OECD Multi-level Governance Studies

Making the Most of Public Investment in Colombia

WORKING EFFECTIVELY ACROSS LEVELS OF GOVERNMENT

OECD

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BETTER POLICIES FOR BETTER LIVES

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Foreword

Public investment is a shared responsibility across different levels of government – national, regional and local – which makes its governance particularly complex. In today's tight fiscal environment, making the most of public investment across levels of government is more crucial than ever. National governments have an important role to play in establishing the framework conditions needed to better select and implement sound infrastructure projects. Subnational governments also play a specific role, although this is often neglected in the literature. Subnational governments – defined as all levels of government below the national one, i.e. administrative regions, states/provinces, counties and municipalities – are responsible for a large share of public investment: on average, around 60% in the OECD. Most of this public investment goes to infrastructure.

This role of subnational governments poses specific challenges for both the financing and governance of infrastructure investment. Effective public investment requires both substantial co-ordination across levels of government to bridge any gaps in information, policy or financing that may occur, as well as critical governance capacities at different levels to design and implement public investment strategies and projects targeted to local needs. When done right, public investment can be a powerful tool for boosting growth, enhancing well-being and providing the right infrastructure to leverage private investment. In contrast, poor investment choices or badly managed investment waste resources, erode public trust and may hamper growth opportunities.

This study examines the multi-level governance framework for public investment in Colombia. It provides a diagnosis of the strengths and challenges of the Colombian system and includes comparative data and a set of benchmarks to promote the exchange of good practices and learning. It makes recommendations for how Colombia can further improve its system, make more effective use of existing resources and catch up to OECD countries in terms of infrastructure development. The review also suggests a set of indicators against which Colombia can measure its progress.

This study is part of the OECD Series on Multi-Level Governance and of the implementation of the OECD *Recommendation of the Council on Effective Public Investment across Levels of Government* adopted by the OECD Council in March 2014. An Implementation Toolkit was developed to help countries in its application and is available at: www.oecd.org/effective-public-investment-toolkit. Colombia adhered to the Recommendation in 2014 and has adopted many of the policies/instruments recognised as good practices by the OECD Regional Development Policy Committee.

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The report relies on a broad variety of sources, including interviews during the fact-finding mission, answers to a questionnaire completed by Colombia and OECD reviews recently conducted on Colombia in different policy areas. The work also builds upon previous work carried out by the OECD Regional Development Policy Committee as part of the accession process of Colombia to the OECD, in particular the missions in the different regions, Bogota, Leticia, Pasto and Medellín.

Kate Lancaster, Pilar Philip and Andrea Uhrhammer provided guidance to prepare the publication. Jennifer Allain edited the final manuscript and prepared it for publication.

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Definitions and methods

- **General government** includes four sub-sectors: central/federal government and related public entities; federated government ("states") and related public entities (only in federal countries); local government, i.e. regional and local governments and related public entities in unitary and federal countries; and social security funds. Data are consolidated within the general government sector and within each of the four sub-sectors.

- **Subnational government** is defined as the (non-consolidated) sum of federated governments ("states") and related public entities (only in federal countries) + local government, i.e. regional and local governments and related public entities in federal and unitary countries.

  In Colombia, which is a unitary state, the "subnational government" is equivalent to the "local government" sector. It includes the departments and municipalities, the public establishments and the decentralised entities at departmental and municipal levels, comprising the following governmental entities: mixed culture funds, institutions of higher education, metropolitan areas, municipalities partnerships, funds for social interest housing, healthcare entities, institutes of recreation and tourism (DANE, 2015).

- **Expenditure** comprises current expenditure (compensation of employees, intermediate consumption, social expenditure, subsidies and other current transfers, taxes, financial charges, adjustments) and capital expenditure.

- **Capital expenditure** is the sum of capital transfers + investment.

- **Investment** is defined as capital expenditure on physical infrastructure (i.e. roads, government buildings, etc.) and soft infrastructure (i.e. human capital development, innovation, research and development, etc.) with a productive use that extends beyond one year. More specifically, in the national accounts, investment is defined as gross capital formation and acquisitions less disposals of non-financial non-produced assets. Gross fixed capital formation (or fixed investment) is the main component of investment and can be used as a proxy for investment. Since the new standards of the System of National Accounts (SNA 2008) expenditures on research and development and weapons systems are included in gross fixed capital formation.

- **Public investment** corresponds to investment of the general government sector, i.e. including all four sub-sectors (see above). Subnational government investment corresponds to investment of federated states and local governments in federal countries and regional and local governments in unitary states. In Colombia, subnational investment includes investment made by the departments and municipalities as well as by related public entities.
- **Investment by economic function** follows the Classification of the ten Functions of Government (COFOG): general public services; defence; public order and safety; economic affairs; environmental protection; housing and community amenities; health; recreation, culture and religion; education; and social protection.
- **Public procurement** expenditure is defined as the sum of intermediate consumption, gross fixed capital formation and social transfers in kind via market producers.
- **Revenue** comprises tax revenues (taxes on production and imports; current taxes on income and wealth; and capital taxes), transfers (current and capital grants and subsidies), tariffs and fees, property income, and social contributions. Tax revenue includes both own-source tax and shared tax.

Methods

- The comparative data on public investment employed in this report come from the national accounts contained in the OECD database, unless otherwise specified. They are publicly available at: http://stats.oecd.org.
- OECD averages are presented as the weighted average of the OECD countries for which data are available, unless otherwise specified (i.e. unweighted average, arithmetic mean, OECD UWA).
- Data were extracted in current national currency and converted to USD using purchasing power parities.

Defining public investment in Colombia

The breakdown of public investment, following the standard System of National Accounts (SNA), is not available by sector in Colombia. Although Colombia reports aggregate public investment data using the National Accounts definition, these data are not broken down by sector. In fact, the definition of public investment used by Colombia differs from the SNA’s definition. According to Colombia, investment is defined as spending allowing growth in productivity and production capacity for physical, economic and social infrastructure. It encompasses gross fixed capital formation, but also includes economic and social capital, considered as current expenditures by the National Accounts. Most resources available to local governments are mainly (Sistema General de Participaciones [SGP], General Participation System, for instance), if not exclusively (Sistema General de Regalías [SGR], General System of Royalties) dedicated to “investment”, but in its broader meaning.

This definition issue raises a number of challenges, as it: 1) mixes capital and current expenditures, which prevents getting a clear picture of public investment; 2) is not comparable with other countries; 3) tends to overestimate investment rates.

In this report, the OECD definition of public investment will be used, unless specified otherwise. Colombia should consider extending the use of the SNA definition of public investment, to clarify measurement and facilitate international comparisons.

Reference

DANE (2015), Annual National Accounts Methodology – Institutional sectors.

Acronyms and abbreviations

APP	*Asociaciones Público Privadas*
BPIN	National Investment Programme and Project Bank *Banco Nacional de Programas y Proyectos*
CAR	Autonomous regional corporation *Corporacione autónoma regionale*
CHIP	Consolidated System on Finance and Public Information *Consolidador de Hacienda e Información Pública*
CONPES	National Council for Economic and Social Policy *Consejo Nacional de Política Económica y Social*
COP	Colombian peso (currency)
CP	Contract Plan *Contratos Plan*
CRC	Regional commission for competitiveness *Comisione regionale de competitividad*
CTP	Territorial Planning Council *Consejo Territorial de Planeación*
DANE	National Administrative Department of Statistics *Departamento Administrativo Nacional de Estadística*
DNP	Department of National Planning
DTSER	Working Documents on Regional Economy *Documentos de Trabajo sobre Economía Regional*
EDI	Integral Performance Evaluation *Evaluación de Desempeño Integral*
EPM	*Empresas Públicas de Medellín*
EU	European Union
FCM	Colombian Municipalities Federation *Federación Colombiana de Municipios*
FDI	Foreign direct investment
FONADE	National Development Fund *Fondo Nacional de Desarrollo*

GDP	Gross domestic product
INCODER	Colombian Institute for Rural Development *Instituto Colombiano de Desarrollo Rural*
IDB	Inter-American Development Bank
IGAC	Geographic Institute Agustín Codazzi *Instituto Geográfico Agustín Codazzi*
LOOT	Organic Law governing the Territorial Organisation in Colombia *Ley Orgánica de Ordenamiento Territorial*
MGA	General Adjusted Methodology *Metodología General Ajustada*
MHCP	Ministry of Finance and Public Credit *Ministerio de Hacienda y Crédito Público*
MTEF	Medium-term expenditure framework
NDP	National Development Plan
OCADs	Collegiate bodies of administration connected with the reform of royalty payments *Órganos colegiados de administración y decisión*
OECD	Organisation for Economic Co-operation and Development
PDT	Territorial development plan *Plan de desarollo territorial*
POT	Land-use plan *Plan de ordenamiento territorial*
PPI	Pluri-annual investment plan *Plan plurianual de inversion*
PPP	Public-private partnership
RAP	Administrative and planning region *Región Administrativa de Planeación*
RPG	Management and planning region *Regione de planeación y gestión*
SGP	General Participation System *Sistema General de Participaciones*
SGR	General System of Royalties *Sistema General de Regalías*
SMSCE	System of Monitoring, Control and Evaluation *Sistema de Monitoreo, Seguimiento, Control y Evaluación*
SNA	System of National Accounts

SNG	Subnational government
SRF	State revolving funds (United States)
USD	US dollars
WB	World Bank

Executive summary

1. Colombia has made major progress in recent years in strengthening macro-economic and fiscal framework conditions for effective and inclusive public investment, supporting subnational investment and improving overall multi-level governance. This has contributed to strong growth and decline in national poverty – from 49% to 28% of the population from 2002 to 2015. The conclusion of the peace talks could further boost confidence, promoting investment and job creation.

2. Income and territorial inequalities have declined over the past decade, but remain very high by international standards. Many regions, in particular rural ones, lack access to transport infrastructure and local public services such as education or housing. Colombia lags behind most OECD countries in terms of the quantity and quality of its infrastructure.

3. Public investment has increased substantially in recent years – notably after 2010- rising from 2.4% of GDP in 2000 to 3.9% in 2014.The negative gap on public investment between Colombia and OECD countries have diminished and turned positive in the aftermath of the financial crisis. The level of public investment remains however lower than many other middle income countries, in which public investment stands around 6-7% of GDP.

4. The increase in public investment has been driven both by central and subnational governments, which play an increasing role in investment, notably since the 2012 royalties' reform. Subnational governments were responsible for 52% of public investment in 2014, compared to 44% 15 years ago. While spending autonomy is limited, Colombia is among the most unitary decentralised countries in terms of subnational public spending in Latin America.

5. Colombia needs to sustain public investment efforts to respond to huge infrastructure gaps and territorial disparities. The pace of capital accumulation needs to continue for a sufficiently long period in order to boost productivity levels and GDP per capita. Investment in infrastructure in a variety of sectors (transport, health, education, housing) is needed to move up in the value chain making economic growth more sustainable and enabling income convergence. Sustaining high levels of public investment

requires finding new sources of funding, as the fact that oil reserves are estimated to last another decade put pressures on the long-term financing of public investment.

6. Challenges for Colombia to sustain public investment lie essentially on the governance framework. Efforts to further support financing should be accompanied by a more systemic approach to the governance of public investment. Colombia needs to reduce the overall fragmentation of the system. Supporting more strategic investment requires greater links between planning and budgeting, incentives to support horizontal cooperation across jurisdictions, in particular to strengthen functional urban areas, relatively small in Colombia. Overall, subnational governments have the appropriate mandates and tools, but the low level of capacities in more than two thirds of Colombian jurisdictions is probably the most important bottleneck for effective public investment.

Recommendations

Enhance subnational revenues to finance investment

- Given that most **transfers** are strictly earmarked, there is room to introduce some flexibility in the transfer' system, notably to re-allocate unspent funds.
- **Enhance the capacity of SNGs to raise own-source revenues**, through: (i) continuing efforts to update and modernize the cadastral and land registries in order to improve the municipal property tax performance; (ii) streamlining the portfolio of taxes levied by departments and municipalities and promote shared taxation between the central and subnational governments; (iii) reducing the number of earmarked taxes; (iv) allowing instruments such as congestion charges or tolls; (v) promoting more flexibility in terms of user tariffs and local fees and optimise income from properties (rents, dividends).
- **Borrowing** could be further used by SNGs as a financing mechanism within the limits of current fiscal rules, as the level of financial debt (loans and bonds) has decreased both in terms of GDP and total public debt. It is important to protect fiscal discipline, in a context of strong dependence on potentially volatile resource revenues, but at the same time make best use of existing borrowing possibilities at the subnational level. SNGs need to be further assisted to improve their use and management of loans. Innovative financing tools for investment such as revolving funds could be explored.

- Given the existing **high fiscal disparities** and the risks that supporting capacities of SNGs to raise own-source revenues increases them further, equalisation mechanisms should be reinforced as part of the reform of the system of transfers currently being discussed. Existing tools such as Contratos Plan and new Peace Contracts should be strengthened as key mechanisms to support investment in lagging regions.

Achieve more strategic investment prioritisation and co-ordination

- Strengthen the **effective use of local development plans as strategic planning tools, better articulated with effective budgeting and implementation**. SNGs need more adequate time schedule to design PDT, allowing better diagnosis and priorities setting, and better articulation between the national, departmental and municipal levels. Intensify the effort to increase technical assistance to subnational governments for the design of PDTs and POTs and enhance local capacity.

- Support the preparation of **integrated investment programmes/projects**, including financial plans, considering different and articulated funding sources. The new monitoring system currently being implemented will be helpful.

- Better articulate the **royalties' system** with the revenue sharing arrangements and the General Budget to better anticipate the impact of capital expenditures on future current expenditures. Further encourage joint sessions of OCADs in a sub-regional way. Implement the scoring system that allows prioritization for royalties based on objective criteria including explicitly maintenance costs.

- **Provide financial incentives to support horizontal associations across municipalities** and departments, for example through matching grants/co-financing projects between the national government and subnational associations. Further supporting horizontal cooperation across jurisdictions is particularly important at the metropolitan level, notably for Bogotá, Cali or Cartagena, which are not yet structured as metropolitan areas. Specific contractual arrangements targeting metropolitan areas could be envisaged. Departments could also take a more pro-active role supporting critical projects with cross-jurisdictional cooperation, in particular vis-à-vis rural municipalities.

Strengthen subnational capacities for effective public investment

- **Strengthen the capabilities of public officials involved in public investment**. Colombia should ensure continuity and stability in the rules to strengthen subnational capacities. Colombia may consider developing a comprehensive assessment (both quantitatively and qualitatively) of employees to get a clearer picture of the needs and gaps of territorial entities. The role of Departments for municipal capacity building and technical support should be further developed.

- **Support asymmetric decentralisation** in two directions (i) devolving additional competences to most capable SNGs as planned in the programme currently in place; (ii) simplify reporting mechanisms of weaker SNGs to alleviate the administrative burden. Colombia could take advantage of pilot experiences in the devolution of competencies as a way to ensure a gradual institutional change and learning by-doing.
- **A systemic approach to capacity building for public investment.** Colombia should identify obsolete or overlapped procedures that could be modernised and consolidate financial monitoring reports separated by funding source to reduce administrative burden at the local level.
- Colombia should put **more emphasis on the design and selection of projects.** The General Adjusted Methodology, currently unevenly used by municipalities, should be simplified. Appraisal methodologies may be differentiated according to the size or complexity of the project.
- **Monitoring should focus more on programmes and project evaluation with an integrated perspective among financing sources.** The reform under way of merging GESPROY and Investment Projects Monitoring System within a unique device, with a visualization and georeferencial module for all public investment projects consolidation (MapaInversiones) could bring significant progress.
- Data improvement should include **alignment to international standards for the definition of investment**. Colombia should consider generalising the use of the national account definition of public investment to clarify measurement and facilitate monitoring.

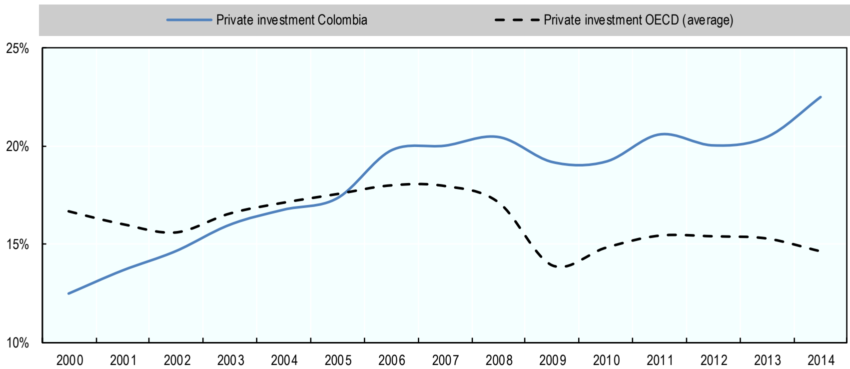
Assessment and recommendations

Colombia has considerably improved its macroeconomic and fiscal framework conditions for both private and public investment

Colombia has made major economic and social progress in recent years. A solid monetary, fiscal and financial framework reduced the macroeconomic volatility of the previous decades (OECD, 2015b). This has contributed to strong growth and a decline in national poverty, from 49% to 28% of the population from 2002 to 2014 (DANE, 2016). The improved macroeconomic and fiscal conditions have also created an environment favourable to both private and public investment. Private investment has risen, from 12.5% of gross domestic product (GDP) in 2000 to 22.5% in 2014. Foreign direct investment flows, which benefited from the commodity price boom until 2014, have increased substantially in recent years. Colombia signed a major peace agreement in August 2016. The conclusion of the peace talks could boost confidence, promoting investment and job creation.

Public investment, which used to be low in Colombia, has increased quite substantially in recent years, particularly since 2010. Public investment is now almost 4% of GDP, i.e. above the OECD average. It has been driven both by central and subnational governments, which play an increasing role in investment, notably since the 2012 royalties reform. This level of public investment remains, however, lower than many other countries (Figure 0.2). In many emerging markets, public investment rates peaked at over 8% of GDP in the late 1970s/early 1980s, declined to around 4-5% of GDP in the mid-2000s, but have since recovered to 6-7% of GDP (IMF, 2015).

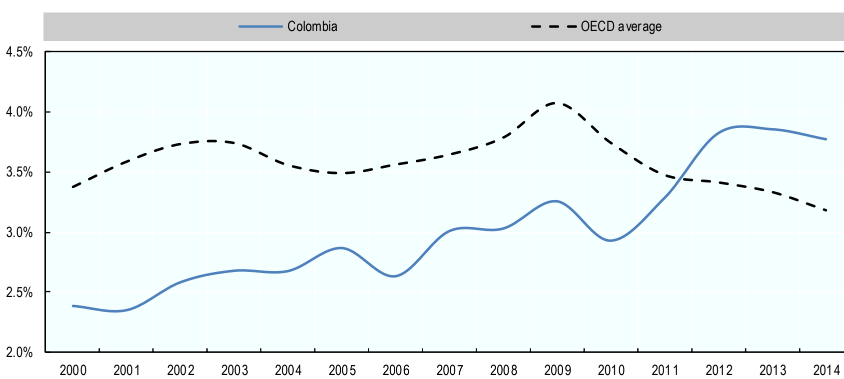
Figure 0.1. **Private investment as a percentage of GDP, Colombia and OECD average**



Note: Private investment: measured by investment by enterprises and households in the National Accounts. No data were available for Australia, Chile, Canada, Greece, Luxembourg and Turkey for calculating the OECD average.

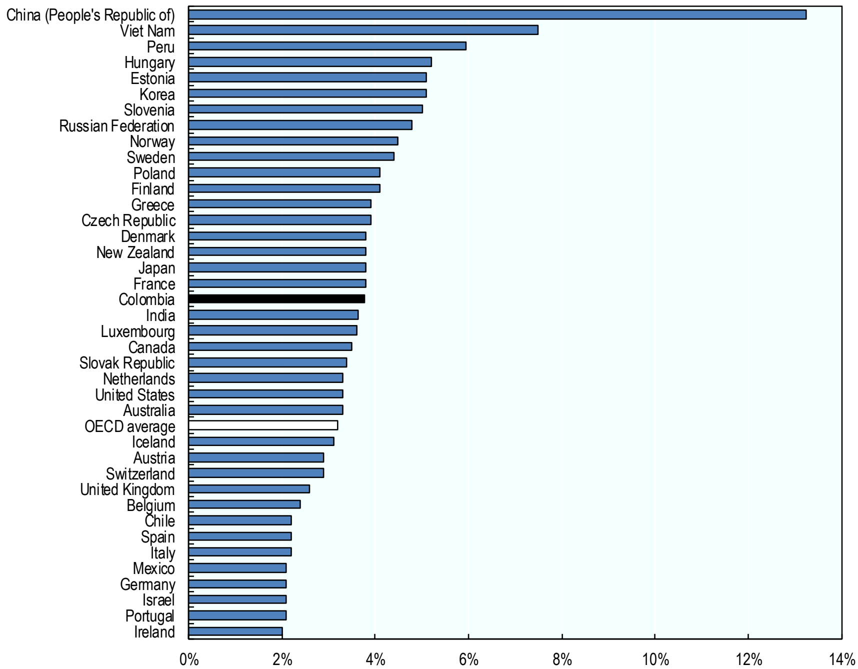
Source: Authors' calculations based on (2016a), OECD National Accounts.

Figure 0.2. **Public investment as a share of GDP over time: Colombia vs. the OECD average**



Source: Authors' calculations based on (2016a), OECD National Accounts.

Figure 0.3. **Public investment as a share of GDP, 2014**



Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

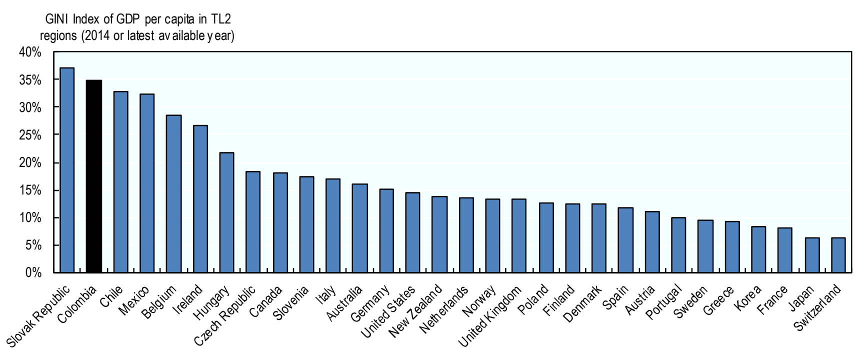
Source: Authors' elaboration based on OECD (2016a) and on OECD (2016d).

Colombia needs to sustain its public investment efforts to respond to huge infrastructure gaps and territorial disparities

Even if public investment in relation to GDP has increased substantially in recent years, the pace of capital accumulation (measured by investment to GDP) needs to continue for a sufficiently long period in order to raise productivity levels and GDP per capita. Like other countries which are in a rapid catching up process, the challenge for Colombia is to sustain its level of public investment over the longer term, to avoid being caught in a middle-income trap and in order to address its huge infrastructure needs. Investment in infrastructure in a variety of sectors (transport, health, education, housing, economic development) is needed to diversify the economy away from commodities, boost productivity and move up the value chain to make economic growth more sustainable and achieve convergence with OECD countries in per capita income (OECD, 2015b).

Colombia has huge infrastructure needs, in different sectors – from transport, to water, ICT or housing. It lags behind other Latin American countries and most OECD countries in terms of the quantity and quality of its infrastructure. This infrastructure gap has a strong territorial dimension: many regions, in particular rural ones, lack access to transport infrastructure and local public services such as education, housing or welfare. For example, two-thirds of the rural population lacks ready access to the road network. Colombia has a very high level of territorial disparities across regions, but also within urban areas. While absolute income poverty fell between 2002 and 2014 from 49% to 28% at the national level, and from 45% to 24.6% among urban households, it continued to affect 40.3% of rural households in 2014. At the regional level, in comparison with OECD countries, Colombia has among the highest level of territorial disparity in GDP per capita, similar to the Slovak Republic, Chile and Mexico (Figure 0.4).

Figure 0.4. **Gini Index of territorial disparities in GDP per capita, OECD countries (TL2 level), 2014**



Source: OECD (2016e), *OECD Regional Database*.

Colombia not only needs new infrastructure, but also to maintain its existing assets: it was estimated in 2013 that more than half of Colombia's roads needed maintenance. Colombia has improved the conditions in favour of private sector participation in infrastructure and launched a fourth generation programme of public-private partnerships (PPPs). While PPPs should be supported, they can only be a partial response to investment needs; in particular, they cannot fully address challenges for lagging regions, as by definition private actors are looking for bankable projects which might not be the case in lagging/poor regions. In most OECD countries, PPPs account for less than 10%, or even 5%, of overall infrastructure investment (Burger and Hawkesworth. 2013).

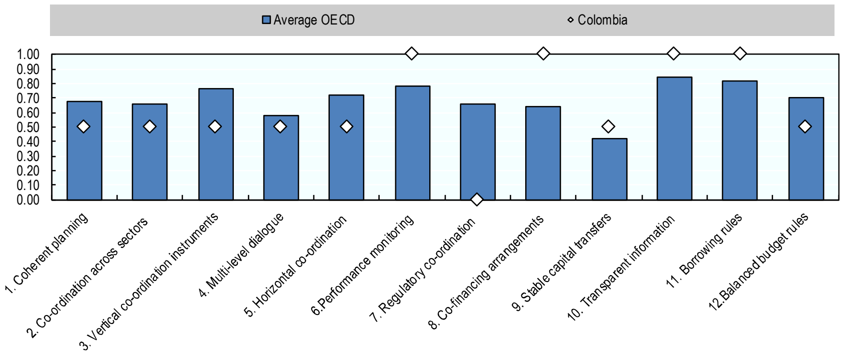
Colombia's approach to investment should have a strong place-based dimension to reflect different territorial needs and challenges. Infrastructure and improved connectivity can help lagging regions converge and improve their performance as long as other key growth factors, especially human capital, are also improved (OECD, 2009). The different investment priorities need to be articulated in coherent territorial strategies. Colombia has taken a more territorial approach to investment at the national level in recent years, in particular in the 2014-2018 National Development Plan. At the subnational level, major efforts have also been made to improve the territorial development plans for 2016-19.

Colombia needs to address its public investment framework in a more systemic perspective

Colombia needs to maintain fiscal stability, and at the same time strengthen the capacity of subnational governments to raise additional revenues to fund investment. New challenges are indeed emerging to the sustainability of financing for public investment. Royalties revenues from oil are an important source of investment funding at the subnational level, but they are currently declining. Oil reserves are estimated to last only another six to ten years (OECD, forthcoming), putting pressure on the long-term financing of public investment. It is therefore critical that Colombia find new sources of funding for investment and make the most of existing financing mechanisms. Efforts to support financing should be accompanied by efforts to adopt a more systemic approach to the governance of public investment, to reduce the overall fragmentation of the system, as many systems coexist with little connection among them. The Department of National Planning (DNP) is currently working on several policies to tackle this fragmentation issue. In particular, Colombia should further support subnational governments in their capacity to finance and plan investment in a more strategic manner.

The multi-level governance indicators developed by the OECD allow for a comparison between Colombia and OECD countries on the key principles of the OECD *Recommendation of the Council on Effective Public Investment across Levels of Government*. They measure formal mechanisms of co-ordination of multi-level governance of public investment but do not measure their effectiveness per se. As indicated above, Colombia has solid fiscal framework conditions for public investment, but scores below the OECD average with respect to vertical and horizontal co-ordination, as well as regulatory co-ordination. Across levels of government, investing together is inextricably linked to the broader challenges of governing together.

Figure 0.5. **Multi-level governance of public investment: OECD preliminary indicators**



Note: 1. See Annex A for the methodology on the multi-level governance indicators.

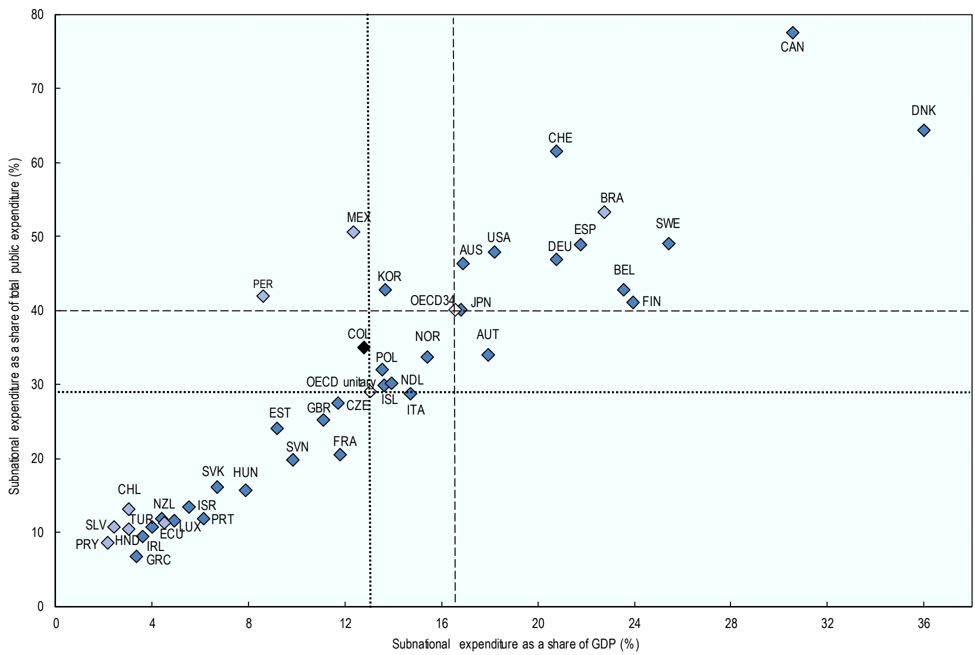
Source: OECD (2016f), Preliminary indicators on co-ordination of public investment for regional development.

Framework conditions: Enhancing subnational revenues to finance investment

In a context of reduced revenues from royalties, some framework conditions need to be revised to sustain a framework more conducive to public investment

Subnational governments have been playing an increasing role for public investment since the decentralisation and royalties reform which has allocated revenues from royalties to all departments, and not just resource-producing departments. When compared to OECD countries, Colombia has a slightly lower level of fiscal decentralisation – regarding spending – than the OECD averages. However, if only OECD unitary countries are considered, Colombia stands around the OECD averages, which amounted respectively to 29.1% of public expenditure and 13.0% of GDP in 2014. Municipalities represent around two-thirds of expenditure and departments one-third. Colombia has a higher share of subnational public investment than countries like Chile, Greece, Ireland, New Zealand or Turkey where local governments have limited competencies, and a lower share than unitary countries where local governments' involvement in the economy is significant, such as Japan and the Nordic countries (Denmark, Finland, Sweden). In Latin America, Colombia is, with Peru, among the most decentralised unitary countries in terms of the importance of subnational government public spending. However, spending autonomy is largely limited by the fact that they are constrained by their revenue sources. Most expenses are earmarked to education, health, water and sanitation.

Figure 0.6. **Subnational government expenditure as a percentage of GDP and public expenditure in 2014, OECD and selected Latin American countries**

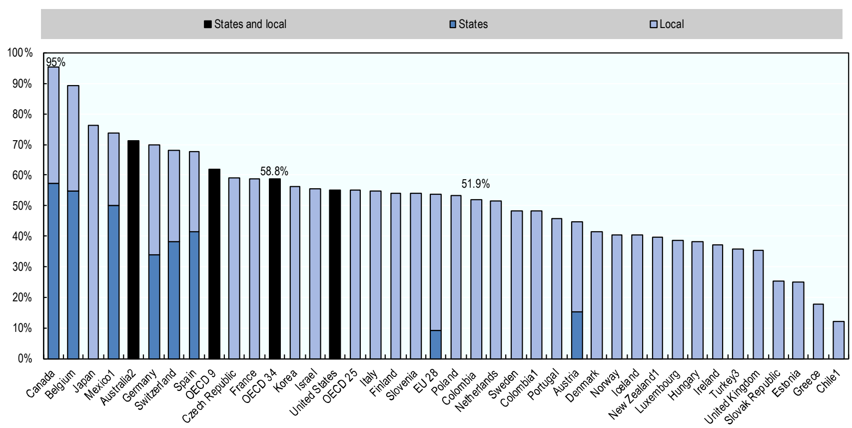


Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Source: Authors' elaboration based on OECD (2016a), OECD (2016b) *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en; OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; authors' calculations for non-OECD Latin American countries based on OECD National Accounts and national sources.

Subnational government capital expenditure, including investment and capital transfers, represents 15% of total subnational government expenditure in Colombia. It is slightly below the OECD unitary countries' average but significantly below some unitary countries where the main functions of subnational governments are investment, such as France or Japan, more than the management of public services and benefits. As for current expenditure, an important part of this investment is earmarked, depending on sectorial subsidies which limit the "investing autonomy" of subnational governments. In the same vain, although it has increased in recent years, subnational governments' share in public investment (51.9% in 2014) is lower than in the OECD (58.8% for all OECD countries and 55.2% for OECD unitary countries only).

Figure 0.7. **Subnational governments' share of public investment, 2014**



Notes: 1. 2013 figures. 2. 2012 figures. 3. 2011 figures. The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Sources: Authors' elaboration based on OECD (2016a) and OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; authors' calculations for Colombia based on OECD National Accounts

Given that most transfers are strictly earmarked, there is room to introduce some flexibility in the transfer system, notably to allow some flexibility to reuse unspent funds from one sector in another sector. An in-depth review of the way the General Participation System (SGP) allocation criteria are determined could be conducted to simplify them and include new equalisation mechanisms, including criteria based on territorial specificities.

This should be encouraged as part of the reform of the SGP system currently being discussed. Earmarked investment grants or matching grants could be established for specific projects and places, such as the City Fund. The reform of the SGP system is a step in the right direction as it includes some of these recommendations.

Another important systemic challenge is the existence of a separate budget for royalties, which is disconnected from the national budget. It is a specific budget defined for two years, the latest of which is for 2016-17. This contributes to the disconnection between royalties and transfers – despite the connections between capital and current expenditures, and to the under-exploitation of local investment plans for the planning of projects to be financed by royalties. The royalties system (SGR) needs to be better articulated with the revenue sharing arrangements (SGP) and the general budget, to better anticipate the impact of capital expenditures on future current expenditures. For example, the impact of planned investment projects on current expenditures could be regularly assessed and included as information in the annual budget. As planned by the current National Development Plan, the central government should be allowed to submit projects to collegiate bodies of administration connected with the reform of royalty payments (OCADs) in areas where the money is not spent, as it is substantial in some places.

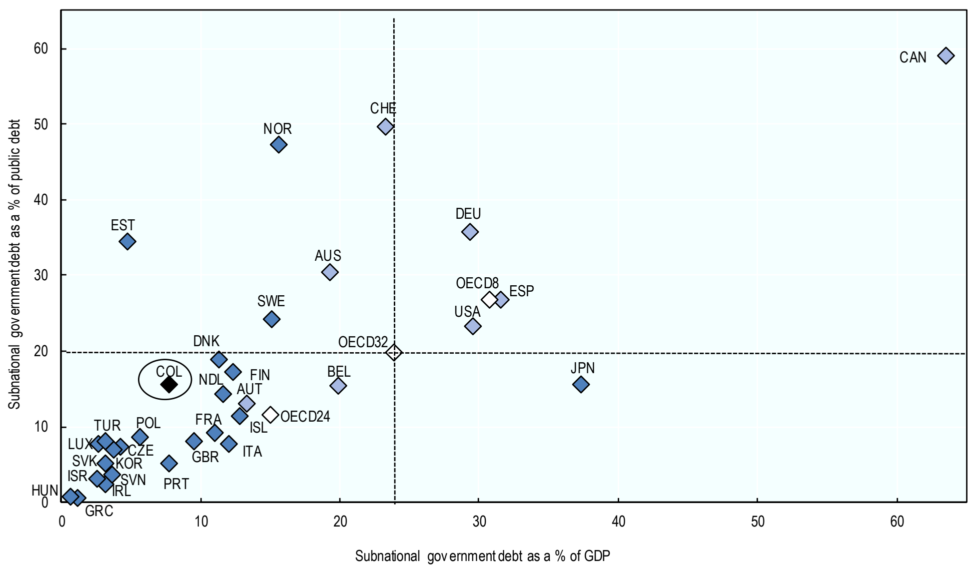
The capacity of subnational governments to raise own-source revenues should be enhanced, through: 1) continuing efforts concerning the update and modernisation of the cadastral and land registries in order to improve the performance of the municipal property tax; 2) streamlining the portfolio of taxes levied by departments and municipalities and promoting tax sharing between the central and subnational governments; 3) reducing the number of earmarked taxes; 4) allowing instruments such as congestion charges or tolls; 5) promoting more flexibility in terms of user tariffs and local fees and optimising income from properties (rents, dividends).

Protecting fiscal discipline, while further supporting external financing of investment

The fiscal situation of subnational governments has considerably improved over the past decades and is solid. In 2014, subnational governments presented a budget balance of 1.2% of GDP. This good situation is the result of fiscal responsibility rules implemented between 1997 and 2003 which introduced several restrictions to excessive spending and constraints to subnational borrowing. Such a low debt level is justified by Colombia’s strong dependence on potentially volatile resource revenues and its exposure as an emerging market economy to global financial shocks.

It is important to protect fiscal discipline while at the same time make the best use of existing borrowing possibilities at the subnational level and explore new options. The level of financial debt (loans and bonds) has decreased both in GDP and total public debt. Borrowing could be further used by subnational governments as a financing mechanism within the limits of the current fiscal rules. Subnational governments need to be further assisted to improve their use and management of loans, including support in project structuration, and better understand the merits, and potential for use, of other asset financing mechanisms.

Figure 0.8. **Subnational government debt as a percentage of GDP and public debt, Colombia and OECD countries, 2014**



Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Sources: Authors' elaboration based on OECD (2016a) and OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; authors' calculations for Colombia based on OECD National Accounts.

Innovative financing tools for investment, such as revolving funds, could be explored for Colombia. The objective is to use transfers with a view to attracting matching funds from municipalities, for example, or to serve as a guarantee for private finance. Revolving funds involve "pump priming" by the central government to stimulate borrowing by subnational governments, creating revenues from loan repayments.

Financing mechanisms to support lagging regions should be strengthened

Efforts to support the capacity of subnational governments to raise own-source revenues are likely to mostly benefit large cities. Fiscal disparities across subnational governments are high in Colombia. In particular, disparities in revenues are large, due to different fiscal, human and technical capacities and autonomy. Around 60% of the revenues of the seven largest municipalities belonging to the "special category" are own-sourced, while the ratio falls to approximately 15% for almost 90% of Colombian municipalities.

Given the existing high disparities and the risk that fiscal decentralisation increases them further, it is necessary to strengthen financial solidarity. Equalisation mechanisms to support these regions should be reinforced as part of the reform of the system of transfers that is currently being discussed. They could also include specific equalisation mechanisms within metropolitan areas which are confronted with high disparities. Existing tools such as the *Contratos Plan* and new peace contracts under preparation should be strengthened as key mechanisms to support investment in lagging regions. In general, supporting investment at a supra-municipal scale can also contribute to support lagging regions, through higher scale projects with greater impact.

A more systemic approach: Improving horizontal and vertical co-ordination for public investment

Colombia has developed a sophisticated planning framework to guide investment priorities, at both the national and subnational levels

The national and subnational development plans are key tools to help prioritise investment and align objectives. The 2014-2018 National Development Plan has a strong territorial dimension with sophisticated mechanisms to monitor progress in "closing gaps" across regions. The outcomes of both the City Mission and the Rural Mission, integrated in the National Development Plan, have contributed to make significant progress to a better understanding of the specificities of the different types of territories, and the priorities for investment. At the subnational level, departments and municipalities also design four-year "local development plans" (PDT). These plans are designed at the beginning of each local electoral mandates and are supposed to be articulated with the National Development Plan. The PDTs will remain valid for the 2016-19 period. The 12-year Land-Use Plan defined at the local level (POT) is also supposed to be articulated with the PDT.

However, in practice, subnational development plans are often considered a formal exercise and are disconnected from other instruments such as land-use plans

Turning strategic planning into effective investment prioritisation is a major challenge for any public investment policy. Subnational governments often consider the planning activity as merely a formal exercise. One of the difficulties is the short timeframe subnational governments have to design their development plans (around two months). In addition, the PDTs tend to be disconnected from the POTs. In addition, many municipalities lack the adequate capacities to design their development plans and lack data on infrastructure needs or rural-urban linkages. Many PDTs lack clear objectives with adequate indicators, which also hampers the evaluation process. The design and implementation of local development plans is overseen by a territorial planning council in each department and municipality, which include representatives from the civil society and the private sector. However, they lack financing for functioning, leading to weak implementation monitoring.

An improved connection between planning and budgeting is needed to help prioritise investment needs on a multiannual basis

The national and subnational development plans are in theory connected with multiannual investment plans and budgets. However, in practice, there is often no direct connection between subnational planning and budgeting. Local development plans are not connected to the medium-term fiscal framework nor to annual budgets or the selection of projects to be funded by royalties. In principle, subnational governments are required to design medium-term fiscal frameworks valid for ten years. They have to be updated each year and show compatibility with the budget surplus and public debt objectives. However, less than 30% of subnational governments develop such frameworks.

Improved PDTs, better co-ordinated with the POTs, could significantly help medium-term prioritisation of investment as part of subnational governments' medium-term fiscal frameworks. They could play a significant role in better articulating the diverse financing sources which so far follow disconnected planning and evaluation approaches. The strategic framework provided by the PDTs could be used as input into the decision-making process of the OCADs to select investment projects to be financed by royalties, with priorities mentioned in the PDT used as selection criteria. This would allow using royalties in a more strategic manner. The *Contratos Plan* also need to be better articulated with local development plans. The departments could have a role in scrutinising this.

There is a need to encourage the integration/merging of different sources of funding (royalties, the SGP, taxes, private funding) to finance projects/programmes. This also means moving towards a budgeting system based on outputs instead of on the inputs of disconnected funding sources, to allow a more integrated approach to planning and budgeting. Colombia is making progress in that direction. The DNP is working on a common framework with indicators to be used in development plans and budgets. In a first stage, the programmes included in the budget will seek to match the programmes of the National Development Plan and the next development plans will be structured with the objective to be integrated with the budget structure. This new framework is supposed to be applied to the national budget in 2017 and to subnational governments' budget in 2018 (DNP, 2016).

Moving away from a pure project-based approach to a more strategic/programme-based approach

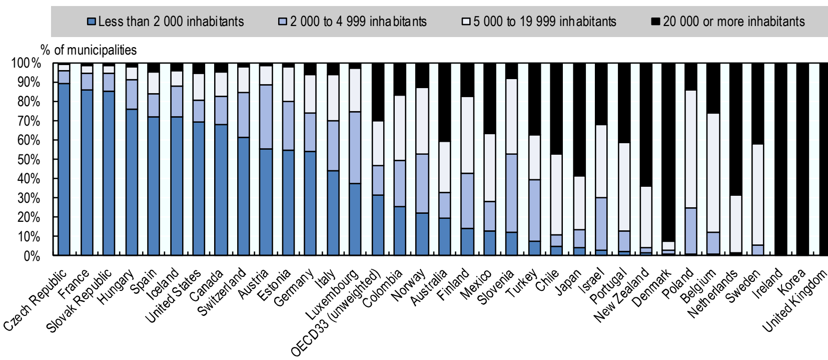
Colombia is seeking to move from a project-based approach to a more strategic/regional approach to investment, through articulated programmes rather than just individual projects. This is notably true for the governance of royalties – but also for other sources of funding like the SGP and the national budget. Although the royalties reform is a significant progress, challenges are mainly linked to the atomisation of royalties and to the disconnection between the governance of the royalties system and the subnational planning system for investment. In practice, projects funded by royalties are atomised in thousands of projects – managed by the 1 025 OCADs. This fragmentation means that large-scale infrastructure projects with higher social returns are not prioritised. Even if it is clear that not all royalties are appropriate to finance projects with a regional impact, only 5% of the projects approved had a regional dimension (DNP, 2016). Even considering the fact that the value of the projects financed by regional funds is six times higher than the average value of the "local" projects, this proportion seems very low.

Some progress is being made, however, notably in the context of the 2014-2018 National Development Plan. Indeed, the DNP is now allowed to propose regional projects to OCADs. Although the number of OCADs was not reduced – and has even increased as in 2016 there are 39 new OCADs – the number of sessions and the way they are organised has changed, as sessions can happen with groups of OCADs, in a sub-regional way. This should be further encouraged, and the calendar set for OCADs could also take into account the annual budgeting process for subnational authorities, to facilitate the co-ordination between overall revenue and investment. The requirements for project formulation and approval of SGR projects might also be differentiated according to a project's size and complexity.

Support to more strategic investment requires greater horizontal co-operation across jurisdictions and specific incentives to support it

Like in many countries, horizontal co-operation across jurisdictions is a top priority to support more strategic investment – particularly at the metropolitan scale and for smaller municipalities in rural areas. In Colombia, there are 1 101 municipalities (Figure 0.9). The size of Colombian municipalities is relatively large on average (43 370 inhabitants on average compared to 9 570 on average in the OECD), and 25% of these municipalities have less than 2 000 inhabitants (compared to 31% on average in OECD countries). A specificity of Colombia is that the urban system in characterised by relatively small functional urban areas, with the population concentrated in the city centre and few limited commuting areas (Sanchez-Serra, 2016). Urban-rural linkages are generally weak, leading to a low spillover effect (OECD, 2014). Improved connections between core cities and their surrounding areas would contribute to enlarge local labour markets, strengthen agglomeration economies and support productivity. This requires not only a strong infrastructure investment effort, but a focus on urban-rural linkages and strong support to mechanisms of co-operation across jurisdictions to develop joint investment strategies.

Figure 0.9. **Municipalities by population size, OECD countries and Colombia**



Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Source: OECD (2016d) “Subnational government structure and finance”, *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en and (OECD 2016g) Subnational governments in OECD countries: Key data, 2016 edition”, www.oecd.org/gov/regional-policy/Subnational-governments-in-OECD-Countries-Key-Data-2016.pdf; DANE (2016) for Colombia.

Since 2010 and the adoption of the Organic Law on Land Use Planning Colombia has made progress in fostering inter-jurisdictional co-operation on investment and public service delivery. Metropolitan governance is also more advanced than in many OECD countries. In 2016, there are 11 formalised associative structures at the municipal level and 14 are currently being formalised.

Municipal associations and planning regions remain limited so far. This is notably due to a lack of incentives (financial) and competence for designing and implementing regionally co-ordinated investment, to overcome reluctance to complex and potentially costly co-ordination processes. Besides, associations have to be financed through members’ resources (DNP, 2016). There are also common difficulties in identifying joint issues to be solved through joint investment. The lack of financial incentives to support cross-jurisdictional co-operation is an important obstacle. The experience of France and Italy, which have put in place specific financial incentives to promote inter-jurisdictional co-operation, might be of interest to Colombia.

The government might consider providing financial incentives to support horizontal associative schemes across municipalities and departments, for example through matching grant/co-financing projects between the national government and associations of subnational governments' entities. Such associations could also promote joint procurement. They could have access to royalties revenues. Regional co-operation and its results should be analysed and evaluated on a regular basis at the national level to allow monitoring, promote learning and disseminate good practices.

Further supporting horizontal co-operation is particularly needed at the metropolitan scale to reinforce functional urban areas, in particular in Bogota, Barranquilla, Cali, Cúcuta and Cartagena

Further supporting horizontal co-operation across jurisdictions is particularly a priority at the metropolitan level, given the small size of functional urban areas in Colombia (Sanchez-Serra, 2016). Successive laws in Colombia have strengthened metropolitan governance, and several metropolitan areas (like Medellín or Bucaramanga) have more competencies or access to resources today than in many OECD countries. The 2011 law established a special tax regime for metropolitan areas. The 2013 law (1625/2013) strengthened the legal framework for co-ordination of metropolitan areas, establishing new conditions for the creation, operation and financing of metropolitan areas. Overall, fiscal integration and the taxing power of metro areas remain limited. In addition, metropolitan areas are not recognised as "territorial entities" by the Organic Law governing the Territorial Organisation in Colombia.

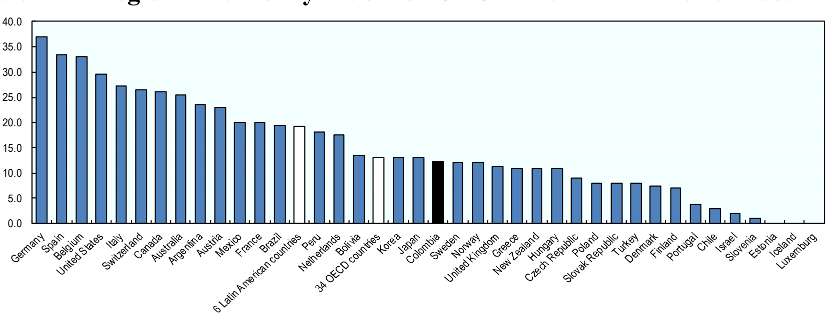
Besides, and most importantly, many of the larger Colombian conurbations, such as the capital city Bogota, Cali or Cartagena, are not structured as metropolitan areas. There are several explanations for the difficulties in structuring efficient metropolitan areas, among which the fear of mayors of losing powers, strong internal disparities between the municipalities or the lack of incentives (financial in particular). Improved metropolitan governance in Bogota, which has for decades struggled with its public transport system, would be of benefit for the entire country. Creating a regional mobility authority as a means of building capacity for managing the region's transport system at the metropolitan scale is also an option. Germany's "communities of transport", particularly the transport authority in Frankfurt, could be a useful example for the Bogota metro region. It sets transport policy, is in charge of planning, takes investment decisions, sets rates, and co-ordinates the 153 public and private operators.

