

Revising the Allocation of Functions of Government

(Version of 8 January 2017)

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The allocation of government functions¹ to the different state levels is a core element of a decentralization reform. Often, the existing allocation of functions is the result of historical circumstances and not designed in a rational way. Therefore, in the case of a decentralization process, the allocation of functions needs to be reconsidered.

The following guidelines are designed for Mongolia. They consider the following three state levels: Central state, Aimags, and Soums/Districts. In addition, specific capital city functions are taken into account as well. The methodology is based on Swiss experiences at Cantonal level, further developed and adjusted to the context of Mongolia after field-tests.

1. Guiding principles

From a public finance management perspective, the following principles are crucial:

- (1) The principle of disentanglement which means that a strict separation of powers between the different state levels is applied; for each function, the responsibilities of each state level are clearly defined; it is made clear who is responsible for which management function, e.g. strategic planning and control vs. operation of a function. It is neither effective nor efficient to build up similar, highly specialized capacities at the upper and lower state level at the same time.
- (2) The principle of subsidiarity, which means that functions are allocated towards the level closest to the citizens; a higher state level only takes over responsibility for a function if and in so far the objectives of the function cannot be sufficiently achieved by the lower state level.
- (3) The principle of fiscal equivalence, which means that the community that uses a public good or service should have the authority to take decisions on it and the obligation to finance its provision.
- (4) The principle of cooperation, which means that in case of shared or delegated functions, collaborative management approaches should be applied which facilitate the effective and efficient provision of services by higher together with lower state levels. This principle may also be applied if there are spillover effects across jurisdictions on the sub-central level, or if, due to economies of scale, the effective and efficient provision of services can only be ensured by horizontal collaboration.

¹ The term function is used in this methodology for policy-sector related functions like health, education, environmental protection, defense, etc. This concept of government functions should not be confused with management functions like planning, financing, implementation, etc.

2. Categories of functions of government and legal regulation

It is recommended to define clear types of functions. For each type, guiding considerations for the allocation are required. In addition, its legal regulation should be clearly defined. When functions are assigned to the appropriate type, the kind of regulation is implicitly specified.

The process should start with the analysis of the current allocation of functions and their financing per policy area. Policy areas are called “divisions” under COFOG. Then the question should be asked how it should look like in the future. In general, this should be done on the 2nd level of the COFOG classification, dedicated to sub-functions which are called “groups” by COFOG. In Mongolia, the existing programme classification will be used for that purpose. This classification is represented in the annex; it is generally quite detailed and comparable to the COFOG classification.

Soum and District Functions (SD)

Description

The function is completely assigned to Soums/Districts. They are responsible for planning, decision making, implementation, and financing.

Considerations for the allocation

The function can be carried out by the Soum or District independently. There is no need for coordination by a higher state level. The function is not part of a connected overall system as this would be the case with roads or sewerage or with region-wide public transportation. Soums of a medium size as well as Districts are capable to carry out the function in the quality required; they have the adequate size to fulfil the function in a cost-effective way (making use of economies of scale). Furthermore, Soums and Districts are in a position to finance the function autonomously.² It is acceptable that Soums or Districts of different areas carry out the function differently, respecting differences in citizen preferences (no bigger conflict with equity considerations exists). The function is of local interest; citizens might be attracted to participate in the planning and decision making process. There is scope for different types of solutions. Allocative efficiency is of particular interest. Finally, it is economically cost effective to carry out the function at local level (travel cost of customers should be considered together with the direct costs for service provision).

Legal regulation

Soums or districts are obliged to carry out the function by law. But there are no policy-related standards set by the higher level which go beyond basic standards.³

Examples: Street lighting, maintenance of sidewalks.

Aimag Functions (AM)

Description

The function is completely assigned to Aimags. Aimags are responsible for planning, decision making, implementation, and financing.

² We assume that revenues follow suit when functions are re-adjusted. In addition, we assume that an effective fiscal equalization system will provide a minimum level of resources for each sub-national entity.

³ Such standards are generally applicable for all policy sectors like construction or environmental standards or policy-related minimum standards.

Considerations for the allocation

The function can be carried out by each Aimag independently. There is no need for coordination by a higher state level; the function is not part of a connected nation-wide system as this would be the case with national roads, high-voltage lines or nation-wide public transportation. In addition, interest for the particular service is not uniform across the country; it differs from aimag to aimag as an effect of the socio-demographic or topographic situation in the Aimag or of tradition. Therefore, it is of a particular interest that Aimags of different areas can carry out the function differently, respecting differences in citizen's preferences (issue of allocative efficiency). There is scope for different types of solutions and ways of procedure. If services are delivered in such a differentiated way, no bigger conflict with equity considerations exists. Furthermore, the function is of Aimag-wide interest. Moreover, Aimags are in a position to finance the function autonomously and capable to carry it out in the quality required. Also, Aimags have the adequate size to fulfil the function in a cost-effective way (making use of economies of scale). Finally, it is cost effective to fulfil the function at Aimag level also when travel costs of customers are considered.

Legal regulation

Aimags are required to carry out the function by national legislation. But there are no policy-related standards set by the central state which go beyond basic standards.

Examples: Aimag museums and theatres, sports facilities, programs and measures to support employment and alleviate poverty in the Aimag

Capital City Functions (CC)

Description

The function is completely assigned to the Capital City. The Capital City is responsible for planning, decision making, implementation, and financing.

Considerations for the allocation

The function is of particular interest for the Capital City. It can be carried out by the Capital City independently. There is no need for coordination by the central state. The function is not part of a connected nation-wide system. The Capital City is capable to carry out the function in the quality required and it has the adequate size to fulfil the function in a cost-effective way (making use of economies of scale). Furthermore, the Capital City is in a position to finance the function autonomously.⁴ It is acceptable that the Capital City carries out the function in a different way than elsewhere in the country or that the Capital City may be responsible for a function that is carried out by the Central State elsewhere in the country. If services are delivered in such a differentiated way in the Capital City in order to respond to the specific preferences of its citizens and to the specific circumstances of a Capital City, no bigger conflicts with equity considerations exist. Finally, it is economically cost effective to carry out the function in the Capital City.

