

# REPUBLIC OF NORTH MACEDONIA

UNITARY COUNTRY

EUROPE

## BASIC SOCIO-ECONOMIC INDICATORS

INCOME GROUP: UPPER MIDDLE INCOME

LOCAL CURRENCY: MACEDONIAN DENAR (MKD)

### POPULATION AND GEOGRAPHY

**Area:** 25 710km<sup>2</sup>  
**Population:** 2.083 million inhabitants (2017), an increase of 0.1% per year (2010-2015)  
**Density:** 81 inhabitants / km<sup>2</sup>  
**Urban population:** 57.7% of national population (2017)  
**Urban population growth:** 0.4 % (2017 vs 2016)  
**Capital city:** Skopje (28.0% of national population)

### ECONOMIC DATA

**GDP:** 31.9 billion (current PPP international dollars), i.e. 15 290 dollars per inhabitant (2017)  
**Real GDP growth:** 0.2% (2017 vs 2016)  
**Unemployment rate:** 22.4 % (2017)  
**Foreign direct investment, net inflows (FDI):** 381 (BoP, current USD millions, 2017)  
**Gross Fixed Capital Formation (GFCF):** 21.9% of GDP (2017)  
**HDI:** 0.757 (high), rank 80

## MAIN FEATURES OF THE MULTI-LEVEL GOVERNANCE FRAMEWORK

The Republic of North Macedonia is a unitary state and a parliament democracy. The President is the Head of the State and is elected for a five-year term; the Prime Minister leads the Government. The Parliament is a unicameral assembly composed of 120 to 140 Representatives elected during general, direct and free elections and by secret ballot for a four-year term.

The Republic of North Macedonia is composed of two tiers of government – central and municipal, and the principles of local self-government and decentralisation are enshrined in the Constitution of 1991. Central authorities oversee the legality of municipal government's acts and endeavours; whereas the municipalities, on the other hand, have the right to appeal to the Constitutional Court if the State authorities encroach on their prerogatives.

In addition to the Constitution of 1991, legal provisions dealing with decentralisation and subnational government matters include the Law on Local Self-Government, the Law on Territorial Organisation and the Law on Financing of the Local Self-Government Units. The municipal governing body is comprised of the Mayor (*gradonačelnik*) and the municipal council (*sovet na opština*) – the former being the executive body and the latter the representative body of the citizens. The mayor is elected by direct universal suffrage for a four-year mandate according to the majority electoral model. On the other hand, municipal councillors are elected by proportional vote. The number of seats depends on the population size of the municipality. The city of Skopje is an exception to this rule, as its council consists of 45 members.

During the Yugoslav period, North Macedonia was a very decentralised country; however, several territorial organisation reforms were passed in the aftermath of the country's independence and municipal responsibilities were limited. Nevertheless, the decentralisation process began anew in 1995 when the Law on Local self-government was passed and in 1997 when the European Charter for Local Self -Government was ratified. In 2002, a new Law on Local Self-Government was adopted under the "Ohrid Framework Agreement" of 2001. It primarily aimed at transferring some administrative responsibilities to the municipalities. In 2004, a law on the territorial organisation of local self-government was adopted. The new provision reorganised local government units into 84 municipalities and further enhanced the transfer of responsibilities to local governments. Throughout 2004 and 2005, significant reforms were carried out with the objective of consolidating the local public finance system. In 2007, those municipalities that had improved their fiscal situation became responsible for financing and managing all schools, as well as a number of other cultural and social welfare institutions and received block grants to finance these new tasks. Today, decentralisation and strengthening SNG capacity are priorities that have emerged from the Accession Partnership of the Republic of Macedonia with the EU and the Framework Agreement. The government has committed to the 2015-2020 Programme on Sustainable Local Development and Decentralisation in the Republic of Macedonia, which is in the process of being revised.

