McKinsey&Company

Municipal Revenue Maximization

WORKSHOP DOCUMENT

10 July 2018

Agenda

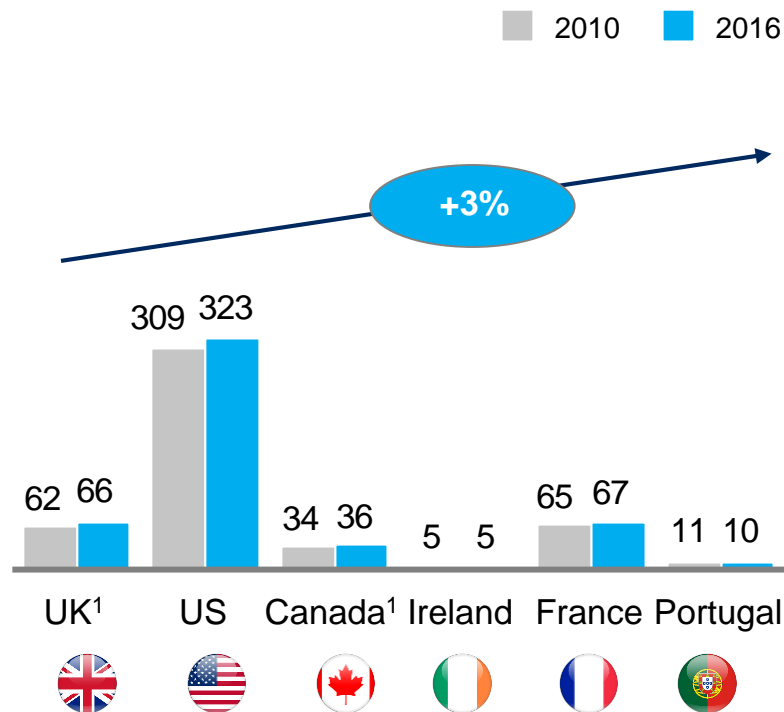| 5 mins	Introduction
20 mins	Group exercise
30 mins	Approach for revenue maximization
15 mins	Case study
20 mins	Q&A

Context and problem statement

■ Focus of this session

Central government funding for municipalities is decreasing…

… and population growth is adding a cost burden to municipalities

Need for municipalities to become more financially sustainable

Central government funding as the share of total municipal revenue[1], %

☐ 2010   ■ 2016

-55%

	UK[1]	US	Canada	Ireland	France	Portugal
2010	19	11	9	9	9	5
2016	14	9	8	3	5	4

Total population, mn

☐ 2010   ■ 2016

+3%

	UK[1]	US	Canada[1]	Ireland	France	Portugal
2010	62	309	34	5	65	11
2016	66	323	36	5	67	10

There are **two ways for municipalities to establish financial sustainability**:

1 Revenue maximization

2 Cost optimization

1 Based on OECD report on intergovernmental transfers; internally consolidated between the Central and Social Security sectors only

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Exercise: identify top 10 revenue levers in your city and allocate them to framework

NON-EXHAUSTIVE

Service fees	Fines	Charges/taxes	Assets/Investments

Revenue levers

Solution space: potential revenue levers

Revenue levers

Service fees

- Toll road fees
- Business licenses fees
- Construction permit fees
- Development permit fees
- Land registration fees
- Excavation fee
- Telco tower
- Waste fees
- Public parking fees
- Public toilet fees
- Public Wifi fees
- Funeral fees
- Pet licensing fee
- Universal municipal services fee
- Utility fees

Fines

- Building license violation
- Gardens and public parks violation
- Public health violation
- Residential units and real estate violations
- Roads and infrastructure violations

Charges/taxes

- Congestion charge
- Property (municipal) tax
- Land transfer tax
- Vacant land tax
- Betterment levies
- Advertisements tax
- Hotel occupancy tax
- Municipal sales tax
- Recycling tax (e.g. bottled water tax)
- Municipal vehicle/carbon tax
- Municipal alcohol tax
- Other excise taxes

Assets/ Investments

- Naming rights
- Billboards & Signs
- Municipal vacant land
- Municipal data
- Parks
- Beaches
- Mountain resorts
- Housing units
- Commercial units
- Slaughterhouses
- Public markets
- Returns from equity and bond investments

