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EQUALIZATION OF LOCAL BUDGETS IN POLAND  
AND FRG (A COMPARATIVE ANALYSIS)

I

In the local budget system the general principle of balance is binding, which in short means it is necessary to conform expenditure to the planned and realised revenue. The principle is regulated *expressis verbis* by art. 43 of the Act on the System of People's Councils and Local Government of 20th July 1983, which states that „the expenditure voted by People's Councils cannot exceed their revenue”.

The revenue of local budgets comes from various sources. Therefore they have a differentiated character. As a rule each budget has two basic kinds of revenue: own revenue and equalizing revenue. Although they both form one common quota of financial means and eventually are one total source for financing tasks realised by People's Councils, they are different in substance and legal character. The difference is broadly the fact that the own revenue is collected from legally determined sources on own behalf and risk, but the equalizing revenue depends more or less on decisions of superior organs.

There is no need to give reasons to show the preponderance of own revenue over the equalizing revenue, or to present the complex motives which confirm the aim and necessity to eliminate the deficit of budgetary means of People's Councils. Irrespective of recognition of the need for a full financial budgetary autonomy of local governments, and providing them with sufficiently efficient sources of own revenue, there will always be communes in different conditions followed by different financial demand and different possibility of meeting it. At least for these reasons a certain equalizing system seems to be rational.

That is perhaps not the main problem. The matter is not a complete elimination of an equalizing revenue, but a restriction of its variety and size to a necessary minimum, and elimination of elements of arbitrament, luck and rivalry.

The equalizing revenue is often referred to as a balancing or regulating revenue. Also the budgetary legislation often applies different terminology which results in divided interpretation.

The equalizing revenue is not homogeneous in the legal aspect. It includes so-called shares, general grants and purpose grants. Equalization revenue is a legal-financial institution. The equalization system and its particular elements are regulated by legislation. They are changed and altered by the legislator.

In Poland the problem is regulated not by one but by two basic legal acts: by the Act on People's Councils and by the budgetary law. It seems not to be advantageous because, apart from technical reasons, it creates a real danger of confusion and misinterpretation.

Shares as a form of balancing local budgets were already applied in Poland between 1918-1939. Although financial autonomy was assumed, the local budget revenues mostly came from the national taxes surcharge or a certain share in those taxes. Both forms of balancing had their faults as the surcharge was in practice another or additional levy upon taxpayers, in fact increasing the levy, whereas shares in national taxes restricted or even deprived the local budgets of the possibility of using their own revenues.

In the first period after 1945 the pre-war system and structure of local revenue was preserved. Only the shares and surcharge upon national taxes were abolished and replaced by three basic sources of local budget revenue: the land tax, the real property tax and the tax on premises. Apart from those, purpose grants were rather largely applied.

After the 1950 reform of the organs of uniform local state authority, local budgets were still given an equalization revenue. It was provided by the statute which read that „unless People's Councils have a sufficient revenue to meet all needs, the central budget will provide necessary sums to balance the local budgets”.

As the new sources of revenue conferred on People's Councils did not compensate for the decrease in income from the lost sources, and new larger tasks and consequently expenditure were not followed by an increase in own revenue, a need appeared for creation of new or additional sources of equalizing revenue. So beside the existing equalizing grant a share of local budgets in some central budget revenues was introduced, including the turn-over tax on units of nationalised economy, the land tax, the tax on non-agricultural private enterprises, the war excess profit tax, the income of the State Land Fund, and others. As a result of those changes, in 1951 i. e. the first year after the reform, the revenue was made in 48 p. c. of shares, 33 p. c. of grants, and only 19 p. c. from own sources.

Basing upon the above quoted statute of March 1950, the Council of Ministers passed an unpublished resolution of 17th April 1950 concerning the

preliminary directives for designing the national budget for 1950, which introduced an obligatory principle of balancing all local budgets in the form of fixed sums or percentage shares in the central budget revenue, or in the budgets of People's Councils of higher tier and through grants.