The Colombian government still has an important role to play in aligning incentives and fostering co-ordination among local governments to build metropolitan areas. The possibility of a broader specific tax system could be studied, but it should not take resources away from the municipalities, which would be a great disincentive. Equalisation mechanisms could be fostered within metropolitan areas to foster solidarity based on a new tax, e.g. linked to a metropolitan competence. Finally, specific contractual arrangements targeting specifically metro areas committed to improve their governance could be envisaged, like City Deals in the United Kingdom.

Reinforcing more strategic vertical co-ordination through, in particular, a stronger co-ordination role for departments

Departments have, in principle, the mandate to play a multifaceted key role for regional development and territorialised public investment, and to be the key players for vertical co-ordination in the interaction between municipalities and the central government. They are supposed to have institutionally, technically and financially a co-ordination role to support municipalities in their investment policy. However, despite this important role stated in the Constitution, departments have limited resources to fulfil their responsibilities and respond to the demands of municipalities. Colombia ranks relatively low in terms of "regional authority" as measured by the Regional Authority Index, lower than Peru or Bolivia for instance (Marks and Hooghe, 2016).

Figure 0.10. **Regional Authority Index for OECD and Latin-American countries**



Notes: OECD 34 corresponds to the OECD average; 6 Latin American countries corresponds to the average of unitary Latin American countries. This index synthetises the five dimensions of self-rule (institutional depth, policy scope, fiscal autonomy, borrowing autonomy and representation) and shared rule (law making, executive control, fiscal control, borrowing control and constitutional reform).The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Source: Marks and Hooghe (2016), Regional Authority Index, www.arjanschakel.nl/regauth_dat.html.

The role of departments should be enhanced as regional integrators through investment projects. Departments could take a more proactive role to support critical projects with cross-jurisdictional co-operation, in particular *vis-à-vis* rural municipalities. They could have the mandate to incentivise regional co-operation for investment projects (financed through the SGR or other sources), as technical support and political facilitator. Departments could also play a stronger role in scrutinising the co-ordination of land-use and development plans. The new tool under discussion – department land-use plans (POD) – would also contribute to strengthen a regional approach of relevant issues regarding land use.

At the same time, planning regions could be further strengthened as they can act as key co-ordination levers. The central government may co-finance strategic investment projects with the RAPs, which are associations between two or more adjacent departments whose purpose is the socio-economic development of a specific territory.

Colombia could also introduce pilot experiences of regional management offices in a small number of departments, from which lessons could be learned before generalising the experience.

Finally, *Contratos Plan*, launched in 2011, has been effective in strengthening co-ordination, supporting capacity building and overall infrastructure development. They need to be further developed and supported. They are key instruments to create powerful positive incentives for the evolution of subnational stakeholders' "behaviour", such as to promote municipal cooperation and strengthen the capacities to develop long-term development strategies. Incentives could be set for the contract enforcement, for example allocating part of the funding based on good performance (performance reserve, on the model of Italy or the European Union); and part of the funding could be dedicated to projects with a regional impact. The timing of these contracts, which for the moment varies greatly, should be standardised in order to facilitate monitoring and capacity building. The new generation of *Contratos Plan* called *Contratos Paz*, will be instrumental to support inclusive territorial development with regions the most hit by the conflict.

Strengthening subnational capacities to design, implement and monitor investment strategies

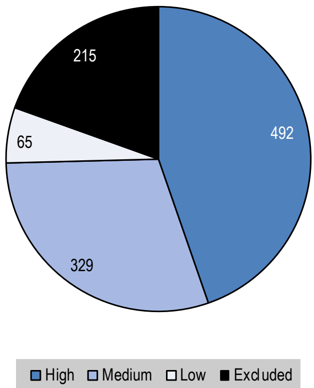
A continuous effort to strengthen subnational capacities

The low level of capacities in more than two-thirds of Colombian jurisdictions (DNP, 2016) is probably the most important bottleneck for effective public investments. The DNP has developed an innovative index to assess subnational capacities, which shows that two-thirds of municipalities have low capacities, whereas 30% have medium or high capacities. Many (672) municipalities did not execute more than 20% of their budget in 2014. While subnational capacities, in particular at the municipal level, vary greatly across the country, the most important challenges are linked to the relatively small size of the subnational public sector, high staff turnover, low wages, and the political rather than technical profiles of executives in municipalities. Weak capacities to design projects in rural regions contribute to territorial disparities.

The rapid turnover of mayors and governors, resulting from their term which is restricted to only one four-year mandate, neither facilitates the emergence of experienced senior executives over the long-term nor creates incentives for long-term investment.

In terms of subnational public employment, there are recruitment constraints, and the size of the subnational workforce is relatively small in comparative perspectives. Municipal employment has not quantitatively nor qualitatively evolved in parallel to the devolution of competences. In addition, salaries tend to be very low in the subnational public workforce. The legislation limits increases in operating costs (especially for municipalities with less than 30 000 inhabitants), without considering the needs of new staff and qualified skills to perform their duties and new assignments transferred to them. The shortage of a skilled workforce is a bottleneck for the design and implementation of investment projects at the local level. Colombia needs to develop mechanisms to quantify subnational public employees to be able to get a clearer picture of the gaps and needs in terms of staff at the subnational level. On this basis, it would be advisable to better assess the most problematic capacity gaps and to list a required set of skills for subnational public employees in charge of managing investment/ development plans.

Figure 0.11. **Classification of municipalities by general criteria**



High: municipalities having one or two certifications and the highest indicators of performance and efficiency.

Medium: municipalities with relatively high performance and efficiency indicators but which lack certification.

Low: municipalities with relatively low indicators.

Excluded: municipalities without the ability to manage resources.

Source: DNP (2015a), "Evaluación de Desempeño Integral 2015", PowerPoint presentation

The DNP strongly supports capacity building

Colombia has intensified its efforts to increase technical assistance to subnational governments for the design of the PDTs and the POTs and to enhance local capacity. A new Program for Strengthening of Institutional Capacity for Territorial Governments was introduced in 2014, which includes a territorial management diagnosis tool and a specific module on financial management and public investment. Subnational governments are trained to apply this diagnosis and take adequate corrective actions. So far 70 subnational governments have already benefited from this programme in all public management areas (DNP, 2016).

The limitations of the territorial development plans have also been tackled very seriously and significant improvements in their implementation have been set up in the last years. The DNP has also actively supported municipalities in the design of the new 2016-19 PDTs. Given the very tight timing to elaborate these plans, the DNP had anticipated some of the needs, in the "Strengthening new heads of subnational governments" strategy (*Estrategia para el Fortalecimiento de Nuevos Mandatarios*). This strategy includes information, methodological tools (KiTerritorial), training and technical support to the candidates prior to the election, and then to the elected authorities. This assistance targets 462 subnational governments with weak capacities (according to the "closing the gap" strategy criteria or in conflict areas), while other municipalities are provided with international co-operation assistance (183) or by the public administration school ESAP

(300). A majority of subnational governments consider that this technical assistance is excellent, but that more technical assistance is needed.

Taking advantage of the great numbers of POTs to be revised in the following months, DNP plans to support 100 municipalities and 10 departments identified as key for the country's development (89 POT will be co-financed by DNP). This support will come through the Land-Use Plan's Program (Programa Nacional de POT/POD Modernos). The programme will co-finance a dedicated unit within each selected municipality to update the POT, and participate in its implementation through capacity building.

The various technical assistance programmes need to be better co-ordinated, with a special focus on weaker municipalities. The assistance could pay special attention (although not exclusively) to the design phase of projects. The role of departments for municipal capacity building and technical support should also be better acknowledged and supported. Partnerships with departments and with the Colombian Municipalities Federation need to be promoted, including the exchange of good practices among subnational governments and peer learning mechanisms.

Ensuring continuity and stability in the rules to strengthen subnational capacities in a sustainable way

The absorption by municipal staff of the numerous tools and methodologies proposed (PDT, POT, MGA, Sinergia, SMSCE, etc.), which are often not integrated, is challenging. Municipalities have to deliver a large number of reports (248 per year, according to Colombian Municipalities Federation), which are often quantitatively far beyond the capacity of municipal staff. Collecting and providing timely data is an important challenge. These difficulties are amplified in smaller municipalities. To address this, the Department of National Planning is currently working on the implementation of a unified information system as an effort to reduce barriers in the data collection process.

It is crucial to ensure continuity to strengthen subnational capacities on a continuous basis. To address the need of building the long-term capacities of subnational governments' staff and elected representatives, it seems necessary to implement a permanent and comprehensive training and technical assistance system specifically dedicated to them.

Recently, the DNP has developed planning prototypes (26) for projects with similar characteristics, defining guidelines for standardised projects to improve the quality of public investments. These guidelines trigger a learning-by-doing process at the subnational level while subnational government officials take advantage of capacities concentrated at the central level. At the same time, it helps to reduce time and costs in the preparation of projects and reducing the gaps between regions.

Reducing administrative burdens is a top priority

One of the major constraints for subnational governments for effective public investment is linked to high regulatory and administrative burdens and the fact that regulations are the same for all governments, regardless of their capacities. For example, the current system, which already distinguishes between "certified" and "non-certified" municipalities for certain competencies (education and health), is criticised, as small municipalities have roughly the same obligations as the large ones.

Quality, stability and coherence in the regulatory framework across levels of government are crucial elements for subnational investment. The Department of National Planning has made progress in this domain by launching a programme of technical assistance to territorial entities to improve the quality of their regulations. Colombia lacks institution carrying out systematic *ex ante* assessments of the impact of new regulation. Good practices in this area are found in Denmark and Germany as far as regulatory impact analysis is concerned, in France (policy of simplification and reduction of regulatory burden), Mexico or Spain. In addition, Colombia should work further at differentiating the different types of administrative requirements according to project size and complexity.

Improved control systems for procurement, an integral function of public investment

Procurement is integral to public investment and can help achieve more than just procurement goals. But procurement is also the government activity the most vulnerable to waste, fraud and corruption. In 2012, Colombia Compra Eficiente was established as the government's new central procurement entity in charge of setting up framework agreements, co-ordinating and advising on procurement policy, and assisting buying entities and suppliers in procurement practices. It is important to build the right administrative framework and capabilities to manage procurement at that level as 41% of the value of public procurement in Colombia is carried out at the subnational level.

Colombia has substantially reinforced its control and audit system in order to reduce corruption at the regional and local levels. The fight against corruption through a robust integrity framework at the subnational level has been identified as a core issue to implement the decentralisation process in Colombia and a pre-condition to enlarge the autonomy of the subnational governments in the management of public funds. One of the remaining challenges is to reform the election of regional comptrollers, since they are currently appointed by regional assembly, i.e. those they are supposed to control.

There are also challenges linked to the subnational governments' capabilities to conduct procurement, which vary across places. Capacity challenges are more acute in small towns in rural areas, with few and often poorly trained officers. According to the Delegated Attorney for Decentralisation, Procuraduría delegada para la descentralización, out of 28 000 investigations conducted, 60% of offences resulted from ignorance and lack of standards.

Colombia Compra Eficiente has recently simplified regulation, specifically bearing in mind the capability constraints at the subnational level. Furthermore, Colombia Compra Eficiente has issued guidance manuals for subnational governments as well as standard procurement documents for public works, trusts and ICT procurement, among others. Colombia Compra Eficiente has encouraged collaborative procurement through framework agreements, but these are still little used. Several challenges remain, such as to implement a decentralised procurement system allowing subnational governments to purchase goods and services at the local level and to use the new advanced electronic platform set up in 2015. Another challenge is that the focus tends to be on processes rather than outcomes. Therefore, it seems necessary to move from a control system based on a formalist approach (compliance requirements) to a system based on the evaluation of results.

Support to subnational governments in using public-private partnerships should be amplified

Similar to that of Mexico, Colombia's PPP model is significantly more decentralised than that of other countries in the region and each level of government entity is responsible for planning, implementing and supervising PPPs. This requires thus significant capabilities from subnational governments as PPPs are very complex types of procurement mechanisms. In 2012, Medellín created an institution entirely dedicated to PPP development, which is the first in Colombia (the Agencia para las Alianzas Público Privadas). So far, with the exception of large cities, PPPs are little used by subnational governments, as they are considered as debt at the subnational level, but not for the central government. PPP projects are, in general, technically, legally and financially complex, and imply a high-level of expertise that is not available outside the bigger cities and departments.

The DNP is, however, trying to support subnational governments in this field and has set up and manages a database to register PPP projects. The experience of the United Kingdom in reinforcing local authorities' expertise could be helpful for Colombia, through, for example, the introduction of line ministry PPP units, enhanced project scrutiny and the standardisation of contracts. The experience of the Philippines, which has put in place revolving funds to help public actors at the national or subnational levels prepare project pre-feasibility and feasibility studies for PPP projects, could also be interesting for Colombia.

Simplify ex ante *assessments (General Adjusted Methodology) to more effectively use them in the selection of projects*

In Colombia, it is estimated that more than two-thirds of the problems associated with the investment cycle of a project is due to weaknesses in structuring projects at the planning phase (Fedesarrollo, 2014). On paper, most tools in Colombia exist for effective *ex ante* appraisal processes: the General Adjusted Methodology (MGA) is a detailed appraisal methodology that all individual public investment projects are supposed to follow and development plans are supposed to be linked to yearly subnational investment budgets. However, there is some evidence of deficiencies at the subnational level in the project preparation phase, restricting the efficacy of the *ex ante* appraisals, mostly due to its complexity and inadequate skills of subnational governments to manage it. Progress is, however, being made: the MGA has been simplified and will be accessible online in 2016. Training has been performed in 98% of subnational governments since the beginning of the MGA use.

Simplifying the MGA would allow it to be used more effectively. In addition, strong and continuous technical support needs to be provided to the weaker subnational governments, possibly combined with funding for externalisation of part of the *ex ante* appraisal (external expertise). In some extreme cases for weaker municipalities and/or complex projects (for example the SGR ICT fund), it may be worth considering the possibility of substitution by the department or government agencies (DNP, Findeter, FONADE) for project preparation and implementation.

Extending *ex ante* appraisals following the MGA methodology to all subnational governments' investment projects would allow more adequate prioritisation and higher quality projects, as well as faster validation – by the OCAD for instance. In addition, appraisal methodologies may be differentiated according to the size of the project, or its complexity/risk.

This would mean a more lenient appraisal for smaller projects and a more rigorous assessment for larger/riskier projects.

Better use the MGA in the prioritisation of projects funded by royalties, implement the new scoring system and consider maintenance costs

Although all projects financed by royalties (SGR) are supposed to follow the MGA methodology, there are deficiencies from subnational governments in the analysis and project preparation process (formulation, cost and benefits estimates, definition and use of indicators). Most SGR projects, for instance, do not include operational costs, which weakens their sustainability. Since mid-2015, the DNP has been implementing a scoring system (*Sistema de Puntajes*) that allows prioritisation by OCADs of fund allocation for co-financing and for royalties based on objective criteria linked to needs. A sectoral scoring mechanism was also approved in April 2016 for tertiary roads. A similar scoring is being discussed for water and sanitation, housing, etc. These developments, if they are successfully implemented, would represent a major progress, as it would facilitate the prioritisation of the allocation of funds for co-financing and for royalties based on objective criteria, in line with the "closing gaps" approach. The question of maintenance costs should be made more explicit in the scoring system.

Moving away from formal control of execution phases to improved project selection and design

The main issue for project monitoring is that emphasis is put on a formal control of the contracting and execution phases of the projects, leading to a highly bureaucratic process that puts a heavy burden on subnational government administrations and general fear of not complying with the numerous formal obligations and being subject to penal pursuit. Subnational governments need to put more emphasis on: 1) checking coherence with the overall public investment strategy; 2) checking technical and financial feasibility, sustainability and efficiency (including an appraisal of the impact of the investment on current expenditures). Overall, Colombia should put more emphasis on the selection and design of projects as well as on *ex post* evaluations (World Bank, 2016), without neglecting control on the contracting and execution stage.

The monitoring system for public investment is fragmented and mirrors the fragmentation in funding sources

Colombia has developed a comprehensive array of evaluation mechanisms, focusing on institutions, programmes, projects, budgetary and strategic aspects. Some of them are considered very sophisticated by international standards, such as the royalties monitoring system, Sinergia or *desempeño integral*. Colombia holds the fourth position after Chile, Mexico and Brazil within the Monitoring and Evaluation Index developed by the Inter-American Development Bank for Latin America and the Caribbean (IDB, 2015). But, like funding sources, they are not articulated. The monitoring system for public investment is fragmented, and mirrors the fragmentation in funding sources (national budget, SGP, SGR). The SGP uses, for example, efficiency indicators from the "Evaluación de desempeño integral" (DNP, 2016), whereas the General Royalties System has used a Monitoring, Tracking, Control and Evaluation System since 2013 focused on the execution of budgeted investment. The limited coherence in the evaluation process between strategic planning and the various financing sources weakens the articulation of monitoring between strategic planning and budgeting/execution.

Strong effort is, however, being made to improve the evaluation system. One example is the Bank of Investment Projects (Banco Único de Proyectos) that manages information on public investment projects during the entire investment cycle, for monitoring and financial planning purposes. In practice, however, there is not one single integrated standard methodology to report projects, thus preventing any consolidation of data received from the different funding sources. The DNP is working on the standardisation of reporting mechanisms through user-friendly tools, that all subnational governments would have to use. The reform under way of merging GESPROY (used for SGR projects) and the Investment Projects Monitoring System (SPI) within a unique device, with a visualisation and georeferencial module for the consolidation of all public investment projects (*MapaInversiones*), would bring significant progress. The idea behind this key programme is to switch from a monitoring differentiated by funding source to a programme-oriented integrated monitoring system that would incorporate the various funding sources (national budget, SGR and SGP mainly) and connect planning to budgeting and execution.

Efforts to simplify data collection through MapaInversiones

Challenges also include problems regarding data collection from subnational governments (DNP, 2016). Although the situation has improved in the last years, there are still problems with timely and accurate information reporting. Improvements have been made through the Sinergia monitoring system, but this requires capacities for subnational governments to regularly collect the adequate set of data. Indicators exist from many sources (*Fichas territoriales*, Sinergia, *MapaRegalías*, *Contratos Plan*), but they need to be standardised and systemised and updated in a timely manner. Over the past few years, several initiatives have been taken to standardise and simplify data collection and presentation, among which the MapaRegalías project can be highlighted. The MapaRegalías project aims at providing timely accessible information on any project financed by the SGR, through Internet access. It will be extended to all public investments (MapaInversiones). MapaInversiones will be available the first trimester of 2017 with information about public investment corresponding to the national budget, SGR and SGP.

Information accessibility also faces the challenge of data comparability among sources (for instance the DNP and Ministry of Finance have distinct figures on investment, due to distinct ways of aggregating data). Data improvement should include alignment to international standards for the definition of investment (gross fixed capital formation). Colombia should consider extending the use of the National Accounts definition of public investment, to clarify measurement and facilitate monitoring.

Differentiating competencies and reporting requirements according to the degree of capacities

To address the fact that capacities vary greatly across jurisdictions, Colombia is currently considering a new reform to differentiate competencies according to the degree of capacities. Some variation in the allocation of competencies already exists. For example, the certification of municipalities for health and water entails some differentiated competencies: in the uncertified municipalities, the department is responsible for these competences. The new Differentiated Competences National Program included in the 2014-2018 National Development Plan goes further, as it intends to respond to the disparities among the capacities of subnational governments by providing the possibility of allocating more responsibilities to the more qualified ones. Sectors that could be more efficiently managed at the municipal level were identified, some of which are strongly related to investment policies. Following a multi-criteria analysis (including the provision of basic services, generation of own resources, accomplishing goals of development planning, appropriate use of financial resources, financial solvency and respect of fiscal procedures), the DNP identified 105 municipalities with high skills levels which could assume functions that now are being given by the national government to ensure a more efficient delivery of goods and services. The priorities will be to delegate competencies for rights for victims, cadastres and transport (tertiary roads). The delegation depends on the function to be delegated. General and specific criteria should be established for each function.

This policy is not associated with any specific financial incentive, but the corresponding budgets would be passed on to the municipalities. The first delegation underway is the multi-purpose cadastre in the municipality of Barranquilla.

Asymmetric decentralisation needs to be further exploited in both directions: 1) the most capable subnational governments can handle additional competencies; 2) weaker subnational governments need simplified reporting mechanisms to alleviate the administrative burden. Experiments could be made to grant some exemptions to government requirements. Such asymmetry in competencies also requires differentiated tax management, as highlighted above.

Continue to further involve stakeholders in public investment governance at all levels of government

Colombia has set up various innovative mechanisms to enhance stakeholders' involvement (citizens, civil society, private sector, academics and experts) in the design and implementation of investment policies ("visible auditing", MapaRegalías, MapaInversiones, citizen watchdogs) at all levels of government. At the local level, the city of Medellín and the department of Antioquia have developed sophisticated co-ordination arrangements and mechanisms to involve citizens. Medellín is one of the largest cities to implement participatory budgeting. Participation in Colombia has also been strongly encouraged in the planning stage, both at the national and the local level, and in the evaluation of investments funded by the SGR. Yet, stakeholders' involvement appears to be limited by low skills and scarce financial resources for participatory and networking processes in many subnational governments.

Information accessibility should be improved for citizens and stakeholders alike (make investment information available in a timely, visible and simple way). A compulsory timely and standardised display of accounts on subnational governments' website (or on a specific dedicated website) would enhance transparency on their financial management as a whole. Italy has set up such a web platform for all public investment projects.

Finally, the participative approach with communities in the preparation of the new *Contratos Paz* has been considerably strengthened. This will contribute to help build social capital in these regions, and these joint investments will ultimately contribute to building peace in Colombia.

Table 0.1. **Summary assessment: OECD Recommendation on Effective Public Investment across Levels of Government**

Colombia

System is in place and works in a satisfactory way	System is not in place or not functioning well
System is in place, but improvements are needed	Additional information needed

PRINCIPLE 1:	
To engage in planning for regional development that is tailored, results-oriented, realistic, forward-looking and coherent with national objectives	COHERENT PLANNING ACROSS LEVELS OF GOVERNMENT Mechanisms exist to ensure that subnational investment plans reflect national and subnational development goals.
	TAILORED, PLACE-BASED DEVELOPMENT PLAN Assessment of territorial needs and strengths corresponds with planned projects.
	CLEAR PUBLIC INVESTMENT PRIORITIES There is a clear and authoritative statement of public investment priorities at national and regional levels.
To co-ordinate across sectors to achieve an integrated place-based approach	COMPLEMENTARITY OF HARD AND SOFT INVESTMENTS Consideration is given to complementarities between investments in hard and soft infrastructure.
	COMPLEMENTARITIES ACROSS SECTORS Attention is given to potential complementarities and conflicts among investments by different ministries/departments.
	CROSS-SECTORAL CO-ORDINATION Formal or informal mechanisms exist to co-ordinate across sectors (and relevant departments/agencies) at the subnational level.
To support decisions with adequate data	FORWARD-LOOKING INVESTMENT PLANS Authorities assess the potential contribution of investments to current competitiveness, sustainable development, and regional and national well-being.
	DATA AVAILABILITY AND USE FOR INVESTMENT PLANNING Data are available and used to support the territorial assessment and planning process.
PRINCIPLE 2:	
To co-ordinate across levels of government to reduce asymmetries of information	CO-ORDINATION BODIES ACROSS LEVELS OF GOVERNMENT There are formal mechanisms/bodies for co-ordination of public investment (formal platforms and ad hoc arrangements) across levels of government.
	CROSS-SECTORAL APPROACH These co-ordination bodies/mechanisms have a multi-sector approach.
	MOBILISATION OF CO-ORDINATION ARRANGEMENTS These co-ordination mechanisms are mobilised regularly and produce clear outputs/outcomes.
	EFFICACY OF CO-ORDINATION PLATFORMS Stakeholders' perception (or empirical data) regarding the efficacy of these different platforms are available.
	CONTRACTUAL AGREEMENTS/PARTNERSHIPS Contractual agreements/partnerships across levels of government have been developed to manage joint responsibilities for subnational public investment.
	EFFECTIVENESS OF CONTRACTUAL AGREEMENTS The share of subnational public investment covered by these agreements is measured.
To align priorities across the national and subnational levels	CO-FINANCING ARRANGEMENTS There are co-financing arrangements for public investment.

Table 0.1. **Summary assessment: OECD Recommendation on Effective Public Investment across Levels of Government** (*continued*)

PRINCIPLE 3:	
To co-ordinate with other jurisdictions to achieve economies of scale across boundaries	HORIZONTAL CO-ORDINATION Cross-jurisdictional partnerships involving investment are possible. CROSS-SECTORAL APPROACH Cross-jurisdictional partnerships cover more than one sector. INCENTIVES FROM HIGHER LEVELS OF GOVERNMENT Higher levels of government provide incentives for cross-jurisdictional co-ordination. EFFECTIVENESS OF HORIZONTAL CO-ORDINATION The share of investments involving the use of cross-jurisdictional co-ordination arrangements at the subnational level can be measured by mechanism and/or by sector.
To plan investment at the right functional level, in particular in metropolitan areas	DEFINITION OF FUNCTIONAL REGIONS Functional regions are defined and identified in investment policy. USE OF FUNCTIONAL REGIONS Functional regions are used in investment policy.
PRINCIPLE 4:	
To identify social, environmental and economic impacts, ensure value for money and limit risks	*EX ANTE* APPRAISALS A large share of public investment is subject to *ex ante* appraisal. RESULTS OF *EX ANTE* APPRAISALS The results of *ex ante* appraisals are used to prioritise investments.
To conduct rigorous *ex ante* appraisal	QUALITY OF APPRAISAL PROCESS *Ex ante* appraisals are conducted by staff with project evaluation skills. INDEPENDENT REVIEW OF *EX ANTE* APPRAISALS Share of *ex ante* appraisals subject to independent review. GUIDANCE FOR *EX ANTE* APPRAISALS Technical guidelines for *ex ante* appraisal are available and used at all levels of government.
PRINCIPLE 5:	
To engage public, private and civil society stakeholders throughout the investment cycle	MECHANISMS TO INVOLVE STAKEHOLDERS Mechanisms exist to identify and involve stakeholders throughout the investment cycle. FAIR REPRESENTATION OF STAKEHOLDERS Fair representation of stakeholders in the investment cycle consultation process is guaranteed (to avoid capture situations). EARLY INVOLVEMENT OF STAKEHOLDERS Stakeholders are involved from the early stages of the investment cycle. ACCESS TO INFORMATION Stakeholders have easy access to timely and relevant information throughout the investment cycle. FEEDBACK INTEGRATED IN DECISION-MAKING PROCESS Stakeholders are involved at different points of the investment cycle and their feedback is integrated into investment decisions and evaluation.

Table 0.1. **Summary assessment: OECD Recommendation on Effective Public Investment across Levels of Government** (*continued*)

PRINCIPLE 6:	
To mobilise private sector financing without compromising long-term financial sustainability of subnational public investment projects	SUBNATIONAL GOVERNMENTS HAVE ACCESS TO TECHNICAL ASSISTANCE FOR PUBLIC-PRIVATE PARTNERSHIPS Subnational governments have access to and use technical assistance for public-private partnerships (e.g. via PPP units, formal training, good practice guidance). USE OF QUANTIFIABLE INDICATORS The amount of private financing per unit (e.g. EUR, USD) of public investment is known. ACCESS TO INFORMATION Subnational governments have access to information concerning (supra) national funds for investment.
To tap traditional and innovative financing mechanisms for subnational public investment	USE OF INNOVATIVE FINANCING INSTRUMENTS The use of new, innovative financing instruments at subnational levels is accompanied by assessment of their benefits, risks and subnational capacities to employ them.
PRINCIPLE 7:	
To develop institutional capacity and professional skills	SPECIFIC FOCUS ON INVESTMENT REQUIRED SKILLS Human resource management policies demonstrate attention to the professional skills of staff involved in public investment (e.g. hiring is targeted, needs assessments are made, appropriate training is available and used). DEDICATED FINANCIAL ASSISTANCE Dedicated financial assistance is made available for technical training of civil servants involved with public investment; training utilisation rates. TECHNICAL GUIDANCE Technical guidance documents are available for actors at all levels of government to clarify approaches to planning, implementation and evaluation of public investment.
To identify binding capacity constraints and the proper sequence of reforms	ASSESSMENT OF BINDING CAPACITY CONSTRAINTS Specific assessments are conducted to assess binding constraints for effective public investment and identify the needs and the proper sequence of reforms.
PRINCIPLE 8:	
To design and use monitoring indicator systems with realistic, performance promoting targets	PERFORMANCE MONITORING IN PLACE A performance monitoring system is used to monitor public investment implementation. TIMELY REPORTING The monitoring systems facilitate credible and timely reporting of expenditure and performance. OUTPUTS AND OUTCOMES The indicator system incorporates output and outcome (results) indicators. TARGETS Part of the indicators are associated with measurable targets.
To use monitoring and evaluation information to enhance decision making	PERFORMANCE MONITORING INFORMATION IS USED IN DECISION MAKING Performance information contributes to inform decision making at different stages of the investment cycle.
To conduct regular and rigorous *ex post* evaluation	*EX POST* EVALUATIONS *Ex post* evaluations are regularly conducted. Some *ex post* evaluations are conducted by independent bodies (e.g. research organisations, universities, consultancies). Clear guidance documents exist that detail *ex post* evaluation standards.

Table 0.1. **Summary assessment: OECD Recommendation on Effective Public Investment across Levels of Government** (*continued*)

PRINCIPLE 9:	
To define appropriate intergovernmental fiscal arrangements that help align objectives across levels of government	CLEAR FISCAL FRAMEWORK The intergovernmental fiscal framework is clear, with timely indications of transfers between levels of government. PREDICTABLE CAPITAL TRANSFERS Subnational governments are aware of capital transfers from the central government a few months before the start of each fiscal year. MINIMAL VARIANCE There is minimal variance between estimated and actual transfers. PUBLIC INFORMATION Information is made publicly available on the fiscal situation of subnational governments and their comparison.
PRINCIPLE 10:	
To ensure budget transparency at all levels of government	BUDGET TRANSPARENCY Budget transparency principles apply at all levels of government. TIMELY INFORMATION There is budgetary information regarding public investment is publicly available to stakeholders at all levels of government in a timely and user friendly format. MAINTENENCE COSTS INTEGRATED INTO BUDGETING Operations and maintenance costs of infrastructure investment are assessed and integrated into budgeting and planning decisions.
To ensure subnational and national fiscal stability	BUDGET CO-ORDINATION ACROSS LEVELS OF GOVERNMENT Budgetary co-ordination across government in terms of contributions to national fiscal targets. SUBNATIONAL GOVERNMENT BORROWING There are limits on subnational governments' borrowing.
PRINCIPLE 11:	
To engage in transparent, competitive, procurement processes	COMPETITIVE PROCUREMENT The share of public tenders for public investment that are competitively awarded is known and publicly available. The participation rates for tenders are known. Procurement information from the full procurement cycle is publicly available at the national and subnational levels of government. Procurement review and remedy mechanisms are in place at the national and subnational levels.
To encourage procurement at the relevant scale	STRATEGIC PROCUREMENT The share of procurement which involves more than one subnational government is known.
To promote strategic use of procurement	Procurement is used strategically by subnational governments to achieve green objectives. Procurement is used strategically by subnational governments to achieve innovation objectives.
To foster subnational capacity building for procurement	SUBNATIONAL CAPACITIES FOR PROCUREMENT There is recognition of procurement officials as a specific profession. Formal guidance regarding procurement procedures is provided to subnational governments. There is a procurement unit that can assist subnational governments. The percentage of total annual contracts awarded to small and medium-sized enterprises in subnational procurement is known. The percentage of national/subnational procurement conducted online is known.

Table 0.1. **Summary assessment: OECD Recommendation on Effective Public Investment across Levels of Government** (*continued*)

PRINCIPLE 12:		
To engage in "better regulation" at subnational levels, with coherence across levels of government	REGULATORY CO-ORDINATION ACROSS LEVELS OF GOVERNMENT Formal co-ordination mechanisms between levels of government that impose specific obligations in relation to regulatory practice.	
	REGULATORY IMPACT ASSESSMENT Regulatory impact analysis (RIA) are used. A methodology for assessing the quality of RIA exists and indications of quality are available.	
	REDUCTION OF STOCK OF REGULATION Efforts to reduce the stock of regulation or simplify administrative procedures in relation to public investment are made.	
	PUBLIC CONSULTATIONS Public consultations are conducted in connection with the preparation of new regulations of sufficient duration, accessible and appropriately targeted.	
	USE OF E-GOVERNMENT TOOLS E-government tools are used to simplify administrative procedures for public investment projects.	

Source: Indicators selected for the implementation of the OECD *Recommendation of the Council on Effective Public Investment across Levels of Government*, www.oecd.org/effective-public-investment-toolkit, table of self-assessment completed by the Department of National Planning (2016) in co-ordination with the OECD.

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Chapter 1.

Sustaining increased public investment in Colombia

Colombia has made major economic and social progress in recent years. The improved macroeconomic and fiscal conditions have created an environment favourable to both private and public investment. Contrary to the trend in most OECD countries, public investment has increased quite substantially in Colombia, in particular since 2010. It has been driven both by central and subnational governments. This first chapter provides a picture of the trends in public investment at the national and subnational levels in Colombia and the challenges linked to regional disparities. Chapters 2, 3 and 4 will further explore how to find new sources of funding for investment and how to strengthen the governance of the system.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Introduction

Colombia has made major economic and social progress in recent years. A solid monetary, fiscal and financial framework reduced macroeconomic volatility, which had characterised the previous decades (OECD, 2015d). This has contributed to a high level of growth and decline of poverty from 49% to 28% at the national level from 2002 to 2014. The improved macroeconomic and fiscal conditions have created an environment favourable to both private and public investment. Foreign direct investment (FDI) has sharply increased and the government has put procedures in place to identify and remove unnecessary barriers to FDI. Public investment has also increased quite substantially, in particular since 2010, contrary to the trend in most OECD countries. It has been driven not only by the central government, but also by subnational governments, which have been playing an increasing role in investment since the 2012 royalties reform. Colombia has also improved the conditions in favour of private sector participation in infrastructure and launched a fourth generation programme of public-private partnerships (PPPs).

The increase in public and infrastructure investment should be sustained over the longer term, given the huge infrastructure needs in Colombia, which vary greatly across territories. Colombia lags behind other Latin American countries and most OECD countries in terms of quantity and quality of infrastructure. This infrastructure gap has a strong territorial dimension: many regions, in particular rural, lack access to transport infrastructure, education and housing. Colombia has a very high level of territorial disparities across regions, but also within urban areas. Colombia needs to sustain and further support its public investment effort to respond to huge infrastructure gaps and territorial disparities, as the level of investment per capita remains below the level of all OECD countries.

Additional and stable sources of funding need to be found, in a context of volatile – and currently declining – royalties. In addition, Colombian public actors also need to make the most of existing sources of investment. Given that subnational actors are playing an increasing role, improving the governance of public investment across levels of government could be translated into substantial savings and productivity gains. This chapter will focus on highlighting recent trends in public investment at the national and subnational levels in comparative perspectives.

Strong economic performance with high levels of investment

Macroeconomic and fiscal conditions favourable to investment

Colombia has become the fourth largest economy of Latin America in terms of gross domestic product (GDP). A solid monetary, fiscal and financial framework reduced macroeconomic volatility, which had characterised the previous decades. This has been accompanied by low inflation, declining public debt and a reduction in poverty rates. Colombia's GDP has been growing at an average annual growth rate of 4.7% over the last ten years (OECD and DANE) and recovered quickly from the 2008 global financial crisis. Recent strong growth was driven by an oil and mining boom (OECD, 2014b; 2015d). Economic growth has generated new job opportunities, and the unemployment rate has declined to 8.8% (June 2016). Poverty has declined substantially and the share of middle-income households has expanded dramatically over the last decade (OECD, 2015e).

Fiscal stability has been considerably strengthened since the early 2000s thanks to strict fiscal rules to control the budget balance and debt. In 2011, fiscal sustainability was included in the Constitution as a key guideline for public policy (OECD, 2015d). Furthermore, a fiscal rule that targets the central government's budget balance, adjusted for cyclical factors and oil and mining prices, was put in place in 2011 (OECD, 2015d). The law establishes annual targets, such that the adjusted budget deficit will gradually decrease from around 2.3% of GDP in 2014 to 1% by 2022. Furthermore, the law also created a savings and stabilisation fund (OECD, 2015d). The net central government debt is projected to fall from 36% of GDP currently to 26% by 2025. Such a low debt level is justified by Colombia's strong dependence on potentially volatile resource revenues and its exposure as an emerging market economy to global financial shocks.[1] In addition, a solid framework to ensure subnational fiscal sustainability was developed, after problems of over-borrowing and excessive expenditure growth during the 1990s (see Chapter 2). This has contributed to considerably strengthen subnational fiscal stability.

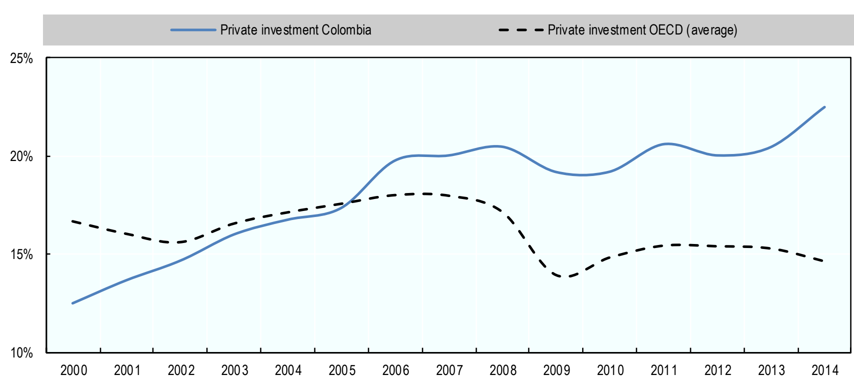
Overall, the framework conditions for investment – private and public – have considerably improved over the past decade, including from a regulatory and procurement perspective. Colombia has reinforced transparency in fiscal management at all levels of government and restored fiscal stability in the 2000s, following the fiscal crisis of the 1990s. Control and auditing processes have been strengthened, as well as the procurement framework, contributing to reduce corruption. These improved framework conditions have contributed to restore trust for private investors and financial markets.

Colombia has also considerably improved the security situation.[2] Today, even if security challenges remain higher than in a majority of OECD countries, only a small portion of the country remains under potential threat from terrorist groups or organised criminal bands. These security challenges have a strong place-based dimension and are concentrated in specific regions – particularly those hit by the conflict. Colombia has just signed a major peace agreement in August 2016 and a final referendum on the peace process is planned in October 2016. The conclusion of the peace talks could boost confidence, promoting investment and job creation.

High levels of private investment and foreign direct investment

Private investment has increased over the past decade and has continued increasing even after the 2008 global crisis, whereas it was decreasing at the same time in most OECD countries (Figure 1.1). Private investment as a percentage of GDP has risen, from 12.5% to 22.5% from 2000 to 2014. Foreign direct investment (FDI) flows, which have also benefited from the commodity price boom, have increased substantially in recent years. Colombia is one of the largest FDI beneficiaries in Latin America, according to the World Bank's Doing Business report. FDI is rather concentrated in the oil and mining sectors but an increased diversification has been observed in recent years (Box 1.1). The government has put procedures in place to identify and remove unnecessary barriers to investment.

Figure 1.1. **Investment trend as a percentage of GDP, Colombia and OECD average**



Note: Private investment: measured by investment by enterprises and households in the National Accounts. No data were available for Australia, Chile, Canada, Greece, Luxembourg and Turkey for calculating the OECD average.

Source: Authors' calculations based on OECD National Accounts.

Box 1.1. **Foreign direct investment in Colombia**

Foreign direct investment (FDI) increased to USD 4 568 million in the first quarter of 2016. The two main destinations of FDI are the hydrocarbon (the oil sector accounted for 30% of FDI in 2014) and mining sectors (10% of FDI in 2014), but an increasing degree of diversification has been observed in recent years, in particular in telecommunications and tourism. The United States is the most important investor in Colombia, followed by Panama and Spain (OECD, 2012). Colombia's investment promotion agency, Proexport, has established a "System to Facilitate and Attract Investment" (SIFAI), which provides details on the impact of barriers to investment in terms of the amount of investment, job creation, etc.

Since the mid-2000s, Colombia has improved its regulatory environment by strengthening its policies and institutions, with the aim of increasing productivity, accelerating economic growth and promoting competitiveness (World Bank, 2013). More than 60 regulatory reforms were conducted, dealing with construction permits, registering property, starting a business and taxes (World Bank, 2013).

Source: Procolombia (2016), www.investincolombia.com; OECD (2012), *OECD Investment Policy Reviews: Colombia 2012*, http://dx.doi.org/10.1787/9789264167742-en; World Bank (2013), *Doing Business 2013: Smarter Regulations for Small and Medium-Size Enterprises*, www.doingbusiness.org/reports/global-reports/Doing%20Business%202013.

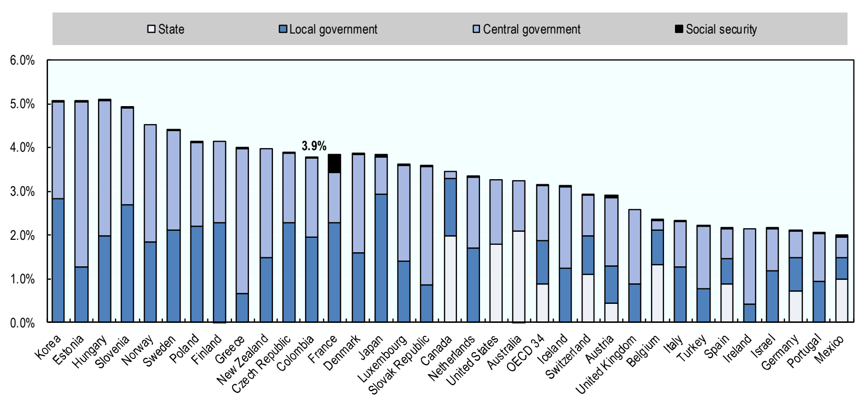
Rather than simply increasing the amount of FDI, the government's objective is to enhance the qualitative role of FDI in the country's development, notably its contribution to job creation and infrastructure improvement (OECD, 2012). The government has taken measures to ensure that key investment principles, such as transparency and procedural fairness, apply to investors bidding for infrastructure contracts.

Public investment has increased substantially in relation to GDP

Public investment[3] has increased in Colombia, from 2.4% of GDP in 2000 to 3.9% in 2014. Colombia experienced only a small dip in public investment between 2009 and 2010; since then it has experienced the steepest increases since the early 2000s. The negative gap in public investment between Colombia and OECD countries decreased over time and turned positive in the aftermath of the financial crisis. Colombia invests 3.9% of GDP, above the OECD average of 3.5%. The public share of total investment is about 13.8%, which is close to the OECD average. By spending almost 4% of GDP on public investment, Colombia places close to the upper half of OECD countries, close to countries like Canada, Japan or New Zealand. Korea, with 5.5% of GDP spent on investment, is the country that invests the most in the OECD area. The increase in investment was driven both by the central government and by subnational governments.

At the central government level, investments in transport and housing have been keen priorities over the past few years, notably due to an expansion of public housing programmes. The national investment budget steadily increased, from 2010 to 2015 (COP 21.5 trillion to COP 46 trillion) (DNP, 2016). The 2014-2018 National Development Plan (NDP), which sets out national investment for the President's term, has placed territorial and infrastructure investment at the top of Colombia's policy agenda. The Multi-year Investment Plan for 2014-18 projected in the National Development Plan represents close to 330 USD billion (slightly higher than 100% of GDP in 2014). Investments planned in the NDP have increased from COP 629 billion in 2010-14 to COP 704 billion in 2014-18. Two-thirds of this is supposed to be financed from public resources and 34% from private investment.

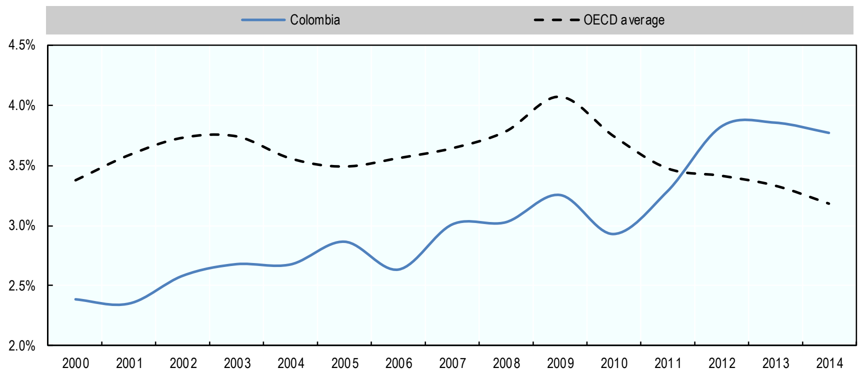
Figure 1.2. **Public investment as a share of GDP in OECD countries and Colombia, 2014**



Sources: Authors' elaboration based on OECD (2016a), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; OECD (2016d), authors' calculations for Colombia based on OECD National Accounts.

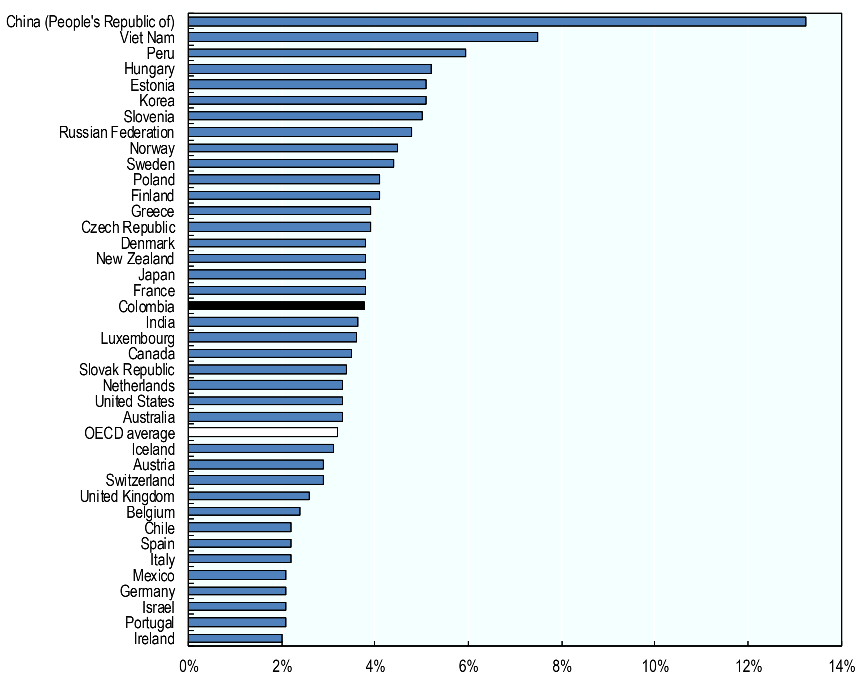
This level of public investment remains, however, lower than many other countries (Figure 1.3). In many emerging markets, public investment rates peaked at over 8% of GDP in the late 1970s/early 1980s, declined to around 4-5% of GDP in the mid-2000s, but have since recovered to 6-7% of GDP (IMF, 2015).

Figure 1.3. **Public investment as a share of GDP over time: Colombia vs. the OECD average**



Source: Authors' elaboration based on OECD (2016a), OECD national Accounts.

Figure 1.4. **Public investment as a share of GDP, 2014**

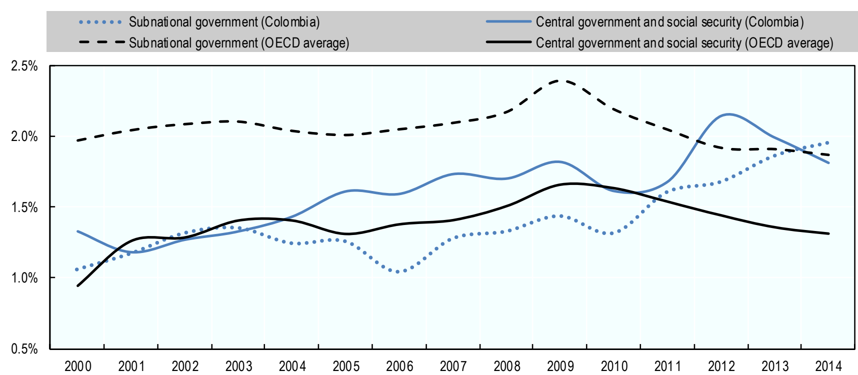


Source: Authors' elaboration based on OECD (2016a) and on OECD (2016d).

An increasing role for investment for subnational governments

Subnational governments' role in public expenditures has increased since the decentralisation reforms (see Chapter 2). From 2000 to 2013, subnational capital expenditure increased from 1% of GDP to 1.7% of GDP. On a yearly basis, subnational investment has been slightly more volatile at the subnational level compared to the national level. Overall, however, subnational investment has been increasing as a proportion of GDP, with the increase being more marked after 2010. The royalties reform of 2012 has given substantial resources to subnational governments for investment. The share of subnational government investment in total public investment has increased from 44% to 51.9% over the last 14 years. This share remains below the OECD average of 59% (see Chapter 2).

Figure 1.5. **Public investment in Colombia as a share of GDP**



Source: Authors' elaboration based on OECD (2016a), OECD National Accounts.

A new generation of public-private partnerships

The government has launched several reforms to encourage private investment in infrastructure to address the huge investment needs in this field. In the early 2010s, private sector participation in infrastructure remained low compared to other emerging economies, including in Latin America (OECD, 2012).

