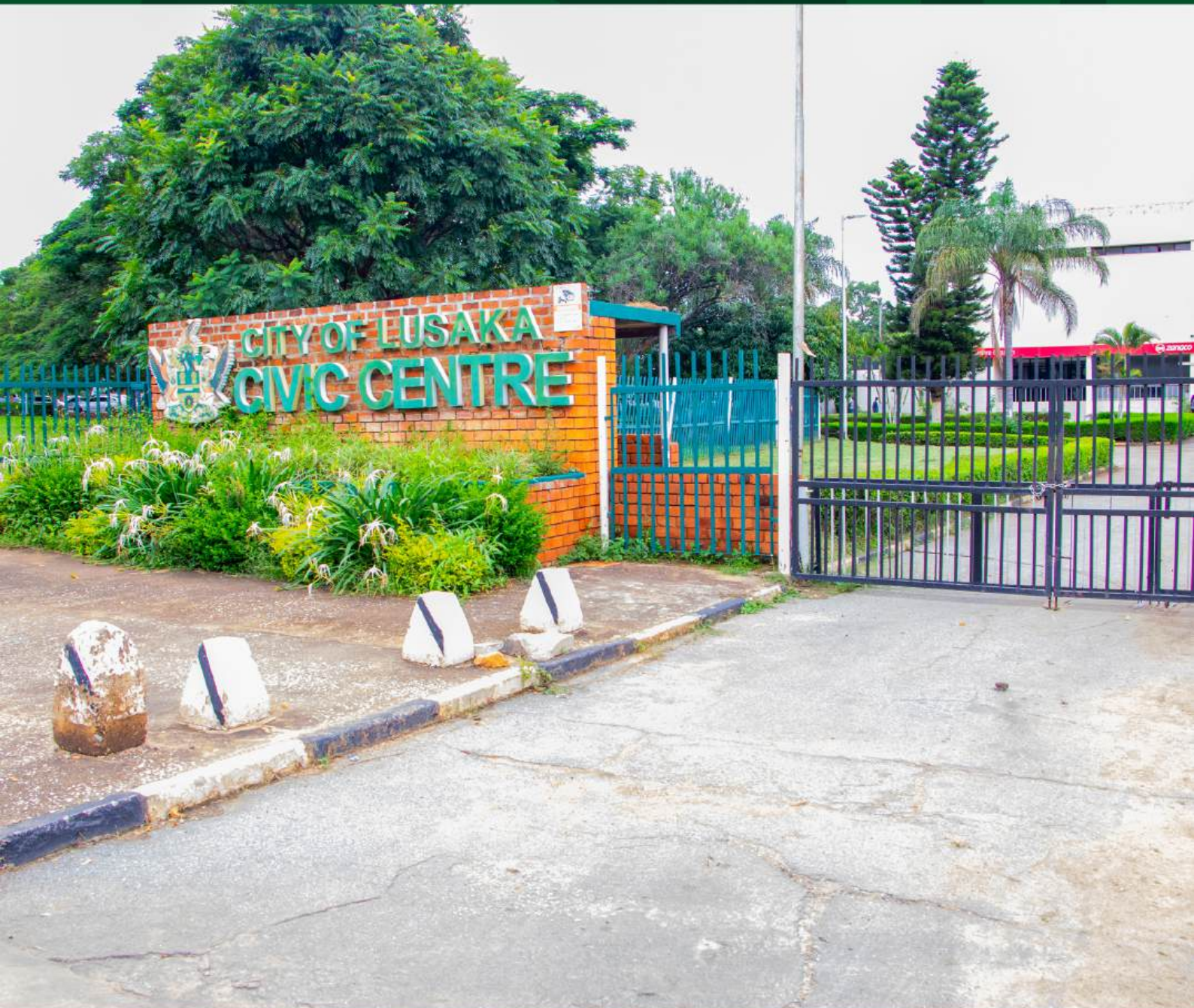




AN ANALYSIS OF LOCAL AUTHORITIES' DEBT AND ARREARS IN ZAMBIA

ACKNOWLEDGMENTS

This report was prepared by Mbewe Kalikeka, Sydney Sihubwa, Liana Chikwekwe, Jones Bowa, Muchimba Sarah Siamachoka and Mwelwa Banda. Special appreciation is extended to the teams from the Ministry of Finance and National Planning (Desmond Banda, Kennedy Nkhoma, Trevor Mwaba, and Joel Phiri), the Ministry of Local Government and Rural Development (Chazya Musukuma, Andrew Mwiinga, and Ackim Machila), UNICEF (Miselo Bwalya, Mervis Pepino, and Margret Louise Irving), and GIZ (James Kema) for their valuable contributions.

EXECUTIVE SUMMARY

This report examines the accumulation of debt and arrears for all 116 Local Authorities in Zambia, analysing key factors contributing to their financial strain and evaluating policy interventions aimed at enhancing fiscal sustainability. The study covers the period 2022–2023, drawing on primary data from key informant interviews and secondary data from audited financial reports.

Over time, Local Authorities have faced increasing financial pressures, driven by historical policy shifts, reduced revenue bases, and rising expenditure needs. Decentralization efforts have not been fully implemented, leaving Local Authorities dependent on transfers from Central Government while struggling to generate adequate own-source revenue (OSR). The debt burden among Local Authorities has risen significantly, with total outstanding liabilities reaching K4.6 billion as of September 2023 — a 67.9% increase from June 2020. The largest portion of this debt stems from pension arrears owed to statutory bodies such as the National Pension Scheme Authority (NAPSA) and the Local Authorities Superannuation Fund (LASF), as well as unpaid taxes and penalties owed to the Zambia Revenue Authority (ZRA).

Several structural factors contribute to debt accumulation, including weak internal revenue mobilisation, delays in government disbursements, inefficient financial management, and staff transfers that shift financial obligations between councils. Additionally, penalties for non-payment of statutory contributions have exacerbated the problem, particularly in Lusaka and Copperbelt provinces, where debt levels are highest. The debt-to-revenue ratio for Local Authorities remains unsustainable, standing at 194.3% in 2023 — indicating that liabilities exceed revenue generation capacity by more than double.