The first to a certain degree complex legal act regulating the question of balancing local budgets was the decree of 17th December 1952 concerning the passing and execution of state budget. The decree introduced a duty to design a plan of balancing of local budgets, which had to be an integral part of the state budget. The plan determined the amount of shares in the central budget revenue and grants from that budget for particular voivodship budgets. Similar plans of balancing were elaborated on the voivodship tier for budgets of lower tiers. The principles were later confirmed by resolutions of the Council of Ministers in 1953 and 1954.

Symptomatic for the period which was characterised by a progressive centralization and restriction of financial-budgetary autonomy of People's Councils was the above quoted resolution of the Councils of Ministers of 1954. It obliged e. g. the presidia of People's District Councils to elaborate such directives which determined for each single budget the total sum of expenditure that would be covered by the total sum of revenue, specifying the own revenue, the shares in the central budget revenue from the land tax, and the grants. The directives were the basis for elaborating projects of local budgets.

The solutions introduced in early 1950s were consolidated in 1958 in the Act concerning People's Councils and in the Budgetary Law Act. Two antagonistic tendencies were confronted: the tendency toward a legal regulation of the decentralizing process started after 1956, and on the other hand the willingness to consolidate the centralized character of the state budget with all disadvantageous consequences for the autonomy of local budgets.

The People's Councils Act of 1958 introduced for the first time, existing till today, dual character of shares in the central budget revenue. They have been legally recognised as shares and at the same time as own revenue of People's Councils. Budgetary law approved the existing principle that if the planned expenditure of local budgets cannot be covered from their own revenue, the People's Councils involved will receive equalizing grants from the central budget, or from a territorial budget of a higher tier, in order to balance their budgets. At the same time purpose grants, abolished in early 1950s, were re-established as one of the forms of balancing local budgets. The grants had to be given to finance tasks determined by the National Economic Plan.

The provisions referring to equalizing revenue, regulated in the budgetary law of 1958, were specified in the Act of 1st July 1958 on People's Councils revenue. It included a detailed register of own revenue of village, town and settlement People's Councils. Again shares in the central budget revenue were included, following the People's Councils Act. The amount of shares of

voivodship People's Councils in the central budget (in the turn-over tax upon certain economic subjects) was determined in the annual budgetary act.

The system of local budget revenue, including the equalizing system, shaped in late 1950s, was not substantially changed in subsequent years. It was consolidated in the budgetary law of 25th November 1970. Although it empowered the Council of Ministers to transfer some central budget revenues to local budgets, partly or completely, still it confirmed the known and commonly practised principle that if the own revenue of local budgets is not sufficient to cover their expenditure, shares in the central budget revenue and equalizing grants can be given. Whereas to finance certain tasks People's Councils could be given purpose grants.

Details about kinds and amount of shares in the central budget revenue were in the 1970s determined in the annual budgetary acts. Symptomatic was the budgetary act of 1976 which allocated local budgets (voivodships) with a new source of „own” revenue, in the form of share in the central budget revenue, determined as a percentage of the value of retail sale and services of nationalised commercial and servicing units, covered by central and local plans. The shares were continued in subsequent budgetary acts, and then consolidated in the People's Councils Act and the new budgetary law.

As it has been demonstrated above, shares in the central budget revenues, as well as the equalizing and purpose grants have been known and practised for years. Their advantages and disadvantages have been thoroughly discussed in the literature of the subject. Thus there is no need to present them again. However, an opinion can be expressed that in the face of the fact that it is impossible to provide the People's Councils budgets with sufficient own revenue to secure their full financial autonomy, the existence of a certain equalizing system seems reasonable. As it has already been mentioned above, the problem is not securing the local budgets full self-sufficiency, but rather elaborating a possibly optimal system of balancing, applying objective, clear and stable criteria.

It should be also postulated to delimit clearly shares from actual own revenue of People's Councils. It refers in particular to the above mentioned revenue at a percentage rate (and fixed sums) to the value of retail sale, which has been negatively evaluated in financial literature. E. g. it has been pointed out, not without reason, that it has an ambiguous character (shares in the central budget revenue and at the same time own revenue of local budgets), which makes it difficult to determine clearly their legal and factual character. This inconsequence results from an artificial, substantially and formally incorrect inclusion of shares into the own revenue. No doubt this ambiguous legal construction resulted in an artificial increase of amount and structure of own revenue of People's Councils.