Solution space: potential interventions

Revenue streams

Interventions		Service fees	Fines	Charges	Assets/Investments
Charge More	Market Prices	Increase pricing based on benchmarks and/or associated cost to serve wherever applicable			
	Differentiated Levels	Revise pricing model leveraging differentiating factors specific to each revenue lever category • Examples of differentiating factors include size, location, validity period etc.			
	Fees for Convenience	Increase pricing by providing faster processing time and/or higher quality service			
Increase number of transactions		• Increase quantity of service offerings and/or assets/investments • Increase surveillance/inspection for selected fine sources to maximize detection of violations			
Improve collection		Optimize collection and audit process to increase collection rate and minimize leakage			
Introduce new revenue levers		Introduce new types of service fees, fines and charges			

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A four step approach could help municipalities to have a robust and efficient revenue optimization program

I

Preparatory work

(A) Finalize **data collection of current revenue baseline**

(B) Develop and **run a citizen sentiment survey** to understand receptiveness of citizens to changes in fees and charges

II

Gap analysis and opportunity sizing

(C) Analyse **revenue baseline** for municipalities across all streams

(D) Conduct **benchmarking across all streams** and identify potential gaps

(E) Determine **revenue generation levers with initial adjustment for relevance and size the potential revenue impact**

III

Opportunity Prioritization

(F) Assess the **feasibility of each lever along three dimensions**:

– **Social acceptance**: Citizens & businesses receptiveness

– **Impact on economy**: Impact on inflation, GDP and ranking on global competitiveness indices

– **Ease of implementation**: Technical feasibility & readiness

(G) Prioritize **the levers along revenue impact and feasibility dimensions**
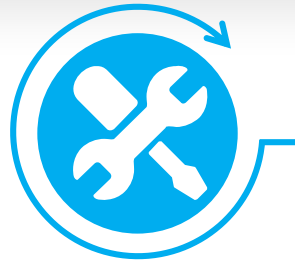
IV

Implementation planning and detailing

(H) Develop **implementation plan for prioritized levers** with needed intervention

(I) Review the **current regulations and identify the regulatory changes** that need to be made

B A critical part of preparatory work lies in understanding public perception of fees, fines and charges

List of services	Willingness to pay for better service delivery[1]

