

Service Provision
by a Local Government
Association (LGA)



Colophon

This publication was made within the framework of the LOGO South VNG Association Capacity Building programme 2003-2010.

Main contributor:

Ewout van Haeften, Director Centraal Inkoopbureau (CIB)

Other contributors:

Barbara Seelt, VNG International project manager

Design:

Bertine Colsen

[©] 2007 VNG International

This publication forms part of a series of documents intended for Local Government Associations, all available from VNG International. This series was made possible by financial contributions from the Netherlands Ministry for Development Cooperation and VNG, the Association of Netherlands Municipalities.

VNG International
The Hague, the Netherlands
Email: vng-international@vng.nl
Tel: +31 (0)70 373 8401
Fax: +31 (0)70 373 8660
www.vng-international.nl

Table of contents

Introduction

1 Key tasks of a Local Government Association (LGA) and its services 6

- 1.1 Information and documentation services
- 1.2 Advisory services
- 1.3 Training of municipal staff and exchanging experiences
- 1.4 Economic and financial services

2 Financing through members' subscription fee 10

- 2.1 Determining the subscription fee
- 2.2 Collecting fees

3 Financing through donor programmes 13

4 Financing through paid services 15

- 4.1 Paid services for individual municipalities
- 4.2 Paid service in case of common need for products and services

5 Criteria regarding (paid) services 18

- 5.1 Criterion 1 – The activity should add value to the association's mission
- 5.2 Criterion 2 – Can the market provide the service?
- 5.3 Spectrum of possibilities

6 Organisational form 24

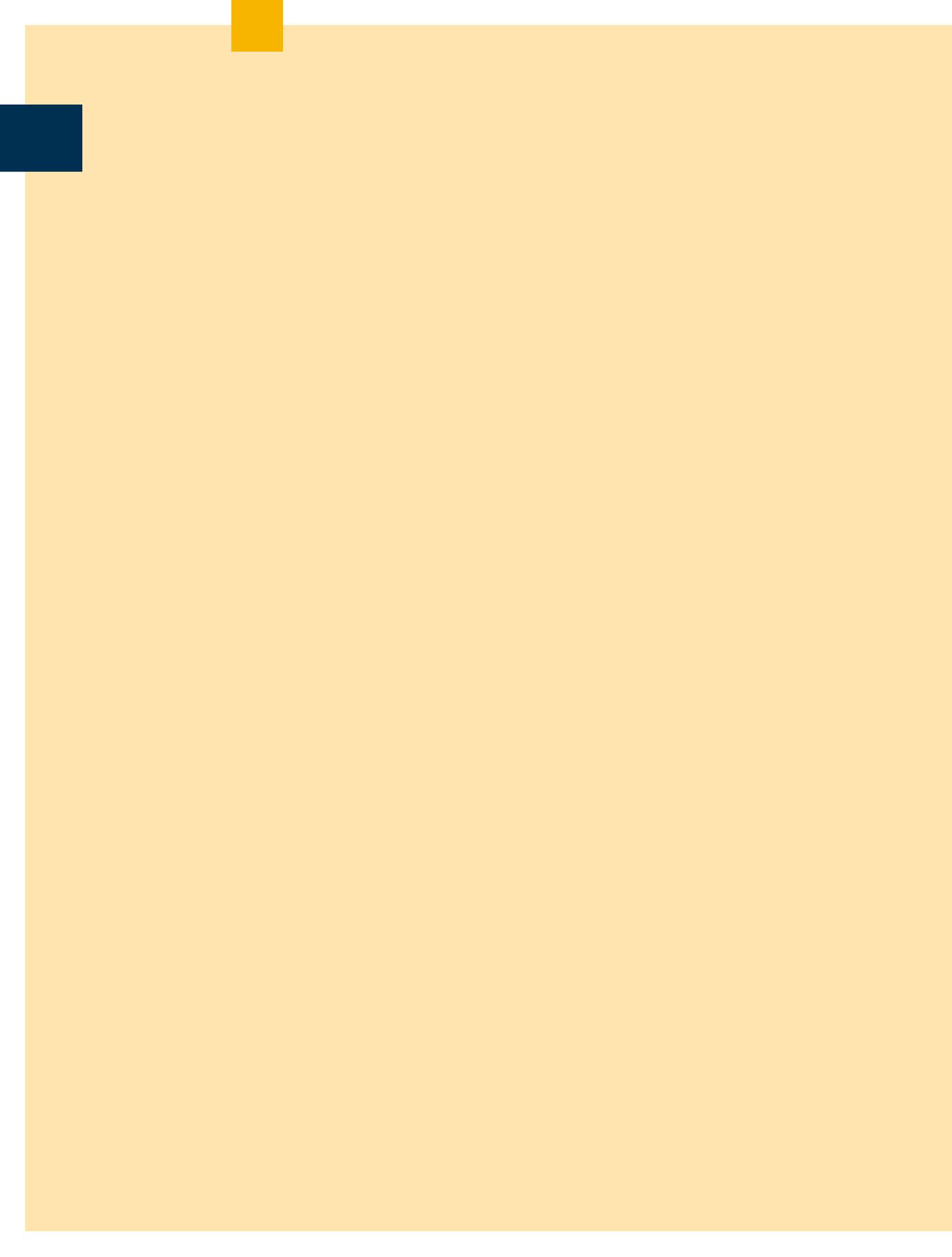
- 6.1 Organising a new service within the own association
- 6.2 A new entity for providing the service (company)
- 6.3 Restricting the entrepreneurial risk

7 Conclusion 27

Annex 1: Example of a commercial service 28

VNG International 31

UCLG 32



Introduction

Associations of municipalities across the world are in different phases of development and thus organised very differently. Some associations have developed a whole range of activities offering their members an extensive package of services, while others concentrate solely on lobby activities. Nevertheless, the themes and difficulties which associations of municipalities have to face show many similarities. Also, members' need for assistance is usually similar.

Naturally it is vital that each association has a solid financial basis. How an association generates income is thus a central question in the association founding process. Obviously the association must have funds to be able to pay the office, hire staff and launch activities.