Colombia has strengthened its framework conditions for public-private partnerships (PPP). There has been a concerted effort in recent years to develop favourable frameworks, through the "Vigencias Futuras" scheme (availability payments) and the first PPP framework created in 1993. This framework was reformed in January 2012 to adopt a clearer and more stable regulatory framework for PPP, called "Asociaciones Público Privadas"

(APP), inspired from the UK system of private finance initiatives (PFI).[4] The 2012 law improves bidding mechanisms, levels the playing field for participating companies, and seeks to increase transparency and objectivity. It allows the implementation of unsolicited proposals for PPP projects (PPP Knowledge Lab). The public-private partnership legislation also puts an emphasis on value-for-money analysis in choosing the contractual form for executing projects.

The recent creation of a Vice-Ministry of Infrastructure and a National Infrastructure Agency should increase administrative and technical capacities to strengthen the overall investment project cycle (OECD, 2015d). The National Infrastructure Agency created in 2012 now replaces the former National Institute of Concessions to improve the country's PPP fourth generation programmes.[5] New legislation has also recently been approved to streamline the land acquisition process, which will also support infrastructure investment (OECD, forthcoming).

The government has launched a new generation of public-private infrastructure programme (fourth generation, so-called 4G) on road concessions. Over the next eight years, the new programme 4G is expected to deliver 5 892 kilometres of roads in three waves via public-private partnerships, requiring an investment of COP 10.7 billion (Bell and Schipani, 2015). The target mentioned by the government in the 2014-2018 National Development Plan is to build 7 000 kilometres of roads for the 2016-20 period and reduce travel times by 30% and transport costs by 20%. Most PPPs are for large projects financed by the central government, but subnational governments have the possibility to contract PPPs as well (see Chapter 4). In April 2016, the government held its first concession as a part of its highway plan.

Pension funds also have played a stronger role in recent years in financing infrastructure investment. The move was modelled after that of Chile, where pension funds have played a key role in infrastructure development (Glickhouse, 2014).

Sustaining high levels of public investment in the coming years is critical

Huge infrastructure and investment needs

Colombia has huge infrastructure gaps, in particular in transport, but also in housing, water or ICT, that need to be addressed. Colombia lags behind other Latin American countries and most OECD countries in terms of the quantity and quality of its infrastructure. This infrastructure gap is a product not only of the country's mountainous topography but also of its violent past: the security situation both lowered the demand for inter-urban transport networks and increased the cost of infrastructure provision (OECD, 2014a). The infrastructure gap is one of the biggest growth obstacles for the Colombian economy (S&P, 2014).

Colombia exhibits a larger transport infrastructure gap than other emerging and developed economies, and costs of internal freight transport rank among the highest in the world. According to the World Economic Forum’s 2013-2014 Global Competitiveness Index, out of 148 countries, Colombia ranks 130th in quality of roads, 110th in port infrastructure and 96th in airport infrastructure. On the quality of overall infrastructure, Colombia falls below all of the countries that it borders except for Venezuela. High transportation costs compared to other Latin American countries due to weak infrastructure and poor logistics are significant impediments to growth (OECD, 2015d). Despite improvements in easing regulations, exporting a container still costs more than twice as much in Colombia as in OECD countries, mainly because of domestic transport costs (World Bank, 2013). Of all of the countries that have free-trade agreements with the United States, Colombia has the highest export costs. Reducing transport and logistics costs would therefore allow diversifying the economy by significantly raising the competitiveness of many tradable goods (OECD, 2015d).

Colombia has important spending needs and previous levels of investment from the early 2010s were not sufficient to close its infrastructure gap, in particular in transportation and energy (Clavijo, Vera and Vera, 2013). In addition, the maintenance of existing infrastructure also requires significant investment. One assessment estimated, for example, that current road conditions require around 50% of road investments to be spent on maintenance (Ang and Marchal, 2013).

Strong territorial heterogeneity and different investment needs

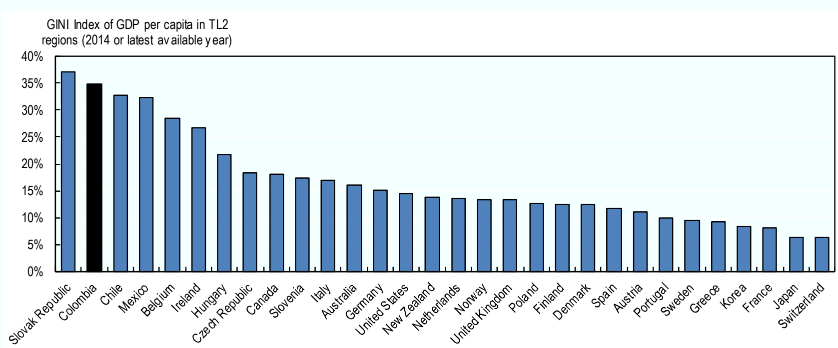
The infrastructure gap has an important territorial dimension: Colombia has large territorial disparities (Figure 1.6), in particular across urban and rural areas. Rural communities suffer disproportionately from poor access to infrastructure and poor service delivery. Many rural areas, in particular in border regions, have been affected by the presence of guerrilla groups and drug traffic, social unrest, and lack of basic public institutions for decades. These regions remain isolated and disconnected from urban areas. The most important gaps between urban and rural areas concern access to transport infrastructure, education and housing. For example, two-thirds of the rural population lacks ready access to the road network. In most rural areas there are too few secondary and tertiary roads and their quality is poor. Besides, the majority of the rural working-age population (61%) has either not attended school or not completed primary school.

Colombia has made significant progress to reduce territorial disparities over the past few years, but challenges remain very high. While absolute income poverty fell between 2002 and 2014 from 49% to 28% at the national level, and from 45% to 30% among urban households, it continued to affect 41% of rural households in 2014 (from 62% in 2002). Extreme income poverty has also decreased substantially since the early 2000s, but it remains more than three times higher in rural areas than in urban ones (18% of households in rural areas compared to 4.9% in urban ones). A recent study finds that it would take the department of Choco 200 years to converge to Bogota's income per capita levels (Galvis and Meisel, 2012).

Box 1.2. **Territorial disparities in Colombia**

Data are lacking in Colombia to compare small territorial units (TL3) with OECD countries in terms of territorial disparities. In comparison with OECD countries, Colombia has among the highest level of territorial disparity in GDP per capita at the regional (department) level, similar to the Slovak Republic, Chile and Mexico. Income disparities are large within Colombian departments. Colombia has witnessed a decade of strong economic performance, but growth opportunities have not occurred everywhere. They have been driven by metropolitan areas and resource-rich departments (coffee, energy and mining), whereas poorly connected rural areas display a low performance in terms of growth (OECD, 2014b). Overall, the conflict had a major impact on territorial development in the country, the widening rural-urban gap and internal displacements of population.

Figure 1.6. **Gini Index of territorial disparities in GDP per capita (TL2 level), 2014 (or latest available year)**



Source: OECD (2016e), *OECD Regional Database.*

Due to the lack of transport infrastructure, the functional area of each urban hub tends to be relatively small and isolated from the others (OECD, 2014b). In this sense, each functional urban area resembles an island surrounded by sparsely populated rural areas. Settlement patterns in Colombia display an archipelago of urban regions surrounded by (often) poorly connected rural areas, due to the high concentration of economic activity and scarce road network. Disparities in access to infrastructure and public services are also very high within urban areas. Addressing infrastructure gaps and overall investment needs in a strategic manner could contribute to reducing regional disparities, better connecting rural areas to cities and better connecting cities among themselves.

The approach to investment thus requires a strong place-based dimension, to reflect the different territorial needs and adopt investment mixes that respond differently to challenges in metropolitan areas and lagging remote regions, and promote urban-rural linkages. Public investment choices should be linked to a development strategy based on an assessment of the potential opportunities for and impediments to growth in each region (or locality), as recommended by the OECD *Recommendation of the Council on Effective Public Investment*. In addition, there is a common need for mutually reinforcing impacts in the form of policy complementarities among sectoral strategies to make the most of a public investment. Infrastructure alone has little impact on regional growth unless regions are endowed with adequate levels of human capital and innovation (OECD, 2009). A combination of investments in both "hard" and "soft" infrastructure are therefore needed to maximise potential for long-term growth (OECD, 2011; Garcilazo and Oliveira Martins, 2013). In Colombia, infrastructure and improved connectivity can help lagging regions converge and improve their performance as long as other key growth factors, particularly human capital, are also improved. The different investment priorities need to be articulated in coherent territorial strategies.

Colombia has strongly enhanced the territorial approach to its national investment in the 2014-2018 National Development Plan. Closing social and economic gaps across regions is the main goal of the National Development Plan. It includes for the first time a specific part with a regional structure, for the territorial planning of the six macro-regions of Colombia. Approaches to rural and urban development are also more comprehensive and bridging the rural-urban gap is seen as one of the most important development challenges for Colombia. The plan also introduces a new "closing gaps" approach to better measure and fight regional disparities. At the subnational level, major efforts have also been made to improve the preparation of the territorial development plans for the 2016-19 period. The most important challenges now are to better link these planning exercises to effective budgeting and implementation. Chapter 3 will address this issue in depth.

The level of public investment needs to be sustained for a sufficiently long period in order to raise productivity levels and GDP per capita

Sustaining high levels of public investment is critical in Colombia to address huge infrastructure and investment needs and promote a more balanced development for the country. PPPs are useful to finance large-scale or complex infrastructure projects, but cannot substitute for public investment efforts, in particular to address needs in remote regions. PPPs can only be a useful, but partial, response to investment needs. In most OECD countries, PPPs account for less than 10%, or even 5%, of overall infrastructure investment (Burger and Hawkesworth, 2013).

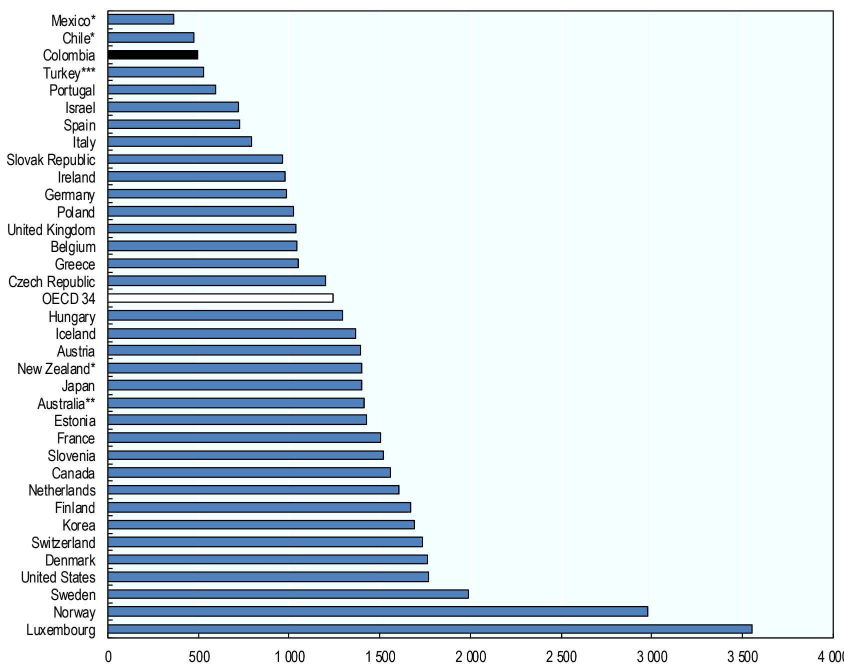
Although public investment has considerably increased in Colombia when measured as a proportion of GDP, the pace of capital accumulation (measured by investment to GDP) needs to continue for a sufficiently long period in order to raise productivity levels and GDP per capita. When measured per capita, the level of public investment in Colombia is lower than in most OECD countries, except Chile and Mexico. This is expected, as Colombia has a level of GDP per capita which is below OECD countries. However generally, Latin-American countries and South-European countries tend to have lower absolute amounts of public investment, compared to other OECD countries. According to the IDB, the level of public investment in Colombia could rise to 8% of GDP to reach adequate levels (IDB, 2013).

Like other countries which are in a rapid catching up process, the challenge for Colombia is to sustain its level of public investment over the longer term, to avoid being caught in a middle-income trap and to address its huge infrastructure needs. Investment in infrastructure in a variety of sectors (transport, health, education, housing, economic development) is needed to diversify the economy away from commodities, boost productivity, and move up the value chain to make economic growth more sustainable and achieve convergence with OECD countries in per capita income.

Challenges both on the financing and governance sides

New challenges are emerging to sustain the financing of public investment, mainly linked to the decline in royalties revenues – one of the main sources of investment funding at the subnational level. The main engine of growth in the past decade, the boom in commodity prices, has lost steam and falling oil prices undermine public revenues for royalties. Given the inverse relationship between oil prices and the exchange rate, the effect of lower oil prices has been partially offset by a greater depreciation of the peso. Colombia is adjusting to the large terms of trade shock better than other commodity exporting economies in the region (OECD, 2017 forthcoming). However, lower oil revenues and the fact that oil reserves are estimated to last another six to ten years (OECD, forthcoming) put strong pressures on the long-term financing of public investment. Beyond the question of financing investment, the fall in oil and coal prices requires investment outside the natural-resource sector to sustain long-term growth and create formal jobs[6] (OECD, 2015d).

Figure 1.7. **Level of public investment per capita, Colombia and OECD countries, 2014**



Notes: * 2013; ** 2012; *** 2011. Data were not available for Iceland, Luxemburg and New Zealand.

Source: Authors' elaboration based on OECD (2016a), OECD National Accounts.

In this context, it is critical for Colombia to find new sources of funding for investment and to make the most of the untapped potential of subnational governments for investment, to address the different territorial needs and sustain inclusive development in the country. In particular, Colombia should further support subnational governments in their capacity to finance and plan investment in a more strategic manner. This is a top priority given the increasing role that subnational governments play in the country for public investment. Overall, Colombia needs to address its public investment framework in a more systemic way and to reduce the overall fragmentation of the system, to enhance synergies among funding sources at the subnational level and limit co-ordination costs. Improved governance also implies a better connection between planning and budgeting to help prioritise investment needs on a multiannual basis. These issues are analysed in greater depth in Chapters 2, 3 and 4. Chapter 2 focuses on the need to diversify sources of financing at the subnational level, while Chapters 3 and 4 focus on the changes needed on the governance side.

Recommendations

- Sustaining high levels of public investment is critical in Colombia to address huge infrastructure and investment needs and promote a more balanced development of the country. Even if public investment in relation to GDP has increased substantially in recent years, the pace of capital accumulation (measured by investment to GDP) needs to continue for a sufficiently long period in order to raise productivity levels and GDP per capita.
- Like other countries which are in a rapid catching up process, the challenge for Colombia is to sustain its level of public investment over the longer term, to avoid being caught in a middle-income trap and address huge infrastructure needs. Investment in infrastructure in a variety of sectors (transport, health, education, housing, economic development) is needed to diversify the economy away from commodities, boost productivity, and move up the value chain to make economic growth more sustainable and achieve convergence with OECD countries in per capita income
- PPPs are a useful to mobilize to finance large-scale or complex infrastructure projects, but cannot substitute for public investment efforts, in particular to address needs in remote regions. In most OECD countries, PPPs account for less than 10%, or even 5% of overall infrastructure investment (Burger and Hawkesworth, 2013).

- Additional and stable sources of funding need to be found, in particular at the subnational level, in a context of volatile – and currently declining - royalties. Chapter 2 will explore these additional sources of financing in depth.
- Efforts to support financing should be accompanied by efforts to adopt a more systemic approach to the governance of public investment, to reduce the overall fragmentation of the system, as many systems coexist with little connection among them. In particular, Colombia should further support subnational governments in their capacity to finance and plan investment in a more strategic manner. Chapters 3 and 4 will further explore how to strengthen the governance of the system.

Notes

1. Indeed, emerging market economies have been excluded from international capital markets in the past during periods of international capital market turmoil. Moreover, Colombia still has higher debt levels than similar emerging market economies, such as Chile or Peru, which enjoy better ratings and lower financing costs (OECD, 2015d).
2. The number of guerrilla members has significantly declined in the past few years. The homicide rate has declined, from almost 69 homicides per 100 000 population in 2002 to 33 in 2010, and 23 in 2014.
3. The National Accounts definition of public investment is used for comparative purposes.
4. Only projects over 6 000 times the current minimum legal monthly wage (almost USD 2 billion) are eligible for a PPP scheme. Concessions can now only last up to 30 years including extensions. The funding of a PPP project can be wholly private or a mixture of private and public but the law makes the differentiation between projects originated by a public entity and those originated by a private partner. For this category, funding can be 100% private or with public participation (central government, departments and municipalities, other decentralised entities or public fund, e.g. royalties). In that case, the public funds cannot exceed 20% of the total investment of the project. In public initiative PPP projects or private initiatives with public funding, a public bidding will be required.

5. The new PPPs developed are instruments that engage private capital in the design, construction, operation and maintenance of infrastructure projects, including their associated services. PPP contracts must include the allocation of risks between the parties and payment mechanisms subject to the adequate service levels of the infrastructure.

6. Colombia needs to move up the value chain to make economic growth more sustainable and achieve convergence with OECD countries in per capita income (OECD, 2015a).

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Chapter 2.

Financing subnational investment in Colombia

Subnational governments have been playing an increasing role in public investment since the decentralisation and royalties reforms. Colombia has significantly improved its overall framework conditions for public investment over the past two decades. Jointly with these efforts to strengthen fiscal stability, Colombia has made significant efforts to promote the allocation of national resources for investment in a more inclusive way. However, challenges linked to fiscal disparities across territories remain high. In addition, because of constraints on revenue, subnational governments have little autonomy regarding how and where to invest. This chapter focuses on the financing system for subnational investment and ways to strengthen it. It is thus particularly connected to the third pillar of the OECD Recommendation of the Council on Effective Public Investment.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Introduction

Subnational governments have been playing an increasing role for public investment since the decentralisation and royalties reforms. Subnational investment as share of gross domestic product (GDP) increased from 1.1% in 2000 to 2% in 2014 while GDP rose sharply at the same time. In 2000, investment accounted for 10% of subnational spending; in 2013 it amounted to 15%. Subnational governments in Colombia are now key public investors, representing almost half of overall public investment.

Colombia has improved its overall framework conditions for public investment over the past two decades. Jointly with these efforts to strengthen fiscal stability, Colombia has made significant efforts to promote the allocation of national resources for investment in a more inclusive way, notably though the 2012 royalties reform. Although this reform has helped better equalise public resources across the national territory, challenges linked to fiscal disparities across territories remain very high.

This chapter will focus on the financing system for subnational investment and ways to strengthen it. It is thus particularly connected to the third pillar of the *OECD Recommendation of the Council on Effective Public Investment* (Principles 9 and 10). The main priorities for Colombia in the coming years are to maintain fiscal stability as a key objective in a context of greater fiscal risks, while at the same time strengthening the capacity of subnational governments to raise additional revenues to fund investment, and reducing the fragmentation of the governance of public investment, as many systems coexist with little co-ordination among them.

Increased decentralisation, but limited subnational spending autonomy

The most decentralised unitary country in Latin America

Over the past three decades, and especially since 2010, Colombia has increased decentralisation to become the most decentralised unitary country in Latin America. The Colombian decentralisation process essentially started in 1986 with Law No. 1 on the election of mayors by universal suffrage and was strengthened in the 1991 Constitution which enshrined the departments and municipalities. In the 32 departments and 1 101 municipalities, the executive power is in the hands of a governor and a mayor, both elected by popular vote, giving them a high legitimacy but for a four-year term which is not immediately renewable. A departmental assembly and a municipal council are also elected by popular vote every four years.

Box 2.1. **Tiers of government in Colombia**

In Colombia, the top tier of government is made up of the 32 departments (*departamentos*), headed by a popularly elected governor and an assembly, as well as the Capital District of Bogota, which has its own status giving the city similar power to those of departments. The capital, Bogota, is the country's largest and most populous city with 7.8 million inhabitants in 2014 (16% of the Colombian population) and 9.5 million inhabitants in the metropolitan area (DANE). It constitutes approximately 24.5% of the national GDP.

The second tier is made up of 1 101 municipalities (*municipios*) headed by a popularly elected mayor and council. Among the 1 101 municipalities, not including Bogota, 5 are categorised as special districts (*distritos especiales*) due to their particular political, commercial, historical, industrial, cultural or environmental characteristics, among other important factors: Barranquilla, Buenaventura, Cartagena de Indias and Santa Marta. They have a municipal status with certain prerogatives as specified in their new regime as of 2013 (Law 617 adopted in 2013).

The Colombian Constitution and following regulations establish competences and responsibilities for the national government, the departments and Bogota (Laws 715/2001 and 1176/2007), and the municipalities and districts (Law 136/1994). However, the limits between the national and subnational levels, and even more so between departments and municipalities, remain somewhat unclear (OECD, 2014b). There is a dual system of decentralised and delegated responsibilities and the majority of competences are shared between all levels of government (education, health, water and sewerage, housing). Basically, the government creates national development policies. Municipalities are supposed to organise and provide basic services, and the departments serve as intermediaries between the other levels and are in charge of planning, while also supporting the provision of basic services (notably health and education) (OECD, 2014b).

- The national government is responsible for formulating development goals and policies, supervising and monitoring compliance with these policies and implementation of public resources and the supply of basic services, providing large-scale services such as justice and security/public order, carrying out projects of national interest, managing the national economy, and directing international relations.
- Municipalities have a broad scope of competences. They provide delegated competences in the areas of education, health, water and sanitation when they are classified as "certified". In addition, they are responsible for territorial planning; local infrastructure; solid waste

management; housing; sports, culture and leisure; and the promotion of social, economic and environmental development.

- Most of these competences are shared with departments, which set orientations (within the national framework), co-ordinate, supervise and give financial, administrative and technical assistance to the municipalities, in some case substituting them (uncertified municipalities for education or water for instance). Departments also have a role of co-ordination and intermediation between the central government and municipalities. They also have specific competences such as a health service network for uninsured, low-income population; the management of teaching and administrative personnel in basic primary and secondary education; human rights protection; rural development; risk and disaster management and environmental protection; and traffic management. More broadly speaking, departments are responsible for planning, promoting the economic and social development of their territory, and supervising regional policies when they are beyond the geographical reach of municipalities, which include environmental protection, transport infrastructure and regional territorial planning.

Box 2.2. **Allocation of competencies in OECD (unitary) countries**

There are some similarities across OECD countries for the allocation of responsibilities across levels of government. Municipalities are generally responsible for providing and managing basic community services, while higher tier local governments are responsible for supra-municipal tasks such as health, roads or economic development. “Environmental” responsibilities are very often at the local level (water, waste, roads, urban planning).

Economic development, culture and tourism are often shared among levels of government; and when regional authorities exist, they play an important role. Education and public health are also frequently shared among levels of government.

The co-ordinating role of regions, serving also as an intermediary body between the central and municipal levels is, however, not very widespread in OECD unitary countries (excluding regionalised countries such as Italy or countries having some autonomous regions such as Portugal [Azores, Madeira] or the United Kingdom [Scotland, Northern Ireland, Wales]), where there are often no hierarchical links between upper and lower subnational governments (e.g. in the Czech Republic, Denmark, France, Poland and Sweden, for example).

Box 2.2. **Allocation of competencies in OECD (unitary) countries** (*continued*)

A country which is similar to Colombia is the Netherlands, where the provinces play a key role in vertical co-ordination, bringing together a wide network of formal and informal stakeholders from different levels of government. They also ensure the quality and consistency of public administration by supervising lower levels of government, in particular, by ensuring the financial oversight of municipalities and regional water authorities. Provincial representatives are involved in setting long-term strategies in economic policy and transport and act as intermediaries between the central government and municipalities to implement national priorities (OECD, 2014c).

Figure 2.1. **Breakdown of responsibilities across subnational governments: A general scheme**

Municipal level	Intermediary level	Regional level
*** A wide range of responsibilities:** - General clause of competence - Eventually, additional allocations by the law *** Community services:** - Education (nursery schools, preelementary and primary education) - Urban planning and management - Local utility networks (water, sewage,waste, hygene, etc.) - Local roads and city public transport - Social affairs (support for families and children, elderly, disabled, poverty, social benefits, etc.) - Primary and preventative healthcare - Recreation (sport) and culture - Public order and safety (municipal police, fire brigades) - Local economic development, tourism, trade fairs - Environment (green areas) - Social housing - Administrative and permit services	*** Specialised and more limited responsibilities of supra-municipal interest** *** An important role of assistance towards small municipalities** *** May exercise responsibilities delegated by the regions and central government** *** Responsibilities determined by the functional level and the geographic area:** - Secondary education or specialised education - Supra-municipal social and youth welfare - Secondary hospitals - Waste treatment - Secondary roads and public transport - Environment	*** Heterogeneous and more or less extensive responsibilities depending on countries (in particular, federal vs unitary)** *** Services of regional interest:** - Secondary/higher education and professional training - Spatial planning - Regional economic development and innovation - Health (secondary care and hospitals) - Social affairs, e.g. employment services, training, inclusion, support to special groups, etc. - Regional roads and public transport - Culture, heritage and tourism - Environmental protection - Social housing - Public order and safety (e.g. regional police, civil protection) - Local government supervision (in federal countries)

Source: OECD (2016c), *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en.

Wide-ranging subnational responsibilities but limited spending autonomy

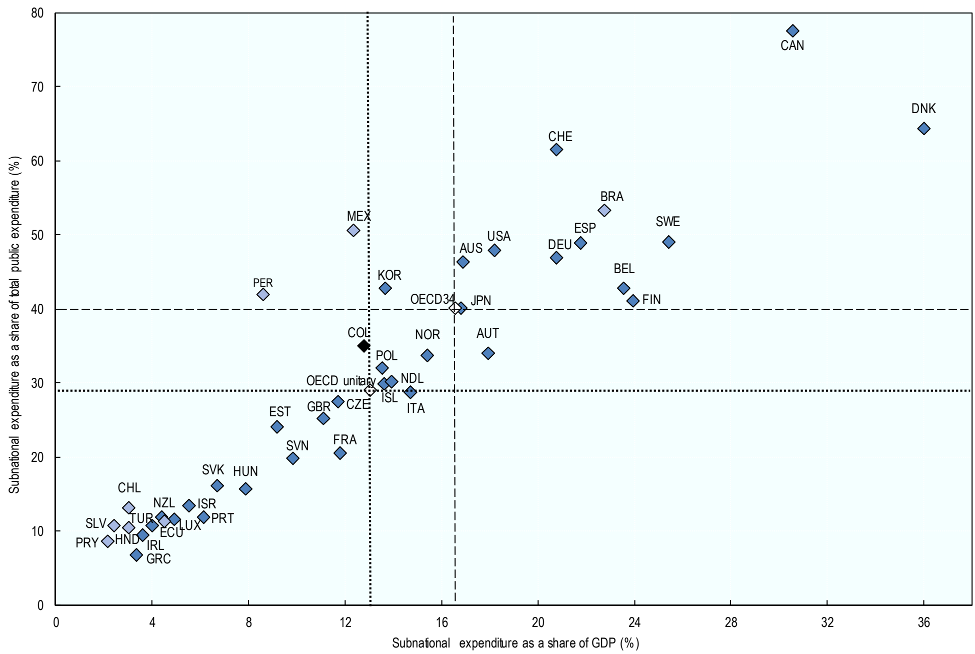
Like in many OECD countries, fiscal decentralisation is imbalanced, with wide-ranging competencies allocated to subnational governments and limited fiscal autonomy. The 1991 reform – and subsequent adjustments – assigned wide-ranging spending responsibilities to departments and municipalities. Although the 2011 Organic Law governing the Territorial Organisation (Ley Orgánica de Ordenamiento Territorial, LOOT) helped clarify the rules for decentralisation, this distribution of competencies across levels of government remains complex.

As a result, subnational government expenditure accounted for 35% of total Colombian general government expenditure in 2013 and 12.8% of GDP while it represented 6.2% of GDP in 1994. Municipalities represent around two-thirds of expenditure and departments one-third. When compared to OECD countries, Colombia has a slightly lower level of fiscal decentralisation – regarding spending – than the OECD averages, which was 40.2% of public expenditure and 16.6% of GDP in 2014. However, if one considers OECD unitary countries only, Colombia stands around the OECD averages, which amounted respectively to 29.1% of public expenditure and 13.0% of GDP in 2014. Colombia is significantly ahead of countries such as Chile, Greece, Ireland, New Zealand and Turkey, where local governments have limited competencies, but is behind more decentralised unitary countries where local governments' involvement in the economy is significant, such as Japan and the Nordic countries (Denmark, Finland and Sweden) (OECD, 2016e). In Latin America, Colombia is, with Peru, among the most decentralised unitary country in terms of the importance of subnational government public spending (Figure 2.2).

However, spending autonomy is largely limited by the fact that subnational governments are constrained by their revenue sources (earmarked transfers, see below). Most expenses are earmarked to three areas, namely education, health, water and sanitation.

Therefore, subnational governments can be considered mainly as a "vehicle" for central government policy with a "payment function" channelling to the territory the central government funds (OECD, 2014b). The Colombian decentralisation process appears to be more a "delegation" model than a "devolution" one which would have supposed transfers of fiscal powers and spending autonomy (Bird, 2012). Unsurprisingly, subnational spending is predominant in the sectors for which expenditure is earmarked. Education is the first budget item (36% of subnational government spending) and health the second (20%). Other important items are general public services (15%), economic affairs and transport (11%), social protection, and housing and community amenities (5% each) (DANE, 2013).

Figure 2.2. **Subnational government expenditure as a percentage of GDP and public expenditure in 2014, OECD and selected Latin American countries**

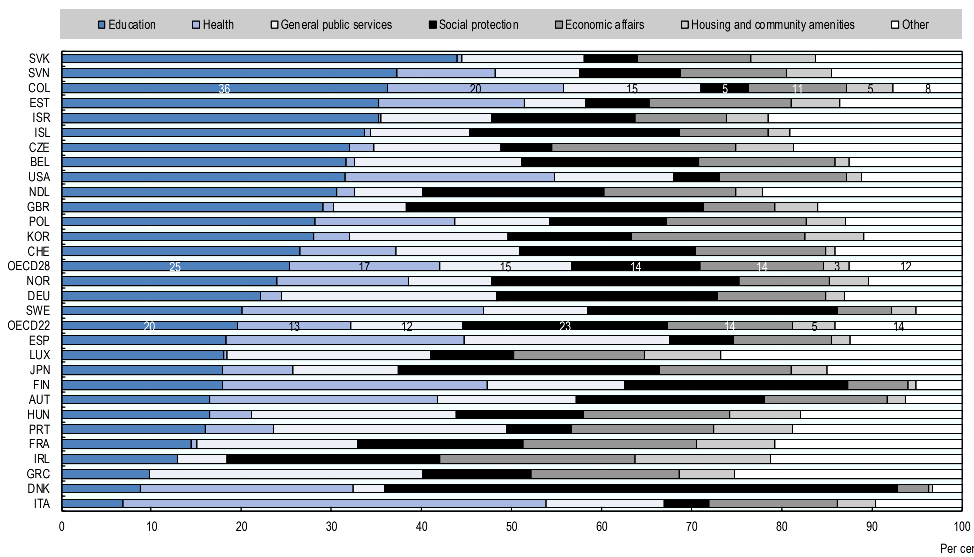


Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Sources: Authors' elaboration based on OECD (2016b), *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en; OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for non-OECD Latin American countries based on OECD National Accounts and national sources.

In general, subnational governments basically execute expenditures with little autonomy regarding how to manage these services and few incentives to improve them (OECD, 2014b). Universal coverage targets and quality standards are determined by the central government in each sector (health, water and sewerage, education). Only when a territorial administration reaches these targets and standards is it entitled to use the surplus resources in other areas of its own competence. Universal coverage must be met in the sector to be certified and it has to accomplish certain indicators of quality defined by the central administration. Certification is granted by demand of the territorial entity. Currently, according to the information received from the Department of National Planning (DNP), there are a few subnational governments that have achieved the targets (OECD, 2014b). Fifteen municipalities have achieved the highest rating. In a comparison of the period 2011-14 of the ten municipalities that showed the greatest improvement, four of them are concentrated in the department of Bolivar. Fifty-three municipalities met the minimum qualification.

Figure 2.3. **Breakdown of subnational government expenditure by economic function, OECD countries and Colombia, 2013**



Source: Authors' elaboration based on OECD (2016b), *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en; OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

In addition, most of these earmarked expenditures consist of current expenditure, including the payment of teachers and health staff, which are incompressible costs and on which subnational governments have no control. This explains the fact that the share of subnational staff expenditure in public staff expenditure reached almost 48%.

Constraint on expenditure is reinforced by Law 617 of 2000 which established tight limits on the growth of operating expenditures based on demographics, imposing strict control on subnational spending. Current expenditure represents around 85% of subnational governments' total expenditure. Law 1551 of 2012 modified Law 6177 of 2000, defining seven categories of municipalities and five categories of departments to determine appropriate ceilings for current expenditure according to demographic size and capacity to generate current income.

Box 2.3. Categorisation of municipalities and departments

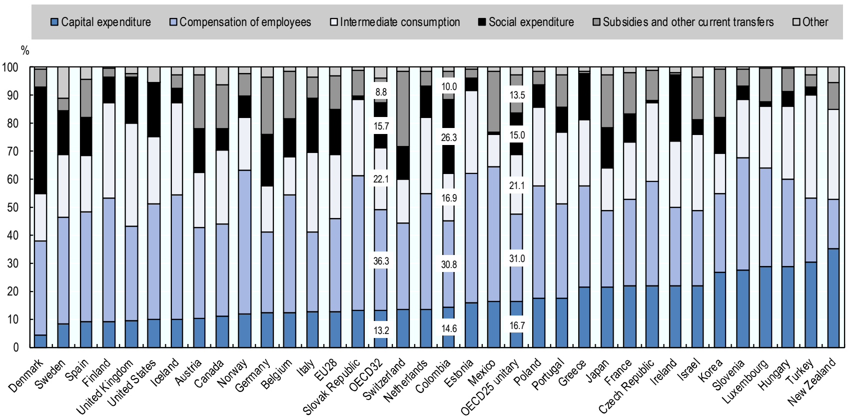
For financial management and monitoring purposes, departments and municipalities are categorised. Law 617 of 2000, modified by Law 1551 of 2012, had defined seven categories of municipalities and five categories of departments according to both demographic size and current own revenues (i.e. revenues generated by their real capacity of tax collection). The smaller subnational governments and those with a lower capacity to generate current income (due to a fragile tax base or a poor demographic profile) have a higher ceiling for current expenditures and conversely, the bigger and more financially autonomous subnational governments have a stricter ceiling, e.g. from 50% (special category) to 80% (categories 4, 5 and 6) for the municipalities and from 50% (special category) to 70% (categories 3 and 4) for the departments (Law 617/2000).

Although subnational governments' role for investment has increased, it remains relatively limited

Subnational government capital expenditure, including investment and capital transfers, represent 15% of total subnational government expenditure in Colombia. It is slightly below the average for OECD unitary countries but significantly below some unitary countries, where the main functions of subnational governments are investment, more than management of public services and benefits, such as in France or Japan. As for current expenditure, an important part of this investment is earmarked, depending on sectorial subsidies which limit the "investing autonomy" of subnational governments.

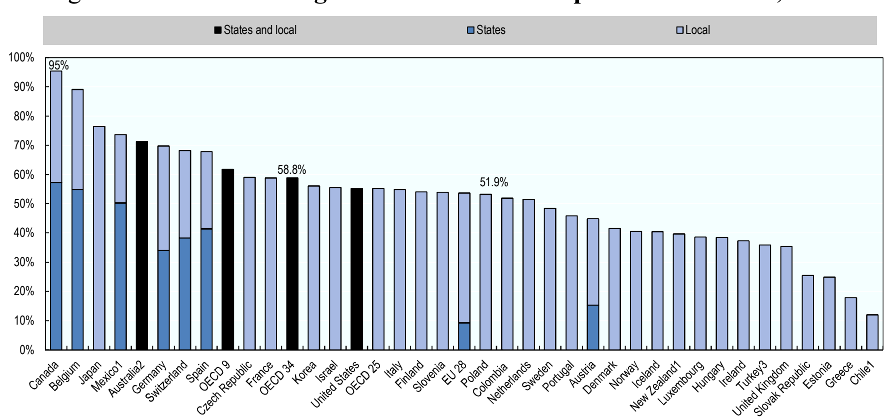
If we focus on investment only (i.e. capital expenditure less capital transfers), the increasing role of subnational governments since the decentralisation and royalties reforms must be acknowledged. Subnational government investment as a share of GDP increased from 1.1% in 2000 to 2% in 2014, in line with the OECD average, which is particularly remarkable as GDP rose sharply during the same period. In 2000, investment accounted for 10% of subnational spending, but it amounted to 15% in 2013. Subnational governments in Colombia are now key public investors, representing a bit more than half of overall public investment (51.9%). However, this share of subnational government in public investment remains lower than in the OECD (58.8% for all OECD countries and 55.2% for OECD unitary countries). In addition, the level of subnational investment per capita is low (see Chapter 1).

Figure 2.4. **Breakdown of subnational government expenditure by type, OECD countries and Colombia, 2014**



Sources: Authors' elaboration based on OECD (2016b), *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en; OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

Figure 2.5. **Subnational governments' share of public investment, 2014**



Notes: 1. 2013 figures. 2. 2012 figures. 3. 2011 figures. The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Sources: Authors' elaboration based on OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

Subnational capacities to raise additional revenues to finance investment

In 2013, 53% of subnational revenue came from transfers from the general budget. In 1985, before the reform introduced by the Constitution of 1991, central government transfers only represented 20% of subnational revenues. Today, Colombia stands among the countries where subnational governments depend highly on central government grants (Austria, Estonia, Mexico, Netherlands). On average, grants represent 38% of subnational government revenues in the OECD and 50% when considering OECD unitary countries only. Tax revenues represented 29% of total subnational government revenues in 2013 while they amounted more than 60% in 1985 (Bousquet, Daude and de la Maisonneuve, 2015). The share of other revenues is particularly high in Colombia (18%), in particular compared to the OECD average, as they include property income (oil and mining royalties, assets sales and other rents, dividends; i.e. around 10% of subnational government revenues), user tariffs and fees (around 3%) and social contributions. Other sources for subnational government financing are external, and include borrowing, equity financing and public-private partnerships.

In this general framework, the main financing sources for investment are the national investment budget (sectorial subsidies and grants), own-source revenue (taxation, user tariffs and fees), royalties (the General System of Royalties, SGR) and external funding. The main central government transfer, the General Participation System (Sistema General de Participaciones, SGP) is not primarily aimed at financing investment.

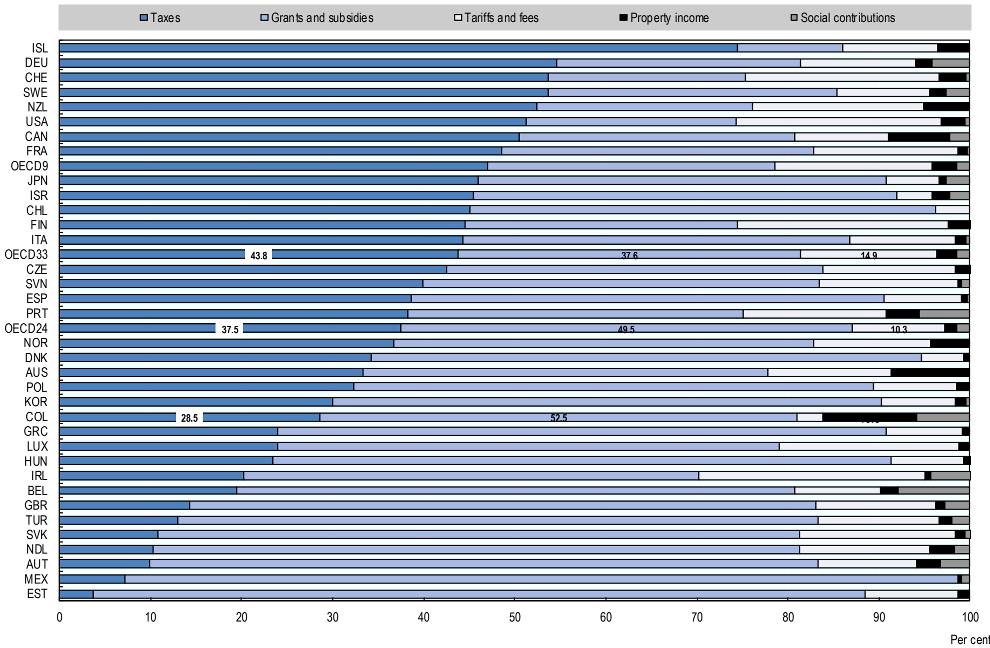
Table 2.1. **Subnational revenue and national investment budget in Colombia, 2010-14**

COP trillion

	2010	2011	2012	2013	2014
General Participation System (SGP)	19 303	21 135	23 456	25 728	27 823
General System of Royalties (SGR; investment part)	5 208	7 507	5 578	5 592	6 231
Own tax revenues	15 859	17 264	18 775	20 692	23 567
Other own revenues	7 309	9 050	9 824	11 667	15 303
Total	47 679	54 956	57 633	63 679	72 924
National investment budget	21 528	28 812	34 418	40 917	42 720

Source: DNP (2016), Answers to the OECD questionnaire.

Figure 2.6. **Subnational sources of revenues in OECD countries and Colombia, 2014**



Sources: Authors' elaboration based on OECD (2016b), *OECD Regions at a Glance 2016*, http://dx.doi.org/10.1787/reg_glance-2016-en; OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en; OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

Transfers are rigid and mainly targeted at current expenditure

Central government transfers are the first source of revenues for subnational governments. They come mainly from the SGP, the main transfer device from the national government, benefiting both departments (35% of the SGP and 37% of their revenue in 2014) and municipalities (65% of the SGP and 42% of municipal revenue). Recently, these revenues have increased steadily in current terms, from COP 19.3 trillion in 2010 to COP 28.8 trillion in 2014 (DNP, 2016). SGP resources are mostly considered as financing current expenditures, often labelled "social investment" in Colombia. The share of investment dedicated to infrastructure (gross fixed capital formation) within the SGP is much lower, accounting for 11% in 2015.

Organic Law 715 of 2001 on resources and competencies, modified by Law 1176 of 2007, determined the distribution of the SGP funds between key sectors and types of expenditure (as indicated above operating expenditure is privileged, in particular payrolls). The system is rigid: funds can only be used for the purpose indicated by the SGP; they cannot be used to cover any debt. As a result, 83% of funds must be dedicated to sectoral current expenditure, in particular in the education sector (58.5% of funds), health (24.5%), and water supply and sewerage (5.4%). Around 4% of the SGP funds are allocated to special current expenditure, in particular school meal services, the Territorial Pensions Fund (Fondo de Pensiones de Entidades Territoriales, FONPET), indigenous reserves and municipalities on the Magdalena River. Only 11.6% of the SGP funds are for municipal general purpose expenditure.

The SGP combines a series of distribution criteria which take into account population coverage, social equity and efficiency (coverage targets, quality standards, control of operating expenditures, efficiency of tax collection, etc.).

Strict earmarking provides a certain number of advantages to guarantee equal access to local public services, in particular for jurisdictions with limited capacities. In fact, transfers have a strong redistributive effect, as in 2014 the Gini Index for departments was 0.4 if considering only own resources, and 0.31 with the SGP (respectively 0.41 and 0.23 for municipalities) (Bonet-Morón and Ayala-García, 2015).

Transfers are considered a highly stable and predictable source of revenues for subnational governments. The allocation is transparent, as most are determined through clearly defined formulas. Transfers may only be affected by inflation, whereas royalties (see below) are more sensitive to global economic trends – like the current fall in oil prices. Until 2016, by law, transfers to subnational governments will grow by 3% per annum in real terms. Additional one-off resources are transferred when real GDP passes 4%. After 2016, transfers will increase at the same rate as revenues in the four previous years. This smoothes out most short-run fluctuations, but linking transfers to the central government's structural revenues, in line with the fiscal rule, would be better (OECD, 2015d). However, following a transitional period that will end in 2017, transfers will be indexed to general government revenues, possibly introducing more instability, even if some steps have been taken to try to limit this.[1]

The most important challenges for transfers are the following:

- Large and fast growing transfers from the central government might reduce the incentives to raise more own revenues and improve the quality of expenditures at the subnational level (Bousquet, Daude and de la Maisonneuve, 2015). However, a recent study commissioned by the DNP (2014) showed that there is no evidence of fiscal laziness resulting from national transfers.

- The grant allocation rules are very strict, leaving little incentive to improve the allocation of these resources at the local level (OECD, 2014a). The system substantially reduces subnational government decision-making powers, especially since, within each sector, the use of funds comes with guidelines, certifications systems and strict controls, further restricting subnational governments' real spending autonomy. There is evidence showing that the current system is too rigid. Some municipalities, for instance, complained that they received many resources for water and sewerage when infrastructures in these fields were finished and they could not use these resources to finance other needs.
- A 2014 evaluation states that the objectives set for the SGP were not fulfilled (Bonet, Pérez and Ayala, 2014). The problems mentioned in the evaluation are that the allocation criteria do no distinguish between urban and rural areas – although the conditions for implementation are quite different, and that they focus more on coverage than on quality of service. Besides, they are a great burden for departments – which substitute municipalities in service provision if they are not certified but without the corresponding resources.
- Although basic public services are financed (health, education, and water and sanitation), other issues have a major impact on territorial development, such as transport or social housing, that are not addressed in the system.
- Although the SGP formula allocation takes into account population, poverty rates, dispersion and coverage deficit, among others, the system does not (yet) allow[2] considering the specificities of certain territories (urban or rural). In fact, the lack of territorial data makes it difficult to take Colombia's rich diversity and socio-demographic changes into account (urbanisation, rural exodus, etc.), and the amount of funds allocated through transfers has remained virtually unchanged since 2005. Given the large internal migration flows, it is more than likely that local needs have changed (OECD, 2014b). In addition, although the criteria to allocate resources in the SGP have so far been quite clear and based on unbiased variables (population coverage), since the royalties reform the system is becoming more and more complex. According to several sources, the transfers from the SGP are, in practice, sometimes used to finance the operating costs of royalties projects (OECD, 2014b).

  In fact, the transfers' system is disconnected from the royalties framework while both systems are in reality indirectly interrelated. Most capital investments (roads, schools, hospitals, utility networks) require recurrent expenditures over time that need to be funded mainly by the SGP, as subnational tax collection is limited (see below). Therefore, the SGP will bear a strong increase in current expenditure as a consequence of the capital investments built with royalties. Against this backdrop, a long-term vision of the development of both systems is needed (OECD, 2014b).

- The resources of the SGP do not seem to be sufficient to fund basic public services required by territorial governments. To fulfill this resource gap, subnational authorities use royalties to finance some projects that should have been funded by the SGP or other sources.
- In addition, the rules for financing current expenditures through the SGP have undergone numerous changes, thus creating uncertainty for local authorities. Some specific funds could be implemented targeted at specific needs, for example in urban and rural areas. Some OECD countries have created such specific grants and subsidies for metropolitan infrastructures such as transportation, business parks or cultural facilities, e.g. the Metropolitan Fund in Mexico, EU Structural Funds in Italy and Poland (special contracts), a special fund for traffic infrastructure in Switzerland, special transport funds in the Netherlands for Amsterdam and Rotterdam-The Hague, the City Fund in Flanders, City Deals in England. Reforms could also allow or facilitate innovative financing schemes such as a multi-level metropolitan fund, for example the Regiofonds, a special fund of the Groningen-Assen Regional Alliance in the Netherlands, made up each year from the financial contributions of the different partners and supplemented by the central government and European grants (OECD, 2014c) (see Chapter 3).

Royalties are key to finance subnational investment, but they are volatile and currently declining

Royalties linked to natural resources (hydrocarbon) are collected by the central government, which then returns these funds to the departments and municipalities. In 2012, the government shifted from a system in which royalties benefited resource-rich departments to one in which the allocation of royalties is spread out more evenly across the country and distributed according to criteria related to need and population (OECD, 2014b). The intention of the government was also to take advantage of the commodity boom to close some infrastructure gaps. Before the reform, most of the royalties were allocated to the oil- and mining-producing departments and municipalities, and spent on recurrent expenditures for education, healthcare, water sanitation and some basic infrastructure. As several resource-rich regions were institutionally weak, a lot of the resources were diverted towards unproductive projects due to corruption (Echeverry et al., 2011).

Box 2.4. The royalties reform in Colombia in an international perspective

Colombia is not the only country to have implemented a reform of its royalty system due to skyrocketing international prices for commodities, and its experience mirrors a global trend. Many resource-based countries have been reforming their tax or royalty regimes or revenue mechanisms to better respond to changes in market prices and evolving market conditions.

Given the substantive contribution of the extractive sector to the public purse in oil- and mining-producing economies, the ability of governments to collect royalties and taxes, and to generate and manage volatile revenues, has been the subject of increasing public debate. In particular, when commodity prices are on the rise, as they were for the ten years prior to 2015, producing countries may become more exposed to public scrutiny for the need to reach a fair balance between the need to achieve overall public benefits, share risks and reward investors. In this regard, many producing countries have recently undergone or announced the adoption of reforms of tax/royalty regimes or revenue mechanisms in an effort to better respond to evolving market conditions. Among OECD countries, in July 2012, Australia imposed a new mining rent tax (MRTT), widened the base of the petroleum resource rent tax (PRRT) and launched a number of initiatives aimed at spreading the benefits of the mining boom throughout the economy and helping businesses adapt to the transformations underway (OECD, 2012). In Canada, the province of Alberta introduced in 2009 a new royalty tax regime that also applies to oil sands and factors in oil prices and well production. In 2011, the Chilean government approved the Fund for Regional Investment and Restructuring (FIRR). This fund allocates USD 100 million per year – for a four-year period – to the mining regions of the country, to fund development projects of regional governments and municipalities. The national government is also negotiating a new fund to be directed to mining municipalities and regions (Fondenor).

