SRI LANKA

UNITARY COUNTRY

BASIC SOCIO-ECONOMIC INDICATORS

INCOME GROUP: LOWER MIDDLE INCOME

LOCAL CURRENCY: SRI LANKA RUPEE (LKR)

POPULATION AND GEOGRAPHY

Area: 65 610 km^2
Population: 21.444 million inhabitants (2017), an increase of 0.5% per year (2010-2015)
Density: 327 inhabitants / km^2
Urban population: 18.4% of national population (2016)
Urban population growth: 1.5% (2017 vs 2016)
Capital city: Colombo (2.8% of national population)

ECONOMIC DATA

GDP: 275.2 billion (current PPP international dollars), i.e. 12 811 dollars per inhabitant (2017)
Real GDP growth: 3.3% (2017 vs 2016)
Unemployment rate: 4.2% (2017)
Foreign direct investment, net inflows (FDI): 1 375 (BoP, current USD millions, 2017)
Gross Fixed Capital Formation (GFCF): 26.3% of GDP (2017)
HDI: 0.77 (high), rank 76 (2017)
Poverty rate: 0.8% (2016)

MAIN FEATURES OF THE MULTI-LEVEL GOVERNANCE FRAMEWORK

Sri Lanka is a unitary democratic republic (Constitution of 1978) with a unicameral parliament. The president, both the Head of state and Head of government, is directly elected and may serve up to 2 mandates of five years. The president appoints the prime Minister, reflecting the parliamentary majority. The 229 members of Parliament are elected through a proportional system.

In the early 80's, the country entered a period 25-year civil war, mainly opposing Tamil and Sinhalese groups over the independence of the northern and eastern regions. Devolution of powers was initially introduced through parliamentary regulation. Such "statutory devolutions" were often the result of political negotiations with ethnic constituencies. In 1980, the national government created the District Development Councils, in agreement with the Tamil constituency, thus abolishing village and town councils. District Development Councils were then abolished by the 13th amendment to the Constitution in 1988, which acknowledged Local and Provincial Councils as the two subnational tiers of government, composing a shared system of service delivery between deconcentrated sectorial agencies and local councils.

At national level, there is an important fragmentation of ministries (51 ministries in 2017) and 425 line agencies. The national government has kept a strong hold on subnational tiers. At national level, the Ministry of Local Government and Provincial Councils (MLGPC) is responsible for policy and legislation, retaining constitutional powers to intervene in subnational affairs for purposes of national planning. Monthly coordination meetings are held with provincial commissioners and organizations supporting both local councils and the national ministry for the formulation of local government policies, such as the Sri Lanka Institute of Local Governance. The MLGPC has powers to create a local council based on the recommendations of an ad-hoc committee; it may curtail or extend the term of office of any local council by one year.

Other powers of the MLGPC were transferred to the Provincial Minister of Local Government who has become responsible for supervising local councils. Provincial councils do not have legislative autonomy. They must detail the provincial implementation of the regulations voted by national Parliament through statutes. At provincial level, the chief ministers, head of the provincial executive body, organize regular conferences in which the MLGPC represents the national government. Similar meetings are held between representatives of sectoral ministries, the provincial chief secretaries, and the secretaries of the Provincial Public Service Commission. Local councils are required by law to promote social inclusiveness, civil society participation and partnership (Extraordinary Gazette, 1632/26 of December 2009). This could only be implemented with the support of external actors in some local councils.

TERRITORIAL ORGANISATION

2018	MUNICIPAL LEVEL	INTERMEDIATE LEVEL	REGIONAL OR STATE LEVEL	TOTAL NUMBER OF SNGS
	24 Municipal councils 41 Urban councils 276 Rural councils *(Pradeshiya Sabhas)*		Provincial councils	
	Average municipal size: 62 880 inhabitants			
	341		9	350

OVERALL DESCRIPTION. Sri Lanka has two tiers of subnational government: provincial and local councils (13th amendment of the Constitution - 1988). There are 9 provincial councils and 341 local councils. Local councils are composed of municipal councils (in average, 30 000 – 100 000 inhabitants), urban councils (in average, 20 000 – 75 000 inhabitants) and rural councils (in average 10 000 – 60 000 inhabitants). Elections to local and provincial councils are not synchronized. In addition, provincial council elections also take place at different times in different provinces.