Children are significant stakeholders in national debt management, especially in Zambia. Debt impacts local authorities' ability to deliver essential services under the decentralization agenda. Reduced access to quality education, health services, and social protection are direct impacts of public debt. When debt repayments span decades, children lose critical services during childhood and inherit the responsibility of repaying today's debts. The LADA report shows that the total debt at the local level stood at K4.5 billion, which is more than six times the 2025 Early Childhood Education Budget. This discrepancy highlights the crowding-out effect of debt on social spending, undermining children's rights to essential services.

In response, Government has introduced several measures to improve financial management and reduce debt. The Local Authorities Debt and Arrears Monitoring Mechanism (LADAMM) aims to enhance debt tracking and accountability, while the deduction of debt service payments at the source from the Local Government Equalisation Fund (LGEF) seeks to prevent further arrears accumulation. Local Authorities have also transitioned to Output-Based Budgeting (OBB) to improve financial planning and expenditure control. However, implementation challenges persist, particularly in integrating fiscal reporting across all Local Authorities.

To enhance financial sustainability and improve debt management, the following policy recommendations are proposed:

1. Local Authorities should adopt approaches that are customized to the unique features of each locality.

- Conduct Development Finance Assessments (DFA) to map all revenue sources within each Local Authority;
- Implement Integrated Financing Frameworks (IFF) to improve property valuation and tax collection in urban areas;
- Expand alternative revenue sources, such as community-based levies and natural resource taxation in rural councils.

2. Automate Revenue Collection

- Introduce digital systems to streamline tax collection, reduce leakages, and improve financial reporting.

3. Enhance Transparency and Accountability

- Implement a monthly fiscal reporting framework to improve financial oversight; and
- Introduce legal provisions requiring Local Authorities to standardize and publish debt and arrears reports in a timely manner.

4. Implement Debt Swap Initiatives with Statutory Bodies

- Conduct a thorough analysis to explore debt swap opportunities with ZRA, NAPSA, and other statutory bodies; and
- Enable Local Authorities to collect revenue on behalf of the Central Government in high-informality areas to offset debts.

5. Align Staff Transfers with Financial Capacity

- Ensure staff transfers do not impose additional financial strain on Local Authorities; and
- Establish a policy framework to assess the budgetary implications of staff transfers before approval.

In conclusion Local Authority debt remains a serious challenge to Zambia's decentralisation agenda and the effective delivery of public services. The findings of this report indicate that while some progress has been made in managing debt, significant fiscal risks persist. Addressing these challenges will require a multi-faceted approach that combines enhanced revenue mobilisation, stronger debt management frameworks, and improved financial transparency. The implementation of the proposed recommendations will be crucial in ensuring that Local Authorities can sustainably finance service delivery and contribute to Zambia's overall economic development.

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1.1. BACKGROUND

This report examines the debt and arrears accumulated by Local Authorities in Zambia. Firstly, the report analyzes changes in the governance framework for Local Authorities. Secondly, it examines the overall debt stock and outstanding financial obligations. Thirdly, it explores the key factors driving debt and arrears accumulation during 2022–2023, identifying structural and operational challenges contributing to the financial burden on local governments. Fourthly, the report highlights key interventions by the Central Government aimed at ensuring the financial sustainability of Local Authorities. Finally, it highlights the implications of these financial constraints on service delivery and fiscal sustainability, offering insights into potential policy interventions to enhance debt management and improve financial stability within Zambia’s local governance framework.

The methodological approach for this study combines both primary and secondary data collection methods to ensure a comprehensive analysis of Local Authorities debt and arrears in Zambia. Primary data was gathered through key informant interviews (KIIs) with officials from selected Local Authorities, the Ministry of Finance and National Planning (MoFNP), the Ministry of Local Government and Rural Development (MLGRD), and key Cooperating Partners (CPs). These interviews provided firsthand insights into the causes, challenges, and potential policy responses related to debt accumulation and arrears management. In addition to primary data collection, the study also conducted an extensive desk review of relevant policy documents, financial reports, government publications, and previous studies. This mixed-methods approach enabled a deeper understanding of the structural and operational factors influencing local government debt, while also allowing for cross-validation of information obtained from different sources.

The analysis is based on data obtained from the Central Government for the period 2022–2023, specifically from the MoFNP and the MLGRD. This two-year period was selected as the focus of the study due to data unavailability and inconsistencies in previous years, as earlier records were fragmented, unverified, and lacked comprehensive audits. However, beginning in 2022, Local Authorities’ financial data has improved having undergone auditing by the Office of the Accountant General (OAG), ensuring greater accuracy and reliability. This audited data forms the basis of the analysis, providing a more credible assessment of Local Authorities’ debt and arrears during the study period.



THE ROLE OF CHILDREN IN DEBT AND DECENTRALIZATION: WHY THE LADA REPORT MATTERS FOR CHILDREN

Debt may seem distant to children, but they are significant stakeholders in national debt management, especially in Zambia. Debt impacts local authorities' ability to deliver essential services under the decentralization agenda. The Local Authority Debt Analysis (LADA) report highlights how local debt affects service delivery, particularly for children and their families. Children are silent stakeholders in public debt discussions. They don't participate in borrowing decisions but bear long-term consequences. Reduced access to quality education, health services, and social protection are direct impacts of public debt. When debt repayments span decades, children lose critical services during childhood and inherit the responsibility of repaying today's debts. Globally, 3.3 billion people live in countries that spend more on interest repayments than on health and education combined. The LADA report shows that the total debt at the local level stood at K4.5 billion, which is more than six times the 2025 Early Childhood Education Budget. This discrepancy highlights the crowding-out effect of debt on social spending, undermining children's rights to essential services.