Source: OECD (2013), “Policy Dialogue on Natural Resource-Based Development: Scoping paper”; OECD (2012), *OECD Economic Surveys: Australia 2012*, http://dx.doi.org/10.1787/eco_surveys-aus-2012-en; in OECD (2014b), *OECD Territorial Reviews: Colombia 2014*, http://dx.doi.org/10.1787/9789264224551-en.

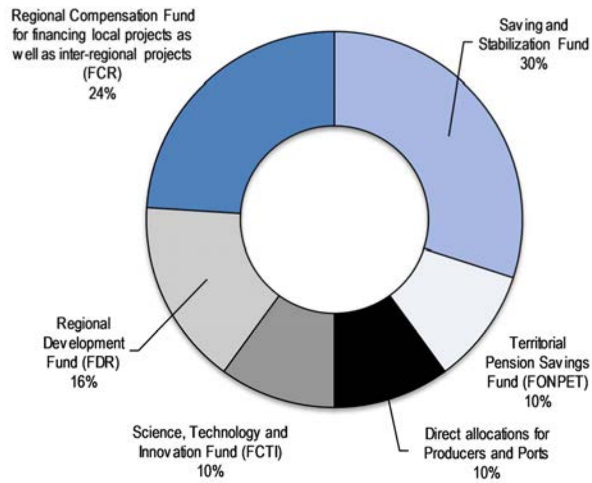
The royalties reform (Legislative Act 05 of 2011, complemented by Law 1530 of 2012) aimed at achieving sustainable economic growth and improving living conditions in the most vulnerable areas. Since the reform, all departments can benefit from revenues from royalties. For example, between 2002 and 2010, the four departments of the Pacific region, which is one of the poorest in the country, received an average of COP 40 million annually. With the reform, the region will receive more than 20 times this allocation. After the reform, all departments and most municipalities receive funds from the SGR for investment projects. The projects have to be approved by a collegiate body (*órgano colegiado de administración y decision*, OCAD) that includes public authorities from all levels of government and technical experts (Bousquet, Daude and de la Maisonneuve, 2015).

Box 2.5. **Equity focus of the royalties reform**

Firstly, the reform aimed at ensuring that all territorial entities were now beneficiaries of the exploitation of non-renewable natural resources and not only those located in producing regions. Secondly, the Regional Compensation Fund (Fondo de Compensación Regional, FCR) aims at financing local projects, in particular submitted by the poorest and smallest municipalities. Thirdly, the amount of the resources allocated by departments is calculated thanks to a formula integrating social variables, in particular poverty, population and unemployment. Before the reform, 8 departments (Casanare, Meta, Guajira, Huila, Arauca, Cesar, Santander and Córdoba) and their municipalities – i.e. 17% of the Colombian population – received 80% of the total resources that were generated from the royalties from exploiting mining and hydrocarbon resources. Only 20% of resources benefited the rest of the country. Since the reform, it is the opposite: 80% of resources go to non-producing regions and 20% remain in producing ones. All departments and 1 089 municipalities became beneficiaries in 2013 (instead of only 522 municipalities in 2010), receiving important resources to put toward the financing of their investment projects. Therefore, it is also a regional and local integration tool: it allows territories affected by armed conflict and illicit crops to integrate to the rest of the country. It also allows distributing the profits from natural resources even to small local communities which can now access these funds.

Revenues derived from royalties are placed in the SGR, which comprises six funds (Figure 2.7). Funds are allocated through a sophisticated formula-based system. Only the two regional funds (Regional Development Fund [Fondo de Desarrollo Regional, FDR] and the Regional Compensation Fund [Fondo de Compensación Regional, FCR]) and the Science, Technology & Innovation Fund (Fondo de Ciencia, Tecnología e Innovación, FCTI) are earmarked to investment projects only, i.e. 50% of the SGR. Therefore, royalties are mostly aimed at financing investment – and they now represent a crucial source of funding for investment – contrary to transfers, which are mainly dedicated to current expenditures. The executing agent for investments financed by the SGR is decided project by project by an OCAD, which approves the projects. It is not necessarily the subnational governments to which the funds are assigned that executes them.

Figure 2.7. **Breakdown of royalties between six funds**



Source: Authors' elaboration from Legislative Act 05 of 2011 and Law 1530 of 2012.

Royalties are mainly assigned to departments and a significant share has a regional development focus, even though in practice they mainly finance local small investment projects. In 2014, these revenues accounted for 7.6% of municipal revenues (0.6% of GDP) and 28% of departmental revenues (1.1% of GDP).

The reform has had positive impacts on boosting investment and ensuring more equity across regions and municipalities. From 2012 to 2015, royalties financed around 10 000 approved projects amounting to around COP 21.2 trillion, out of COP 24.1 trillion earmarked for investment during the period (the difference is funding that does not yet have a corresponding approved project). The new system has significantly increased the allocation of resources to poor regions compared to the old system (Bonet and Urrego, 2014).

However, some challenges remain or have emerged:

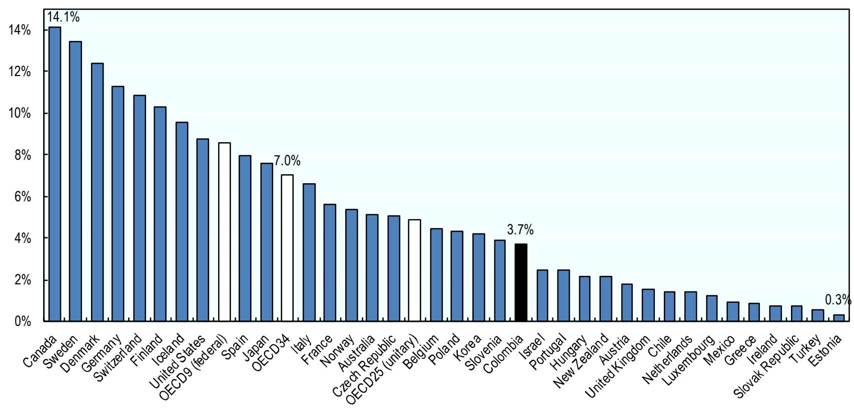
- In principle, this division between the SGP and the SGR is reasonable: royalties are transitory one-off revenues that should be used to foster investment projects, while current expenditures are excluded from the SGR due to their recurrent nature. Nevertheless, the increase in subnational investment will require higher recurrent maintenance expenditures from the SGP in the medium term. This will put pressure on the system, as departments and municipalities have too little own revenues (OECD, 2014b). In particular departments have limited own resources compared to municipalities, despite the fact that departments not only have their own responsibilities, but often have to administrate the resources and deliver public goods and services in smaller municipalities without sufficient capacity (Bousquet, Daude and de la Maisonneuve, 2015).

- The governance of royalties is disconnected from the other sources of investment funding. Since 2013, two budgetary systems currently coexist in Colombia. Royalties are not included in the annual budget, and have a separate bi-annual budgetary framework. They are also disconnected from the SGP system (see above).
- The allocation of royalties is itself atomised in thousands of small projects, rather than large-scale projects with a regional impact (see Chapter 3). The SGR is a project-based system instead of a programme-based one that implements medium-term, viable and sustainable development strategies (OECD, 2014b).
- Finally, royalties cannot by themselves represent the sole answer to public investment needs in the country to reduce regional gaps. So far, the funds allocated by the SGR to regional development only represented 6% of a total of USD 35.2 billion revenue at the disposal of subnational governments (i.e. total subnational revenue) in 2012.
- In addition, this source of funding is very volatile as it fluctuates with the international oil prices. For example, they increased from COP 5.2 trillion in 2010 to a maximum of COP 7.5 trillion in 2011, before returning to COP 5.5-6.2 trillion between 2012 and 2014, oscillating between 8.5% (2014) and 13.7% (2011) of total subnational revenues. In the current context of a drop in oil prices, it is clear in any case that royalties resources should be complemented by other sources of subnational revenues.

Subnational governments' tax revenues are limited and outdated

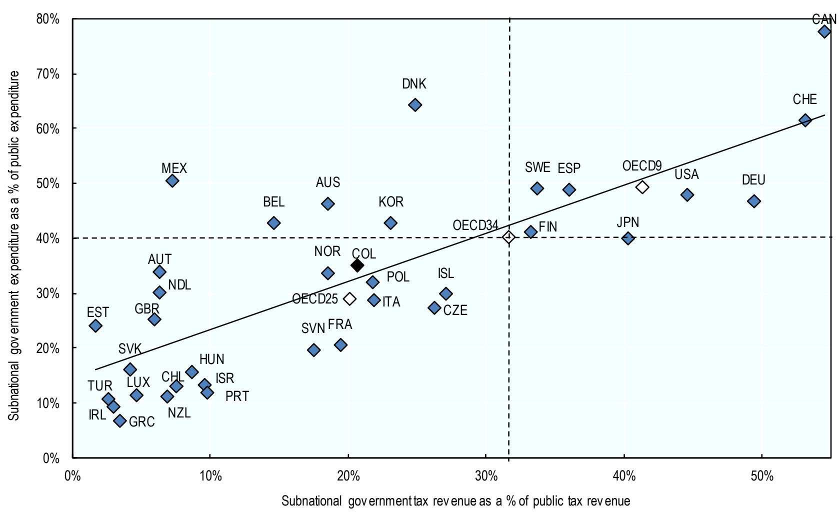
Subnational tax revenues are limited. They account for 29% of total subnational revenues, representing 3.7% of GDP and 20.7% of overall tax revenue in Colombia, well below the OECD averages which were respectively 7.0% and 31.6% in 2014. This reveals a mismatch between responsibilities allocated to subnational governments and their funding, in particular a vertical fiscal imbalance between expenditures and tax revenues.

Figure 2.8. **Subnational government tax revenue as a percentage of GDP, OECD countries and Colombia, 2014**



Sources: Authors' elaboration based on OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en and OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

Figure 2.9. **Fiscal imbalances in OECD countries and Colombia, 2014**



Sources: Authors' elaboration based on OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en and OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

While over the last two decades there has been a trend towards more decentralisation of key expenditures to departments and municipalities, it has not been matched with key institutional changes in the tax revenue-sharing system.

Tax revenues are more significant for municipalities than for departments, representing 29% of municipal revenues and around 21% of departmental revenues in 2014. Departmental tax revenues include receipts from the excise taxes (beer, tobacco and liquor, i.e. around 60% of their tax revenues), vehicle tax (10%), register tax and gasoline tax. At municipal level, there are around 20 different taxes, but 80% of the tax receipts come from only 3 taxes: industry and commerce tax (around 40% of municipal tax revenues), property tax (Predial, around 33%) and gasoline surtax (7%).

The local tax system, which dates back to the 1980s, is criticised for different reasons:

- Despite the power to levy their own taxes, subnational governments have limited taxing autonomy, with little room for manoeuvre over tax rates and bases. They can establish fiscal benefits or vary the tax rate only for some taxes and within a maximum and minimum rate predetermined by law. They cannot create new taxes. In addition, several taxes are earmarked for specific uses and current expenditures defined by law. For example, municipalities are required to give between 15% and 25.9% of the property tax receipts to the autonomous regional corporations (*corporaciones autónomas regionales*, CARs), Colombia's regional environmental authorities, which use these resources to fund environmental and renewable natural resources projects. In the same manner, revenues from the gasoline surtax are often directed to the maintenance of the road network and investment in the mass transportation system.
- Several of these taxes are not related to subnational competences, such as excise taxes, while departments have an educative role and have to fight against addictions. In the same vein, the industry and commerce tax is given to municipalities which have no competence in this field. Moreover, several taxes are sensitive to economic fluctuations or to political decisions (excises taxes, industry and commerce tax ICA, tax on vehicle and gasoline, etc.).
- Many subnational governments have a relatively weak tax performance. Subnational governments have limited incentives and political reluctance to raise local taxes. Tax revenue is below its potential, due to tax rates set below the maximum authorised amount, multiple exemptions and deductions, dated and undervalued tax bases (e.g. lack

of an updated and reliable cadastral and land registry despite some progress since 2008, monitoring of economic activity), collection inefficiencies (tax collection is very expensive, and its efficiency varies widely, bad management and delays of payment, tax evasion, fraud and smuggling) and low elasticity (taxes based on “consumption of vices”).

- The tax system is uniform for all municipalities and departments (with some exceptions); it does not give more autonomy to the more dynamic and well-equipped ones in terms of human, technical and financial capacity to levy and collect taxes effectively. The system is heavy and expensive to manage for municipalities with weak capacities. Larger municipalities have professional tax offices in charge of collecting tax receipts while the collection costs are sometimes greater than the collected tax revenues in small municipalities (Kalmanovitz and López Enciso, 2006).

- Municipalities lack reliable and updated registries of companies. Few municipalities have up-to-date cadastral and land registries (only three cities – Bogota, Medellín and Cali – have their own cadastre offices) as they currently have to compensate the Geographic Institute Agustín Codazzi (Instituto Geográfico Agustín Codazzi, IGAC) to compute property values and they are often pressured by local lobbies not to do so. Bogota has attained 100% registration of land. In comparison, only 43% of all rural areas are included in the registry system (World Bank, 2012). The system is very complex for taxpayers, and subject to contestation, with 72 legal texts dealing with the topic, according to the Colombian Federation of Municipalities (FCM).

- There are large disparities in tax revenues between subnational governments which have different fiscal capacities (social and economic taxable basis, assets, human capital, etc.). Many lack sources to generate their own income from taxation. Typically large urban municipalities and wealthy departments, with a strong economic base thanks to a concentration of firms, economic actors and population as well as a good cadastre, enjoy a greater own-revenue tax base than more remote and impoverished municipalities and departments, which have less economic activities and population.

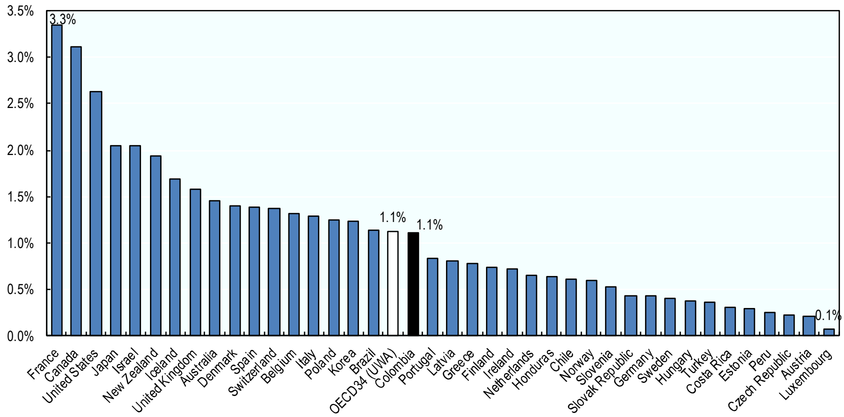
  For example, the four departments of Antioquia, Cundinamarca, Valle de Cauca and Santander concentrated 50% of all departmental tax revenues in 2014. On the other hand, half of departments received only 14% of tax revenues (DNP, 2014a). The share of tax revenues in total departmental revenues varies greatly, ranging from 10% for the less favoured departments to almost 40% for richer ones, such as Antioquia or Cundinamarca. Tax disparities are also very high across municipalities. Five municipalities concentrate 57% of all municipal tax receipts, with Bogota having the highest share (38%) followed distantly by Medellín, Cali, Barranquilla and Cartagena. As a result, taxation is the main source of revenue for these municipalities. In 2014, the seven largest municipalities of Colombia extracted 43% of their revenues from taxation against 12% for the 975 smallest municipalities (less than 10 000 inhabitants, i.e. 90% of Colombian municipalities included in category 6 of the municipal classification) which, by contrast, depend largely on central government transfers.

In summary, the financing model does not encourage own resource generation, in particular in the departments (IDB, 2012). Subnational governments could raise more tax revenue, to offset potential adjustments in the royalties system in the medium term, reduce the dependence from the central government and thereby increase resources for the development of public services and infrastructures in the country.

In that perspective, it is essential for Colombia to continue efforts to update and modernise the cadastral and land registries in order to improve the performance of the municipal property tax. Property tax receipts have increased significantly since 2012. Property tax represented 0.8% of GDP in 2011, reaching 1.1% in 2014, close to the OECD unweighted average. The central government could provide cadastral services free of charge, or at a lower cost. Inter-municipal co-operation could be promoted in this area (shared services, municipal agreements) and/or more involvement of departments as co-ordinating entities (see Chapter 3). Other proposals could include decentralising some functions carried out by the IGAC which would regulate, monitor and prepare guidelines while registers would be decentralised to third parties, including subnational governments, through delegation of competences (e.g. the case of Baranquilla).

In addition, it could be envisaged to reward greater subnational tax effort by, for example, linking increases in transfers from the central government to tax (or own-source) revenue growth. This would also help develop land markets needed to increase efficiency in the use of land. For example, linking increases in transfers from the central government to increases in structural revenues, in line with the central government's fiscal rule, may be a better approach. The current proposal for the SGP reform would include such orientations.

Figure 2.10. **Property tax as a percentage of GDP, OECD and Latin America countries**



Source: Authors' elaboration from OECD (2016c), "Revenue statistics", *OECD Tax Statistics* (database), http://dx.doi.org/10.1787/ctpa-rev-data-en.

Box 2.6. **A new policy for land tenure and taxation in Colombia**

Two Councils of the National Economic and Social Policy (CONPES) dedicated to land were adopted in 2010 and 2016. CONPES 3641 (February 2010) seeks to improve the relationship between the cadastre and registration, investing in a technology platform that allows major interrelations between both systems and co-ordinating the two entities responsible for the cadastre and registration (IGAC and the Superintendency of Notaries). CONPES 3859 aims at setting up a "multi-purpose cadastre". This pilot project will allow collecting property tax information for approximately 100 municipalities in 2016. The objective is to obtain updated tax information for 25% of the country. It will be not only be a key tool for the formalisation of land in the country, the reinforcement of legal certainty of properties and the improvement of land taxation, but also a tool to provide information useful to various public policies, such as environmental policy or land police (conflicts of use, illegal use, etc.). In that context, it is also important to note the recent creation of the National Land Agency (Decree 2363 of 2015), which is in charge, in particular, of the formalisation of land tenure in Colombia, particularly in the post-conflict context.

Assessments show that municipalities with higher tax revenue get the best results for poverty reduction, even taking into account the degree of administrative capacity and initial poverty level (Ramírez, Díaz and Bedoya, 2014). More room for manoeuvre could be given to subnational governments to manage taxes, by giving them more leeway over rates and bases, allowing the subnational entities to decide the allocation of the over-taxation, and reducing the number of earmarked taxes. As recommended in the *OECD Territorial Review of Colombia* (OECD, 2014b), the government could also review the portfolio of taxes levied by the departments and municipalities. In fact, subnational governments, in particular urban areas, cannot rely solely on property tax, which provides insufficient revenue to cope with huge metropolitan needs (Bird and Slack, 2013). There are a lot of small taxes which are administered by subnational governments but which do not represent much revenue and which cost a lot in terms of administrative burden. It could take the form of creating more productive own-source taxes or introducing tax sharing (between the central and subnational governments) or piggy-backing (e.g. to levy a local surtax as a supplement to a national income tax), which would create incentives for subnational governments to be more active in the field of economic development.

Box 2.7. **Reforms to support local revenues in unitary countries**

In most of central and Eastern European countries, new acts on local government revenue were adopted or revised in the 1990s (during the transition) and 2000s (at the time of EU accession). These reforms were often linked to the decentralisation of expenditure duties. In Poland for example, the 2004 Act on Local Government Revenue profoundly modified the financing of subnational governments. Subnational governments gained more financial autonomy, with a decrease in the share of central transfers (and of earmarked grants), and increased shared tax revenues (higher proceeds from the personal income tax and corporate tax). In the Slovak Republic, the 2005 Act on Local Financing deeply modified the subnational financial system, by raising both shared and own-source taxes, and reducing central government transfers to subnational governments. In Slovenia, a new Law on Municipal Financing came into effect on 1 January 2007 (replacing the 1998 law). The system of vertical tax equalisation was consolidated, with a transitional period. The financial autonomy of municipalities was reinforced through the introduction of new resources, in particular a poll tax aimed at covering the average costs necessary to perform urgent municipal tasks. In these two countries, the reforms led to a significant increase in the share of tax revenues in GDP and public tax revenues.

Important fiscal reforms were also implemented in other unitary countries such as Portugal (2007 local finance reform), Denmark (2007 local government reform, introducing new financing and equalisation systems), Korea (2005 and 2009 fiscal reforms creating general purpose grants), Norway (2007 reform of the property tax), Turkey (2008 Law on Allocations from Tax Revenues under the General Budget to Special Provincial Administrations and Municipalities), Sweden (2005 reform of equalisation), Italy, France and Japan. In Denmark and France, these reforms led to a decrease in subnational revenue autonomy, while in Turkey, Korea, Finland, Portugal, Italy and Japan local revenue autonomy increased.

Box 2.7. **Reforms to support local revenues in unitary countries** (*continued*)

France: an important tax reform took place in 2010, after years of discussions. Its primary objective was to abolish the local business tax (*taxe professionnelle*), paid by companies and based on the rental value of fixed assets. This tax had always been criticised for its negative impact on companies, employment and investment, and for the important inequalities it created both among subnational governments and businesses. The business tax reform led to a broader reshuffling of the local tax system, decreasing the share of own-source tax in favour of shared taxation. The local business tax was partially replaced by a new "territorial economic contribution", composed of two taxes: a business tax on real estate (own-source), and a business value-added tax (CVAE). Other shared taxes were created in parallel. The reform led to a tax "specialisation" between subnational government tiers (all subnational governments used to benefit from the same four local taxes before the reform). Departments and regions lost many of their taxing powers. They are now particularly limited for the regions. New horizontal equalisation mechanisms were introduced: the equalisation fund for inter-municipal and municipal resources (redistributing 2% of total tax revenues in 2016), the departmental fund based on the property transaction tax (*droits de mutation*), and the equalisation funds based on the business value-added tax (CVAE, for departments and regions). These new mechanisms supplement existing vertical equalisation instruments based on central government grants, allocated according to different criteria (expenditures, resources or specific constraints). Several other reforms have been prepared since 2010 but were postponed to 2017. In particular, reforms of the main general purpose grant and of the equalisation system were considered. Regional financial resources should be reformed to match the new regional competences. At the time of writing, the future of the regional taxation system remains unclear. In 2015, the government announced a major increase (from 25% to 50%) of the regional share in CVAE revenues. According to the 2016 Finance Law, the costs corresponding to new transfers of responsibilities resulting from the reform will be, prior to their transfer, assessed by local commissions for the assessment of transferred costs and resources.

In **Japan,** the 2004 Trinity reform included three major components: 1) the transfer of tax revenues from the central government to local governments (creation of a tax-sharing system); 2) a reform of the equalisation tax; 3) the abolishment and reduction of national earmarked grants. The reform aimed at increasing the share of own revenues in local governments' budgets while decreasing their reliance on inter-governmental transfers. A Committee for the Decentralisation Reform was created, and the six major regional government associations proposed plans for reforming the national transfer system. However, these recommendations were not taken into account, which was strongly criticised. Local governments argued that they didn't gain enough financial autonomy and independence. Critics also objected that the primary aim of the reform may have been fiscal consolidation rather than decentralisation. Transfers of tax revenue sources were insufficient to compensate for the cuts in grants, which led to financial deterioration at the local level and increased the gap between rich and poor local authorities. New reforms implemented since the Trinity reform included a reform of special funds, the conversion of earmarked grants into general-purpose grants in 2011 and 2012, and increases in the local rate of the national sales tax in 2014. New reforms are also under preparation.

Source: Chatry I. and Hulbert C. (2016), "Multi-level governance reforms: Overview of OECD country experiences", OECD Publishing, Paris.

Other sources of revenue, such as tariffs and fees and property assets

On top of a tax reform, it could be envisaged to give more freedom and flexibility to subnational governments to manage tariffs and fees associated with the provision of local public services (e.g. public transports). Restrictions are imposed on subnational governments to modify user tariffs and fees and they are still under-developed in Colombia (2.7% of subnational revenue compared to 14.9% in the OECD in 2014). There is scope to increase infrastructure funding streams by raising user charges. These own revenues may be freely used for current or investment expenses and are widely seen as the most appropriate source of revenues for metropolitan areas to finance the operation and maintenance expenses of infrastructure (parking fees, transport fees, fees on other public services – e.g. waste, water, energy). An appropriate legal framework and pricing scheme would need to be established. In particular, Colombian metropolitan areas may also charge the major negative externality through "smart taxes" and fees (congestion, pollution, road safety, waste of time, quality of life, health and environmental degradations) resulting from excessive car use in metropolitan areas. For example, the revenues of congestion charges adopted in London, Seoul, Singapore, Oslo, Milan, Berlin or Stockholm have been used to finance urban public transport and other urban facilities.

Property income (financial interests, dividends, rents, sales) are another source of funding which could provide additional revenue for investment to Colombian subnational governments. This source is often underestimated, but financial and non-financial assets could be used better (Bova et al., 2013).

In particular, making the most of revenue coming from local industrial and commercial companies in the form of dividends could be further considered. Some large Colombian cities already benefit from this type of revenue. Empresas Públicas de Medellín (EPM),[3] the city's profit-making publically owned utility, contributes 30% of financial surplus to the city's administrative budget according to the Governance Framework Agreement signed between the city and the company. In addition to this regular annual contribution, the EPM also provides discretionary grants to the municipality for carrying out its social development programmes, especially in the sectors of education, employment, recreation programmes, environmental improvement, mobility and urban infrastructure. In 2011, ordinary transfers corresponded to 55% of total contributions while 45% were provided by extraordinary transfers for joint programmes and investment projects between the EPM and the city of Medellín. Roughly 40% of own-source revenues (or 24% of total revenues) of the city of Medellín come from dividends from the EPM. However, the EPM remains a unique case. Other interesting examples are the Water and Sewerage Company of Bogota (Empresa de Acueducto y Alcantarillado de Bogotá), whose income is equivalent to 24.45% of the revenues of the municipal government, reaching a surplus of COP 338 billion in 2014, or the Mass Transport Company of Cali S.A. (Empresa de Transporte Masivo de Cali S.A.), whose income represents 14% of the revenue of the municipality, with a surplus of COP 100 billion in 2014 (Ministry of Finance and Public Credit, 2014).

To go a step further, it would be essential to prepare a clear diagnostic of financial (company shares, financial investments, savings, cash deposits, loans, etc.) and physical assets (lands and buildings) owned by subnational governments. Having a full national strategy for land assessment is important in distributing land, taxing property and ensuring property rights. In many countries, including in the OECD, such assets inventories are lacking although they are critical to the design of performant fiscal management frameworks.

Land-based financing instruments

Several Colombian cities are already a leader in land-based financing instruments in Latin America, with a long-standing experience in this field. Inspired by the Constitution which stipulates that one of the state's duties is to capture the added value generated by public actions, Colombia has created, quite some time ago, two interesting revenue-raising mechanisms aimed at financing urban developments by capturing the capital gains from property and land generated by public infrastructure projects: the *Contribución de valorización* (created in 1921) and the *Participación en Plusvalías* (1997). The first one is a betterment levy (also called a special assessment), i.e. a "compulsory charge imposed by a government on the owners of a selected group of properties to defray, in whole or in part, the cost of a specific improvement or services that are presumed to be of general benefit to the public and of special benefit to the owners of such properties". The second mechanism aims at recovering part of the increased land values resulting from the change in land-use regulations (changing zones, change in the designation of the type of land, change in density regulations). These instruments are used mainly by large cities and have limited penetration beyond them (World Bank, 2012). For example, from 1950 to 1990, this tool allowed the city of Bogota to finance more than 30 public works (roads, bridges and public spaces). In 2014, Bogota collected COP 231 billion via the *Contribución de valorización* and COP 11 billion via the *Participación en Plusvalías*. Other cities that stand out for their collection of the *Contribución de valorización* are Cali, Bucaramanga and Barranquilla (CHIP).

Box 2.8. **Subnational government non-financial assets: Towards better knowledge and a better use**

Non-financial assets comprise mostly structures (such as roads and buildings) and land. Their values have increased over time mostly due to higher property and commodity prices. They are generally divided into those that are produced and those that are non-produced. Following the 2008 System of National Accounts terminology, produced assets include: 1) fixed assets, namely buildings and structures (like dwellings owned by the government, roads and other infrastructure), machinery and equipment, computer software and, since 2008, research and development; 2) inventories; and 3) valuables (such as works of art, precious metals and stones). In turn, the OECD classification groups non-produced assets into those that are tangible (such as land and subsoil resources) and non-tangible (such as leases and licenses). Non-financial assets are usually greater than financial assets, and total assets typically exceed general government gross debt.

While the availability of comparable cross-country data is limited, the International Monetary Fund has found that a large portion of non-financial assets is owned by lower level governments. On average, subnational governments hold more than one-half of total non-financial assets. The share of regional and local governments is particularly high in federal states, such as Canada, Germany and the United States, where subnational government assets exceed the holdings of the central government by a ratio of at least four. In Germany, local governments hold the largest share of fixed assets, mostly as buildings and structures. At around 60%, the local authorities' share in the ownership structure has remained broadly constant over time, with the federal government (and social security funds) accounting for 22% and the state governments for 18%. France is an example of a unitary state where most non-financial assets, including large reported values of land, are in the hands of local governments. Local governments account for three-quarters of the non-financial assets ownership. Specifically, with the decentralisation reform of 1982, the property of some buildings and land has shifted from the central government to local governments. In Japan, almost 70% of non-financial assets are owned by local governments. Colombia also reports an important share of subnational government in non-financial assets.

Sales of assets could be problematic for long-term sustainability if the one-off receipts are used for permanent spending. However, there are other promising sources for future revenues, including rents and the collection of user charges, including through public-private partnerships. In countries with subsoil assets, exploitation could yield significant future revenues, which is already the case in Colombia and OECD countries such as Australia, Canada, Chile or Norway.

Governments are now taking further steps to improve information gathering and public asset management. In the United Kingdom, the government has followed a strategy for better use of non-financial assets in support of the overall deficit reduction, as laid out in the 2010 Spending Review. It has created a Government Property Unit in charge of property management in the public sector and set up a new central database for all departments and local governments.

Source: Bova, E. et al. (2013), "Another look at governments' balance sheets: The role of nonfinancial assets", https://www.imf.org/external/pubs/ft/wp/2013/wp1395.pdf.

In that domain, the Colombian government could provide technical assistance to subnational governments, in particular large and medium cities. Other schemes of land value capture tools, developed in OECD countries, could be also assessed, such as “development charges” in Canada and in the United States, tax increment financing districts in the United Kingdom, development rights or development contributions in New Zealand that councils require from developers as part of granting consent for development so that developers bear the costs of new infrastructure (roads, water and wastewater infrastructure, and community facilities) and which represent around 2% of their revenues. In Denmark, the extension of the metro line in Copenhagen was financed through fees from the development of the Ørestad area of Copenhagen (OECD, 2009). New York City is financing the Hudson Yards subway line extension and station through the issuance of bonds by a special purpose vehicle, the “Hudson Yards Infrastructure Corporation”, with debt service guaranteed by innovative sources of revenues, including: 1) tax equivalency payments, provided by the city in anticipation of future tax revenues from land value increases; 2) payments in lieu of taxes, which offer land tax exemptions to project developers in a specific area; and 3) transferable development rights from the transfer of public property land and building rights (OECD, 2013).

Co-financing is increasingly used

Other revenues for subnational government investment include co-financing from the national government. The main structured device for co-financing are the *Contratos Plan*, introduced in 2012 and signed between the central government and one or several departments or groups of municipalities. They aim at combining a shared medium-term strategic vision on territorial development focused on key sectors with stable financial commitments for execution of the associated investments. The *Contratos Plan* do not constitute a new source of funding for investment themselves. They allow access to different existing sources from the national budget, the General System of Transfers, the General System of Royalties, subnational governments’ own resources as well as private resources to be mobilised. The first 7 *Contratos Plan* included 9 departments and 272 municipalities with a timespan between 3 and 8 years, and are being extended to new departments. They focus in priority on lagging regions and areas with the weakest capacities. The local counterpart comes mainly from the SGR, but also from own revenues and the SGP. These tools facilitate bottom-up approaches and engagement, including the tailoring of development strategies to the specific territorial needs of departments or municipalities (see Chapter 3).

Even though the National Cofinancing System (Sistema Nacional de Cofinanciación) created in the 1990s was discontinued more than ten years ago, co-financing is also commonly practiced on an ad hoc basis between subnational governments and line ministries. Subnational governments looking for co-financing shall align their projects with the national priorities in the sector and negotiate with the relevant line ministry.

Fiscal disparities in investment capacities remain high

Efforts to support the capacity of subnational governments to raise own-source revenues are likely to benefit more large cities. Fiscal disparities across subnational governments are high in Colombia, as explained above. In particular, disparities in revenues are large, due to different fiscal, human and technical capacities (see above), and autonomy. Many subnational governments lack resources to generate their own income from taxation, royalties, public services (fees/tariffs), and management of assets (dividends from the sale and rental of local public companies, real estate). Typically, large urban municipalities and wealthy departments with a strong economic base and a concentration of population, firms and economic actors, enjoy greater own revenues than lagging rural regions. They also have the specific capacities to use innovative financing instruments, in particular those which are land-based or to develop public-private partnership projects.

There is no fiscal equalisation system per se to address fiscal disparities, although the SGP transfer mechanism has an equalisation function. The SGP is progressive in all its components and several allocation criteria aim at reducing the gaps across municipalities and departments which suffer from a lack of resources or excessive spending needs. They are based on social equity (population, relative poverty as quantified by the unsatisfied basic needs index) in order to guarantee access to a basic basket of key public services of comparable quality in several basic sectors (education, health, water, etc.) to all citizens, wherever they live. SGP transfers have a redistributive effect, as in 2014 the Gini Index for departments was 0.4 if considering only own resources, and 0.31 with the SGP (respectively 0.41 and 0.23 for municipalities) (Bonet-Morón and Ayala-García, 2015). In addition, the 2012 reform of the SGR was conceived to achieve regional equity and to increase, through investments, the speed of convergence of lagging regions and local areas within the country. It has a strong regional equity focus (see chapter 3).

However, much remains to be done to reduce the fiscal disparities gaps across subnational governments. The existing system does not compensate for the better ability of well-off departments and municipalities to raise their own revenues from local and departmental taxes compared to the poorer departments (Bousquet, Daude and de la Maisonneuve, 2015). More flexible framework conditions for the municipalities/departments with the highest institutional capacities should thus be compensated by reforms to further support lagging regions. The current proposal of the SGP reform includes the objective, among others, to reinforce equalisation mechanisms, through more progressivity and differentiation criteria for allocating funds. Other reforms, such as those linked to improved cadastre and land assessment, would also ultimately help improve the unequal fiscal capacity across regions. Finally, *Contratos Plan* also plays a role for the development of lagging regions and the reduction of fiscal disparities (see Chapter 3). However, given the existing high disparities and the risk that fiscal decentralisation will increase them further, it seems necessary to strengthen financial solidarity. Appropriate equalisation mechanisms to support these regions should be established. They could include specific new equalisation tools (horizontal and vertical) as well as the amplification of existing instruments such as *Contratos Plan* and the peace contracts which are currently under preparation and can play a key role in that respect.

Borrowing is not properly used as a mechanism for financing investment

A strong subnational fiscal discipline

The fiscal situation of subnational governments has considerably improved over the past decades and is solid. In 2013, subnational governments presented a budget balance of 1.2% of GDP, while higher investment expenditures will reduce it to 0.5% of GDP in 2014 (OECD, 2015d).

This good situation is the result of fiscal responsibility rules implemented between 1997 and 2003 which introduced some restrictions to excessive spending and constraints to subnational borrowing which had dramatically increased since the 1991 decentralisation reform. In fact, decentralisation of new responsibilities resulted in a considerable increase in expenditures in the 1990s which was not matched by sufficient revenues. Subnational governments had to borrow increasingly to cover their deficit. Subnational government debt attained unsustainable levels at the end of the 1990s (from 2.6% of GDP in 1991 to 4.6% in 1997), which jeopardised the overall public finances in the country (OECD, 2014b).

To deal with the fiscal sustainability problems of subnational governments, the Colombian authorities introduced a series of reforms starting in the late 1990s. In particular, Law 358 of 1997 introduced a “traffic light” system that classified subnational governments according to liquidity and solvency indicators. This law was reinforced in 1999 by Law 550 dealing with subnational government insolvency and in 2000 by Law 617 which introduced current expenditure caps. In addition, subnational governments are authorised to contract long-term debt to finance their physical investments ("golden rule").

Box 2.9. **The "Traffic Light" Law for subnational governments in Colombia**

The fiscal context of the 1990s at the subnational level required the central government to enact a set of fiscal discipline laws to address these imbalances. To increase the central government's control over subnational debt, the so-called Traffic Light Law 358/1997 (Ley de Semáforo) was adopted, introducing prudential rules for territorial governments, based on a liquidity ratio (interest payment/operational savings) and a solvency ratio (debt/current revenue) (caps on outstanding debt and debt service). Highly indebted local governments were prohibited from borrowing (thus given a red light when the interest to operational savings ratio is greater than 40% and the debt stock to current revenues ratio is greater than 80%). Those in the green light zone were allowed to borrow. Intermediate cases were given a yellow light, which meant that they had to obtain prior approval from the central Ministry of Finance for borrowing and fulfil certain performance conditionalities.

This law was complemented in 1999 by Law 550 which deals with bankruptcy procedures of highly indebted subnational governments, enabling them to sign debt restructuring agreements with creditors. This law was reinforced in 2000 by Law 617 which aimed at limiting growth of current expenditure (it sets limits to municipal expenditure based on the demographic size of the municipality), forbidding transfers to other public entities, creating new municipalities (and municipalities that are proven to be non-viable have to merge with other municipalities), and adopting two-year rescue plans in case of financial distress and non-compliance with fiscal rules. Law 617/2000 also established a budgetary classification of the municipalities based on population and current incomes.

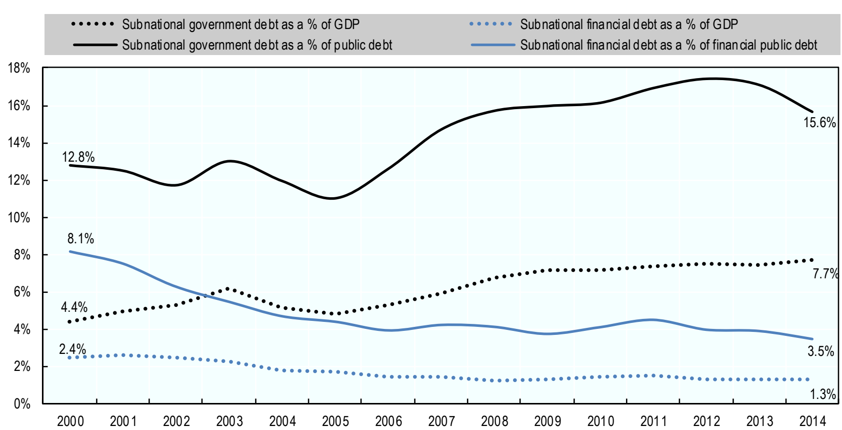
In 2003, fiscal rules were again strengthened through a proper Law on Fiscal Transparency and Responsibility (Law 819/2003), giving more institutional backing to pursue its national fiscal-balance strategies. This law, which applies both to the national and subnational governments, sets budget targets at subnational levels and links them to target ranges for debt and deficits. The law eliminated the "yellow light" category in the Traffic Light Law. Entities previously categorised as yellow then fell under the red light category, with tightened borrowing restrictions. It also tightened the regulations on the credit supply side (banking sector) and required that departments and large municipalities obtain satisfactory credit ratings from international rating agencies before they could borrow on the market. In addition, to discourage tying fiscal policy to the electoral cycle, it prohibited governments from committing future spending (*vigencias futuras*) or increasing personnel spending in an election year (OECD, 2014b). The observance of these rules is constantly monitored by the central government, which has implemented sound financial and administrative information systems allowing risks of insolvability to be detected. In general, the rules to enhance controls on subnational expenditure have been very successful.

Recent trends in subnational debt

If all debt liabilities are considered,[4] i.e. financial debt, pension liabilities and the other accounts payable (commercial debt to suppliers and arrears), total subnational government debt as a percentage of GDP and public debt has increased substantially since 2005, reaching 7.7% of GDP and 15.6% of public debt in 2014. This is the result of the pension reform,[5] which integrated territorial pension liabilities into subnational debt (pension liabilities represented 65% of total debt liabilities in 2014; other accounts payable 18%; and the financial debt, mainly loans and bonds, 17%).

As explained above, a strong fiscal discipline has been the main driving force of Colombia's fiscal reforms over the last 15 years, and, in general, the rules to enhance controls on subnational expenditure and borrowing have been quite successful (OECD, 2014b). Subnational government financial debt has decreased since 2000, both as a percentage of GDP and as a share of public debt. It amounted 2.4% of GDP and 8.1% of public total general government financial debt in 2000 but 1.3% of GDP and 3.5% of total general government debt in 2014.

Figure 2.11. **Subnational debt as a percentage of GDP in Colombia**

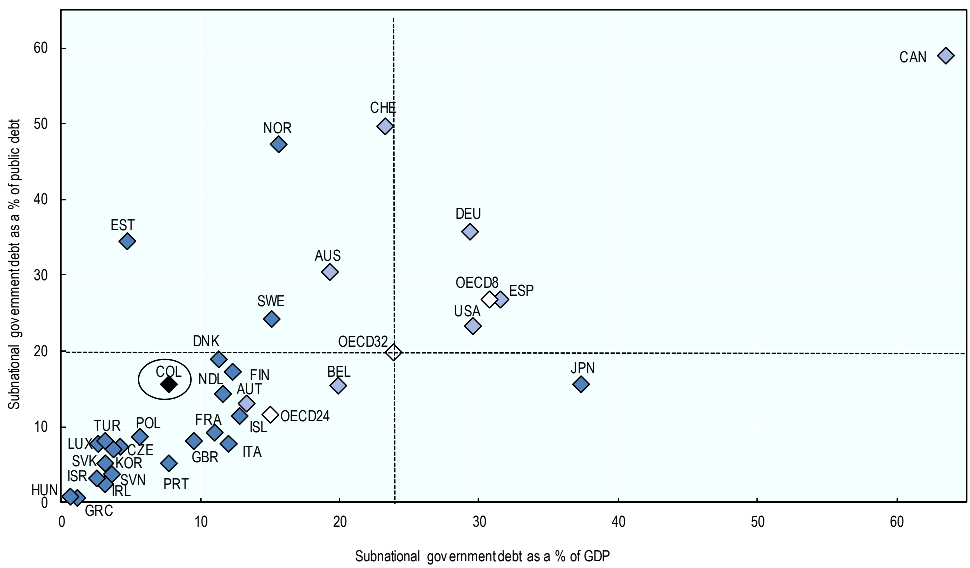


Note: SNG: subnational government.

Source: Authors' elaboration based on OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en.

Compared with OECD countries, the level of subnational government debt is below the OECD average (23.9% of GDP and 19.8% of total public debt) as well as below the average of OECD unitary countries in terms of share in GDP (15%), but above it when considering it as a share of public debt (11.6%).

Figure 2.12. **Subnational government debt as a percentage of GDP and public debt, Colombia and OECD countries, 2014**



Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Sources: Authors' elaboration based on OECD (2016d), "Subnational government structure and finance", *OECD Regional Statistics* (database), http://dx.doi.org/10.1787/05fb4b56-en and OECD (2016a), *National Accounts Statistics* (database), http://dx.doi.org/10.1787/na-data-en; authors' calculations for Colombia based on OECD National Accounts.

If the financial debt of local public companies (called *entidades descentralizadas subnacionales*) is included in the subnational government debt, the level of indebtedness is significantly higher, i.e. 4.2% of GDP (instead of 1.3%). Among the 20 local public companies which detail debt, 5 are particularly active: Empresas Públicas de Medellín (EPM), Empresa de Transporte Masivo del Valle de Aburrá (ETMVA), Empresa de Energía Eléctrica de Bogotá (EEEB), UNE EPM Telecomunicaciones (a subsidiary of EPM) and Empresas Públicas Municipales de Cali. Altogether, they represented around 80% of local public companies' total debt, of which 38% was for the EPM and 24% was for the ETMVA (Ministry of Finance and Public Credit, 2015).

As far as the subnational government debt per se is concerned, departments represented around two-thirds of subnational government debt and municipalities one-third in 2014 (DNP, 2014a). In addition, debt is very concentrated in a few departments and some large cities (Box 2.10).

Box 2.10. **Subnational debt concentrated in a few regions**

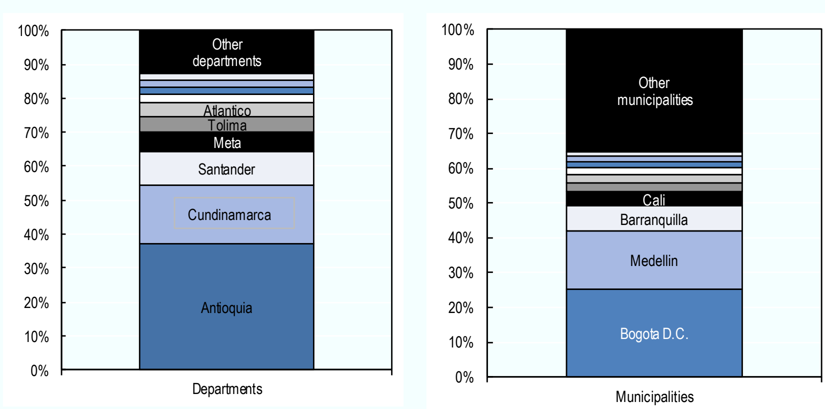
In 2014, 67% of departments' debt (86% of which is domestic) was concentrated within four departments: Antioquia, Cundinamarca, Santander and Meta. Only four of them contracted external debt (Antioquia amounting to 73% of the total in 2014).

Fourteen municipalities concentrated 70% of total municipal debt, of which nine regional capital cities including Bogota D.C, Medellín, Barranquilla, Cali, Pereira, Pasto and Neiva. Half of debt is owned by three cities: Bogota D.C., Medellín and Barranquilla. Only five capital cities contracted external debt (Bogota and Medellín, accounting for 95% of it). In the other cities, debt was also relatively concentrated, with 20 subnational governments concentrating 45% of total debt.

Figure 2.13. **Distribution of outstanding debt, 2014**

A. Departmental debt, by department

B. Municipal debt, by municipality



Source: Authors' elaboration from DNP (2014a), "Desempeño fiscal de los departamentos y municipios 2014".

Only 13% of subnational financial outstanding debt is in the form of bonds, the great majority (87%) being loans from commercial, specialised public banks or intermediaries (e.g. FINDETER, FONADE), multilateral and foreign financial institutions (World Bank, Corporación Andina de Fomento, Inter-American Development Bank), international banks (Agence Française de Développement) or even from the central government.

Box 2.11. **The role of FINDETER**

FINDETER (Sociedad Financiera de Desarrollo Territorial S.A.) is a Colombian public development finance agency created in 1989 and owned by the Colombian government (92.55%) and departments to fund significant local and regional infrastructure projects. FONADE (Fondo Nacional de Desarrollo, or the National Development Fund) focuses on smaller scale projects. FINAGRO concentrates its activities on financing agriculture and industry.

FINDETER acts as a second-tier lender, encouraging first-tier lenders (commercial banks) to enter into direct relationships with local governments by rediscounting loans that commercial banks make to local borrowers. Therefore, it makes it more financially attractive for commercial banks to lend to local entities and it allows longer maturities at attractive rates to be proposed. For its funding, FINDETER relies on international financing (Inter-American Development Bank, World Bank, Agence Française de Développement) and financial markets receiving very high credit ratings. According to the most recent data from July 2014, FINDETER has 1 838 projects underway in 320 municipalities and 29 departments.

Worth noting is a USD 600 million credit line from the Inter-American Development Bank, managed by FINDETER for "innovative financing", which means that the projects financed by the loan and/or accompanying institutional strengthening programme aim at increasing subnational government revenues (and pay back the loan), for instance cadastre upgrading and updating.

Most often, innovative financing schemes – such as access to bond markets and loans from international or foreign financial institutions – are reserved for stronger governments and cities. Domestic bonds are used mainly by large cities and account for almost a quarter of their domestic borrowing. External financing is mainly performed with multilateral institutions and other governments, even though some capital cities also issued international bonds (accounting for 30% of their external financing).

Most debt (95% in 2014, compared to 93% in 2013) is rated with an "A" grade (lowest risk), and the share of subnational government debt with the central government or with its guarantee diminished from 30% to 27% between 2013 and 2014 (86% of which is for subnational government public companies, and 81% for domestic borrowing).

As far as financial debt is concerned, the fiscal rules implemented in 1997 (Law 358) and reinforced in 2000 (Law 617) and 2003 (Law 819 on Fiscal Transparency and Responsibility) have proven their efficiency. This reinforcement of fiscal discipline and surveillance – together with the strengthening of subnational revenue sources – led to good results and greatly improved the financial performance of subnational governments.

