

Bertelsmann Stiftung (Hrsg.)

Städte in Not

Wege aus der Schuldenfalle?

Abstract

Cities in Crisis – Getting Out of the Debt Trap?

For some 20 years, the discussion regarding local politics and administration in Germany has been dominated by concerns over growing public sector debt and pressures placed on the capacity of municipalities to deliver services. Even though deficits aren't the norm everywhere, the number of cities and towns affected is growing, as is the extent of the overall problem.

The Bertelsmann Stiftung, in promoting strengthened powers of municipal self-administration, examines this issue as it generates public awareness and brings actors together in dialogue on related topics. This is the ethos behind this anthology. The 16 contributions comprising this publication's four rubrics address various aspects of the municipal budgetary crisis in Germany, focusing on potential solutions rather than root causes. It combines contributions from both academia and those on the ground, and aims to fulfill the needs and interests of both target groups. The following gives a brief overview of the individual chapters.

The contributions in the first section, "Befunde" ("Findings"), explore the origins and characteristics of the crisis faced by municipalities. Monika Kuban deals with the (involuntary) role of cities and towns acting as guarantors for services where federal education, social and family policies are falling short. The resulting increase in social spending on the part of municipalities as a manifestation of the welfare state is a significant driver of the budgetary crisis. This in-

crease derives from the state's long-standing refusal to acknowledge shifting social conditions, particularly in familial structures. Municipalities are feeling the impact not only in financial terms, but also in the form of accelerating societal decay. A change in national policy is needed, for example, through measures such as universal childcare. A comparison of spending among different municipalities shows great disparities even among those facing comparable issues. This fact highlights the leeway afforded municipalities in taking action, the diversity of strategies pursued and the importance of wise leadership.

Germany's Länder, or federal states, have responded to the budgetary crisis by tightening municipalities' budgetary powers and oversight. Lars Holtkamp looks at the consequences of this development in the state of North-Rhine Westphalia (NRW), where the application of budgetary rights effectively constrains local politicians' capacity to act, decreases voluntary spending, and results in non-transparent negotiations taking place between regulatory authorities and finance departments. On the one hand, this diminishes the effectiveness of levels of escalation in fiscal consolidation or state commissioner power. On the other hand, municipalities forfeit some of their autonomy and self-administering capacities. This leads to problems from the standpoint of democratic theory. As a result, instead of resolving municipalities' budgetary crisis, budgetary powers have become near drivers of the crisis itself.

Nevertheless, rights of oversight offer an essential and potentially effective steering mechanism which the Länder have utilized to varying degrees. In looking at the framework of budgetary law, Benjamin Holler addresses a hitherto underappreciated factor in explaining municipal deficits. The fiscal regulatory framework is determined by the Länder and is essentially embedded in municipal bylaws and financial regulations. It contains target values and procedure guidelines as well as sanctions, which are organized differently in each case. The form of these components was defined and codified in 2003 and 2009. The result is an index of budget law frameworks comparing both Länder and periods. Along with supplementary variables, this index can serve

as both a cause of municipal deficits and a measure of the efficacy of municipal oversight.

Constant demands from the population, interest groups as well as politics and administration put pressure on the budgetary policies of cities and towns. The interplay of local politics and citizen's expectations as voters is referred to as a political economy. In theory, this can lead to continuous overstretching of budgets and the exacerbation of debt. Using an NRW population survey, René Geißler investigates the validity of these assumptions by collecting citizens' views on the budgetary policies of their local government and on debt. The results contradict the assumptions of a political economy by showing that citizens reject debt and value austerity. However, this attitude does not extend to a willingness to offer solutions.

The second part of the anthology encompasses five contributions addressing "Innovationen der Länder" ("The Länder's Innovations"), which deal with the role of the Länder in the municipal budget crisis. Ulrich Keilmann and Marc Gnädinger profile in their contribution a protection mechanism in the state of Hessen designed to help indebted municipalities find their way out of on-going debt through financial assistance and advice. The idea for the mechanism was developed by the state of Hessen in cooperation with municipal associations. The selection of eligible municipalities was based on certain budget parameters. The mechanism allows Hessen to relieve the majority of accumulated debt through its own means and act as a guarantor for assistance with interest payments. For their part, local authorities are contractually obliged to carry out consolidation measures. This phase has already produced positive results by bringing greater objectivity to discussions, facilitating comparison between municipalities, providing renewed motivation for local actors and a willingness to take major steps toward consolidation.