MUNICIPALITIES AND INTER-MUNICIPAL COOPERATION. The local government level is made up of 24 municipal councils for cities and larger towns; 41 urban councils for smaller towns, and 276 Pradeshiya sabhas covering the former villages and town councils in mostly rural areas. Local governments in Sri Lanka were originally introduced by the Urban Councils Ordinance 1939, with additional provisions outlined by the Municipal Councils Ordinance 1947 and the Pradeshiya Sabhas Act 1987. These governing laws were amended in 2014 and with the Local Authorities Elections (Amendment) Act No. 31 of 2017 already implemented in the last election of 2018. Councillors are elected via mixed electoral system composed of a ward-based proportional system (40% of elected body) and a first-past-the-post system (60%). In addition, a quota for women was implemented. Local councils are headed by mayors (in municipal councils), or chairpersons (urban councils and pradeshiya sabhas), nominated for a period of four years by the political coalition holding the majority in the council. Municipal councils are mandated to appoint overseeing standing committees on matters such as finance or housing and community development. Legislative amendments have been proposed to introduce similar provisions for urban councils and pradeshiya sabhas.

PROVINCES. As one of the main requirement of the Indo-Sri Lanka Accord, attempting to bring civil war to an end, eight provincial councils were established through the 13th amendment to the Constitution and are governed by the Provincial Councils Act, No. 42 of 1987. The Northern and Eastern provinces were merged into one (Provincial Councils Act 42 of 1987 (Section 37 1A)) until 2009. A Supreme Court decision overrode the decision, creating nine Provincial councils. The members of the council are directly elected by the citizens while executive powers are held by a governor, appointed by the president for a five-year term. A board of four ministers is appointed by the governor amongst the members of the provincial council to advise the chief minister at its head. In practice, the chief minister is the leader of the provincial parliamentary majority. By law, the Governor must act in accordance with the advice of the Board of Ministers. For administrative purposes, the nine provinces are subdivided into deconcentrated administrative units: 25 districts and 331 divisional secretariats. These secretariats – which are further sub-divided into over 14 000 *grama niladhari* divisions – coincide with the local authorities, and serve an administrative coordinating role for the central government.

SUBNATIONAL GOVERNMENT RESPONSIBILITIES

The Constitution allocates powers and responsibilities between national and provincial governments: the "Provincial Council List" outlines functions under the responsibility of the provincial councils, the "Reserved List" outlines central government's exclusive responsibilities, and the "Concurrent List" outlines the responsibilities to be exercised by either tier, acting in consultation and concurrence with each other. Despite such constitutional provisions, there is still significant overlap in the implementation of development plans, education, health, social welfare, rural development, land use and development, and local government oversight. In accordance with their governing legislation, local councils are responsible for the regulation, operation and maintenance of public health, public utility services and, in general the protection and promotion of the wellbeing of the people. They are also vested with the power to create by-laws, with the approval of the MLGPC and provincial councils, to fulfil additional responsibilities. The pradeshiya sabhas have some additional development responsibilities.

MAIN RESPONSIBILITY SECTORS AND SUB-SECTORS

	PROVINCES	LOCAL COUNCILS
1. General public services	Statistical offices	Public facilities; Townhouses; Cemeteries and crematoria
2. Public order and safety	Police (shared with national government)	Firefighting (shared between all local councils)
3. Economic affairs /transports	Agriculture, forestry and fishery	Road management; Urban transportation (shared with provincial government); Slaughterhouses; Local economic development; Tourism and trade
4. Environmental protection		Sanitation and environmental protection; Solid waste collection and disposal
5. Housing and community amenities		Housing and town planning (shared between all local councils); Water management; Parks and open spaces
6. Health	Primary and preventative healthcare; Maintenance of medical centers; Hospitals and specialized healthcare (e.g. dental care)	Primary and preventative healthcare; Maintenance of medical centers
7. Recreation, culture & religion	Museums and libraries; Sports and leisure (all shared with local councils)	Theatre and concerts; Religious facilities (discretionary power)
8. Education	Pre-school and nursery; Primary, secondary and higher education (shared with national government); Vocational education	Vocational education (shared with provincial and national government)
9. Social protection	Family welfare services (shared with national government); Support to elderly and disabled persons; Social inclusion and poverty elimination	Support to elderly and disabled persons; Social inclusion and poverty elimination

