REPORT BRIEF

AN ANALYSIS OF LOCAL AUTHORITY DEBT AND ARREARS IN ZAMBIA

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INTRODUCTION

The research study examines the financial health of local authorities and identifies opportunities to foster revenue generation crucial for service delivery at local level. It explores the accumulation of debt and arears for all 116 local Authorities in Zambia, analysing key factors contributing to financial strain and evaluating policy interventions aimed at enhancing fiscal sustainability.

The methodological approach for this study combined both primary and secondary data collection methods to ensure a comprehensive analysis of Local Authorities debt and arrears in Zambia. Primary data was gathered through key informant interviews (KIIs) with officials from selected Local Authorities, the Ministry of Finance and National Planning (MoFNP), the Ministry of Local Government and Rural Development (MLGRD), and key Cooperating Partners (CPs). These interviews provided firsthand insights into the causes, challenges, and potential policy responses related to debt accumulation and arrears management. In addition to primary data collection, the study also conducted an extensive desk review of relevant policy documents, financial reports, government publications, and previous studies. This mixed-methods approach enabled a deeper understanding of the structural and operational factors influencing local government debt, while also allowing for cross-validation of information obtained from different sources.

FINDINGS

The analysis is based on data obtained from the Central Government for the period 2022–2023, specifically from the MoFNP and the MLGRD. This two year period was selected as the focus of the study due to data unavailability and inconsistencies in previous years, as earlier records were fragmented, unverified, and lacked comprehensive audits. However, beginning in 2022, Local Authorities financial data has improved having undergone auditing by the Office of the Accountant General (OAG), ensuring greater accuracy and reliability. This audited data forms the basis of the analysis, providing a more credible assessment of Local Authorities debt and arrears during the study period.

Findings as at end September 2023, indicate the stock of debt had risen to K4.6 billion from K2.8 billion end-June 2020, representing a 67.9% increase. As a share of the economy, this represents approximately 0.86% of Gross Domestic Product (GDP) in 2023. Further more, Local Authorities' debt falls into three main categories: statutory obligations, staff-related arrears, and debts for goods and services. The largest share is attributed to statutory obligations, including payments and penalties owed to institutions such as the Zambia Revenue Authority (ZRA), the National Pension Scheme Authority (NAPSA), the Local Authorities Superannuation Fund (LASF), and the National Health Insurance Management Authority (NHIMA).

Pensions account for the largest portion at 47.9% (K2.2 billion), affecting employees due to missed contributions and increasing penalties, with NAPSA-related arrears alone making up 14.0% (K645.0 million). Furthermore, Pay- As-You-Earn (PAYE) and its arrears represent 20.8% and 2.6%, respectively.
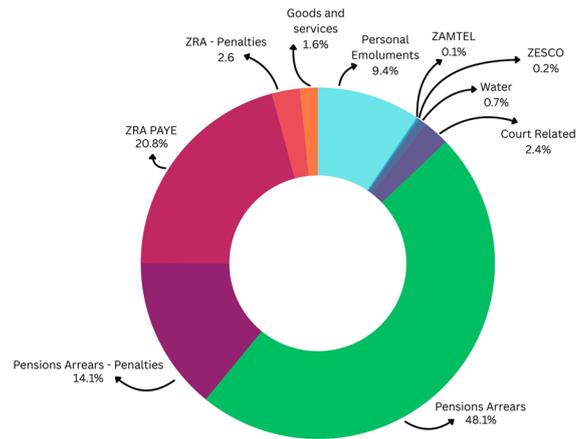
DRIVERS OF DEBT AND ARREARS

Penalties for non- payment of statutory contributions. The study results reveal that Local Authorities are under increasing pressure to remit statutory contributions such as pensions and PAYE, leading to the accumulation of penalties imposed by statutory bodies like NAPSA and ZRA in line with the legal framework. Non-compliance penalties for pension contributions have grown from K638.4 million as of 1st July 2022 to K645.-0 million as of 30th September 2023. By 30th September 2023, penalties accounted for 29.3% of the pension arrears.
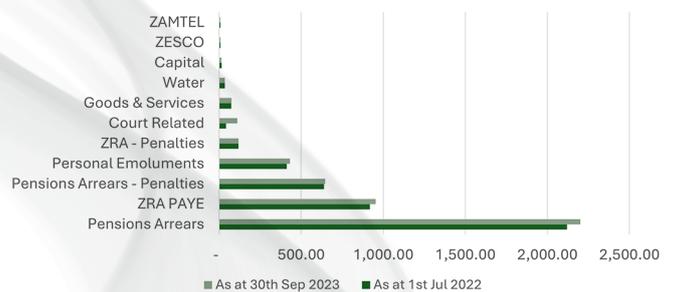
Provinces with high economic activity and stronger revenue bases hold the largest portion of debt and arrears. Findings as at the end of September 2023 Lusaka Province represents 22.6% of total debt and arrears, followed by Copperbelt Province at K807.6 million, or 17.6%. These provinces have higher economic activity and stronger revenue bases. This counterintuitive trend can be attributed to weak internal controls, which undermine financial discipline despite higher revenue potential. Inefficiencies in payroll management, non-compliance with statutory obligations, and revenue leakages weaken the financial health of Local Authorities, making it difficult for them to meet their obligations.

