only made available to the cities, and is the equivalent of the District Development Fund (DDF) for rural councils. The fund forms part of the National development budget but the choice of projects is discretionary to the councils based on their local development plans. Usually these are community projects chosen by the communities themselves in a participatory manner. Donor funds can be filtered through this fund, however, because the projects cannot be earmarked for specific activities they tend to prefer the LDF.

- **The Constituency Development Fund (CDF**) was introduced in 2006 with the intention to help develop small-scale projects that respond to immediate and short-term development needs. It comes from the same pot of funds as the IDF and is for the same purpose, but projects are selected by councillors rather than by the community in a participatory manner. The assertion is that this fund has not been used efficiently due to political interference and several irregularities have been found in the management of the fund.[10]

- City roads allocations are made to the **Road Fund Authority** by the **Road Fund Administration** to assist city councils with their mandate to maintain and construct new road infrastructure. The Road Fund Authority is a quasi government institution established by an act of parliament in 2006 and reports to the Ministry of Transport and Public Works.[11] The Road Fund Administration are mandated to collect and account for funds intended for road works in Malawi. These funds come from the fuel levy, parliamentary appropriations, donors and development partners. It does not show up in the budget of the local councils and is usually the most significant form of contribution to local governments.

- **The Local Development Fund (LDF)** was created in 2008 as a vehicle to pool resources from multiple development partners and national government to achieve local development initiatives. The LDF operates on a performance-based system, whereby more grants are provided to those who do well. Its size fluctuates over time, depending on development partner interest and central government investments.

For the 2018/19 financial year, the LDF allocation was only 1.7 per cent of the total national budget, or MWK 20 billion (US$ 27 million). It also has funds of US$ 107 million from the World Bank, US$ 25.7million from the African Development Bank (AfDB), and US$ 15 million from the German Development Group (KfW).[12] Donors prefer this fund as it allows funding to be ring-fenced for specific projects or types of projects.

In 2018, the LDF merged with the NLGFC, to further improve coordination of central government funding dispersed to local authorities. Policymakers acknowledge that the LDF and NLGFC are still trying to establish the legal structures to make it a coherent and coordinated institution for efficient financial management and local government development financing.

In addition to these funds, the government makes transfers of conditional grants to specific sectors, such as health and education. In theory, these should make up 9 per cent of national revenues to health and 15 per cent of national revenues to education. Together with the GRF, this means that a minimum of 29 per cent of national revenues should be transferred to local governments. While transfers of the national budget to local government have increased from only 5 per cent in 2015/16 to 17 per cent in 2018/19, this is still far below what the Constitution promises.

Other sources of revenues include:

Ceded revenues: Non-tax revenues that are collected for central government and then redistributed to local governments using a formula. Although legally allowed, Malawi is yet to operationalise many of these. As per the Decentralisation Policy, these include toll fees, fuel levies, vehicle registration fees, and industrial registration fees.

Borrowing and partnerships: These are somewhat unexplored sources of finance given the under-developed financial management capacity of cities in Malawi. The Local Government Act states that councils can borrow money from commercial banks and other lending institutions, as well as enter into partnerships with the private sector, provided the national Ministry of Finance approves these interactions. However, operationalisation of this legislative provision is problematic due to the Ministry's hesitation to guarantee such loans in fear of abuse and bloating the domestic debt burden of government. The Development Fund for Local Authorities (DFLA) is one exception that is explored in more detail below, but this has also been underutilised.

Development partner contributions: Although not always consistent, these contributions form a fundamental part of the financing of development and social protection in Malawi's local authorities. However, their provision is generally to the national level before it is transferred to the local governments.[13] In particular, both health and education allocations receive funding from the sector support budgets.

Development partners also contribute through the LDF. For example, the World Bank's Fourth Social Action Fund for Malawi (MASAF IV) implements public work programmes and social cash transfers, and develops local government capacity and administrations to take this forward.[14]

In terms of **expenditure,** cities in Malawi are forced to make difficult trade-offs - given both the financial and personnel capacity constraints - to deliver on their mandates. As detailed in the section above, many core 'development expenditures' are allocated by central government funds, leaving only personnel emoluments and other recurrent transactions as responsibilities for the city councils. The split between capital investment and recurrent operational expenditure averages around 50 per cent. Strong capital investment is a result of the IDF and CDF being earmarked allocations, which means they cannot be diverted towards operational expenditure .

Since the 2017/18 financial year, all city councils started rolling out **programme-based budgeting (PBB)**.[15] This approach is designed to ensure budgets are comprehensive and comply with international practices, classifying expenditure by programme, as well as economic, functional, and administration impacts. It also improves monitoring of individual budget lines.

For the 2019/20 financial year, Mzuzu prioritised infrastructure development, improved waste management, the establishment of the metropolitan police, and the improvement of Council employees' wellbeing, amongst other impacts.[16] More specifically, they focussed on the maintenance of the markets, cold rooms, and clock tower, as well as capacity building for waste management staff. They are planning the construction of a 10 km road running from the M5, connecting to Matete, then Mzuzu Technical College, and onto Luwinga, via the Botanical Gardens. The road will act as a by-pass for traffic passing through the city. Other city roads will also be improved from earth to formal gravel roads.

Comparing this to actual expenditure, however, the majority of funding still goes towards the Council, internal travel, and maintenance of city vehicles. Furthermore, there have been multiple incidents over the years where the city council has been unable to afford their staff wage bill – forcing them to sell land and property assets to make up the shortfall in revenue collection.[17] Given that actual expenditure was less than half what was budgeted - MWK 661 million (US$ 899,000) as opposed to MWK 2.4 billion (US$ 3.3 million) - it is unlikely that Mzuzu was able to meet its targets for the year.