SUBNATIONAL GOVERNMENT FINANCE

Scope of fiscal data: : provincial councils.	Other	Availability of fiscal data: **Low**	Quality/reliability of fiscal data : **Low**

GENERAL INTRODUCTION. The Parliament has full authority over public finance (Section 148 of the 1978 Constitution). The core constitutional provisions define a centralized oversight of spending powers and revenue mobilization through: (i) Assignment of expenditure and revenue powers (Provincial List) (ii) Guarantee of the allocation of funds from the annual budget to meet the needs of the provinces; and (iii) Apportionment of such funds among the provinces on the basis of principles formulated by the Finance Commission. The design of the fiscal framework for devolution to provinces results in a significant shortfall in revenue over expenditure and there are important imbalances within and between the nine provinces, with a relative dominance of the Western province, where both the country's capital city and economic centre are located.

The financial resources of local governments are derived from the establishment of funds specific to each category of local government and regulated by the respective constitutional laws: Municipal Fund (Section 185), Local Fund (Section 158) and Pradeshiya Sabha Fund (Section 129). Overall, municipal councils and pradeshiya sabhas collect and spend the largest share of revenue.

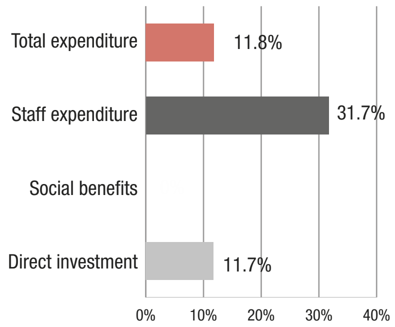
SRI LANKA

UNITARY COUNTRY

SUBNATIONAL GOVERNMENT EXPENDITURE BY ECONOMIC CLASSIFICATION

2016	DOLLARS PPP / INH.	% GDP	% SNG EXPENDITURE
Total expenditure	**286**	**2.3%**	**100%**
Inc. current expenditure	246	2%	86.1%
Staff expenditure	189	1.5%	66.1%
Intermediate consumption			
Social expenditure			
Subsidies and current transfers			
Financial charges			
Others			
Incl. capital expenditure	40	0.3%	13.9%
Capital transfers			
Direct investment (or GFCF)	40	0.3%	13.9%

% GENERAL GOVERNMENT EXPENDITURE (SAME EXPENDITURE CATEGORY)



EXPENDITURE. The available data (reported in the table) from the Ministry of Finance's 2016 Annual Report refer to the provinces excluding the local governments/councils. Recurrent expenditure declined between 2016 and 2017, except staff expenditure, which in fact increased by 2.5% in the period. Representing nearly 70% of total expenditure, staff costs are the largest item of provincial expenditure.

As far as local governments themselves are concerned, a 2017 comparative study of their recurrent and capital expenditure in 2011 concludes that almost 80% of their revenues are spent on recurrent costs for service provision. The Monitoring Division of the MPCLG prepared a detailed Review of the financial performance of Local Authorities for the year 2017. It shows that local governments spend approximately 78% in recurrent expenditure, mostly staff expenditure (45% of total local government expenditure). In comparison, capital expenditure in 2017 represented 28% of local government expenditure. According to the review, total actual expenditure increased by 7.5% between 2016 and 2017.

DIRECT INVESTMENT. Investment of provincial councils amounts to 40 dollars PPP per capita in 2016. Among capital expenditure, acquisition of capital assets and investments in Special projects has been declining since 2015. The Central Bank of Sri Lanka highlights that capital expenditure of Provincial Councils in 2017 reached the same levels as in 2015, 0.5% of the GDP. This was mainly due to increases in Province Specific Development Projects and capital transfer to local governments, which grew by 28.1% from one year to the other.