Improve the use and management of subnational borrowing

Borrowing remains, however, an interesting tool and presents some advantages to finance investment projects, but only in certain conditions, as it also has costs and risks. Large infrastructure projects cannot be funded only through self-financing capacities and capital transfers and should be complemented by alternative sources, which is the case in most OECD countries (see above). There are other arguments in favour of borrowing to fund investment projects: it allows more projects to be funded and accelerates their delivery; it permits the costs of infrastructure to be shared with future beneficiaries and not only with the current taxpayers, reflecting the philosophy of intergenerational equity, where local councils seek to spread the cost of infrastructure across generations, as in the case of councils in New Zealand. Borrowing therefore allows a better matching of costs paid and benefits derived over time, which is more equitable, and also conforms more closely to standard cost-recovery principles. Borrowing may also strengthen the sense of community ownership over inherited local infrastructure. On some particular macroeconomic conditions determined by the level of inflation and interest rates, an appropriate loan could be economically more interesting than paying cash and permit real savings in overall infrastructure costs. Developing a relationship between the borrower and the lender (banking institution or the market) can also improve the financial management of the local government and improve its creditworthiness, monitoring and reporting practices. Finally, it provides a sort of accountability as the local government must present its financial accounts. Therefore, a municipality with infrastructure loans could have a financial incentive to promote transparency and good governance (World Bank, 2009).

In these conditions, an effort could be made to assist Colombian subnational governments to improve their use and management of borrowing to fund investment projects. In particular, it is crucial to determine which investment programmes and projects should be financed, in part or fully, through debt according to their characteristics. In that perspective, preparing multiannual capital investment plans together with strategic planning documents should be promoted as a management tool (see Chapter 3).

In this framework, the development of local bonds, which are underused, could be encouraged for large subnational governments, taking advantage of the fact that all departments and large municipalities as well as metropolitan areas are rated by international rating agencies. An agency, on the model of local government funding agencies used in New Zealand or the Nordic countries, could be established by the central government in partnership with subnational governments and other financial partners (public and private banks).

The Colombian government could also develop further initiatives such as the Sustainable and Competitive Cities Initiative, developed by the Inter-American Development Bank, which partnered with FINDETER (see Box 2.12). The initiative consists of supporting action plans in cities, including loans which are coupled with a non-reimbursable technical assistance subsidy to finance capacity building. Such innovative approaches allow, in addition to providing additional funding, improving technical capacities of financial managers and local governance.

Box 2.12. **Platform for Sustainable and Competitive Cities**

In 2012, the Inter-American Development Bank partnered with the Colombian National Development Bank, FINDETER, in the creation of the "Platform for Sustainable and Competitive Cities". This platform consists of supporting the implementation of action plans with technical assistance and resources for pre-investment and credit, as well as developing partnerships with public and private institutions in order to ensure the execution of projects.

Action plans define priority actions needed in areas including: public transport, water and sanitation, urban development, energy, infrastructure, education and health, fiscal management, safety, information technology, climate change adaptation, and resilience infrastructure.

Resources are found by the two organisations, which work together in order to channel funding from a variety of external sources, including bilateral donors (British and Swiss governments and the French Development Agency). In addition, FINDETER has channelled long-term financing for projects prioritised in the action plans and the Inter-American Development Bank is also developing a loan to support the prioritised interventions in these cities, which will be implemented through FINDETER.

In order to involve citizens in this process, the Emerging and Sustainable Cities Initiative and Findeter have established an alliance with the 15-year-old Colombian citizen monitoring initiative "Cómo Vamos", to monitor the implementation of the prioritised actions.

The initiative started in four cities (Barranquilla, Bucaramanga, Manizales and Pereira) and has now extended to eight cities, adding Monteria and Pasto in 2013, and Cartagena and Valledupar in 2014. Between 2012 and 2014, seven projects to improve the sustainability of these cities had received technical assistance, and another six were in the pre-investment phase. Four cities, Barranquilla, Bucaramanga, Manizales and Pereira, had received action plans. So far, USD 480 million in resources has been channelled for investment in these projects, which represents 25% of the amount identified in the action plans.

Source: FINDETER and Inter-American Development Bank.

Innovative financing tools for investment could be explored for Colombia, such as revolving funds. The objective is to use transfers with a view to attract matching funds from municipalities, for example, or to serve as a guarantee for private finance. Revolving funds involve "pump priming" by the central government to stimulate borrowing by subnational governments, creating revenues from loan repayments. The United States and the Philippines have successful schemes of this nature, in particular in the water sector (OECD and World Water Council, 2015).

Box 2.13. **Exploring the use of revolving funds**

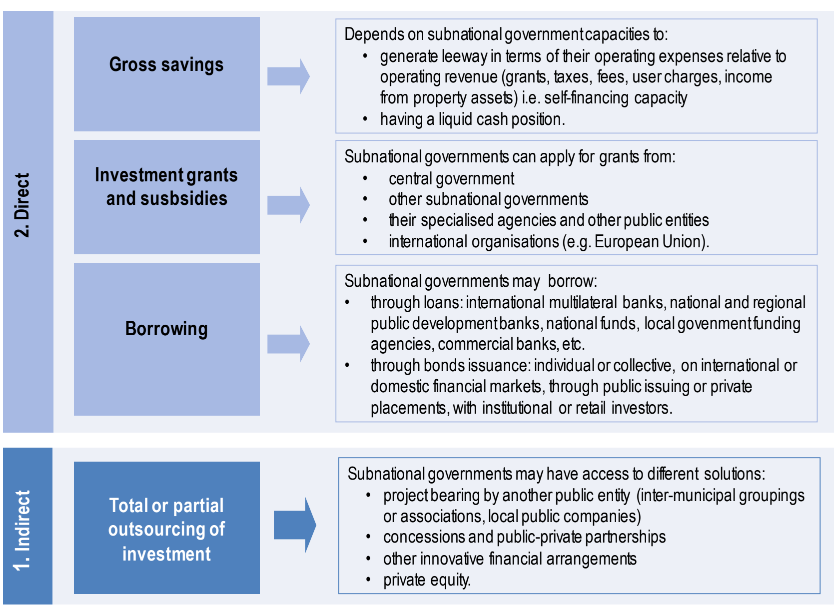
In the United States, the model of state revolving funds (SRFs) has worked well. This financing scheme was set up as a consequence to the "Federal Clean Water Act" in 1984. The US federal government decided to create SRFs for wastewater and water projects in the United States. The idea was to make capital grants to state governments, matched by a contribution from the state. Several states used these subsidies to create dedicated reserve funds to collateralize pooled bond flotation to support the financing needs of local governments in the state. The pooled SRF bonds of New York state are AAA rated, even when many participating local governments have lower ratings or are not rated at all. The SRFs typically provide a number of credit enhancements, like debt service reserve funds and state transfer payment intercept provisions to provide additional comfort to lenders and thereby lowering the cost of borrowing. Another key advantage of the SRF model is the low overheads. The Maine Municipal Bond Bank (which administers the SRF) raises USD 100 million a year with a staff of four. Typical savings from pooling range from 250-650 basis points. Small and medium municipalities often are unable to identify and prepare bankable projects. The SRFs provide three-year interest free loans to local governments for project preparation. This has helped create a strong pipeline of creditworthy projects using SRF resources.

Source: Fay, M. and M. Morrison (2005), "Infrastructure in Latin America & the Caribbean: Recent developments and key challenges", http://siteresources.worldbank.org/INTLAC/Resources/LAC_Infrastructure_complete.pdf.

The need to better connect the different funding sources to finance integrated investment strategies

Efforts to support financing should be accompanied by efforts to adopt a more systemic approach to the governance of public investment, to reduce the overall fragmentation of the system, as many systems coexist with little connection among them, favouring competition, instead of synergies. Investment needs to mobilise and combine various sources of direct and indirect funding from internal and external sources (Figure 2.14). There is no one single model of financing in the OECD. A majority of countries seems to promote a model based on the use of external funding to finance investment (e.g. Japan or New Zealand), while others tend to promote self-financing, complemented by capital transfers. In the European Union, the financing of local government investment (excluding the federated states of Austria, Belgium, Germany and Spain) was provided in 2011 on average by self-financing (49%), capital transfers – i.e. investment grants, subsidies and capital tax (37%) – and 14% through borrowing. With the crisis, these percentages may have changed and do not take into consideration indirect funding (private participation and outsourcing), but they give an idea of the diversity of sources of funding and how they can be activated according to the economic situation and needs. To make the most of public investment funding sources, subnational governments need to prepare integrated investment strategies, including financial plans, financed by different and articulated funding sources. The link between planning and budgeting and the pre-requisites in terms of horizontal and vertical co-ordination are further explored in Chapter 3.

Figure 2.14. **Investment sources of funding**



Source: Authors' elaboration.

Recommendations

Pursuing the reforms of the SGP and SGR systems

- Given that most transfers are strictly earmarked, there is room to introduce a bit of flexibility in the transfer system, notably to allow some flexibility to use unspent funds from one sector in another sector (OECD, 2014b). An in-depth review of the way the SGP allocation criteria are determined could be conducted to simplify them and include new equalisation mechanisms, including criteria based on territorial specificities. Colombia could consider using more matching grants to finance investment. Earmarked investment grants or matching grants could be established for specific projects and places, such as the City Fund. The reform of the SGP system which is currently being discussed is a step in the right direction as it includes some of these recommendations.
- The royalties system (SGR) needs to be better connected with the revenue-sharing arrangements (SGP) and the general budget, to better anticipate the impact of capital expenditures on future current expenditures. The two budgetary systems and royalties should be harmonised. In addition, as planned in the current National Development Plan, the central government should be allowed to submit projects to OCADs in areas where the money is not spent.

Further supporting subnational revenues

- The local tax system should be progressively modernised to review the portfolio of taxes raised by subnational governments so that they better reflect their responsibilities and increase their yield while reducing collection and management costs. More leeway could be given to subnational governments on rates and bases, together with incentives to take full advantage of their taxing power. Another major problem is weak incentives to collect higher property taxes. Efforts concerning the modernisation of the cadastre should be pursued as well as those for reliable and updated company registries. Tax collection and management should be improved and supported by the central government to realise economies of scale and improve efficiency.
- There is scope to increase infrastructure funding streams by increasing user charges and fees by giving more freedom and flexibility to subnational governments to manage them, including in metropolitan areas faced with the need to finance the operation and maintenance

expenses of large urban infrastructure. It would imply establishing an appropriate legal framework and pricing.

- Property income (financial interests, dividends, rents, sales) are another source of funding which could provide additional revenue for investment and which could be developed. In that perspective, making the most of revenue coming from local industrial and commercial companies in the form of dividends could be further considered. The DNP could commission a review on this issue to carry out a diagnostic of the current situation and make recommendations for improvement. In addition, an inventory of financial (company shares, financial investments, savings, cash deposits, loans, etc.) and physical assets (lands and buildings) owned by subnational governments could be prepared providing a clear and updated diagnostic allowing an assessment of the potential for making better use of financial and non-financial assets.

- Such a diagnostic would also allow taking more advantage of and developing land-based financing instruments. The Colombian government could provide technical assistance to subnational governments, in particular large and medium cities. Other schemes of land-value capture tools, developed in OECD countries, could be assessed.

- Co-financing used through *Contratos Plan* should be encouraged, integrating the new generation of *Contratos Plan* for Peace (see Chapter 3). They can be an adequate tool to articulate different sources of funding, promoting synergies instead of competition.

- Fiscal disparities across subnational governments are high in Colombia and efforts to support the capacity of subnational governments to raise own-source revenues are likely to benefit mostly large cities, further increasing these disparities. The reform of the SGP is a step in the right direction by promoting progressivity and integrating new differentiation criteria, including based on territorial characteristics. However, equalisation mechanisms remain limited in Colombia and lagging regions are the ones with the most critical infrastructure needs. Financial solidarity mechanisms to support these regions should be amplified. They could include specific new equalisation tools (horizontal and vertical) as well as the reinforcement of existing instruments, such as *Contratos Plan* and the launch of the peace contracts under preparation which can play a key role in that respect. The DNP could set a working group on that topic to make specific recommendations on equalisation for regional development.

Better use of borrowing for investment

- The main priorities for Colombia in the coming years are to maintain fiscal stability as a key objective in a context of greater fiscal risks.
- While maintaining fiscal stability, it seems necessary at the same time to strengthen the capacity of subnational governments to raise additional revenues to fund investment. Borrowing could be better exploited to address investment needs, taking advantage of a low level of financial debt at the subnational level and sound debt monitoring.
- The use and management of borrowing should be improved by helping subnational governments to prepare borrowing plans, co-ordinated with investment strategies and financial plans.
- The development of local bonds could be encouraged for large subnational governments, taking advantage of the fact that all departments and large municipalities as well as metropolitan areas are rated by international rating agencies. An agency, on the model of local government funding agencies used in New Zealand or the Nordic countries, could be established by the central government in partnership with subnational governments and other financial partners (public and private banks).
- The Colombian government could also develop further initiatives such as the Sustainable and Competitive Cities Initiative. Innovative financing tools for investment could be explored for Colombia such as revolving funds. The objective is to use transfers with a view to attract matching funds from municipalities, for example, or to serve as a guarantee for private finance or stimulate borrowings by subnational governments.

Better connecting the different funding sources to finance integrated investment strategies

- To make the most of public investment funding sources, subnational governments need to prepare integrated investment strategies, including financial plans, financed by different and articulated funding sources.

Notes

1. The macroeconomic formula uses the average of the country's current incomes from the last four years in order to smooth the instability of the economic cycle.
2. The current proposal for the SGP reform includes the introduction of a "rurality criterion" for the distribution of funds.
3. Founded in 1955 by the city of Medellín, the EPM has become the largest multi-utility company in Colombia providing services in the energy sector (generation, transmission, distribution and commercialisation of electricity), distribution and commercialisation of natural gas, water services (supply of water and sanitation), and telecommunications. Since 2010, the company has key investments in Central America, Chile and Mexico.
4. The debt definition here used is based on the System of National Accounts (SNA). It includes the sum of the following liabilities: currency and deposits; debt securities; loans; insurance pensions and standardised guarantees; other accounts payable. Some liabilities such as shares, equity and financial derivatives are not included in this definition. The financial debt includes the sum of currency and deposits, debt securities and loans.
5. Law 549 of 1999 created the FONPET (Fondo de Pensiones de Entidades Territoriales) in order to make gradual provisions of subnational pension liabilities. Subnational governments must make actuarial estimates of their pension liabilities that are revised by the Ministry of Finance and contribute to the FONPET. The FONPET's resources are managed and invested by private pension fund managers.

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Chapter 3.

Achieving strategic vertical and horizontal investment co-ordination in Colombia

Colombia has developed a sophisticated planning framework to guide investment priorities, at both the national and subnational levels. The challenges lie in the effective implementation of the plans and their links with budgeting. These limitations have been tackled seriously and several reforms to improve the implementation of these plans are currently being put in place. Supporting a more strategic approach to public investment requires moving away from a strict project-based approach. This implies greater horizontal co-operation across jurisdictions to invest at the relevant scale, and improved vertical co-ordination with the national government, to foster matching investment schemes and aligning priorities. This chapter will focus on ways to strengthen co-ordination across sectors, jurisdictions and levels of government, which corresponds to the first pillar of the OECD Recommendation of the Council on Effective Public Investment across Levels of Government.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Introduction

Colombia has developed a comprehensive set of tools for planning and budgeting investment at all levels of government and has made significant efforts to improve their coherence. The challenges lie in the effective implementation of the plans and their links with budgeting. Local development plans (*planes de desarrollo territorial*, PDT) have so far often been considered by many subnational governments as pure planning exercises, disconnected from actual budgeting. These limitations have been tackled seriously and some actions to improve the implementation of these plans are currently being implemented, mainly regarding the 2014-2018 National Development Plan (NDP), the 2016-2019 PDTs and forthcoming update to the Land-use Plan (*Plan de Ordenamiento Territorial*, POT).

Turning strategic planning into effective investment prioritisation is a major challenge for any public investment policy. Supporting a more strategic approach to public investment requires moving away from a strict project-based approach. This implies greater horizontal co-operation across jurisdictions to invest at the relevant scale, and improved vertical co-ordination with the national government, to foster matching investment schemes and aligning priorities. This chapter will focus on ways to strengthen co-ordination across sectors, jurisdictions and levels of government, which corresponds to the first pillar of the *OECD Recommendation of the Council on Effective Public Investment across Levels of Government*.

Improved strategic planning framework

National planning

The main planning tool at the national level is the four-year NDP, designed at the beginning of each mandate, and supposed to integrate the country’s development and investment strategy within a unique coherent framework document. The plans include a diagnosis, leading to development goals and objectives. The NDP includes a strategic part and a pluri-annual investment plan (Plan Plurianual de Inversiones Inversion, PPI), regionalised by department, which are key inputs for the annual budgets at national and local levels. They also include indicators, an annualised investment plan, its cost and funding sources. This operational part of the NDP is called the “Plan Indicativo”, and is supposed to be the base for the Annual Operational Investment Plan (Plan Operativo Anual de Inversión, POAI), which is the investment part of the annual budget. The Action Plan (Plan de Acción) further details the way the POAI will be implemented. The National Development Plan structures the action of line ministries and is also supposed to orient subnational governments in their local strategy.

Until 2010, the NDP did not really have a territorial focus. The 2010-2014 NDP for the first time acknowledged the importance of basing sectoral policies on geographic specificities. The 2014-2018 National Development Plan has considerably amplified the territorial focus, compared with the previous plan. It has a strong focus on reducing regional disparities and has for the first time a clear regional structure. The plan has six regional chapters – one for each macro-region identified in the country, the same as those used for royalties – with differentiated regional strategies tailored to local needs. The plan adopts an approach based on "closing gaps" to reduce territorial disparities with systematic indicators of measurement. The 2014-2018 NDP introduces an intra-regional convergence index to measure inequalities among municipalities both nationally and intra-regionally, based on six variables (education, health, water, transport, institutional capacities, housing). It is planned to gradually include other variables such as physical and digital connectivity, rural development and justice, among others. It allows the development of differentiated targets and levels of effort depending on the identified gaps, aiming at reducing them.

Investments planned in the NDP have increased from COP 629 billion in 2010-14 to COP 704 billion in 2014-18 (USD 330 billion). Two-thirds is supposed to be financed from public resources and one-third from private investment. Financing sources included within the development plans include the General Participation System (Sistema General de Participaciones, SGP), the General System of Royalties (Sistema General de Regalías, SGR), the national budget, own revenues from the national government, own fiscal and non-fiscal revenues from the subnational governments, decentralised entities, and private financing (see Chapter 1). The National Development Plan is approved by the higher collegial decision entity of the government, the National Council for Social and Economic Policy (Consejo Nacional de Política Económica y Social, CONPES), chaired by the President of the Republic and composed of the Department of National Planning (DNP) (executive secretary) and all ministries. The NDP is then approved by the Congress through a specific law. On the specific issue of territorial planning, it is worth mentioning the advisory Land-use Planning Commission (Comisión de Ordenamiento Territorial), created with the Organic Law governing the Territorial Organisation in Colombia (Ley Orgánica de Ordenamiento Territorial, LOOT) in 2011, whose members include ministers and experts, and which makes suggestions about land-use policy at the national level.

Rural and urban cross-cutting approaches in national planning

The National Development Plan has become a key tool to foster cross-sectoral approaches, in particular focusing on rural and urban development. The rural pillar is in particular a core axis of the plan, recognising that bridging the rural-urban gap is the most important development challenge for Colombia. In 2012, the Department of National Planning put in place two "missions" to support the design of territorialised cross-sectoral policies for cities and rural areas, through the City Mission (Misión para el Fortalecimiento del Sistema de Ciudades, 2012-2013) and the Rural Mission (Misión para la Transformación del Campo, 2014-2015). The results of the City Mission have been integrated into a specific CONPES, and the outcomes of both missions have been integrated into the 2014-2018 National Development Plan. These missions have addressed cross-cutting issues linked to demographics, productivity, cost of living and quality of life, infrastructure, institutions and planning, rural-urban linkages and finance, and aim at better articulating sectoral policies in urban and rural areas.

Colombia's overall approach to rural development has been dramatically progressing over the last few years (OECD, 2014b). The outcomes of the Rural Mission constitute a major step to understanding the challenges and needs in rural areas and improving the quality of life in these areas. One of the major outcomes of the Rural Mission is a new classification of rural areas, better aligned with the OECD typology. It is expected that Colombia will adopt this new definition of rurality for targeting policies and programmes. It would also be desirable that the statistical agency DANE accepts this new definition. The Rural Mission also identified policies for more inclusive development of rural areas, focusing on education, health, housing and food security. According to the Rural Mission, 0.6 points of annual GDP should be spent on social investment for rural areas on an annual basis through 2035.

Colombia has developed a more comprehensive approach to urban development policy, with a better understanding of the system of cities in the country with the City Mission (Misión para el Fortalecimiento del Sistema de Ciudades), as well as new spatial planning and governance arrangements at the city level. The City Mission has established a very clear diagnosis of the main challenges for urban development to address in the short to medium term, and has developed an action plan to be implemented in the coming years. For example, the mission diagnosed that only 3% of existing POTs include a risk analysis, and 3% a strategy for their rural areas. According to a study conducted by the Ministry of Housing and Territorial Development (2015), 32% of municipalities determined rural land according to its vocation for agriculture, livestock, forestry and similar activities. Referring to disaster risk management, 50% of POTs have made progress in identifying and categorising threats but only 14% have made progress in defining risk and their categorisation. The urban policy agenda goes well beyond the need to connect cities by improved transport as in the previous programming period 2010-14 (Box 3.1).

Box 3.1. **Recent trends in rural development policy: Greater focus on investment to support rural communities**

The current national rural policy is based on three pillars:

1. Direct support to farming. The new system, however, allocates subsidies to all farmers regardless of the crop they cultivate and the size of their holdings.
2. Access to local public services (including healthcare, road connectivity, housing and education).
3. Improvement and reduction in informality in land-use.

The rural development policy connects with other important policy agendas. For instance, the reform of royalties should provide rural communities with the possibility to fill the large infrastructural gap that penalises their development as well as the strengthening of equalisation mechanisms and flexibility through the reform of the General Participation System (SGP).

The rural development policy has focused on redefining rural areas, including the rural municipalities' central towns, previously considered as urban. Actions identified by the Rural Mission included a rationalisation of responsibilities at the national level, and substitution of inefficient INCODER by two agencies (created by decree in December 2015): 1) a Rural Development Agency (Agencia de Desarrollo Rural), in charge of structuring, implementing and co-financing integrated projects, prioritised according to their impact and pursuing finance and sharing project ownership with local public and private stakeholders; 2) a National Land Agency (Agencia Nacional de Tierras), to increase access to land and to formalise ownership and regulation of its use in a supply-oriented logic (from the needs of the territory). This agency will be closely linked to the generalisation of multipurpose cadastres (fiscal, property, territorial) identifying the use and ownership of land, as validated by CONPES 3859 in 2016 with a timeframe of eight years (up to 2023). and implemented throughout the country in seven years (up to 2022). It is important to strengthen the co-ordination between the Geographic Institute Agustín Codazzi, the National Land Agency and the Superintendence of notaries and public registries.

The Department of National Planning also co-ordinates the Territorial Integrated Approach to Rural Development Programme (Programa de Desarrollo Integral con Enfoque Territorial, PDRIET, 2012): pilot projects implemented with municipalities, aimed to assess policy options to improve poor rural households' accessibility to public services and implementing them in a cross-sectoral approach with a focus on endogenous development (OECD, 2014b). This programme has been evaluated through a Sinergia evaluation, which emphasised the necessity to broaden and deepen territorial analysis, to better take political aspects and institutional development into account, and to more explicitly focus on productive development and related technological issues. Replication and expansion of the PDRIET depend on financial resources, but also on not relying solely on financial incentives.

Source: OECD (2014b); OECD (2015b); DNP (2016a), Answers to the OECD questionnaire.

Box 3.2. **Priorities defined by the City Mission**

The City Mission has placed particular emphasis on the need to improve the connections of Colombian cities to both each other and the outside world. Connectivity among its urban centres has always been a challenge, owing to the size and topography of the country, which raises the cost of overland transport infrastructure. This is particularly true of connections among inland cities and between inland cities and the coast. In the more recent past, as noted in Chapter 1, the internal security situation reinforced the isolation of Colombia's cities. The pacification of the country has dramatically eased movement among cities, but infrastructure investment has not kept up – the road network is saturated on most international trade corridors as well as most lines of access to the main cities. The emphasis on upgrading and expanding connective infrastructure thus makes sense and is likely to improve national economic performance and competitiveness. It is likely to be one of the more promising uses of the country's resource rents.

The City Mission has identified more than 40 actions, with specific budget commitments and time schedules. The results of the City Mission have been integrated in a specific CONPES, which establishes a policy for the System of Cities (Sistema de Ciudades) that seeks to answer the problems identified by the mission. The National Policy for Cities focuses on six strategic issues: 1) sustainable development and green growth; 2) physical and digital connectivity within and among cities; 3) productivity and economic development; 4) quality of life and equity; 5) adequate financing, including an extended use of land-related financing instruments within the Land-use Plan (POT) updating programme (Modern POT/POD National Program and multipurpose cadastre); and 6) co-ordination and governance, fostering associative schemes for specific purposes (for instance water distribution). The CONPES on Urban Policy defining the System of Cities should now be implemented, and sectoral ministries should apply the System of Cities approach within their sectorial policies (World Bank, 2014).

The Department of National Planning has defined the functional size of metropolitan areas, with criteria of population (above 100 000 inhabitants) and commuting flows. It identified a System of Cities of 151 municipalities (113 of which grouped in 18 urban agglomerations) accounting for 67% of the country's population. The OECD is also applying its functional urban areas methodology to Colombia.

Source: City Mission and OECD (2014b), *OECD Territorial Reviews: Colombia 2014*, http://dx.doi.org/10.1787/9789264224551-en.

Other tools that promote a cross-sectoral approach to investment are the sectorial Commission on Strategic Infrastructure and Projects and the competitiveness policy, with the regional plans of competitiveness. In 2013, an Inter-sectorial Commission on Strategic Infrastructure and Projects was created and "strategic and national interest projects" were identified in order to more efficiently plan and execute them. Thirty-nine mining/energy, 27 transport and 1 telecommunication projects have been identified. In 2014, following the Law on Infrastructure which aimed at streamlining the infrastructure process, the Vice President assumed the co-ordination of inter-institutional and inter-sectoral infrastructure projects dealing with housing, transport and urban renovation, and created a Direction for Infrastructure Co-ordination (Dirección para la Coordinación de Infraestructura) (DNP, 2016a). The implementation of these projects faced territorial challenges, such as important local resistance in some cases, due, for instance, to the environmental impact of the projects in fragile areas, which highlighted some deficiencies in vertical co-ordination.

Another cross-sectoral approach to investment is the National System of Competition and Innovation (2012), co-ordinated by the Ministry of Commerce, Industry and Tourism and the National Association of Chambers of Commerce, which created regional plans of competitiveness. These plans are designed at the department level by regional commissions for competitiveness (*comisiones regionales de competitividad*, CRC), composed of regional representatives of the public and private sectors. They are supposed to be articulated with the national and local development plans. These CRCs are unevenly powerful and efficient, depending on the department (DNP, 2016a). This integrated competitiveness agenda will be further strengthened through the Productive Development Policy put in place by the DNP at the end of 2014 and approved in a CONPES in August 2016 (CONPES 3865) (Box 3.3). Rutas Competitivas is a programme led by the Ministry of Commerce, Industry and Tourism to stimulate competitive cluster strengthening, in partnership mainly with local chambers of commerce. It has invested COP 11 billion since 2012 to foster 60 clusters in 22 departments. Rutas Competitivas is considered a strategic tool within the current National Development Plan (DNP, 2016a).

Strategic and spatial planning at the subnational level

At the subnational level, departments and municipalities design four-year "local development plans" (*plans de desarrollo territorial*, PDT). These plans are designed at the beginning of each local electoral mandate and are supposed to be articulated with the National Development Plan. This is facilitated by the fact that the NDP is validated before the PDTs are developed, due to different election schedules. For example, the National Development Plan was elaborated in 2014, whereas the PDTs were prepared in the first quarter of 2016, following the 2015 local elections. They will remain valid for the 2016-19 period. The 12-year Land-Use Plan defined at the local level is also supposed to be articulated with the local development plan. Approval of any public investment project at the subnational level is in theory conditioned by its coherence with the departmental and municipal PDT. For all development plans, results and outcome indicators have to be defined, to measure its implementation. However, there is no distinction between outputs and outcomes, which makes evaluation more difficult (see Chapter 3).

Box 3.3. **The Productive Development Policy**

The Productive Development Policy was approved in a CONPES in August 2016 (CONPES 3865). From a diagnosis of fragmentation and weak efficiency of public investment in innovation, the Department of National Planning, together with Harvard University, designed a tool to define the development potential of productive sectors at the municipal and departmental level across the country, with 200 variables taking into account the endowment factors (local context). This analysis will allow the identification of around 20 potential sectors by department, to be discussed with regional commissions for competitiveness so as to select two or three for concentrated intervention focused on the identified market failures and public goods provision to be enhanced at the production unit, production factors or context levels, and corresponding actions to be taken (30 "standard" instruments have already been defined, such as certification, soft skill transfer programmes, innovation vouchers). All national and local policies focusing on productive development, competitiveness or innovation will then have to comply with this action plan. It will include policies by the ministries and entities dealing with education and technical education, trade, industry, agriculture, transport, ICT, etc. From 2017 on, every ministry will have to use this method to prioritise its investments. In order to facilitate its articulation with planning tools, the PDP has been divulgated through the Nuevos Mandatarios programme (Estrategia para el Fortalecimiento de Nuevos Mandatarios) to be taken into consideration within the new local development plans, and the productive sectors supported by the *Contratos Plan* will be prioritised locally. The CONPES 3865 also plans to strengthen the role of the regional commission for competitiveness, better articulated with other territorial institutions.

Local PDTs also include pluri-annual investment plans and *planes indicativos*, that should translate on a yearly basis into the prioritisation and selection of concrete projects in the investment part of the budget (POAI), with defined financing sources. Each project is supposed to go through an *ex ante* appraisal methodology called the General Adjusted Methodology (Metodología General Ajustada, MGA), and to follow the approval process linked to its financing source before being implemented and evaluated (see Chapter 4).

The other key planning tool at the municipal level is the Land-Use Plan, which is valid for 12 years (i.e. a much longer timeframe than the four-year development plans). Municipalities are responsible for their design and implementation. In 2008, all municipalities had a POT. Currently, 81% (894) of the POTs issued between 1998 and 2003 have gone beyond 12 years and need to be renewed (CONPES, 2016). In principle, the POTs are articulated with the corresponding development plans through its execution programme (Programa de Ejecución del POT), which defines the investments to be implemented in the territory. It is included in the local pluri-annual investment plans (PPI).

Challenges and priorities: Linking subnational planning to budgeting

Under-exploited potential of subnational development plans

Turning strategic planning into effective investment prioritisation is a major challenge for any public investment policy. One of the challenges in Colombia is that subnational authorities consider the planning activity as merely a formal exercise and planning at the subnational level has often been transformed into a bureaucratic activity. The challenges linked to the design and implementation of the PDT and the POT are of uneven magnitude depending on the subnational government, as their capacities differ greatly. In general, local governments do not recognise the importance of the POT and the need to articulate it with the PDT given the fact that it is not recognised as a tool of development financing. Some keys issues in most places are lack of motivation and/or institutional and technical capacity from local governments to use in an integrated manner the PDTs and POTs as strategic tools for defining, implementing and monitoring inter-sectorial investment policy with diverse financing sources.

Many municipalities lack the adequate capacities to design their development plans and lack data on infrastructure needs or rural-urban linkages. Many PDTs lack clear objectives with adequate indicators, which also hamper the evaluation process. In the design phase of local PDTs, many subnational governments have difficulties in building a diagnosis of their needs and defining investment priorities, notably due to weak human resources, combined with high turnover in the weaker municipalities (see Chapter 4). Municipalities lack methodological tools, leading to difficulties to use existing data and to build an integrated strategy (DNP, 2016a). In many cases, the PDT is designed through external contracting, based on a precarious diagnosis, and does not reflect the real political orientations. This leads to "virtual" PDTs not reflecting priorities, and a disconnect with effective budgeting and implementation. Municipal planning bureaus are often focused on urban planning rather than strategic planning, leading to a merely infrastructural approach and not a systemic approach based on local needs and complementarities across sectors. In the implementation phase, this often leads to isolated projects disconnected from any strategy.

The nature of the challenges also depends on the territorial positioning of subnational governments, as some face metropolisation challenges – with or without a legal framework – while others need to connect better with the cities network. The profusion of regulations and the lack of guidelines on planning has hindered the process of consolidation of the POT as promoting investment in the territory. In particular, this problem is caused by lack of integrated approach at the national level and lack of guidance to subnational governments in access to and use of technical, mapping and statistical inputs (CONPES, 2016). In general, the POTs show deficiencies in formulation and implementation of their rural and urban components (World Bank, 2014). Subnational governments face the challenge to better connect their rural neighbourhood to their development.

The tight schedule to design development plans –only two months after the election for local diagnosis and the design process – is also a great limitation. This exercise has to be undertaken straight after the beginning of the new mandate, when the new authorities are not yet familiar with the functioning of the municipalities and have to organise and staff their administration.[1] The short (four years) and not immediately renewable mandates ask for rapid development design to be able to implement concrete projects as quickly as possible. In comparison, the National Development Plan (2014-2018) took almost a year and a half up to its final validation in June 2015. Finally, the fact that departmental and municipal PDTs have to be designed at the same time does not help to take the orientations of the departmental PDTs into account in the municipal ones. However, some subnational governments argue that the fact that municipal and departmental PDTs are designed with the same timing allow for more interaction between them.

Local development plans tend to be disconnected from land-use plans (POTs). Many lack technical rigour, and even those that are technically sound tend to be of limited use in the absence of serious participatory analysis of the issues. In addition, most of the land-use plans are outdated (DNP, 2015b).

The design and implementation of local development plans is overseen by a territorial planning council in each department and municipality, which include representatives from the civil society and the private sector. They lack finances for functioning, leading to weak implementation monitoring. Strengthening the role of the territorial planning councils in the elaboration of the PDT could be considered.

The PDT tends therefore to be seen as a mere theoretical planning exercise by many subnational governments, not connected with political priorities nor effective financing, notably from own revenues or royalties.

This situation is worsened by a funding system where each source of finance (SGP, SGR, national budget) has its own process for project selection and approval, which makes it even more difficult to integrate investment projects within a global strategic framework. This leads to a lack of integration of financing sources within the local development plan's framework. Overall, development plans and the POTs need to be better connected and linked to effective budgeting and execution.

Strong efforts to improve the new generation of local development plans and land-use plans

The Department of National Planning has considerably increased its support to subnational governments in the design of their 2016-19 development plans. The training and support offered by the DNP to candidates for local elections in 2015 and to subnational governments in the beginning of 2016 (Nuevos Mandatarios Program) helped subnational governments to better understand the strategic nature of development plans, even though the schedule remains tight. The Department of National Planning has designed a kit (called "KiTerritorial") to help subnational governments and guide them on the numerous programmes and plans: the NDP of course, but also the POT update, the new *Contratos Plan*, the Integrated Productive Development Policy. The kit is a free access web platform with useful information, guides, videos and virtual technical assistance (see Chapter 4).

Taking advantage of the great number of POTs to be revised in the following months, the DNP plans to support 100 municipalities and 10 departments identified as key for the country's development. Another 300 municipalities will receive international co-operation support (notably from the World Bank) and 89 POTs will be co-financed. This support will come through the Land-Use Plan Program (Programa Nacional de POT/POD Modernos). This new Land-Use Program, which started in February 2016 and has a budget of COP 38 million for 2016-18, has the objective of supporting municipalities in designing and updating their plans with quality technical standards, in order to promote sustainable growth and urban-rural linkages. The programme will co-finance a dedicated unit within each selected municipality to update the POT, and participate in its implementation through capacity building. Rules to establish the programme are currently being validated by CONPES. Rules for the formulation of the POT are defined by law, and its proper implementation and enforcement is to be fostered through the programme. The dedicated units should be in place by December 2016, and the update should last 9-24 months. The departmental land-use plans under discussion (*planes de ordenamiento departamental*, POD) are a new tool, which have not yet been implemented, aiming at strengthening a regional approach of relevant issues regarding land use. They are supposed to set guidelines to be followed by municipal POTs regarding a series of issues of regional relevance, such as connectivity, environment, solid waste management, housing provision policy, productive development and competitiveness policies, and the regional system of education, health and sanitation infrastructure.

An improved connection between subnational planning and budgeting is needed

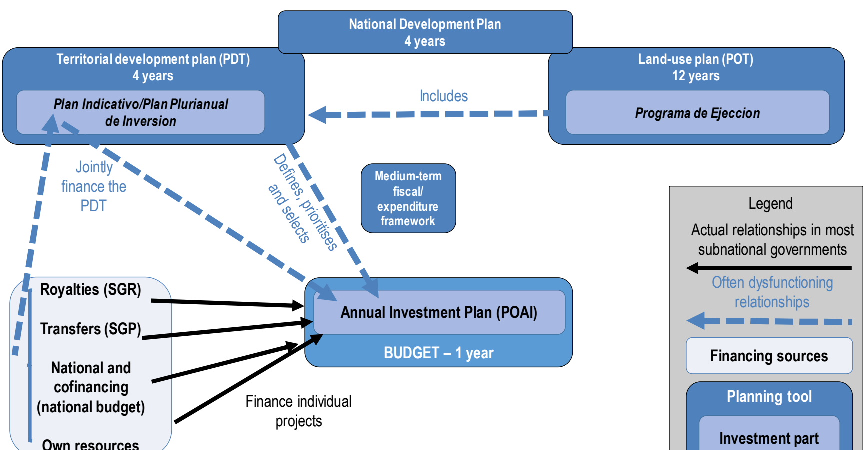
In principle, subnational governments have to design a medium-term fiscal framework valid for ten years and updated each year, which is submitted to their respective assemblies. It displays estimates for the coming year, forecasts for the ten years to come, and shows their compatibility with the budget surplus and public debt objectives. However, this tool is not very widely used by subnational governments. Less than 30% of subnational governments develop such a medium-term fiscal framework (DNP, 2016a).[2] Even when they are developed, medium-term fiscal frameworks are often not directly connected to local development plans. In practice, there is often no direct connection between subnational planning and budgeting. Local development plans are not connected to the medium-term fiscal framework, nor to annual budgets or the selection of projects to be funded by royalties.

Improved PDTs, better co-ordinated with POTs, could significantly help medium-term prioritisation of investment as part of subnational governments' medium-term fiscal framework, but also help the prioritisation of OCADs and of *Contratos Plan*. They could play a significant role in better articulating the diverse financing sources, which so far follow disconnected planning and evaluation approaches. The strategic framework provided by the PDT could be used as input in the decision-making process of the OCADs to select investment projects to be financed by royalties. This would allow using royalties in a more strategic manner. The strategic agreement for the development of the territory in the *Contratos Plan* (Acuerdo Estratégico para el Desarrollo del Territorio) also needs to be better articulated with local development plans. The departments could have a role in scrutinising this.

Overall, local development plans could be the strategic umbrella to guide investment priorities funded by different sources. There is a need to encourage the integration/merging of different sources of funding (royalties, the SGP, taxes, private funding) to finance projects/programmes. This also means moving towards a budgeting system based on outputs instead of inputs of disconnected funding sources, to allow a more integrated approach to planning and budgeting.

Colombia is making progress in that direction by shifting from monitoring differentiated by funding source to a programme-oriented integrated monitoring system that would assimilate the various funding sources (national budget, SGR and SGP mainly) and connect planning to budgeting and execution. The DNP is working on a common framework with indicators to be used in development plans and budgets. In a first stage, the programmes included in the budget will seek to match the development plans programmes and the next development plans will be designed with the objective of being integrated with the budget structure. This new framework is supposed to be applied to the national budget in 2017 and to subnational governments' budgets in 2018 (DNP, 2016a). Future development plans 2020-23 would be fully aligned with the budget structure. This new system would help make significant progress to strengthen the link between planning and budgeting and to strengthen performance monitoring of public investment across the country (see Chapter 4).

Figure 3.1. **Strategic planning at the subnational level in Colombia: Linking subnational planning to budgeting**



Source: Authors' elaboration.

Box 3.4. **Articulating planning and funding: The experience of EU funds**

With a budget of EUR 454 billion for 2014-20, the European structural and investment funds are the European Union's main investment policy tool. National co-financing is expected to amount to at least EUR 183 billion, with total investment reaching EUR 637 billion.

The post-crisis period has provided additional motivation for reforming the way the European structural and investment funds are planned and used. In a climate of declining overall investment, maximising the impact of these funds is a top priority, especially as they provide the majority of public investment in many countries.

Box 3.4. **Articulating planning and funding: The experience of EU funds** (*continued*)

Following the lessons learned from previous programming periods and taking into account the need for better use of European structural and investment funds, the 2014-20 regulations introduced several key reforms. There is a clear move towards a more focused policy approach, a stronger results orientation, solid framework conditions for investments, better co-ordinated use of funding through the common strategic framework, and improved links between EU priorities and regional needs.

Member states are required to draw up and implement strategic plans with investment priorities covering the five European structural and investment funds. These "partnership agreements" are negotiated between the European Commission and national authorities, following their consultation of various levels of government, representatives from interest groups, civil society, and local and regional representatives.

Partnership agreements outline each country's strategic goals and investment priorities, linking them to the overall aims of the Europe 2020 strategy for smart, sustainable and inclusive growth.

Once the partnership agreements have been adopted, the European Commission and the national authorities agree on programmes, setting out the priorities for each country, region or policy area concerned.

Combining different funds to finance local investment projects

- Integrated territorial investments make it possible to combine funding from different European structural and investment fund programmes to support the implementation of territorial development strategies. Twenty member states will use integrated territorial investments in areas ranging from deprived urban neighbourhoods to metropolitan areas, from cultural heritage routes to sub-regions hit by economic restructuring.
- Community-led local development empowers local action groups to implement strategies creating jobs and growth and enhancing social inclusion by combining different EU funds. Over the programming period, multi-fund community-led local development is supported with more than EUR 12 billion. In rural development, more than 2 500 local strategies will reach out to half of the EU's rural population, while the European Maritime and Fisheries Fund will support some 280 such strategies in coastal and inland communities. Seventeen member states will support local development strategies in cohesion policy.

Source: European Commission (2015), "Investing in jobs and growth: Maximising the contribution of European Structural and Investment Funds", http://ec.europa.eu/contracts_grants/pdf/esif/invest-progr-investing-job-growth-report_en.pdf.

Reduce the fragmentation of royalties

Royalties and OCADs should be better connected to the wider investment system

The General Royalties System (SGR) was heavily restructured in 2012 (see Chapter 2) to act as a main tool to promote the development of all regions. To accompany this reform, another form of vertical co-ordination was introduced: the collegiate bodies of administration connected with the reform of royalty payments (*órganos colegiados de administración y decisión*, OCADs) in each department and municipality. The OCADs are responsible for defining, evaluating, making feasible, prioritising according to a series of criteria (viability, impact, sectorial or geographical priority, etc.), approving investment projects and appointing executing agencies for them. There are OCADs at different levels of government: 6 regional, 31 departmental, 9 linked to *corporaciones autónomas regionales*, 1 for ICT and 978 at the municipal level, for a total of 1 025. Municipalities with less than 2 000 in royalty income can decide to be part of a departmental OCAD or start their own OCAD. The OCADs decide on which projects to finance. They are constituted from representatives of the three levels of government, each one having a vote, and projects are approved by simple majority. This system allows local interests to outweigh the national level if subnational actors agree with each other. A specificity of the royalties' system (SGR) is that it earmarks 2% of the funds for the SGR operation and 1% for monitoring, control and evaluation.

Six regions have also been created to facilitate the territorial distribution of the SGR's resources (Caribe, Centro-Oriente y Bogotá, Eje Cafetero y Antioquia, Llano, Pacífica and Centro-Sur-Amazonía) (defined previously within the SGR system) and 145 sub-regions, with specific data collection, diagnosis and objectives. This is an important step towards analysis and investment at the relevant functional scale, but it has yet to translate into concrete investment, with the key issue of the project holder, as there is no institutional structure at this scale).

The royalties reform is a major achievement to help reduce regional and social disparities in Colombia (see Chapter 2). Its implementation was helped by the fact that normative adaptation was quick and that the reform was accompanied by strong capacity building through technical assistance provided by the programme (DNP, 2016a). The system specifically allocates 2% of total funds to capacity-building activities. Part of these funds is directly allocated to strengthen the capacities of the OCADs and of planning units within departments and municipalities. As a result, in 2013-14, the system allocated approximately USD 30 million to enhance the planning capacities of territorial entities. This represents about USD 25 000 per municipality and USD 64 000 per department (OECD, 2014b).

Figure 3.2. **The six planning regions identified as part of the 2012 royalties reform**

Source: Department of National Planning.

Challenges are mainly linked to the atomisation of royalties and to the disconnection between the governance of the royalties system and the subnational planning system for investment. Another important systemic challenge is linked to the fact that there is a separate budget for royalties, disconnected from the national budget. It is a specific budget defined for two years, the latest being for 2016-17. This contributes to the disconnection, as royalties funds are totally disconnected from transfers – despite the connections between capital and current expenditures, and to the under-exploitation of local investment plans for the planning of projects to be financed by royalties (see Chapter 2).

Royalties are supposed to encourage regional-scale projects, but because of the high number of OCADs (1 025), projects financed by royalties are atomised into thousands of projects. This fragmentation means that large-scale infrastructure projects with higher social returns are not prioritised. In some cases, municipal OCADs are set up for a very small amount of investment and number of projects. Even if it is clear that not all royalties have vocation to finance projects of regional impact, only 5% of the projects approved had a regional dimension (DNP, 2016a). Even considering the fact that the value of the projects financed by regional funds is six times higher than the average value of the "local" projects, this proportion seems very low.

Box 3.5. **Limited regional dimension of projects financed by royalties**

Projects funded by SGR direct assignments with a local impact amount to 87%. Most of the 10 000 projects financed so far do not have a regional scale, even if theoretically around half of the funds are earmarked for "regional projects", as in principle they benefit at least two municipalities for the Regional Compensation Fund and two departments for the Regional Development Fund, each accounting for roughly a quarter of SGR investment funds. However, in October 2015, only 5% of projects (465 out of 8 985) and 15% of the COP 26.8 trillion approved had a regional dimension (DNP, 2016a). Moreover, the regional aspect of some of these projects is often questionable (DNP, 2016a). On average, projects financed by royalties between 2012 and 2015 accounted for less than COP 3 billion (USD 1 million) per project (SGR, 2016).

Some progress is being made, however, in the context of the 2014-2018 NDP. Indeed, the DNP is now allowed to propose regional projects to the OCADs. The DNP also manages a fund for co-financing regional projects led by several subnational governments, but it is limited to *Contratos Plan* (the DNP finances 12% of it). It seeks to make the administrative, budgetary and contractual processes required for the approval and implementation of projects included in the *Contratos Plan* more efficient. Although the number of OCADs was not reduced – and has even increased as in 2016 there are 39 new ones, the number of sessions and the way they are organised has changed, as sessions can happen with groups of OCADs, in a sub-regional way.

Even if reducing their number might be complicated, the functioning of OCADs should be rationalised. The central government could consider putting in place a calendar for OCAD meetings with the possibility to hold additional sessions when there are a large number of investment projects piling up in the same territory. Moreover, the calendar set for OCADs could also take into account the annual budgeting process for subnational authorities, to facilitate the co-ordination between overall revenue and investment. The requirements for project formulation and approval of the SGR projects might also be differentiated according to a project's size and complexity (see Chapter 4).

Investing at the relevant scale: Horizontal co-ordination across jurisdictions

There are 1 101 municipalities in Colombia (Figure 3.3). The size of Colombian municipalities is relatively large on average (43 370 inhabitants on average compared to 9 570 on average in the OECD), and 25% of these municipalities have less than 2 000 inhabitants (compared to 31% on average in OECD countries). Like in many countries, horizontal co-operation across jurisdictions is a top priority to support more strategic investment – particularly at the metropolitan scale and for smaller municipalities in rural areas. A specificity in Colombia is that the urban system in characterised by relatively small functional urban areas, with the population concentrated in the city centre and few limited commuting areas (Sanchez-Serra, 2016). Urban-rural linkages are generally weak, leading to a low spillover effect (OECD, 2014b). Improved connections between core cities and their surrounding areas would contribute to enlarge local labour markets, strengthen agglomeration economies and support productivity. This requires not only a strong infrastructure investment effort, but a focus on urban-rural linkages and a strong support to mechanisms of co-operation across jurisdictions to develop joint investment strategies.

As in many countries, co-ordination between jurisdictions is a recurrent concern, as for many development and investment issues the relevant scale goes beyond administrative boundaries of a single jurisdiction. In particular, urban and metropolitan governance is critical to exploit positive externalities across jurisdictions and make the most of agglomerations economies, while at the same time mitigating negative externalities linked to the concentration of population (OECD, 2015c). Urban-rural linkages are also critical.

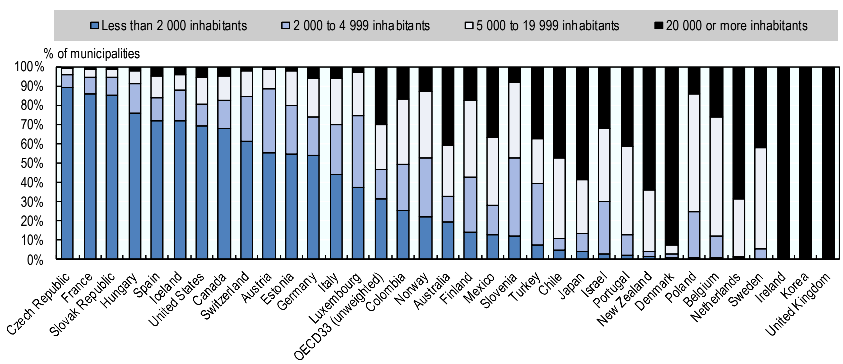
Colombia has made progress since 2010 to foster inter-jurisdictional co-operation on investment and public service delivery. Metropolitan governance is also more advanced than in many OECD countries. However, important challenges remain to move from a pure planning exercise to effective co-ordination across municipalities for investment projects. One of the reasons for this is that co-operation remains voluntary, without any financial incentive to support such co-operation.