## TERRITORIAL ORGANISATION

2016	MUNICIPAL LEVEL	INTERMEDIATE LEVEL	REGIONAL OR STATE LEVEL	TOTAL NUMBER OF SNGS
	80 municipalities ( <i>opština</i> ) and the city of Skopje			
	Average municipal size: 28 050 inhabitants			
	81			81

**OVERALL DESCRIPTION.** In 2016, there were 81 local government units in North Macedonia, including 80 municipalities (*opština*) and the City of Skopje. This number is the result of reforms affecting municipalities. In 1996, there were 123 municipalities. The number dropped to 84 in 2004 and then to 81 in 2013 when four municipalities merged to form the new Kičevo municipality. Today, municipalities are large by international comparison: 28 050 inhabitants (vs 9 700 in the OECD and 5 900 in the EU). However, the median average is lower (14 050 inhabitants). Around 20% of municipalities have less than 5 000 inhabitants. Skopje accounted for 28% of the total population in 2017. The second largest city (Kumanovo) was home to around 110 000 inhabitants in 2017 while three other cities counted between 83 000 and 93 000 inhabitants (Gostivar, Bitola and Tetovo).

Urban and rural communities can be delimited or established within each municipality with the objective of enabling the residents to take positions or address issues particularly relevant to their municipalities. The powers of such entities are defined by the municipalities and therefore vary from one municipality to the next. The villages and neighbourhood are not political entities and can only make recommendations to the local governments or work in the interest of their communities. North Macedonia has a dense network of urban and rural settlements (around 1 780 units).

The capital city, Skopje, is recognised as having special status and consists of 10 independent municipalities (which are part of the overall number of 80 municipalities).

Eight regions are established for statistical and planning purposes only. These regions have no administrative roles; they were created partly in accordance with the EU NUTS system and correspond to NUTS level 3. Each region has a council, which is made up of the mayors of its constituent municipalities.

## SUBNATIONAL GOVERNMENT RESPONSIBILITIES

According to Article 22 of the 2002 Law on Local Self-Government, municipalities have both own and delegated competences. Overall, Macedonia has a highly decentralised public sector with the municipalities undertaking responsibilities in important areas such as education, the provision of basic utilities and social welfare, economic affairs and transport, environment, health etc. According to the 1991 Constitution (Article 115) and the Local Self-Government Act (Article 23), a public administration body may also delegate the execution of specific tasks from its competence to the municipality. In these cases, the funds anticipated for the performance of these tasks shall also be transferred from the national budget. The delivery of the delegated competences may be adjusted to local conditions, in accordance with the relevant laws. Examples of shared competences include education, health, road maintenance, urban planning and building permits. The capital's independent municipalities have individual competences, some of which are shared with Skopje, and which set them apart from the country's other municipalities.

### MAIN RESPONSIBILITY SECTORS AND SUB-SECTORS

MUNICIPAL LEVEL	
1. General public services	Municipal administration; Oversight of all activities within the municipal competence
2. Public order and safety	Civil protection; Natural and other disasters; Fire protection
3. Economic affairs/transport	Local public transportation; Local economic development and planning; Entrepreneurial development; Construction and maintenance of local roads and other infrastructure facilities; Public parkings; Construction of markets
4. Environmental protection	Environmental protection (water, atmosphere, land, pollution); Maintenance of forests; Green areas and parks; Rivers in urban areas; Sewerage; Drainage
5. Housing and community amenities	Water supply; Waste collection and treatment; Natural gas and energy supply; Cemeteries; Public lighting; Regulation and maintenance of buildable land; Public hygiene; Management of state land (since 2011)
6. Health	Governance of the network of public health organisations and primary care buildings; Preventive health control over contagious diseases; Assistance to patients with special needs (mental health, child abuse, etc.)
7. Recreation, culture & religion	Cultural heritage preservation; Maintenance and construction of sports and recreational facilities; Cultural centres; Libraries; Museums
8. Education	Pre-schools; Primary and secondary education (in coordination with central authorities), including the payment of teachers' salaries; Transportation of pupils; Accommodation and dormitories
9. Social protection	Social welfare most notably for elderly, disabled and children, including children with special needs and persons exposed to social risk