Citizen satisfaction survey N = 1114

(Low) ... (High) scale: 0 1 2 3 4 5 6 7 8 9 10

- Cemetery affairs — 5.1
- Protection against natural disasters — 4.3
- Obtaining title deeds — 4.3
- Execution of land grant decisions — 4.2
- Garbage collection — 4.0
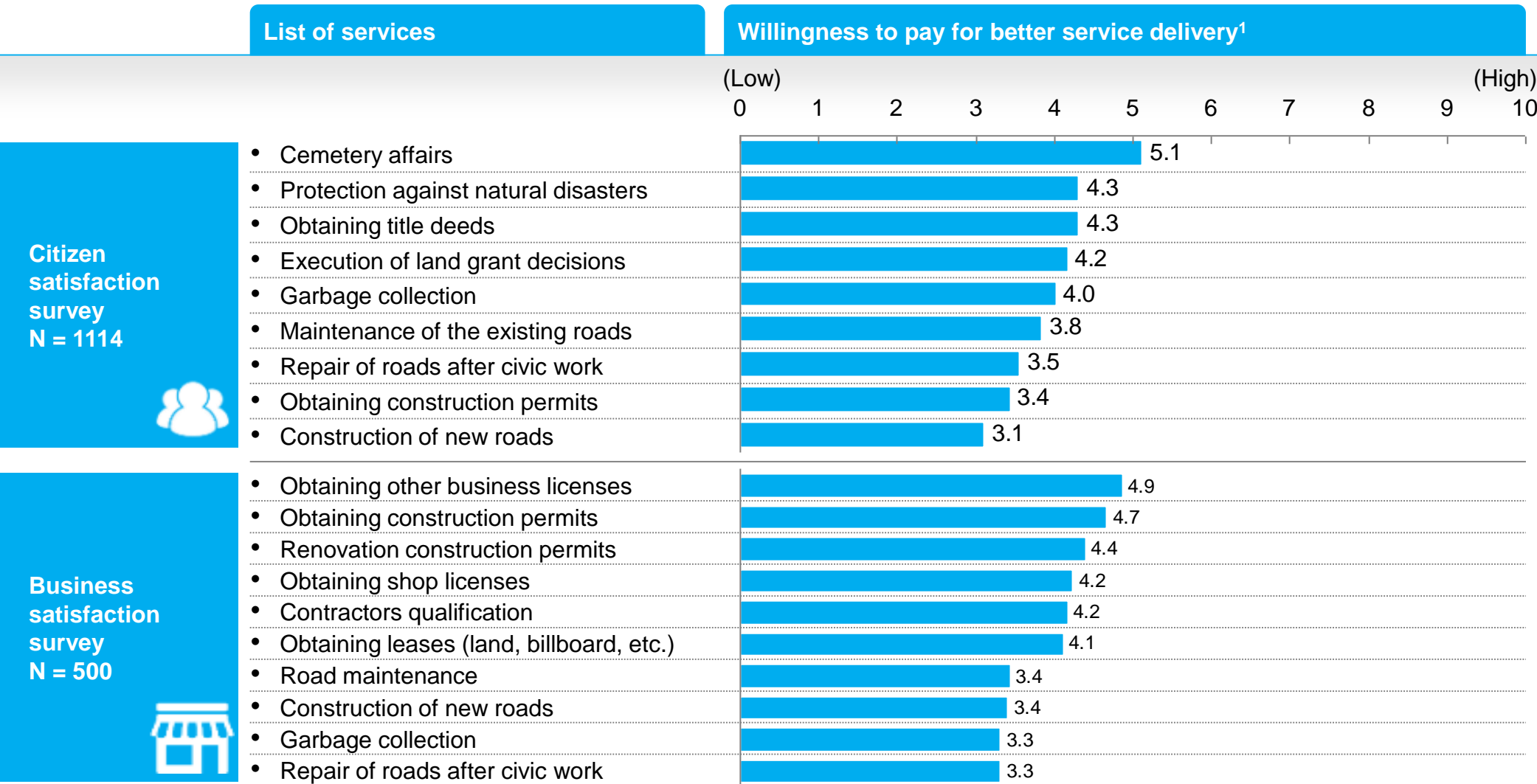- Maintenance of the existing roads — 3.8
- Repair of roads after civic work — 3.5
- Obtaining construction permits — 3.4
- Construction of new roads — 3.1

Business satisfaction survey N = 500

- Obtaining other business licenses — 4.9
- Obtaining construction permits — 4.7
- Renovation construction permits — 4.4
- Obtaining shop licenses — 4.2
- Contractors qualification — 4.2
- Obtaining leases (land, billboard, etc.) — 4.1
- Road maintenance — 3.4
- Construction of new roads — 3.4
- Garbage collection — 3.3
- Repair of roads after civic work — 3.3

Global case studies indicate that **successful** increases in prices for fees and fines were in turn **compensated by offering higher quality services**

1 Based on 1-10 scale; 1 (Will not pay) - 10 (High willingness to pay)

SOURCE: McKinsey & Company

D | A comparative perspective assessing city performance vs. international benchmarks could help to define the upside potential

