



**REPUBLIC OF ALBANIA
MINISTRY OF FINANCE AND ECONOMY
GENERAL BUDGET DIRECTORATE
LOCAL FINANCES DIRECTORATE**

**REPORT ON THE FINANCIAL DIFFICULTIES
ENCOUNTERED BY LOCAL GOVERNMENT
UNITS
YEAR 2020**

Overview of the Key Findings

The consolidated report was prepared by the Directorate of Local Finance at the Ministry of Finance and Economy with the support of the project team “Local Finance”¹, based on the data reported by municipalities and with the purpose of implementing Instruction No. 27, dated 27.9.2019 “On procedures for managing financial difficulties of local government units” (Article 2/i) in order to implement a monitoring system to identify local self-government units which are faced with financial issues, financial difficulties, serious financial difficulties or insolvency. The data include arrears for 58 municipalities, in which the municipalities of Konispol, Pustec and Rrogozhina are missing.

The year 2020 should be considered a special and exceptional year, given the damage caused by the earthquake at the end of 2019 and the COVID 19 pandemic situation, which affected local financial management processes in Albania. Therefore, 2020 is not recommended to be taken as a basis for comparing the trends of LGUs’ financial performance over the years. Due to the limited financial resources, municipalities were forced to cut local expenditures, to reallocate funds trying on one hand to keep only vital services for the community and, on the other hand, to control the risk of creating/increasing outstanding liabilities. The unexpected and far-reaching emergencies led many municipalities to a “stagnant progress” (and some to regression). This experience, however, has helped municipalities by raising awareness and capacity to respond to the current crisis, but also to prepare for future crises.

By the end of December 2020, the stock of arrears for local government units (according to the Government Financial Information System) amounts to ALL 7 billion (ALL 6,895,013,355), which makes up 49% of total financial liabilities of the general government (ALL 14,064,627,507.98²). As can be observed, this is a significant amount which affects directly the fiscal situation of general government. Hence: (i) senior municipal management should pay attention to overdue debt management and should ensure to take on new commitments, and (ii) the Ministry of Finance and Economy must closely monitor or directly control public commitments taken by the municipalities resulting in financial difficulties or insolvency.

Status of Municipalities at the end of 2020 (self-assessment of municipalities)

No. of Municipalities	% of arrears to the total approved annual for 2020	Financial situation of the end of 2020
37 Municipalities	From 0 to 15 %	No financial problems
11 Municipalities	From 16% to 25%	With financial problems
10 Municipalities	From 26% to 70%	In financial difficulties

¹ The “Local Finance” project is funded by the Swiss State Secretariat for Economic Affairs, SECO

² According to the official data of the Ministry of Finance and Economy, “Overdue liabilities-December-2020-as per the final-institutions”

Assessments and Issues

The Ministry of Finance and Economy assessed the financial performance of 37 municipalities in the country that have been able to keep the stock of arrears low, despite the financial difficulties of 2020. It is worth to point out in particular the municipalities of Shkodra, Dropull and Patos. with 0% arrears and 18 municipalities: Tirana, Durrës, Fier, Elbasan, Gjirokastër, Maliq, Shijak, Gramsh, Mallakastër, Vau i Dejës, Prrenjas, Kolonjë, Fushë-Arrëz, Mat, Përmet, Bulqizë, Krujë, Libohovë which arrears are at the level of 1 to 6% of the approved expenditures.

Regardless of the pandemic crisis, total arrears have reduced in absolute value compared to 2019. 38 municipalities have reduced the arrears stock during 2020. Municipality of Kavaja with serious financial difficulties, or other municipalities with financial difficulties such as Dimal, Kukës have made significant efforts to improve their financial situation during 2020 (referring to the approved annual expenditures). Based on the criterion of MFE instruction that assesses the level of financial situation based on the planned annual expenditures, the arrears stock for Vora Municipality is at the level of 75% of approved expenditures and for Kavaja Municipality is at the level of 70% of approved expenditures marking the status of financial difficulty. Ten municipalities are faced with financial difficulties (Roskovec, Lezha, Tepelena, Këlcyrë, Belsh, Pogradec, Kuçovë, Poliçan, Kavaja, Vora), 11 municipalities (Kamëz, Divjaka, Klos, Cërrik, Selenica, Finiq, Tropojë, Delvinë, Kukës Dibër) have financial problems, while 37 other municipalities have a normal financial situation. It is observed that the municipalities with financial problems or financial difficulties are mostly the municipalities with planned per capita expenditures for 2020, below the average of 20,130 ALL per inhabitant.

Meanwhile, the liabilities stock for 20 municipalities increased during 2020. The financial situation has deteriorated for the municipalities of Lezha and Roskovec, which were classified as municipalities in financial difficulties at the end of 2020, while Divjaka Municipality is classified for the first time as a municipality with financial problems.

