

Krystyna PIOTROWSKA-MARCZAK*

THE IMPORTANCE OF GRANTS AND SUBVENTIONS FOR MUNICIPALITY INCOMES

The division of public finance into national and local was originally intended to provide local governments with financial independence and consequently autonomous decision-making. This developed from the belief that it is local government that has all the competencies and meets the requirements of recognising and then meeting daily, elementary needs of the community. To implement this approach, public funds have to be appropriately apportioned. On the other hand, apportionment may result in conflicts arising from the distribution of income from taxes, both in general and other terms. James H. Buchanan wrote „It is the financial conflict that, revealing the necessary existence of ultimate inter-relationship between spending and taxation-related decisions, causes that a concrete solution of this contradiction becomes an essential issue” [Buchanan, 1997, 123].

There can be various approaches to this problem, as there are many ways of achieving a pursued goal which employ different methods and tools.

At the bottom line, however, this choice will have to be made taking into account the pursued fiscal policy being interpreted as „... a selection of public money sources and methods for collecting it, as well as directions and ways of spending public funds to achieve social and economic goals set by relevant public agencies” [Fedorowicz, 1998, 7].

In regard to this approach, it is worth answering the question regarding how the global decentralisation process runs or what its direction is, and how its elements behave in the course of the transition that verify that process in specific time periods.

* Prof. Krystyna Piotrowska-Marczak, Łódź University, Chair of Finance and Banking.

Many analyses assume that transfers of revenue from the central level downwards is a measure of public finance decentralisation, regardless of the number of lower levels functioning in a given country. Another issue is the question of the autonomy of local governments. Redistribution of public funds is presented by proportions of funds controlled by the state and local governments, respectively, but financial autonomy has to be taken into consideration when local funds and other financial sources including grants and subventions are examined. The level of the autonomy of local government cannot be assessed without referring to funds flowing down from central level.

Consequently, it is necessary to quote data that illustrate the degree to which public funds are decentralised.

According to 1987–1996 IMF data, for which information on incomes and expenses is available for at least two local levels in OECD countries, a tendency prevails aiming to „... reduce the degree of centralisation, *i.e.* to increase the share of regional and local funds in public finance. Poland belongs to the group of countries, whose decentralisation of public finances is slightly above the European average, *i.e.* the share of central funds in total public funds is higher. In 1996 the centralisation of revenue dropped significantly compared with the two previous years, *i.e.* from 87% to 85%, and regarding expenses from 83% to 79%” [Polarczyk, 1998]. This is illustrated by Table 1.

The data in the table clearly show that the degree to which public funds are decentralised depends on factors such as the population, level of GDP *per capita* and geographical location.

In countries with the largest populations the share of average central level revenue in public funds is smaller than in less populated countries. This means that the larger country the lower centralisation.

A similar relationship can be observed regarding GDP *per capita*. The higher revenue, the lower its centralisation. The last factor, *i.e.* geographical location, shows the following phenomenon: public revenue is least centralised in Western European countries. Such conclusions also hold true in the case of the degree of centralisation of expenses.

In this context the question as to how public money is transferred from central level down to local levels seems natural. Such transfers are mainly subsidies and grants. Poland belongs to a group of countries with a relatively low share of measurable forms of transferring revenue from central to local levels (8.5%), whereas in Denmark this rate is 36%. However, there are countries such as Croatia where the rate is only 1.2% [Polarczyk, 1998, 17].

Table 1. The average share of revenue at central level as % of total public revenue by groups of countries

Group of countries	112 countries	56 countries	30 countries
Total	89.6	81.0	78.3
<i>Number of population (million):</i>			
to 15	91.6	82.3	79.6
15-60	88.8	83.4	82.3
Over 60	78.8	73.5	67.0
<i>GDP per capita (US\$ thousand):</i>			
to 15	92.1	83.9	80.2
5-15	91.6	82.4	83.3
Over 15	82.2	77.0	75.2
<i>Location:</i>			
Western Europe	83.0	80.2	78.8
Eastern Europe without Poland	82.4	82.4	80.7
Non-European countries	92.2	80.9	73.9
Poland	85.4	85.4	85.4

Source: Polarczyk, 1998, 14.

Table 2. The average share of expenditure at central level as % of total public expenditure by groups of countries

Group of countries	112 countries	56 countries	30 countries
Total	85.2	73.2	69.9
<i>Number of population (million):</i>			
numto 15	88.7	75.8	71.7
15-60	81.6	72.6	71.7
Over 60	72.9	66.5	61.0
<i>GDP per capita (US\$ thousand):</i>			
to 15	88.7	77.3	76.2
5-15	87.9	74.9	74.1
Over 15	74.9	67.8	64.5
<i>Location:</i>			
Western Europe	74.2	69.9	66.7
Eastern Europe without Poland	76.8	76.8	77.0
Non-European countries	89.0	73.7	65.6
Poland	79.3	79.3	79.3

Source: Polarczyk, 1998, 14.