As Zambia advances its decentralization agenda, local authorities are increasingly responsible for services like education, health, and social protection. However, local governments burdened by debt struggle to provide these services. The LADA report shows that local debt, accumulated through arrears and financial mismanagement, restricts funding for key services benefiting children

In Zambia, local authority debt impacts sectors crucial to children's well-being. Lack of funding for schools, understaffed healthcare clinics, and insufficient resources for child protection services are direct consequences of debt. UNICEF's stance on public debt management is rooted in its commitment to children. As the most vulnerable group, children must be prioritized in borrowing and debt repayment decisions. Transparency and accountability in debt agreements are crucial to monitor effects on essential social services. By advocating for public access to debt management information, UNICEF can protect children's interests

UNICEF can also push for policy changes prioritizing social spending, especially at decentralized levels. With debt growing rapidly in developing countries, including many in Africa, action is needed now. Ensuring debt management frameworks consider children's needs is critical for their present well-being and future stability

The LADA report is crucial for understanding debt's impact on local authorities and their capacity to deliver social services. For UNICEF, it represents an opportunity to advocate for children as central stakeholders in debt discussions, particularly at the local level. By supporting improved local governance and debt management, UNICEF can help ensure children's rights to education, health, and social protection are not compromised by financial constraints

CHARTING OUT THE HISTORICAL EVOLUTION OF LOCAL GOVERNMENT STRUCTURES

Since gaining independence in 1964, Zambia has made ongoing efforts toward decentralisation, aiming to transfer powers and responsibilities from the Central Government to Local Authorities. In 1972, the Government declared Zambia a one-party state forming the supremacy of the ruling party over the Government, resulting in the erosion of financial bases of Local Authorities. The Government withdrew the housing grant, health grant and fire grant, among others, in 1973, which were key revenue sources for Local Authorities. The 1974 Rent (Amendment) Act restricted councils from evicting defaulting tenants (until after accruing arrears in excess of three months). In addition, the Government transferred electricity distribution from local councils to the Zambia Electricity Supply Corporation (ZESCO), without transferring the liabilities that were related to those services thereby increasing the stock of debt and arrears. These reforms meant that between 1980 and 1990, the ruling party and Government functions were merged creating additional offices in councils without corresponding financing. Furthermore, some Central Government functions were transferred to Local Government equally without finances following these functions. These functions included registration of villages, construction of feeder roads, and water supply schemes.

Following the change of Government in 1991, various Central Government policies and pieces of legislation were passed that either reduced the revenue bases of councils or imposed additional expenditure on councils. These included: the complete withdrawal of Government grants to councils declared in the 1992 National Budget; the transfer of motor vehicle licensing functions from councils to the Road Traffic Commission (RTC) while leaving the responsibility to maintain the roads with the council; the 1996 Presidential directive ordered the sale of council and parastatal housing units to sitting tenants at below market prices thereby wiping out rental income from the council revenue bases; the Rating Act No. 12 of 1997 which increased the categories of properties exempt from paying rates (which was later reversed in 1999, however, councils had already lost substantial income); water supply & sanitation undertakings were transferred from councils to commercial utilities, without the offsetting transfer of related liabilities; and finally the granting of backdated 50% salary increments to unionised council employees just before the 2001 elections without providing the required financial resources to cover those increments.¹

2001 marked the beginning of Government providing a fresh drive to the decentralisation agenda. The Government devised the National Decentralisation Policy in 2002 resulting in the set-up of the Decentralisation Secretariat. In 2010, the Local Government Service Commission, with oversight from the Ministry of Local Government, was re-established to enhance human resource management for councils. But the decentralisation policy largely remained unimplemented. The Government then rebooted the decentralisation agenda in 2011. Some key notable changes included the establishment of the Local Government Equalisation Fund (LGEF) in 2014, which was meant to provide financial stability in Local Authorities. The Government then issued Cabinet Circular No.10 of December 2014, which provided clear timelines on the implementation of the selected devolved functions from Central Government to the Local Governments, over a three-year period beginning 1st January 2015.²

¹ B.C. Chikulo (2014) Decentralization Reforms in Zambia 1991-2010, Journal of Social Sciences, 40:1, 95-105,

² <https://www.lgazambia.org.zm/hub/resources/cabinet-office-circular-no-10-of-20141>

In 2016, the Government amended the Constitution, which legitimised the political, administrative, as well as the fiscal decentralisation institutions. The Constitution lists the concurrent and exclusive functions of the different levels of governance. However, significant milestones were not achieved in the decades immediately following independence. In 2003 for example, the Government established the Decentralisation Secretariat under Cabinet Office to coordinate and harmonise decentralisation reforms. Despite this, meaningful progress was delayed until 2011 when the Government re-engaged in national dialogue, culminating in the launch of a revised Decentralisation Policy in 2013. The 2016 constitutional amendment reinforced the need for devolution, emphasising on the transfer of functions from central to local governments to promote development. For instance, the amended constitution in Article 147, prescribes a system of devolved governance in which the management and administration of political, social, legal, and economic affairs shall be devolved to local government level. In Article 148 of the Constitution, it stated that local governance shall be undertaken through sub-structures while Article 150 further stipulates that there shall be provincial administration.

Government increased the allocation towards the Constituency Development Fund (CDF), a significant step towards decentralisation. In 2022, the Government gave new life into the decentralisation agenda by significantly increasing the allocation to the Constituency Development Fund (CDF), which jumped from K1.6 million per constituency in 2021 to K25.6 million per constituency in 2022. Though not explicitly used to support the operations of the Local Authorities, the increase in the CDF was meant to bring development closer to the people. This decentralisation agenda was further complimented in 2023 with the launch of the Revised National Decentralisation Policy, reaffirming the Government's intention to bring development closer to the grassroots.

Over time, the significant changes have eroded the revenue base of Local Authorities, while expenditure needs have grown substantially. These challenges have led to mounting debt and the accumulation of arrears for many Local Authorities, despite having a robust legal and institutional framework severely limiting their ability to fund essential services, infrastructure development, and poverty reduction programs. Additionally, without strong or sustaining revenue streams, Local Authorities struggle to maintain fiscal autonomy, leading to delayed or underfunded public projects that negatively impact community welfare and economic growth.³

³ Smoke, P. (2015). Rethinking decentralized governance and local government finance in Africa. *Public Administration and Development*, 35(4), 239-251. This article provides an in-depth examination of the challenges of fiscal decentralization in Africa, focusing on local government finance and revenue-expenditure balance issues.



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The Local Government system in Zambia is built on a comprehensive framework of policies, strategies, key legislation, and institutional frameworks designed to support oversight and management. This section gives an overview of the legal and institutional frameworks that guide the establishment and fiscal management of Local Authorities.