New types of associations of subnational governments, but little used

Important progress has been made for co-operation across jurisdictions since 2011 and the adoption of the Organic Law on Land Use Planning (LOOT). Until the LOOT, there were few legal frameworks for subnational government association, except for metropolitan areas, which were created in 1968 and reformed by Law 1625 in 2013. The LOOT defined 12 associative figures at various levels and with diverse functions, which can give legal support for territorial association, with mutualisation of administrative, technical and financial resources (DNP, 2016a).[3]

The LOOT sought to reinforce the regulatory framework of municipal associations. There are currently 11 formalised associative structures at the municipal level and 14 are currently being formalised (Table 3.1). One example, considered as a good practice of inter-municipal co-operation in a rural area, is the Association of Municipalities of Catatumbo, Provincia de Ocaña and Sur del Cesar. Created in 1993, this association of 14 small municipalities aims at promoting the planning and development of the sub-region through joint processes (management of agricultural loans, technical assistance to producers), projects (rural electrification programme, construction of an irrigation district, cacao project) and the provision of public services (training of public civil servants). It also plays a role of interlocutor between the municipalities and the departmental and national governments. Around Bogota, 23 municipalities also created an association.

Figure 3.3. **Municipalities by population size, OECD countries and Colombia**



Sources: OECD (2015e), "Subnational governments in OECD countries: Key data, 2015 edition", www.oecd.org/gov/regional-policy/Subnational-governments-in-OECD-Countries-Key-Data-2015.pdf; DANE (2016) for Colombia.

Table 3.1. **Type of association of subnational governments**

Type of association	Formalised associations	Initiatives (not formalised)	Total
Management and planning regions (RPG)	1	1	2
Administrative and planning regions (RAP)	0	1	1
Special Administrative Planning Region (RAPE)	1	0	1
Association of municipalities	2	4	6
Metropolitan areas	6	0	6
Association of metropolitan areas	1	0	1
Administrative and planning province (PAP)	0	8	8
Total	11	14	25

Source: DDTS-DNP (2016).

Overall, municipal associations remain limited so far. This is notably due to a lack of incentives (mainly financial) and competence for designing and implementing regionally co-ordinated investment, to overcome reluctance to complex and potentially costly co-ordination processes. Indeed, associations have to be financed through members' resources (DNP, 2016a). There are also difficulties in identifying common issues to be solved through common investment. Their reality and strength often depend on personal links among local authorities, which are fragile and may disappear at each election. In general, when there is co-operation between subnational governments – for instance, access to the SGR regional funds, it is generally done on an ad hoc basis, not through a formal association. The experience of France, which has put in place specific financial incentives to promote inter-jurisdictional co-operation, might be of interest to Colombia (Box 3.6). In Italy, a recent law from April 2014 established new financial incentives for mergers and union of municipalities (Box 3.6).

The government might consider providing financial incentives to support horizontal associative schemes across municipalities and departments, for example through matching grant/co-financing projects between the national government and associations of subnational governments and their entities. Such associations could also promote joint procurement. They could have access to royalties revenues. Finally, associations of municipalities and cities could have the possibility to establish and finance joint cadastres, as recommended by the Association of Capital Cities, in order to assume jointly the management of the cadastre, for efficiency reasons and economies of scale if done in partnership.

The LOOT also promotes two new types of institutions for regional planning: the administrative and planning regions (RAP in its Spanish acronym)[4] and the management and planning regions (*regiones de planeación y gestión*, RPG). The RPGs are a mechanism of co-operation between subnational governments (as well as the central government) to handle investment projects with regional impact. In that perspective, they are in charge of planning and executing the funds assigned from the royalties through the Regional Development Fund. However, the operationalisation of these associations remains limited so far. The only RAP that exists formally is the RAPE (Administrative Planning Region Especial). It covers the Region Central (gathering Cundinamarca, Bogota, Tolima, Boyacá and Meta) and is active in regional-scale planning (environmental and competitiveness issues). Other RAPs are currently being structured (like Pacífico, Caribe, Oriente). Some RPG are also being formalised (around Cali, Santander, Grupo de los 8). Planning regions could be further reinforced as they are key co-ordination tools. The central government may co-finance strategic investment projects with the RAPs.

Regional co-operation and its results should be analysed and evaluated on a regular basis at the national level to allow monitoring, promote learning and disseminate good practices.

Box 3.6. **Financial incentives for cross-jurisdictional co-operation**

France

- France has more than 36 000 communes, the basic unit of local governance. Although many are too small to be efficient, France has long resisted mergers. Instead, the central government has encouraged municipal co-operation. There are about 2 145 inter-municipal structures with own-source tax revenues aimed at facilitating horizontal co-operation; 99.8% of communes are involved in such structures. Each grouping of communes constitutes a "public establishment for inter-municipal co-operation" (EPCI). The EPCIs assume limited, specialised and exclusive powers transferred to them by member communes. They are governed by delegates of municipal councils and must be approved by the state to exist legally. To encourage municipalities to form an EPCI, the central government provides a basic grant plus an "inter-municipality grant" to preclude competition on tax rates among participating municipalities. The EPCIs draw on budgetary contributions from member communes and/or their own tax revenues.

Italy

- At the sub-regional level in Italy, there is a long tradition of horizontal co-operation among municipalities, which takes the form of *Unione di Comuni*, intermediary institutions grouping adjoining municipalities to reach critical mass, reduce expenditures and improve the provision of public services. A recent law from April 2014 established new financial incentives for mergers and unions of municipalities. Functions to be exerted in co-operation include all the basic functions of municipalities. All municipalities up to 5 000 inhabitants are obliged to the associated exercise of fundamental functions.

Source: OECD (n.d.), Effective Public Investment across Levels of Government Toolkit, www.oecd.org/effective-public-investment-toolkit.

Box 3.7. **Regional autonomous corporations**

A specific regional figure that is worth mentioning is the autonomous regional corporations (*corporaciones autónomas regionales*, CAR), created in 1993 within the National Environmental System in charge of implementing locally the environmental policy set by the government. The 33 existing CAR (theoretically distributed by catchment area, in practice often aligned with the departments' limits) are autonomous and raise 90% of their revenues from their own resources (environmental tax, authorisations, concessions, fines). They manage the natural resources within their territory, control the enforcement of environmental regulation and implement conservation projects, often together with departments. They are theoretically independent from national and local political influence, but the reality is sometimes less clearly defined.

Strengthening metropolitan governance

Successive laws in Colombia have strengthened metropolitan governance and several metropolitan areas (like Medellín or Bucaramanga) have today more competencies or access to resources than in many OECD countries. Metropolitan areas were recognised as early as the 1968 constitutional reform, but few of them were implemented in practice until the early 2010s. To date, the six existing metropolitan areas are Barranquilla, Bucaramanga, Cúcuta, Valle de Aburrá (Medellín), Centro-Occidente (Pereira) and Valledupar. Most of them were created in 1980-81 (except for Cúcuta [1991] and Valledupar [2005]), and they have been recognised as "administrative units" by the 1991 Constitution. Metropolitan areas are formed on a voluntary basis with the aim to promote the co-ordination of territorial development and public services provision across municipal boundaries.

The 2011 LOOT (LOOT 1453, Article 25) established a special tax regime for metropolitan areas. The 2013 law (1625) strengthened the legal framework for co-ordination of metropolitan areas, establishing new conditions for the creation, operation and financing of metropolitan areas. Metropolitan areas are governed by a metropolitan board (*junta metropolitana*) consisting of the mayors and a number of member municipalities as well as the governor of the department in which the metropolitan area is located. Metropolitan areas have access to various financing sources, including transfers from national, departmental and municipal budgets; betterment levies collected from metropolitan development projects; taxes (including an environmental surtax on property tax); user charges and fees related to public service provision; borrowing; and a gasoline surtax (OECD, 2015d). They may take over the competences of CAR on environment for the metropolitan area, together with 50% of their revenues on their territory (mainly environmental surtax on property tax).

Metropolitan areas are of uneven strength. Well-established metropolitan areas, such as Valle de Aburrá (Medellín) or Bucaramanga, can be considered as good practices of successful co-ordination (Box 3.8). Other metropolitan areas are less integrated, such as Barranquilla or Cúcuta. Overall, fiscal integration and the taxing power of metro areas remain limited. In addition, metropolitan areas are not recognised as "territorial entities" by the LOOT.

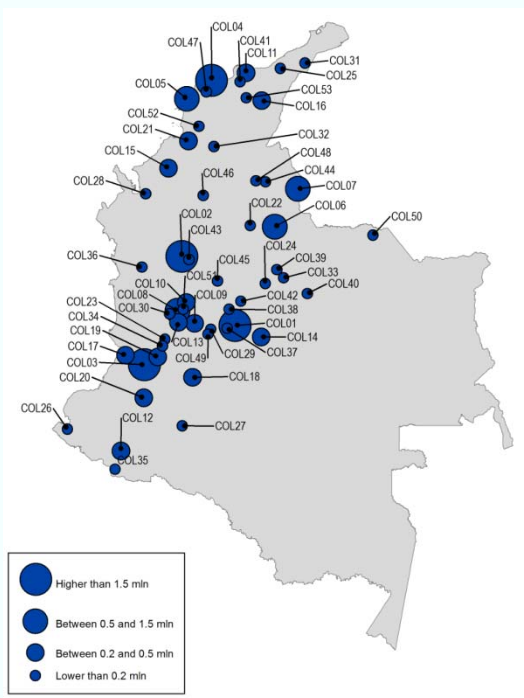
Box 3.8. **Metropolitan areas identified in Colombia**

Colombia's *Misión para el Fortalecimiento del Sistema de Ciudades* identified 18 urban agglomerations and the OECD, using another methodology, 8 metropolitan areas of more than 500 000 inhabitants.

The OECD, using a common methodology applied to 30 OECD countries, has identified 53 functional urban areas (FUAs), of which 8 metropolitan areas of more than 500 000 inhabitants; many of these urban areas coincide with the 56 urban areas identified in Colombia through the *Misión del Sistema de Ciudades* methodology. According to the OECD methodology, the urban system in Colombia is characterised by relatively small functional urban areas, with the population concentrated in the city centre and few limited commuting areas.

These are FUAs with a "commuting zone", i.e. surrounding municipalities with at least 15% of the workforce commuting to another city centre of the metro area. Forty-five other FUAs were identified, but with no commuting zone (Sanchez-Serra, 2016). There are only six official metropolitan areas to date, excluding major urban areas such as the capital city Bogota.

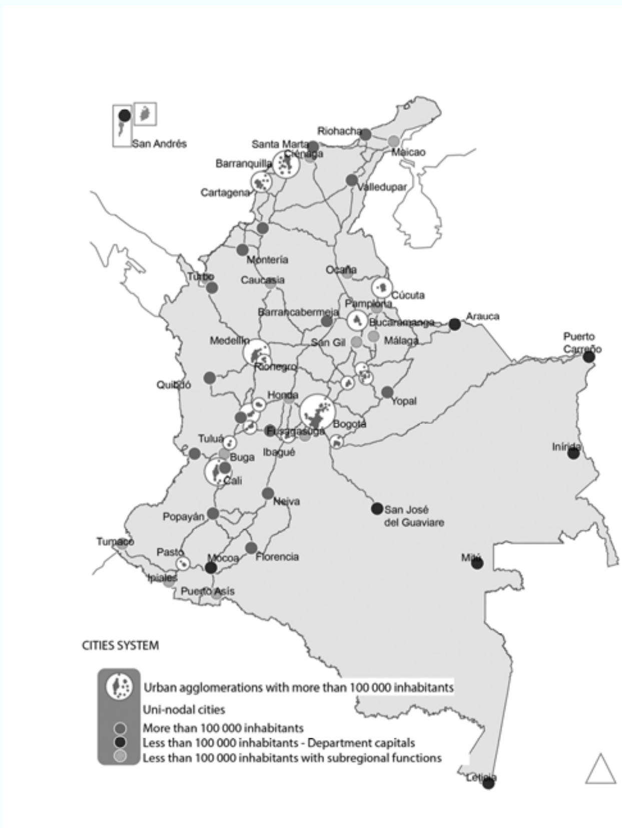
Figure 3.4. **Functional urban areas by population, Colombia**



Source: Sanchez-Serra, D. (forthcoming), "Identification of the national urban system in Colombia".

Box 3.8. **Metropolitan areas identified in Colombia** (*continued*)

Figure 3.5. **Urban agglomerations identified by Colombia in the *Misión para el Fortalecimiento del Sistema de Ciudades***



Source: DNP (2016).

Besides, and most importantly, many of the larger Colombian conurbations, such as the capital city Bogota, Cali or Cartagena, are not structured as metropolitan areas. There are several explanations for the difficulties in structuring efficient metropolitan areas, among which the fear of mayors of losing powers, strong internal disparities between the municipalities or the lack of incentives (financial in particular).

Box 3.9. **Examples of good practices of metropolitan co-operation: Medellín and Bucaramanga**

The metropolitan area of Medellín (Valle de Aburrá) comprises ten municipalities including the town core Medellín, representing 58% of the population of the department of Antioquia (almost 3.7 million inhabitants) and 67% of its GDP (Fitch Colombia, 2014). The metropolitan area of the Valle de Aburrá was formed with the objective of promoting, planning and co-ordinating the development and service delivery of its member municipalities. To date, the metropolitan area has defined an Integrated Metropolitan Development Plan which aligns municipal territorial plans (POTs) and a transport plan and is active in environment and housing development. The metropolitan area acts as an environmental authority and has created a Metropolitan Environmental Council which takes care of water resources management, waste collection and management, and emission control from industry and transport. It has created a transport authority in charge of mass transit, in particular of the bus, rail, metro and metrocable systems in the Medellín area. The metropolitan area also promotes co-ordination across levels of governance to align development objectives. For example, a voluntary agreement has been signed between the Governor's Office of Antioquia, the metropolitan area and the municipality of Medellín – a group called the "Comisión TriPartita". Financial management of the Valle de Aburrá metropolitan area is considered remarkably solid for a voluntary association (World Bank, 2012). The metropolitan area uses almost every possible source of financing in the framework of existing laws to generate revenue, in particular an environmental surtax of 2 per thousand on the property tax, which provided 44% of total revenue in 2013. Contributions from the member municipalities amounted to 22% of total revenue, the major part coming from the city of Medellín and representing 85% of all municipalities' contributions (Fitch Colombia, 2014).

The metropolitan area of Bucaramanga, composed of four municipalities with a population of approximately 1.1 million, i.e. half of the department of Santander, is also a widely cited example of effective metropolitan co-ordination on social and economic development issues. Since the creation of the metropolitan area in 1981, quality of life and social indicators have shown marked improvement across member municipalities, with a notable decrease in poverty. There is a high degree of economic integration within the metropolitan area, led by a clear effort to consolidate a common market. However, this integration is not reflected in environmental and planning issues, which are not co-ordinated, thus having negative repercussions for the entire area, in terms of pollution for example (World Bank, 2012).

Source: OECD (2015b), "Accession RDPC briefing note for Colombia", unpublished.

Improved metropolitan governance in Bogota, which has for decades struggled with its public transport system, would be of benefit for the entire country. For the objective of the 2014-2018 NDP of building a new metro in Bogota to be successful, the national government is playing an important role in fostering the creation of the Regional Mobility Authority, as a means of building capacity for managing the region's transport system at the metropolitan scale. Germany's "communities of transport" (Box 3.10), particularly the transport authority in Frankfurt, could be a useful example for the Bogota metro region. It sets transport policy, is in charge of planning, takes investment decisions, sets rates and co-ordinates the 153 public and private operators.

Box 3.10. Strengthening metropolitan governance for transport: The example of Frankfurt

The Rhein-Main Transport Association (Rhein-Main Verkehrsverbund, RMV) is the single authority over public transport in the metropolitan area of Frankfurt. The RMV brings together 3 levels of government: 15 counties, 11 cities and the *Land* of Hesse. It is led by a board where all member governments are represented. Its geographic coverage includes about two-thirds of the *Land* of Hesse and the city of Mainz (outside of Hesse).

The creation of the RMV was facilitated by a former association of municipalities, called Umlandverband Frankfurt (UVF) and created by the *Land* of Hesse in 1975, as a vehicle for inter-municipal policy co-ordination in the region. The UVF had wide-reaching competencies in policy planning and implementation for many specific-purpose functions at the local level. Membership of the 43 municipalities with about 1.6 million inhabitants was compulsory by law. The assembly (*Verbandskammer*) of the UVF consisted of non-elected delegates from member governments. In 1990, the UVF proposed a new expanded transport association that incorporated several smaller transport associations and municipalities that did not belong to any transport associations. Thus, it paved the way for the creation of the RMV in 1995, also supported by federal transfers through the *Gemeindeverkehrsfinanzierungsgesetz*.

The RMV defines metropolitan transport policy and is in charge of planning, investment decisions, price setting and co-ordinating 153 public and private operators (subway, bus, suburban railway, trains). It integrates regional and local transport under uniform and needs-based rules for the entire metropolitan area: one timetable, one price and one ticket. This includes important tasks such as tariff design, scheduling, allocation of transport services to carriers, the development of the network, the tendering of transport services, the assurance of quality and security standards, innovation (e-ticket, mobile ticket, touch&travel, R&D) as well as communication, information and marketing. It ties individual traffic, car-sharing services and the bicycle in its mobility concept, and partners with shipping lines and taxi companies. Similar associations exist in nine other German regions. In terms of number of trips, the RMV holds the fourth position (after Berlin-Brandenburg, Rhine-Ruhr and Hamburg) in Germany. It comprises 42 railway connections with 390 stations and 943 bus routes with 11 900 stops. On average, it handles some 2.5 million passengers per workday, with an average length of travel of 10 kilometres.

Since its inception, the RMV has seen the number of passengers increase by about 25%, from 520 million in 1995 to 708 million in 2013. In terms of revenue per trip, it achieves a top value in Germany, covering its costs at 57%, with the remainder coming from federal regionalisation funds passed through the state budget, and from municipalities via state financial equalisation.

Source: OECD (2015c), *Governing the City*, http://dx.doi.org/10.1787/9789264226500-en.

The Colombian government has still an important role to play in aligning incentives and fostering co-ordination among local governments to build metropolitan areas (Box 3.11). Equalisation mechanisms could be fostered within metropolitan areas to foster solidarity based on a new tax, e.g. linked to a metropolitan competence. Finally, specific contractual arrangements specifically targeting metro areas committed to improve their governance could be envisaged, like City Deals in the United Kingdom.

Box 3.11. **Financing metropolitan structures: The key role of central/federal and state governments**

Financial issues are indeed a crucial element of metropolitan governance reforms. Although they are often perceived as an impediment to co-operation, they can also be the reason, as well as a lever, for co-operation, if metropolitan financial arrangements are well designed and managed. In fact, the metropolitan governance body should provide added value in terms of new financial resources or financial solidarity. It must also improve efficiency, such as by reducing unnecessary duplication in public spending or generating economies of scale.

Because of their size, of their “rurban” characteristics, of the extent and nature of their responsibilities, and of their international positioning, metropolitan entities are subject to both internal (within their area) and external challenges (international attractiveness and competitiveness) that justify specific and innovative financing solutions.

In that context, the primary task of central/federal and state governments is to design and implement an adequate local government fiscal framework, including fiscal arrangements that ensure that local governments’ financial resources are commensurate with the responsibilities provided for by constitution and law (Article 9, Paragraph 2 of the European Charter of Local Self-Government of the Council of Europe) and that sound fiscal rules are in place. Local governments must be sufficiently financed, and in a sustainable manner to fulfil their mandates so that suitable services are rendered to communities. But beyond this fiscal framework, central/federal and state governments should also carry out specific metropolitan finance reforms to consider more effective ways to finance the growing needs of metropolitan areas for infrastructure and services, while accounting for spillover effects and responding to pressing new urban challenges (e.g. related to ageing, migration, social cohesion, climate change).

These reforms should establish appropriate and diversified funding mechanisms and incentives to ensure that metropolitan bodies can be as self-sufficient as possible. They also have a greater ability to raise revenues in principle. Large cities and metropolitan areas are often not treated any differently from smaller cities and towns – but they should be (Slack, 2010). In addition, sound specific transparency and accountability mechanisms should be designed in the particular case of complex metropolitan arrangements (multi-level or inter-municipal structures).

Box 3.11. **Financing metropolitan structures: The key role of central/federal and state government** (*continued*)

In that perspective, metropolitan finance reforms may:

- Provide specific grants and subsidies for metropolitan services or infrastructures, such as transportation, parks, cultural facilities or metropolitan projects, e.g. the Metropolitan Fund in Mexico, EU Structural Funds in Italy and Poland (special contracts), the special fund for traffic infrastructure in Switzerland, special transport funds in the Netherlands for Amsterdam and Rotterdam-The Hague, City Deals in England. Reforms could also allow or facilitate innovative financing schemes such as a multi-level metropolitan fund, e.g. Regiofonds, a special fund of the Groningen-Assen Regional Alliance in the Netherlands, made up each year from the financial contributions of the different partners and subsidised by central government and European grants (OECD, 2014a).

- Grant taxing powers to the metropolitan body based on own-source taxation with a certain leeway over rates and bases (property tax). However, metropolitan areas cannot rely solely on property tax, which provides insufficient revenue to cope with huge metropolitan needs (Bird and Slack, 2013). Therefore, reforms should also consider the possibility of diversifying the tax portfolio besides the property tax, through tax sharing, piggy-backing (e.g. to levy an income tax as a supplement to a national income tax), or the creation of additional taxes directly connected to urban characteristics and metropolitan competences (tax on public transport, environmental taxes, business tax, dog tax, etc.). This would allow an increase in tax receipts to fund complex and increasing demands in metropolitan areas but also to provide both stability (through the property tax) and elasticity (through more dynamic taxes such as income tax, sales or business tax). Some leeway could be also given to metropolitan bodies over rates for some specific taxes (e.g. tourist and hotel taxes).

- Ensure an appropriate legal framework and pricing through user fees which are widely seen as the most appropriate source of revenues for metropolitan areas to finance the operational and maintenance expenses of infrastructure (parking fees, transport fees, fees on other public services – e.g. waste, water, energy). In particular, metropolitan areas may also charge major negative externality (congestion, pollution, road safety, waste of time, quality of life, health and environmental degradations) through "smart taxes" and fees for excessive car use in metropolitan areas. The revenues of congestion charges adopted in London, Seoul, Singapore, Oslo, Milan, Berlin or Stockholm, for example, have been used to finance urban public transport and other urban facilities.

- Ensure that metropolitan areas have access to property income, which can also provide significant resources, such as royalties from the extraction of non-renewable resources and revenues from municipal industrial and commercial companies in the form of dividends. It can represent an important source of revenue in Colombia roughly 40% of own-source revenues (or 24% of total revenues) of Medellín come from dividends from Empresas Públicas de Medellín).

Box 3.11. **Financing metropolitan structures: The key role of central/federal and state government** (*continued*)

- Provide a legal framework and adequate instruments for land-based financing, under the rationale that existing residents of a municipality should not be required to pay for the costs of infrastructure required by new residents. These "development charges" are also a way to discourage urban sprawl.
- Establish a clear legal framework and instruments allowing private actors and financing institutions to be mobilised to diversify sources of funding to build metropolitan infrastructure projects (transport, green infrastructure, utilities, educational, sport and cultural facilities, etc.), in particular through public-private partnerships (PPPs). A legal framework adapted to local projects should be established to regulate, secure, facilitate and stimulate metropolitan PPPs.
- Help municipalities gain greater access to borrowing for financing infrastructure, including access to loans from a variety of actors, direct access to international and national capital markets via bond issue and pool financing.

Source: OECD (2015c), *Governing the City*, http://dx.doi.org/10.1787/9789264226500-en; OECD (2013), "Towards more inclusive growth in the metropolitan area of Aix-Marseille: International insights", https://www.oecd.org/gov/regional-policy/Summary-Aix-Marseille.pdf; Slack, E. (2010), "Financing large cities and metropolitan areas", www.munkschool.utoronto.ca/imfg/uploads/174/enidslack_imfg_no._3_online_.pdf.

Specific tax regimes for inter-municipal groupings or metropolitan areas could be envisaged. Some pilot experiments could be launched in this regard. It should not take resources away from the municipalities, which would be a great disincentive. Establishing an inter-municipal tax regime at the level of inter-municipal groupings could also be envisaged, such as municipal associations. It would be earmarked at the financing of inter-municipal infrastructure projects (e.g. transport, economic development, etc.). At the level of functional urban areas, the taxing power of metropolitan areas remains limited, despite Law 1454 of 2011 which already improved the metropolitan tax system and Law 1625 of April 2013 which strengthened the legal framework for the co-ordination of metropolitan areas and established new conditions for the creation, operation and financing of metropolitan areas. Specific additional taxes directly connected to urban characteristics and metropolitan competences (tax on public transport, environmental taxes, business tax, etc.) could be established. This would allow increasing tax receipts to fund the complex and vast needs of metropolitan areas but also to provide both stability and elasticity.

Vertical co-ordination across the national and subnational governments

Colombia has made significant progress in recent years to improve vertical co-ordination. New co-ordination actors have been included or a new association of capital cities, new tools such as the *Contratos Plan*, and new local institutions for co-ordination, such as tripartite OCADs for the management of royalties. However, the approach remains highly fragmented at the subnational level. Development plans are key tools for vertical co-ordination, but their limited enforcement and connection to the budget are serious weaknesses.

New institutions to support co-ordination

Department of National Planning

At the national level, the Department of National Planning (Departamento Nacional de Planeación, DNP), which has a rank of ministry, is in charge of cross-sectoral, vertical and horizontal co-ordination, in particular for the design and implementation of the National Development Plan. In 2012 it created a General Deputy Direction for Territorial Affairs and Public Investment (Subdirección General Territorial y de Inversión Pública) in charge of fostering articulation between national and territorial planning, between sectors, government levels and financing sources, and to support subnational capacities. The design of the National Development Plan involves a National Planning Council (Consejo Nacional de Planeación) put in place in 1991, and which gathers representatives of the central government, departments, municipalities, private sector and civil society. The council is not involved, however, in the plan's implementation and monitoring. Countries like Australia, Germany and Italy have put in place co-ordination institutions which play an important role in fostering central-local dialogue on investment issues (Box 3.12).

Four associations represent subnational governments and aim at defending their interests, strengthening vertical co-operation at the national level and also co-ordinating their members among themselves: the National Federation of Departments, the Colombian Municipalities Federation (Federación Colombiana de Municipios, FCM), the Colombian Association of Capital Cities created in 2012 for departments' capital cities, and the Colombian Association of Metropolitan Areas. These associations are very active and are the key interlocutors for the central government. The Federation of Municipalities, which gathers almost all municipalities of Colombia, is particularly active.[5] It is consulted by the central government to discuss and give opinions on all matters impacting municipalities, conducting negotiations in some cases. It also serves as a platform for exchange of information and experiences among municipalities and provides legal assistance and municipal staff training.

Box 3.12. **Institutions in charge of the central-local dialogue in Australia, Germany and Italy**

The Council of Australian Governments (COAG) is the main forum for the development and implementation of inter-jurisdictional policy. The members of the COAG are the Prime Minister, state premiers and chief territory ministers and the President of the Australian Local Government Association. The role of the COAG is to promote policy reforms that are of national significance, or which need co-ordinated action by all Australian governments. The COAG meets as needed, usually twice a year, though at times it has met up to four times in a year. Through the COAG, the federal and subnational governments have endorsed national guidelines on public-private partnerships (PPPs), agreed to a national port strategy, and concluded intergovernmental agreements on heavy vehicles, rail and maritime safety.

- Within the COAG, there is the Transport and Infrastructure Council, whose membership is composed of the Minister for Infrastructure and Regional Development along with its state and territory counterparts. While the objective of the Transport and Infrastructure Council is primarily focused around transport issues, there is some overlap with regional development initiatives, given that some of these transport projects occur in regional areas of Australia.
- The COAG is advised and assisted by the Transport and Infrastructure Senior Officials' Committee on infrastructure priorities; the Infrastructure Working Group provides advice and guidance on the co-ordination of infrastructure planning and policy, across governments and the private sector.
- In October 2006, the states established a Council for the Australian Federation, comprising all the state premiers and territory chief ministers. The Council for the Australian Federation aims to facilitate COAG-based agreements with the Commonwealth by working towards a common position among the states, as well as common learning and sharing of experience across states. The council provides a forum for dialogue between states and territories and contributes to the COAG reform agenda through sponsoring policy analysis, collecting best practice policies and contributing to the policy agenda.

Joint Task for the Improvement of Regional Economic Structure in Germany

- In Germany, the Joint Task for the Improvement of Regional Economic Structure was created in 1969 to reduce gaps between regions. It is a joint federal-*Land* framework (financed jointly) used to set a commonly agreed framework for regional economic development and finance direct aid to business and business-oriented infrastructure. A transparent indicator-based system for assessing regional problems; a consensus-based co-ordination framework which allows equal problems to be treated equally; a systematic rules-based approach to awarding or granting aid; facility for co-ordinating EU and national regional policy interests; and the ability to provide a co-ordinating framework for other policy fields with spatial effects. The Joint Task for the Improvement of Regional Economic Structure is jointly financed by the federal government (50%) and the *Länder* (50%).

Box 3.12. **Institutions in charge of the central-local dialogue in Australia, Germany and Italy** (*continued*)

Italy

- Political dialogue and vertical co-ordination between the regional and national governments is ensured through the State-Region Conference, a permanent negotiating arena between central and regional authorities. Created in 1997, this conference brings together Italy's regions twice a month and plays a key role in influencing the national political debate and decision-making processes on issues of regional importance.

Source: OECD (n.d.), Effective Public Investment across Levels of Government Toolkit, www.oecd.org/effective-public-investment-toolkit.

Making the most of co-financing instruments

New co-financing instruments

Efforts to better co-ordinate investment among the three levels of government in a cross-sectoral way led to the introduction in the early 2010s[6] of "*Contratos Plan*", investment programmes in specific areas defined jointly by the national government (which finances most of it), departments and municipalities. Seven *Contratos Plan* were developed as a first step in the 2010-2014 NDP (in 9 departments and 272 municipalities) and 17 are planned in the 2014-2018 NDP until 2018. They focus on lagging regions and on improving road connectivity or service delivery – education, healthcare and water sanitation. While Colombian contracts are inspired by the French "*contrats de projets État-région*", they differ from these in that the French system provides for simultaneous preparation of all the contracts, and each lasts for seven years. The *Contratos Plan* signed so far have different timings (from three to eight years) and have a different territorial coverage: some focus on a department (e.g. Santander); one focuses on a group of departments (Atrato-Gran Darien covering 25 municipalities in the 3 departments of Chocó, Antioquia and Córdoba) and the majority focuses on groups of municipalities. For the seven pilot *Contratos Plan*, parties had to agree to a strategic agreement for the development of the territory. These initial *Contratos Plan* had no clear connection with the local development plans, as they were not designed jointly.

The 2014-2018 NDP extends the use of *Contratos Plan* to ten new territories. The new generation of *Contratos Plan* have a specific focus on peace and post-conflict. They are now called "*Contratos Paz*" (*Contratos Plan para la Paz y el Posconflcito*) and are being developed in the framework of Colombia's post-peace development agenda. They are currently being defined, crossing the strategic importance of the areas for the country (areas affected by conflict and/or suffering from a socio-economic and/or infrastructure gaps) and local demand. They focus on improving road connectivity or service delivery – education, healthcare and water sanitation. They will include long-term infrastructure projects, as well as other smaller development projects. They have a great potential for joint investments that contribute to building peace and, in this regard, other prioritisation variables, as the incidence of armed conflict will be taken into consideration.

Box 3.13. **First generation of *Contratos Plan* in Colombia**

The first generation of seven *Contratos Plan* in Colombia collectively amounted to COP 12.6 trillion, 63-81% of which is financed by the national government. Around USD 3 000 million have been allocated for the first pilot period, 50% of which are already executed. This has so far allowed financing more than 300 projects. In 2013, it represented COP 1.7 trillion, 70.7% of which came from the national budget and 29.3% from local governments (DNP, 2016a).

Source: DNP (2016a), Answers to the OECD questionnaire.

Box 3.14. **New generation of *Contratos Paz***

A new generation of *Contratos Plan* for Peace (*Contratos Plan para la Paz y el Posconflcito*) is being developed in the framework of Colombia's post-peace development agenda. They target in priority the regions the most affected by the conflict. Several new *Contratos Paz* are currently being prepared, including, for example, Norte de Santander, Meta-Caqueta, Guaviare, Putumayo, Bolívar-Sucre and Amazonas. Other requests have been received from the Valle and Coffee regions, and are currently being discussed in the Valle. The amounts are not known yet and will depend on the content of the various plans, but although the precise rate varies in each case, on average the central government will finance around 60% (12% from the Department of National Planning and 48% from line ministries) and subnational governments will finance around 40%. In order to avoid delays in implementation, a Regional *Contratos Plan* Fund has been created, where each plan will have a specific account, to collect the agreed upon funds for the projects from ministries and subnational governments. The new contracts have to be articulated with the National Development Plan and with local development plans. Project definitions and negotiations started at the beginning of 2016. Three new *Contratos Plan* are supposed to be signed before the end of 2016.

Contratos Plan require a great deal of horizontal co-ordination across subnational governments and vertical co-ordination with the central government. With the support of the *Contratos Plan* team of the DNP, subnational governments draw up a list of locally prioritised projects, then match them with national sectorial priorities to arrive at a negotiated agreement on a final list of projects to be financed through the *Contratos Plan*. The timespan of each *Contratos Plan* will vary, and the fact that they do not necessarily match with the local development plan timeframe is seen as an advantage as it guarantees a certain continuity across mandates.

Lessons than can be learned from the pilot experience are that *Contratos Plan* have contributed to capacity building and the development of infrastructure. They also play a role in strengthening trust *vis-à-vis* the central government, especially in remote regions which have benefited very little from state support over the past decades. The most successful contracts are the ones for which governors have mobilised their royalties resources and their political capital (OECD, 2015d).

Although *Contratos Plan* represent clear progress, there are some challenges linked to their implementation. Projects managed through these contracts tend to be highly fragmented. The challenges identified by an assessment conducted by the DNP in 2014 are to better target the spending, reduce the atomisation of projects and focus on projects with more of a regional impact. There are also deficiencies in the projects' design, as projects tend to lack sound technical analysis (DNP, 2016a). The heavy bureaucracy also tends to slow the execution process (DNP, 2016a). Even if *Contratos Plan* are theoretically connected with the local development plans, the first generation plans were agreed upon and designed in 2011, after the validation of the 2010-2014 NDP. The ten new *Contratos Plan* planned until 2018 are more explicitly articulated with the 2014-2018 National Development Plan and associated with the "closing gaps" policy, focusing on areas the most affected by the conflict, and with low economic, social and environmental indicators (DNP, 2016a).

Some adjustments would be necessary to best use this instrument. Processes could be simplified, harmonised and standardised, in particular the timing, which could be better aligned across *Contratos Plan*, to facilitate monitoring. The managing authorities should be better identified, and departments should have a clearer role to co-ordinate the process. Finally, challenges exist to better enforce contracts, since there are no penalties when a contract's objectives are not fulfilled. The experience of the EU performance reserve is in that sense an interesting practice which could inspire Colombia. The implementation of *Contratos Plan* also has significant implications for cross-sectoral co-ordination at the national level. Special attention will need to be paid to horizontal co-ordination across the national government to insure that the key central government players involved in local projects listed in the *Contrato Plan* work together to implement them effectively, efficiently and coherently on the ground.

Other co-financing instruments

The "National Cofinancing System" (Sistema Nacional de Confianciación) created in 1994 was discontinued more than a decade ago, and co-financing is now commonly practiced by subnational governments and line ministries on an ad hoc basis, project by project, depending on the alignment of local and sectorial priorities and on political negotiation. This means that the projects to be financed (directly by the national budget or through co-financing) are mainly chosen by the government (DNP, 2016a), often based on subjective criteria and relative political influence of territories. The local financial counterpart is often an issue (untimely availability of funds).

Since 2014 (Law 1744 of 2014), the DNP has been implementing a scoring system (*Sistema de Puntajes*) that allows prioritizing the allocation of funds for co-financing and royalties based on objective criteria linked to needs. These developments, if they are successfully implemented, would represent a major progress. A first sectoral scoring mechanism was approved in April 2016 for tertiary roads. A similar scoring is being discussed for water and sanitation, housing, etc. The main hindrance to generalising this type of mechanism is the lack of homogeneous and comprehensive data on existing infrastructure and needs. The scoring also might need to explicitly include the question of maintenance costs.

Another important tool to facilitate the access of subnational governments to information with co-financing potential is the Institutional Supply Manual (*Manual de Oferta Institucional*) designed by the DNP. It displays all national sectorial programmes that can be relevant in a territorial approach, including through co-financing mechanisms. Of the 113 national entities analysed, 62 have been identified as having programmes relevant for a territorial approach, and 54 have been included in the manual so far, accounting jointly for COP 26 billion of investment from the national budget. This information is accessible online[7] and regularly updated, and is meant to help subnational governments to design and finance their PDTs, increasing the co-financing potential and medium-term planning.

Box 3.15. **The use of contracts in OECD countries: The case of France, Italy and Switzerland**

Contracts for regional development policy are well developed in the OECD, in federal as well as unitary countries (e.g. Canada, France, Italy, Portugal, Spain). C*ontratos Plan* are multi-year binding agreements between the central government and departments (or group of municipalities) aimed at co-ordinating their multiannual investment agendas among key identified sectors. Their main objectives are to better align objectives, prioritise investment, strengthen co-ordination across the national and subnational levels, and improve subnational capacities.

France

State-region planning contracts (*contrat de plan État-région*) have been in operation since 1982 and are important tools in regional policy in terms of planning, governance and co-ordination. They are characterised by their broad thematic coverage and cross-sectoral nature, with a territorial approach being applied across diverse policy fields, including industrial, environmental and rural issues. The CGET (ex-DATAR) functions as the main national partner of the regions in developing and implementing such planning documents. The President of the Regional Council and Prefect as the representative of the different central government ministries make the contract. The co-financing of interventions is seen as an important co-ordination mechanism.

2007-13 planning contracts: a new generation of state-region contracts was introduced in 2007 alongside the 2007-13 Structural Funds programmes, in order to increase links between French and EU regional policies. The new contracts have the same timeframe as the EU operational programmes, are based on a joint territorial analysis and have integrated systems for monitoring. Similar to the Structural Funds, regions can decide that funding be de-committed 18 months after approval of projects if no commitment has been made. Contracts increased their focus on the Lisbon and Gothenburg agendas. They reflect three priority areas: the promotion of territorial competitiveness and attractiveness, the environmental dimension of sustainable development, and social and territorial cohesion. The emphasis on sustainable development has grown, with a consultation process launched in 2007 (*Grenelle de l'environnement*). Priority is given to soft functions (e.g. education, research and development) as well as infrastructures other than roads.

2014-20 planning contracts: a new generation of state-region planning contracts has been launched for 2014-20. Five topics have been selected: higher education, research and innovation; national coverage by very high-speed broadband and development of digital technologies usages; innovation, promising niches and the factory of the future; multimodal mobility; the environmental and energy transition. As a priority of the government, employment will be treated as a cross-cutting issue in the contracts.

In order to ensure equality between territories within the regions, contracts will mobilise specific resources for priority areas: urban priority neighbourhoods, vulnerable areas undergoing major economic restructuring, areas facing a deficit of public services (rural areas), metropolitan areas and the Seine Valley. Inter-regional contracts for mountainous and fluvial basins will be reconducted. The preparation of this new generation was conducted in two phases: a first phase of strategic thinking and co-preparation between the central government and the regions; a second phase of financial negotiation.

Box 3.15. **The use of contracts in OECD countries: The case of France, Italy and Switzerland** (*continued*)

Italy

Italy has a strong tradition of contractual agreements to commit national and regional public administrations to a common framework of interventions. Programme framework agreements, and the more recent institutional contracts (with longer term horizons, encompassing multiple regions and railroad state companies), are acts signed by the central and regional authorities that define objectives, sectors and areas for infrastructure development. They provide a clear schedule and well-defined reciprocal commitments to be followed by the region and the central administration to develop specific interventions.

Switzerland

Contractual arrangements for regional policy in Switzerland are implemented through a multiannual programme (eight-year period) developed by the State Secretariat for Economic Affairs with cantonal input (OECD, 2014a). The New Regional Policy in Switzerland is largely based on contractual arrangements between the Confederation and cantons to ensure alignment between national and regional programming. A four-year agreement is signed between the different parties. Individual programmes must align to the broader multiannual programme and meet a number of criteria, including evidence of efforts towards sustainable development. The contract lays out the programme's objectives, key milestones, management processes, timetable and financing. In some cases, cantons may be required to return funds if the target is not achieved.

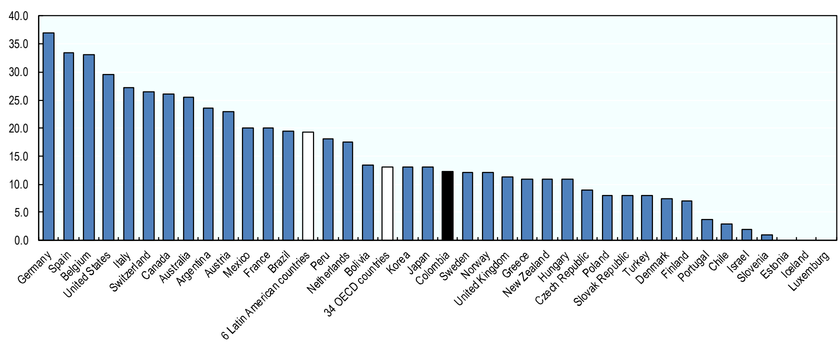
Sources: OECD (n.d.), Effective Public Investment across Levels of Government Toolkit, www.oecd.org/effective-public-investment-toolkit; Charbit and Romano (2016).

Key and under-exploited role of departments

Departments are supposed to play a multifaceted key role for regional development and territorialised public investment, and to be the key players for vertical co-ordination in the interaction between municipalities and the central government. Departments are key partners for municipalities for technical, administrative and financial support, as they are more structured than the weaker municipalities and at the same time aware of local context and closer to their concerns than the national government. As a matter of fact, they are often the institution substituting failing/weak municipalities and co-ordinating regional projects. Most of the municipalities' competences are shared with the departments, which may even substitute the uncertified ones for education or water provision. They have a great role in setting orientations, co-ordinating, supervising and giving financial, administrative and technical assistance to municipalities. Municipalities have to comply with the departmental development plan. Departments are also key players in the royalties system, as one of the three members of the OCAD, but also as one of the main executors for the investment projects. In addition, their role in the co-ordination of *Contratos Plan* is important to mention.

However, despite this important role stated in the Constitution, departments have limited resources to fulfil their responsibilities and respond to the demands from municipalities. Most of their competencies are shared with other levels of government and their own fiscal resources are limited. Even if a major part of royalties funds are displayed as being "departments resources", in reality they are not, since OCADs decide and execute all SGR projects. The size of departments compared to the OECD average size of regions is low (Figure 3.6). Colombia ranks relatively low in terms of "regional power" as measured by the Regional Authority Index, and lower than Peru or Bolivia for instance (Marks and Hooghe, 2016). It is worth noting, however, that Colombia scores higher than many highly centralised OECD countries (Figure 3.6).

Figure 3.6. **Regional Authority Index for OECD and Latin American countries**



Notes: OECD 34 corresponds to the OECD average; 6 Latin American countries corresponds to the average of unitary Latin American countries. This index synthetises the five dimensions of self-rule (institutional depth, policy scope, fiscal autonomy, borrowing autonomy and representation) and shared rule (law making, executive control, fiscal control, borrowing control and constitutional reform). The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Source: Marks and Hooghe (2016), Regional Authority Index, www.arjanschakel.nl/regauth_dat.html.

Box 3.16. **The Regional Authority Index**

The Regional Authority Index is a measure of the authority of regional governments in 81 democracies or quasi-democracies on an annual basis over the period 1950-2010. The sample considers the 35 OECD countries as well as the EU member states, all Latin American countries, some European and Pacific and South-East Asian countries. The dataset encompasses subnational government levels with an average population of 150 000 or more.

Regional authority is measured along ten dimensions: institutional depth, policy scope, fiscal autonomy, borrowing autonomy, representation, law making, executive control, fiscal control, borrowing control and constitutional reform. These intend to capture two domains of regional authority: the "self-rule", which is the authority that a regional government exerts within its territory, and the "shared rule", the authority that the regional government has in the country as a whole.

A regional data set contains annual scores for regional governments/tiers and a country data set aggregates these scores at the country level.

The index does not attempt to identify optimum levels or qualify countries. It is a valuable tool to codify information on the extent to which different tiers of government across the world exert their authority.

Source: Hooghe, L. et al. (2016), *Measuring Regional Authority: A Postfunctionalist Theory of Governance*.

The role of departments as integrators and links between municipalities and the national government should be fostered. Departments could take a more proactive role to support critical projects with cross-jurisdictional co-operation. They should also play a stronger role in the management of royalties. The evaluation of the SGR led by Fedesarrollo suggested that increasing the role of departments for supporting the structuring of projects by municipalities could be instrumental in improving their quality, even though political bias could be a risk in some cases (Fedesarrollo, 2014).

The new tool under discussion – department land-use plans/POD – would also contribute to strengthen a regional approach of relevant issues regarding land use. The departmental land-use plans (*planes de ordenamiento departamental*, POD) are a new tool which have not yet been implemented, but should be designed in parallel with the POT update in 2016-18. The LOOT defined POD as a departmental tool to orient municipal POTs on regional issues. Municipalities would have to comply with it. The PODs will focus on issues like the environment and natural resources preservation, risk management, cultural heritage, regional connectivity/transport, rural development, reducing inequities and territorial integration, and more generally all issues that may have a regional impact (human settlements, housing, water, sanitation and energy, productive infrastructure). As the POT, they will set land-use guidelines and define investment programmes and projects to be implemented, and would be designed in order to inform the POT updating process.

Regional development agencies

The DNP plans to strengthen its deconcentrated units in the six macro-regions and departments. The 2014-2018 National Development Plan mentions the creation of six DNP regional development agencies (RDAs) and 33 departmental agencies, which have yet to be created. Several OECD countries have created such RDAs (Box 3.17). In Colombia, these agencies could be key for giving support to formulating regional strategies and investment policies and accompanying their implementation (going as far as proposing investment projects, as is now allowed for the DNP), and, together with the departmental DNP offices, could be very useful for many issues identified in this report, such as:

- increasing territorial levels of co-ordination and policy integration
- data gathering and support to subnational governments' data production, to inform both national and local levels about local needs and their situation
- supporting subnational governments for PDT monitoring and project design and implementation
- streamlining locally the action of the national government, by centralising information and co-ordinating the line ministries in their actions linked to subnational governments (such as in departmental OCADs, where so far depending on the project, the corresponding line ministry is the main national interlocutor, not always fully dedicated to the issue, which leads to lengthy and complex approval processes) (Fedesarrollo, 2014).

Box 3.17. **Regional development agencies in OECD countries**

Regional development agencies (RDAs) are one governance tool countries have used to organise the delivery of policies targeting specific regions. RDAs of different forms are common in OECD countries. Theoretically, an agency model implies "separateness" and generally a higher set of expectations for performance accountability. The "principal" to which the agency is accountable may be a central or regional government (and sometimes a public-private board), and these models have distinct differences. Most OECD countries have regionally managed RDAs, with a trend towards increasing specialisation in a particular sector, notably business development and/or innovation. Even when RDAs are accountable directly to a region, they are still part of a complex governance landscape involving multiple levels of government. A few countries have nationally initiated RDA networks to support regional development. The choice for central government action is nested in a set of alternatives to address governance challenges, many of which may be used simultaneously.

Box 3.17. **Regional development agencies in OECD countries** (*continued*)

In most OECD countries with a national RDA network, the impetus for creating it was to build capacity at the regional level in a centralised country context. The institution of RDAs or structures of a similar purpose has been driven in many OECD countries by the EU accession process, notably for countries in Eastern Europe, such as Hungary.

A little less common is the development of national RDAs to help organise national interventions for regional development in an already decentralised country. The case of Canada is such an exception. It is the most decentralised country in the OECD with respect to public expenditure, investment and debt. Furthermore, individual provinces and municipalities have their own regional/local development agencies that coexist with the national network. However, it has used RDAs as a way to transition federal action towards a more regionalised approach. The five RDAs play an important role in ensuring that federal policies are tailored to regional economic realities and support improvements in business productivity, competitiveness and growth. This regional perspective on all national policies serves as a regional "proofing" of national action. The United States' Economic Development Administration's regional offices cover areas of a scale similar to those in Canada, with six offices covering the country, but these are not agencies per se, but rather regional offices of a national department (ministry).

In Australia, RDAs are: funded by government, but may also be funded by states, to maintain three- to five-year regional development plans, assist local governments to build projects and get funds, including from the "National Stronger Region Fund", give advice to the national government, increase awareness of Australian government programmes.

One of the goals of an RDA may be to benefit from complementarity of actions across national policy sectors in a given region. The previous English RDA model had multi-ministry financing (six ministries contributed to a single pot) in support of a Regional Economic Strategy. Portugal's commissions for regional co-ordination and development are charged with delivering regional development policy, and are significantly influenced by EU regional policy. As there are no regional governments at this scale, these commissions administer a range of programmes in their coverage area. Although Finland's 15 centres for economic development, transport and the environment are not RDAs per se, they are a form of cross-sectoral decentralised national action to support regional competitiveness, well-being and sustainable development in each region. They therefore cover a wide range of issues from business and industry support (including labour force and skills), transport and infrastructure, and the environment/natural resources.