The status of financial difficulties has significantly deteriorated greatly for 5 municipalities in particular, from municipalities with no financial problems to municipalities with financial problems (Delvina) and in financial difficulties (Kuçovë, Belsh, Këlcyrë). Vlora Municipality in particular, from a municipality with no financial problems in 2019, was classified as a municipality in financial difficulties in 2020, which indicator is at the level 75%, very close to the status of serious financial difficulty.

25.89% of liabilities in 21 municipalities with financial problems or difficulties, are current expenditures, 61.73% are capital expenditures, 11.78% are made up of court decisions and 0.82% are long-term loans. Current expenditures' liabilities have decreased while capital expenditures liabilities have increased as compared to 2019.

The majority of liabilities at all municipalities with over 15% of the approved expenditures are made up of capital expenditures. The following are an exception:

- a. Municipalities of Kavaja, Tepelena and Finiq, which major liabilities are made up of current expenditures, at the level of 72.67%, 70.43% and 55.32% respectively.
- b. Municipalities of Pogradec, Dibra and Lezha, which major liabilities are made up court decisions, at the level of 65.27%, 57.03% and 38.09% respectively.

Lezha is the only municipality which long-term loan liabilities make up 9.08% of its total liabilities.

The ratio of outstanding liabilities to real expenditures of 2020 has deteriorated for a significant number of municipalities. The situation in Vora Municipality is much more serious and outstanding liabilities make up 204% of real expenditures for 2020, given that the budget for 2020 is realized only at the level of 36.6%. In addition, the outstanding liabilities indicator of Kavaja municipality is deteriorated over 100% and the indicators of the Municipalities of Roskovec, Polican is over 50%.

In the circumstances when the average budget of municipalities is realized at the extent of 73.53% and when the budget realization indicator of 28 municipalities is below the average, the municipalities should carefully consider new financial commitments.

Conclusions

The Ministry of Finance and Economy may determine its position according to the responsibilities given by law, adopt support policies for each of the municipalities with financial problems, or give dedicated recommendations regarding the possibility of reducing arrears by improving financial management, only if municipalities submit complete reports (not only tables or partial reports) with an in-depth risk analysis on:

- a) causes that lead to the financial liabilities' accumulation for the municipality.
- b) reaction/decisions of senior management (Mayor, Municipal Council) during the reporting period to prevent or address the risk of creating/increasing arrears in order not to deteriorate the financial situation of the municipality.
- c) difficulties faced by the municipality in settling overdue financial liabilities.
- d) further measures planned for future risk management, specified in the instruction as the plan for settling financial overdue liabilities. It should be pointed out that it does not include only the annual settlement of liabilities in value, but also the relevant actions that calculate the amount to be settled.

Considering the above it is recommended as follows:

- **new financial commitments should be carefully assessed by the municipalities**, in the circumstances when the budget from the municipalities is realized on average at the extent of 73.53% and when the budget realization indicator for 28 municipalities is below the average;
- **all municipalities should approve by the end of 2021 the detailed risk management plan** for creating/increasing arrears and reporting on the basis of this plan according to the above requirements. The Finance and/or Internal Audit units of the municipalities should assess/ verify once again the financial liabilities in accounting on the basis of the debt recognition criteria according to Law no. 48/2014 "On late payments in contractual and commercial obligations";
- **The Ministry of Finance recommends to continue to control the risk of creating/increasing overdue financial liabilities, particularly for the 37 municipalities** listed in graph no. 1 herein, which arrears are at the level of 15% of approved annual expenditures.

The Ministry of Finance and Economy during the following period will pay special attention to:

1. the percentage of the financial arrears stock against real annual expenditures of each municipality, which shows the real figure of financial difficulty, especially in cases of significant differences between the initial budget and the revised annual budget of the municipalities;

2. the progress of settling overdue financial debt from one financial period to another, which shows the level of senior management response to risk and improvement of the municipal financial management. The monitoring will last six months for 10 municipalities with financial difficulties and one year for 11 municipalities with financial problems, shown in graph no. 1 herein.
3. conducting a more in-depth investigation and ongoing monitoring in the municipalities of Vora and Kavaja, which financial situation has significantly deteriorated.
4. considering the possibility of long-term support for the municipalities of Dibra and Pogradec which liabilities are mostly made up of court decisions, 57.03% and 65.27% respectively.

In order to make recommendations for reducing arrears and for better financial management, it is necessary to discuss with municipalities and/or provide assistance in order to be provided with the necessary descriptive information and identify the following:

- difficulties they encounter in settling their liabilities;
- causes leading to the accumulation of new liabilities;
- difficulties encountered by municipalities in preparing arrears monitoring reports.