Similar rates characterise expenditure. The ratio of subventions and grants received from the central level by local levels to their expenditure is 33% in Poland, 8% in Croatia, but 90% in Portugal [Polarczyk, 1998, 17].

This illustration provokes the question as to whether transfers of money such as subsidies and grants indicate a growing autonomy of local governments.

It is out of the question that allocation of funds by central level to local levels testifies to the decentralisation of public finance. However, before stating whether this proves a growing autonomy of local governments, verification is needed based on an analysis of the importance of the transfers discussed in the total revenue of particular levels of government. It is crucial to make such an analysis for the period following the administrative reform, that is to say the years 1999–2000.

Table 3 shows that the local income of municipalities (including participation in taxes) amounted to over 18 bn Zł in 2000. The relations above are best illustrated by the structure of revenue (Table 4).

Table 3. Municipality incomes in the year 2000 by category

Specification	Municipalities		
	Total	Rural	Other
Thousand Zloty			
Total incomes	34,583,800	12,719,193	21,864,607
Including:			
Local incomes	18,164,898	5,032,361	13,132,537
Grants	4,749,580	1,973,610	2,835,970
General subvention	11,669,322	5,773,222	5,896,100

Source: Annual report..., 2001.

Characteristically, the data presented show a downward trend of local revenue in total revenue (2.3% in 2000 compared with 1999), whereas a growth can be observed mainly in grants (2.1%) and to some small extent in general subvention (0.2%).

The trends above become even more evident when categories of municipalities are taken into account, with rural areas treated as a separate group. In the latter group of municipalities the share of local revenue in total revenue dropped even more clearly than in the case of all municipalities. More specifically, there is a 2.5% decline in the share of local revenue in rural municipalities (2.3% for all groups) and a 2.6% increase in grants (2.1% for all municipalities). This means that the share

Table 4. Structure of municipal incomes, years 1999–2000, by category

Specification	Municipalities					
	Total		Rural		Other	
	1999	2000	1999	2000	1999	2000
	%					
Total	100.0	100.0	100.0	100.0	100.0	100.0
Incl.:						
Local income	54.8	52.5	42.1	39.6	62.1	60.1
Grants	11.6	13.7	12.4	15.0	11.1	13.0
General subvention	33.6	33.8	45.5	45.4	26.8	26.9

Source: Annual report..., 2001a.

of local revenue is falling and the portion of funds provided by the national budget is on the rise, particularly in rural municipalities. As the latter funds are mostly grants, that is to say earmarked amounts, it would be false to claim that they contribute to enhancing financial autonomy and the resulting freedom of decision-making. This is especially true about rural municipalities. It is also worth adding that in the year 2000 the amount of revenue from participation in income taxes was lower than expected. In relative terms the drop was 9.9%. It should not be forgotten that the year 2000 was the year in which municipalities received a proportion of income tax according to new rules. Between 1st January 1, 1996, and 31st December 1999 coefficients were applied to compensate for the difference between the proportion calculated under the new system and amounts in force until 1995; for particular years the coefficients were: 1996 – 0.10; 1997 – 0.30; 1998 – 0.50; 1999 – 0.75.

Variations in the declining share of local revenue (one of its sources is income tax) in total revenue listed above mean that the adjustments made having not improved the degree of municipal autonomy.

The above facts lead to certain conclusions that can be presented as follows:

1. Generally, there is a global trend to reduce the centralisation of public finance.
2. Poland belongs to a group of countries where public finance is centralised somewhat above the European average.
3. The centralisation of public funds in Poland is being reduced. This concerns expenditure rather than revenue.
4. Subsidies and grants are tools used to decentralise public finance.

5. The share of subventions and grants in the total revenue of Polish municipalities has gone up since 1999, accompanied by a decline in local revenue.

6. The trend to enlarge municipal revenue using grants and subventions concerns rural municipalities rather than other categories.

7. Increased transfers of money from the state budget to municipalities concern grants rather than subventions.

8. In the years 1999–2000 the portion of municipal revenue provided by income taxes dropped.

9. The progressing decentralisation of public finance does not mean a higher financial autonomy of local government, especially municipalities being its basic units.

10. The real financial autonomy of local government will become a fact when there is a higher share of local revenue in total revenue.

Literature

Annual report on the execution of municipal budgets in 2000, Warszawa, Ministry of Finance, 2001.

Annual report on the execution of municipality budgets in 1999 and 2000, Warszawa, GUS, Ministry of Finance, 2001a.

Buchanan, J.M., *Finanse publiczne w warunkach demokracji* (Public finances under democratic conditions), Warszawa, PWN, 1997.

Fedorowicz, Z., *Polityka fiskalna* (Fiscal policy), Poznań, Wyższa Szkoła Bankowa, 1998.

Polarczyk, K., *Centralizacja finansów publicznych, Polska na tle świata i Europy* (Centralisation of public finances – Poland compared to Europe and the rest of the world), Kancelaria Sejmu Biuro Studiów i Ekspertyz, Raport no 137, May 1998.