Reforms undertaken to enhance the city's financial position

Capturing land value and unlocking dead capital

As mentioned before, property taxes, or city rates, make up the most substantial portion of all local governments own source revenues in Malawi. However, before 2013, property tax collection in Mzuzu was meagre, with several limiting factors:[18]

- The registration roll had only been updated once in the past 20 years and consisted of only 10,000 properties. This represented a quarter of the Council's estimated 40,000 properties in the city. This was due to the formidable valuation fees required to update the roll - the level of which was purported to outstrip current revenue generation - as well as the lack of market data, which was often unavailable or in poor condition.
- Where completed valuations occurred, the value of assessments was often incorrect, due to conflict or collusion between the property owners and valuers.
- The absence of formal addressing systems made the delivery of bills and follow-up for non-payments extremely challenging. Defaulters often managed to get away with not paying.
- Informal settlements, which make up 60 per cent of the city's taxable base, were not included. While this is not a legal prescription, the absence of market data in these areas made the valuation of land and improvements incredibly challenging.
- There was a lack of awareness and sensitisation of the community to the purpose and process of the property tax. This, combined with a lack of trust in the Mzuzu City Council to deliver services, reduced incentives for citizens to comply.

The lack of own source revenues generated in Mzuzu became particularly challenging when development partners made considerable investments in critical infrastructure, but left the city with no way to fund the ongoing maintenance and operations costs. The Council was in need of reforms to help capture land value and unlock dead capital.

In 2013, given the difficulties in own source revenue collection, the German Development Corporation (GIZ) were looking for a way to maintain a recent investment in waste management facilities in Mzuzu. They contacted the Revenue Development Foundation (RDF), a non-profit consultancy that supports governments to increase domestic revenues, to implement their Revenue Mobilisation Programme (REMOP) on a pilot basis. The programme was funded by GIZ, as well as the German Federal Ministry for Economic Cooperation and Development (BMZ), and cost between US$ 300,000 and US$ 400,000 in 2013. The REMOP was deployed over the duration of a full fiscal year to ensure that all procedures would be tested under conditions exactly similar to reality. Mzuzu lent itself well to the REMOP test because of the dynamism of its leaders, their desire for reform and the fact that, being a secondary town, it remained at some distance from the political influences of the capital.

The Revenue Mobilisation Programme (REMOP)

REMOP is an Urban Tax Administration System that automates the entire process of property taxation, from registration to billing and payments.[19] It employs a six-step methodology, which follows the tax year. The six stages of reform, as conducted in Mzuzu, are outlined below:[20]

1. **Discovery:** All properties were registered and given a unique number and index. The process included the identification of surrounding roads and buildings, as well as data collection on property attributes and location. Satellite imaging and GIS software were incorporated to improve property identification. The number of properties on the roll increased four-fold, from 10,000 to 40,000, at the same time enabling the Mzuzu City Council to introduce housing numbers and street names.
2. **Assessment**: A points-based Computer Aided Mass Valuation (CAMV) method was introduced to replace the more complex and expensive market valuation method currently in use. With the points-based method, additional points are added to a property for

positive features, such as having a paved road, a tiled roof, and security features. Similarly, points are deducted for negative features, such as no access to electricity. A more detailed explanation is provided in Box 1.

A comparison study found that, although producing no absolute values, the points system mimics market valuation very closely, as shown in Figure 4, below. A vital benefit of this method was that properties in informal settlements, where there is no market data available, could be included in the assessment, dramatically widening the tax base.

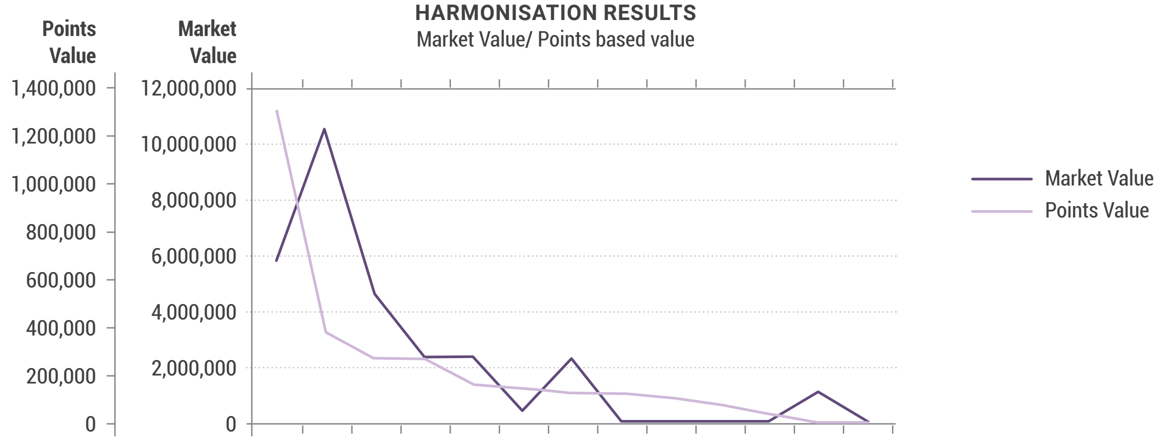
3. **Billing**: The REMOP software automates the updating of outstanding bills, including the systematic delivery of Rate Demand Notices, to all taxpayers, as well as notification upon receipt. The billing period was changed from quarterly to annually, which also helped to ease the administrative burden. To enhance transparency, the demand notices sent out detailed all the characteristics that influenced the value of the property.

4. **Sensitisation**: Implementing the new system required a strong sensitisation strategy. A campaign titled, 'My City, My Responsibility' was rolled out to inform Mzuzu residents of the new system, as well as their rights and obligations. The campaign took care to explain the link between taxes and public services to be delivered to encourage buy-in. It achieved this via weekly radio announcements, posters, billboards, newspaper articles, and updates at ward meetings. Special information meetings were also held with various community business leaders and the elite, given they are responsible for most of the property tax. In Mzuzu, the top 100 of these taxpayers shoulder 30 per cent of potential revenue.

5. **Collection:** The process was restructured from door-to-door collection to payments via banks. This change was a way to reduce pilferage, increase the taxpayer's trust, make payments more convenient, and allow the recording of transactions. The 60 per cent collection rate described by Council staff is relatively high in comparison to other cities. A branch of the bank was encouraged to set up at the Civic Centre to leverage the time of change. This financial hub started the process of creating a 'one-stop-shop' for all citizens' services.

6. **Compliance:** Defaulters were issued with a summons to court. Again, wealthy business people were targeted, as they were liable for a substantial portion of the city rents. The introduction of the court summons yielded initially positive results, as people preferred to pay to avoid the embarrassment. In addition to the social pressure, the prompt sending of bills and follow up letters meant that the Mzuzu City Council could go ahead with legal proceedings, having followed all due protocol. In the past, delays in sending invoices and following up often meant missing the period in which taking legal action was allowed.