Legal regulation

The Capital City is required to carry out the function by national legislation. But there are no policy-related standards set by the central state which go beyond basic standards.

⁴ We assume that the fiscal equalization system will make provisions for the specific role of the Capital City.

Examples: Capital City museums, concert halls, parks, car parking policy, programs and measures to support employment and alleviate poverty in UB, urban public transportation, city planning, flood protection

Central State Functions (CS)

Description of the function

Functions are exclusively allocated to the higher state level. This level is responsible for policy planning, implementation and financing. Centralized governance is needed for this function, no local differentiation is allowed e.g. for reasons of legal equality. Furthermore, it is required that services are delivered country-wide at the same standard. Moreover, the function requires a connected and inter-linked system. Finally, highly specialized capacities are needed to regulate and implement this function.

Two variants exist:

CS-1 Central state function with centralized implementation

Criteria for the allocation

There is little direct contact with clients / citizens. Implementation needs highly specialized staff and large capital investments.

Legal regulation

Policy planning, implementation and financing are a responsibility of the central level.

Examples: High-end medicine, national defence, highways, railway.

CS2 Central state function with decentralized implementation

Criteria for the allocation

Contact with clients is frequent. Services are less costly if they are provided in a decentralized way (including costs of clients for travelling)

Legal regulation

Policy planning and financing is a responsibility of the central level; for the implementation, there are various possibilities: branches of line ministries or local public corporations, contracts with Soum or Aimag governments, Public Private Partnership. In each case, financing of the function remains to be a responsibility of the central state.

A central state function that is implemented by branches of line ministries or local public corporations makes use of the de-concentration approach.

A central state function that is implemented by Soums or Aimags is a delegated function.

A central state function that is implemented by private service providers is outsourcing services.

Examples: Universities, hospitals, customs,

Shared functions (SF)

Shared functions require vertical collaboration, i.e. higher and lower state levels fulfil a function jointly. They must be financed jointly in accordance with the principle of fiscal equivalence. The splitting of costs between the higher and lower state level should depend on the benefit each level has from the fulfilment of the function and from the operative discretion for cost optimization the implementing level has. In accordance with the principle of cooperation, in the area of shared functions, consultation of lower level is needed before the higher level takes any decisions which involve policy changes.

There are two broad variants:

SF-1 Shared functions with partial flexibility

The higher state level and the lower state level collaborate in the execution of a function. The higher state level enacts general binding standards, for example in a framework law, which may be (or must be) specified by the lower state level. The lower state level has operational leeway for the implementation.

Consideration for the allocation

There is a strong common interest for mandatory norms with country-wide applicability. Reasons could be legal equality including equal opportunities (e.g. pre-university education or social security). Furthermore, the regulation may require a high degree of specific knowledge. In addition, if central regulation was lacking, free-riding might occur resulting in spill-over effects. This could be the case if one sub-national government offers poor services only and does this on purpose in order to shoo away citizens in need to other sub-national governments, thus avoiding costs at home but creating additional costs for neighbouring soums or aimags. This could be the case with social welfare services or education. Provision of such services by the central state could be a way out. However, the service should not be centralised but provided locally because of frequent contacts with the local clients, and, according to the principle of subsidiarity, the objectives can be reached best and most efficiently produced by sub-national governments. Sub-national governments do have the necessary capacities to implement the function appropriately. Finally, there is no need that the function is implemented in each sub-national government in an identical way.

Legal regulation

Collaboration between the higher and lower state level is mandatory. The higher state level sets the strategic goals. The lower state level can or must specify these goals to a certain extent and has operative discretion for the implementation.

Examples: pre-university education, local roads, primary health care.

SF-2 Shared functions without flexibility

The higher state level enacts the policy standards in detail and leaves only limited discretion for the implementation by sub-national governments.

Considerations for the allocation

The same considerations for central state regulation apply as for SF-1. However, regarding implementation, there is no room for discretion. Methodologies and procedures need to be standardized for reasons of legal equity, comparability or technical compatibility.

Legal regulation

Collaboration between the higher and lower state level is mandatory. The higher state level sets strategic goals and specifies methodologies and processes for the implementation. The lower state level has little or no operative discretion for the implementation.

Examples: Elections, territorial planning, standards for public finances, national statistics, fighting infectious livestock and animal diseases, pest eradication and control.

Varieties of vertical collaboration

There might be a need for vertical collaboration between different state levels with partial or little flexibility as follows:

<i>Partners for vertical collaboration</i>	<i>Type 1 with partial flexibility</i>	<i>Type 2 without flexibility</i>
Central State and Aimags	SF-CS-AM-1	SF-CS-AM -2
Central State and Capital City	SF-CS-CC-1	SF-CS-CC -2
Central State and Soums/Districts	SF-CS-SD-1	SF-CS-SD-2
Aimags/Capital City with Soums/Districts	SF-AM-SD-1	SF-AM-SD-2

The cost share of the central state needs to be higher for SF-2 than for SF-1.

Horizontal Collaboration Functions (HC)

In the case of horizontal collaboration, two or more governments of the same state level work together. This collaboration may take place for two reasons: making use of a synergy potential (e.g. economies of scale) or addressing spill-over effects. Synergy potentials exist in cases of high fixed costs together with capacity reserves. By actively cooperating, fixed costs per unit can be reduced as capacity utilization increases. Spill-over effects⁵ exist when neighbour state entities can benefit from services or systems provided and subsidized by another regional or local authority, without paying for these services. When these spill-over effects are not addressed, there is a risk that these services are not provided in a sufficiently high quantity or quality.

Considerations for the allocation

Substantial synergy potential or spill-over effects exist. Collaboration is essential.