SUBNATIONAL GOVERNMENT EXPENDITURE BY FUNCTIONAL CLASSIFICATION – COFOG

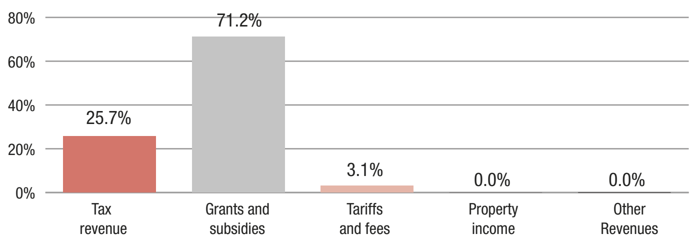
There is no information on the functional distribution of expenditures at local level. At provincial level, the Central Bank of Sri Lanka specifies that between 2015 and 2017 spending on social services increased by approximately 8%. Expenditures in economic services and provincial public administration remained stable also in absolute terms, at approximately LKR 4 billion (approximately 4 dollars PPP per capita) and LKR 18 billion (approximately 19 dollars PPP per capita), respectively.

% GDP | % SNG EXPENDITURE

SUBNATIONAL GOVERNMENT REVENUE BY CATEGORY

2016	DOLLARS PPP / INH.	% GDP	% GENERAL GOVERMENT REVENUE (SAME REVENUE CATEGORY)
Total revenue	**286**	**2.3%**	**16.4%**
Tax revenue	74	0.6%	4.8%
Grants and subsidies	204	1.7%	
Tariffs and fees	9	0.1%	
Property income			
Other revenues			

% SNG REVENUE



OVERALL DESCRIPTION. According to the 1978 Constitution, local governments have the power to raise revenue as provided in the three dedicated legislative 'Acts' mentioned above. The legal framework thus empowers them to mobilize adequate revenue to provide the services they are responsible for. Shared-tax revenue is the main own source of subnational revenue: its single largest component are transfers from the general government's National Building Tax, to both provincial and local governments. Since the 1987 Constitutional Amendment, provinces have been allocated a large number of tax and non-tax revenue sources. Provinces cannot introduce fiscal measures. Thus, subnational governments are relatively constrained in terms of revenue mobilisation.
In 2016, total revenue of provincial governments represented 2.3% of GDP, approximately 286 dollars PPP per capita. In addition, according to the 2017 annual report of the Ministry of Finance, in 2016 local government revenue represented 0.5% of GDP. Provincial and local councils do not have enough capacity mobilize enough local revenue to cover recurrent expenditure. Under a constitutional provision, the national government should allocate adequate funds to cover the fiscal deficit of the provinces, in consultation with the Finance Commission. In practice, subnational governments are highly dependent on central government grants and transfers. These subsidies are divided in four categories: Block grants, Criteria- based grants, Revenue-performance grants and Province Specific Development Grants (PSDG) which together represent 71% of provincial revenue. There is a significant imbalance in local government's capacity to collect revenue in the different provinces. Approximately half of subnational revenues are collected in the Western province. High-potential sources, such as turnover taxes on wholesale and retail sales, motor vehicle license fees and taxes on mineral rights, are always levied within the limits and exemptions prescribed by Parliament.

TAX REVENUE. Subnational governments do not have the power to set direct or indirect new taxes without the agreement of Parliament. They are however in charge of tax collection and can influence tax rates. They are limited when setting the tax base, which requires the establishment of by-laws and compliance with the hierarchy of regulatory Acts. In 2010, via the Fiscal Policy Circular Nº01/2010, the Parliament abolished provincial turnover tax on wholesale and retail sales, which represented approximately half of the provincial revenue as established by constitutional provisions. It was replaced by a system of shared taxes consisting of stamp duty, 70% of motor vehicle registration fees and a fixed share of the National Building Tax (NBT).