In North Rhine-Westphalia, the regional budget crisis has been worsening over decades with the consequence that many areas see little hope of a solution. Johannes Winkel and Benedikt Emschermann report on the "Stärkungspakt NRW" ("NRW Strengthening Pact"). It was introduced in 2010 by the state government and seeks to

direct local authorities' efforts toward consolidation measures and balanced budgets in the mid-term. Participation is mandatory for the worst affected cities and towns. Funding for the Strengthening Pact comes from the state budget as well as a shared municipal fund. The state offers participating municipalities advice on consolidation, with the process scheduled to run for ten years. One result of the Strengthening Pact is that it has stimulated new discussion on consolidation processes in cities and towns, and with the oversight body. However there are risks associated with the implementation of these ambitious plans.

The GPA NRW ("Gemeindeprüfungsanstalt Nordrhein-Westfalen," or "Local Authority Auditing Institute") is a state body which examines municipal budgets on a supra-local level. It was tasked with advising participating cities and towns as part of the Strengthening Pact. In his contribution, Christoph Gusovius reports on the experience and lessons learned from this consultation. This process always began with an analysis of the present budget situation, including the sociodemographic conditions of the city or town. Working from this basis, concrete measures were defined which would bring about a balanced budget within a maximum timeframe of ten years. Here, uncertainties in projected income and expenditure have proved to be an obstacle. In developing consolidation measures it was essential that data supplied by the municipalities undergo careful scrutiny. Any decision on measures was entirely incumbent on local politicians, who were brought on board as early in the process as possible. One outcome was that many cities and towns concentrated on increasing revenue before looking at a reduction in services. However, the increased tax revenues which resulted were soon depleted. Discussions on local service standards, organization and cooperation between local authorities in the mid-term are therefore vital. Maintaining the consolidation coalition established as part of the Strengthening Pact over the whole period is another essential success factor.

In the state of Saxony, municipal budgets are largely stable although still faced with challenges. To increase budget transparency, preemptively recognize risks and introduce countermeasures, the state's Minis-

try of the Interior has developed an early warning system based on key performance indicators (KPIs). Mario Hesse and Florian Woitek chronicle its background and organization as well the experience gained in its implementation. The early warning system is an additional instrument of regulatory oversight. It offers authorities greater transparency in comparisons and allows for more reasoned debate. Moreover, it provides orientation for local politicians and the public. The efficacy of the instrument was dependent on choosing the right KPIs, which had to be multidimensional (e.g., debt, profit and loss, liquidity) and the data for them available in sufficient breadth. For each indicator, a threshold value is determined; anything exceeding this value is tagged as high risk. The authorities have extensive say in putting together these regulatory instruments. The experience in Saxony shows a significant increase in the transparency of budgets and the regulatory function and a corresponding increase in public accessibility.

Like its municipalities, the state of Saxony-Anhalt is faced with significant budgetary challenges following the end of the Solidary Pact (by which states in the former East Germany had received post-reunification funding) as well as demographic changes. One response of the state government is to reduce pressure on municipal budgets by lowering legally mandated service standards. Peter Kuras explains this process and the outcome of the interdepartmental working group tasked with its implementation. At the outset, all relevant ministries, municipal organizations and the audit court were asked to report on legally mandated standards which might potentially be reduced. The return was minimal and financially far from sufficient. This seemed to stem from certain authorities' reluctance to make sacrifices, along with a process of deregulation which had been underway since the mid-1990s. As a further step, the working group submitted its own suggestions to a critique of standards. It showed that the discussion and reduction of legally mandated standards is a task with many hurdles, which requires persistence and political will. Moreover the potential relief effects are difficult to forecast.

In the third part of the anthology, "Handlungsansätze der Städte" ("Courses of Action in Cities and Towns") are the focus. Jochen Gottke

explains the unusual approach of the city of Solingen: objective, process and resource modeling (OPRM). With this self-developed variation on impact-oriented task assessment, the city managed to find a way out of a budgetary crisis which had persisted for decades. In 2009, with debt excess looming, the city was faced with the task of establishing a consolidation volume on an unprecedented scale. Using the OPRM, employees of the most important organizational units analyzed the relationships between resources, processes and the attainment of strategic objectives. This resulted in product-critical measures with consolidation contributions. Political decision makers and management put together a consolidation program based on these proposals, with additional input from residents.

The idea of making municipal services measurable and controllable through KPIs arose in the early 1990s. The real-life implementation of this idea has been suboptimal in many instances. Alexander Kroll introduces the current state of research on working with KPIs. In essence, using KPIs in control functions indicates a shift in the control concept and a decentralization of decision-making authority. In practice, KPIs often meet with indifference from those who are meant to be utilizing them in their control functions. They have no relevance and therefore no steering impact; in any case they require bureaucratic effort. The actual implementation of KPIs is dependent on a number of factors: the quality of data, the support of upper management, the organizational culture and the way they are presented to their target audience. Other factors – such as the budgetary status of the local authority, the size of its administration and hierarchy – are evidently of little relevance here. Those using KPIs have to acknowledge that they are never entirely objective, can never serve as sole decision-making criteria and are rarely compatible with political processes. Overall, however, KPIs are beneficial in supporting the decision-making process.