It is also doubtful that the above mentioned „own” revenue in the form of shares in the central budget revenue, in budgetary practice is determined in two forms, i. e. as fixed sums and as a percentage of the expected value of retail sale and services in the given voivodship. It is inconsistent with the People's Councils System Act and with the budgetary law which clearly provide that shares are determined at a percentage rate. It can be only supposed that the shares still serve as a basic equalizing instrument, covering the deficit of voivodship People's Councils arising from the difference between the own revenue and planned financial demand. That is why, it seems, they are determined as fixed sums for each voivodship budget in a definite amount, which results from a centrally elaborated calculation, whereas a particular percentage is a secondary element and simply results from dividing the determined amount of share by the planned amount of sale.

As example is usually set by the superiors, a similar practice is applied by voivodships to the budgets of the basic tier, introducing the so-called subsidizing revenue in the form of fixed sums and a percentage share in the revenue, in relation to the planned amount of retail sale and services in the given voivodship. So they are in fact certain „shares in shares”.

It seems justified to put here a question whether instead of doubtful shares, determined according to at least disputable measures, which is the value of retail sale and services, People's Councils should not be given real shares in definite sources of revenue of the central budget, e. g. in certain taxes, preserving all features characteristic for such shares (preference in case of over-planned realisation or risk in case of not reaching the planned revenue). What speaks in favour of such solution is not only a concern to avoid ambiguous statutory solutions and to have a clear system of subsidizing local budgets, but also the argument of direct involvement of People's Councils in shares of that type, without a need to call them own revenue. Correctly determined shares can act as desired stimulators for local budget economy. However, to let the function give effect, People's Councils must be able to influence directly the realisation of shares given to them in definite taxes.

The problem seems to have been finally noticed by the legislator. It is confirmed by two exemples. The above mentioned People's Councils System Act of 1983 and the following budgetary law of 1984 have introduced a new source of local budget revenue in the form of a part of income (85 p. c.) from the wage tax. It has been also confirmed by the latest amendments. It is something to approve. However, again fiction has won because the revenue from that source has been considered an own revenue of local budgets, although it is simply a share in the central budget revenue, or at least in common taxes, as it is practised in FRG.

The amendments refer also to an extension of sources of People's Councils revenue by a share of 5-10 p. c. of revenue from income tax on state

enterprises, whose founding organ is a chief or central organ of state administration. According to statute the amount of share should be determined for five-year periods, with a division for particular years. It is a fully reasonable solution and postulated for years. Besides it is a practical and relatively effective source of subsidizing, which is or can be influenced by People's Councils, as it refers to economic units situated in their area and active in production or services. Thus it was quite unnecessary to call that influence *expressis verbis* shares and also own revenue.

And finally the last remark. The amended People's Councils System Act provides in art. 47 that shares and grants are determined basing upon objective criteria, fixed according to budgetary law. Whereas the new, amended in 1988, budgetary law transfers the duty to the Council of Ministers. Thus an obvious inconsistency between two legal acts of equal rank appeared. However, the provision is still a dead letter, because neither the budgetary law nor regulations of the Council of Ministers have fixed such criteria.

## II

The problem of financial balancing between budgers of particular territorial corporations (federation, federated states, communes) is also well-known in the Federal Republic of Germany. Although in some aspects similar, the FRG's equalizing system differs from its Polish counterpart, first of all about the fact that it has been given a constitutional rank, which makes it much more stabile. Besides, its characteristic feature is that it is realised mainly by means of taxation instruments and within the taxation system, whose basic assumptions are also regulated by the Constitution of the FRG.

The federal character of the Federal Republic of Germany justifies the necessity of a precise determination along with delimitation of competence of particular territorial corporations, including financial-budgetary and taxation problems. It has been reflected in the Constitution of the FRG which pays much attention to those problems.

