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BUDGETARY POTENTIAL OF LOCAL GOVERNMENTS IN THE IMPLEMENTATION OF REGIONAL POLICY PRINCIPLES IN LATVIA

The article specifies the principles of regional policy and reveals their main content, the issues of budget sufficiency of local governments are described and the need for result-based budgeting process leveraging is justified in strengthening the budgetary capacity of regional development.

Keywords: budgetary potential; regional policy; result-based budgeting; local government.

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БЮДЖЕТНИЙ ПОТЕНЦІАЛ МІСЦЕВОГО САМОВРЯДУВАННЯ В РЕАЛІЗАЦІЇ ПРИНЦИПІВ РЕГІОНАЛЬНОЇ ПОЛІТИКИ В ЛАТВІЇ

У статті конкретизовано принципи регіональної політики і розкрито їх основний зміст, розглянуто питання бюджетної достатності місцевих органів влади і обґрунтовано необхідність використання можливостей процесу бюджетування, орієнтованого на результат, у зміцненні бюджетного потенціалу регіональному розвитку. Ключові слова: бюджетний потенціал; бюджетування, орієнтоване на результат; місцеве самоврядування; регіональна політика.

Табл. 1. Літ. 14.

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БЮДЖЕТНИЙ ПОТЕНЦИАЛ МЕСТНОГО САМОУПРАВЛЕНИЯ В РЕАЛИЗАЦИИ ПРИНЦИПОВ РЕГИОНАЛЬНОЙ ПОЛИТИКИ В ЛАТВИИ

В статье конкретизированы принципы региональной политики и раскрыто их основное содержание, рассмотрены вопросы бюджетной достаточности местных органов власти и обоснована необходимость использования возможностей процесса бюджетирования, ориентированного на результат, в укреплении бюджетного потенциала регионального развития.

Ключевые слова: бюджетный потенциал; бюджетирование, ориентированное на результат; местное самоуправление; региональная политика.

Problem statement. The European Charter of Local Self-Government outlines the possibilities of a budget system and its capacity to comply with the principle of social justice throughout the state, agility and efficiency in the use of budgetary resources in regulation of social and economic processes within territorial units.

However, in our opinion, the set of measures envisaged by the Latvian legislation on regional development is not free from a number of significant drawbacks. The most evident ones refer to the insufficiently developed theoretical and methodological guidance on both implementation and increased efficiency of state regulation of regional policy, and insufficiently delineated relationships of local governments and their budgets to the formation of financial resources at the regional level.

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The aim of the study is to validate the need for increased social efficiency in the use of budgetary resources of local governments in regional development leveraging the processes of performance-based budgeting.

The principles of the national regional policy. Regions are currently seen as the key level for economic growth and development. A. Scott and M. Storper (2003) point out that "cities and regions act as the essential basis in the overall process of development". Localized territories are the places where a sufficient part of the added value in all the countries is created, with the regional condition, therefore, being crucial for the competitiveness of manufactured goods (Porter, 2001).

In advanced economies this is manifested in numerous programs and research, focused on the analysis of competitiveness of separate territories.

In the traditional understanding, *region* is a sub-system of social and economic systems of a country, its relatively independent part with a completed cycle of reproduction and specific characteristics of socioeconomic processes.

The recognition of the role of spatial factors in economic growth is a relatively new phenomenon in economics. Major factors of territorial development are defined in "the new economic geography" founded by P. Krugman (1991). The so-called "first nature" factors are the availability of natural resources, geographical position etc., they do not depend on people, and the "second nature" factors are distinguished, such as agglomeration effect, human capital, institutionalism, activity of state and society. The more advanced the level of development of a country is, the greater is the impact of the "second nature" factors on regional development. As the experience of the "old" EU member states and other countries proves, the general development policy of state must include the support for regional development and affiliated administrative-territorial formations as an indispensable component serving the basis for economic growth in general (Reshina, 2008).

Currently, most of Central and Eastern Europe hold that managing and preventing the multiplication of regional disproportions undermining economic and social foundations of territorial integrity of the state should be one of the protective functions of any state. Practically in all of these countries the governments, to a greater or lesser extent, implement active regional policy, establish the principles, objectives and long-term priorities for regional development, adopt the strategy for regional development, lend support to backwards regions, which includes direct government grants. Reforms in the area of regional management in Latvia (Law LR, 2002, LV53) started a new structural stage related to strengthening the guiding function of the state and the significance of regional policy determined by the following essential principles in line with the regional development law:

1) the principle of concentration – financing channelled in support of regional development shall be concentrated on specific priority objectives;

2) the principle of programming – regional development support measures shall be implemented on the basis of regional development planning documents developed at the national level, the level of regions, district and territorial local governments, which documents determine the totality of development priorities and support measures;

3) principle of partnership – ensures cooperation between state institutions, international institutions, planning region development councils, local governments, non-governmental organisations and entrepreneurs;