Legal regulation

Collaboration needs to be based on a collaboration agreement of the collaboration partners.

Collaboration is voluntary. However, it can be declared mandatory in case of substantial spill-over

⁵ In fact, there are two classes of spillover-effects; they can be beneficial or adverse. In the case mentioned above, only beneficial spillover-effects are considered. For adverse effects, mitigation strategies or compensation schemes are needed.

effects or economics of scale. The higher state level can intervene when individual sub-national governments refuse to collaborate. Sub-national governments have discretion on how the collaboration should be organized. Nevertheless, the collaboration arrangement should respect the principle of fiscal equivalence.

Examples: Secondary schools, inter-Soum public transportation, waste disposal, water protection of lakes and rivers.

Varieties of horizontal collaboration

There might be a need for horizontal collaboration in the following way:

Partners for horizontal collaboration	Type
Aimag with Aimag	HC-AA
Soum with Soum	HC-SS
District with District	HC-DD

If needed, horizontal collaboration can be combined with vertical collaboration.

3. Allocation of costs

When functions are shifted from one state level to another, this implies that costs are shifted in the same way to another level. According to good practice and the principle of finances follow functions, the process should start with the allocation of functions and then, it is needed to calculate the cost for each function that was transferred. This calculation should be based on the costs of all parties involved, the central level and both sub-national levels in a consolidated way, preferably based on figures of the last three years. With this information, it should be possible to calculate the cost per unit and to estimate the costs for the starting year, when the new system of functional allocation enters into force.

This calculation is needed for each individual function transferred.⁶ By summing up the results, the total of transferred costs can be quantified.

⁶ For functions that do not change hands, there is no need for a consolidated cost view for the purpose of the reallocation of functions and finances.

4. Allocation of taxes and grants

Taxes with a high fluctuation over time should not belong to the local level. This level needs yielding taxes with a steady growth rate. Furthermore, it is highly recommended not to allocate taxes with high horizontal variance at the local level. This would require more fiscal equalization afterwards.

Earmarking of grants should be reserved for shared or delegated functions, i.e. where vertical collaboration is required or central state functions are implemented via Soums. In all other cases, earmarking of grants is not functional. Earmarked grants should be agreed in multi-year performance contracts while, according to good practice, non-earmarked grants should be formula-based block grants.

When functions - and therefore costs - are reallocated, it is required that revenues follow suit.

5. Organization of the reform process

The process for the allocation of functions should be organized as a project with clear and broadly agreed goals and timeframes. Furthermore, a project organization with strong political leadership is needed. A coordination committee organised as a Task Force Team is needed which should be well anchored in the core ministries and include the sub-national level as well. Moreover, an operational structure should work out the details of the reform. This operational structure should be composed of a project implementation unit (PIU) and mixed technical working groups (TWG) for each policy sector. The PIU should be headed by a strong technical project manager; his task would be to coordinate the project. He should be supported by a group of experts. In each TWG, it is recommended to have national and sub-national policy specialists, one or two each side; furthermore, at least one expert for public finances and a legal adviser should complete each working group. Finally, a communication strategy is needed which makes sure that the major stakeholders can continuously follow and validate the project.

Annex

A1-Overview of Functions

Type	Explanation
SD	Soum and District function
AM	Aimag function
CC	Capital City functions
CS	Central State function
CS-1	Central State function with centralized implementation
CS-2	Central State function with de-centralized implementation
SF	Shared function
SF-1	Shared function with partial flexibility
SF-CS-AM-1	Shared function with partial flexibility between Central State and Aimag
SF-CS-CC-1	Shared function with partial flexibility between Central State and Capital City
SF-CS-SD-1	Shared function with partial flexibility between Central State and Soums/Districts
SF-AM-SD-1	Shared function with partial flexibility between Aimag and Soums/Districts
SF-2	Shared function with little flexibility
SF-CS-AM-2	Shared function with little flexibility between Central State and Aimag
SF-CS-CC-2	Shared function with little flexibility between Central State and Capital City
SF-CS-SD-2	Shared function with little flexibility between Central State and Soums/Districts
SF-AM-SD-2	Shared function with little flexibility between Aimag and Soums/Districts
HC	Horizontal collaboration function
HC-AA	Horizontal collaboration function between Aimag and Aimag
HC-SS	Horizontal collaboration function between Soum and Soum
HC-DD	Horizontal collaboration function between District and District

A2-Template for the allocation of functions

(1) Name and programme code of function reviewed

(2) Current allocation of function (type)

(3) Possible problems with current allocation of function

(4) Legal basis of function

(5) Assessment of potential for decentralisation of this function

In accordance with the subsidiarity principle, functions need to be allocated at the lowest state level possible. To allocate a function at a higher state level must be justified. The following set of criteria follows this logic.

Criteria	True	Half true	False	Score
	1	0.5	0	
Allocative efficiency:				
1. Uniform needs across sub-central governments exist				
2. Spill-over-effects or need for coordination				
Operational efficiency:				
3. Economies of scale, cost advantage of large units exist				
4. Expensive know-how required				
5. No frequent contact with local clients				
Equity:				
6. Uniform or minimum service delivery standards required or desired				
7. Affects fairness issues				
Total score				

Scores will be consolidated.

The higher the total score, the more centralized a function should be allocated.

For instance:

If the total score is lower than 2, the function should be allocated at soum/district level.

If the total score is higher than 1,5 but lower than 4, the function should be allocated at capital city and aimag level.

If the total score is higher than 3.5, the function should be allocated at the central government level.

Final proposal to reallocate functions will be made based on consideration of unique features and matters of implementation of the particular functions

(6) Justification of suggested category

(Write down short text. Use all properties mentioned in the description for this functional category in chapter 2 of the guidelines and specify why this property is given.)

(7) Implications for cost assignment

Assessment of the costs for the function, who is responsible for which cost before and after the reform. What should change and why. Who will pay more and how much? Who will pay less and how much?