Figure 4: Market valuation versus points-based valuation in Mzuzu



Source: Chirambo and McCluskey, 2019.

Box 1: Points-based property valuation

Researchers from the International Centre for Tax and Development (ICTD) have studied and piloted a methodology that uses both surface area and easily observable charactersitics to arrive at an estimated market value. Points are added to a property for positive features, such as having a paved road, a high quality roof type, and security features, meanwhile, points are deducted for negative features, such as no electricity. The system is more nuanced than a basic area-based valuation but is more straightforward to administer than a comprehensive market-based system. Therefore, area is still a fundamental determining factor, but with the addition of other housing elements to get a more accurate reading. The application of adjustment factors to each element depends on how the improvement changed the market value. Different methods can be applied depending on the property's classification, either as residential, commercial, or industrial.

Some of the key features of this method include:

- Simplicity: Although there is a trade-off between simplicity and precision, the system is adaptable to the requirement.
- Breadth: It allows the city to assess properties in informal settlements where market data is unavailable.
- Effectiveness: The use of computer-aided mass appraisal also reduces the cost and makes valuation easier to conduct and monitor.w
- Accuracy: It allows for a more detailed breakdown of what elements add to the value of a property, rather than having a total figure for land and one for the value of improvements, as in the market-based system. While the value is likely to be more aligned to the services the house receives, it may be less likely to match the market value.
- Progressivity: Accounting for property characteristics sees the more financially able paying more, but is still less progressive than market valuation.

All of the above are suggested to have strong potential to improve transparency and accountability, curb revenue leakages, and enhance voluntary taxpayer compliance.[21] However, face difficulties in the progressivity of the tax and legal barriers to formal adoption in many countries. The system has been piloted in more than 12 local authorities in Sub-Saharan Africa over the last 10 years, with Mzuzu being among the first.

Source: Fish, P. (2018)

The result of REMOP was a seven-fold increase in property tax revenues, from MWK 50 million (US$ 68,000) in 2013 to over MWK 350 million (US$ 478,000) in 2018. This increase allowed the city to noticeably improve service delivery in garbage collection, street lighting, and road grading, as well as pay off liabilities. For example, Figure 5 shows a waste management vehicle financed with income derived from REMOP.

Figure 5: Waste management vehicles financed with REMOP revenues

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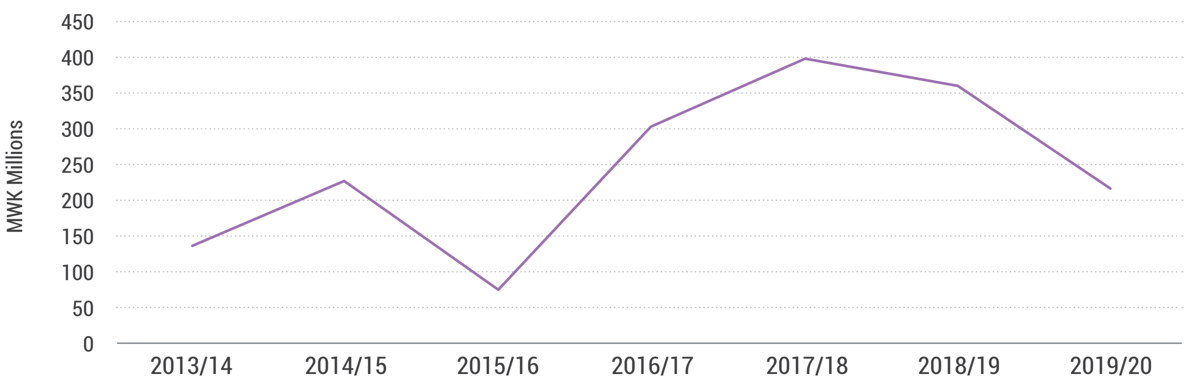
It also proved to be a more straightforward, transparent, and lower-cost way of valuing properties. The project cost between US$ 300,000 and US$ 400,000 in 2013. As a comparison, the current Quinquennial Valuation Roll (QVR) - the standard valuation process in Malawi - is costing the Blantyre City Council US$ 1.9 million, six years later.

Despite the initial successes of REMOP, a number of challenges were highlighted - both general challenges with the implementation process, as well as more fundamental challenges with the use of this methodology within Malawi's legal framework. Figure 6 (above) outlines this, with substantial growth in revenues somewhat tapering off in recent years. The more fundamental issues have halted any further progress in entrenching the new valuation system in Mzuzu, as well as inhibited its expansion to other cities in Malawi.

Challenges with implementation

- **Poor quality data:** During the discovery phase, fieldworkers were given targets for the number of houses they had to collect data on and register each day. This incentivised the fieldworkers to rush the process, leading to compromised data that did not always accurately reflect the properties characteristics or location. For example, recording properties with incorrect amenities, such as additional outbuildings or different building materials. Incorrect locations meant invoices were sometimes sent to the wrong people.
- These issues led to a large number of appeals. However, 80 per cent were associated with incorrect names associated with plots, a consequence of poor land tenure security. The remaining 20 per cent required return field-visits to collect better quality information. Technicians noted that in future rounds of registration, fieldworkers should be given more realistic targets and have a detailed and precise checklist of information they are required to gather.
- **Confusion over the points-based valuation methodology:** Despite the extensive sensitisation campaigns, the community was not sufficiently educated on the point-based methodology. Many citizens, on receipt of their bills, were confused as to why certain elements, such as their 'view' or 'roofing type', affected what they pay for public services. To handle appeals, senior people in the Mzuzu City Council, including the Directors of Finance, Planning and Administration, as well as the Chief Executive Officer (CEO), held open days to listen to people's hesitations and objections. In some cases adjustments were made, but usually the approach was to explain to people how the points-based system worked. It was noted that in future, there should be fewer factors included, and the city council needs to be able to account for how these factors relate to the services households receive from the council.
- **Lacking legal framework to enforce penalties:** It became clear through the systematic implementation of REMOP, that the legal framework and penalties available to local governments to enforce compliance with taxes are lacking for all cities in Malawi. For example, the city councils have to wait three years before they can seize a property to recover rates. Additionally, if a tax payer defaults on a payment, they are not cut off from services, thereby reducing the incentive to comply.