4) the principle of additionality – priorities determined in the state regional policy shall be financed from the state budget with the financial participation of local governments, foreign financial assistance, legal entities and natural persons, including donations; priorities determined at the level of regions, district and territorial local governments shall be financed from the budget of the relevant local governments with financial participation of the state, foreign financial assistance, legal entities and natural persons, including donations; in addition, regional development support financing at various levels shall be mutually supplementary and shall not replace one another;

5) the principle of transparency – the process of regional development planning and decision-making in respect of support measures shall be public, and public shall be informed about the accessibility of regional development planning, support measures and the results already obtained;

6) the principle of subsidiarity – the duties of public authority shall be fulfilled as far as possible by the authority which is closest to a person and can ensure effective fulfilment of duties at a lower level of administration;

7) the principle of sustainability – ensures for the existing and next generations a qualitative environment, balanced economic development, rational use of natural, human and material resources, as well as preservation of natural and cultural heritage.

Local governments' budgets as a constituent of regional development. Viewing political and economic independence of local authorities as an important measure of society democratization, European Charter of Local Self-Government (1985) stipulates that domestic legislation should recognise the right and the capacity of local authorities regulate and manage a substantial share of public affairs under their own responsibility and in the interests of local population. Accordingly, the European Community sees budgetary functions at the local level as the affairs of state. Indeed, any local community, even the smallest one, is a significant element of civil society and is the chief entity for a local government.

Analysing the structure of the local government budget revenue during 2009–2013, we could state that the proportions of tax payments, non-tax payments and grants including specific grants from the fixed state budget for the period under consideration remain almost constant. The planned revenue due to be received in local government budgets in 2013 should amount to 1347.2 mln LVL or 23.7% of the consolidated budget and remain practically the same for the whole period under analysis (Law LR, 2013, LV192, Ministry of Finance: Budget 2013).

The overall share of tax revenues in the total sum of the local governments' budgets fluctuates from 50.9% in 2009 to 61.5% in 2013. At the same time it should be noted that the share of the personal income tax in the entire taxation for the period under consideration approaches or even exceeds 90% (Table 1). In fact, the personal income tax remains the major source of tax revenue which is left in possession of local authorities in the amount of 80%, while the rest of it (20%) goes to the state budget. In Latvia, one of the poorest countries of the European Union, the basic source of local budgeting is tax receipts from the payment for work, which is low compared to the advanced economies of the EU.

In the possession of local administrations are also such budget receipts (with the exception of non-repayable transfers from the state budget and equalization fund) as individual income tax and property tax, including land-value tax and local charges. If

we look at the cadastral values of the taxpayers' property, it will be quite sufficient for the local government budget volumes. However, collection of these taxes fails, because the majority of population do not have money. Poverty is increasing year by year and the reality is that the majority of Latvian population have little opportunity to sneak out of the difficult situation when social and economic conditions turn people from potential taxpayers into permanent applicants for social assistance.

*Table 1. The Structure of Income part of Local Budget, mln LVL
(1 EUR = 0.702804 LVL)*

	2009	2010	2011	2012	2013
	facts			prospects	
1. Income	1334.4	1319.9	1354.4	1369.9	1347.2
1.1. Income taxes	680.1	732.3	768.2	814.0	828.9
% of income tax	50.9	55.5	56.7	59.4	61.5
1.1.1. Resident income tax	599.6	623.3	649.4	697.7	698.3
% of income tax	88.2	85.1	84.5	85.7	87.2
1.1.2. Property tax	73.1	89.7	110.2	116.0	118.7
1.1.3. Natural resources tax	2.4	3.4	4.7	6.7	7.2
1.2. Transfer from other budgets	515.8	470.6	459.7	401.5	392.4
1.3. Income taxes, financial help from other states, personal and other types of income	138.5	117.0	126.5	154.4	125.9

(Law LR, 2013, LV192, Ministry of Finance: Budget 2013).

Alterations made in the process of administrative-territorial and regional reforms to the structural policy of local authorities and optimization of their functions do not allow overcoming the constant shortage of budgetary funds and deep dependence of local budgets on grants and aid, while the tax base, for the above reasons, has become even less stable. Therefore, there is no other way round except keeping grants without curtailing while forming those from the fixed state budget, the share of which in the general structure of the local budgets incomes was 48.9% in 2009 and 38.5% in 2013. More than 79% of all local governments in Latvia actively use interbudget equalization to ensure their survival. For already the second decade poverty seizes more and more administrative-territorial units in the country. No material changes for better are taking place in the life of the people in Latvia, the structural backwardness of its economy persists, the unemployment rate is high as well as the poverty level in depressed regions, there are neither real, nor potential preconditions for territorial-regional development.

As the study shows, the reasons why on different territories incomes vary are manifold: location, the state of the real sector, insufficient capital provision, inadequately developed business infrastructure, low level of general education and professional skills, tragically decreasing number of workforce and young people, in particular, unfavourable economic structure with a big segment of service sector, distributive trade and many other (Reshina, 2008).