In his contribution, Marc Seuberlich shows that there is no automatic linkage between unfavorable socioeconomic conditions (low economic power, shrinkage, peripheral location) and municipal budget figures. Using the example of six medium-sized towns in Sax-

ony, he proves that the scope of action available to local actors is endogenous to their context. Despite a high degree of political fragmentation in the towns in question, they have become models of debt reduction. All the stakeholders managed to overcome urban shrinkage with limited financial means. Budget discussions are objective, confidential and free of influence from regulatory oversight, and focused on reaching consensus. The road to debt reduction is long and one-off politicizing measures are unhelpful. The practices of these towns also result from the unique historical conditions of reunification.

In Germany, there has been a major movement toward citizen participation in budgetary issues since the late 1990s, supported by foundations and pilot projects. The intention was to increase transparency in budgets, dialogue and acceptance. In recent years, critical discussion around practicability and effectiveness has increased. Tobias Fuhrmann and Alexander Koop outline the emergence and expansion of participatory budgeting, examine the sources of current skepticism while also providing recommendations for future projects. They make the crucial observation that the spread of the budget crisis has shifted the objectives of participatory budgeting. The original goal of developing and prioritizing investments has given way to the goal of merely confirming cutbacks or revenue increases. These consequences are illustrated in the contrasting examples provided by the city of Essen and the Berlin borough of Lichtenberg. In Lichtenberg, various forms of participation have been successfully applied since 2005, allowing citizens the opportunity to configure voluntary assignments at the district level, using the district budget. The situation in Essen was completely different. There the discussion took place online with the goal of evaluating consolidation proposals from city authorities. There was no evidence of real citizen influence on council decisions. In the second year, participation collapsed and the project was discontinued. That the term “participatory budgeting” is applied to such fundamentally different formats and objectives has proved problematic. Participation toward a goal of budget consolidation takes place under different conditions and must be conceived differently. Failure to do so

fatally undermines projects, which damages the concept of participatory budgeting as a whole.

The last three articles come under the rubric “Ausblicke” (“Prospects”). In the first article, Busso Grabow and Stefan Schneider demonstrate the connection between sustainable financial policies and infrastructure planning. The conditions for local authorities – such as connectivity or more recently in economic development – have improved in some respects. But other problems persist, including insufficient funding and the cost of demographic change. Cities and towns make the mistake of consolidating in the short term at the expense of investments, which they delay or forego altogether. In using the term “sustainability” we must place greater focus on maintaining assets in the future. The local authorities’ view of the future – as the KfW Municipal Panel demonstrated – is dominated by skepticism. Many authorities seem barely able to maintain and upgrade infrastructure. It is vital that municipalities evaluate long-term infrastructure needs and draw the appropriate conclusions for current investments.

The adjustment of budgeting and accounting processes was and is a long-term, large-scale reform for municipalities. The objective of the reform was for politics to strengthen budgetary transparency and control. The extent to which this has been successful – along with the overall benefit of the new system – is the subject of debate. Andreas Burth and Dennis Hilgers conducted a survey of politicians in urban and rural centers to discover how they evaluate the use of double-entry accounting. Politicians still see no advantage in the legibility of budgets, or if so only in terms of intergenerational justice. Control functions enabled by double-entry accounting are seen as improvements, as is their influence on the economic efficiency of administrations. Ultimately, local politicians recognize the cost of reforms, but see long-term positive effects in the future. There are further opportunities for improvement in the harmonization of legal standards across states, which currently differ widely.

Cities and towns certainly don’t have a monopoly on budgetary risks and consolidation; challenges persist at the national level as well. Uwe Wagschal explains the origins of debt as well as the conditions

for successful consolidation based on a number of research projects in OECD countries and German states. The sources of debt in Germany can principally be traced to economic crises, reunification and, most recently, the banking crisis. Political-institutional factors also contribute. There are a number of lessons to be drawn from research into national consolidation which can be applied at the municipal level. Essential for the consolidation of budgets was economic growth, while a fall in nominal interest rates was also beneficial. Countries which have been successful in consolidation tended to focus on the expense side of their budgets. As far as institutions were concerned, centralization of budget processes and long-term, binding financial planning were more important than debt brakes. Ultimately self-regulation at the political level was a decisive factor. This point is entirely at the discretion of the actors concerned.