Figure 6: Mzuzu revenue generated from property rates, 2013 to 2020



Source: Data from the Mzuzu City Council

Figure 7: Building the social contract in Mzuzu

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Weak social contract: There is strong mistrust between the people and local governments in Malawi due to pilferage, inefficiency, and the general mismanagement of public finances. People will contribute if they know the local government will spend the money on services, however, the perception is that this will not be the case. There are also too many separate departments collecting taxes from individuals and businesses at both the national and local level, which is very time consuming and confusing for citizens. They are often not able to discern between which government entities they have paid, and what services this payment should bring them. Communication campaigns, such as the one pictured in Figure 8, are being used in an attempt to strengthen the social contract.

Fundamental challenges with the new system

- **The Local Government Act stipulates valuers should use market valuation:** One of the main challenges following the implementation of REMOP in Mzuzu, was the lack of legal provision for the points-based valuation method under section 68 of the Local Government Act (1998). Instead, the Act calls explicitly for market valuation, such as assessment using rental or capital values of the properties. While the use of the points-based method for the pilot in Mzuzu was authorised by the Chief Valuation Officer, applying it to the whole city was not. Despite this, the programme went ahead, but left the current rates without legal grounding, held up only by voluntary compliance. Figure 6 suggests that this voluntary compliance has been waning as people have begun to realise that they cannot be held legally accountable. The negotiations for sign-off with the Department of Lands, Housing and Urban Development are still ongoing.

- **The Act stipulates that Valuers registered with the Surveyors Institute of Malawi (SIM) must complete the valuation:** However, REMOP in Mzuzu was undertaken by an external expert from the RDF. As mentioned above, although there was a registered surveyor from Mzuzu University involved in the pilot project, they pulled out when the project was expanded city-wide due to legal and ethical conflicts. The Mzuzu City Council has argued that although they are willing to work with SIM to find ways to incorporate them into REMOP in the future, the current fees charged by the valuers are exorbitant. One of the key benefits of REMOP was its low cost, and the cost charged by valuers for market valuations prevents the city councils from keeping their registers up to date. The fee, as prescribed by law, is a maximum of 1 per cent of the properties valued.

The surveyors refuted this claim, stating that they had always been open to negotiating their fees depending on the economic climate and ability to pay. They were also willing to negotiate depending on the number of houses undergoing valuation. For example, rather than the 1 per cent charged for individual houses, they could charge closer to 0.5 per cent per household when undertaking an entire QVR process. There is the option of conducting annual supplementary valuations, so that each year the system updates with the inclusion of newly built properties, meaning the QVR is not so expensive at the end of the five years.

The case of Blantyre's new QVR provides an example of this approach. In Blantyre, there are around 80,000 properties set to be valued. Updating the QVR through market valuation has been procured for MWK

1.4 billion (US$ 1.9 million), an average of MWK 17,500 (US$ 24) per household. By way of comparison, it was estimated that revenue from property rates equal approximately MWK 3-4 billion (US$ 4-5.4 million) over the year, with the potential to rise to around MWK 7 billion (US$ 9.5 million) per year with the updated roll. If accurate, it thus costs - at most - half of the yearly revenue from property rates to update the QVR every five years. However, this still exceeds the cost of the REMOP system.

- **Points-based system results in higher rates than market valuation:** Some of the stakeholders asserted that the REMOP points-based valuation system was not scientific enough. It was stressed that, given it is more rudimentary than market valuation, it frequently categorises properties into higher rates brackets than the market valuation would, making it inconsistent with the local economy and people's ability to pay. Figure 4 shows that while mirroring market values broadly, it does tend to flatten the distribution, potentially making the tax more regressive. This reinforces another fundamental challenge: residents simply cannot afford to pay.

- **There was already an existing QVR running:** As was mentioned above, the Local Government Act specifies that the QVR should be updated once every five years. However, the assertion was that the Mzuzu City Council implemented REMOP at the same time as an existing QVR was running, and hence rendered the REMOP valuation legally invalid.

- **REMOP does not solve the challenge of lacking political will:** A number of stakeholders stated that the real reason behind the outdated property register is the fact that it takes a lot of time and resources. Therefore, rather than the cost of the valuation, it is the lack of capacity and political will of the city councils that is the main impediment. It was stated that if the city councils were proactive in following up and collecting from all the houses registered on the QVR, the cost of valuation would not be so large, and the valuation method would not make a long-term difference in the maintenance of the register. The assertion was that without constant support from external partners, the city council will not maintain it - even with the points-based valuation - as it still requires input and effort.

The way forward for property taxes

Although the REMOP system was a success in generating increased revenues, the political economy of the valuation method it employed has left it at a standstill. The line between professional protectionism and merited concerns is blurred. Although the Mzuzu City Council is confident that a resolution will be found and that they will be able to continue with the new method, others are not convinced. As it stands, the property tax system operating in Mzuzu is not legally compliant and is relying on the voluntary compliance of its residents. Furthermore, the city have been unable to register any new properties developed using this valuation method, which has meant the proportion of city properties registered has declined to 60 per cent.

This lack of legal clarity has been a significant barrier in expanding the system to other cities in Malawi. The CEO's of all three other city councils have actively requested support to implement the same system as Mzuzu. One of the fundamental reasons in preferring the points-based system to the market-based one is that informal properties, which do not provide formal market data, could be incorporated into the valuation process. Another key element is the use of GIS identification and the automation of their systems.

Until acquiring more clarity on the legality of the use of the points-based method, Blantyre recently initiated an adapted version of the REMOP process to create an updated QVR that complies with current regulations. They are using market valuation with certified valuers for all formal properties, while incorporating informal properties into their register as 'special rating areas' and charging flat rates.

They are also focussing on improved use of GIS, explaining that GIS is the key component that improves the billing and identification of properties, particularly infill properties or properties that have undergone renovation and are otherwise hard to spot. The GIS system also helps in the collection of other revenues, such as fees from markets and trading centres. In addition, digitisation and geographical data have spillover benefits to other areas of city management, such as the identification of flood zones and properties on fragile land.