Source: OECD (2016b), *OECD Regional Outlook 2016: Productive Regions for Inclusive Societies*, http://dx.doi.org/10.1787/9789264260245-en.

Recommendations

Strategic planning

- Strengthen the effective use of local development plans (PDTs) and land-use plans (POTs) as strategic planning tools, better articulated with effective budgeting and implementation.
- Intensify the effort to increase technical assistance to subnational governments for the design of PDTs and POTs and enhance local capacity.
- Use the strategic framework provided by the PDT as input to the decision-making process of the OCADs to select investment projects to be financed by royalties. *Contratos Plan* also need to be better articulated with the PDTs.
- Support the possibility to prepare integrated investment programmes/projects, including financial plans, financed by different and articulated funding sources. The new monitoring system currently being implemented will help integrate the various funding sources (national budget, SGR and SGP mainly).
- Subnational governments need a more adequate time schedule to design PDTs, allowing better diagnosis and priority setting, and better articulation between the national, departmental and municipal levels. This could be partially achieved by extending the process to six months into the mandate, but it may difficult given the short time span of the mandate. A more structural change, that would also allow for a longer term vision from local authorities, would be to allow the re-election of mayors and/or extend their mandate (to six years for instance).

Horizontal co-ordination

- Promote association schemes/planning regions put in place by the LOOT (such as the new association of departments in the Región Central). Provide financial incentives for co-ordinated investment strategies and for operational horizontal associative schemes, for instance through the possibility of contracting projects between the national government and associative subnational government entities, and more broadly speaking access to transfer funds, some of which (within the SGR for instance) could even be earmarked for regional associations. Planning regions could be further reinforced, as they are key co-ordination tools.

- Metropolitan reforms in Bogota, Cali, Cúcuta and Cartagena need to be further encouraged. Improved metropolitan governance in Bogota, which has for decades struggled with its public transport system, would be of benefit for the entire country. Metropolitan areas should be given the status of "territorial entity".
- Specific tax regimes for inter-municipal groupings or metropolitan areas could be envisaged. Some pilot experiments could be launched in this regard. It should not take resources away from the municipalities, which would be a great disincentive.
- Finally, specific contractual arrangements targeting specifically metropolitan areas could be envisaged.

Royalties

- Use the strategic framework provided by the PDT as input to the decision-making process of the OCADs to select investment projects to be financed by royalties.
- Since mid-2015 the DNP has been implementing a scoring system that allows prioritisation by the OCADs of the allocation of funds for co-financing and royalties based on objective criteria linked to needs and in line with the "closing gaps" approach. A sectoral scoring mechanism was also approved in April 2016 for tertiary roads. A similar scoring is being discussed for water and sanitation, housing, etc. The question of maintenance costs should be addressed more explicitly in the scoring system.
- Reduce the number of OCADs and rationalise their way of functioning with greater co-operation across OCADs.
- The calendar set for the OCADs could also take into account the annual budgeting process for subnational authorities, to facilitate the co-ordination between overall revenue and investment.
- The requirements for project formulation and approval of SGR projects might also be differentiated according to a project's size and complexity.

Vertical co-ordination

- Enhance the role of departments as regional integrators through investment projects, strengthening their mandate to incentivise regional co-operation for investment projects (financed through the SGR or other sources), as technical support and political facilitator. Departments could take a more proactive role to support critical projects with cross-jurisdictional co-operation.

- Departments could also play a stronger role in scrutinising the co-ordination of land-use and development plans and the new tool under discussion – departmental land-use plans – would also contribute to strengthen a regional approach of relevant issues regarding land use.
- *Contratos Plan* – and the new *Contratos Paz* – which require a great deal of horizontal co-ordination and vertical, need to be further developed and supported. They are key instruments to create powerful positive incentives for the evolution of subnational stakeholders' "behaviour", such as to promote municipal cooperation and strengthen the capacities to develop long-term development strategies. Incentives could be set for the contract enforcement, for example to allocate part of the funding based on good performance (performance reserve, on the model of Italy or the EU); and part of the funding could be dedicated to projects with a regional impact. The timing of these contracts should be standardised in order to facilitate monitoring and capacity building.
- The National Planning Council could be strengthened to be involved in the implementation and monitoring of the National Development Plan.
- Colombia could introduce pilot experiences of regional management offices and departmental management offices in a small number of regions from which lessons could be learned, before generalising the experience.

Notes

1. On the other hand, the newly elected officials are supposed to have carried out their own diagnosis prior to the elections, to set up a binding government plan they have to register.
2. The Financial Kit developed as part of the KiTerritorial, jointly between the DNP and the Ministry of Finance, includes guidance to develop a medium-term fiscal framework.
3. Áreas Metropolitanas, Asociaciones de Departamentos, de municipios, de Distritos Especiales, de áreas metropolitanas, Provincias Administrativas y de Planeación (PAP), Regiones de Planeación y Gestión (RPG),

Regiones Administrativas y de Planificación (RAP), Regiones Administrativas y de Planificación Especial (RAPE), Asociaciones de Corporaciones Autónomas Regionales, Alianzas Estratégicas de Desarrollo Económico con País fronterizos, Alianzas Estratégicas de Orden Económico, Centros Provinciales de Gestión Agroempresarial (CPGA) and Comités de Integración Territorial (CIT).

4. The RAPs are an association between two or more adjacent departments whose purpose is the socio-economic development of a specific territory. The RAPs have a legal status and manage their own resources. The central government may co-finance strategic investment projects with the RAP.

5. Created in 1988 after the first election by universal suffrage of mayors with the technical support of the Spanish Federation of Municipalities and Provinces, it regroups almost all municipalities of Colombia.

6. *Contratos Plan* were first introduced in the 2010-2014 National Development Plan and then in the LOOT (2011). They started to be operational in 2012.

7. ddtspr.dnp.gov.co/MOI

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Chapter 4.

Strengthening subnational capacities for effective public investment in Colombia

The second pillar of the OECD Principles for Effective Public Investment across Levels of Government *focuses on the required capacities for an efficient public investment and on the means to strengthen them. Capacity building for subnational public investment goes beyond a narrow approach restricted to human resources management or workforce improvement activities. The low level of capacities in more than two-thirds of Colombian jurisdictions is probably one of the most important bottlenecks for effective public investment. This chapter will illustrate the rationale on strengthening capacities, address the current levers to support subnational capacities in Colombia, and identify and develop policy recommendations to go further in this area.*

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Introduction

Capacity building for subnational public investment goes beyond a narrow approach restricted to human resources management or workforce improvement activities. The second pillar of the *OECD Principles for Effective Public Investment across Levels of Government* focuses on the required capacities for an efficient public investment and on the means to strengthen them. The Recommendation defines these capacities as the institutional arrangements, technical capabilities, economic resources and policy practices that affect public investment. Capacity development can have the short-term goal of improving specific practices; however, it should have the long-term objective of improving the quality of key government institutions.

The low level of capacities in more than two-thirds of Colombian jurisdictions (DNP, 2016a) is probably one of the most important bottlenecks to effective public investment. Strengthening the support to subnational governments to deal with the diagnosis and strategy design of investment projects, formulation and implementation, and monitoring process, remains one of the key challenges. Colombia has taken important steps to address the capacity gap, in particular supporting improved *ex ante* appraisals and *ex post* performance monitoring, improving technical capacity building and engaging with stakeholders during public investment processes. This chapter will illustrate the rationale for strengthening capacities, address the current levers to support subnational capacities in Colombia, and identify and develop policy recommendations to go further in this area.

Strengthening the capabilities of public officials involved in public investment

Defining, structuring, implementing, operating and monitoring public investment requires a very diverse set of capacities. Subnational capacities – institutional arrangements, technical capabilities and policy practices – should be an enabler to achieve important goals at different stages of the investment cycle. Capacity challenges usually vary largely across countries, thus requiring tailored approaches to specific needs. This is particularly true in Colombia, where subnational capacities, in particular at the municipal level, vary greatly across the country. The most important challenges are linked to the relatively small size of the subnational public sector, high staff turnover, low wages and the political, rather than technical, profiles of executives in municipalities.

Large disparities in institutional and management capacities across Colombian municipalities

Capacity challenges in Colombia vary strongly across municipalities. To assess the capacity gap at the local level, the Department of National Planning (DNP) has developed an innovative index that allows a measurement of the performance of municipalities along four dimensions: effectiveness, efficiency, compliance with legal requirements and management (see below). As for the 2013 results, the index ranges from 81 points (out of 100) in Bogota to less than 31 points in the department of Vichada and in the Orinoquía region, with a national average of 63.4 points. The 2014 results show an improvement of municipal performance; 57% of the municipalities improved and 20% of them where in the upper category "*sobresaliente*" compared to 17% in 2013. Even if it is not possible to establish a direct correlation between the level of development of municipalities and their institutional capacity, not surprisingly the lowest scores (below 55 points) are found in the ten departments where poverty is the highest or in post-conflict areas (OECD 2015a).

Shortage of skilled workforce is a bottleneck for the design and implementation of investment projects at the local level. While there is no precise quantification of subnational administrative staff, Colombia has a small public sector workforce, both at the national and subnational levels in OECD perspectives (1.16 million public servants). This situation is notably explained by externalisation of certain functions such as healthcare workers who are employed as private contractors, staff restrictions and fiscal pressures which led to a freeze in payrolls in 2000 (OECD, 2013b). At the subnational level, Colombia counts almost 495 000 public workers, i.e. 43% of the total public workforce, with teachers accounting for the bulk of this employment (68% of the subnational government workforce and 39% of the total public workforce (OECD, 2013b).

Despite some flexibility introduced in 2012 to the municipal code for hiring staff, there are still important constraints. For example, the legislation limits the increases in operating costs (especially for the municipalities which have less than 30 000 inhabitants) without considering the needs of new staff and qualified skills to perform their duties and the new assignments that have been transferred to them[1] (OECD, 2014a). Subnational staff expenditures represented 46.9% of total public staff expenditure in 2012 while in the OECD this figure represents 63.3%, placing Colombia in an intermediary position among OECD countries, between Austria (45.0%) and the Czech Republic (48.6%). Municipal employment has not quantitatively nor qualitatively evolved in parallel to the devolution of competences. Given the challenges at stake in terms of local service delivery and infrastructure development, this relatively limited size of subnational public employment has an incidence on the design of policies, notably in the planning phase of projects (OECD, 2014c). To improve the management of subnational staff, Colombia needs to develop mechanisms to quantify subnational public employees to be able to get a clearer picture of the gaps and needs in terms of staff at the subnational level. With this it is possible to assess the most problematic capacity gaps and list a required set of skills for the recruitment of civil servants.

On top of a restricted workforce, high staff turnover and low salaries limit capacity building at the local level. The DNP's Institutional Performance Index shows that in the group of municipalities with "critical" institutional capacities, only 43% of the management staff was the same as the previous year, compared to 87%, 91% and 94% respectively for the "medium", "good" and "outstanding' categories (DNP, 2016a). The human resource challenge, which varies across the territory, concerns not only civil servants, but also elected representatives. The rapid turnover of mayors and governors, resulting from their term which is restricted to only one, four-year term without re-election, does not facilitate the emergence of experienced senior executives over the long term, nor create incentives for long-term investment. Councillors of local mayors often lack qualifications and receive little training. Longer and renewed mandates could provide more incentives to invest in longer term projects (Roland and Gonzalo Zapata, 2000). However, the Colombian Congress has recently rejected the proposed extension of the duration of the municipal mandates from four years to six years; the proposal to extend to at least two mandates was not discussed (OECD, 2014a).

An unstable workforce restricts the possibility of building the managerial capacities of subnational public officials to design, implement and monitor adequate investment projects and low salaries can make attracting the needed skills a challenge. This in turn presents a scenario where weak capacities to design investment projects are currently contributing to the stated territorial disparities; 672 municipalities did not execute more than 20% of their budget (OECD, 2014a). A step forward in human resources management to avoid as far as possible high turnover and low-skilled officials could be to use a list of minimum adequate skills, limiting in this way inadequate clientelist hiring).

Leveraging policies at the central level to improve subnational capacities

To bridge the existent gap and reduce disparities between municipalities, Colombia has developed a range of policies to enhance subnational capabilities. An interesting example is the new approach developed in the

Higher School of Public Administration (Escuela Superior de Administración Pública de Colombia, ESAP), which is being redesigned with the objective of "approaching the territories" by designing and implementing a training policy for local government officials and civil servants. A special assistance fund was established to train municipal councillors and capacity-building programmes to support smaller governments in a variety of management skills. While there is still room for improvement by strengthening and focalising training modules depending on the context, it illustrates the efforts made to reach the local level.

The DNP has also started an active support for municipalities in the design of the new 2016-2019 territorial development plans (PDTs). Ahead of the elections of November 2015 and anticipating possible knowledge gaps of the new public servants, the DNP put in place a Strategy for New Territorial Leaders (Estrategia para el Fortalecimiento de Nuevos Mandatarios). The strategy comprises a training programme designed for mayor and governor candidates, technical assistance regarding the formulation of the PDTs through a specific toolkit called KiTerritorial. The programme focuses on prioritised municipalities which have particular gaps on social development indicators or are strongly affected by the conflict. This assistance targets 462 subnational governments with weak capacities, whilst the other municipalities are assisted via international co-operation (183) or by the Higher School of Public Administration (300). Other technical assistance tools include specific assistance from the DNP for the municipal collegial bodies for administration and decision (órganos colegiados de administración y decisión, OCADs), which serve as planning secretaries, and technical assistance for the use of methodological tools such as the MGA.

The DNP has also developed guides for planning and budgeting, and annual training sessions are held to manage the General Participation System (Sistema General de Participaciones, SGP) and the General Royalties System (Sistema General de Regalías, SGR) (DNP, 2016a). The most recent poll, held in December 2015 with 257 municipal planning secretaries on the perception of technical assistance to municipal OCADs, showed that technical assistance was generally considered excellent (39%) or good (54%), and was key to improving practices. Nonetheless, more technical assistance is needed according to 51% of those polled. The 2014-2018 National Development Plan includes plans for the creation of 6 DNP regional development agencies articulated with 32 department DNP "regional agencies". These agencies would have technical assistance among their core competences. However, there is no consensus so far on the timing for their actual implementation. On the other hand, departments are also mandated to provide technical assistance to municipalities; however, anecdotal evidence provided by the Colombian Municipalities Federation (Federación Colombiana de Municipios, FCM) expresses that they often restrict their action to capital cities and neighbouring areas, deepening the institutional gap with more remote municipalities (Federación Colombiana de Municipios, 2015a).

Box 4.1. **Supporting subnational governments: KiTerritorial**

KiTerritorial is a toolkit developed by the Department of National Planning (DNP) which offers specific instruments to support local leaders in the formulation of their territorial development plans (PDT). The toolkit is organised around four axes that local governments should follow when developing their PDTs: 1) diagnosis; 2) strategy; 3) investment plan; 4) monitoring and evaluation. For each axis, the DNP offers a handbook that explains how to formulate the diagnosis, the strategy or the investment plan; the steps local governments should follow; a timeline; the objectives pursued; the main participants and responsible authorities; and the main inputs.

1. Diagnosis: compiles information and analysis of the main enablers and barriers for the development of the territory. At this stage subnational governments should identify the indicators to prioritise in order to close the socio-economic gap.
2. Strategy: this stage consists of identifying and formulating different objectives, indicators and targets that the territorial entity expects to achieve during its administration term.
3. Investment plan: identifies financial resources available to carry out programmes defined in the strategy. The first step is to analyse the financial situation of the municipality and the efforts needed to generate own resources and articulate effectively all the existing financing sources.
4. Monitoring and evaluation: consist of reviewing whether a PDT is suitable for monitoring and evaluation. Here the municipality should define responsibilities, outputs and outcomes, and the tools that will be used to achieve them.

Source: KiTerritorial website, http://kiterritorial.co.

Taking advantage of the great number of POTs to be revised in the following months, the DNP plans to support 100 municipalities and 10 departments identified as key for the country's development in the formulation and updating of the POTs; 300 other municipalities will receive international co-operation support and 89 POTs will be co-financed. This support will come through a Land-Use Plan Program (Programa Nacional de POT/POD Modernos). The programme will co-finance a dedicated unit within each selected municipality to update the POT, and participate in its implementation through capacity building.

However, challenges linked to a lack of specialised staff remain particularly important in most local governments as a consequence of the difficulty to attract skilled people by offering attractive jobs and salaries. As a way to overcome this challenge and complement the training processes, partnerships with departments and with the FCM need to be promoted, including the exchange of good practices among subnational governments and peer learning mechanisms. Especially for smaller municipalities facing capacity constraints, partnerships and complementary support help to ensure the presence of a capacity that the region or municipality may not need, or be able to, maintain on its own.

Ensure continuity and stability in the rules to strengthen subnational capacities

To address the need of building the long-term capacities of subnational government staff and elected representatives, it is necessary to implement a permanent and comprehensive training and technical assistance system. The multiplicity of tools and methodologies proposed by the central government, which are often not articulated, can constrain local governments instead of alleviating their tasks. The various technical assistance programmes need to be better articulated to avoid overlaps and a proliferation of different rules and roadmaps. Consistent and coherent investment frameworks and rules over time, combined with simplified capacity-building tools, are the key levers to strengthen subnational capacities on a continuous basis.

The DNP has recently developed a tool to strengthen subnational capacities for investments through the CONPES strategy 3856. This strategy provides planning prototypes (26) for projects with similar characteristics, defining guidelines for standardised projects to improve the quality of public investments. These guidelines trigger a learning-by-doing process at the subnational level while subnational government officials take advantage of capacities concentrated at the central level. At the same time, it helps to reduce time and costs in the preparation of projects and reduces the gaps between regions. While in the short run this tool may improve the quantity and quality of investments, in the long term it should be balanced with a certain autonomy of subnational governments for the formulation of their own investment projects that respond to their specific, local needs.

The role of departments for municipal capacity building and technical support should also be better acknowledged. Partnerships between the departments and the FCM could be enhanced, including the exchange of good practices among subnational governments and peer learning mechanisms.

Box 4.2. **Building administrative capacity in member states and regions for the 2014-20 EU programmes**

The new Cohesion Policy for 2014-20 puts the focus on administrative capacity building for member states to fully adapt to the new requirements for using the European Structural and Investment Funds, to implement their investment programmes effectively and achieve the best possible results.

Supporting administrative capacity is about getting the right structures, human resources, systems and tools in place. In other words, making sure responsibilities and tasks are clearly assigned, staff properly trained, and the right kind of people recruited to manage the funds. They also need to be equipped with the right tools – IT systems, manuals, rules – to manage the European Structural and Investment Funds. If the systems and tools are there, organisations are less vulnerable. Another important element is governance. This means holding managers accountable for performance, safeguarding against corruption and conflict of interest, and promoting transparency.

Both the European Commission and member states and regions can contribute to step up the administrative capacity to spend the remaining funds for the 2007-13 on the one hand and to improve the implementation of those for the 2014-20 period and learn from the past on the other.

European Commission

The Directorate-General for Regional and Urban Policy also helps to strengthen the administrative capacity of national and regional administrations using analytical/diagnostic tools, guidance and tailor-made support mechanisms, such as exchange of good practices and experiences or facilitating peer-to-peer networking. The emphasis is mainly on assisting them to better manage EU investment.

The European Commission recently launched a new initiative: the PEER 2 PEER initiative. It is a system designed for the 24 000 officials who work for bodies managing funding and projects under the European Regional Development Fund and the Cohesion Fund. It responds directly to specific requests by authorities logged on the online database and will deliver assistance in the form of expert missions, study visits and specific workshops. Officials willing to share their expertise should register with the Experts Database.

Source: www.euromanet.eu/newsroom/archive/european_commission_launches_initiative_to_improve_investment_and_management_of_eu_cohesion_policy_funds.html.

A systemic approach to capacity building for public investment

Reviewing the stock of regulation to reduce regulatory burdens

Administrative burden in Colombian municipalities is still one of the biggest challenges for capacity building whilst it reduces the efficiency of large investment projects as well as relatively basic public works projects. In Colombia, as in many OECD countries, there are unclear, overlapping and contradictory/divergent regulations across levels of government. This lack of co-ordination can increase costs, reduce efficiency and deter potential investors, in particular from the private sector. In Colombia, the National Planning Department (DNP) is the institution responsible for promoting regulatory reform across the administration; however, it still lags in capacity and co-ordination mechanisms compared to OECD member countries, as well as the absence of comprehensive standards for how to prepare regulations.

According to the Federation of Colombian Municipalities, municipalities must complete 248 reports a year; in other words, one report every working day (OECD, 2015d). Thus, the design and implementation of investment projects may be delayed or even discouraged by overwhelming administrative procedures that affect mostly municipalities where capacities are still a challenge. To move forward, efforts should be put in revising administrative regulations to identify obsolete or overlapping procedures or reports that could be consolidated or modernised.

However, according to the report *Doing Business in Colombia 2013* (World Bank, 2013) there have been some improvements. Between 2009 and 2012, cities included in the study improved in at least one of the areas measured by Doing Business.[2] A total of 62 regulatory reforms for starting a business, dealing with construction permits, registering property and paying taxes easier were implemented in Colombia. Reforms mainly consisted of local implementation of national regulations – but local government initiatives were also carried out, mainly in the starting a business and paying taxes indicators. As a result of the progress made by the 23 Colombian cities towards best global practices, the country ranks today below high-income OECD countries but above the Latin American country average.

In addition, the DNP has made progress in this domain by launching a programme of technical assistance to territorial entities to improve the quality of their regulations. The results of this programme will be an indication of how well local governments are embracing regulatory quality as an element of their reform agendas (OECD, 2014a). The new classification of municipalities that the DNP is currently working on could also ease the reporting requirements for small municipalities for which the evaluation system was a burden, as they do not have the capacities to fulfil these obligations.

The lack of a structure facilitating political commitment and dialogue to address regulatory and policy co-ordination is decreasing the potential for convergence in regulatory practices. There is a need for a widely recognised dialogue platform through which the central government and the territorial entities can discuss national priorities, make high-level political commitments and agree on specific policies to promote competitiveness. A multi-level dialogue platform can serve to define mechanisms by which the central government can support and motivate territorial entities. The platform can also provide a system to monitor compliance with specific milestones, which can feed back to the central government and inform the incentives and support provided to subnational entities (OECD, 2013b).

Efforts in supporting subnational entities to strengthen their institutions and implement tools should be pursued. In some cases, such as the implementation of subnational simplification initiatives, there is scope for the central government and territorial entities to move forward through pilot programmes for specific subnational jurisdictions. Another alternative is to promote the adoption by subnational governments of a simplified methodology for *ex ante* analysis. In any case, there is scope for the central government to advocate for better regulation practices (OECD, 2013b).

Supporting procurement

Procurement is an essential part of improving public investment and can help achieve more than just procurement goals. It is also the government activity the most vulnerable to waste, fraud and corruption, which poses particular challenges for the local level. There are three main requirements to improve the procurement function: 1) need of transparency through the procurement cycle; 2) professionalisation of the procurement function; and 3) better accountability and control mechanisms.

Box 4.3. **Regulatory co-ordination across levels of government in OECD countries: Examples from Canada, Belgium and Mexico**

The OECD established that "high-quality regulation at one level of government can be undermined by poor regulatory policies and practices at other levels, impacting negatively on the performance of economies and on business and citizens' activities". In order to ensure regulatory quality across levels of government, the principles that lower levels of government should follow must be defined. Clear definitions and effective implementation of the mechanisms to achieve and improve co-ordination, coherence, and harmonisation in making and enforcing regulation must also be in place. Finally, measures to avoid and eliminate overlapping responsibilities are also critical.

Canada created a Federal, Provincial and Territorial Working Group on Regulatory Reform. It is a forum that helps build a shared approach to regulatory reform. Its work includes developing common regulatory principles, developing a consistent approach to regulatory impact analysis and sharing best practices.

Box 4.3. **Regulatory co-ordination across levels of government in OECD countries: Examples from Canada, Belgium and Mexico** (*continued*)

Furthermore, other regional-specific programmes have been used by regional governments to facilitate horizontal and vertical co-ordination. In British Columbia, the one-stop shop BizPal is a partnership of all provincial and participating municipal governments. The partnership takes all decisions regarding the overall programme, and the provinces take decisions with respect to the implementation and management of BizPal within their jurisdictions. The programme was launched with a lead group of participating jurisdictions (British Columbia, Yukon and Ontario) in 2005 and continues to expand. It provides one-stop access to permit and license information for all levels of government. OneStop is another electronic tool that has helped in co-ordinating multiple government departments for over ten years. It was the first service in Canada to facilitate business registration with all three levels of government.

Belgium established the Administrative Simplification Agency (ASA) in the Chancellery of the Prime Minister with enough autonomy and with a mandate to solve the administrative complexity for the business environment. The ASA is mandated to encourage and co-ordinate simplification efforts across different administrations. The ASA's tasks include, *inter alia*, organising co-operation between the different federal administrations; organising dialogue on administrative simplification with all levels of authority; establishing a dialogue with administrations over simplification projects for citizens.

In **Mexico,** the Federal Law on Administrative Procedure grants the Federal Commission for Regulatory Improvement (COFEMER) the mandate to promote regulatory quality in states and municipalities. Accordingly, COFEMER helps states develop their own laws on regulatory improvement. One of the main multi-level co-ordination mechanisms used in Mexico consists of covenants between COFEMER, states and municipalities. These covenants establish that COFEMER will provide training, advice and implementation assistance concerning regulatory policies and tools. For example, COFEMER has led the implementation of the System for Quick Business Start-up (SARE), which is a simplification programme for start-up procedures. Until October 2011, 189 SARE had been implemented, leading to the establishment of 264 489 businesses and 701 157 jobs, with an investment of MXN 42 441 million. According to COFEMER, the turnaround time for the municipal start-up licence decreased from 25.2 to 2.4 days in the municipalities that established SARE between March 2010 and November 2011.

Recently, COFEMER started promoting a regulatory governance cycle approach in states and municipalities. Accordingly, it has helped states and municipalities to develop and apply regulatory impact analysis, build centralised registries and carry out regulatory reviews.

Source: Adapted from OECD (2014b), *Mexico, Towards a Whole-of-Government Perspective to Regulatory Improvement*, http://dx.doi.org/10.1787/9789264203389-en; OECD (2010), *Why Is Administrative Simplification So Complicated?: Looking beyond 2010*, http://dx.doi.org/10.1787/9789264089754-en; García Villarreal, J.P. (2010), "Successful practices and policies to promote regulatory reform and entrepreneurship at the sub-national level", http://dx.doi.org/10.1787/5kmh2r7qpstj-en.

Colombia has acknowledged the importance of developing a sound procurement system through Colombia Compra Eficiente – an entity that leads and co-ordinates public procurement. Procurement reform in Colombia was an important component of the governance reform agenda set out in the 2010-2014 National Development Plan. Colombia Compra Eficiente was established in 2012 as the government's central procurement entity in charge of setting up framework agreements, co-ordinating and advising on procurement policy, and assisting buying entities and suppliers in procurement practices (OECD, 2014a).

At the regional and local levels, Colombia has substantially reinforced its control and audit system in order to reduce corruption. It acquires special relevance as 41% of the value of public procurement in Colombia is carried out at the subnational level, hence the importance of building the right administrative framework and capabilities to manage procurement locally. Fighting corruption through a robust integrity framework within subnational governments has been identified as a core issue to implement during the decentralisation process in Colombia and a pre-condition to enlarge the autonomy of subnational governments in the management of public funds (OECD, 2014c).

The powers of control and audit institutions, notably the Comptroller General (Contraloría General), General Prosecutor (Procuraduría General) and Attorney General (Fiscalía General) were reinforced in the Constitution, as well as their independence and territorial coverage. Between 2009 and 2013, the General Prosecutor sanctioned 828 mayors, 622 councillors and 49 governors (La República, 2013).

Colombia Compra Eficiente has recently simplified regulation, specifically bearing in mind the capability constraints at the subnational level. It issued guidance manuals for subnational governments and standard procurement documents for public works, trusts and ICT procurement, among others. It has worked on encouraging collaborative procurement through framework agreements. In certain regions such as Antioquia, there are also examples of consolidated purchases done by the department, the capital city and state-owned enterprises, such as the subway transportation company.

Colombian authorities also implemented in 2005 a new internal control system, based on a Standard Internal Control Model (*Modelo Estándar de Control Interno*, MECI) occurring at all levels of the public sector. Each public entity has set up an internal control office in charge of auditing and supervising the internal control proceedings. Finally, a new legal framework, mainly based on the Anticorruption Statute Law and Transparency Law, has been adopted, which may find difficulties at implementation at the subnational level (OECD, 2014c).

At the subnational level, challenges are strongly determined by unequal capabilities to conduct procurement. Capacity challenges are more acute in small towns in rural areas, with few and often poorly trained officers (OECD, 2014c). According to the Procuraduría Delegada para la Descentralización, out of 28 000 investigations conducted, 60% of offences resulted from ignorance and lack of standards.

However, several challenges remain, such as the implementation of a decentralised procurement system allowing subnational governments to purchase goods and services at the local level and to use the new advanced electronic platform set up in 2015, the Digital Procurement System (Sistema Electrónico de Contratación Pública, SECOP II). An additional challenge is that the majority tends to focus on processes rather than outcomes. Consequently, it seems necessary to move from a control system based on a formalist approach (compliance requirements) to a system based on the evaluation of results (Federación Colombiana de Municipios, 2015b). The formalist approach does not favour good management nor does it impact on corruption reduction.

Strengthening subnational capacities for public-private partnerships

Even if the Colombian PPP model is highly decentralised, PPP contracts at the subnational level remain limited. Similar to that of Mexico, Colombia's PPP model is significantly more decentralised than that of other countries in the region. Every government has responsibilities over the planning, implementation and supervision of PPPs, receiving support from the central level which has set up a database to register PPP projects. However, weak capacities to design and structure projects at the subnational level seem to limit this type of contractual arrangement by departments or municipalities. PPPs are so far reserved mostly to heavy productive investments of national transports; only 1 out of 27 projects already appraised in transportation has been co-financed by a department through SGR funding (Rio Magdalena navigability) and only two projects financed through subnational governments' own resources have been implemented: a stadium in Bogota and Pereira's local airport.

PPPs initiated by subnational governments are still limited compared to PPP projects executed at the national level. However, there are several examples, particularly in large cities, of PPP projects that have been implemented successfully. Since the 1994 Law on Residential Public Services (Ley de Servicios Públicos Domiciliarios), which promotes a system of private participation in the provision and financing of public utility services, several important cities provided their urban services through concessions. For example, in Barranquilla, Triple A provides water, wastewater and solid waste services for the metropolitan area under a concession contract until 2033. In the transport sector, one can cite the Transmilenio in Bogota developed in 2000 to upgrade and operate a bus rapid transit system through a concession contract involving the Colombian government, the city and a number of private companies. Needless to say that Transmilenio has been adopted as a role model for the public transport system in over 100 cities covering every continent.

Box 4.4. **Supporting subnational governments in the procurement process: Examples from OECD countries**

In 2009, **Ireland** established the National Procurement Service (NPS) in order to reform the public procurement function. The principal objective of the NPS is to achieve the best value for money in the procurement of supplies and services. It takes a strategic approach to procurement through aggregating purchases across government departments, agencies and the non-commercial state sector in order to reduce the prices paid for goods and services; providing procurement training and advice to the public sector; and promoting simplification and standardisation of the tendering process. Based on market analysis, the NPS identified the top 50 categories of procurement expenditure to target for intervention. In **Spain**, in the region of Galicia launched a shared web platform for managing its public procurement system available to all public entities in the region (around half are already involved). Public tenders are published on this platform, where companies can register (3 500 have done so thus far) for pre-approval and access past successful tender applications. Bid submission online is in a pilot stage. Increased transparency and competition is visible through an increase in tender applicants as well as a reduction in contracting costs for municipalities.

EU Commission 2014-20: integrity pacts were developed by the NGO Transparency International to support governments, businesses and civil society to improve trust and transparency in public procurement. The European Commission now aims to pilot integrity pacts for several EU co-funded projects by the European Regional Development Fund and the Cohesion Fund.

An integrity pact for the Cohesion Policy funds will be a legally binding agreement between the managing authority and companies bidding for public contracts that will be followed in a transparent and efficient procurement process. To ensure greater accountability, the integrity pacts will include a monitoring system led by a selected civil society organisation.

Source: OECD Toolkit http://www.oecd.org/effective-public-investment-toolkit/

Medellín has also been very active in this field, and several urban projects have been implemented through public-private partnerships with business or non-governmental organisations: Parque Explora, Botánico, Convention Bureau, Plaza Mayor convention centre, Salvia Salud, amongst others. Proantioquia, one of several business coalitions in the city, and the Chamber of Commerce of Medellín support many municipal initiatives, such as the well-being survey "Medellín, ¿Cómo Vamos?" as a clear example regarding the involvement of civic associations in the matter.

Following the 2012 PPP law, Medellín decided to create a legal, administrative and financial autonomous entity entirely dedicated to PPP development, which is the first in Colombia at the subnational level, the Public Partnership Agency. The agency's mission is to promote, manage, evaluate and structure investment projects with high socio-economic impact involving public and private actors. It has been operational since June 2013 and several projects are already in the pipeline at different stages of development (Lleras Park urban renewal project, the football stadium, Nuevo Occidente, the urban highway Parques del Río, etc). This agency will be a major step to upgrade the level of knowledge on this matter of the municipality.

However, for the majority of local governments (in particular for those belonging to categories 5 and 6), there is a lack of financial resources, scarce human capacity and expertise to design, implement, administer and monitor PPP projects, in addition to cultural constraints in some cases. In light of these challenges, the DNP is providing support to municipalities and departments eager to implement PPP projects and has set up a database to register PPP projects. Training has been provided to several potential stakeholders at the national as well as at the local level, including departments, municipalities, chambers of commerce, investment banks, etc. Between 2012 and 2014, 305 public officers were trained. In this regard, the main challenge is the high staff turnover and the subsequent loss of information and expertise. Following the example of the United Kingdom, it could be helpful for Colombia to reinforce local authority expertise, through for example the introduction of the national PPP unit, line ministry units and enhanced project scrutiny. An important step forward is the standardisation of projects through the CONPES 3856, which will reinforce expertise in the preparation of projects in subnational governments.

There are also important bottlenecks to the participation of the private sector in public initiatives; there is certainly a lack of trust of private actors in subnational governments and territorial entities have less capacity to reduce visibility through third-party debtors. One of the biggest restrictions from the point of view of private actors is the maximum threshold of 20% for the level of public participation in private initiative projects.

Box 4.5. **Supporting local capacities for public-private partnerships: Examples from non-member and OECD member countries**

From the outset of the Private Finance Initiative (PFI) programme, the **United Kingdom** has been active in trying to build and reinforce public sector capacity to effectively engage with the private sector. Its primary strategy has been to establish public-private partnership (PPP) units and other institutional structures to strengthen government capacity for PPPs, reinforce project scrutiny and to provide financial resources to local governments to access technical support.

With respect to institutional support, until 2010 the United Kingdom had three units at the national level working on PPPs: Partnerships UK, HM Treasury's PPP Policy Team, and HM Treasury's Infrastructure Finance Unit. In 2010, the three entities were consolidated and replaced by Infrastructure UK (Istrate and Puentes, 2011).

The use of standardised contract documents helped to attenuate some of the risks presented by the complexity of PPP contracts and the administrative capacity constraints of the public sector. The standardisation of PFI contracts (SoPC), developed by PUK and HM Treasury in 1999, provided standardised guidelines for PFIs. Updated four times through 2007, the last version (SoPC4) was succeeded by PF2 guidance. The use of the SoPC and the limitation on alternatives has led to relatively uniform PFI contracts in England (EPEC, 2012) and likely reinforced a minimum level of local capacity.

Much of the attention to public sector capacity appears to have revolved around project appraisal and effective procurement. Yet, because most PFI contracts have a life in excess of two decades, contract management is a critical, but often underdeveloped, public sector capacity. According to PWC (2011), "PFIs rely upon the private sector regulating its own performance but this self-monitoring must be managed and tested as part of the public sector contract management function". Unfortunately, contract management teams are often "woefully under-resourced and contract managers are often unaware of their rights under the contract or how to enforce them". The experience of indexing in Scotland, the problematic local waste projects and the need for deal restructuring among English local authorities reveals the need for continued reinforcement of public sector capacity and the importance of flexibility in contracts.

In **France,** since June 2004, the "public-private partnership contracts" enable a public entity to entrust a company with a global project as part of a long-term contract and in return for a staggered payment from the public entity. It is used for major construction projects (educational establishments, train stations, etc.), urban infrastructures (street lighting, roads, etc.), and even sport and cultural facilities (theatres, stadiums, swimming pools, etc.). The introduction of public-private partnerships was primarily designed to help France to catch up with other countries such as the United Kingdom, which has used this type of tool since the early 1990s. Great progress was made in the number of public-private partnerships signed between 2005 and 2012. Since then, the amounts involved with such contracts are falling a long way behind the other two public procurement tools available, i.e. public procurement and concessions (around 0.2% of GDP).

Box 4.5. **Supporting local capacities for PPPs: Examples from non-member and OECD member countries** (*continued*)

About EUR 14 billion of investments in infrastructure were financed through PPP contracts in France between 2004 and 2015, that is to say, less than 3% of public investments in infrastructures made over this period. The majority of contracts have been signed at the local level (city or urban areas levels). Contracts signed at the local level are of lower amounts (the average amount at the local level is EUR 28 million compared to an average of EUR 220 million for contracts signed at the national level).

Project Development and Monitoring Facility (PDMF) in the Philippines

The Project Development and Monitoring Facility (PDMF) in the **Philippines** refers to a revolving fund with initial funding from the government of the Philippines and the government of Australia through the Asian Development Bank and made available for the preparation of pre-investment studies, project documentations, guidance and assistance in the tendering process of PPP projects of implementing agencies/Local Government Units (LGUs) in accordance with the established guidelines.

PDMF funds are administered by the PPP Center and may be utilised to finance consultancy services in the following areas: 1) preparation of project pre-feasibility and feasibility studies; 2) project structuring; 3) preparation of bid documents and draft contracts; 4) transaction advisory; 5) assistance in the tendering process, including bid evaluation and the award of the PPP contract.

Prospectively, PDMF funding might also be available to finance post-award activities (for instance, assisting the contracting authorities in the pre-financial closure phase as well as in the management of the PPP contract in the construction and operation phase).

Only projects included on the government's list of infrastructure priorities are eligible for PDMF assistance. Upon receipt of a request from an implementing agency, the PPP Center evaluates the request on its merits and initiates its internal approval processes.

In order to access PDMF services, implementing agencies apply to the PPP Center requesting PDMF assistance for a particular project. Applications are substantiated in a project concept note that describes the project and its rationale and sets out the preliminary scope of work of the consultant – the final scope of work being determined in consultation between the PPP Center and the relevant implementing agency. Successful applications are submitted for approval to the PDMF Board.

The process is an efficient one: once an application is approved, the average time between issuance of the request for proposals and the completion of negotiations with transaction advisors is 2.5 months.

Source: Saussier (2016) in OECD based on French PPP task force – data updated 8 October 2015; Mizell in OECD (2017), "Public-private partnerships at the subnational level"; https://ppp.gov.ph/wp-content/uploads/2013/07/PDMF-Guidelines-June-2013.pdf.

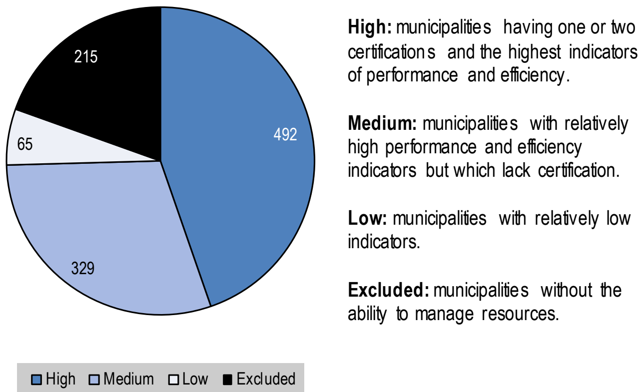
Supporting subnational capacities requires differentiated competencies

In a context of high disparities in subnational capacities or various territorial, political or cultural contexts, asymmetric decentralisation of responsibilities can be an interesting way forward in devolving responsibilities in subnational governments. Asymmetric governance approaches contain risks, in terms of creating institutional complexity and preference treatments, but at the same time they are ways to better take into account various territorial, political or cultural situations. Such an asymmetric approach is increasingly being adopted for various reasons in France, Italy, Spain, Sweden and the United Kingdom.

The new Differentiated Competences National Program included in the 2014-2018 National Development Plan intends to respond to the disparities in the capacities of subnational governments by devolving more responsibilities to the more qualified municipalities. For the delegation of competencies to municipalities, the government identified sectors that can potentially be more efficiently managed at the municipal level; these include protection and reinsertion of victims, transport (tertiary roads), early childhood, and agricultural and rural development. For this, the DNP has defined general and specific criteria linked to financial, technical and institutional capacities. General criteria assess the institutional capacities of local actors independently of the competence to be delegated. This evaluation qualifies 492 municipalities with high results while 215 are in the lowest category (Figure 4.1). For a competence to be devolved, the municipality needs to comply at the same time with specific criteria defined by the national authority that will delegate the competence. Following these two steps of multi-criteria analysis, the DNP identified 131 municipalities that could assume functions currently delivered by the central level.

For the devolution to take place, the municipality has to ask for the delegation of a specific competence. The transfer depends strongly on the political will of the local government in assuming further responsibilities, as devolution is not encouraged by any financial incentive beyond the transfer of the corresponding budget. The request is then analysed by the sectorial ministry involved, which may be resistant to give up part of its prerogatives. The process becomes more complex when the competences to be transferred involve various sectors. This is the case of victims, which potentially involves agriculture, land management, transport, health, education and social care. In asymmetric processes of decentralisation, the use of pilot initiatives can be highly useful as a way to ensure a gradual institutional change and learning-by-doing. The Swedish experience with pilot regions has proven to be a smooth and successful way to empower regional actors, in areas with well-developed local capacities well-suited for regionalisation. If well selected, pilot experiences in Colombia can enlighten this process and strengthen future experiences for the transfer of competencies. The case of Barranquilla that will handle the cadastre will set the basis for future experiences.

Figure 4.1. **Classification of municipalities by general criteria**



Source: DNP (2015d), "Evaluación de Desempeño Integral 2015", PowerPoint presentation

Asymmetric decentralisation of capacities may also have a fiscal dimension, in particular regarding the future tax reform. An important step forward to strengthen local autonomy can be a tax reform that differentiates between municipalities depending on their size and capacity. Cities with stronger managerial skills should have more autonomy on the use of and decisions concerning their financing mechanisms. For instance, cities can have the autonomy to define tariff ranges to grant them more flexibility in the management of their own resources. This differentiation allows also territorial entities to exploit their particular economic characteristics.

Better assessing investment projects *ex ante* and *ex post*

Prioritising investment: Effective ex ante *appraisals*

Turning strategic planning into effective investment prioritisation is a major challenge for any public investment policy. Governments should use comprehensive, long-term appraisals to select their investments as they clarify goals and reveal information. Like in many other countries, Colombia has made important efforts to improve *ex ante* project evaluation, both at the national and local levels. Since 2003, all investment projects need to pass through the *ex ante* appraisal of the General Adjusted Methodology (Metodología General Ajustada, MGA) in order to be integrated into the different databases for programmes and projects (Banco Nacional de Programas y Proyectos, Banco de Proyectos de Regalías or the Bancos de Programas y Proyectos of each territorial entity), which is the first stage of resource allocation for any public investment project. The MGA methodology, structured around five modules (Figure 4.2), provides a complete and standard tool for *ex ante* evaluation, linked to planning through the development plans.

Box 4.6. **Asymmetric decentralisation in select OECD countries**

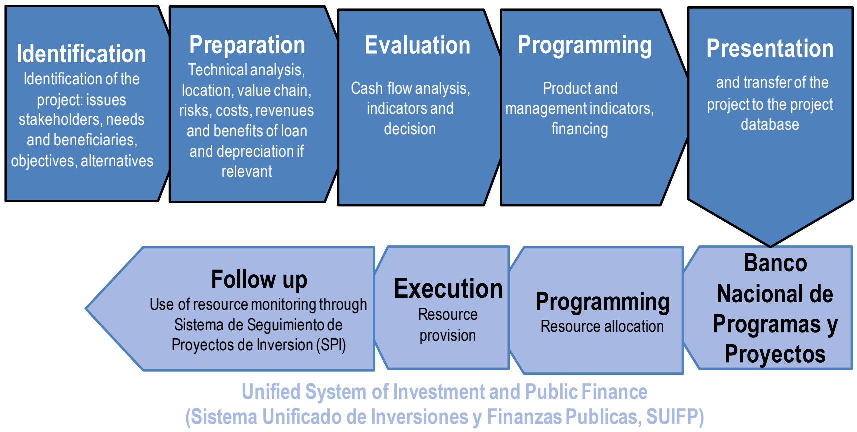
Since the late 1990s, **Sweden** has developed a rather unusual regionalisation process by proposing different options to different regions and pursuing an asymmetric decentralisation. In contrast with reforms driven by the central government in some other OECD countries, Sweden's regionalisation reforms have adopted a bottom-up approach based on a conscious choice to take the time to experiment, to achieve consensus through in-depth consultation and to learn from results. The result is a very heterogeneous map in which regional development responsibilities (notably the task of designing regional development programmes and regional growth programmes) have been assigned to: county councils (directly elected regional authorities) in two "pilot regions" since the late 1990s (Västra Götaland and Skåne, both urban regions in Southern Sweden); regional co-ordination bodies (indirectly elected associations of all municipalities in a county, called *kommunala samverkansorgan*) in two-thirds of counties through the 2000s; and to county administrative boards in one-fourth of counties (Norrbotten, Västernorrland, Jämtland, Västmanland and Stockholm).

One clear advantage of bottom-up regionalisation is that it allows a smooth decentralisation process on an earning-by-doing basis, with the right to experiment and to learn from the results. Various external assessments have been conducted since the late 1990s in the two pilot regions, and the outcome appears to be positive. However, their achievements are difficult to measure quantitatively, and lessons from Västra Götaland and Skåne, two metropolitan areas with almost a third of the total Swedish municipalities, cannot necessarily be extrapolated to all Swedish regions.

Between 2012 and 2015, nine local municipalities in **Denmark** were granted some exemptions from government rules and documentation requirements in order to test new ways of solving their tasks, in a policy experiment known as the "Free Municipality" initiative. The main focus has been on simplification, innovation, quality and a more inclusive approach to the individual citizen, with many of the experiments focusing on the employment effort. The Free Municipality experiment is currently being evaluated, in order to form the basis for potential future legislation on de-bureaucratisation for all municipalities. The concept of Free Municipalities continues in an adjusted form until 2019, and is extended to more municipalities.

Source: OECD (forthcoming), Monitoring Review of Sweden.

Figure 4.2. **Five steps of the General Adjusted Methodology**



Source: DNP (2016e), "Nueva Evaluación de Desempeño Integral – NEDI", PowerPoint presentation.

Although all projects are supposed to follow the MGA methodology, there is some evidence of deficiencies at the subnational level in the project preparation phase, which restricts the efficacy of the *ex ante* appraisals. These limitations affect the formulation of projects, the cost and benefits estimations, and the definition of appropriate indicators for the *ex post* evaluation (see below). Fedesarrollo estimated in 2014 that more than two-thirds of the problems associated with the investment cycle of the project are due to weaknesses in structuring projects at the planning phase (Fedesarrollo, 2014).

A comprehensive, long-term view of costs, benefits and risks is important to avoid an unwarranted bias in favour of some forms of investment over others. For the prioritisation of projects at the local level it is of utmost importance to fully assess early in the investment cycle long-term operational and maintenance costs, which are often under-estimated. In Colombia, operation costs are often disregarded at the pre-investment and investment phase; most SGR projects do not include operational costs, which harms their sustainability in the long run. But comprehensiveness also means a broad view of the investment objectives to consider. Some other key dimensions are missing in the pre-investment analysis, such as the impact of the projects on competitiveness and on sustainable and inclusive development; Colombia may not neglect important social or environmental costs or benefits of an investment. Given the high territorial heterogeneity across the country, there can be risks pertinent to a particular region or locality which should be also considered as part of this assessment.

An important step forward for *ex ante* appraisals on the General Adjusted Methodology is to simplify the methodological guidebook. While the MGA is in itself a complex instrument, especially for low-skilled civil servants, understanding a big and complex guidebook can represent a challenge in itself, harming the implementation of the methodology. The training on MGA for civil servants currently in place needs to be pursued in parallel to the simplification of the instrument to facilitate its use at the local level. It is worth noting that high turnover may hamper the training process, thus it is possible that this training effort has to be constantly repeated.

In some cases, for major projects where appraisal is particularly complex, there may be a need to tap technical expertise in organisations or units (public or private) with independence, experience and a good reputation for such analysis. In some cases, for weaker municipalities and/or complex projects, it may be worth considering devolving the preparation of investment projects to the department or government agencies (DNP, Findeter, FONADE). In parallel, technical assistance for municipalities could be combined with funding for externalisation of part of the *ex ante* appraisal to the benefit of external expertise, as technical requirements may extend beyond standard project appraisal skills and require specific types of expertise.