The Constitution determines first of all the basic principle of realisation of material tasks according to which each territorial unit covers, on own behalf and in own capacity, the expenditure connected with realisation of its statutory tasks, duties and rights. However, when it also realises commissioned tasks, the expenditure is covered by the orderer.

A constitutional rank has been given to the principle that for particularly important tasks communes can be granted a definite financial aid in the form of grants. The aid can refer e. g. to investment which would eliminate an imbalance and would serve to level the socio-economic standards between particular regions, or help with their development.

The basic principles, procedure and forms of equalizing local budgets is called „communal system of financial equalization”. Its aim is providing communes with means necessary for realisation of their statutory tasks and levelling their financial abilities. The system works in two directions: vertical and horizontal. The vertical equalizing serves a correct division of means between federated states and communes, and the horizontal equalizing is aimed at a proportional division of means between particular communes. The aims of the equalizing system are the same in all federated states.

The local financial-budgetary economy, represented by commune budgets, is regulated not only by the Constitution, but also in relatively numerous legal acts passed both by federal and federated states authorities. The whole of legal provisions regulating the financial-budgetary problems makes the so-called „financial constitution”, which is given great importance. As it is stressed not the constitutional statutes but the legal norms regulating the problems of communal finance are the real basis of autonomy of local organs.

As the system of financial equalization in the FRG is extraordinarily stable and also effective, securing each local unit sufficient financial means, much more attention is given, in practice and in financial literature, to free expenditure of budgetary means than to the sources and structure of revenues. Characteristic is e. g. the opinion of the Scientific Council of the Federal Minister of Finance which stresses that local autonomy provides for a certain competence of decision of communes concerning local financial policy and its autonomous realisation. Still there is no need for giving the communes an unlimited competence. However, the minimum of financial autonomy, in the opinion of the Scientific Council, should be a right of each local government to independent and free spending their financial means. From the material point of view it includes the right to an adequate share for local budgets in the revenue of the Federation and federated states budgets. Thus the financial autonomy of local government organs would exist even when communes were completely incorporated in the federal financial and tax system, or if their full demand for financial means was met exclusively from the budgets of the federated states. If, however, as the opinion formulates it, the financial means were given to the communes in the form of purpose grant, it would mean an obligation to realise the state tasks, for which the means were allocated. However, it would mean a restriction of the scope of competence of local authorities and would have a destructive influence on their autonomy and independence.

Similarly to Poland, the total of budget revenue of communes in the FRG can be divided into own revenue, shares in the revenue of the Federation or federated states budgets and grants, though as it has been mentioned before, from the practical point of view the division is of no decisive importance. The basic source of own revenue is taxes raised by the communes on own behalf

and risk. They are first of all the so-called property tax, which includes the corporation tax and the land tax. Then shares are a part of the revenue from income tax (in the part concerning the wage tax). It is one of the so-called „common taxes”, which according to the constitutional classification refer to the Federation or federated states. A part of the revenue from that tax for a federated state makes a specific equalization fund and is then divided within a financial equalization system among communes in the form of shares. Communes are in general entitled to a share of 15 p. c. in the tax, but the amount due to a particular commune is determined by the federated state using a special key, taking into account e. g. the number of inhabitants and other factors used for the calculation. Thus in practice the share in the tax in particular communes amounts 15-20 p. c.

As it has been mentioned above, shares are the basic part of financial equalization system. The share system has a two-way character, as it means a participation of communes in the national taxes, and on the other hand a participation of the Federation and federal states in the corporation tax, attached by statute to the communes. Thus each commune is obliged to pay a part of revenue from the tax in equal parts to the Federation and federated states, of a total of 15 p. c., i. e. 7.5 p. c. to each of the above territorial corporations.

It cannot be denied that as a result of the two-way division of revenues, from among the taxes meaningful for their budgets, the communes have at their full disposal only the land tax. It is not meaningless for their financial situation, although as already mentioned, the situation is not received as a nuisance, for the equalization system secures a revenue rather sufficient to meet the basic needs, according to the area, population, economic potencial, etc.