Box 2: The political economy of surveyors in Malawi

A large component of the resistance to the REMOP system comes from the surveyors and SIM. Together, they have managed to stop the REMOP system in Mzuzu from being legally signed off and have halted the progression of the system to other cities in Malawi, despite significant interest. While citing many legitimate reasons, others stated they were merely trying to protect a well-guarded profession for their benefit, at the cost of the public good. Programmes like REMOP have the potential to reduce their source of livelihood, and they are condemning it to protect their income.

There are strict rules around becoming a qualified surveyer/property valuer in Malawi - one needs to have a relevant qualification in land management, work under a professional valuer for two years and submit a diary of experience, and then pass a final exam. This is costly, and because of the strict requirements, there are only 24 qualified valuers in the entire country.

The profession is also highly privatised, with little interaction and influence from government employees. As a result, the surveyors feel that the methodology they employ is necessarily more sophisticated than simplified indicators predicted using machine automation. They believe the new methodology will fall short of internationally prescribed standards that are not worth sacrificing.

However, others have noted that with only 24 registered surveyors, it is very difficult to conduct market valuations for every building in each district every five years. Some automation is always going to be necessary, is more cost efficient, and provides a more efficient service to the public overall.

Optimising other land-based revenues

Many stakeholders asserted that better management of urban land was a crucial factor in enhancing their financial positions. Apart from the city rents, urban land can provide revenue in the form of:

- **Ground rents**: These are an annual levy on public land, charged at a flat rate payable to the owners of the land (either a Ministry, housing corporation, or local government authority). The current collection is almost negligible across all local and national governments in Malawi, because the rates were last reviewed in 2005 and are extremely low, and because the systems to operationalise, monitor, and enforce them are lacking.

- **Returns on land-based investments:** Significant revenue could be generated by investing in city-owned land and generating an ongoing return. For example, guesthouses, shopping malls, and stadiums. Although some of these investments have already been implemented and running for many years, the norm is to sell the land at low prices to provide immediate income, spending this on consumable goods rather than long-term capital gain. Contributing city-owned land to large commercial ventures in exchange for a share of revenues was also posited as a way to better leverage city assets.

- **Sale of serviced plots:** Currently, the supply of serviced land for housing, industrial, and commercial uses is statutorily placed in the hands of the Department of Lands, the Malawi Housing Corporation, and the Local Authorities. They each have their respective target groups of high, medium, and low-income populations. However, the supply of serviced plots has always fallen short of demand, increasing the cost of land and resulting in wide-spread informality encroaching on peri-urban land that is typically managed by traditional chiefs.

There is potential for the undeveloped land that is undergoing severe encroachment to be serviced and allocated to developers, with the associated development charges generating a source of revenue for the councils. This would also have a multiplier effect of increasing the property stock and hence increasing property rates and ground rent. Cross-subsidisation of plots for low income residents by plots for high-income developers can also reduce informal settlement development. The significant challenge to enact this is the limited portfolio of land administered by the city councils and lack of clarity over ownership.

Realising the potential of investment in improving infrastructure

Although the Local Government Act decentralises most responsibilities, the Public Financial Management Act stipulates that local governments cannot take loans without prior approval from the National Government Financial Committee. The Ministry of Finance assesses projects that require loans based on their bankability and potential to generate revenue. The Ministry of Finance is then the official custodian of the loan, taking on all liability if anything goes wrong. Given this onus, the national government is hesitant to encourage borrowing for local councils. One exception to this is the DFLA, which is a special unit designed to assist local governments with inexpensive loans to maintain municipal services and invest in infrastructure. PPPs are another option being explored to leverage private investment, but difficulties mean that grants and loans from development partners are still the mainstay for infrastructure investment.

The Development Fund for Local Authorities (DFLA)

The DFLA is a special unit designed to assist local governments with inexpensive loans to maintain municipal services and invest in infrastructure. It was initiated in 1993 by the World Bank funded Local Government Development Project, but was recently brought under the national government for ongoing management. This change has reignited interest in it as a source of infrastructure financing. However, it desperately needs recapitalisation to finance larger infrastructure projects to be of use to urban local authorities in Malawi. One of the key goals and benefits of the

Box 3: The Development Fund for Local Authorities (DFLA)

The DFLA was founded in 1993 with the primary purpose of increasing the capacity for revenue generation in Malawi's local governments. It is a revolving fund, with seed capital of MWK 8.7 billion (around US$ 12 million). Initially, the World Bank provided this sum as 50 per cent grant and 50 per cent loan, and the fund survived by giving out good loans at a competitive rate, with minimal delinquency and arrears. They offer two products, the first is a commercial loan, covering projects that will generate income in a short amount of time, and the second is a longer-term infrastructure loan. In 2017, the fund was transferred from management by World Bank consultants, to management by a local CEO and team, which has reignited interest in it as a viable 'lender of first resort' for local authorities.

Since its inception, the DFLA has had a steady loan recovery rate, with interest paid covering future loans. This is because the repayment terms are very favourable, with a repayment period of up to 10 years, and an interest rate of 14.5 per cent (the same rate as the Reserve Bank of Malawi). By comparison, commercial bank rates are around 26 per cent. Compliance is also encouraged by engaging the entire city council in the loan process rather than just liaising with one representative, to ensure full knowledge and buy-in. In the rare cases that loans see a default, the DFLA tries to assist the councils in rescheduling payments, or as a last resort recoups their losses through the pledged collateral. One of the critical goals of the DFLA is to motivate the council to think commercially and generate revenues.

The fund operates on a first come first served basis, with the caveat that the DFLA do try to distribute money evenly among all 35 councils. Common projects funded include refuse collection vehicles, updating the valuation roll, the construction of guesthouses, and machinery or equipment. There is no cap on how much they can apply for (other than total funds available in the portfolio). However, the loan size granted will depend on the capacity of the council, the project bankability, and the availability of funds.

For the sake of accountability, the loan is not given directly to the council, but rather the council receives the go-ahead to follow the standard procurement process. Once selecting the service provider, the DFLA pays the money directly to the supplier. The low capacity for developing viable projects and proposals and poor financial management in city councils are some of the main challenges faced in issuing new loans. Assisting the local councils with this so that they can verify the loans requires significant input, assistance, and follow up.

