

## AZERBAIJAN

UNITARY COUNTRY

## BASIC SOCIO-ECONOMIC INDICATORS

INCOME GROUP: UPPER MIDDLE INCOME

LOCAL CURRENCY: MANAT (AZN)

## POPULATION AND GEOGRAPHY

**Area:** 86 600 km<sup>2</sup>  
**Population:** 9.854 million inhabitants (2017), an increase of 1.3 % per year (2010 - 2015)  
**Density:** 114 inhabitants / km<sup>2</sup>  
**Urban population:** 55.3% of national population  
**Urban population growth:** 1.6% (2017 vs 2016)  
**Capital city:** Baku (23.2 % of national population)

## ECONOMIC DATA

**GDP:** 172 billion (current PPP international dollars), i.e. 17 398.2 dollars per inhabitant (2017)  
**Real GDP growth:** 0.1% (2017 vs 2016)  
**Unemployment rate:** 5% (2017)  
**Foreign direct investment, net inflows (FDI):** 2 867.5 (BoP, current USD millions, 2017)  
**Gross Fixed Capital Formation (GFCF):** 23.6% of GDP (2017)  
**HDI:** 0.757 (high), rank 80 (2017)  
**Poverty rate:** N.A.

## MAIN FEATURES OF THE MULTI-LEVEL GOVERNANCE FRAMEWORK

According to the Constitution adopted on 12 November 1995, Azerbaijan is a unitary republic with a presidential form of government. Executive power is held by the President, who is directly elected for five-year terms. The President is the Head of State, and in agreement with the Parliament, appoints the Prime Minister, who is the Head of Government. Legislative power is vested in the unicameral Parliament (*Milli Majlis*), composed of 125 members who are directly elected for five-year terms. Parliament membership is not based on regional or local considerations. The *Milli Majlis* has authority over the promulgation of constitutional laws, acts and orders within its jurisdiction, giving the vote of (no) confidence to the Cabinet of Ministers, the Prime Minister's appointment and the approval of the state budget. Moreover, the *Milli Majlis* has the responsibility to appoint the nine judges of the Constitutional Court (following the President's recommendation).

Decentralization is acknowledged in the Constitution, according to which, local government in Azerbaijan is exercised both through local bodies of state administration and through municipal governments. Section 4 of the Constitution recognizes municipalities' right to local self-government and the principle of their autonomy. Municipalities were created in 1999, following the approval in the same year of the laws "On the Status of Municipalities", "On Municipal Servants" and "On Municipal Elections". The normative framework of local self-government is still in the process of further development and improvement and after the year 2000, new laws were enacted with the objective of regulating local governments, including the Laws "On Joint Activities, Unification, Division and Liquidation of Municipalities" and "On Management of Municipal Lands". In the Nakhchivan Autonomous Republic (NAR), municipalities are regulated in accordance with the Constitution of the Nakhchivan Autonomous Republic and the decisions of the Cabinet of Ministers of the Nakhchivan Autonomous Republic. Presently, there are over 20 laws which regulate different aspects of local self-government. The national government began in 2009 a process of municipal amalgamation, reducing the number of municipalities by 40%. The latest amalgamation process took place in 2014, entailing a reduction in the number of municipalities from 1718 to 1607. Besides mergers and consolidation of municipalities, no other reforms are envisaged for the future. Conversely, the central government and its territorially-decentralized entities have increased administrative supervision over municipalities and self-government bodies.

Local bodies of state administration are regulated by the 1999 Constitutional Provision on Local Executive Authority, which addresses the activity of local state administrations, their structure and the eligibility requirements of the local administrations' heads. Relations between the municipalities and local state administrations are only vaguely described in current Azeri legislation. There are no explicit standards for the division of authority in current legislation and the topic is not mentioned in the Constitution. With respect to the relationship between the municipal and national levels, the Centre for the Work with Municipalities and a special department of the President's Office coordinate and oversee the national government's relationship with local governments.