DISGUISED CLIENT EXAMPLE

Per capita per annum municipal revenue, USD
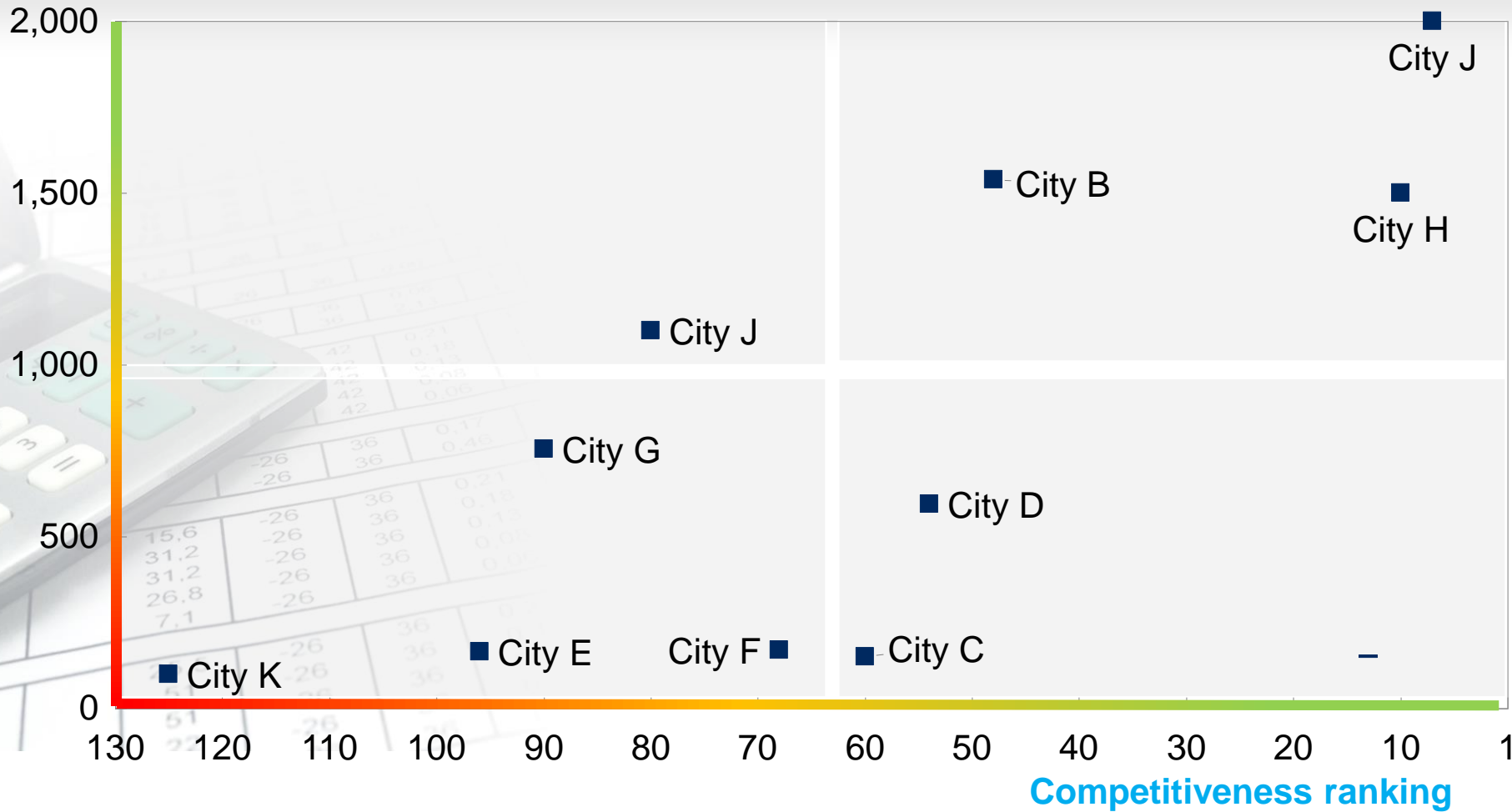
Comparative perspective could help municipalities to **determine top-down upside potential** based on the revenue generated by the cities with similar competitiveness ranking

Competitiveness ranking

F | Assessment along three dimensions for each lever could help determine the feasibility

Dimensions	Factors	Assessment Questions
1 Social Acceptance	Visibility	Is the *magnitude of change significant*, hence *visible for citizens and businesses*?
	Potential public benefit	Does the *revenue lever induce positive behavior* and/or does it have *a clear public benefit*?
	Price against benchmarks	Is the level of fees, fines or charges *higher or lower compared to regional benchmarks?*
2 Economic impact	Impact on GDP	What will be the *impact* of lever *on GDP*?
	Impact on inflation	What will be the *impact* of lever *on inflation*?
	Impact on competitiveness	How does the lever *affect the position of city on various competitiveness indices*?
3 Ease of implemen-tation	Technical readiness	Is municipality *technically ready* to introduce the selected lever?
	Resources requirements	What *kind of additional resources* does the lever require?
	Alignment with government agenda	Is the lever *in line with government agenda/ roadmap* for the corresponding area?