4.1. LEGAL FRAMEWORK

The current legislative framework provides the legal foundation for regulating, managing and promoting financial and debt sustainability for Local Authorities in Zambia. It consists of sector-specific laws and cross-cutting legal Acts and regulations that address thematic areas essential to effective local governance. This framework establishes the basis for fostering transparency, accountability, and fiscal discipline by ensuring compliance with statutory obligations and promoting sustainable financial practices. It also aligns local financial governance with national development goals, enhancing service delivery and contributing to economic growth. Key legislative instruments supporting this framework include the Constitution (Amendment) Act No. 2 of 2016, the Local Government Act No. 2 of 2019, the National Pension Scheme Act No. 1 of 2023, the Income Tax Act No 3 of 1997, and the Public Financial Management Act No. 1 of 2018, among many others.

The Constitution (Amendment) Act No. 2 of 2016 of the Republic of Zambia. Part XI, Article 151, provides the legal framework for the establishment of Local Authorities and forms the basis for decentralisation. In alignment with the constitution, the Local Government Act No. 2 of 2019 details the operational guidelines for Local Authorities, which are overseen by MLGRD and further empowers them to borrow funds as outlined in Section 48. While Section 50 stipulates Local Authorities can secure loans, issue bonds, or utilise other financial instruments, with all the borrowed funds being charged against the Local Authorities' General Fund. However, borrowing or receiving grants and donations from foreign sources requires prior approval from the Minister in charge of Local Government, in accordance with Section 49, to ensure regulatory compliance.

Article 189 (1) of the Constitution (Amendment) Act No.2 of 2016 specifies the conditions under which a pension benefit shall be paid. Failure to comply with this provision requires the individual to remain on the payroll and continue receiving their last salary until the pension benefit is fully disbursed. This requirement has significantly contributed to the accumulation of salary arrears by Local Authorities resulting from the failure in compliance. This has resulted in the obligation to retain retirees on the payroll due to delayed pension payments which has imposed a substantial financial burden on Local Authorities, further hindering their capacity to meet other critical financial obligations, such as ensuring the timely payment of salaries to active employees.

Pension contributions are mandated under Part IV, Section 14 and 15 of the National Pension Scheme Act No. 1 of 2023. Section 14(1) stipulates that contributing employers must remit contributions to the scheme on a monthly basis, including both the employer's and employee's shares at the prescribed percentage. Section 15(1) specifies that these contributions are due at the end of each month, accompanied by supporting documentation detailing the employee's identity, period of employment, and earnings. Non-compliance with

these provisions carries penalties, as outlined in Section 15(2), where a penalty equal to 20% of the unpaid amount is added for each month or part thereof. This penalty is recoverable as a debt owed to the scheme, further increasing the financial strain on Local Authorities that are already grappling with delayed pension payments and accumulated salary arrears.

The Income Tax Act provides the legal backing for remitting income tax for persons working for Local Authorities. Employers are obligated to deduct and remit Pay-As-You-Earn (PAYE) taxes from employees' taxable income to the Zambia Revenue Authority (ZRA) by specified due dates. Failure to remit on-time attracts penalties, including interest on overdue payments (Section 78A), general penalties (Section 98), and potential legal actions, such as asset seizures or recovery proceedings (Sections 79A-79C). Additionally, unpaid PAYE takes priority during employer insolvency (Section 73), ensuring tax obligations are met before other debts.

Further, there are a number of pieces of legislation that govern Local Government borrowing and arrears. The Public Finance Management Act (2018), through Section 26(1), regulates local authority borrowing under strict oversight to ensure financial accountability and oversight is provided by MOFNP. Other relevant laws include the Employment Code Act No. 3 of 2019 and the Public Debt Management Act No. 15 of 2022. These legal provisions establish a clear framework, and non-compliance often leads to the accumulation of debt and arrears.



This section examines the evolution, composition, and key drivers of debt and arrears among Zambia's Local Authorities. It analyses the major liabilities, including pension arrears, statutory obligations, and unpaid salaries, while exploring the factors contributing to debt accumulation, such as weak revenue mobilization, inefficient financial management, and delayed government disbursements. The section also highlights geographic disparities in debt levels and assesses debt sustainability metrics, such as the debt-to-revenue ratio and debt servicing trends. This analysis provides insights into the growing financial strain on Local Authorities and lays the groundwork for policy interventions to enhance fiscal stability.

