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

Central government funding for municipalities is decreasing...

Central government funding as the share of total municipal revenue\(^1\), %

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2016</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK(^1)</td>
<td>19</td>
<td>14</td>
<td>-55%</td>
</tr>
<tr>
<td>US</td>
<td>11</td>
<td>9</td>
<td>-25%</td>
</tr>
<tr>
<td>Canada</td>
<td>9</td>
<td>8</td>
<td>-11%</td>
</tr>
<tr>
<td>Ireland</td>
<td>9</td>
<td>3</td>
<td>-67%</td>
</tr>
<tr>
<td>France</td>
<td>9</td>
<td>5</td>
<td>-44%</td>
</tr>
<tr>
<td>Portugal</td>
<td>5</td>
<td>4</td>
<td>-20%</td>
</tr>
</tbody>
</table>

... and population growth is adding a cost burden to municipalities

Total population, mn

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<th>2016</th>
<th>Change</th>
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<tbody>
<tr>
<td>UK(^1)</td>
<td>62</td>
<td>66</td>
<td>+6%</td>
</tr>
<tr>
<td>US</td>
<td>34</td>
<td>36</td>
<td>+6%</td>
</tr>
<tr>
<td>Canada</td>
<td>5</td>
<td>5</td>
<td>0%</td>
</tr>
<tr>
<td>Ireland</td>
<td>65</td>
<td>67</td>
<td>+3%</td>
</tr>
<tr>
<td>France</td>
<td>11</td>
<td>10</td>
<td>-9%</td>
</tr>
<tr>
<td>Portugal</td>
<td>1</td>
<td>1</td>
<td>0%</td>
</tr>
</tbody>
</table>

Need for municipalities to become more financially sustainable

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

SOURCE: OECD, World Bank
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Exercise: identify top 10 revenue levers in your city and allocate them to framework

<table>
<thead>
<tr>
<th>Service fees</th>
<th>Fines</th>
<th>Charges/taxes</th>
<th>Assets/Investments</th>
</tr>
</thead>
</table>

SOURCE: McKinsey & Company
### 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

**SOURCE:** McKinsey & Company
Solution space: potential interventions

Revenue streams

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

SOURCE: McKinsey & Company
## Agenda

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

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

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

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

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

SOURCE: McKinsey & Company
A critical part of preparatory work lies in understanding public perception of fees, fines and charges.

<table>
<thead>
<tr>
<th>List of services</th>
<th>Willingness to pay for better service delivery¹</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(Low)</td>
</tr>
<tr>
<td></td>
<td>0</td>
</tr>
<tr>
<td>Cemetery affairs</td>
<td></td>
</tr>
<tr>
<td>Protection against natural disasters</td>
<td></td>
</tr>
<tr>
<td>Obtaining title deeds</td>
<td></td>
</tr>
<tr>
<td>Execution of land grant decisions</td>
<td></td>
</tr>
<tr>
<td>Garbage collection</td>
<td></td>
</tr>
<tr>
<td>Maintenance of the existing roads</td>
<td></td>
</tr>
<tr>
<td>Repair of roads after civic work</td>
<td></td>
</tr>
<tr>
<td>Obtaining construction permits</td>
<td></td>
</tr>
<tr>
<td>Construction of new roads</td>
<td></td>
</tr>
<tr>
<td>Obtaining other business licenses</td>
<td></td>
</tr>
<tr>
<td>Obtaining construction permits</td>
<td></td>
</tr>
<tr>
<td>Renovation construction permits</td>
<td></td>
</tr>
<tr>
<td>Obtaining shop licenses</td>
<td></td>
</tr>
<tr>
<td>Contractors qualification</td>
<td></td>
</tr>
<tr>
<td>Obtaining leases (land, billboard, etc.)</td>
<td></td>
</tr>
<tr>
<td>Road maintenance</td>
<td></td>
</tr>
<tr>
<td>Construction of new roads</td>
<td></td>
</tr>
<tr>
<td>Garbage collection</td>
<td></td>
</tr>
<tr>
<td>Repair of roads after civic work</td>
<td></td>
</tr>
</tbody>
</table>

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

Global case studies indicate that successful increases in prices for fees and fines were in turn compensated by offering higher quality services.
A comparative perspective assessing city performance vs. international benchmarks could help to define the upside potential.
Assessment along three dimensions for each lever could help determine the feasibility

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

SOURCE: McKinsey & Company
Municipalities could leverage revenue-feasibility matrix to prioritize levers

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

SOURCE: McKinsey & Company
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

Impact

USD 400bn
New revenue sources

30%
Increase in revenues in first few months of implementation

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

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

Baseline revenue indexed to 100

<table>
<thead>
<tr>
<th>Baseline</th>
<th>Identified potential</th>
</tr>
</thead>
<tbody>
<tr>
<td>100</td>
<td>200</td>
</tr>
</tbody>
</table>

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...

Sample assets:
- Slaughterhouse
- Public markets
- Shopping centre/Strip mall

McKinsey & Company 17
Successful case study: deep-dive on land monetization for non-income generating assets

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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