Municipalities could leverage revenue-feasibility matrix to prioritize levers

■ High ■ Medium ■ Low

Potential revenue impact

Wave-III

✓ **Have significant impact on competitiveness AND lower social acceptance**

Wave-II

✓ **Potential upside <5% of municipal revenue AND require strategic intervention for implementation**

Wave-I

✓ **Potential upside >5% of municipal revenue AND no major impact on competitiveness**

✓ **Potential upside <5% of municipal revenue AND can be implemented immediately**

Feasibility

Guiding principles for revenue maximization programs

1 **Fix the home**

A significant upside can be generated from (A) enhancing collections and (B) enhancing asset monetization

2 **Cover cost to serve whenever possible**

For direct fees, ensure fee levels **cover at least the cost to serve**

3 **Introduce innovative fees / charges**

- Offer **new charges only** if they **induce positive behaviour and/or have a clear public benefit**
- Offer **VIP services** where higher fee levels come with higher quality

4 **Close remaining revenue gap with a bundled charge(s)**

Limited number of charges/taxes ensures **higher social acceptance and minimal collection leakage**

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Successful case study: we supported a municipal system in generating 30% year-on-year increase in municipal revenues

Approach

- **Identify revenues increase opportunities** from new fees and services (e.g., hotel occupancy fees, commercial waste fees, excavation fees)

- **Define and approve all regulatory** requirements needed to launch the new fees and fines

- Design and implement **performance management** tools and process and governance model

Impact

USD 400bn
New revenue sources

30%
Increase in revenues in first few months of implementation
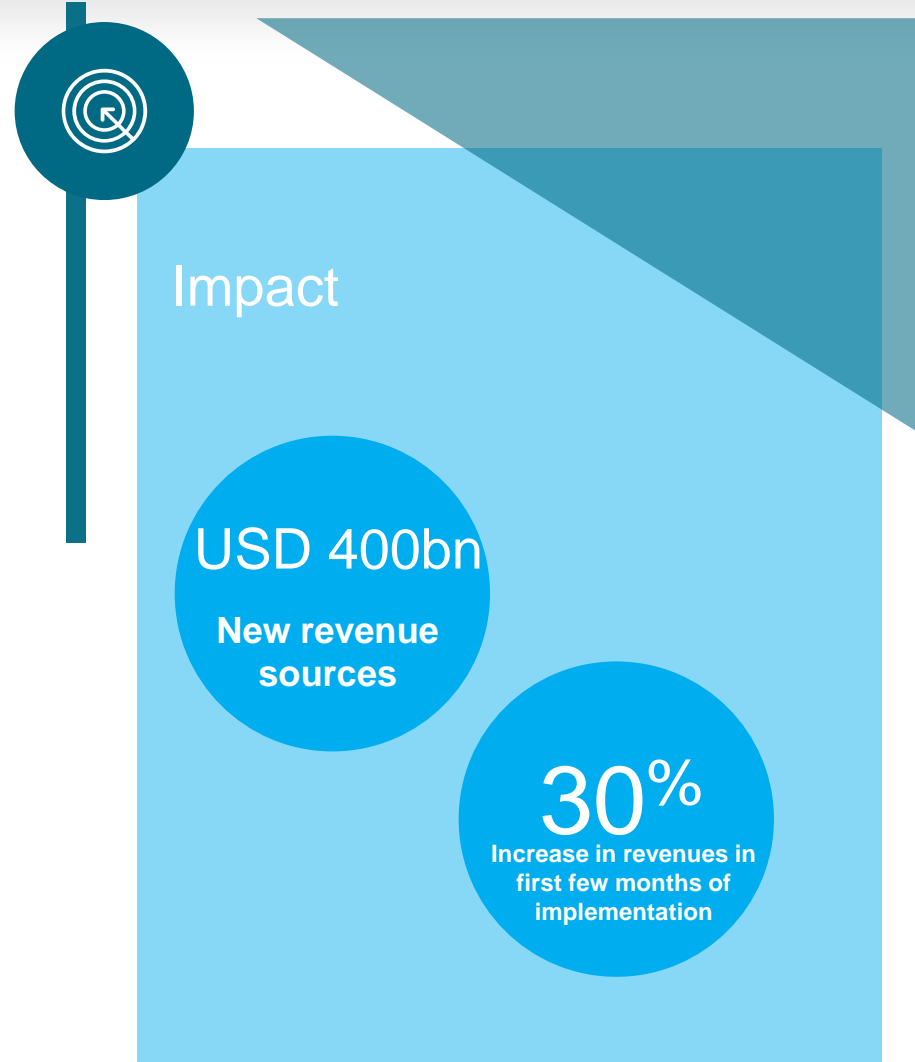
Successful case study: deep-dive on land monetization for income-generating assets