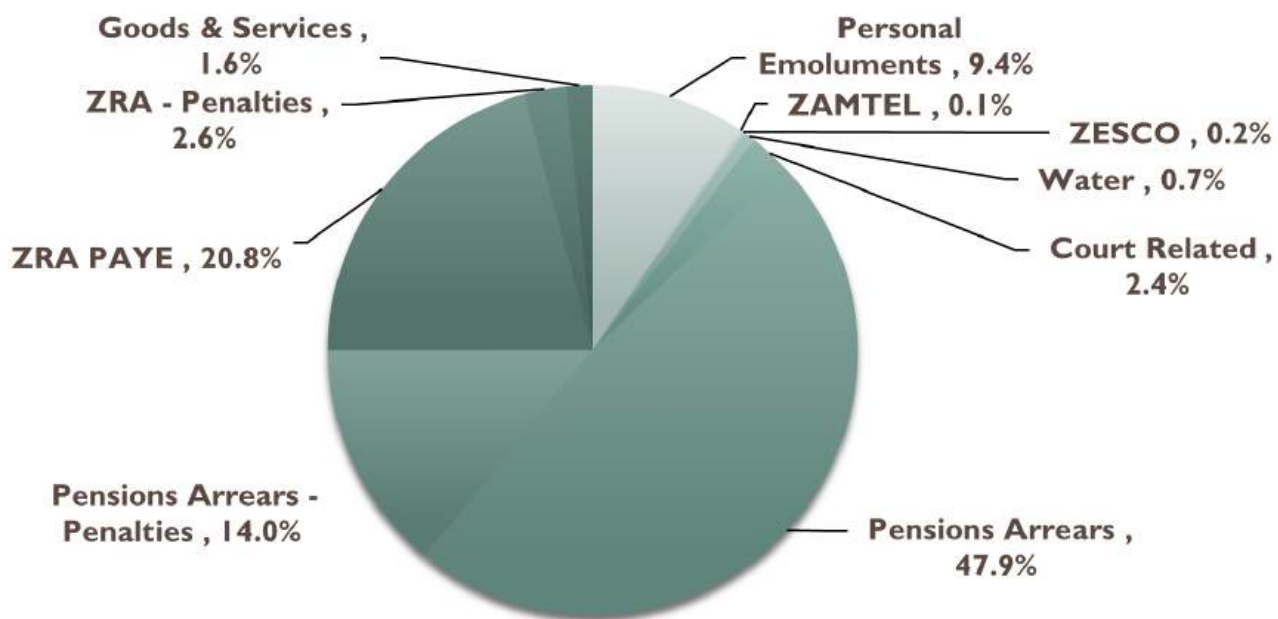
5.1. DEBT COMPOSITION

Over the past years, Local Authorities have faced excessive financial pressure, and this has led an increase in the accumulation of debt and arrears. As at end September 2023, the stock of debt had risen to K4.6 billion from K2.8 billion as at end June 2020, representing a 67.9% increase.⁴ As a share of the economy, this represents approximately 0.86% of Gross Domestic Product (GDP) in 2023. As stated in Section 1, there have been data inconsistencies in previous years, therefore, the study focuses on the period 2022-2023, as prior records were fragmented, unverified, and lacked comprehensive audits.

The largest portion of the debt is owed to pensions. Local Authorities' debt falls into three main categories: statutory obligations, staff-related arrears, and debts for goods and services. The largest share is attributed to statutory obligations, including payments and penalties owed to institutions such as the Zambia Revenue Authority (ZRA), the National Pension Scheme Authority (NAPSA), the Local Authorities Superannuation Fund (LASF), and the National Health Insurance Management Authority (NHIMA). As shown in Figure 1, pensions account for the largest portion at 47.9% (K2.2 billion), affecting employees due to missed contributions and increasing penalties, with NAPSA-related arrears alone making up 14.0% (K645.0 million). Furthermore, Pay-As-You-Earn (PAYE) and its arrears represent 20.8% and 2.6%, respectively. Additionally, arrears to suppliers for unpaid goods and services stand at 1.6%, creating liquidity constraints, disrupting economic activity, and causing cash flow challenges for businesses.⁵

⁴ Ministry of Local Government and Rural Development (MLGRD), 2024. Debt and Arrears Monitoring Mechanism. [pdf] Available at: <https://www.mlgrd.gov.zm/wp-content/uploads/2024/02/Debt-Arrears-Monitoring-Mechanism-FINAL-COPY8-min-1.pdf>

⁵ International Monetary Fund. (2019). Domestic arrears in sub-Saharan Africa: Causes, symptoms, and cures. In Regional Economic Outlook: Sub-Saharan Africa, October 2019 (Chapter 3). International Monetary Fund. <https://www.imf.org/-/media/Files/Publications/REO/AFR/2019/October/English/ch3.aspx>

Figure 1: Composition of Local Authority Debt and Domestic Arrears, September 2023

Source: Ministry of Finance and National Planning

The accumulation of Local Authority debt is historical. The Auditor General's reports covering the period 2015 to 2023 highlights recurring challenges that have contributed to the increase in debt and arrears. Many Local Authorities have struggled to remit pension contributions on time due to cash flow constraints, often resulting from inadequate revenue collection and a heavy reliance on transfers from the Central Government. Since contributions to NAPSA are statutory obligations, delays in remittance lead to increased debt and penalties from the pension authority as outlined in Section 15 (2) of the National Pension Scheme Act.⁶ Similarly, delayed remittances to LASF arise from the late disbursement of funds from the Central Government. Additionally, weak internal controls have contributed to rising tax arrears, as Local Authorities have frequently failed to deduct or remit PAYE taxes from employees' salaries, resulting in arrears with ZRA, which is clearly outlined in Section 71 (3) and (5) of the Income Tax Act.⁷