Stamp duties on immovable property (Section 36.5 of Provincial List) as well as court fees have to be transferred to local governments. The NBT was introduced in 2009 (Act No 9 of 2009) and subsequently amended. It represents a social contribution towards the welfare of security forces and the reconstruction of communities and infrastructure facilities. One third of the funds collected go to the provincial councils

GRANTS AND SUBSIDIES. The central government allocates annual funds to provinces and local governments, through the provinces. In 2016, transfers from central to local governments, through the provinces, represented 2 dollars PPP per capita and 0.7% of general government total capital expenditure. The grant structure does not provide for equalization of fiscal capacity between provinces, resulting in significant fiscal imbalances and disparities as 6 of the 9 provinces remain highly dependent on central governments transfers. Grant decisions are made on a case-by-case basis by the Finance Commission. Of the four types of existing grants, the two main ones are the Block grant and the Criteria–based grant.The **Block Grant** represented 86% of total transfers from the central government to provincial governments, and 61% of provincial revenues, in 2016,. It is earmarked to cover recurrent expenditures. In practice, it covers the salary costs of provincial administrations. Block grants are transferred to local governments, through provincial councils to cover all their staff costs. According to CLGF, the situations are diverse: In the Pradeshiya sabhas, the total cost of salaries is covered. In Colombo Municipal Council, they cover about 50% of this cost.

The **Criteria-based grant** incorporates socio economic indicators that take into account provincial development disparities: (a) the population of each province; (b) the per capita income of each province; (c) the targeted reduction of social and economic disparities; and (d) the targeted reduction of gaps between the per capita income of each province and the highest per capita income among provinces. In 2016, these grants amounted to 1.5% of provincial revenue, for a total of 3.15 dollars PPP per capita.

In addition, the **Province Specific Development Grant** (PSDG) is the funding allocated to line ministries to be transferred to provincial councils for specific development purposes. In 2016, it accounted for 2.2% of the provincial revenue. Lastly, **Revenue-performance Grants** are provided as an incentive for provincial councils to raise revenue.

SUBNATIONAL GOVERNMENT FISCAL RULES AND DEBT

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

* Currency and deposits, loans and bonds

FISCAL RULES. In Sri Lanka, the Fiscal Management (Responsibility) Act (FMRA) of 2003, amended in 2013 and 2016, makes fiscal discipline mandatory. Under the current framework, at national level, the ceiling of budget deficit is set at 5% of GDP under plurennial budget framework. Likewise, debt ceiling is 60% by the end of 2020 and guarantees must not exceed 10% of GDP. Under the same rules, Provincial Council are expected to provide an Annual Financial Statement and Municipal councils and Urban councils must prepare budgets of Accumulated Reserves & Income and Expenditure Statements. According to the Asian Development Bank, the public financial management of provincial councils is independent from central government since they do not have direct responsibility for reporting their expenditure to the central government. The national deficit has never been less than 5 % of GDP over the past two decades.

DEBT. Local governments can access borrowing through local loans and development funds. The main statutory body providing this source of financing is the Local Loans and Development Fund (LLDF), established through the Local Loans and Development Ordinance No. 22 of 1916. Its objective is to provide loans to any local government at below-market rates with a focus on infrastructure development. The fund functions under the authority of the MPCLG. Its primary function is to meet the capital investment needs of local authorities and provide long-term loans at concessionary interest rates. In 2016, the central government granted a total of LKR 144 million to local governments through the LLDF (0,15 dollar PPP per capita). The LLDF is managed by a Board of Commissioners (BoC), comprising seven chief secretaries, two provincial commissioners, one member appointed by the Minister of Finance and three members nominated by the MPCLG. The Secretary of the MPCLG is the ex-officio chairperson.

SNGWOFI
World Observatory on Subnational Government Finance and Investment
Lead responsible: UCLG
Last update: 02/ 2019
www.sng-wofi.org

Socio-economic indicators: World Bank // UNDP // UN DESA // ILO.
Fiscal data: Sri Lanka Finance Commission.
Other sources of information: CLGF (2018) Country fact sheet Sri Lanka // Parliament of Sri Lanka (2018) Assessment of the financial management and the performance of the Public institutions, Provincial Councils and Local Authorities through a computerized information management system (The First Report of the Committee on Public Accounts) Parliamentary Publications No 35 // Finance Commission of Sri Lanka (2017) Annual Report 2017 // Ministry of Finance, Government of Sri Lanka (2017) Annual report 2017 // Finance Commission of Sri Lanka (2016) Annual Report 2016 // J. Uyangoda (2015), Local Government and Local Democracy in Sri Lanka: Institutional and Social Dimensions // Ministry of Provincial Councils and Local Governments.