Staff transfers between Local Authorities have significantly contributed to the mounting of debt arising from statutory obligations. In recent years, the Local Government Service Commission (LGSC) has been transferring staff between Local Authorities. However, a key challenge is that transferred staff bring with them accrued debts, including salary arrears and pension liabilities from their previous Local Authority. These liabilities are then passed on to the receiving Local Authority, which often struggles to absorb the additional financial burden due to limited revenue.

MPAs	PENSIONS ARREARS	PENSIONS ARREARS - PENALTIES	ZRA PAYE	ZRA - PENALTIES	Personal Emoluments	OTHER	TOTAL
	K'million	K'million	K'million	K'million	K'million	K'million	K'million
LUSAKA PROVINCE	1,049.754	-	243.621	-	65.786	45.388	1,404.548
CENTRAL PROVINCE	215.863	17.699	210.916	-	63.504	12.351	520.333
COPPERBELT PROVINCE	234.677	122.653	165.244	81.101	69.250	134.684	807.609
N - WESTERN PROVINCE	171.734	0.097	51.154	2.372	35.936	8.231	269.524
WESTERN PROVINCE	32.261	54.329	26.125	1.645	39.002	2.487	155.849
SOUTHERN PROVINCE	130.890	363.575	83.596	28.836	40.169	9.843	656.909
EASTERN PROVINCE	122.865	63.595	68.908	2.195	27.673	11.845	297.082
MUCHINGA PROVINCE	30.400	3.188	23.517	-	26.247	2.519	85.871
LUAPULA PROVINCE	143.774	12.828	29.518	1.235	16.024	8.337	211.716
NORTHERN PROVINCE	69.944	7.049	51.562	-	47.931	10.006	186.492

SUSTAINABILITY OF LOCAL AUTHORITIES' DEBT AND ARREARS

I. The ratio of debt and arrears to locally generated revenues reveals a concerning trend, indiating that local authorites are increasingly struggling to manage their financial obligations relative to their revenue- generation capacity.

II. The Local Authorites debt- to- revenue ratio (excluding CDF), trend raises significant concerns about debt sustainability.

III. Local Authorities allocate a small fraction of their budgets to debt service.

ZAMBIA'S BLUEPRINT FOR FINANCIAL SUSTAINABILITY AND LOCAL AUTHORITY DEBT MANAGEMENT

- **The Local Authorities Debt and Arrears Monitoring Mechanism (LADAMM)** fraamework has been developed to address the long standing dificulties in monitoring and tracking of debt and arrears. The framework aims to easily capture, monitor and analyze data on debt and arrears and will enhance transparency on debt dismantling.

- The Government has implemented a **Deduction at Source** measure where a portion of the Local Government Equilization Fund (LGEF) is deducted at source (Central Government) and channeled to debt service before being transferred to Local Authorities.

- Local authorities have transitioned from **Activity- Based Budgeting (ABB) to Output- Based- Budgeting (OBB)** to align budget to align their budgeting processes with central government systems to improve accountability and transparency

CONCLUSION AND POLICY RECOMMENDATIONS

This study examines Local Authority debt, arrears, and the financial governance framework. Despite reforms like the LGEF, revenue shortfalls have led to rising debt, especially in pension and tax arrears. While mechanisms like LADAMM aim to manage this, limited resources and weak financial systems continue to strain Local Authorities, highlighting the need for stronger fiscal management, the report makes the following policy recommendations

1. Strengthen Local Revenue Mobilisation and adopt a differentiated approach that considers the unique characterisitcs of each local authority.

2. Automate Revenue Collection.

3. Enhance Transparency and Accountability.

4. Implement Debt Swap Initiatives with Statutory Bodies.

5. Align Staff Transfers with Financial Capacity.