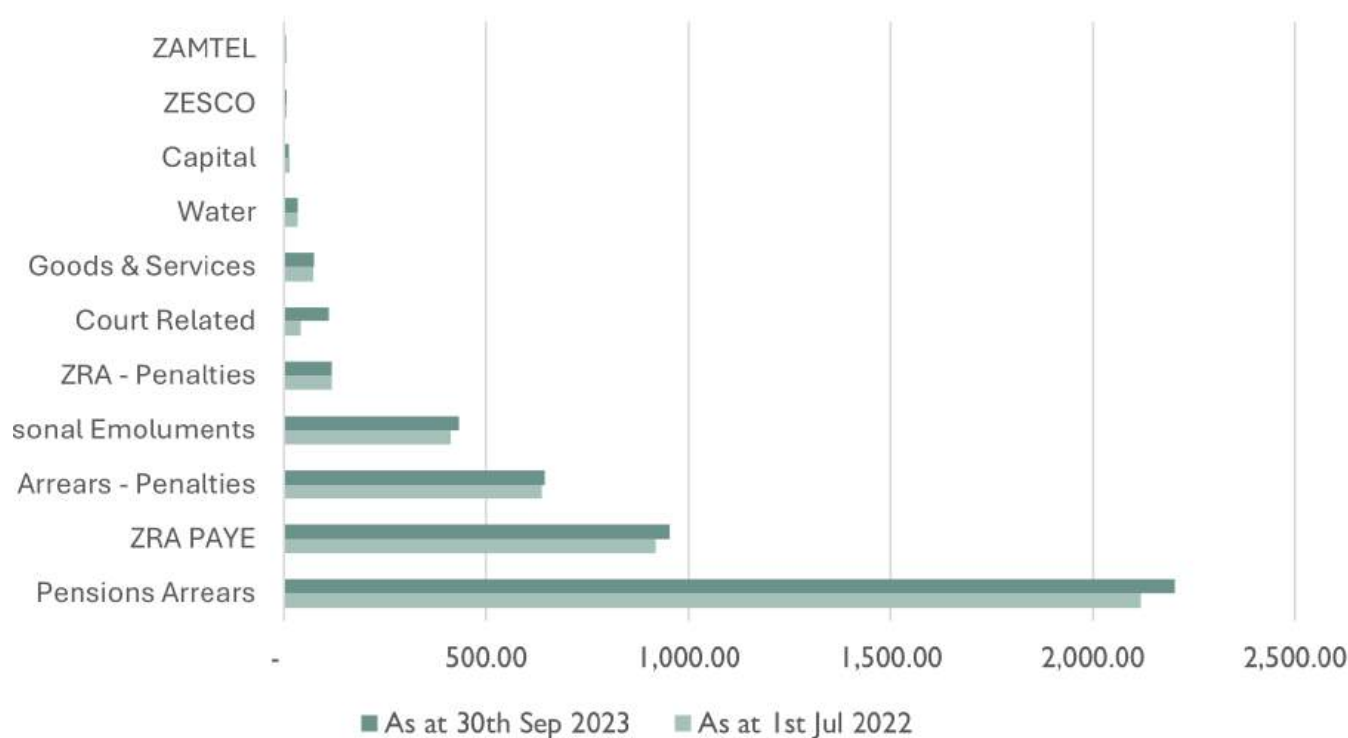
5.2. DRIVERS OF DEBT AND ARREARS

Penalties for non-payment of statutory contributions represent the second-largest component of the debt and arrears portfolio. Local Authorities are under increasing pressure to remit statutory contributions such as pensions and PAYE, leading to the accumulation of penalties imposed by statutory bodies like NAPSA and ZRA in line with the legal framework. Non-compliance penalties for pension contributions have grown from K638.4 million as of 1st July 2022 to K645.0 million as of 30th September 2023. By 30th September 2023, penalties accounted for 29.3% of the pension arrears. Similarly, ZRA PAYE penalties amounted to K117.4 million by the same date in 2023, representing approximately 12.1% of the ZRA PAYE arrears, which are estimated at K954.2 million (Figure 2). As a portion of the total debt, penalties from NAPSA and ZRA represent 16.6% as at September 2023. This is shown in Figure 2 below.

⁶ <https://www.parliament.gov.zm/sites/default/files/documents/acts/National%20Pension%20Scheme%20Act.pdf>

⁷ <https://www.parliament.gov.zm/sites/default/files/documents/acts/Income%20Tax%20Act.pdf>

Figure 2: Comparison of Local Authority Debt and Domestic Arrears, 2022 and 2023



Source: Ministry of Finance and National Planning

Data inconsistencies and discrepancies have significantly pushed the stock of debt and arrears. According to a 2024 NAPSA report, the total estimated outstanding debt on pensions was K6.6 billion with K4.9 billion accounting for penalties on unpaid contributions and K1.0 billion for penalties on paid contributions.⁸ This indicates discrepancies between the figures reported by the Treasury as stated in Section 4.1. and those provided by NAPSA. Key attributed reasons include lack of standardized record-keeping practices due to data inconsistencies, making it difficult to resolve periods with missing returns. Other reasons include poor and unstable internet connection in several local authorities which disrupted their ability to access the eNAPSA platform and other essential online tools to submit data on time. Additionally, Local Authorities face challenges of irregular audits and periodic reviews which has impacted their capacity to identify and address discrepancies which is key in the reconciliation process. However, there have been efforts by NAPSA and Local Authorities to reduce the stock of debt and arrears as explained in Text Box 1 below.

TEXT BOX I: NAPSA Waiver on Penalties

To address the Local Authority arrears owed to NAPSA, the NAPSA penalty waiver was introduced as a key step in alleviating the financial burden of penalties incurred during non-compliance, which resulted from local councils not meeting their contribution obligations on time. The councils were made to calculate their total outstanding liabilities they each owed to NAPSA, to resolve any outstanding debts, reconcile payroll information and improve compliance moving forward. To qualify for the penalty waiver, Local Authorities were expected to capture various issues such as variances on their accounts due to missing or unreported returns. This exercise was carried out in 2024 by NAPSA in a series of workshops where local authorities were grouped in zones to upload and reconcile their returns.

⁸ INAPSA. (2024). Local Authorities Engagement Report on Return Upload, Data Clean Up and Waiver . Lusaka : NAPSA

Provinces with high economic activity and stronger revenue bases hold the largest portion of debt and arrears. As of 30th September 2023, pension arrears in Lusaka Province stood at K1.0 billion, accounting for more than two-thirds of its total debt, estimated at K1.4 billion. Nationally, Lusaka Province represents 22.6% of total debt and arrears, followed by Copperbelt Province at K807.6 million, or 17.6%. Surprisingly, as highlighted above, provinces with higher economic activity and stronger revenue bases, such as Lusaka and Copperbelt, hold the largest shares of debt and arrears compared to less economically active provinces as shown in Table 1. This counterintuitive trend can be attributed to weak internal controls, which undermine financial discipline despite higher revenue potential. Inefficiencies in payroll management, non-compliance with statutory obligations, and revenue leakages weaken the financial health of Local Authorities, making it difficult for them to meet their obligations. For instance, Lusaka City Council failed to deduct NAPSA contributions totalling K3.5 million and PAYE amounting to K17.8 million, leading to penalties for delays. Similarly, in Copperbelt, unpaid NAPSA contributions of K11.6 million on salaries of K233.2 million and delays in pension payments resulted in retirees remaining on payroll and receiving irregular allowances. These issues, combined with inefficient revenue collection systems, have led to a shrinking revenue base, preventing Local Authorities from generating sufficient funds to cover operational expenses.⁹

Table 1: Debt and Arrears Composition by Province, 2023

MPAs	PENSIONS ARREARS	PENSIONS ARREARS - PENALTIES	ZRA PAYE	ZRA - PENALTIES	PERSONAL EMOLUMENTS	OTHER	TOTAL
	K'million	K'million	K'million	K'million	K'million	K'million	K'million
LUSAKA PROVINCE	1,049.754	-	243.621	-	65.786	45.388	1,404.548
CENTRAL PROVINCE	215.863	17.699	210.916	-	63.504	12.351	520.333
COPPERBELT PROVINCE	234.677	122.653	165.244	81.101	69.250	134.684	807.609
N - WESTERN PROVINCE	171.734	0.097	51.154	2.372	35.936	8.231	269.524
WESTERN PROVINCE	32.261	54.329	26.125	1.645	39.002	2.487	155.849
SOUTHERN PROVINCE	130.890	363.575	83.596	28.836	40.169	9.843	656.909
EASTERN PROVINCE	122.865	63.595	68.908	2.195	27.673	11.845	297.082
MUCHINGA PROVINCE	30.400	3.188	23.517	-	26.247	2.519	85.871
LUAPULA PROVINCE	143.774	12.828	29.518	1.235	16.024	8.337	211.716
NORTHERN PROVINCE	69.944	7.049	51.562	-	47.931	10.006	186.492