Cost implication of reallocation of specific function			
in Billion MNT	Before reform	After reform	Change
National costs			
Salaries			0
Goods and services purchased			0
Transfers paid			0
Transfers received			0
Interest rates			0
Capital investment costs			0
Capital investment contributions from sub-national governments			0
Others			0
Relevant Total			0
Aimag costs			
Salaries			0
Goods and services purchased			0
Transfers paid			0
Transfers received			0
Interest rates			0
Capital investment costs			0
Capital investment contributions from national government			0
Capital investment contributions from lower state level			0
Others			0
Relevant Total			0
Capital City costs			
Salaries			0
Goods and services purchased			0
Transfers paid			0
Transfers received			0
Interest rates			0
Capital investment costs			0
Capital investment contributions from national government			0
Capital investment contributions from lower state level			0
Others			0
Relevant Total			0
Soum / District costs			
Salaries			0
Goods and services purchased			0
Transfers paid			0
Transfers received			0
Interest rates			0
Capital investment costs			0
Capital investment contributions from national government			0
Capital investment contributions from intermediate state level			0
Others			0
Relevant Total	0	0	0

In case of a full reallocation of the function under review from one state level to another, the form needs to be filled out completely.

In case of a disentanglement of a function, it is only needed to fill in the details of what changes.

In case the function remains unchanged, there is no need to fill in the form.

Fields shaded in grey need entries with a negative sign. The last column is calculated automatically.

Example

Cost implication of reallocation of specific function			
in Billion MNT	Before reform	After reform	Change
National costs			
Salaries			0
Goods and services purchased			0
Transfers paid	2500	0	-2500
Transfers received			0
Interest rates			0
Capital investment costs			0
Capital investment contributions from sub-national governments			0
Others			0
Relevant Total	2500	0	-2500
Aimag costs			
Salaries	3000	0	-3000
Goods and services purchased			0
Transfers paid		0	0
Transfers received	-1500	0	1500
Interest rates			0
Capital investment costs			0
Capital investment contributions from national government			0
Capital investment contributions from lower state level			0
Others			0
Relevant Total	1500	0	-1500
Capital City costs			
Salaries	2000	0	-2000
Goods and services purchased			0
Transfers paid		0	0
Transfers received	-1000		1000
Interest rates			0
Capital investment costs			0
Capital investment contributions from national government			0
Capital investment contributions from lower state level			0
Others			0
Relevant Total	1000	0	-1000
Soum / District costs			
Salaries	0	5000	5000
Goods and services purchased			0
Transfers paid			0
Transfers received	0	0	0
Interest rates			0
Capital investment costs			0
Capital investment contributions from national government			0
Capital investment contributions from intermediate state level			0
Others			0
Relevant Total	0	5000	5000

Explanation

This shows a disentanglement case. We assume that there are only salary costs. Before the reform, the function was carried out by the intermediate state level with 50% subsidies of the costs (transfers for the function) from the national level. After the reform, it is suggested that the function is implemented by soums and districts without subsidies.

In our example, the soums and districts will have to pay the full costs (5000). In contrast, the central state pays 2500 less, aimags 1500 less (net), Capital city 1000 less (net).

These results will be imputed in the global balance together with the results for other functions.

(8) Implications for administrative competences.

Indicate with a cross “x” for each function how administrative competences have to be allocated according to the suggested functional allocation. In case of changed administrative competences compared to the actual situation, highlight the cross with colour.

	Central State	Aimag	Capital City	Soum	Private Sector
Long term policy formulation and/or legal basis					
Setting of norms and standards: e.g. health and safety standards, standards of service quality, quantity and frequency, minimal management standards, etc.					
Medium term strategy formulation: e.g. development objectives, setting priorities, service provision approach (contracting out or not), timetable, etc.					
Regulation: e.g. frequency, quantity, tariff policy, location of service delivery; instructions, directives, etc.					
Financing					
Human resources management: e.g. wage structure, hire and fire policy, gender equality, capacity building, etc.					
Procurement					
Service provision					
Monitoring and evaluation					

[Check again whether administrative suggestions are in conformity with the functional category.]

(9) Assessing the Potential for Outsourcing

Checklist for assessing the outsourcing potential for service production or delivery				
1	Categorical criteria	yes	no	Result
1.1	Function is not a sovereign task	1	0	
1.2	Public security is not concerned	1	0	2
2	Economic criteria			
2.1	Standard product	1	0	
2.2	Competitive market for the product exists with capable suppliers	1	0	
2.3	Quantity easy to define and measure for client	1	0	
2.4	Quality easy to define and to supervise for client	1	0	
2.5	Low risk of market entry barriers, resulting from high fixed costs	1	0	
2.6	Easy to change provider when limited time contract is over	1	0	
2.7	In case of public infrastructure, maintenance easy to supervise	1	0	
2.8	Potential for innovation high	1	0	
2.9	Regulation costs low	1	0	
2.10	Clearly defined objectives, no need for frequent re-negotiation of contract	1	0	
2.11	Specialised know how too expensive for public sector especially when only for temporary use	1	0	11
3	Political criteria			
1.1	Acceptance of public for private delivery of particular service high enough	1	0	
1.2	Acceptance of public for cost coverage with fees exists	1	0	
1.3	Risk of corruption and patronage in particular sector low	1	0	
1.4	No state liability for service provider, neither explicit nor implicit	1	0	
1.5	Labour conditions in concerned private sector acceptable	1	0	
1.6	National identity/national heritage not affected	1	0	6

Interpretation of results	
1	Categorical criterion / no sovereign task
	If result = 2, then no categorical objection. If result < 2, then outsourcing needs critical deliberation. Transfer of sovereign power or transfer of public security related functions to private sector need restrictive regulation and close oversight.
2	Economic criteria
	If result > 9 then expected economic benefit relatively high, economic risks low.
	If 6 < result < 10 then potential for economic benefit exists, economic risks more substantial. Carefully prepared contracts are needed as well as accompanying measures.
	If result < 7, then benefit of contracting out compared with long turn-cost of the approach is probably too low.
3	Political criteria
	If result > 4, political viability relatively positive.
	If 2 < result < 5, political resistance increased, accompanying strategy needed
	If result < 3, politically not favourable