The participation of communes in national taxes is treated as one of the methods of financial equalization and a kind of general grant. A contrast is here the purpose grant, which like in Poland, is allocated for strictly definite purposes. The purposes are determined by the Federal and federated states authorities. During the last years the preference included modernisation of roads, improvement of aesthetic look of towns and settlements, protection of environment, etc.

Purpose grants now amount about 18-20 p. c. of the equalization means for local budgets. As they finance as a rule only a certain part of expenditure, communes are obliged to provide the rest of financial means themselves. Such influencing the economic and financial decisions of local governments by means of a system of grants is in the literature of the subject referred to as the policy of „golden hold”.

To sum up, it should be stressed that the advantage of the FRG's equalization system is its stability. That feature results from the fact that its

basic principles have been regulated both by the Constitution and other statutes. Its basic aim and task is to secure each commune the means covering the difference between the real demand and own financial ability, to a degree meeting a certain minimum of the needs of the population. Still it is not a matter of complete elimination of differences existing between particular communes, due to unequal financial abilities, but only their levelling to an average. As it is stressed here, a complete elimination of differences would not only be in conflict with the idea of autonomy, self-government and self-responsibility of local authorities, but would mean a uniform treatment of matters which naturally are not uniform.

As it has already been mentioned, the financial equalization system is realised mainly through taxes. Its essence is providing local government budgets with a proper share in the Federal or federated states taxes, according to a definite index (key). The index is differentiated and ranges from 15 to 20 p. c. Of the total revenue of federated states budgets a proper part gets divided into shares and equalization grants for the communes.

The amount of share, mostly in the income tax in the part concerning the wage tax, is individually determined for each commune, taking into account the two basic calculation elements, i. e. the number of inhabitants and the average financial demand. The average minimum of expenditure per inhabitant is annually determined by federated states authorities. Thus the share due to each commune is a result of multiplication of the minimum by the number of inhabitants.

Another part of share, in the form of general equalization grant, is determined considering the real financial demand, also calculated according to the number of inhabitants of the commune. The so calculated demand is then compared with the financial ability of the commune, i. e. the amount of own taxation revenue together with shares in the federated states taxes, calculated per inhabitant. If the result of such comparison indicates that the demand exceeds the financial ability of a given commune, the missing means will be given in the form of equalization grant. The demand is as a rule supplemented not to a full amount (e. g. to 70-75 p. c.) to force the communes to develop their own initiative and domestic economy. It is also a feature of the already mentioned policy of golden hold. When the financial ability of the commune equals the calculated financial demand or exceeds it, an equalization grant is not due.

Thus the rules are rather clear. However, in practice calculation of equalization means in the form of shares and grants due to local budgets is relatively complicated and time-consuming, and rather not clear for an average citizen. Here are some details to confirm it.

The financial ability of a commune is determined as a ratio of sums of the calculated for the planned period revenue from own property taxes together

with shares in federates states taxes. The ratio is calculated separately for each of the property taxes, where the planned sum of revenue from the corporation tax is reduced by the part due to be poud to the Federal or federated states budgets.

Similarly time-consuming and complicated is the calculation of the planned financial demand. It is determined by two indexes of reference: the main index and an additional or complementary index. The main index relates to the number of inhabitants in the given commune. To take into consideration the differentiated demand depending on the size of the commune, the number of its inhabitants is multiplied by a so-called conversion index, ranging from 100 to 135 p. c.

The additional index is usually the number of school children, considering the type and size of the school. An additional index can also be, e. g. the total milage of roads in the area of a commune, or another measurable element of calculation, essential for determining the real financial demand.

The sum of the main and additional indexes becomes the total index. It is used to determine the final amount of supplementary means for each commune.

### III

Comparing the Polish and the FRG's equalization systems, both certain similarities and differences can be noticed. The main similarity is first of all the fact that in both countries local governments and their budgets are not fully self-sufficient in the financial aspect. Real demand more or less exceeds the own ability based on own revenue. Therefore in both countries a need exists for a certain system of equalization or supplementary revenue. The forms of realisation of the supplementary revenue are also similar. They are first of all shares and grants, including purpose grants.