Source: Ministry of Finance and National Planning

Staff transfers between Local Authorities have significantly contributed to the mounting of debt arising from statutory obligations. In recent years, the Local Government Service Commission (LGSC) has been transferring staff between Local Authorities. However, a key challenge is that transferred staff bring with them accrued debts, including salary arrears and pension liabilities from their previous Local Authority. These liabilities are then passed on to the receiving Local Authority, which often struggles to absorb the additional financial burden due to limited revenue. This problem is particularly prevalent in City and Municipal Councils, especially in the Copperbelt and Lusaka Provinces, where the strain on local finances is most acute.

⁹ <https://www.times.co.zm/?p=133280>

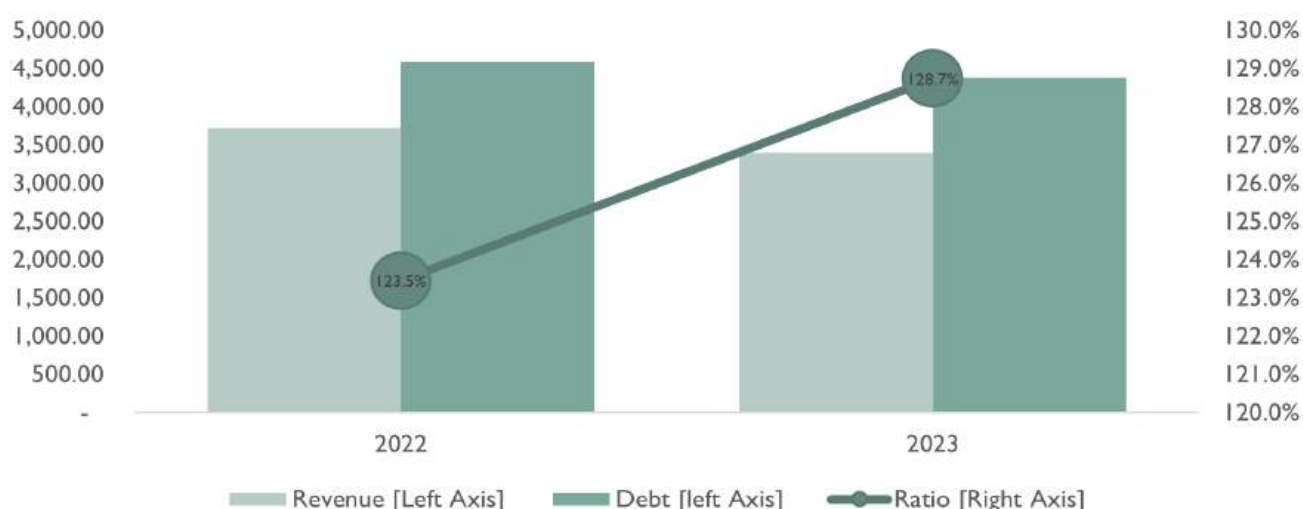
5.3. SUSTAINABILITY OF LOCAL AUTHORITIES' DEBT AND ARREARS

This sub section evaluates the sustainability of Local Authorities using key metrics related to debt and arrears. These include debt and arrears as a share of Own-Source Revenue (OSR), which measures the proportion of liabilities relative to the revenue generated independently by the Local Authority; debt and arrears as a share of the Local Authorities' total resource envelope, assessing the extent to which liabilities consume overall available resources, including external funding; and debt service, which tracks the allocation of resources toward servicing existing debt. Together, these metrics provide a comprehensive view of the financial health and sustainability of Local Authorities.

The ratio of debt and arrears to locally generated revenues reveal a concerning trend, indicating that Local Authorities are increasingly struggling to manage their financial obligations relative to their revenue-generation capacity. Data from 2022 and 2023 reveals that Local Authorities have exceeded acceptable standards for the debt-to-revenue ratio, signalling a serious financial concern. In 2022, the ratio was estimated at 214.3%, decreasing slightly to 194.3% in 2023. Despite this decline, the figures remain alarming. For 2023, this means that total Local Authority debt is 2.14 times the annual OSR, effectively requiring the Local Authority to allocate K2.14 for every K1 generated. This indicates poor financial standing and highlights the urgent need for corrective measures.

The Local Authorities debt-to-revenue ratio (excluding CDF) trend raises significant concerns about debt sustainability. The ratio averaged 126.0% over the 2022–2023 period, underscoring a significant financial burden for local authorities as debt consistently exceeded revenues as shown in Figure 3. Notably, local authorities' revenues include CDF allocations, which are earmarked for specific purposes and cannot be used for operational expenses or debt repayment. Excluding CDF revenues offers a clearer view of financial sustainability. The increase in the ratio over the period highlights the inability to liquidate debt and arrears using available resources. This is despite ongoing financial support from the Central Government through the LGEF.

Figure 3: Debt-to-Revenue (excl. CDF) Ratio, 2022- 2023



Source: Author' Construction from Consolidated Local Authorities Budgets

Local Authorities allocate a small fraction of their budgets to debt service. The 2022 and 2023 consolidated Local Authority budgets revealed allocations of K637.9 million in 2022 and K118.5 million in 2023 toward other expenses, including debt servicing, from total budgets of K7.4 billion and K8.1 billion, respectively. Despite the increase in total debt stock from K2.8 billion in 2022 to K4.3 billion in 2023, debt service costs declined during this period.

ZAMBIA'S NEW BLUEPRINT FOR FINANCIAL SUSTAINABILITY AND LOCAL AUTHORITY DEBT MANAGEMENT

This section examines the ongoing efforts to strengthen the financial position of Local Authorities and address the persistent challenges related to debt and arrears. Key areas of focus include the enhancement of the regulatory framework, a comprehensive review of the policy framework, and improvements to the institutional framework. These measures are part of a broader strategy aimed at fostering fiscal discipline, improving financial management practices, and ensuring the sustainability of Local Authorities. Additionally, other complementary efforts are being explored to address systemic issues and promote long-term financial stability.