The DFLA is now actively looking to recapitalise, as there has been no injection of funds since its 1993 inception. So far, they have only managed to secure a small contribution from the central government of MWK 400 million (US$ 545,000), for utilisation on Blantyre's QVR. Development partners are not willing to invest until the modernisation of the Funds' systems so that they are better able to monitor the money's use. However, the DFLA's financial model has no provision for excess income to invest in a system update, and the interest charged covers only a few administrative employees' salaries, marketing, and overheads. As a first step, therefore, they are currently looking for funds to invest in an automated operating system so that they can expand their portfolio.

DFLA is allowing local governments to build creditworthiness through these smaller inexpensive loans.

Apart from the DFLA, it is unlikely that municipalities will achieve autonomy to take on debt financing themselves any time soon. One of the main obstacles is the inability to have a history of transparent and certified financial accounts, which until very recently has not been a widespread phenomenon in Malawian cities. For example, when the new CEO of Lilongwe City Council came into office in 2018, there had been no financial reports for the last seven years. The new Director of Accounts has had to complete this retrospectively. Without better financial management and modernised administration systems in place, the risk of investment will remain too high to be feasible.

Public Private Partnerships (PPPs)

Instead of taking loans that they might not be able to pay back, the National Government is trying to encourage the cities to make use of Public Private Partnerships (PPPs) to achieve their investment and service delivery goals. There was a sentiment that this would also enable the city councils to focus on their core business, i.e. to create a conducive environment for the private sector, rather than taking loans to operate all services themselves.

However, it was asserted that most private entities do not see how they can recover their investments in the current economic climate. Furthermore, PPP's have a high rate of failure in similar contexts. To overcome the extraordinary coordination costs, successful PPP projects tend to be very high in value, around US$ 50 million.[22] An additional hurdle is the feasibility of recovering investments through user fees – which currently only make up 11 per cent of revenue.

Even if such PPP arrangements were to become feasible, the processes by the Private Partnership Commission (PPC) in Malawi are lengthy and rigorous. This lack of timeliness can end up frustrating the private partner. There is a need for the PPC to devise simple PPP processes befitting local councils. Additionally, councils need contracting and assessment capacity building to analyse projects that bring real public value.

Grants and loans from development partners

Grants and loans from development partners, therefore, continue to be the preferred source of infrastructure financing for city councils. Although they are tied to particular projects, they incur very little cost. However, all financial partnerships with external parties still need to go through the national level. For example, while the LDF comprises of both loans and grants from development partners, the loan liability sits with the central government, and the local government receives it as though it were a grant. The requirement for national partnership means that development partners often align their support to national priorities, which in this case means that the focus is often on the rural districts. For urban councils, more direct funding aligning with municipal and local authority priorities would be far better suited to assisting them with their elected mandates.

The Government of Malawi and several development partners are trying to build a partnership-oriented approach to development assistance, rather than the old model of grants. This cooperation has culminated in a strategy to align national systems with new financing arrangements.[23] Blended finance is one example, where grants are used to de-risk and incentivise private investment. The Organisation for Economic Co-operation and Development's (OECD) 2019 report on blended finance in the Least Developed Countries (LDC's) states that Malawi attracts 12 per cent of all blended finance in LDC's, with an average deal size of US$ 194 million.[24] However, these partnerships are still largely focussed at the national level.

Improving the regulatory environment for access to finance

A strong regulatory environment underpins the ability of local governments both to generate own source revenues, as well as define the options available for financing larger infrastructure projects over time. The most pertinent areas for regulatory reform are refocussing Malawi's rural bias, reforming land administration and the legal requirements for valuations and building the social contract for citizen buy-in.

Refocussing Malawi's rural bias

There is a strong rural bias from the national level, which filters into development partner relations who invest in projects according to national priorities. The fact that the Ministry of Local Government and Rural Development is the Ministry responsible for oversight and project approval of all local councils (including cities) reinforces this bias. Furthermore, the Department of Lands, Housing and Urban Development can provide input to urban development strategies, but it has no official say over the activities of the city councils. As a result, there is often conflict and confusion between the two parties as to who takes the lead in certain areas, resulting in duplication in some areas and neglect by both in others. As the country becomes more urbanised, there will be increasing pressure to restructure these departments to give equal weighting to both rural and urban development.

Reforming land administration

As per the updated Land Act of 2016, Malawi's land is designated as public, private, or customary ownership.[25] In terms of public land, the central government is always the principal landlord by law. However, the legislation also states that where the President declares a city, the central government requirement is to transfer all land within the city's jurisdiction to the custodianship of the city council. The city council then has control over the management of that land, as well as the financial benefits that accrue from investments in it.

However, the full transfer of land to cities is not currently happening in practice. Instead, the administration of land is done by a combination of the city councils, the Malawi Housing Corporation (MHC), and the National Department of Lands.[26] In addition, the national government continues to charge city councils to rent the land at the same rate as a private developer - even when the land is used to provide public infrastructure.

Moreover, where adequate compensations are not paid by the national authorities to relocate communities out of the city boundary, traditional authorities still maintain rights to large tracts of land in the city centres. Private organisations also own parts of the cities land, which intensified during the International Monetary Fund (IMF) structural adjustment programmes, with some transfers to private ownership not following due protocol.

In addition to inhibiting a critical source of incomes for the cities, policymakers have attested that the multitude of landlords and unclear land rights also makes any spatially expansive infrastructure development projects very difficult to implement. Decentralising land administration and development control to the city councils would therefore streamline investment, as there would be one entity that investors need to deal with when trying to lease land in the city. It also makes it simpler to service, and provides more clarity in terms of which government entity citizens should pay their ground rents to, encouraging compliance.

Currently, a cabinet paper is being prepared to push forward the ideal that all land in each city should be transfered to the relevant city council. This proposal includes dealing with the improper transfers of land to the private sector, as well as providing the necessary compensations to buy urban land from traditional authorities. This legislation could have dramatic benefit in aligning incentives for urban development if passed, subject to the capacity and will of local governments to invoke change.

Also relating to land and property regulation are the legal requirements for valuations. As explained above, the REMOP system has been stilted by the fact that the valuation conducted does not align with the Local Government Act. Instead, the Act specifies that to calculate city rents, councils must use (i) market valuation, and (ii) that a certified surveyor from SIM must provide sign-off. This restricts the use of simpler and potentially more fit-for-purpose systems. Negotiations and discussions are ongoing, but until achieving a resolution, Mzuzu's revenues from property taxes rely on the voluntary compliance of the citizens.