Baseline revenue indexed to 100

200

100%

100

Baseline

Identified potential

Sample assets[1]

Slaughter-house

Public markets

Shopping centre/ Strip mall
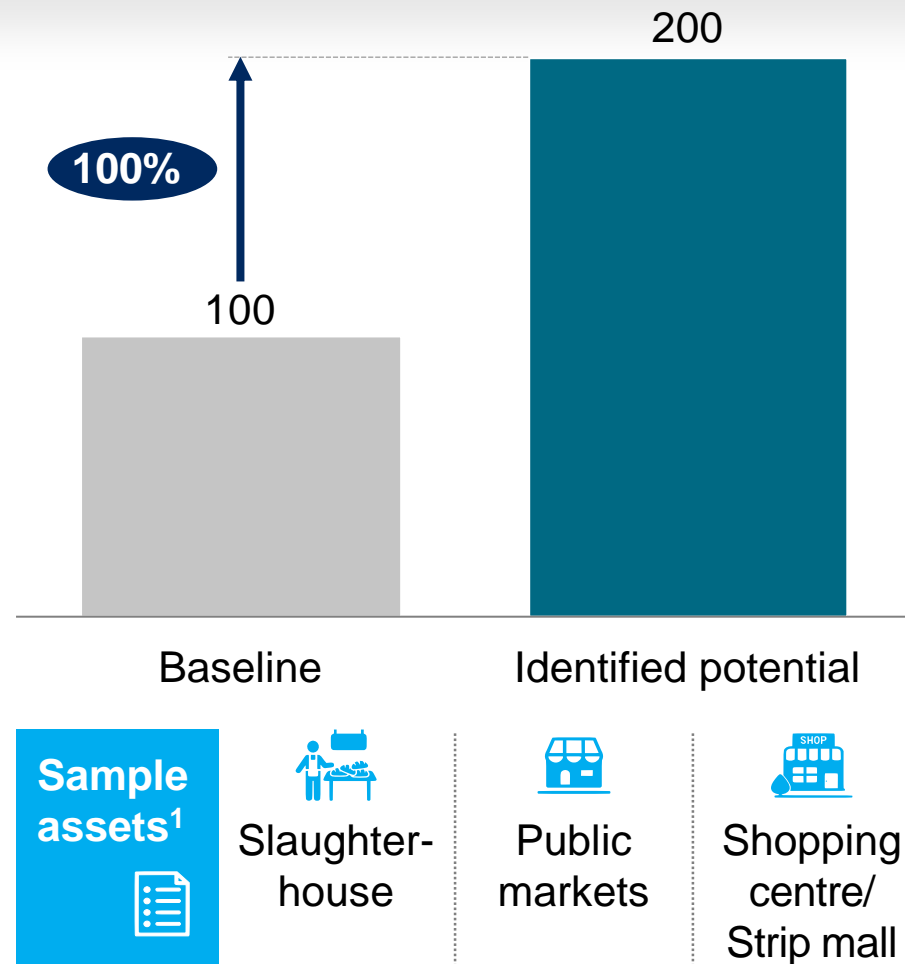
Key optimization levers