After years of facing financial woes, and unsustainable debt, the Central Government introduced the Local Authorities Debt and Arrears Monitoring Mechanism (LADAMM). This was to address the longstanding difficulties in monitoring and tracking of debt and arrears, one of the key factors behind the rapid debt accumulation. With the framework in place, the MOFNP is yet to engage all 116 Local Authorities to build capacity in the use of the LADAMM. With this, data on debt and arrears will be easily captured, monitored and analysed. The framework will further enhance transparency on how debt is increasing and being dismantled by monitoring how Local Authorities are doing on their debt servicing. The analysis of the data will be based on prescribed metrics which are based on the Debt Management Strategy for Local Authorities (2021-2025) by preventing new debt accumulation, addressing existing debt, and guiding future borrowing practices.

To address the growing stock of debt and arrears, the Government has implemented a measure whereby a portion of the LGEF is deducted at source and is channelled to debt service before being transferred to Local Authorities. Central Government began enforcing deductions at source in 2023, particularly for Local Authorities' obligations to the Local Authorities Superannuation Fund (LASF) and other minor liabilities. To enhance financial flexibility, the 2024 National Budget allowed Local Authorities to use 100% of the LGEF for operations, shifting capital project funding to the CDF. However, Local Authorities have raised concerns over the lack of consultation, as deductions managed by MLGRD are often communicated only after being implemented, creating uncertainty and disrupting budget planning. The absence of a clear governance framework further hampers effective financial management.¹⁰

Local Authorities have transitioned and are now implementing a more strategic and performance-based approach to planning and management of Budgets. In efforts to improve accountability and transparency in the budgeting planning process, all 116 Local Authorities have transitioned from Activity-Based Budgeting (ABB) to the more accountable and transparent Output-Based Budgeting (OBB). The OBB allows Local Authorities to align their budgeting processes and templates with the central government systems. However, some Local Authorities have encountered challenges with the OBB due to numerous glitches in the software.

The monitoring of district budgets on a monthly basis through a national standardised system is yet to be fully rolled out. The Government has introduced a Fiscal Reporting Framework for Local Authorities, modelled after the one used at Central Government level, to track monthly revenue and expenditure transactions.

¹⁰ Zambia Institute for Policy Analysis and Research. (2024). Katete Development Finance Assessment . Lusaka : ZIPAR.

This framework requires Local Authorities to submit reports to the MOFNP and the MLGRD, facilitating the monitoring of progress in dismantling debt and arrears. As decentralisation advances and staff are devolved to Local Authorities, the tracking of monthly transactions becomes increasingly critical. However, at the time of writing this report, the fiscal reporting framework was being utilized only by Local Authorities in the Southern and Western provinces of Zambia, with plans for its rollout to other provinces still pending.

Individual Local Authorities have devised and are implementing debt management efforts. The Zambia Institute for Policy Analysis and Research (ZIPAR) conducted Key Informant Interviews (KIIs) with selected Local Authorities to assess strategies for managing debt. For example, Choma Council has set up payment plans with institutions like ZRA and LASF, with payments deducted directly from the Treasury. However, limited resources and growing debt strain efforts to balance salary payments, community services, and debt management. Livingstone City Council is another example that has implemented quarterly reporting mechanisms to track debt and repayments, working with ZRA and NAPSA for monthly payments.



CONCLUSION AND RECOMMENDATIONS

This report provides an analysis of Local Authority debt and arrears, and the legal and institutional framework governing Local Government finance. Since independence, Zambia has faced challenges in decentralising power to Local Authorities, exacerbated by various policy shifts and financial constraints. Despite constitutional amendments and the establishment of mechanisms like the LGEF, Local Authorities have struggled with a widening gap between revenue and expenditure, leading to significant debt accumulation, particularly in pension arrears and taxes owed to statutory bodies. The Government's recent efforts to address these issues include the Local Authorities Debt and Arrears Monitoring Mechanism (LADAMM), which aims to prevent new debt accumulation and manage existing obligations. However, Local Authorities remain under pressure, with limited resources allocated for debt servicing and the need for more robust financial management systems to ensure long-term fiscal sustainability. In light of the above, the report makes the following policy recommendations:

- i. **Local Authorities should adopt approaches that are customized to the unique features of each locality.** Local Authorities must conduct a mapping exercise of all revenue sources within their localities through a Development Finance Assessment. This, with the utilisation of financing frameworks (such as an Integrated Financing Framework), aims to ensure targeted support for property valuation updates and tax system improvements in urban areas, while expanding alternative revenue sources, such as community-based levies and natural resource-based taxation, in rural councils.
- ii. **Use automated systems for revenue collection.** Local Authorities must adopt automated revenue collection processes. By implementing digital systems, Local Governments can reduce manual errors, curb corruption, and eliminate revenue leakages that undermine financial performance.
- iii. **Implement additional measures to improve transparency and accountability of Local Authorities.** Strengthening the reporting standards of Local Authorities through the prompt implementation of monthly fiscal reporting frameworks is essential for public accountability. Additionally, legal provisions should mandate the standardized and timely dissemination of reports on Local Authorities' debt and arrears.
- iv. **Set up initiatives for debt swaps with Statutory bodies.** Conduct a thorough analysis to identify opportunities for Local Authorities to implement debt swaps. For example, in areas with high informality, such as markets, Local Authorities could collect revenue on behalf of the Central Government, addressing ZRA's challenges in taxing the informal sector. Such specialised arrangements, conducted for a fee, could help reduce the debt burden. A notable global example is Brazil, where Local Authorities play a significant role in tax collection. Municipal governments in Brazil are responsible for collecting key taxes, including the Imposto Sobre Serviços (ISS), a tax on services. This tax is levied on service providers within their jurisdictions and is an essential source of revenue for Local Governments.
- v. **Make staff transfers based on the Local Authority budget and their ability to pay.** Staff transfers should be contingent on the financial capacity of the receiving Local Authority to meet inherited obligations. A policy framework is needed to assess budgetary implications before transfers are approved, ensuring that liabilities are adequately planned for or offset by corresponding revenue allocations.

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