Building the social contract

Tax compliance in Malawi is low, partially due to the lacking legal framework to enforce penalties, as well as mistrust of people towards the local government. The mistrust is due to perceived corruption, pilferage, and general mismanagement of public finances. Introducing electronic payment systems, reducing the number of agencies collecting taxes, visible service delivery, and communication campaigns were all highlighted by the City of Mzuzu as ways of strengthening citizens´ trust in the regulatory environment. This would build on the 'My City, My Responsibility' campaign that was rolled out to inform Mzuzu residents during the implementation of the new property tax system. Figure 7 below shows some current initiatives in this regard.

To complement the Council's development efforts, some residents of Mzuzu devised the Mayor's Development initiative. The initiative is a people centered movement that seeks to solicit resources and ensure prudent management of resources for the development of Mzuzu. Members of the initiative have diverse educational backgrounds and expertise in professional private sectors, academia, and public sector colleagues. The initiative works in collaboration with the Mzuzu City Council Secretariat to prioritise development activities.

The initiative's activities include fundraising, for example, for medical equipment or the education sector. In parallel, the initiative solicits resources for infrastructure development in areas such as roads, markets rehabilitation, opening up of new markets, police units, bus depots and broader promotion of tourism in the city. The Mayor's development initiative further helps in the dissemination of information targeting Mzuzu residents and other clients. The main aim is that they pay city rates and other fees owed to the Council.

Enhancing the capacity of city financial management

The previous two sections highlight how low levels of capacity and limited structures for financial management continue to limit the city councils in Malawi. This is compounded by a lack of good quality data and information. However, councils are making progress, particularly in long-term planning for investments, as well as systems and technologies investment. Both these can aid the financial health of the city. Some of these projects are highlighted below:

- **Electronic billing:** National Integrated Technology Limited (NITEL) piloted electronic billing in Zomba City Council in 2017 to enhance transparency in the collection of market fees, ground and city rates, and business licences. It works by instantly recording when a payment is made on the Council's service system, reducing the chances of fee-collectors skimming some of the revenues collected. One year later, the system had increased revenue collection by 53 per cent.[27] Mzuzu and other cities are now doing the same.

- **Local revenue investment plans:** The NLGFC has set up an initiative to encourage the development of detailed and implementable local revenue investment plans through the Local Authority Performance Assessment (LAPA) tool. By creating a competition between cities with the incentive of MWK 5 million (US$ 6,700) for winning the best strategic plan as well as having results published in the newspapers, they have added an element of social pressure. Initiative officials reported the resulting improvement in the quality of submitted projects - around 20 percent in the third year and 60 percent in the fourth year.

- **Improving council capacity:** As mentioned above, one of the most critical obstacles to improving the financial position of cities in Malawi is poor financial management capacities, with cities like Lilongwe having no financial reports for the last seven years. The European Commission and the Malawi Local Governments Association (MALGA - an inter-governmental voice for local governments) are also partnering to deliver a project on developing the institutional, technical and management capacities of councils in order to improve local government performance, transparency, and accountability.[28] A competition between cities for fund allocations was considered as a possible way to create sustainable change in proper financial management.

- **Integrated Financial Management Information System (IFMIS):** A complementary reform is an initiative of the central government with support from the World Bank to implement an Integrated Financial Management Information System (IFMIS) to control government expenditure better and enhance transparency and accountability. There is both a new central government IFMIS and a local government IFMIS in all 35 councils, managed by the NLGFC.[29]

Figure 8: Posters to enhance the social contract

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Lessons, success factors and priorities for future reform

Although much of Malawi's urban story is still progress in the making, the example of the REMOP reform in Mzuzu sheds light on one potential way that partners can use to enhance the financial position of cities. Mzuzu, as a smaller secondary city, with little funding from central government, had to think 'outside the box' to become more self-reliant.

Current and future reforms are centred on improving the stability of own source revenues through internal systems and the regulatory environment to begin building creditworthiness. There seems to be a coherent narrative amongst many stakeholders that before looking at new avenues of raising finance, there is a need to optimise the sources they already have available. The DFLA is one example of an existing entity that could be better leveraged.

Another key element of reform as urbanisation continues to pick up pace is re-focussing the rural bias. Malawi is at a critical juncture where they can invest in the urban infrastructure essential for livability and productivity before mass settlement takes place. This will require large and targeted investment. Along with financial reform, there is a strong need to support economic growth, given that people's ability to pay is a key determining factor of compliance.

Lessons and success factors

Flexibility of small cities: Mzuzu's small size and distance from the capital meant it had more flexibility to trial new initiatives and strong incentive for reform. It also had fewer existing systems and lower levels of bureaucracy to navigate in order to facilitate change. By comparison, decision makers noted that this reform would be much harder to acheive in a capital city like Lilongwe, where political interests would play a far greater role in decisions and procedures.

Motivated and well-trained staff: In terms of capacity for reform in Mzuzu, new people had to be brought in and trained on the new systems. The understanding was that retraining of existing people rarely works, as they are averse to change and often cause disruption. Often, the new people hired were straight out of university and motivated to be a part of the change. This change needs to be expanded, with careful attention paid to how to integrate a new culture through to the rest of the administration, without causing too much disruption to existing personnel.

Immediate source of funds for reform: REMOP was born out of a need to ensure the sustainability of an existing GIZ project. GIZ was actively looking for something to invest in that would provide ongoing revenues to the Mzuzu City Council to maintain the infrastructure built. Having this funding in place for the REMOP system meant that they did not have to go through the slow and tedious process of funding applications. The assertion was that in other contexts, this often means missing a political window of opportunity.

Systems built to fit capacity: In terms of property valuation, while market valuation is usually more accurate, it also costs a lot of money, requires specialist skills, and requires detailed land registry and sales data. In developing cities, these three things are often in limited supply. Matching the system in use to the capacity of the people and the environment, can deliver much more effective results, and can be adapted as capacity increases over time.