There are, however, more differences which make the FRG's system more favourable, although it also seems not to be free from faults. The major difference is the differently understood and realised in practice conception of financial autonomy of commune budget. E. g. in the FRG more attention is paid to an autonomous disposal of budgetary means than to their sources, whereas in Poland own revenue is as a rule treated as a synonym of autonomy, although its real scope is rather limited. The different approach to that extremely important question can be explained by the fact that the Constitution of the FRG secures the local budgets a rather full meeting their basic demand for financial means. It is realised within the framework of a stabile equalization system. As the communes have their revenue secured by statute, its source becomes in this situation a secondary problem.

An additional advantage of the FRG's equalization system is the fact that the supplementary means are determined according to objective criteria, which on one hand secure certain unified minimum of demand, and on the other take into account individual differentiated conditions of each commune.

Not unimportant is also the fact that shares as the basic form of balancing local budgets are connected, differently from the present Polish solution, with definite taxes. So defined shares in definite taxes perform at the same time an important stimulating function, for they encourage local governments to get involved in their realisation, no matter whether it is a Federal, federated state or communal tax.

A complete contrary is the Polish equalization system, which is based on rules too frequently changed. The 1970s and 1980s practice of shares in the central budget revenue, as one of basic forms of supplying local budgets, is little precise and the amounts for particular People's Councils are determined voluntarily and at random, often as a result of some competition and so-called „get-through power”, and not basing upon objective criteria. Besides, the Polish system of realisation of local budgets is too formal, little flexible and restrained with a superfluous number of legal regulations, which make a real autonomy of local organs doubtful.

However, it seems that with all its advantages the FRG's equalization system could not be transplanted to Poland without reservations. Apart from quite uncomparable socio-economic conditions in which the supplying of local budgets is realised, an argument against a complete adaptation of the West German solutions seems to be their complicated internal structure. It is based on numerous elements of calculation in the form of ratios, indexes, etc. which are not clear and their calculation is time-consuming.

These are, however, technical elements and reservations of formal nature and they do not negate the right and correct idea which became the foundation of the system of local budgets and their supplying in the FRG, which is worth following.

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Przedmiotem opracowania jest analiza porównawcza sposobów równoważenia budżetów lokalnych w Polsce i RFN. Za punkt wyjścia do rozważań nad realizacją zasady równowagi budżetowej przyjęta została ustawa z 20 lipca 1983 r. o systemie rad narodowych i samorządu terytorialnego i ustawa prawa budżetowego z 1984 r.

Autor zajmuje się stroną dochodową budżetów terenowych, w tym podziałem dochodów na własne i wyrównawcze, ich wzajemnymi relacjami oraz charakterem prawnym. Poprzedzone jest to rysem historycznym ukazującym, jak problematyka ta była uregulowana we wcześniejszych okresach. W opracowaniu przedstawione zostały także uregulowania prawne dotyczące równoważenia budżetów korporacji terytorialnych (związków, kraje i gminy) w RFN, ze szczególnym uwzględnieniem problematyki źródeł dochodów tych budżetów. Sformułowany w postaci „komunalnego systemu wyrównywania finansowego” zespół zasad, tryb i formy równoważenia budżetów lokalnych w RFN został porównany z systemem równoważenia budżetów lokalnych w Polsce.

Porównując te dwa systemy można dostrzec zarówno pewne podobieństwa, jak i różnice. Głównym podobieństwem jest to, iż w obydwu państwach samorządy lokalne i ich budżety nie są w pełni samowystarczalne pod względem finansowym. Więcej jest jednak różnic, które przemawiają na korzyść RFN-owskiego systemu wyrównawczego. Nie oznacza to jednak, by system ten mógł być bez zastrzeżeń przeniesiony na rodzimy grunt. Pomijając zupełnie nieporównywalne warunki społeczno-gospodarcze, przeciwko wzorowaniu się na rozwiązaniach zachodnioniemieckich przemawia ich wewnętrzna, stosunkowo skomplikowana konstrukcja. Te zastrzeżenia natury formalnej nie przekreślają jednak słuszności i trafności samej idei, jaka legła u podstaw systemu budżetów samorządowych i ich zasilania w RFN, a która zasługuje na naśladowanie.