Appraisal methodologies may be differentiated according to the size of the project or its complexity. This would mean less rigorous appraisal for smaller projects and more rigorous assessment for larger or riskier projects. Cost-benefit analysis is most effective where there is a great deal of information about the project, the context and the risks involved over the investment cycle (OECD, 2013a). For example, it might be relatively straightforward to assess the potential gains from relaxing a transport constraint on a well-travelled route. By contrast, far greater analysis is required for major new infrastructure, altering existing traffic flows or generating new ones. The state of Victoria in Australia has developed an innovative “High Value High Risk” process which reflects the importance (and difficulty) of sound *ex ante* appraisal for certain investments (Box 4.7).

The DNP is implementing a grading system (*Sistema de Puntajes*) that would allow prioritisation of the allocation of funds for investment projects financed by the SGR. This grading system gives recommendations for the approval of projects in the OCADs based on four criteria: the “closing gaps” approach, the impact and magnitude of the project, the territorial impact and co-financing arrangements. The information for the evaluation comes primarily from the MGA. The *Sistema de Puntajes* prioritises investments with high impact focused on closing gaps that consider the articulation of various funding sources. This development, if successfully implemented, would represent a major progress. A major challenge in the implementation can be the managerial skills needed in the OCADs to apply the evaluation system. For this prioritisation system to be successful, it has to consider explicitly the future maintenance costs that big projects will necessarily imply. The main hindrance to generalising this type of mechanism is the lack of homogeneous and comprehensive data on existing infrastructure and needs. The scoring also might need to include explicitly the question of maintenance costs. Finally, a real articulation between the scoring system and the MGA methodology needs to be ensured. Colombia could integrate both tools to prioritise investments based on the *ex ante* appraisals, thus avoiding overlaps and confusion and taking advantage of the complementarities of both analyses.

Box 4.7. **The "High Value High Risk" process in the state of Victoria, Australia**

The Department of Treasury and Finance in the state of Victoria has more direct accountability for assuring the quality of major public investment proposals. The Victorian government recently established a "High Value High Risk" process. Under this process, for investment projects which have a value above a defined threshold or which are deemed to be high risk even if they fall under the monetary threshold, the Treasurer (i.e. the minister) must personally verify and approve the investment proposal at crucial points before it is presented for final decision. In contrast with its former role of *ex post* review of spending proposals, this process engages the Department of Treasury and Finance in the decision-making process directly and "in real time". The focus of the new central quality assurance arrangements is on enhanced *ex ante* control – improving the business cases for major investments. These now require much more effort and expertise from the ministry responsible, and are subjected to rigorous scrutiny, both at a technical level and in terms of their wider assumptions. The process has reduced one important source of investment failure – the tendency for the scope of investment projects to increase as they are developed, without express approval.

Source: Bounds, G. (2012), "Public investment across levels of government: The case of Victoria, Australia", www.oecd.org/regional/effectivenessofpublicinvestmentatsub-nationallevelintimesoffiscalconstraints.htm.

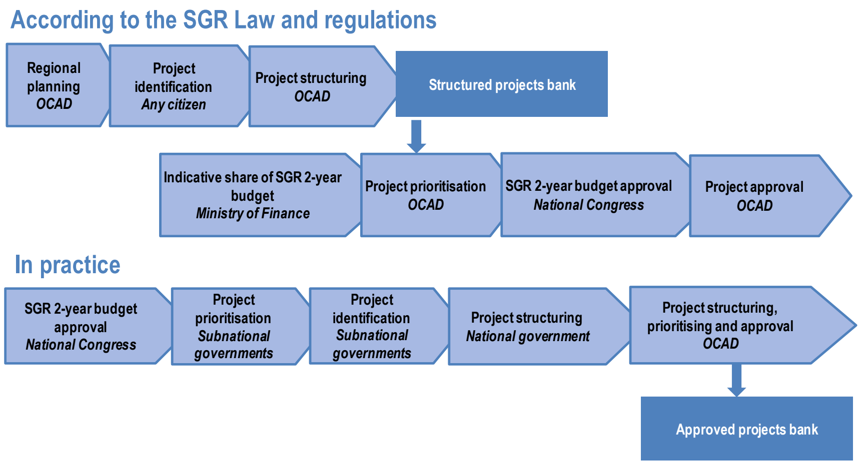
Selection and appraisals of projects funded by royalties

There are serious shortcomings in the appraisal process of SGR projects. The limitations were analysed in an evaluation through Sinergia

Evaluaciones (2013-14), including a lack of motivation from OCAD members to analyse projects and attend meetings and the tendency of some OCAD members to put political considerations before technical aspects for project validation. In general, the validation process is considered very heavy by many weak municipalities, which rely more on royalties than richer municipalities do. The result is that poorer municipalities are candidates for more projects, but get proportionally fewer projects approved than richer and bigger ones. The rate of approval also increases with the number of projects previously approved – probably due to a learning curve, and is higher for projects co-financed by the national level. Institutional capacity inequalities seriously limit the possibility of weak municipalities to get projects approved: it makes the SGR system somewhat regressive (Fedesarrollo, 2014).

The DNP has estimated that 52% of municipalities have insufficient capacities to structure projects. The projects presented often lack technical information (DNP, 2016a). National government line ministries, generally solicited to evaluate the projects, give an uneven response, depending on their priorities, leading to variable quality of evaluation and delays in analysis. Often, the technical part of the project is considered, but not its financial relevance and feasibility. According to the law, projects should be defined and structured in line with a prior regional planning exercise, then prioritised and approved. In practice, however, projects tend to be prioritised and structured by subnational governments in a hurry once they know the amount allocated to them, without any regional planning consideration (i.e. after the SGR budget law). They are then evaluated, and in many cases restructured by line ministries and approved on precarious basis by the OCAD.

Figure 4.3. **General System of Royalties project approval process: Theory and practice**



Source: Ministry of Finance and Public Credit.

Since the 2012 reform, COP 2.9 trillion were unspent in accumulated balance for 2012-15, mainly because municipalities and departments lack well-structured projects. Around COP 2 trillion were approved, but not yet executed – contract not yet signed, and 90% of the projects are not totally executed and “closed” (DNP, 2016a). This situation leads to great amounts of money remaining, sometimes for a long time, in subnational governments’ bank accounts without being used. Royalties also sometimes contribute to finance other expenditures than investment – such as school nutrition in certain departments, despite the fact that it is supposed to finance only capital expenditures. It is also worth mentioning the difficulty in spending the ICT Fund (10% of the SGR), due to a lack of local projects in this sector.

Efforts are being made to improve the SGR system:

- In order to help subnational governments to better structure their projects, 26 standard projects (*proyectos tipo*) were defined in the CONPRES 3856 (technical, methodological and financial standards) for the more recurrent investments (school, sport field, road), corresponding to more than 15% of the projects (see above).
- As the 2014-2018 national budget establishes, public financial institutions (like FINDETER or FONADE) were allowed to help subnational governments to structure projects, recovering the costs

through the project financing. The 2016-2017 Budget Law also states that the funds will be transferred only after the contract is signed, which should not occur more than six months (renewable once) after approval. The money is otherwise returned to the SGR, even if it remains earmarked for the municipality.

Fragmented monitoring and evaluation that mirrors fragmented funding

Monitoring and evaluation activities are of particular value for public investment activities. Monitoring allows actors to follow the implementation of investment portfolios and projects, to track the achievement of contractual obligations, to encourage performance, to make mid-course adjustments and to identify medium-term outcomes. For this, Colombia has developed a comprehensive array of monitoring and evaluation mechanisms that meet international standards – the Sinergia programme and MapaRegalías are some examples of these good practices. However, as it is the case for planning process, monitoring and evaluation mechanisms are structured around the financing sources of projects, resulting in a fragmented and disperse set of information both for policy makers and citizens. The multiplicity of monitoring and evaluation systems includes budgeting monitoring on a project basis, the definition of indicators, comprehensive performance monitoring or territorial appraisals of projects, among others. While some of these mechanisms are complements, others provide partial pictures of the investments made at the local level.

Monitoring financial performance

During the last years, Colombia has developed some tools to monitor the financial performance of subnational governments. The unified territorial form (*formulario único territorial*, FUT), in place since 2005, registers the budget execution of the revenues and expenditures of subnational governments. Since 2008, this information is reported quarterly on the CHIP website in an organised and timely manner, increasing transparency and improving the quality of the information reported (OECD, 2015c). All national public entities also have to report budget execution by territories since 2015 through the Investment Project System (Sistema de Proyectos de Inversion, SPI).

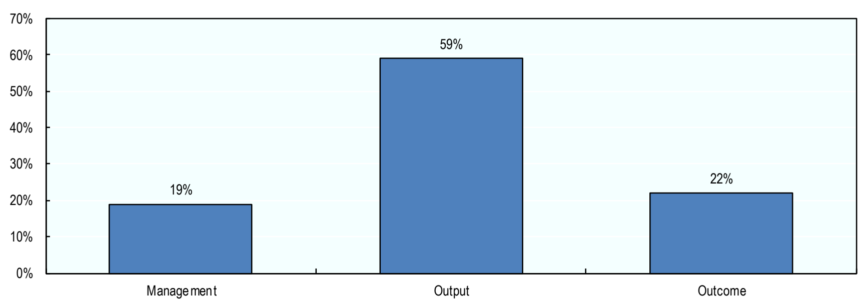
The Banco Nacional de Programas y Proyectos is the first module of the Unified System of Investment and Public Finance (Sistema Unificado de Inversiones y Finanzas Públicas, SUIFP), which manages information on public investment projects financed by the SGR and the general budget during the entire investment cycle for monitoring and financial planning purposes. However, territorial entities do not transfer their projects to the Banco Nacional de Programas y Proyectos, which prevents consolidation and a comprehensive picture of national and local investment projects, as each subnational government has its own bank of projects. Responding to this challenge, the DNP is working on the standardisation of reporting mechanisms through user-friendly tools that all subnational governments would have to use from the end of 2016. This, together with a unified and integrated system that groups all investment projects during the entire investment cycle, will improve conditions to effectively monitor financial performance.

Performance evaluation of investment projects

The main monitoring and evaluation instrument of development plans is the National System for Management and Results Evaluation (Sistema Nacional de Evaluación de Gestión y Resultados, SINERGIA), which has three main components: Sinergia Seguimiento, Sinergia Territorial and Sinergia Evaluaciones.

- The first component, Sinergia Seguimiento, monitors government goals to verify the progress of the National Development Plan through output and outcomes indicators defined in the NDP. It includes a special module to follow-up on the regional indicators according to the regional strategies of the general budget 2014-18.

Figure 4.4. **National Development Plan 2014-2018 indicators by type**



Source: Sinergia, https://sinergia.dnp.gov.co/Paginas/inicio.aspx.

- The second component, Sinergia Territorial, consolidates information from the National Development Plan objectives that have a territorial scope. It also has a component to follow-up on the physical and financial execution of the *Contratos Plan*. Sinergia Territorial aims at building autonomous strategic monitoring systems at the subnational level, strengthening the capacities of territorial entities to create their own monitoring and evaluation systems. For this, Sinergia Territorial supports subnational governments with technical assistance to design and implement monitoring and evaluation systems based on the PDTs. Between 2012 and 2014, Sinergia Territorial implemented PDT monitoring of 83 municipalities and 12 departments, based on high-quality technical assistance, peer learning and autonomy. It is planned to be extended to other municipalities in the years to come through the Program for Strengthening Institutional Capacity of Territorial Governments.

- The third component, Sinergia Evaluaciones, has four types of evaluations: 1) process evaluations focused on how processes help to meet the objectives of a specific policy or programme; 2) institutional evaluations, which assess the institutional capacity of a public entity to operate a policy or programme; 3) results evaluations, which assess how the policy meets the targets and the intended or unintended effects of the public intervention; 4) impact evaluations, that allow the identification of particular effects directly linked to the intervention attempting to identify causal effects. In 2016, eight evaluations are being conducted, two of which are impact evaluations and the remaining six are a mix between process, results and/or institutional evaluations.

Evaluation of subnational investment projects financed by the SGP is done through the Municipal Performance Evaluation (Evaluación de Desempeño Integral), conducted annually by the Department of National Planning since 2005. The evaluation results in an aggregate indicator combining quantitative evaluation of: 1) efficacy; 2) efficiency; 3) legal requirements; 4) administrative capacity and fiscal efficiency (Figure 4.5). During the last years, the participation of municipalities has increased, with 707 municipalities giving complete and accurate information in 2014, compared to 557 in 2013 (some municipalities only provided partial information on the different components). The evaluation has shown that municipalities have made an important effort to fulfil their duties. While in 2006 27% of municipalities were qualified as "satisfactory", in 2014 this number rose to 61%. This indicator is also used by the DNP to identify the difficulties subnational governments may have in designing and implementing their PDT, and on that base, define the relevant technical support. However, this methodology falls short in evaluating outcomes, mainly regarding the "efficacy" component and compliance with the PDTs' objectives. On top of this, the evaluation does not consider territorial heterogeneity across the country. A New Municipal Performance Evaluation (Nueva Evaluación de Desempeño Integral) is currently being developed to solve some limitations of the actual system (Box 4.8).

Since 2013, the General Royalties System (SGR) has used a Monitoring, Tracking, Control and Evaluation System (Sistema de Monitoreo, Seguimiento, Control y Evaluación, SMSCE) exclusively focused on budgetary performance, administration and execution. All the strategic information is available on the platform MapaRegalías fed by subnational data recorded in Gesproy and information from the Ministry of Finance and Public Credit, the National Mining Agency, the National Agency of Hydrocarbons and the DNP. It is mandatory for subnational governments to report the progress of the different projects on a monthly basis. Yet, high turnover of staff responsible for recording information in Gesproy and lack of adequate skills to report information are the main barriers for a timely and accurate reporting (DNP, 2016a). Gesproy is connected to the Unified System of Investment and Public Finance SUIPF-SGR and allows the follow-up of indicators defined when designing the investment project. However, at the planning stage, subnational governments often fall short of formulating projects correctly and setting adequate indicators for evaluation (DNP, 2016a). Consequently, the usefulness of the information provided by the system is limited.

Figure 4.5. **Components of performance evaluation: Municipal Performance Evaluation**

Source: DNP (2015a), "Desempeño fiscal de los departamentos y municipios 2014".

An important shortcoming of project monitoring is that the emphasis is put on a formal control of the contracting and execution phases of the projects, leading to a highly bureaucratic process that puts a heavy burden on subnational government administrations. Instead, efforts should point to a better and more efficient project selection and *ex post* evaluations providing information for future planning. With this, incentives for local governments are on the planning stage instead of on the contracting phase, which comes along with a general fear of not complying with the numerous formal obligations (World Bank, 2016). It would imply, in particular, putting the emphasis on: 1) checking coherence with the overall public investment strategy; 2) checking technical and financial feasibility, sustainability and efficiency (including an appraisal of the impact of the investment on current expenditures).

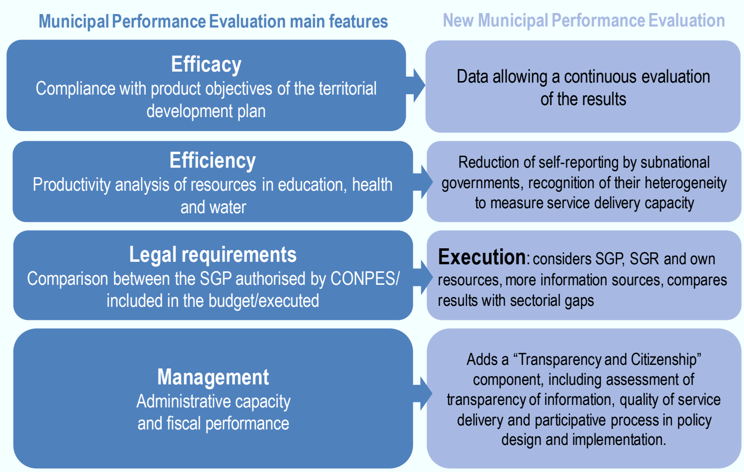
Box 4.8. **A new performance evaluation index for municipalities**

Colombia is currently developing a New Municipal Performance Evaluation (the Nuevo Desempeño Integral) to be implemented from September 2016.

The new evaluation system changes the focus of the evaluation, moving from a performance evaluation focused on outputs towards an evaluation of the outcomes of municipal management. The evaluations will be structured around five main axes: 1) efficacy; 2) efficiency; 3) execution capacity; 4) fiscal performance; 5) institutional capacity (administrative capacity and transparency):

1. Efficacy: evaluates the degree of compliance of the strategic goals defined in the territorial development plans (outputs and outcomes).
2. Efficiency: measures the productivity level of the outputs and resources assigned to the provision of basic services. It will consider special characteristics of the territorial entities.
3. Execution capacity: assesses the effectiveness and efficiency on the use of investment resources.
4. Fiscal performance: establishes a balance between revenues and expenditures.
5. Institutional capacity: assesses the ability to promote participatory and transparent processes.

Figure 4.6. **New overall performance: Municipal Performance Evaluation: Main evolutions**



This new methodology will reduce self-reporting from subnational governments from 75% to 55%, include more objective evaluation criteria and facilitate monitoring.

Source: DNP (2015a), "Desempeño fiscal de los departamentos y municipios 2014"; DNP (2016d), "Evaluación del desempeño integral 2015"; DNP (2016e), "Nueva evaluación de desempeño integral – NEDI".

The multiplicity of monitoring tools mirrors the multiplicity of funding sources for investment projects at the local level, which are weakly articulated. Monitoring through a diverse set of tools prevents a coherent and comprehensive overview of the programmes being evaluated and their results. As planning should move away from the funding logic, monitoring and evaluations should do so as well. At the same time, *ex post* evaluations, such as the ones performed through Sinergia Evaluaciones, could be extended (required and financed more systematically), and used for informing policy makers at the local and national levels. It may also be relevant to build Sinergia Seguimiento indicators at intermediate territorial levels, as the update for 2014-18 only considers the six macro-regions.

The integration of the various monitoring and evaluation tools is a key step for Colombia to get a comprehensive picture of investment assets and needs. This issue is being addressed in co-operation with the World Bank, through the design of a "Result-oriented Budget" project (DNP, 2016a), and with the Inter-American Development Bank through the "Public Investment System Strengthening Program" (CONPES 3751 of 2013; DNP, 2016a). One of the objectives of this programme is merging Gesproy and the Investment Projects Monitoring System (SPI) within a unique device, with a visualisation and georeferenced module for all public investment projects, called MapaInversiones (DNP, 2016a), which will complement the integration of all the investment financing sources (general budget, the SGR and the SGP) throughout the investment cycle. The idea behind the programme is to switch from monitoring differentiated by funding source to a programme-oriented integrated monitoring system, which would integrate the various funding sources mentioned above and connect planning to budgeting and execution through a uniform structure. MapaInversiones will be a user-friendly website integrating information of *ex ante* evaluations (MGA), projects database (BPIN) and follow-up information (SPI). The full system should be operational in 2017.

In many OECD countries, monitoring tools are linked to a reward to good performance to incentivise subnational governments to plan and implement projects efficiently. Colombia could make a step forward in this direction by using the performance monitoring to explicitly inform future decisions on investments (Box 4.9).

Improving data collection

Although data collection has improved in the past years, there are still problems with timely and accurate information reporting. It is recognised that a strong limitation for the Performance Evaluation EDI is the frequency of the reporting – only once a year – and the untimely and incomplete information received from subnational governments. At the same time, the different monitoring systems require information at different times during the year, which sometimes limits the consistency of the information available in the different systems. The problem of data provision is directly linked to local capacities, high turnover, and complex and unfriendly reporting tools. In some cases, especially in more disadvantaged municipalities, Internet access is also an important barrier to reporting data. An interesting step forward in data reporting is the project to reduce self-reporting data by subnational governments from 75% to 55% in the new Performance Index, as well as the standardisation of data. Making the use of the Bank of Investment Projects (Banco Único de Proyectos) compulsory for all subnational government investment projects from the end 2016 will also improve data for monitoring.

Box 4.9. **EU Performance Reserve 2014-2020**

The EU Cohesion Policy 2014-2020 offers strong incentives to deliver Europe 2020 objectives through a result orientation based on three pillars. First, it requires a clear articulation of the objectives of programmes. It also defines that a number of framework conditions must be in place *ex ante* before the funds are disbursed (for instance, the proper functioning of public procurement systems) to ensure that investments can be made in the most effective manner. Third, progress towards the achievement of objectives will be closely monitored and measured against a set of milestones agreed as part of a performance framework.

The policy establishes that programmes and priorities which achieve milestones set for 2018 in the performance framework can benefit from the performance reserve after a review undertaken in 2019. The objective of the performance reserve is to ensure and reward good performance in the implementation of programmes. Where there is a serious failure to achieve milestones (i.e. serious under-performance compared to what was initially planned), the respective programmes and priorities cannot benefit from an allocation from the performance reserve. The European Commission agreed that the performance reserve will be 6% of the funding allocated in 2019 to programmes and priorities which have achieved 85% of their milestones.

Source: European Commission (2013), "Q&A on the legislative package for EU Cohesion Policy 2014-2020", http://europa.eu/rapid/press-release_MEMO-13-678_fr.htm.

Improvements have been made through the Sinergia monitoring system, which works directly with territorial entities so that the indicators are reported periodically. As of March 2016, 83% of the system was up to date. Additionally, over the past few years, several initiatives have been taken to standardise and simplify data collection and presentation, among which the MapaInversiones project can be highlighted. This initiative is an extension of MapaRegalias to all investments and not only royalties (SGR). Progress in the implementation of MapaInversiones would allow major advances in the systemic governance of public investment.

Still, continuous training of subnational officials is necessary to obtain the necessary information appropriately. Collecting and providing timely data is an important challenge, especially for smaller municipalities. Additional human resources and incentives to stimulate data provision are also key levers to collect local information.

Using information to invest smarter

Learning happens only if the information produced in a first step is used in a subsequent step. Harnessing the productive value of monitoring and evaluation information requires governments to produce information that is timely, relevant and actionable, and to use it in a meaningful way. Colombia has made significant efforts to collect data and improve the information available. However, the production of information by itself does not improve the efficiency of investments; the information has to be used to enhance decision making. In parallel, results of *ex post* evaluations have to feed decisions on investments. Beyond *ex post* evaluations by independent bodies, the information produced has to feed future decisions on investments.

Engaging with stakeholders throughout the investment cycle

Colombia has developed a more inclusive institutional framework over recent years aiming at better involving economic and social stakeholders in policy making at all levels, increasingly aligning with some of the OECD good practices in this field. Many initiatives seek to enhance transparency and consultation, while generating trust (OECD, 2014a). However, participation remains uneven and dispersed due to difficulties in access to information, low capacities in certain territories, lack of political will or mistrust.

Box 4.10. **Monitoring and evaluation: Examples from OECD countries**

In **Canada**, regional development agencies (RDAs) are generally subject to the same accountability requirements as federal departments and they developed specific indicators in order to monitor the effectiveness of their interventions. The indicators are not the same among different RDAs; they are developed specifically for their programmes and needs. In addition to the indicators used to report to the parliament, some RDAs have developed indicators as part of their performance measurement framework in order to monitor the effectiveness of their programmes. Moreover, each programme has its own strategic management framework. In addition, all programmes have to be evaluated every five years, against various criteria such as effectiveness, continuity, efficiency and results. All the departments have to produce a management action plan to address the recommendations for each evaluation report.

Box 4.10. **Monitoring and evaluation: Examples from OECD countries** (*continued*)

Another tool for evaluation in Canada is the Management Accountability Framework, a framework for management excellence, accompanied by an annual assessment of management practices and performance in most departments and agencies of the government of Canada. It is a key oversight tool that is used to help ensure that federal departments and agencies are well managed and accountable and that resources are allocated to programmes and projects that would deliver the best results.

The **Italian National Evaluation System (NES)** includes the national entities responsible for evaluation activities and the evaluation units of central and regional administrations responsible for operational programmes co-financed by European Structural Funds. The NES is structured as a collective entity in the implementation of its activities. In particular, it is an important forum for discussion on issues concerning the results of regional policy, for diffusion of evaluation results and their use, for implementation of monitoring systems. The NES provides technical and methodological guidance and facilitates exchange of experience and good practices between administrations in order to strengthen evaluation capacity and support the quality of evaluation in Italy. The NES regularly carries out surveys on the implementation of evaluation plans, collecting information from public administrations (central and regional) on completed, underway and under preparation evaluations. The NES' website makes available all the evaluations classified by thematic area, programming period and type of evaluation.

In **Chile**, CHILEINDICA is an investment data repository that provides investment information of central and regional government levels. It allows monitoring the implementation of different projects at all levels, improving information flows between regional and sectoral public institutions, and the management of investment. CHILEINDICA is an online platform providing the history of territorial interventions for regional governments and ministries in a transparent and timely manner. In parallel, Chile has implemented a number of indicator-based performance management programmes, such as the Management Improvement Programme and the Municipal Services Accreditation System. These both include monitoring and certification processes and the use of indicators and training programmes to support municipal and regional governments in improving their capacity and responsiveness to government administration.

In **Mexico**, the National Institute of Statistics and Geography develops an integrated system of georeferenced data, matching information from different sources and at different geographical scales. Indicators are used to help link budget allocations to socio-economic variables in regions in order to provide simulations of further funding according to policy objectives, such as fighting poverty.

Box 4.10. **Monitoring and evaluation: Examples from OECD countries** (*continued*)

Ex post evaluations EU: Poland is carrying out an *ex post* evaluation of its Rural Development Programme 2007-2013 according to EU regulations. The evaluation will summarise the process of implementing the Rural Development Programme 2007-2013, will present and evaluate results of implementing particular measures and the programme as a whole. *Ex post* evaluation will examine the degree of use of funds, the effectiveness and efficiency of the programme, its socio-economic impact and its impact on EU priorities.

Box 4.11. **Portugal 2020 Territorial Approach and lessons from past experience**

The EU Cohesion Policy 2014-2020 has a strong results orientation (performance framework) and considers new territorial instruments to target less developed regions. One of the most important axes is the definition of indicators throughout the policy cycle to identify how the policy outcomes are related to the final results; align the objectives of different sectors and different levels of governments and stakeholders; and finally identify the right scale of analysis.

The Portugal 2020 Territorial Approach follows previous experiences on the use of EU funds to promote regional policy and benefits from the three territorial strategies of the EU Cohesion Policy: the Integrated Territorial investments to pursue in all the mainland territory the contracts with municipal associations at NUTS III/TL3 level; the integrated Sustainable Urban Development Actions to promote the urban renewal and urban mobility in the main urban centres as defined in the National and Regional Spatial Plans; and the Community-Led Local Development implemented through Local Development Strategies to promote a bottom-up strategies, mainly for low density territories.

In a broader perspective of regional policy over the last decades, Portugal has learnt some important lessons with the implementation of the EU Cohesion Policy:

- Firstly, the basic step for territorial policies is to develop accurate information and regional tendencies. It is of utmost importance to develop indicators for the entire investment cycle and not only focused on results. For this to be successful, a direct and close co-operation between the government and the statistical institute is key.
- Secondly, policies need to be sustained in the medium and long term. Results take time and when a policy persists over time it becomes a credible policy to establish partnerships and contracts across levels of government.
- And finally, while it is relevant to focus on results, it is even more important to find a right balance between focus (results) and flexibility to adapt policies to specific objectives, needs, potentialities, and national and regional specificities.

Source: Rodrigues (2016), *Portuguese Regional Policy within EU Regional Policy,* Powerpoint presentation, Bogota Seminar (May 2016).

Stakeholders participation at the planning stage

Colombia's government, aware of the benefits that effective consultation and feedback mechanisms bring, has greatly improved participation to engage with public, private and civil society stakeholders in the investment cycle. In particular, participation in Colombia has been strongly encouraged in the planning stage both at the national and the local levels. For the design of the NDP 2014-2018, the government organised 33 regional dialogues and 27 sectoral forums throughout the country to gather information on local needs and priorities, ensuring the involvement of stakeholders early in the investment cycle. These forums helped the central government to validate its proposals at the subnational level.

At the national and local levels, Colombia has advisory councils for planning investments, a tool that – if well implemented – can give greater legitimacy for investments and greater adherence to the decisions. Since 1994, the National Planning Council (Consejo Nacional de Planeación, CNP) gathers territorial and sectorial representatives as well as community and minorities representatives to analyse and discuss the National Development Plan and ultimately, provide recommendations on the content of the NDP. The territorial expressions of this council (Consejo Territorial de Planeación, CTP) established at the departmental, municipal or district level, aim at favouring the participation and engagement of civil society in local public affairs. Like the CNP nationally, these advisory councils include representatives from different sectors of civil society (education, economic, social, environment, culture and communication), from ethnic minority populations and from subnational governments. They review the PDTs, issue non-binding recommendations and follow-up on the goals established in the PDTs. Yet, the functioning of these councils in territories is limited by low levels of representativeness as well as low capacities and restricted funding (DNP, 2016a). In order to achieve the potential of these existing mechanisms, an evaluation could be held in order to detect the main deficiencies at the local level and design tailored solutions to improve the effectiveness of these councils. Based on this evaluation, the role of the CTPs could be strengthened, especially in the monitoring role of the implementation of the PDTs.

In parallel, Colombia has special committees to evaluate investment projects funded by the SGR. To analyse the suitability, usefulness and the technical, financial and environmental accuracy of SGR investment projects, the OCADs have to settle consultative committees (*comités consultivos*), composed of representatives from the regional commissions on competitiveness (see below), of the CTPs, business and social organisations, higher education institutions, and indigenous local authorities. These committees are by law mobilised to advise the technical secretary of each

OCAD in project evaluation, structuring, prioritisation and approval. Yet, their recommendations are non-binding, which seems to limit interest regarding these mechanisms (DNP, 2016a). To go beyond a symbolic participation of the consultative committees, the agreements reached at the meetings could be made binding. This would also encourage the voluntary participation of local stakeholders and probably balance the representativeness to avoid capture by certain groups.

With the new MGA, citizens will have the possibility to propose investment projects on their own. This is an interesting platform, but the degree to which it will be used will be an important challenge for Colombia. As it is the case for territorial entities, when projects stem from civil society, a challenge is quite present regarding the technical quality of the projects and their high specialisation. Additionally, the process should be accompanied by guidance issued by the central government explaining the framework and the elements required for a successful project. The guidance material should be in simple and in plain language that enables all citizens – not only highly specialised professionals – to propose projects that can be fully and efficiently implemented. Furthermore, opening this possibility may imply important costs for the government as well as a potential risk of capture; while efforts should be focused on developing, strengthening and articulating the existing participatory fora.

So far, stakeholders’ involvement appears to be limited by low skills and scarce financial resources for participatory and networking processes in many subnational governments. At the same time, local authorities may show resistance to stakeholders’ involvement, seeing it as a constraint for their administration. This could lead to an absence of commitment in providing adequate information. High levels of mistrust also hamper participation, as stakeholders do not believe in the real impact of such processes. To overcome this, the challenge of integrating the feedback of consultative committees into investment decisions should be complemented by an improvement of communication channels to socialise the concrete impacts of these processes.

It is worth mentioning that stakeholder engagement is not without risk. Effective stakeholder involvement can help governments craft an informed strategy for long-term development. However, governments face a trade-off between improving their knowledge and the potential for “capture” when particular stakeholders drive investment strategy. In Colombia this is particularly important, especially in conflict areas. It is crucial that while engaging stakeholders the government take steps to prevent capture by special interest groups. Thus, either in the CTP or in the consultative committees, the government or the OCADs have to ensure balance when incorporating stakeholders’ views, as well as open and transparent processes.

Stakeholders monitor the implementation of investment projects

Although Colombia has developed channels for stakeholders to monitor investment projects, fragmented information and weak feedback limit the usefulness of these mechanisms. As for investments funded by the national budget, information is available through the Investment Project Monitoring (Seguimiento a Proyectos de Inversión, SPI), which provides the data of all investment projects included in the national budget. In parallel, investment projects funded by the SGR can be monitored through MapaRegalías. These platforms seem to be underused by stakeholders for two main reasons: weak diffusion and no articulation between the SPI, Sinergia Seguimiento and MapaReglías. To improve the information available to stakeholders, the Result-oriented Budget project being developed with the World Bank seeks to improve articulation between both systems to ensure better accessibility to information on public investment for citizens, regardless of the funding source.

Some efforts to integrate civil society's and citizen's inputs have been made. Visible auditing (*auditorías visibles*) is an interesting process managed by the DNP (and supported by the UNDP and Transparencia por Colombia) to foster citizens' involvement in monitoring and social control of SGR project execution. They consist of public meetings gathering the main stakeholders (authorities, communities and project holder), in which the authorities and project holder discuss the project and its implementation process, and commit themselves with the citizens on key aspects. During the implementation phase, technical visits and/or a citizen auditing group check the compliance with these commitments, and at the end, a collective evaluation is performed. This space has proven to be successful, and national authorities (but not subnational governments) are considering using this tool for other sectorial policies. Between 2008 and 2016, 657 projects have been audited, involving 90 546 people (DNP, 2016a).

The Citizen Perception Poll (*Encuesta de Percepción Ciudadana*, EPC), which measures citizens' perception on public policy results, is an interesting instrument to reinforce citizens' feedback and enhance trust in government. Between 2011 and 2014, eight polls were held on all of the pillars of the 2010-2014 NDP. From 2015 on, it focuses on the 2014-2018 NDP, with biannual polls. They include about 10 000 adult citizens from urban and rural areas in all 6 regions, 3 metropolitan areas and Bogota. Since 2015, the government uses the results to monitor by sector the extent to which public policy is meeting citizens' expectations (DNP, 2016a).

Still, while participation mechanisms in the planning stage and monitoring tools are numerous in Colombia, integrating civil society's and citizen's input in later stages is still limited. The legitimacy of participatory processes is at stake when it is not sustained throughout the investment cycle and participation may be discouraged if citizens' feedback or evaluations are not considered.

Box 4.12. **Monitoring investments: OpenCoesione in Italy**

The OpenCoesione web portal provides analysis and monitoring on the use of regional policy resources, offering information, accessible to anyone, on what is funded, who is involved and where. The web portal contains information about every single project carried out to implement EU Cohesion Policy, and more specifically: funds used, places and categories, subjects involved and implementation timeframes. It concerns more than 700 000 investment projects (around EUR 17 billion, funded by national and local governments). Users can either download raw data or surf through interactive diagrams itemised by expenditure categories, places and type of intervention, as well as have access to files on single projects and subjects involved. Data on the local economy and social context are provided as well.

Source: OECD (2015b), "Effective public investment across levels of government: Principles for action", https://www.oecd.org/effective-public-investment-toolkit/Effective-Public-Investment-Brochure.pdf.

Dialogue and participation beyond public investment

Other interesting initiatives that focus on local stakeholders' dialogue and participation – that go beyond strict public investment – can be mentioned at both the national and local levels:

- The agreements for prosperity (*acuerdos para la prosperidad*): deriving from the community councils established by the previous government, the agreements for prosperity are conceived as co-ordinating institutions between citizens, subnational governments and the central government to support and monitor regional development. One of the most relevant characteristics of these agreements is that they are monitored by the High Council for the Regions and Citizens' Participation with the Presidential Office and involve personally the President of the Republic who participates directly in public debates.

- Colombia's citizen watchdogs, *veedurías ciudadanas*: created by civic leaders, the approximately 500 watchdogs promote the social surveillance of public management at the local level. Their objective is to stimulate the exercise of substantive citizenship and participation, mobilise volunteer work in social responsibility activities and anti-corruption education. This is one of the most successful examples of social accountability in Colombia (OECD, 2014a).

- The Rural Pact: in the framework of the pact, a major consultation process based on public hearings and discussion between citizens and representatives of the government has been launched all over the country. These hearings will inform the National Development Plan 2014-2018.
- Regional commissions for competitiveness (*comisiones regionales de competitividad*, CRC): the CRC are entities that aim at favouring the dialogue and co-operation between business and the public sector on issues related to competitiveness and productivity (and play an important role in creating an environment in which business and public authorities can co-operate. These commissions are co-chaired by public authorities and the private sector, and they will increase their scope with the implementation of the Integrated Productive Development Policy.
- At the local level, the city of Medellín and the department of Antioquia have developed sophisticated co-ordination arrangements and mechanisms to involve citizens – Medellín is one of the largest cities to implement participatory budgeting. It has sought to build its long-term vision with the enhanced engagement of private actors.
- With the new MGA citizens may propose projects. It is designed in a way that allows traceability on the process during the life cycle of the project.

Box 4.13. **Benchmarks on stakeholders' involvement**

In **Canada**, different stakeholders intervene in regional development, including local not-for-profit organisations, universities and other post-secondary institutions, and the private sector (banks, small and medium-sized enterprises, etc.). A key element of the regional development authorities (RDAs) model is to establish a network with all relevant stakeholders when delivering programmes and initiatives. The partnerships are partly the reason why RDAs can cover a large territory with limited resources and thus, the network is key to succeed. The RDAs' role is complementary to that of the other players; RDAs create synergy, cross-sector collaboration and community economic development opportunities. RDASs work with other federal departments and agencies as well as provincial governments and academia to strengthen SMEs' innovation, commercialisation and exports. The RDAs work with the private sector in two different ways: 1) to take into consideration the needs of businesses when developing programmes; 2) to facilitate access to capital for firms which complements funding received by banks and other financial institutions.

Box 4.13. **Benchmarks on stakeholder's involvement** (*continued*)

In co-operation with the provinces, territories and municipalities, as well as First Nations and the private sector, the government of Canada has implemented a variety of joint infrastructure programmes on a nationwide scale. Some of these programmes are delivered by RDAs, such as:

- Building Canada Fund: provided funding for municipal infrastructure projects, particularly in smaller communities from 2007 to 2014. It focused on improving infrastructure in areas such as water, wastewater, culture and recreation.
- Canada 150 Community Infrastructure Program: supports projects that rehabilitate existing community and cultural facilities across Canada, including projects designed to promote the Government's priorities to ensure a better future for Indigenous peoples and promote a clean growth economy. A part of the federal government's celebration of Canada's 150th anniversary of Confederation in 2017, this program responds to the significant demand for community infrastructure improvements.
- The Municipal Rural Infrastructure Fund: aimed at improving the stock of core public infrastructure for municipalities with populations of less than 250 000 in areas such as water, wastewater, culture and recreation.

In 2007, **Denmark** sought to promote greater efficiency as well as a more regional approach through municipal reform. Fourteen counties were restructured into 5 regions, and 271 municipalities reduced to 98. As part of the reform process, each region was required to appoint at least one regional growth forum to guide regional business development strategies and the use of associated regional and EU Structural Funds. By law, the 20-member public-private boards include regional and municipal elected officials, business persons, representatives of the higher education and research community, and trade unions. Members are appointed by the Regional Council upon recommendation by the municipalities and social partners. They meet four to six times a year and are supported by the regional administration.

In **Germany**, the decision to build a new runway at Frankfurt Airport (Germany's largest airport) was accompanied by a so-called mediation process initiated by the state government of Hesse. It had the goal of reconciling concerns about noise and other environmental effects with the economic case for the new runway. The process was initiated prior to the decision to build the runway and included extensive consultations with proponents and opponents of the new runway. Most recommendations made by the mediators were implemented in the planning process. After the end of the mediation process, a regional forum continued the dialogue between stakeholders until the planning process for the new runway was completed and construction started.

Source: OECD (2012) and OECD (2015b).

Recommendations

Strengthen the capabilities of public officials involved in public investment

- The various technical assistance programmes need to be better co-ordinated with a special focus on weaker municipalities.
- To develop institutional capacity and professional skills, Colombia should avoid changing the rules of the game too often. A consistent investment framework over time is a key lever to strengthen subnational capacities on a continuous basis. The CONPES strategy 3856 is a step in the right direction, with the standardisation of certain investment projects.
- To improve the management of subnational civil servants, Colombia may consider developing a comprehensive quantification of subnational public employees to get a clearer picture of the needs and gaps of territorial entities. With this it is possible to identify the most problematic capacity gaps and list a required set of skills for the recruitment of civil servants.
- The role of departments for municipal capacity building and technical support should be better acknowledged and supported. The departmental level has greater expertise and can perceive undeveloped capacities in municipalities designing targeted training. The EDI should be used to guide technical assistance and training.
- Partnerships with departments and with the Colombian Municipalities Federation need to be promoted, including the exchange of good practices among subnational governments and peer learning mechanisms. Asocapitales proposes this kind of process among capital cities and within metropolitan areas.
- If created, the future regional and departmental development agencies should be used as technical support co-ordinators.

A systemic approach to capacity building for public investment

- To reduce regulatory burden, a multi-level dialogue platform can serve to define mechanisms by which the central government can support and motivate territorial entities. The platform can also provide a system to monitor compliance with specific milestones, which can feed back to central government and inform the incentives and support provided to subnational entities (OECD, 2013b).

- Efforts should be put in revising administrative regulations to identify obsolete or overlapping procedures or reports that could be consolidated or modernised. In particular, Colombia should reduce or consolidate financial monitoring reports of investments separated by funding source to reduce administrative burdens at the local level.

- Efforts on supporting subnational entities to strengthen their institutions and implementation of tools should be pursued. In some cases, such as the implementation of subnational simplification initiatives, there is scope for the central government and territorial entities to move forward through pilot programmes for specific subnational jurisdictions.

- Colombia could implement a decentralised procurement system allowing subnational governments to purchase goods and services at the local level and to use the new advanced electronic platform set up in 2015, the Digital Procurement System (Sistema Electrónico de Contratación Pública, SECOP II).

- Procurement needs to be focused on outcomes and not just compliance with formal requirements. It seems necessary to move from a control system based on a formalist approach to a system based on the evaluation of results.

- Colombia has to consistently work to strengthen subnational capacities for public-private partnerships, through for example the introduction of a national PPP unit, line ministry units and the standardisation of contracts.

Support asymmetric decentralisation

- Asymmetric decentralisation needs to be further exploited in two directions: 1) the most capable subnational governments can handle additional competencies as planned in the programme currently in place on differentiated competences; 2) weaker ones need simplified reporting mechanisms to alleviate the administrative burden.

- Colombia could take advantage of pilot experiences in the devolution of competencies as a way to ensure a gradual institutional change and learning-by-doing. The delegation over the cadastre to Barranquilla needs to be carefully monitored to replicate good practices and avoid pitfalls.

- To strengthen local autonomy, an important element of the tax reform could be the differentiation of own-managed taxes between municipalities depending on their size and capacity. Cities with stronger managerial skills should have more autonomy on the use of and decisions concerning their financing mechanisms.

Better assess investment projects **ex ante** *and* **ex post**

- Colombia should put more emphasis on the selection and design of projects as well as on *ex post* evaluations – without neglecting control on the contracting and execution stage.
- Include operational and maintenance costs in the *ex ante* appraisals of investment projects. Colombia may also include social or environmental costs or benefits in these evaluations. Given the high territorial heterogeneity across the country, it is important to consider risks particular to some regions or localities.
- Simplify the General Adjusted Methodology guidebook that is currently very unevenly used by municipalities. In parallel, Colombia should pursue training that is currently underway. Given the high turnover of staff it is possible that this training effort has to be constantly repeated.
- Standardise and simplify the reporting mechanisms to the National Bank of Programmes and Projects - Banco Nacional de Programas y Proyectos.
- In some cases, for major projects where appraisal is particularly complex, there may be a need to tap technical expertise in organisations or units (public or private) with independence, experience and a good reputation for such analysis. In some cases, for weaker municipalities and/or complex projects, it may be worth considering devolving the preparation of investment projects to the department or government agencies (DNP, FINDETER, FONADE).
- Technical assistance for municipalities could be combined with funding for the externalisation of part of the *ex ante* appraisal to the benefit of external expertise.
- Appraisal methodologies may be differentiated according to the size of the project or its complexity. This would mean less rigorous appraisal for smaller projects and more rigorous assessment for larger or riskier projects.
- Monitoring should focus more on programmes and project evaluation with an integrated perspective among financing sources.
- Pursue the "Result-oriented Budget" project to integrate the various monitoring and evaluation tools.

- Colombia should set incentives for contract enforcement. For example, it could allocate part of the funding based on good performance (performance reserve, on the model of Italy or the EU).
- To improve the availability of data and its use it may be relevant to build Sinergia Seguimiento indicators at intermediate territorial levels (departments), as the update for 2014-18 only considers the six macro-regions.

Engage with stakeholders throughout the investment cycle

- To engage effectively with stakeholders throughout the investment cycle, Colombia should articulate and homogenise participation and information platforms. A multiplicity of platforms may hinder rather than encourage participation. Articulation between consultative committees and the CTPs should be improved and the information of Sinergia Seguimiento, MapaRegalías and the Investment Projects Monitoring System should be co-ordinated and homogenised. The system of MapaInversiones currently being prepared is a good step in that direction.
- To achieve the potential of the CTPs, Colombia may carry out an evaluation to detect their strengths and weaknesses and design tailored solutions to improve the effectiveness of these councils. Based on this evaluation, the role of the CTPs could be strengthened, especially in the monitoring role of the implementation of the local development plans.
- Participatory platforms and platforms to access information are quite developed in Colombia. Efforts should therefore be focused on developing, strengthening and articulating the existing participatory fora. Improving communication channels to socialise the concrete impacts of these processes is crucial.
- Going beyond a symbolic participation of civil society in consultative committees, the agreements reached at the meetings could be mandatory. This would also encourage the voluntary participation of local stakeholders.
- Information accessibility should be improved for citizens and stakeholders alike. Make investment information available in a timely, visible and simple way. A compulsory, timely and standardised display of accounts on the subnational governments' website (or on a specific dedicated website) would enhance transparency on their financial management as a whole.

- While engaging stakeholders, the Colombian government has to take steps to prevent capture by special interest groups. Thus, either in the CTP or in the consultative committees, the government or the OCADs have to ensure balance when incorporating stakeholders' views, and open and transparent processes.
- Citizens' control mechanisms such as visible auditing should be used more widely and more generally. There is a need to ensure that engagement procedures are transparent and consistent with the *OECD Principles for Transparency and Integrity in Lobbying*.

Notes

1. In this sense, the new municipal code of 2012 (Law 1551) may conflict with Law 617 of 2000, which set limits on the ratio of discretionary current expenditure (e.g. to pay some new officials) to non-earmarked current revenues according to the size of subnational governments.
2. The *Doing Business in Colombia 2013* report is the third subnational report of the Doing Business series in Colombia. It compares business regulations across 23 cities. The report focuses on local and national regulations that affect five stages in the life of a small to medium-size domestic firm: starting a business, dealing with construction permits, registering property, paying taxes and trading across borders. It identifies differences in local regulations and the enforcement of national regulations at the local level that can enhance or constrain local business activity.

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Annex A.
Indicators for multi-level governance of public investment in Colombia

1. Coherent planning across levels of government		
	The country has regional development policies/strategies to support regional development and local investments.	
a	No explicit national policies to support regional development	
b	Explicit national policies to support regional development in all or parts of the country	X
c	Explicit national regional development policies completed by regional investment strategies aligned with it	
2. Co-ordination across sectors in the national planning process		
	The country has mechanisms to co-ordinate across sectors national policies and investment priorities for regional development	
a	No mechanism	
b	At least inter-ministerial committee and/or cross-ministerial plan	X
c	Inter-ministerial committee and/or plan + other mechanisms	
3. Vertical co-ordination instruments		
	The country has mechanisms to ensure co-ordination across levels of governments (regional development agencies, national representatives in subnational governments, and contracts or agreements)	
a	None of these	
b	At least one of these mechanisms	X
c	At least one of these mechanisms involving many sectors	
4. Multi-level dialogue to define investment priorities for regional development		
	The country conducts regular dialogue(s) between national and subnational levels on regional development policy including investment priorities	
a	No regular dialogue	
b	Formal or ad hoc dialogue	X
c	The platform has decision-making authority	
5. Horizontal co-ordination across jurisdictions		
	The country has formal horizontal mechanisms/incentives between subnational governments to co-ordinate public investment	
a	No mechanisms	
b	Formal horizontal co-ordination mechanisms at the municipal level	X
c	Formal horizontal co-ordination mechanisms at the municipal level and other subnational levels (state, regions)	

6.Performance monitoring and learning		
	The country has mechanisms in place to monitor and evaluate regional development policy	
a	No mechanisms	
b	The country has indicators to monitor the effectveness of regional development policy	
c	The country has conducted evaluations of regional development policy	X
7. Regulatory co-ordination across levels of government		
	The country has mechanisms to co-ordinate regulations across levels of government	
a	No intergovernmental co-ordination mechanisms	X
b	Formal co-ordination mechanisms between national/federal and state/regional governments	
c	Requirement of national government to consult subnational governments prior to issuance of new regulations that concern them	
8. Co-financing arrangements across national and subnational levels		
	There are co-financing arrangements for public investment	
a	No co-financing arrangements	
b	Co-financing arrangements exist but funds are not tracked	
c	Co-financing arrangements exist and funds are tracked	X
9. Subnational governments benefit from predictible capital transfers over time		
	Variations in total capital transfer from one year to the next	
a	Large variation: more than 20%	
b	Medium variation: between 10% and 20%	X
c	Little variation: less than 10%	
10. Transparent information across levels of government		
	Subnational fiscal situation is publicly available	
a	Not available for any type of subnational government	
b	Available for regions/states/some level of subnational government only (on an individual basis)	
c	Available for each subnational government individually	X
11. Fiscal stability: rules for subnational governments		
	There are limits on subnational borrowing	
a	No limits on subnational government borrowing	
b	Non-binding borrowing constraints	
c	Binding borrowing constraints	X
12. Safeguarding capital spending at subnational level		
	Balanced budget rules protect subnational capital spending	
a	No balanced budget rule	
b	Balanced budget rule with no exception for capital spending	X
c	Balanced budget rule protecting capital spending (type golden-rule)	

Source: OECD (2016), Indicators of co-ordination of public investment for regional development.

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