Recommendation of the TWG for the outsourcing of production or delivery of the service

Justification, considerations and need for accompanying measures

A-3 Global Balance Template

(Illustration: Simplified form for Aimags)

Global Balance Aimag Sector																			
Period		2013/14																	
Production		December 2, 2015																	
in 1'000 Tugreg (+ = credit, - = debit)																			
		Functional Allocation										Fiscal Equalization					Cohesion Fund	Global Balance	
		Disentangelment				Shared functions			Horizontal cooperation			Balance Functional Allocation	Ressource		Cost compensation				Balance
		Central Government	Aimags	Capital City	Soums and Districts	Central State - Aimags	State - Capital City	State - Soums and	Aimag - Aimag	Soum - Soum	District- District		Vertical	Horizontal	Socio- demo- graphic	Geographic topo- graphic			Fiscal Equali- zation
		CS	AM	CC	SD	SF-CS-AM	SF-CS-CC	SF-CS-SD	HC-AA	HC-SS	HC-DD		BA	VRE	HRE	SCC			GCC
1	Arkhangai																		
2	Bayankhongor																		
3	Bayan-Ölgii																		
4	Bulgan																		
5	Darkhan-Uul																		
6	Dornod																		
7	Dornogovi																		
8	Dundgovi																		
9	Govi-Altai																		
10	Govisumber																		
11	Khentii																		
12	Khovd																		
13	Khövsgöl																		
14	Orkhon																		
15	Selenge																		
16	Sükhbaatar																		
17	Töv																		
18	Ömnögovi																		
19	Uvs																		
20	Övörkhangai																		
21	Zavkhan																		
22	Ulaanbaatar																		
	Total Aimags																		
	Central Government																		
	Balance																		

[illegible]

A-4 Classification of the Functions of Government

Below, the list of functions classified in accordance with COFOG is compared with the of programme classification as used by the Ministry of Finance in Mongolia.⁷

GFSM 2001 Functional Classification (COFOG)		Program Code MOF Mongolia	
code	Transactions	Code	Transactions
701	General public services	70100	President, the legislative and the executive governance
7011	Executive and legislative organs, financial and fiscal affairs, external affairs	70101	President of Mongolia - policies and activities
70111	Executive and legislative organs	70102	Legislative, monitoring of law enforcement
70112	Financial and fiscal affairs	70103	Executive organs, secretariat
70113	External affairs	70104	R&D President, legislative and executive organs
7012	Foreign economic aid	70105	Operations of local self-governing bodies
70121	Economic aid to developing countries and countries in transition	70106	Administration of local governments
70122	Economic aid routed through international agencies	70200	Overall planning, financial and fiscal affairs
7013	General services	70201	Economic development planning
70131	General personnel services	70202	Financial, fiscal and economic management
70132	Overall planning and statistical services	70203	Government debt servicing
70133	Other general services	70204	Financial market regulation
7014	Basic research	70205	Tax collection, revenue mobilization
7015	R&D General public services	70206	R&D Economic, finance
7016	General public services n.e.c.	70207	Projects funded by foreing loans and grants
7017	Public debt transactions	70300	External affairs
7018	Transfers of a general nature between different levels of government	70301	Operation of diplomatic missions stationed abroad
702	Defense	70302	Services of IFIs and diplomatic missions in Mongolia
7021	Military defense	70303	Development of international cooperation
7022	Civil defense	70304	Services rendered to Mongolians residing abroad
7023	Foreign military aid	70305	Foreign policy and management
7024	R&D Defense	70306	Research and studies on foreign affairs
7025	Defense n.e.c.	70400	Other general public services and operations
703	Public order and safety	70401	Administration, coordination of the civil service
7031	Police services	70402	State audit services
7032	Fire protection services	70403	Organizing elections at all levels
7033	Law courts	70404	Monitoring of the Constitution enforcement
7034	Prisons	70405	Offical statistics
7035	R&D Public order and safety	70406	State registration, information
7036	Public order and safety n.e.c.	70407	Standardization and measurement
704	Economic affairs	70408	Anti-corruption activities
7041	General economic, commercial and labor affairs	70409	Human rights monitoring
70411	General economic and commercial affairs	70410	Promoting market competitiveness and protecting consumers' rights
70412	General labor affairs	70411	State archives
7042	Agriculture, forestry, fishing and hunting	70412	State special security services
70421	Agriculture	70413	Government services
70422	Forestry	70414	Economic assistance to foreign countries
70423	Fishing and hunting	70415	Advanced training and retraining of civil servants
7043	Fuel and energy	70416	Rehabilitation of victims of political repression
70431	Coal and other solid mineral fuels	70417	Professional inspection
70432	Petroleum and natural gas	70418	Procurement
70433	Nuclear fuel	70419	Program and project management, regulation
70434	Other fuels	70420	Immigration, registration of foreign citizens
70435	Electricity	70421	Refunding the loss from wrongful activities of civil servant
70436	Non-electric energy	70422	National public press
7044	Mining, manufacturing and construction	70423	Activities of domestic, foreign news agencies
70441	Mining of mineral resources other than mineral fuels	70424	Internal and external newflash activities
70442	Manufacturing	70425	Local press
70443	Construction	70426	Exercising state property rights
7045	Transport	70427	R&D general public services
70451	Road transport	70428	Intellectual property rights
70452	Water transport	70500	Transfers between the governance levels
70453	Railway transport	70501	Revenue transfers to local budget
70454	Air transport	70502	Financial support to local budget
70455	Pipeline and other transport	70503	Targeted local investment
7046	Communication	70600	Defense
7047	Other industries	70601	Operations of armed forces
70471	Distributive trades, storage and warehousing	70602	Border protection
70472	Hotels and restaurants	70603	R&D military and defense