Associations may obtain income in different ways: (1) by collecting members' subscription fees (2), receiving subsidies from donors or other external parties such as national ministries (3), or they may offer paid services to members and other external parties.

These incomes allow associations to pay their activities and develop services. Activities and services may differ per association and vary from publishing information bulletins to providing specific legal advice.

To determine the services which an association will offer, it must find out which services are required by members and whether investments for instance are necessary. A number of questions must be considered which are covered in this brochure:

- 1 Does the activity contribute to the association's mission?
- 2 Is the market capable of delivering the service?
- 3 How can services be best organised?

This brochure addresses associations that are or are considering offering certain (paid) services. It can be used as a reference material, it provides a number of specific considerations that might have a role and includes examples of other associations that have experienced similar challenges.

We realise the fact that each situation and each association is unique. So the guidelines will not always interest all readers equally and will not always be applicable. Nevertheless, we sincerely hope that this brochure will offer all those interested a spectrum of new ideas and serve as a source of inspiration.

1 Key tasks of a Local Government Association (LGA) and its services

The similarities between associations are mainly related to their tasks, as all associations basically share the following key functions:

- Representing municipalities to the central government (lobby)
- Helping members carry out their municipal tasks by delivering services
- Being a platform where municipalities can exchange information and learn from each other's experiences

Basically, many associations focus mainly on the first type of activity: lobbying to the central government. For many associations this representative role is their main reason of existence. The third function, being a platform where municipalities can exchange experiences, is also a task that is easily undertaken by most associations. Compared to offering services, these two functions do not demand major financial effort. Providing services is a different story; it requires major investments in manpower and money. Nevertheless, providing services is becoming ever more important in many countries. Especially countries in which the decentralization process is running smoothly, local governments face a whole range of new tasks. Tasks which until a certain point in time they will not have dealt with and for which they thus simply lack the experience. Precisely in these type of cases an association can effectively support its member municipalities. This can be done on a small scale, for instance by circulating a newsletter informing municipalities about current affairs and recommended practices, but also on a larger scale providing in-depth individual advice and assistance. Naturally, the type of services offered by an association depends on how developed it is and what members need.

The following chapters discuss the aspects considered when deciding on providing a service, and how to finance this; firstly we discuss the different types of service an association may develop and offer. This list is not restrictive and is based on the following classification:

- 1 Information and documentation services
- 2 Advisory services
- 3 Training of municipal staff and exchanging experiences
- 4 Economic and financial services

1.1 Information and documentation services

Associations are in the best position to collect and provide information on and for the local government organisations. To properly carry out their tasks, collecting and analyzing information is also highly significant. To associations this is the key way to translate municipalities' wishes to the national government, meet members' needs for new services and actively keep in touch on trends and developments. Having a good information management system is essential to an effective information and documentation system. A system like this can prevent information from lingering within an organisation without reaching its destination to serve its actual purpose. Within any information management system one must distinguish between information supply as an external service (members, third parties) and internal use of information by the association's internal departments.

Information tools come in different types and sizes. Some tools require relatively more efforts and investments than others, however they all need to create the opportunity for feedback to the association. Examples of frequently used information tools include information bulletins, special publications, case studies and best practices, (interactive) websites and databases.

CASE: MUNICIPAL BEST PRACTICES IN COSTA RICA

In 2003 the association in Costa Rica, the Unión Nacional de Gobiernos Locales (UNGL), became one of the structural partners in the VNG Association Capacity Building programme. To strengthen the association, the project includes a component for collecting and analysing municipal Best Practices. These Best Practices cover different subjects but they all indicate how municipalities in the rather centralised state of Costa Rica successfully carry out their tasks. Best Practices are published in manuals and offered to municipalities. On the so-called 'municipal days' (Jornadas municipales) which the UNGL organises for municipalities, these examples are then further explained and discussed.

1.2 Advisory services

Offering advisory services allows an association to help its members in a targeted manner. Advisory services might help municipalities gain knowledge on subjects on which they would otherwise lack expertise. Many municipalities lack the financial capacity to gain specialized knowledge for specific subjects. And quite frequently municipalities need not have that specific knowledge at all times, for they only need it occasionally. The association's support in this can help many municipalities.

In case of a specific advisory service, the association needs to properly consider whether a particular service is desired by several municipalities and how the service will be financed. For specific advisory services a certain financial contribution could be requested from members who will use that service. This mainly applies to services which are interesting to some of the members but also in which other members show no interest. In this respect, full service financing on the basis of members' subscription fee would be less suitable.

Examples of advisory services include: providing specific legal advice to individual municipalities, research activities, producing local regulations to be used by municipalities, helping municipalities draw up a HIV AIDS policy and advising municipalities in situations requiring legal guidance.

CASE: SERVICE PROVIDED BY THE AMM, MALI

In 2004 and 2005 the Association of Malinese Municipalities (AMM), with support of VNG's ACB programme, produced brochures on land distribution, urban land registry, and spatial planning. These brochures explain the roles that the laws assign to municipalities, what other institutions are involved, and provide examples. The brochures have been sent to all of Mali's 703 municipalities. As a further service, a small team of AMM staff tours its provinces to train municipal staff. The brochures and the training meet a need for knowledge, and also enhance the confidence of the municipalities, most of which are very young. Mali's decentralised system of governance is very good on paper, but much effort is still needed to put it in practice. With this service the AMM aims to assist their municipalities with this.

1.3 Training of municipal staff and exchanging experiences

Being a platform for local governments, an association is in a good position to promote exchange of experiences between municipalities and contributing to professionalisation of municipal staff. Several associations offer municipalities (paid) trainings. Or they help other parties arrange for training sessions for municipalities. Some countries also have specific training centres for local government staff which of course operate in consultation with other parties. The training sessions offered by an association may cover municipal tasks but they may also have a more general character. For instance, several associations provide special training programmes for newly selected councillors to introduce them to the details of the municipal world.