## TERRITORIAL ORGANISATION

2017	MUNICIPAL LEVEL	INTERMEDIATE LEVEL	REGIONAL OR STATE LEVEL	TOTAL NUMBER OF SNGS
	73 city, 147 settlement and 1387 village municipalities ( <i>Bələdiyyə</i> )		The Nakhchivan Autonomous Republic ( <i>Naxçıvan Muxtar Respublikası</i> )	
	Average municipal size: 3 700 inhabitants			
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**OVERALL DESCRIPTION.** Local government in Azerbaijan comprises both deconcentrated local state administrations, representing the national government at the local level, and elected municipal governments. Organs of local executive power and organs of local self-government are not subordinated to each other and their powers are not intermingled or overlapping. Azerbaijan's largest cities are Baku (with 2 204 thousand inhabitants), Gyandja (with 330 thousand inhabitants), Sumgait (with 300 thousand inhabitants), Khyrdalan (with 97.2 thousand inhabitants) and Shirvan (with 78.1 thousand inhabitants). With the exception of Khyrdalan, the countries' largest cities do not have the status of municipality. They do not have elected representative bodies and their executive governments are centrally appointed.

**MUNICIPALITIES AND INTER-MUNICIPAL COOPERATION.** There is one-tier of elected municipal governments in Azerbaijan, including those located in Nakhchivan Autonomous Republic. Municipalities may be classified as cities, settlements or villages according to the number of permanent residents, which also determines the number of members that the local council may have. There is no hierarchy among municipalities irrespective of the status of the administrative-territorial units within which they are located, their fiscal capacity and number of people living in their territory. Article 142 of the Constitution stipulates that municipal councils are elected every 5 years. The elected members to the representative municipal body then elect the municipal Chair amongst the council members.

The Constitution promotes inter-municipal cooperation. The main legal framework for inter-municipal cooperation in Azerbaijan is the Law “On Joint Activities, Amalgamation, Splitting and Liquidation of Municipalities”. However, no inter-municipal cooperation examples exist based on the mentioned form of agreement.

**INTERMEDIARY LEVEL.** 11 cities (including the capital city of Baku) are governed by state deconcentrated entities at territorial level. Heads of executive power in cities and districts (*rayon*) are appointed by and accountable to the President. They represent the national government in local territorial units. These heads then appoint their own persons or representatives in the villages and settlements located within their boundaries.

The two biggest cities, Baku and Ganja, are subdivided into districts. The capital city of Baku is divided into 12 administrative districts (*rayon*) and 48 rural settlements. The president appoints the head of Baku and the heads of all districts (*rayon*). District or settlement bodies of local executive authority are subordinate to the city executive authority. The Autonomous Republic of Nakhchivan is subdivided into 7 administrative districts. Their executive governments are appointed by the Nakhchivan central government.

**REGIONS.** There are 66 regions in Azerbaijan. Each region is comprised of one central city with the same name and a different number of settlements and villages. Regions have centrally appointed executive committees. The Nakhchivan territory enjoys a special status as an Autonomous Republic. As an exclave in Armenian territory, it does not have a common border with mainland Azerbaijan. The Nakhchivan Autonomous Republic has its own Constitution, which is however hierarchically subordinated to Azerbaijan’s National Constitution as a source of law. The Chief executive of Nakhchivan Republic is elected by members of Nakhchivan Parliament.

## SUBNATIONAL GOVERNMENT RESPONSIBILITIES

According to Article 144 of the Constitution, local councils are responsible for the establishment of local taxes and duties, the adoption of the local budget and the implementation of programs for the development of the local economy and social protection. Municipalities’ competences are established in more detail by the national law “On the Status of Municipalities”. The responsibilities of municipalities in the Nakhchivan Republic are outlined in Constitution of the Nakhchivan Autonomous Republic. While the regulation on municipalities provides for a whole range of municipal competencies, municipal governments only perform a limited set of tasks. The actual scope of local self-governments’ competences across the country remains, thus, quite unclear. The role of self-government elected bodies is marginal in the system of public government. Although they are in charge of approving municipal budgets, the division of powers between municipalities and local executive bodies are not regulated by explicit legal mechanisms.