Regional potential growth cannot take place without a sustainable basis for capital investments. Meanwhile, the figures for 2009–2013 show the sharp reduction of capital in local government budgets expenditures as compared with the increase of current expenses. Thus, if in 2009 the ratio was accordingly 23.4% and 76.6%, in 2011 it was 22.4% and 77.6%, then in 2013 it was already 20.5% and 79.5% (Ministry of Finance: Budget 2013). Such small proportion of capital investments in the local governments' fixed budget expenditures and the trend towards a greater decline, in practice, results in

continuous growth of expenses for regular renovation of the municipal structure and rendering impossible further territorial development and regional planning.

Result-oriented budgeting. The procedures of budgeting, approval of a budget, and budget execution with local governments should be reoriented from budgetary fund management to result-oriented management (with planning of budgetary allocations based on the outcomes of budget programs implementation and precisely coordinated with the functions of budgetary funds management and establishing clear priorities in expenditure assessed based on realization). Budgetary policy as the entire range of all the decisions taken in the field of local government planning and budgeting with the purpose of overall regional development, in our opinion, should conform to the three-step scheme: local government long-term development – elaboration of a project budget – elaboration and execution of annual budget of local government, including the development budget and current expenses budget. Functioning of such a scheme of budgetary planning with regard to the development-linked expenditures can be based on working out of 3 documents, acquiring the status of normative regulatory documents of a municipal entity: the long-term development plan; project budget; annual development budget.

The above approach broadens the independence and responsibility of the budget planning entities, managing budgetary means, as with that, long-term carry-over allocations with annual adjustment in conformity with the medium-term financial plan are set, long-term development budget for implementation of specific programmes is created, incentives appear for the use of resources (financial, human, material etc.) to be optimized, at the same time internal audit becomes a priority, the responsibility for decision-taking is delegated to lower levels.

Generally speaking, the result-oriented budgeting (ROB) is a system of budget formation and implementation, reflecting the relationship between the budget expenditure planned/implemented and the results expected/achieved. The purpose of such a model is to bring into balance the resources expended and the results thus achieved, to evaluate the economic and social effectiveness of various types of activities financed from the budget.

In many European countries the implementation of the result-oriented budgeting is increasingly becoming one of the most significant institutional changes in the social sector of economy as an alternative to estimates-based budgeting. In the countries having made substantial progress in the process of budgeting, a lot of attention is paid to the congruence among the machinery of government restructuring, requiring special-purpose practices of selection of discrete structure alternatives (DSA) to be developed and maintained in the context of budgeting (Tambovtsev, 2007). It is reasonable to consider the introduction of budget planning and budget apportionment methods in the context of regional development referred to as "New Public Management". The philosophy of "New Public Management" puts an emphasis on sound management, highlights well-defined objectives, external and internal systems of performance evaluation with the responsibility for the results achieved. Relevant management technologies comprise structural organization, reorganization of budgeting, alterations to budgetary policy, adopting the responsibility centers, the approved indicators of efficient performance, concentration of the selected services and functions (Hogue and Moll, 2001).

Literature on result-oriented budgeting pays much attention to the issues of setting up the systems of performance evaluation, and, also to the ways strategic decisions taken concerning the priority detection in budgetary funds allocation are validated against the relevant information (Hogue and Moll, 2001; Robinson, 2005; Schick, 2003). Methods and forms of result-oriented budgeting implementation could be seen as a more efficient alternative to budget estimate, if the risks that budget makers would manipulate information can be minimised, as well as the risks of lowering the efficiency of management both at the level of central administration and at the level of local governments and regional coordination.

Therefore, special support mechanisms should take the key role, allowing removing or substantially reducing the risks involved in budgeting processes, such as (Shastitko, 2007):

- the DSA selection mechanisms;
- the control (enforcement) and incentive mechanisms;
- the mechanisms of settling disputes and adoption "ex post";
- feedback mechanisms.

All of the above mechanisms add up to create the indispensable conditions for ROB efficiency, while the failure to provide those, actually, suggests imitation.

Conclusions. The necessity of regional development, as specified above, implies that the function of control over economic and social processes is increasingly transferred from central authorities to local governments. However, in the present situation of economic uncertainty and unstable financial base local governments budgets, marked contradictions are observed between regional development objectives and the insufficiency of financial resources to meet those.

Statistical data and analytical calculations for the recent period show a downswing of budget investments into fixed capital assets along with inappropriate increase of current expenses; the inability of the own tax basis to maintain budget soundness.

The budgetary policy measures intended primarily to level off budget provision through redistribution of budgetary funds in favour of financially unfounded local governments demonstrate their extremely low efficiency linked to the theory of economic growth incentives for local governments, and, thus the entire region, in general.

Information of resource base budgets of local governments their planning capabilities proportionally to the capacity of the financial sector in the regions are justified, using of income and self-government budgets, budget planning in proportion with financial potential across the sectors in the regions would be justified, while implementing state protection for the policy selected for the post-crisis recovery and subsequent development. For this, it seems necessary to change approaches to budgetary policy formation at the regional level making use of the result-based technologies. The methods of purposeful program planning made use of will ensure that the interrelations between expenditures of self-governments and the expected results are reflected accurately and clearly.

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