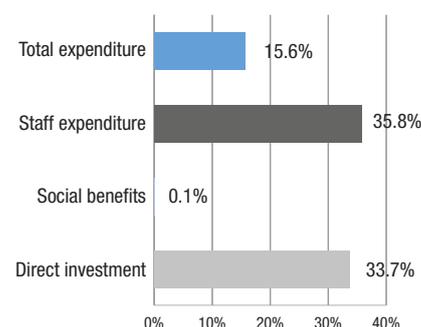
## SUBNATIONAL GOVERNMENT FINANCE

Scope of fiscal data: all municipalities including the city of Skopje	SNA 2008	Availability of fiscal data: <b>Medium</b>	Quality/reliability of fiscal data : <b>Medium</b>
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**GENERAL INTRODUCTION.** Throughout 2004 and 2005, significant reforms were carried out with the objective of consolidating the local public finance system. The 2004 law on local government finance indicates that SNGs are financed through own-source revenues, shared revenues, grants from the budget of the republic and from the budget of the funds, and borrowing. The 2004 law abolished the previous Law on Limitation of Own Source Revenues, transferring full responsibility in administering and collecting local taxes and establishing the rights of SNGs to receive either a share of or all tax revenues collected within their respective jurisdictions by the central government. A Committee for Monitoring and Development of Local Government Finance System whose members are issued from national and local governments has been established.

### SUBNATIONAL GOVERNMENT EXPENDITURE BY ECONOMIC CLASSIFICATION

2016	DOLLARS PPP / INH.	% GDP	% SNG EXPENDITURE	% GENERAL GOVERNMENT EXPENDITURE (SAME EXPENDITURE CATEGORY)
<b>Total expenditure</b>	<b>720</b>	<b>4.9%</b>	<b>100%</b>	
<b>Incl. current expenditure</b>	<b>572</b>	<b>3.9%</b>	<b>79.5%</b>	
Staff expenditure	361	2.5%	50.2%	15.6%
Intermediate consumption	177	1.2%	24.5%	
Social expenditure	2	0.0%	0.3%	
Subsidies and current transfers	31	0.2%	4.3%	
Financial charges	1	0.0%	0.2%	
Others	0	0.0%	0.0%	
<b>Incl. capital expenditure</b>	<b>147</b>	<b>1.0%</b>	<b>20.5%</b>	
Capital transfers	3	0.0%	0.4%	
Direct investment (or GFCF)	144	1.0%	20.1%	33.7%



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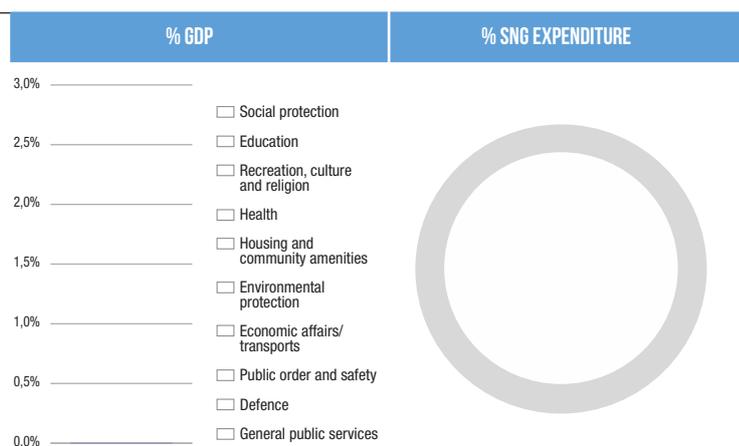
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**EXPENDITURE.** In 2016, local government expenditure amounted to 4.9% of GDP and 15.6% of public expenditure, percentages which were significantly below the averages for OECD unitary countries in 2016 (9.2% of GDP and 29% public expenditure), despite large areas of responsibilities transferred to municipalities. SNG expenditure is mostly comprised of current expenditure (79.5% of their expenditure) and it is noted that half of the current SNG expenditure is related to staff compensation (50.2%). This high level of municipal staff spending is explained by the fact that municipalities are in charge of paying teachers' wages in primary and secondary education.

**DIRECT INVESTMENT.** Capital expenditure represented 20.5% of total SNG expenditure, a ratio that is higher than the average for OECD unitary countries, which stood at 10.5% in 2016. Local governments undertook approximately a third (33.7%) of total public investment in 2016, a significant increase compared to the ratio of 2015 (25% of total public investment). However, that ratio remains very much below the average for OECD (50.7% in 2016) and EU (46.1% in 2017) unitary countries. A large share of SNG investment is also carried by the capital city.