CASE: MANUAL FOR COUNCILLORS IN THE CZECH REPUBLIC

Recently elected local politicians anywhere in the world face questions on how they can best represent citizens' interests, how to discuss and develop new policies and how to handle local budgets. These local politicians sometimes lack practical and accessible instruments to help them do this. That is why the Czech Ministry of the Interior, together with VNG International, a Czech training institute and the Czech association of municipalities, developed a handbook for councillors. The main goal of the handbook was to increase understanding of the roles and responsibilities of local town councillors in the Czech Republic. The handbook is a practical guide, attractive and easy to read, and is supported by a series of video programmes. Evaluations showed that the handbook was very popular and that 93% of councillors used it to improve their daily performance.

1.4 Economic and financial services

This type of service tends to concentrate on purchasing products or services for members of the association at more attractive prices and terms than individual municipalities would have to pay. Municipalities benefit because they pay less. The association can also earn a modest margin and so contribute to its own financial viability. To many associations this type of service sounds like a wonderful thing; central purchasing is seen as a quick, easy and honourable way of earning money. Central purchasing however requires sound preparations and accepting the risk of earning less than what might be expected by the association. Properly studying demand and supply, market and the association's capacity to facilitate these services, is therefore vital.

CASE: COLLECTIVE INSURANCE FOR MUNICIPALITIES IN RWANDA

Although RALGA, the Rwandese LGA, has only been in existence for a very short time (it was founded in 2002), it has already been working on its first joint purchasing effort, namely insurance. RALGA has issued a tender for insurance services to cover the vehicles in use for all municipalities. The winner of the tender offered a price 25% lower than the previous average rates. Within one year of the tender, the old insurance companies suddenly proved willing to offer the same tendered price to their ex-customers. Obviously, these companies were too late but will have another chance when the current tender period runs out. It all however, shows the eagerness of companies to do business with the LGA. This is a first effort and a very encouraging sign that RALGA is indeed able to negotiate and come up with an umbrella contract that saves money for all.

2 Financing through members' subscription fee

As is the case with every association, municipalities pay a subscription fee to their LGA. In principle, this payment is not related to the number, type or amount of services used by the association member. In practice, some municipalities use products and services more frequently than others. Larger municipalities for instance such as capital cities, sometimes require less intrinsic support from the association because they have many employees themselves who can do the work, while smaller municipalities with limited staff often use services offered by experts of the association.

2.1 Determining the subscription fee

Obviously, associations must collect fees to finance their activities. The question is how does an association determine the subscription fee payable by a member? Which formula is used, bearing in mind the many differences that exist between a country's local governments?

Subscription fees are determined on the basis of different formulas. One possibility is to collect an amount from each citizen of a municipality. Another is to collect a fixed amount from every municipality plus an amount per citizen. The fee may also be based on the budget of a municipality. Whatever formula is chosen, in most countries richer municipalities (should) pay more than less prosperous local governments. Determining the level of the subscription fee and the distribution code is an outstanding issue determined during the Annual General meeting; it is typically reviewed annually or every couple of years.

To determine a subscription fee formula, it is important to have answers to some questions:

- What is the financial capacity of municipalities in a certain country? What would be a reasonable amount to ask?
- Is the association capable of delivering the products and services that would justify the contribution?
- Are contributions expected to generate the entire budget required by the association, or are there any other sources of income (e.g. donors or paid services)?

CASE: MEMBERSHIP FEE AT THE ASSOCIATION OF NETHERLANDS MUNICIPALITIES (VNG)

Every year the VNG draws up a contribution memorandum explaining the suggested fee; this proposal is based on a fixed calculation method to which adjustments were made over the years. The adjustments are always submitted to members for their approval. Currently the fee calculation method has three modules: a *'wage and price increase'* module, a *'real costs calculation for the actual wage and price increase plus the effects of municipal geographical redistribution'* module and a *'policy developments'* module. These three modules lead to the proposed increase of subscription fee. This proposal is submitted to the members at the Annual General Meeting held every July. The VNG's articles of association then lay down the basic principles of the contribution calculation for each municipality. That is a fixed amount per citizen, whereby VNG maintains 4 rates for different citizens. In December prior to the year in question municipalities receive an invoice and in the course of the first quarter the VNG collects members' subscription fees. In the meantime calling rounds may take place. VNG faces few difficulties when it comes to payment of subscription fees. Should difficulties present themselves, however, VNG's Board of Directors visit and reach agreement as to payment and terms.

CASE: COLLECTING FEE AT ALGAK, KENYA

The Association of Local Government Authorities of Kenya (ALGAK), was established in 1959. Kenya has 175 local authorities and all these are members of ALGAK. ALGAK closes the members' register every year before the Annual General Meeting (AGM). Paid up members are then determined and are the ones who have voting power during elections (1 vote per council). Any amount of subscription payable after the closure of the register accrues a penalty. The local authorities are divided in to four categories: city councils (one - Nairobi), municipal councils (45), county councils (67) and town councils (62) and a membership fee is determined for each category. The total number of members fully paid up has been increasing every year, resulting in 115 paid up members in 2005 (compared to 44 paid up in 1999). The subscription fee for each local authority becomes payable on the first day of January and must be paid by March 31 each year. This also requires that in case of failure to meet this obligation for more than twelve months, the municipality is liable for exclusion from taking part in the ALGAK affairs.

2.2 Collecting fees

Besides determining the level of the subscription fee one should also make agreements as to how the fee will be collected. Generally speaking many associations in the South are facing difficulty in actually collecting members' subscription fees in full. Good procedures can certainly contribute to a smooth collection but naturally one should always take into account municipalities' usually tight financial situation.

Some associations are quite inventive when it comes to motivating their members to pay the fee. For instance, members who have paid their fees receive discounts for attendance at seminars and courses. Many associations align subscription fee payments to the timing at which local governments receive their contributions from the State. For example, if municipalities receive payment from central government three times a year, members' contributions can be paid in three instalments closely behind these.

Usually municipalities pay their contributions directly to the association. Some countries, however, operate a different construction whereby the contribution is deducted from the payments made by the central government to the local government. In this way it is the central government that makes the payment of the contribution. This is the case at the associations in Ecuador and Ghana.