### MAIN RESPONSIBILITY SECTORS AND SUB-SECTORS

	REGIONS (NAKHICHEVAN AUTONOMOUS REPUBLIC)	MUNICIPAL LEVEL
1. General public services	Administrative services; Public buildings and facilities	Administrative services; Public buildings and facilities
2. Public order and safety	Public order and safety	
3. Economic affairs/transport	Economic affairs; Transport	Park spaces; Urban transports
4. Environmental protection	Environment protection	Parks and green areas; Waste management; Street cleaning
5. Housing and community amenities	Housing and community amenities	Distribution of drinking water; Public lighting; Urban and land use planning
6. Health	Health (joint with the central government)	
7. Recreation, culture & religion	Recreation, culture and religion	
8. Education	Education (joint with the central government)	
9. Social protection	Social protection (as a supplement to the central social policy)	Social programs

## SUBNATIONAL GOVERNMENT FINANCE

<b>Scope of fiscal data:</b> all municipalities and the government of Nakhichevan Autonomous Republic.	SNA 2008	Availability of fiscal data: <b>Medium</b>	Quality/reliability of fiscal data : <b>Medium</b>
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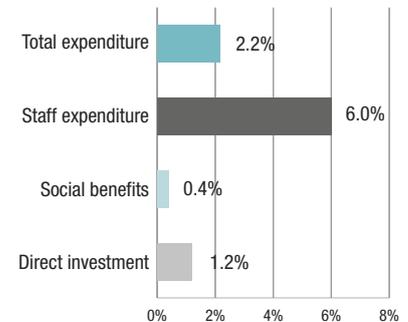
**GENERAL INTRODUCTION.** The Constitution of Azerbaijan empowers the municipal councils to impose local taxes and levies, to approve local budgets and to possess, use and dispose of municipal property. The 1999 Laws “On the Status of Municipalities” and “On bases of Finance of Municipalities” contain detailed rules on the “economic basis of local self-government” and specify the financial resources of municipalities, the conditions of their economic activity and their financial and economic management rights. The 2002 Law “On the budget system” of Azerbaijan guarantees the independence of municipalities with regard to preparing, approving and spending their own local budgets and enshrines the key principle that legislative and executive authorities must not interfere with the budget activities of the municipalities. However, despite the formal guarantees of the economic basis of local government autonomy, Azerbaijan’s municipalities are in an extremely weak financial position.

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## SUBNATIONAL GOVERNMENT EXPENDITURE BY ECONOMIC CLASSIFICATION

2015	DOLLARS PPP / INH.	% GDP	% SNG EXPENDITURE	% GENERAL GOVERNMENT EXPENDITURE (SAME EXPENDITURE CATEGORY)
<b>Total expenditure</b>	<b>144</b>	<b>0.8%</b>	<b>100%</b>	
<b>Incl. current expenditure</b>	<b>117</b>	<b>0.7%</b>	<b>81.1%</b>	
Staff expenditure	41	0.2%	28.1%	
Intermediate consumption	18	0.1%	12.1%	
Social expenditure	5	0.0%	3.4%	
Subsidies and current transfers	3	0.0%	1.8%	
Financial charges	0	0.0%	0.0%	
Others	52	0.3%	35.7%	
<b>Incl. capital expenditure</b>	<b>27</b>	<b>0.2%</b>	<b>18.9%</b>	
Capital transfers	0	0.0%	0.0%	
Direct investment (or GFCF)	27	0.2%	18.9%	

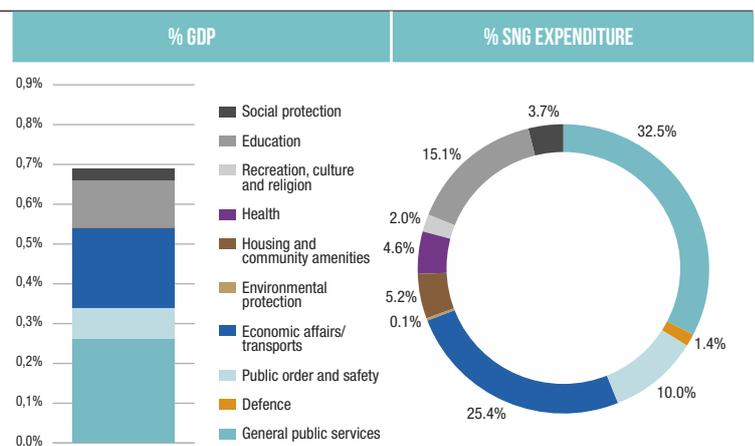


**EXPENDITURE.** Municipal governments' expenditures are marginal, representing 2.2% of the total public expenditure in the country. Such level of local expenditure is very low compared to other countries of the region, even to the countries with a similar scope of local governments. 81% of expenses incurred at the subnational level are devoted to current expenditures, of which 28% are used to pay for personnel expenses. Approximately 1% of subnational expenditures correspond to direct investment in capital expenditure.