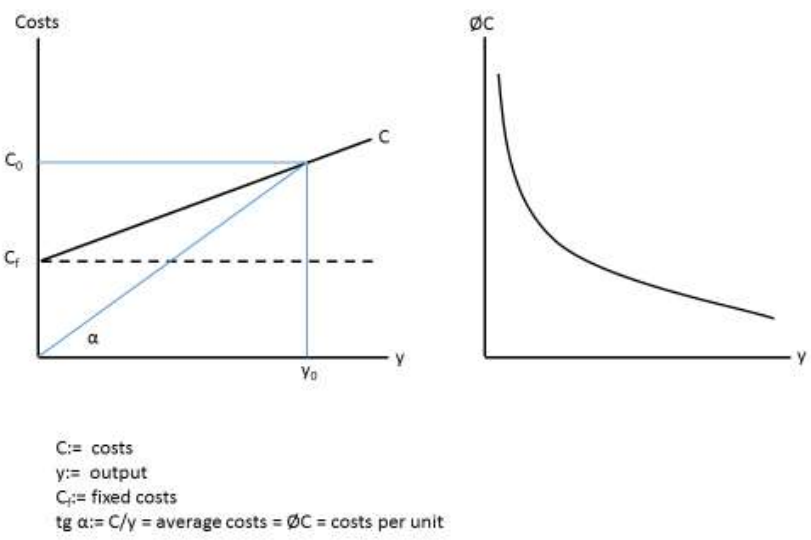
⁷ See: Fischer, R. (2016). Mission to Mongolia on Fiscal Equalization, Government Finance Statistics and Global Balance: Findings and Recommendations for Future Work, p. 28-29.

GFSM 2001 Functional Classification (COFOG)		Program Code MOF Mongolia	
code	Transactions	Code	Transactions
70473	Tourism	70700	Legial, public order, safety affairs
70474	Multipurpose development projects	70701	Ensure judicial independence
7048	R&D Economic affairs	70702	Supevisory court legal proceedings
70481	R&D General economic, commercial and labor affairs	70703	Prosecutor's oversight
70482	R&D Agriculture, forestry, fishing and hunting	70704	Police
70483	R&D Fuel and energy	70705	Enforcement of Court ruling
70484	R&D Mining, manufacturing and construction	70706	Protecting national security
70485	R&D Transport	70707	Court examination
70486	R&D Communication	70708	Disaster mitigation and rehabilitation
70487	R&D Other industries	70709	Crime prevention
7049	Economic affairs n.e.c.	70710	Legal assistance to defendants and suspects who are unable to pay for services
705	Environmental protection	70711	Protection of judges, witnesses and their families
7051	Waste management	70712	Law, public order, safety and security administration
7052	Waste water management	70713	R&D law, public order, security research and analysis
7053	Pollution abatement	70800	Agriculture, crop production, manufacturing
7054	Protection of biodiversity and landscape	70801	Development of agriculture
7055	R&D Environmental protection	70802	Development of crop production
7056	Environmental protection n.e.c.	70803	Development of food industry
706	Housing and community amenities	70804	Light industry development
7061	Housing development	70805	Agriculture, crop production, manufacturing policy, administration
7062	Community development	70806	R&D agriculture, crop production, manufacturing
7063	Water supply	70807	The development of heavy industry
7064	Street lighting	70900	Energy, mining
7065	R&D Housing and community amenities	70901	Electric power
7066	Housing and community amenities n.e.c.	70902	Coal
707	Health	70903	Oil and fuel
7071	Medical products, appliances and equipment	70904	Radioactive minerals and nuclear energy
70711	Pharmaceutical products	70905	Extraction, mining
70712	Other medical products	70906	Energy, mining policy and administration
70713	Therapeutic appliances and equipment	70907	R&D energy, mining research and study
7072	Outpatient services	71100	Road and transport
70721	General medical services	71101	Autoroad
70722	Specialized medical services	71102	Water transport
70723	Dental services	71103	Railway
70724	Paramedical services	71104	Air transport
7073	Hospital services	71105	Traffic control, regulations, public transport
70731	General hospital services	71106	Border port services
70732	Specialized hospital services	71107	Road and transportation administration
70733	Medical and maternity center services	71108	R&D road and transportation
70734	Nursing and convalescent home services	71200	Trade
7074	Public health services	71201	Development of free zones
7075	R&D Health	71300	Communications
7076	Health n.e.c.	71301	Administration of communication
708	Recreation, culture and religion	71302	General information system, infrastructure
7081	Recreational and sporting services	71303	R&D Communications
7082	Cultural services	71400	Environment
7083	Broadcasting and publishing services	71401	Waste management
7084	Religious and other community services	71402	Biodiversity conservation
7085	R&D Recreation, culture and religion	71403	Afforestation
7086	Recreation, culture and religion n.e.c.	71404	Water resource, lake and river management
709	Education	71405	Security of protected areas
7091	Pre-primary and primary education	71406	Environmental pollution and degradation
70911	Pre-primary education	71407	Air pollution abatement, climate change
70912	Primary education	71408	Meteorology
7092	Secondary education	71409	Protection of endangered animals, plants and species
70921	Lower secondary education	71410	Reduce land degradation and prevent from desertification
70922	Upper secondary education	71411	Environment policy and administration
7093	Post-secondary non-tertiary education	71412	R&D Environment
7094	Tertiary education	71500	Construction, urbanization, community amenity affairs
70941	First stage of tertiary education	71501	Construction
70942	Second stage of tertiary education	71502	Community development
7095	Education not definable by level	71503	General urban planning
7096	Subsidiary services to education	71504	Land mapping, cadastre
7097	R&D Education	71505	Land confirmation survey
7098	Education n.e.c.	71506	Water supply of residential area
710	Social protection	71507	Sanitation facilities
7101	Sickness and disability	71508	Street lightening
71011	Sickness	71509	Construction, urban development, community service policy and administration
71012	Disability	71510	R&DConstruction, urban development, community amenity affairs