CASE: COLLECTING FEE AT NALAG, GHANA

Local governments in Ghana mainly depend on the central government's payments for their income. Their own tax collection process is not well developed and local inhabitants are usually too needy to pay taxes. Consequently, payment of local governments' fees to NALAG, the association of municipalities, would also be a problem. In this case, as the central government, before paying the amounts from the so-called Common Fund to the local governments, skims off the association subscription fee and transfers it to NALAG, this problem is luckily overcome. This means that NALAG receives members' subscription fees directly from Ghana's central government. A key advantage here is that the association receives the members' fees immediately at the start of the year. A disadvantage, however, is that the municipalities are unable to properly assess the value and the significance of their association if they do not feel what it is like to pay contributions directly from their own wallets. In this way the association's services appear to be 'free' which can devalue the significance of the work carried out by NALAG. Another risk is that local governments consider the association to be an extension of national government, for in a certain sense the association is indeed paid by the national government.

3 Financing through donor programmes

To many southern associations, besides members' fees, the financial contributions from international donors are an essential part of their budget. Although the budgets of development organisations concentrate primarily on the non-governmental sector, worldwide more money is becoming available for local government bodies and their associations. Some associations receive a lot of attention from donors; and they have external financial contributions to thank for a substantial part of their budget. Local governments and associations, however, which are located in the relatively richer southern countries, usually have to settle for restricted (or no) contributions from the international world.

To many associations donor-based financing might open the possibility to actually start developing a certain service or product. Donor programmes might abolish finance to give a service shape which previously was unfeasible because of lack of money and thus be a tool to break down the old 'no resources so no services' circle. The association can learn how to offer a particular service, what aspects are involved and how to tune the service to members' wishes. Donor-based financing ideally functions like a seed or trigger in continuing to offer the service subsequent to the donor programme and to arrange for finance itself. Once members have experienced the services or products that their association is capable of delivering, they will be better inclined to pay, either through members' subscription fees or specific payments for that particular service.

Obviously the disadvantage of donor-based financing is dependence on it. Many years of structural contributions to southern associations' budgets is not ideal either. To avoid strong dependence on donors, associations should also not have donor programmes finance their key functions. Associations would then not run the risk of their entire organization collapsing should donor funds cease. Southern associations should keep their own strategic plans central and not focus too much on the desirability and possibilities of donor programmes which might poorly dovetail with the actual needs of their members.

CASE: SERVICES OFFERED BY AMDEPANDO, BOLIVIA

AMDEPANDO is one of Bolivia's ten regional associations. **AMDEPANDO** has proven to be capable of attracting finance from several European bilateral donors. **AMDEPANDO** spends most of this money on providing services to its members. **AMDEPANDO** offers technical assistance in the field of municipal financial management, formulation of policy and drawing up the legally obliged

municipal budgets and plans. Most Bolivian municipalities need help to follow these guidelines as in Bolivia there are no municipal training institutions or administration academies while municipal staff in general is not fit for the job. AMDEPANDO expects its members to be willing to pay for this technical assistance within a manageable amount of time. AMDEPANDO's expectation is based on the following:

- Municipalities will soon have their own larger tax collection area
- In the future municipalities will have to meet more guidelines from the central government
- AMDEPANDO has already informed its members of the actual costs of this technical assistance
- AMDEPANDO is better capable of providing this assistance than the average consultancy firm

Should members actually pay for these services, this will be the perfect example of how donor-based financing can be used to initiate a service which is subsequently taken over by the association and its members.

4 Financing through paid services

4.1 Paid services for individual municipalities

In principle, association's activities are carried out for the sake of all its member municipalities. After all, if an association invests manpower and time to answer the needs of one municipality, then another municipality can claim the same thing. This is indeed the case in some countries; in fact happening to such an extent that municipalities will appeal to the association for issues that could be seen as not forming part of an association's core activities. Usually the dividing line between activities the association should and should not support is difficult to draw. The risk is that, if an association (and its members) is used to basing its work on municipalities' ad hoc requests, it will be very difficult to change this. Consequently, the association might sometimes lack the time to develop services that will truly serve all municipalities, for it is too much preoccupied with the (ad hoc) requests of a few of its municipalities.

As it is impossible to cover the needs of all municipalities with activities that matter to all or to most, and because in ever more countries municipalities have questions which specifically concern them individually, more associations are adding supplementary individual contributions for specific (commercial) services to the standard contribution (and any other contributions from third parties). For example, some associations charge hourly rates for services they offer to individual municipalities. After all, the association possess specialist knowledge and it would be a pity if individual municipalities fail to benefit from this. The main difference is then that not all services are paid from memberships contributions.

In any case the introduction of a system whereby individual municipalities pay for certain services remains difficult. Especially if municipalities do not have plentiful resources and are used to covering all services by means of members' contributions. Good communication as to reason and method with members is essential for a successful introduction of paid individual services.

CASE: INDIVIDUAL PAID SERVICE

In practice only a few associations charge their municipalities for services which in fact are not covered by the members' contribution fee and which are only useful to an individual member. Many associations see the possibilities, but find difficulty in putting them into practice. Reasons are usually hidden in deeply rooted habits and the idea that municipalities need to rely on their association no

matter what. Municipalities usually assume the right to expect things from their association, especially if they invest a great effort to pay their contribution. Weaker associations in particular fear losing members. An example of an association that does invoice its members, be it in a limited way, for individual services, is VNG. In The Netherlands municipalities must observe European guidelines in case of public tenders, which is no easy task. Ever more municipalities need advice in this field while advice differs per municipality. By requesting an hourly rate for this specific advice VNG is able to deliver tailored work without interfering with the members' contribution.

4.2 Paid service in case of common need for products and services

In addition to the individual paid service another form of paid service also exists. This service regards the needs of all, or at least most municipalities but which cannot (yet) be effectively implemented by an association. One might think of a common demand for products and services like purchasing office supplies, ICT products and such. In principle, all municipalities might benefit from these services. But for this, purchasing expertise is required. While market knowledge is developing promptly in this field, it remains to be seen whether an association is capable of and intends to gain this knowledge, paid from contribution fees. A possibility is to introduce paid services: the association offers paid services which basically are interesting for all municipalities.