Automation of revenue systems and GIS: One of the critical challenges for revenue collection in all of Malawi's cities is the pilferage of local government revenues. Introducing mechanisms to automate processes and create records of transactions or reduce the number of hands that money passes through is essential to limiting this leakage of valuable public resources. Electronic billing and automating the revenue management system improves transparency, and means the council can produce and audit accurate accounts. The emergence of mobile money also provides opportunities for easing payments and hence reducing default.

GIS is the component of the automated systems that improves identification of properties, particularly infill properties, properties that have undergone a renovation that are otherwise hard to spot, as well as those in informal settlements. It improves not only the collection of city rents, but also other revenues, such as fees from markets and trading centres. It also has spill-over benefits to other areas of city management, such as the identification of flood zones and properties on fragile land, enabling effective urban planning.

The importance of stakeholder consulation and working within the legal framework: The key limiting factor in the Mzuzu REMOP reform is that the new valuation has not been signed off by a registered surveyor in Malawi, a critical requirement for the valuation roll to be legally enforceable. There were many stakeholders that felt there was not adequate consultation of the necessary groups before the new valuation method was rolled out. As a result, they felt excluded and threatened by the reforms, and increased resistance to the method being legislated and adopted more broadly.

The DFLA as a tool for building creditworthiness: By providing access to small, low-cost loans solely aimed at local authorities, as well as step-by-step guidance on meeting the requirements to access the funds, the DFLA has potential to make a large contribution to smoothing cashflow and demonstrating creditworthiness for future debt financing as the city grows.

Priorities for current and future reform

Potential for expanding own source revenues:

- **Business licences:** Historically, the focus has been on market fees, however, evidence shows that the operational costs of the markets are much higher than the money coming from them. Business licenses are much better as the cost of collection is lower due to less frequent visits.
- **Investing in real estate:** The perception is that investing in hotels, shopping malls, and other real estate assets on local government owned land is a sound way of bringing in long term rents from which the city council can benefit. However, complexities in managing these assets, and diversifying away from the city councils core mandate are strong trade-offs that need to be considered.
- **Water and electricity provision:** Currently water and electricity are provided by statutory corporations. However, the Mzuzu City Council suggested that the corporations should instead be doing back supply, with distribution done by the city. This would enable them to earn the user fees, as is done in South Africa. However, the delivery of this service requires significant capacity to operate and would require considerable adjustment to the city council.
- **Other revenue sources:** Mzuzu, given their position as the central passway from Tanzania, is considering the use of toll gates and carbon tax for vehicles passing through as an alternative source of revenue.

Improving the social contract: People want to see value for their payments, meaning they want to see the connection between rates paid and services delivered. As one of the stakeholders at the Mzuzu City Council stated, “people are not looking for plans for roads, they are looking for roads”. The ‘My City, My Responsibility Campaign’ and the Mzuzu Mayor´s Development Intiative is making inroads on building the social contract, but more needs to be done. One stated desire was that future development partners could brand and market their investments as city council initiatives in order to encourage a stronger connection between service delivery and tax collection.

Increasing the tax base: Malawi’s cities suffer from a shallow tax base, underpinned by a large portion (60-70 per cent) of each city being part of the informal economy. Incorporating the informal sector into the tax register, as a number of the cities are doing with their property rates, could make a tremendous difference. However, the more fundamental challenge is that many of these residents cannot afford to pay. MALGA is also currently engaging the Ministry of Local Government and Rural Development to expand the revenue base for local councils – transferring certain functions and human resources from the central government to local councillors. The central government currently has control over all the high potential and easy to collect revenue items, some of which may be better suited to the local level.

Enabling economic growth: There is a recognition that increasing public revenues depend on citizens having enough money to pay and therefore the city council needs to do more to focus on economic growth. The Council noted that Mzuzu’s critical economic sectors are distribution and administration. In terms of agriculture, there is also fish, rice, tobacco, and the famous Mzuzu coffee that they could be processing. They could also do better as serving as a hub for tourist activities in the north of Malawi. The Mzuzu City

Council is therefore looking to the Ministry of Trade to help boost economic activity and create special economic zones to improve infrastructure and attract investors.

Automation of revenue sources: Stakeholders highlighted that for future property valuations, the fieldwork component should include a more significant number of data points related to other taxable activities, such as businesses and city assets. This expansion could enable the automation of a higher number of revenue sources, without having to pay for separate surveys to be done, and result in a more holistic and integrated revenue system.

The primary goal of this would be to improve accounting and financial management and to be able to show central government and development partners what their funds are achieving in an attempt to advocate for more resources. Accordingly, the Mzuzu City Council identifies the following benefits from automating their property taxes: Instant audits and financial reports, bulk electronic billing, easier 'client' payment, links with mobile money or internet banking, SMS alerts for clients, mapping of compliance, and finally, transparency – leading to a virtuous cycle of trust and further revenue generation.

Improved partnerships: There was a view that there are strong synergies with other entities that are underleveraged. For example, partnerships with other cities for capacity building and exchange of best practice. Also, partnership with local universities. For example, in Mzuzu, there are urban planners, land surveyors, and GIS planners all nearby that are underutilised.

Partnership with the central government, particularly the Ministry of Trade and Industry, and the Ministry of Transport and Public Works is key. Strong local/national relationships could also begin to unravel the rural bias in Malawi, ensuring that urban investment is prioritised before mass urban migration takes place.

Furthermore, the example of Mzuzu provides a stark reminder of the vital importance of widespread stakeholder engagement and extreme caution for the law in order to achieve sustainable project success. For the REMOP reform, had stronger relationships been formed with SIM, and co-generation of projects taken place, perhaps the new system would have met far less resistance.

Reforming regulations: Ensuring that the legal requirements are met for all public land owned in a city to be transferred to the control of the local authority will bring significant additional opportunity to all the cities of Malawi. If handled correctly, this will not only increase revenues, but also allow city councils to better plan their cities, and improve the environment for investment and doing business. Another regulatory area for reform is the ability of local governments to enforce tax compliance – both in general, and more specifically, to make a final decision on the legality of the new points-based valuation method used in Mzuzu.

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UNITED NATIONS HUMAN SETTLEMENTS PROGRAMME
P.O. Box 30030, Nairobi 00100, Kenya
unhabitat-info@un.org
www.unhabitat.org

@unhabitat