**DIRECT INVESTMENT.** Municipalities do not incur capital investments. It is the central government that invests directly in local property via deconcentrated local executive governments. Or often, the government imposes mandates on local entrepreneurs to invest in municipal property (when not too large or too expensive). The NAR, in contrast, invests significantly (19.3% of total expenditures). These investments seem to be made out of own resources as the budgetary reporting does not indicate that the NAR receives earmarked capital transfers. In 2015, government finance statistics reported negative direct investments at the municipal level which indicates negative change in inventories and depreciation of municipal property.

## SUBNATIONAL GOVERNMENT EXPENDITURE BY FUNCTIONAL CLASSIFICATION – COFOG

The largest expenditure line both for the NAR and for municipalities corresponds to the provision of general public services (31.9% and 42.3% respectively). The next most important expenditure lines for the NAR are economic affairs/transport (25.6%) followed by education (16%), while in municipalities, housing and community amenities represent the second largest expenditure (29.9%), followed by economic affairs / transports (22.0%). For the NAR, expenses in security and public order correspond to 10.6% of the republic's total expenditures, while health and social protection make up for 4.9 and 3.6% of expenditure, respectively. For municipalities, social protection plays a more important role and amounts to 5.0% of municipal expenditure, while the share of such expenditure devoted to environmental protection corresponds to 0.8%.



## SUBNATIONAL GOVERNMENT REVENUE BY CATEGORY

2015	DOLLARS PPP / INH.	% GDP	% GENERAL GOVERNMENT REVENUE (SAME REVENUE CATEGORY)	% SNG REVENUE
<b>Total revenue</b>	<b>129.3</b>	<b>0.7%</b>	<b>2.1%</b>	
Tax revenue	25.8	0.1%	0.9%	20.0%
Grants and subsidies	99	0.6%		76.6%
Tariffs and fees	2.8	0.0%		2.2%
Property income	0.2	0.0%		0.1%
Other revenues	1.5	0.0%		1.2%

**OVERALL DESCRIPTION.** The Law "On bases of Finance of Municipalities" defines the sources of income for the local budget, which include fiscal, non-fiscal and transfer sources of revenue. Tax revenues constitute 48% of total municipal revenues and only 18% of NAR revenues. User charges, fees and property income represent a major source of revenues for municipalities (31%) while they are negligible for the NAR. The major source of NAR revenues are grants

(80.1%), while the share of grants in municipal revenues is smaller (21.6%). The reason is that NAR is assigned with significant spending obligations in education and roads construction that have to be provided by central government funding.

Total municipal revenues represent about 0.1% cent of the consolidated general budget (this share has shrunk since 2012). This low level of revenues is clearly insufficient to enable municipalities to fulfil their assigned responsibilities.

**TAX REVENUE.** Local taxes established by the Law “On bases of Finance of Municipalities” include land tax on individuals and personal property tax, mining tax on construction materials of local importance and corporate income tax on municipally-owned enterprises. The tax base of local taxes as well as the tax rate ceiling and provision of tax benefits are prescribed by the national Tax Code. Localized state administrations may centralize a portion of municipal tax collections for their budgets. The NAR is totally dependent on shared taxes (PIT, CIT, VAT, sales tax and excises). Shared taxes are assigned to the NAR through the Law “On the National Budget” every fiscal year. These shares are not established on a permanent basis but differ from year to year depending on estimated expenditure needs. Thus, the shared taxes play the role of regulating taxes. The most important source of tax revenues for the NAR is VAT (58.2% of tax revenues) followed by PIT (27.4%). The role of the excise (5.5%), sales tax (2.8%) and CIT (2.4%) is quite small. All taxes are collected by the National Ministry for Taxes and Duties. Tax revenues make up 48% of municipalities’ revenues, which may, in accordance with current tax legislation, provide tax exemptions as they deem convenient.