CASE: VNG'S CENTRAL PURCHASING

VNG's central purchasing office (known in Dutch as the CIB) focuses on purchase of products and services which municipalities often need. As municipalities have many archiving tasks, the CIB specialises in filing products such as long-life paper, protected paper, high-quality filing boxes and such. The CIB also offers 5000 office supplies from a municipal catalogue. In addition to purchasing and sales, the CIB also takes on a state agent role in the central purchasing procedure. In this the CIB centralizes demand by order of Dutch municipalities and combines demand in a tender. The benefits to municipalities include not only a low price but also lower purchase-related processing costs. The CIB also concludes framework contracts for goods which only a few suppliers can provide; a tender is usually senseless if there are only two or three suppliers. Negotiating directly with the member municipalities, suppliers will usually deliver products for lower prices for all members.

CASE: SUMMER COURSES OFFERED BY THE ASSOCIATION OF CHILEAN MUNICIPALITIES

Since 1995 the Chilean Local Government Association (ACHM) has been organising paid courses twice a year for mayors, councillors and municipal executives. These courses consist of two rounds (October and January) and are organised in three cities. The cities change every year. Each course in every city has room for about 150 participants. The courses, covering 30 hours in total, highlight several municipal subjects such as waste management, land registry and municipal finances. Financially speaking the courses are entirely self-supporting. Municipalities sending a delegation to the course will pay \$200 per participant plus travel and accommodation. The AChM provides the content of the courses and logistics, frequently using municipalities' practical knowledge. Many speakers are thus employed by the municipalities. The courses are an excellent tool to upgrade the practical knowledge of managers and officials, and encourage exchange between municipalities. For years the courses have been organised to the full satisfaction of both the association and its members.

5 Criteria regarding (paid) services

To make a good decision as to **whether and how** a service can be delivered and how it should organisationally be imbedded in the association, one should consider a number of factors. The following chapters discuss questions as to *whether* a certain service should be offered by an association and subsequently *how* this should be organised.

In general, one could say that the more specifically a certain product or service is related to the work of the local government, the higher the chance of it being developed by and within the association. Once a service becomes more general, in the sense that it regards skills that are not specifically relevant or interesting to the local government, we often find associations and municipalities using the open market or working together with an external party.

Whether an association should offer a certain (paid) service, depends on two factors:

- 1 To what extent does the activity contribute to the association's mission?**
- 2 What market structures are there and what are the risks for the association with regard to offering the service?**

The two criteria are discussed individually below and this is followed by a review of how these overlap and create different options.

5.1 Criterion 1 – The activity should add value to the association's mission

An association's mission expresses the long-term ambitions of the association in practical terms, shows what the association hopes to achieve and how it distinguishes itself from others. To determine whether or not an association should offer a service, the first question to be answered is whether the service provides an essential contribution to realising the association's mission. It here concerns a service which has not been offered in the association until now, but which can be obtained from other organisations. If a service has nothing or little to do with achieving the association's long-term objective, it is questionable whether the service should be offered.

CASE: VNG'S MISSION STATEMENT

VNG's mission statement says: *'The VNG is the association representing all Dutch municipalities. It promotes powerful local government within our democracy. It focuses on promoting the interests of its members and provides services to support this. It is the platform for opinion forming, knowledge development and innovation. The membership-inspired organisation is service-driven, professional and flexible'.*

The mission statement also states the following with regard to providing services: *'Providing services is an essential pillar of VNG's work. By supporting municipalities with products and services, VNG wants to contribute directly to a powerful and good quality local government. Good service by VNG is also crucial in its relationship with the members. Services and products are concrete and tangible results and so proof of VNG's efforts on behalf of its members'.*

Although this mission statement says nothing about the type of services which the association can offer, it does indicate that the VNG attaches importance to supporting its members through services. Mission statements rarely discuss the specific services which an organisation can or should provide to realise its objective, but can offer the opening to further develop services. In this case it is important that it involves a service which is 'part of' the association and which makes the association as a whole stronger. Examples include organising workshops or meetings (for which municipalities would possibly pay separately, see the Chilean example). During these meetings local administrators and officials gather knowledge so that the quality of local administration can be lifted to a higher level, which could be a contribution to the mission statement.

It is important to make the entire decision-making process regarding service provision as open and transparent as possible. This certainly applies if members must pay for specific services. This can be achieved by providing members with clear information (e.g. via members' meetings) and involving them in the deliberations. The process of generating support must not be underestimated and requires a lot of time: a preparation time of one year before the service gets off the ground is not unusual. During that year administrators and officials will frequently have to update members on why the current course has been taken.

5.2 Criterion 2 – Can the market provide the service?

A second important question which needs to be asked is whether the service is already offered by the market. In other words: are there providers who already satisfy a certain need or is this demand so new that no provider has yet ventured in this field? If the free market does not or cannot provide the desired services, then

the association can choose to develop these itself. This sometimes involves a new service which is simply not found in the regular products' package available in the market. This is not a typical public sector phenomenon. Large companies can also set up new companies when they want to develop new, innovative products. Companies can also jointly establish a new company and so spread the risk.

To assess whether a service is suited to be set up as a commercial or other activity, it is important to review the different market forms. A certain type of market form combined with a certain service or product could give cause to commercialise the service itself, while this could not be the case for other market forms. When we look at the balance between supply and demand in the market we can, broadly speaking, distinguish four forms. By looking at this balance the LGA can determine whether it is running a high or low business risk when setting up a certain service.

A Monopoly

In a monopolistic market there is only one supplier and many customers. This means the price does not fluctuate with demand as there is no competitor who the customers can turn to when the price seems too high. Price elasticity is how demand and supply vary with price. In the case of monopoly there is no elasticity, demand remains stable when the price is high. An example of this is if there is only one telephone company in the country. A public official will hardly reduce the number of telephone calls if the telephone company doubles the costs of a call. Another example is the energy supplier. If the price per kWh doubles, the city hall will still need to use the lights and the municipality will still need to pay the bill. In other words consumption hardly drops in the event of price increases.

B Duopoly

Here we see two suppliers and many customers. Also in this case the price is hardly subject to fluctuation because the suppliers will not underbid each other and will possibly make price agreements. One example is the situation in a country where there are two suppliers of software for the municipal administration. If the municipality is dissatisfied with the price and service of the supplier of the software on which the municipal services run, then they can switch supplier. If the other supplier also fails in their performance or is too expensive, the municipality's only other option to go back to the first supplier.