## SUBNATIONAL GOVERNMENT EXPENDITURE BY FUNCTIONAL CLASSIFICATION – COFOG



## SUBNATIONAL GOVERNMENT REVENUE BY CATEGORY

2016	DOLLARS PPP / INH.	% GDP	% GENERAL GOVERNMENT REVENUE (SAME REVENUE CATEGORY)	% SNG REVENUE
<b>Total revenue</b>	<b>723</b>	<b>4.9%</b>	<b>17.1%</b>	
Tax revenue	193	1.3%	7.2%	26.7%
Grants and subsidies	460	3.1%		63.6%
Tariffs and fees	54	0.4%		7.5%
Property income	16	0.1%		2.2%
Other revenues	0	0.0%		0.0%

**OVERALL DESCRIPTION.** SNG revenue has been on the rise in the last decade, from 1.9% of GDP in 2005 to 4.9% in 2016, signalling progress in the fiscal decentralisation process. Despite this improvement, the responsibilities of Macedonian municipalities often go unfunded. Despite the 2004 law on local government, SNGs still depend largely on central government transfers, which represented almost 64% of their revenue in 2016 (vs 43.3% in the EU), while tax revenue and other sources of own revenues (tariffs, fees and property income) are still low by international standards.

**TAX REVENUE.** Local government tax powers are regulated in the 2004 Law on Local Government Finance, the Law on the Property Tax, the Law on Communal Taxes, and other sectoral laws that influence the local public finance system. In 2016, SNG tax revenues stood at 7.2% of public tax revenues, and only 1.3% of GDP, ratios which are well below the averages for EU unitary countries (16% of public tax revenues and 4.5% of GDP) and OECD unitary countries (19.8% of public tax revenues, 4.7% of GDP in 2016). Tax revenue comprises both shared taxes and own-source taxes.

Shared taxes are however very limited. They include 100% of the personal income tax (PIT) from the self-employed and 3% of revenues generated from the PIT of other residents in the form of wages where the employer is responsible for paying the PIT on behalf of the employee. Shared revenues from the PIT stood at 3.7% of SNG tax revenues, yet only 1% of SNG revenues in 2016.

Since the 2004 law on local government finance, SNGs have the full responsibility in administering and collecting three taxes: the property transfer tax, the inheritance and gift tax and the recurrent property tax. The base and the rate of these tax instruments are set by law, while municipal councils approve the final rates for their respective jurisdictions within these legal limits. The property transfer tax accounted for 20.2% of SNG tax revenue in 2016 and 5.4% of SNG revenue. The inheritance and gift tax is minor, accounting for 1.4% of municipal tax revenue. The recurrent property tax accounted for 14.8% of SNG tax revenues, 4% of total SNG revenue and 0.2% of GDP, a level which is very low by international standards (1.1% in the OECD on average).

The recurrent property tax is paid by legal entities and individual owners. It is levied on land (agricultural, forest, and pastures) and buildings (residential buildings, flats, business premises, administrative and recreation buildings, etc.). It is charged on the basis of the estimated market value of the property, as determined by municipal staff based on a methodology defined by the central government and approved by the association of municipal councils (ZELS).

Property tax rates are set by municipal councils. They are proportional and range from 0.10% to 0.20%, according to the type of the property. Although the collection of property tax has improved over the years, there remain significant disparities in the capacity of different municipalities to tap into the property tax base. Several municipalities are working towards improving the collection process. Some local councils also collaborate with the public revenue office to limit tax evasion by blocking the accounts of uncompliant taxpayers, while others take on a more administrative approach in updating their fiscal registers. Finally, other sources of tax revenue are utilities fees (for the use of municipal infrastructure) and administrative fees. These local taxes on specific services accounted for 40% of SNG tax revenue in 2016, i.e. 10% of their total revenues.

**GRANTS AND SUBSIDIES.** Intergovernmental transfers include resources from the central budget as well as from different specific funds such as the Road Fund, the Water Fund, and the Fund for Balanced Regions.