Alignment to market value

Providing incentives
- Increased FAR
- Increased duration
- Violations

Enhancing contract terms (e.g. payment terms)
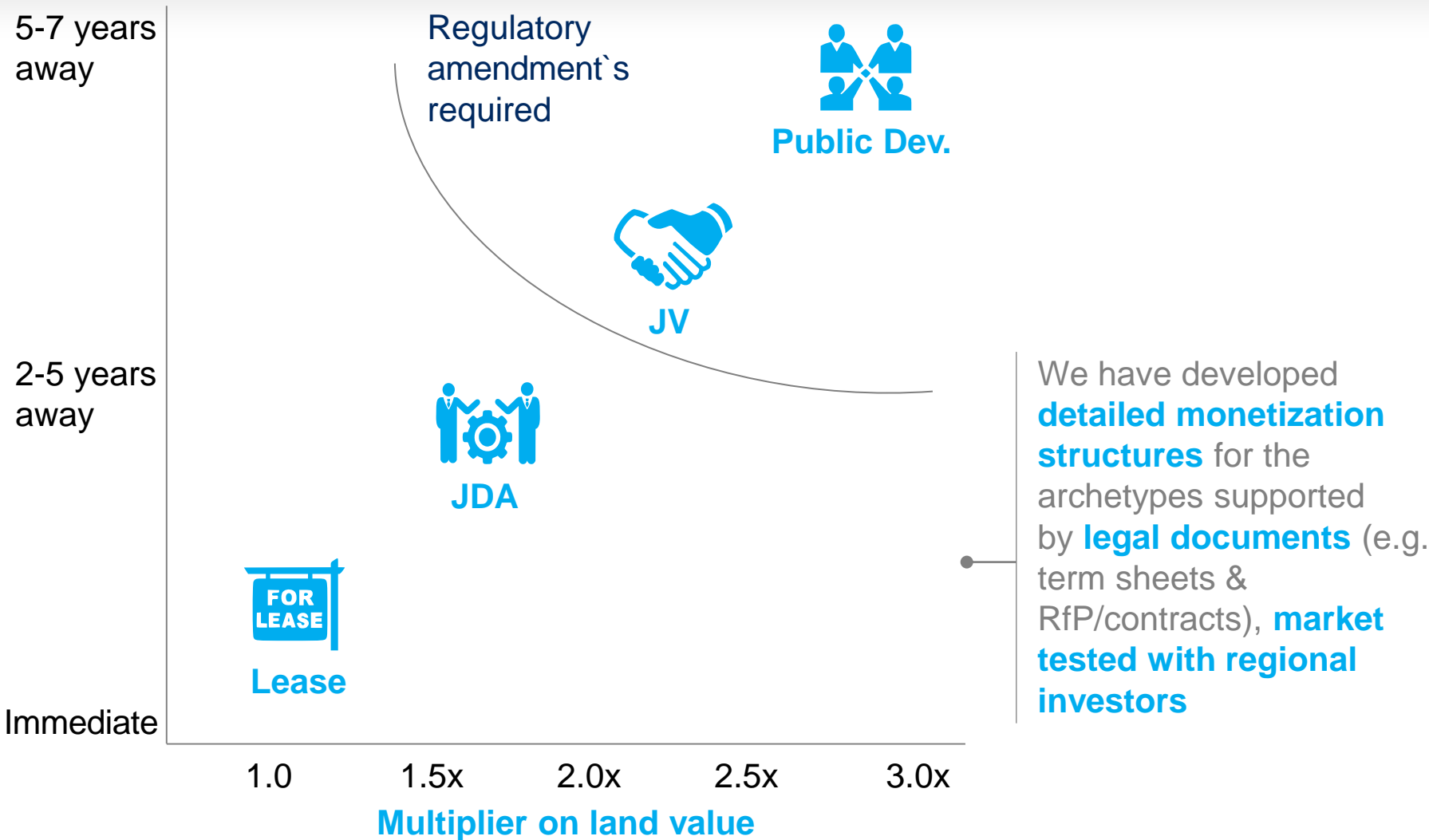
Modifying plot usage

Key enablers

Fact based negotiations supported by detailed fact packs

Training & capability building program
- Negotiations
- Basics of valuation

Key success factor: in the first stage, focus on 10-20% of the assets that generate around 80% of the total value

No need for a lengthy asset register building exercise upfront...

Successful case study: deep-dive on land monetization for non-income generating assets

5-7 years away

Regulatory amendment`s required

Public Dev.

JV

2-5 years away

JDA

Lease

Immediate

1.0   1.5x   2.0x   2.5x   3.0x

Multiplier on land value

We have developed **detailed monetization structures** for the archetypes supported by **legal documents** (e.g. term sheets & RfP/contracts), **market tested with regional investors**

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