C Oligopoly

In this situation we see a handful of suppliers and many customers. The price is slightly negotiable, but there is not much room for negotiation. An example is when there are only three companies that supply road construction equipment. We sometimes see that one of these suppliers has a 60% market share and serves as price leader. The other oligopolists are much smaller and will imitate the policy of the biggest player. They keep the price just as high as the market leader. There is no spontaneous balance between supply and demand. This is also called an a-symmetric oligopoly.

D Polipoly

This is the situation in the free market. In this market form we see many suppliers and many customers. A balance is created where the price is established fairly. The price elasticity is high in this market form: if the price drops, demand for the product will increase. By testing the price elasticity, the producers determine their optimal price and supply. Examples can be seen in the supermarket: sandwich filling, meat or sweets. The daily or weekly market is another example of this free market. The goods which are traded can vary from chicken to rice and flowers. The resulting price is determined by the balance between the supply of chickens and the demand from consumers. If many chickens are offered but the number of consumers who want chicken is low, then the price will go down. If supply decreases and demand increases, the price rises.

5.3 Spectrum of possibilities

In the above there are two factors which must be weighed if an association wants to offer a (paid) service. If these factors are matched, then this provides perspectives and possibilities. Two questions need to be asked:

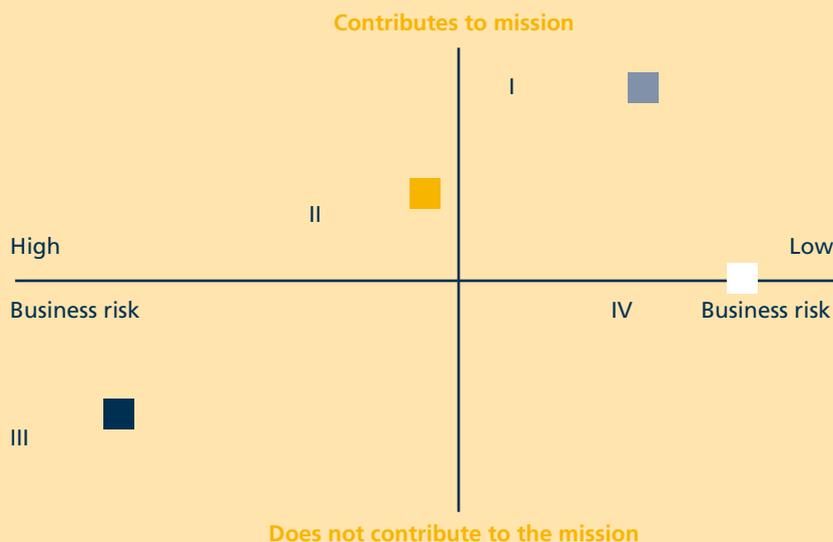
- 1 Is a service of strategic importance to an association?
- 2 Does a service have a high or low entrepreneurial risk?

	A Strategic important	B Strategic unimportant
1 High entrepreneurial risk	Set up a company or joint venture	Do not set up a company
2 Low entrepreneurial risk	Set up a company	Joint venture or small stake

The strategic importance is directly linked to the extent in which the service contributes to the association's mission. If cleaning services are not included in the mission, then this service is strategically unimportant. On top of that, cleaning services are services with a high entrepreneurial risk because it usually concerns a service with many suppliers.

The entrepreneurial risk relates to the market situation. The entrepreneurial risk increases if the market situation has more suppliers: if the number of suppliers increases the price will decrease for the service which is offered which in turn causes the financial risk to increase.

To properly appraise a service, it is useful to put it on a scale line. We then have four quadrants where a service can occupy a position.



As an example of **Service I**, we see a service which contributes to the association's mission and has a low entrepreneurial risk (there are only a few suppliers on the market). This corresponds with section A2 of the classification. The service is important for the members, and is low risk. For example, this could concern projects to develop powerful local government nationally or internationally with funds from development institutions. It could be the case that the market is gradually able to provide this know-how independently, as a result of which there is less need for this service, and the service and the company can be outsourced. In that case the block moves to the second or even third quadrant.

Service II is in a field with a varying market, but also contributes to the association's objective and therefore is of strategic importance. This service concerns for instance issuing publications in the association's field of activities in an oligopolistic market (a market with a few suppliers). This service roughly corresponds with Block A1.

An example of **Service III** is the case where an association sells office supplies to municipalities in a market where supply and demand is in balance (polipoly). This brings financial risks. Additionally it does not contribute to the mission. The positioning of this service for the association can be found in Block B1.

An example of **Service IV** are insurances for municipalities in a market with an a-symmetric oligopoly. Because the price for the municipalities will hardly change

due to the dominant price-determining player in the market, the decision can be made to bundle the municipal demand and to take out insurance through an own company in co-operation with a company that offers market knowledge. In view of the neutral contribution to the mission and the low entrepreneurial risk, we can place this in Service Block B2.

If an association decides to set up a service, it should take into account that this can involve risks. The market conditions can change and the association could, for example, face competition. If the service has been incorporated in a separate company then that company could go bankrupt. Bankruptcy does not only mean financial damage, but also damage to reputation. A bad reputation can certainly be detrimental to an association. Members could lose confidence and no longer view the association as 'their' representative. The confidence which the association has at national government level could also suffer damage and consequently damage its lobby activities. So the association should ask itself if it wants to run this risk.

The supply of products and services should be weighed against the realistic chance that the investment generates a good return. The assessment of the risks remains uncertain and so the assessment of potential returns. Will the municipalities actually want the service once it is offered? Many associations see golden opportunities once the possibility of a paid service presents itself but it is not certain that the service will also be profitable. Managing a commercial risk can for example be handled by actively pursuing and entering into a partnership with a governmental or market party, whereby the profits – and the risks – are shared.

6 Organisational form

6.1 Organising a new service within the own association

If an association has decided to offer a specific service, the question remains how this will be organised and delivered. Will the association choose to undertake this internally or incorporate the service in a separate entity or company, in which the association has a majority interest?