There are six different categories of transfers/grants:

- 1/ Block Grants. They are used to finance the major municipal services. Municipalities receive a grant for primary and secondary education (in particular for the payment of teachers' salaries) based on a formula that takes into consideration enrolment, employment, number of children entitled to free school transport, number of pupils and teachers etc. They also receive a block grant for culture and fire protection services. Municipalities are autonomous in their management of the funds received through the block grants.
- 2/ Earmarked Grants. They include mainly operation or maintenance costs resulting from education, social care, and firefighting. Wages and salaries in all of these sectors are not included.
- 3/ Revenues from VAT (Value Added Tax): SNGs receive a share of the VAT. This share has been increased from 3% to 4.5% of total VAT collection in recent months following an amendment in the local government finance law. Shared VAT revenues are distributed in the form of an equalisation grant scheme to narrow the revenue disparities among rural and urban SNGs and 50% is distributed on a per capita basis. The Ministry of Finance determines the equalisation scheme in consultation with the Committee for Monitoring and Development of Local Government Finance System. Each municipality decides on its use depending on municipal priorities. The distribution formula includes variables such as the population size, territory, and the number of settlements.
- 4/ Capital Grants are used to finance capital projects. The government adopts annual plans for such projects and assigns grants accordingly.
- 5/ Grants for a delegated competency – grants to be used to finance a recent delegated competency from the central government, such as elderly care. The grants are determined by the contract signed between the mayor and the line ministry.
- 6/ Regional Development Fund. This Fund aims at promoting balanced regional development by allocating money to regions according to a formula, which is specified in the law on regional development. The Regional Development Fund is set at 1% of GDP although this share has not been approved in recent years.

Overall, current grants accounted for 91% of total grants in 2016 and capital grants for the remaining 9%.

**OTHER REVENUES.** Besides municipal utility fees and administrative fees, municipalities can charge fees on buildable land, on urban and spatial plans, on municipal services delivery. They are provided by utility companies, and consumers pay them directly for their services. Revenues from tariffs and fees accounted for 7.5% of SNG revenues in 2016, which is below the OECD and EU28 average (respectively 14.9% and 11.6% in 2016).

Property revenues are generated from the sales of properties, rent revenue and interest rate revenue. These revenues are determined and collected by the local authorities. In addition, SNGs also receive revenues from concessions (e.g., on water, agricultural state land) and since 2015, 10% of concessions on agricultural land, a ratio that is expected to rise to 50% as of 2018. Property income accounted for 2.2% of SNG revenue in 2016, above the OECD and EU28 average (respectively 2.0% and 1.2% in 2016).

## ■ 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.** According to the Budget Law, the procedure of preparation, adoption and execution of the Budget of the Republic of Macedonia and the budgets of the municipalities and the reporting on their execution is based on several principles, including that of budget balance, which means that the total revenues and inflows shall cover the appropriations. A "sound Financial Management" is requested, meaning that execution of the budget in accordance with an effective and efficient internal control as a process which is implemented on all the levels of management of funds.

**DEBT.** Under the 2004 law on local government finance, municipalities have the right to borrow but under strict borrowing rules. Borrowing from foreign entities needs the consent of the Ministry of Finance. Short-term borrowing can be used only for covering temporary cash deficits and it cannot exceed 20% of the overall revenues from the current-operational budget of the municipality in the preceding fiscal year. Long-term borrowing is allowed only to finance capital assets or investment projects ("Golden rule"). The limit on the total annual debt-service amount from long-term borrowing in one fiscal year is 15% of the overall revenues in the current operating budget of the municipality in the preceding fiscal year. Still, the total outstanding long-term borrowing including all guarantees shall not exceed the total amount of revenues in the current operating budget of the municipality in the preceding year. Further, commercial banks are required to report all loans to municipalities to the Ministry of Finance.

SNG borrowing remains however very limited. In order to boost SNG investment, the government has provided credit lines from international financial institutions (World Bank, EIB, KfW and EBRD), which have provided for substantial investments, especially in reconstruction and rehabilitation of local streets and bridges, improvement of public hygiene and energy efficiency, construction and reconstruction of the water supply and local spatial landscaping. The government also wishes to help municipalities to begin issuing municipal bonds as an additional instrument for improving liquidity and providing financial resources for capital and municipal projects.