GFSM 2001 Functional Classification (COFOG)		Program Code MOF Mongolia	
code	Transactions	Code	Transactions
7102	Old age	71600	Health
7103	Survivors	71601	Public health
7104	Family and children	71602	Healthcare services
7105	Unemployment	71603	Health policy and administration
7106	Housing	71604	R&D Health
7107	Social exclusion n.e.c.	71700	Culture, art sports, tourism
7108	R&D Social protection	71701	Sports
7109	Social protection n.e.c.	71702	Culture and art
		71703	Tourism
		71704	Culture, sports and tourism policy and management
		71705	R&D Culture, sports and tourism
		71800	Education, science
		71801	Pre-school education
		71802	General education
		71803	Higher education
		71804	Vocational education
		71805	Science and technology
		71806	Lifelong and informal education
		71807	Special education
		71808	Education, science policy and administration
		71809	R&D Education, science
		71900	Social security
		71901	Social insurance
		71902	Social welfare
		71903	Social security administration
		71904	R&D Social security
		72100	Employment
		72101	SME development, employment generation
		72102	Employment promotion
		72103	Labor safety and hygiene
		72104	Employment policy and administration
		72105	R&D Employment
		72200	Targeted social programs
		72201	Gender equality
		72202	Assistance and support to alcohol and drug addicts
		72203	Rehabilitation of victims of political repression
		72204	Activity of acquitting people falsely charged in political crime
		72205	Housing
		72206	Protection and development of disabled people
		72207	Protection and development of children
		72208	Protection and development of elderly
		72209	Youth and students
		72210	Herders, self-employed and informal sector workers
		72211	Combating human trafficking
		72300	Other unclassified
		72301	Other unclassified

A-5 Glossary of technical terms

Allocative efficiency	Allocative efficiency refers to the allocation (or use) of scarce resources. Resources are allocated to the different policy function like health, transportation, education, defence, etc. in a way that considers in an optimal way the preferences (needs) of the society.
Block grant	A grant from central government which can be spent by sub-national governments with great discretion either for the fulfilment of their functions in general or for specified functions only.
Capable supplier	Supplier of an item that meets the design requirements and is delivered on time.
Categorical	foundational, fundamental, basic
Competitive markets	A large number of sellers and buyers (i.e. market actors) exist for a specific product or service. In addition, market entry barriers are low or absent. Market actors cannot manipulate the price of the product either by themselves or by collusion.
Comparability	Comparability means the technical and/or methodological possibility to compare things with each other. For example: the comparability of fiscal data needs standards on the classification of the data.
COFOG	The Classification of the Functions of Government is used internationally in a standardized way by the statistics system of the UN, IMF and OECD to show how public resources are spent according to policy purposes like health, education, defence etc.
Cooperation principle	In case of shared or delegated functions, collaborative management approaches should be applied which facilitate the effective and efficient provision of services by higher together with lower state levels. The cooperation principle may also be applied if there are spillover effects across jurisdictions on the sub-central level, or if, due to economies of scale, the effective and efficient provision of services can only be ensured by horizontal collaboration.
Cost coverage	Costs for the production and distribution of a good or service are covered fully or in part by revenues originating from sales prices or fees for this good or service.
Cost-effective	Producing a good result at relatively low costs
Earmarked transfers or grants	Grants, funds or resources transferred between levels of government designated for a particular purpose or function.
Delegated function	A central state function that is implemented by Soums or Aimags is a delegated function
Disentanglement principle	Powers and responsibilities for a function are clearly allocated to the different state levels. Overlapping responsibilities and multiple responsibilities for the same function are eliminated.
Economics of scale	Cost advantages resulting from higher size, bigger output, or larger scale of operation. Cost per unit of output are generally decreasing as fixed costs are spread out over more units of output.

	 <p> C := costs y := output C_f := fixed costs $\text{tg } \alpha := C/y = \text{average costs} = \text{ø}C = \text{costs per unit}$ </p> <p>Example: When a dump site is used by a bigger number of clients, the cost per unit in tons of waste going to landfill decreases.</p> <p>In such cases, horizontal collaboration may be required or the allocation of the function at a higher state level.</p>
Elite capture	Elite capture occurs when resources designated for the benefit of the larger population are captured by a few individuals of superior status, be it economic, political, educational, ethnic or otherwise. Individuals or groups take advantage of government programs aimed at distributing resources or funds to the general public by using their elite influence to direct such assistance in such a way that it primarily benefits the elite group.
Equity	Synonym for fairness and justice. Equity implies giving as much advantage, consideration, opportunities or freedom to one party as it is given to another. It implies that income, costs, goods, and services are fairly divided among the population.
Fairness	Synonym for equity and justice.
Finances follow functions principle	It would be wrong to start the discussion about the allocation of functions with the question which state level is able to finance it. On the contrary, firstly, it should be assessed, based on functional criteria, which is the adequate state level to fulfil the function. If functions are re-allocated from one state level to another one, this involves additional expenditure for the state level that is newly responsible for the function. Conversely, expenditure of the former responsible state level is reduced. Therefore, in parallel, revenue needs to be transferred from the former to the newly responsible state level. By doing so, finances follow the reallocated functions.
Fiscal equivalence principle	The community that uses a public good or service should have the authority to take decisions and the obligation to finance its provision.
Formula based block grants	A block grant is a general purpose grant with only general provisions as to the way it is to be spent. A formula based block grant is allocated to different recipients according to clear objective criteria, as for example depending on the population size, the surface area, number of students, etc.