Many (southern) associations initially choose to gain experience with a new service within their current organisation. The service is set up by the association's own people and becomes part of the policy sectors for example. Reasons to organise the service from within the current organisation may include:

- The association has insufficient experience in the field and first wants to assess whether the service will succeed
- It is a relatively small service and activity
- The service is only provided a few times a year
- It is uncertain what the prospects for the service are (market, financing etc.)

To gain a clear insight into the costs of a new service the costs must firstly be calculated. And the decision must be made whether or not the service will be financed from contributions. If a service is set up from an existing department then it is often difficult to make a good cost estimate. The 'normal' conditions in which the market price determines the cost do not apply in this case. If an association feels it should set up a service because the market does not sufficiently meet the needs, then the following elements can be taken into consideration:

- What are the hours spent at what salary rate: how many hours do the association's employees spend in providing the service and what do they cost per hour?
- What are the hard costs for providing the service? Does this involve the costs of transport, purchasing equipment etc.?
- What management costs must be included? The association's management will obviously be involved with the new service and will want to supervise. A slight increase in the above mentioned costs to compensate for the management's involvement is therefore realistic.

In these circumstances we often see the 'piggyback principle' applied: riding on the mother's back. In view of the fact that some of the knowledge of the service already exists within an association and other tools are already partly available, the association can limit the costs to its members.

In addition to calculating the cost it is important to advertise the service to members. A promotional programme is needed to ensure the members know about the (advantages of) the service and any extra costs involved. Depending on the situation of the country and the association, a promotional programme may go together with a letter to members and other promotional material.

6.2 A new entity for providing the service (company)

If an association does not want to offer the service from its current organisation, it could offer its members a (paid) service via a new entity. Associations that do this generally choose to set up a wholly owned subsidiary or other structure that is majority owned by the parent association.

The advantage of placing the activities in a new company is that the company has an independent status. This independency is only partially true because the association remains responsible for the company's actions from an administrative point of view: the association must always be able to justify to its members that it owns the company, or has a share in it. The establishment of a company is not primarily a way to exclude the risk for the association.

An important element in considering whether or not to set up a separate company is whether the service concerns policy or administrative matters. Policy and administrative tasks are such an integrated part of an association that they cannot be properly executed by an independent company, even if the company is (partly) owned by the association.

CASE: CONTRACTING OUT ADMINISTRATIVE AND POLICY TASKS

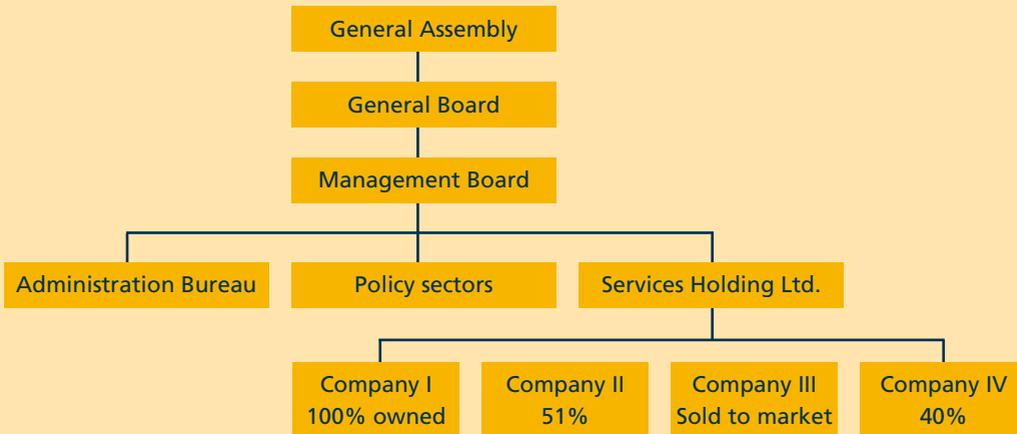
More in the international, and not purely municipal field, after the war in Iraq a number of policy and administrative tasks were contracted out. There were many security companies in Iraq to protect private individuals and employees of foreign companies. It was difficult to distinguish between what was the responsibility of the military and what was not. A stumbling block was who had to protect the civilian drivers of (oil) trucks. To deal with this dilemma the American government contracted a company to make the policy. A policy task was contracted out. Administration, policy and typical municipal or governmental tasks should never be contracted out, or placed in a partnership.

6.3 Restricting the entrepreneurial risk

If an association decides to establish a company, it is important to keep the financial risk, and risk of damage to reputation, limited to a minimum. One organisational form which also aims to limit any liability is the so-called Services Holding Ltd. The Services Holding can contain different services of the association. The Services Holding Ltd. can be held liable up to a maximum of the capital put in yet owes direct responsibility to the association's board. Because the Services Holding Ltd. falls directly under the association's board, the protection of interests is ensured. The company directors meet several times a year for discussions and obtaining in-depth knowledge in each others field. Interaction between the company directors and the policy sectors is desirable; the sectors also put forward their wishes which the companies can convert into commercial solutions.

To keep a perspective on the interests of the association and the companies, a supervisory council can be an important factor to provide the right direction. A supervisory council that understands the company can exercise supervision of the organisation's work. The supervisory council will focus on the profitability and the limits within which the company or companies must operate. Longer term matters can also be scrutinised, so that adjustments can be made on time. The supervisory council will also advise on the company's development and point to dangers. The association ensures proper supervision through the control of the supervisory council.

An organisational chart of an association with a Services Holding Ltd. could be as follows:



7 Conclusion

Offering services to members is one of the three tasks of an association of municipalities. The extent to which this occurs differs per association and is highly dependent on the phase of development and the circumstances in the country. An association can finance the services it wants to offer from different sources: the membership contribution, contributions from external donors or charging members for specific services. Especially in the case of the latter, good communication to members as to the added value of the service is very important. In each case the consideration should be made before an association offers a service as to whether the service will contribute to the association's mission and whether the service is already offered by other parties in the market.

Does your association have good experiences with the services of the members? And do you want to share these experiences with other associations? Then please contact VNG International; we are interested in hearing your experiences!

Annex 1: Example of a commercial service

An example of a commercial service which was successfully developed within the Association of Netherlands Municipalities, is presented.