**GRANTS AND SUBSIDIES.** According to the Law “On the Budget System”, the NAR and municipalities may receive matching subsidies and grants from the state budget when it is impossible to finance subnational social-economic development programmes from own source revenues. Central government grants do not play a big role in municipal finance (about 20% of total revenues) though they are nearly the only source of revenues for the NAR (accounting for more than 80% of funds). The criteria laid down in the law for distributing fiscal transfers for municipalities are not clear, and the entire allocation process is therefore not fully transparent. The Law “On the Budget System” only states that subsidies are calculated taking into account the number of municipal inhabitants, its contribution to financial resources of the country, revenues and expenditures of a municipality, location of the municipality (whether in the highlands, plains or on the border), cost of living, expected social and economic projects, etc. However, there is no information as to the per capita fiscal capacity threshold within which subsidies would be activated. This results in uneven allocation of transfers between various municipalities.

In addition to the block grants, targeted funds can also be allocated from the central government for specific purposes at the request of the NAR or particular municipalities. There are no data available on the amount and form of these subsidies. Although this mechanism might provide local governments with extra resources, this kind of central government support does not increase the transparency of the financial system as a whole.

**OTHER REVENUES.** Other revenues of SNGs include fees and property income. Municipal fees include fees for advertising, fees on hotels, sanatoria and health resorts and on persons providing tourist services, parking fees, fees for retail trade, fees on public catering and other services and fees on lotteries. The amount of a fee is established by municipalities themselves within the limits prescribed by national legislation. Property income includes revenues from privatization and lease of municipal or NAR property. User charges are collected by state owned enterprises and do not appear in public budget lines. Fees and property income represent a major source of revenues for municipalities (32.8%) while they are negligible for the NAR. These revenues have stayed stable over the last years. The municipalities may decide on voluntary one-time payments for financing of local activities. Voluntary one-time payments are used only for the intended purposes. The NAR does not have this right.

## SUBNATIONAL GOVERNMENT FISCAL RULES AND DEBT

	DOLLARS PPP/INH.	% GDP	% GENERAL GOVERNMENT DEBT	% SNG DEBT
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### Total outstanding debt

Financial debt\*

\* Currency and deposits, loans and bonds

**FISCAL RULES.** There are only a few fiscal rules for municipal budgeting. The 1999 Law “On the Fundamentals of Municipalities Finance” (last amended in 2018) states that compensation of employees should not exceed 50% of total municipal spending.

The Law “On the Budgetary System” states that each level of government may establish its own limits for the deficit of the corresponding budget. In case expenses are not covered by own revenues the gap can be covered by subsidies from the central budget.

**DEBT.** Deficits may also be covered by contracting short-term and long-term loans from banks and other Azeri credit organizations. There are no legal barriers to municipal borrowing, but formal mechanisms for applying for or receiving loans, are not stipulated in the legislation. The size of public debt and credit resources are established by representative bodies while approving budget provisions for the next fiscal year. The state (central government or NAR depending on the case) is not responsible for the commitments of municipalities to credit organizations. In the case that during the process of execution of sub-national budget, the forecasted revenues appear to be overestimated and the deficit exceeds the established limitations, the municipality or NAR has to exercise the sequestration of its budgeted expenditures.



Lead responsible: UCLG  
Last update: 02/2019

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**Socio-economic indicators:** World Bank // UNDP // UN Desa // ILO

**Fiscal data:** IMF (2018) - The Government Finance Statistic (GFS) // Ministry of Finance (2018) Statistical Bulletin on the Execution of Municipal Budgets, January-December, 2017.

**Other sources of information:** Claire Gordon, Tomila Lankina (2016) The Place of Local and Regional Self-Government in Eastern Partnership Policy-Making and Delivery // OECD/UCLG (2016) Subnational governments around the world: structure and finance // Vusal Mirzayev (2015) Study mapping the obstacles to inter-municipal cooperation in Azerbaijan // Jos Wielen, Gudrun Mosler-Törnström (2013) Local and regional democracy in Azerbaijan // Rovshan Agayev et al. (2007) Strengthening Municipalities in Azerbaijan // Sabuhi Yusifov. Local Government Structure, functions and revenues in Azerbaijan.