Free riding	Free riding occurs when those who benefit from resources, goods, or services do not pay for them.
Function	Function is used in this methodology for policy-sector related government functions like health, education, environmental protection, defence, etc. This concept of government functions should not be confused with management functions like planning, financing, implementation, etc.
Global balance	Overview of the financial impact of re-allocated functions and of a new fiscal equalisation system shown for central government and each unit of sub-national government.
Horizontal collaboration functions	Two or more governments of the same state level work together for two reasons: 1) Making use of a synergy potential in the case of economies of scale (= cost advantage of large units) or 2) Addressing spill-over effects (= cross-border impacts)
Limited time contract	A contract between the public client and the private contractor which lasts for a specific period of several years only. Towards the end of this period, a new invitation to tender is prepared which offers new firms the opportunity to win the new contract with improved conditions for the client.
Legal equality	Everybody must be treated equally under the law regardless of their race, gender, national origin, colour, ethnicity, religion, disability, or other characteristics, without privilege, discrimination, or bias.
Market entry barrier	Factors that prevent a start-up firm from entering a particular market. Economies of scale / high fixed costs, long experience of the incumbent firm, exclusive access to distribution channels, high capital requirements, well established brands or government preferences may create such impediments.
National heritage	National heritage sites have a value of national importance that has been registered by a national agency; these sites include natural wonders, historical sites, religious facilities, ruins, engineering marvels, etc. They are open for the public and can be used for tourism.
National identity	Sense of a group of persons of belonging to one state or nation with distinctive traditions, culture, language and politics.
Need for frequent re-negotiation of the contract	When the objectives of the contract are not clearly defined from the beginning, a contract needs to be re-negotiated from time to time. This may be the case because initially, the contract was not well prepared, the needs were not clearly defined or assessed, the needs and wishes evolve over the contract time or the project was too complex and couldn't be defined in all details from the beginning. Examples: IT-projects, complex construction works, etc. In such cases, the client is dependent on the contractor who can exploit his position to his own benefit.
Non-earmarked transfers or grants	Grants, funds or resources transferred between levels of government for discretionary use, i.e. without reservation for a particular purpose or function.
Operative discretion	Discretion means the freedom to decide what should be done in a particular situation. Operative discretion therefore refers to decisions on operational issues only and not on strategic and legal issues. Example for operational issues are: the daily management, the planning of service provision, etc.
Operational efficiency	Optimal use of resources in view of providing public services in a cost-effective manner.

Operational leeway	Synonym for operational discretion
Patronage	Power to confer favours, give employment, support or protection to a group of individuals with privileged relations to the ruling group.
Preferences	In decision-making, the order of alternatives you would choose in the first, second or third rank, etc. It also shows how much of good A you would give up to have one more unit of good B. Possibly, preferences for public services are not the same in urban areas as in remote rural areas.
Programme code of functions	The programme code of functions refers to the classification of government functions according to programmes of governments. Each programme has a number that is its programme code. In Mongolia, the first level of the code is similar to the classification of functions of the government (COFOG) of the International Monetary Fund (IMF).
Shared function	The responsibility for a government function is shared between a higher and a lower level of government, which requires vertical collaboration between the two.
Shared function with partial flexibility	The higher state level and the lower state level collaborate in the execution of a function. The higher state level enacts general binding standards, for example in a framework law, which may be (or must be) specified by the lower state level. The lower state level has operational discretion for the implementation.
Shared function without flexibility	The higher state level enacts the policy standards and laws in detail and leaves only limited discretion for the implementation by sub-national governments.
Sovereign task	Sovereign tasks are state functions which are derived from the fundamental power of the state. The government is entitled to exercise sovereign authority to carry out the task. Examples of sovereign tasks are foreign policy, defence, taxation, regulatory policy, law enforcement and prosecution, etc. Sovereign tasks can be considered as the “core business” of the state. Usually, the exercise of these tasks is restricted to state organs only. However, in some countries, the fulfilment of some sovereign tasks was contracted out, for example tax collection, prisons, functions of national defense, etc.
Spill-over effects	<p>Side effect of an activity or facility that affects a third party. These side-effects may be beneficial or adverse.</p> <p>Examples for beneficial spill-over effects: Research promotion, cultural institutions, hospitals or public transportation systems which have a supra-regional importance, prevention of water pollution up-stream.</p> <p>Examples for adverse spill-over effects: air or water pollution, economic activities that generate massive transport movements with negative impacts cross local borders.</p> <p>In the cases of beneficial spill-over effects, horizontal collaboration may be required or the allocation of the function at a higher state level. In the case of adverse spill-over effects, mitigation strategies or compensation schemes are needed.</p>
Standard product	Product that can be bought off-the-shelf. It was produced in series and is not customized for the special needs of a customer.
State liability, explicit and implicit	A state liability is established when an organ of the state (the debtor) is obliged, under specific circumstances, to provide funds or other resources to another unit (the creditor). Explicit liabilities are based on legal or contractual arrangements; they become effective if one or more stipulated

	conditions arise. Implicit liabilities do not arise from a legal or contractual arrangement but are recognized after a condition or event is realised; they include risks such as future obligations from social security schemes, solvency of the banking system, uncovered obligations of public enterprises or sub-national governments, humanitarian aid and reconstruction after natural disasters, etc.
Subsidiarity principle	Functions are allocated towards the level closest to the citizens; a higher state level takes over responsibility for a function if and in so far the objectives of the function cannot be sufficiently achieved by the lower state level.
Synergy potential	If the combined power or a result of a group (of things) is greater when they are working together than the total power achieved by each working separately, then there is a synergy potential. This can also lead to a cost reduction.
Technical compatibility	In order to use different machines, hardware and software etc. together, they have to match with respect to technical features. For example: different software used by different government offices should be able to read and edit the same documents. Data exchange between different types of systems is enabled even without sophisticated interfaces.
Uniform service delivery	Public goods and services are delivered to the people in the same way countrywide.
Vertical collaboration function	= synonym for shared function
Working conditions	Characteristics at the workplace, such as working time (hours of work, rest periods, and work schedules), remuneration, health and safety provisions, social protection, as well as the physical conditions and mental demand (e.g. cognitive complexity) at work