The development and organisation of a commercial service in the VNG: The VNG Conference and Study Centre

History

The VNG organises many meetings for members and this important task in this respect was delegated to the VNG communications department. Over time the number of meetings increased and in 1979 a conference agency was set up. In 1990 the VNG Conference and Study Centre was set up. In 1999 the VNG decided to privatise a number of its activities and since 2001 the VNG Conference and Study Centre has been an independent company within the Services Holding. The company grew as conference organising agency for (decentralised) government and the non-profit sector. The VNG Conference and Study Centre now also organises activities for commercial organisations. As a sign of professionalism the Association of Dutch Conference Interests awarded the Conference and Study Centre the certified conference award in 2003. This makes the Conference and Study Centre one of nine certified conference organising agencies in the country. Over the years the VNG's Conference and Study Centre has evolved into a commercial service provider which expressly protects the interests of the VNG and its members.

Activities

The VNG Conference and Study Centre has a varied package of activities: conferences and other meetings, fairs and courses. These meetings cover a wide range of themes: nearly all themes which concern the ins and outs of local government are offered. Traditionally the Conference and Study Centre organises the VNG annual conference and other meetings of the VNG. The company not only provides conferences and other meetings on behalf of the VNG, but also on behalf of ministries, municipalities, trade and umbrella organisations and the service sector. The Conference and Study Centre also initiates meetings, fairs and courses on its own initiative, and so for its own account and risk. A general characteristic of all these meetings is that the target group is often administrators and local government. The scale of activities is very diverse: from a workshop or expert meeting for 10 to 20 people to conferences of several days with excursions for almost 3,000 participants, or an in-company course for 15 participants. A new offering in 2005 was the VNG municipal fair: a trade fair for public officials who were able to meet a large variety of suppliers, manufacturers and service providers. Annually the Conference and Study Centre serves over 30,000 participants.

The VNG Conference and Study Centre offers its customers a wide range of possibilities varying from administrative and secretarial support such as registering participants to contributing to the content and form of a conference, from invoicing the participant contributions to finding and briefing speakers and chairpersons, from arranging conference accommodations to producing a conference newspaper, to conducting electronic surveys among participants to sponsoring. In short, from just a few tasks to nearly everything. To ensure that the logistics and administrative process is effective and efficient, the VNG Conference and Study Centre has a specially designed computer system where participants register via internet.

The mission

The VNG Conference and Study Centre is considered as one of the communications tools with which VNG realises its mission:

- It offers the possibility to transfer information
- It offers the possibility to exchange information and form opinions (discussion)
- It offers the possibilities for relationship management (networking)
- It offers platform possibilities (recognisable and pro-active support)

Through the activities organised by the VNG Conference and Study Centre the VNG is able to reach a wide range of target groups, varying from own members to external authorities and from social organisations to community representatives.

Organisation

The VNG Conference and Study Centre organises some 300 activities per year, collectively drawing over 30,000 participants. It operates on a cluster structure, each cluster covering one or more VNG policy sectors. There is also a policy sector-independent cluster focusing strongly on own productions.

The centre employs 16 people:

- A director
- Three conference managers who each manage one cluster
- Seven conference coordinators
- Five secretaries, among whom also a web master

The financial accounting and the personnel administration have been contracted out. These paid services are respectively conducted by VNG's Financial Control and Human Resources. The Conference and Study Centre pays to make use of VNG's copy room and post room. The office accommodation is leased from VNG.

Benefits for the VNG

The privatisation of the VNG Conference and Study Centre has provided VNG with solid benefits and no drawbacks. Activities which the VNG Conference and Study Centre conducted for the VNG prior to privatisation, are still executed. The privatisation has allowed the company to spread its wings, with a positive effect on operating results. As sole shareholder the VNG thus clearly benefits. More risky activities can now also be undertaken which will only provide tangible and intangible benefits to VNG upon success, but will not directly damage the VNG if they fail.

In addition to a financial contribution to the VNG (the financial surplus of the past 3 years has increased by a multiple of seven), the Conference and Study Centre offers a platform where the opinions of VNG members can be analysed and where VNG's vision and strategy can be communicated. Additionally, the centre works with participation prices for meetings which are around 40% under the market price and to which VNG members are given an additional 25% discount. Through its activities the Conference and Study Centre also contributes to improving the quality of local government in the Netherlands, for example such as with the VNG Academy for Local Government.

VNG International

International co-operation agency of the Association of Netherlands municipalities

Committed to strengthening democratic local government worldwide

The key task of VNG International is strengthening democratic local government. It is a small, dynamic company annually managing some 60 plus projects and programmes with a focus on decentralisation and capacity-building. VNG International supports local governments, their associations and training institutions in developing countries and countries in transition.

VNG International's approach

For VNG International, strengthening democratic local government means working on three inter-related levels:

- The individual level – training and motivating municipal staff and elected representatives
- The organisational level – advising local authorities on their organisation structures and working methods
- The institutional level – adapting financial relations, laws and institutional arrangements

The VNG International approach builds on:

- Colleague-to-colleague co-operation
- Institutional linking

UCLG

United Cities and Local Governments

Founded in May 2004, United Cities and Local Governments (UCLG) is the united voice and world advocate of democratic local self-government. UCLG is the largest local government organisation in the world and is based in Barcelona, Spain.

Representing over half the world's population, the city and association members of UCLG are present in 127 UN Member States across seven world regions – Africa, Asia-Pacific, Europe, Euro-Asia, Middle East and West Asia, Latin America and North America. Its membership includes 1000 leading cities and virtually all the existing national Local Government Associations in the world.

Worldwide, the capacity, resources, influence and range of activities of Local Government Associations vary enormously. Local Government Associations have a key role to play in development, decentralisation and effective governance, but often need strengthening, before they can effectively support their individual local government members, or liaise well with central government, donors and other actors.

Building on the Association Capacity Building (ACB) concept pioneered by the global network of local governments, UCLG works to strengthen the capacity of the associations within its network through lobbying, encouraging cooperation and exchange of experience between its members, and through working with its members and partners on initiatives such as the VNG Association Capacity Building programme.