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The Financing of Public Tasks Delegated to Local Governments – An Unresolved Systemic Problem

***Abstract.** The paper addresses problems relating to dysfunctions observed in the performance of public tasks delegated to local governments by the state's central authorities. The paper aims, in the first place, to investigate the factors behind these dysfunctions and to suggest recommendations for systemic improvements. In addition, an attempt is made to identify elements that should be taken into account in determining the costs of tasks delegated to local government units. The discussion is based primarily on a review of relevant regulations and a critical reading of topical literature, but also includes practical insights.*

***Keywords:** delegated tasks, devolved responsibilities, local governments, public finance*

Introduction

Under the Constitution of the Republic of Poland, public tasks geared to satisfy the needs of the local population are designated as local government's statutory tasks and are therefore to be performed by a specific local government unit (LGU). However, if need arises on the part of the state's central authorities, LGUs may be mandated, through a parliamentary bill, to perform public tasks other than statutory ones. Methods and procedures for the delegation and performance of such tasks should be laid down by the relevant bill. The absence of specific regulations has been raising disputes between the central government and LGUs, since LGUs may not refuse to perform delegated public tasks but, at the same time,

expect to be provided with commensurate funding to cover the expenses involved in pursuing these. The problem has not yet been adequately addressed and leads to clashes between central and local government bodies. Many of such disputes have to be resolved by courts, which is not only time-consuming but also incurs additional costs for taxpayers.

The main strand of discussion in the paper aims to investigate the factors behind dysfunctions in task delegation to local government units and to suggest recommendations for systemic improvements. Further, the author attempts to identify elements that should be taken into account in determining the costs of tasks delegated to LGUs.

1. Delegated Tasks and Their Funding Schemes

LGUs are responsible for all public affairs with local, supra-local and regional implications that are not expressly assigned by relevant legislation to other government bodies. Unless a law stipulates otherwise, local affairs are handled by municipalities, while supra-local and regional ones are tackled by the other respective levels of local government. Tasks involving the satisfaction of the needs of a local community are considered the LGU's basic, or statutory, responsibilities. A specification of these tasks can be found in laws laying down the rules for the formation and operation of local governments at respective levels: that of municipality (*gmina*), district (*powiat*), and region/province (*voivodeship*). These laws allow the state's central authorities to devolve, under other applicable laws, specific public tasks, such as e.g. the preparation and administration of general elections or referenda, to local governments.

LGUs are intrinsically vested with the execution of public tasks that are not explicitly assigned by the Constitution or parliamentary bills to other public bodies. An LGU will typically have all the responsibilities of local government that are not expressly assigned to other LGUs. Public tasks focused on the needs of a specific local community are designated as an LGU's basic, or statutory, tasks. At the same time, the Constitution of the Republic of Poland allows for parliamentary bills, if deemed necessary for the good of the state, to delegate the performance of public tasks from outside the list of statutory responsibilities to specific local government units. Relevant legislation then specifies how such tasks shall be delegated and executed, at the same time providing LGUs with a share in public revenues commensurate with the tasks devolved. Local government revenues are composed of an LGU's own income alongside open-end and closed-end subsidies from the state budget (or other public sector units). The sources of LGU's income are clearly defined in legislation, primarily by the 2003 Law on Local Govern-

ment Revenues¹ (further referred to as LGU Revenue Law). Importantly enough, any shifts in the powers and responsibilities, and hence in the statutory tasks, of local government units are to be followed by parallel changes in the distribution of public sector revenues.²

Aside from parliamentary bills, public tasks may be delegated to LGUs via agreements with central governmental institutions and agencies or other LGUs [Moll 2012: 213]. In carrying out a delegated task, a given LGU acts on behalf of central government and under its responsibility. This is because a public task that has been delegated to an LGU does not immediately among its statutory responsibilities but it remains a responsibility of central government. Therefore, the rule whereby an LGU shall perform public tasks on its own behalf and bear responsibility for these does not apply.³

Although LGUs themselves have never objected to the need of attending to public tasks devolved from central government, there is a lot of controversy around the funding scheme, notably around the method for determining financial allocations to specific delegated tasks. K. Wójtowicz cogently observes that the greatest threats to the financial stability of LGUs arise from persistent non-compliance with the constitutional rule of adequacy [Wójtowicz 2014: 306]. What makes it even more difficult to abide by the rule of adequacy is the fact that the relevant laws are not very accurate in defining the methods for establishing the funding requirements associated with the performance of public tasks devolved to local government [Kornberger-Sokołowska 2013: 142].

General provisions for the financing of delegated tasks can be found in the LGU Revenue Law. Namely, an LGU that is entrusted with the performance of public tasks devolved from the central government level, or other tasks delegated to it under relevant laws, is entitled to receiving closed-end subsidies that should cover the expenses involved in performing these tasks. What the Law further stipulates is that the amounts of closed-end subsidies granted toward the execution of public tasks devolved from central government or other public tasks delegated under specific laws should be determined by the same method that would be applied in determining similar expenses under the state budgeting process (Art. 49 of Law on Local Government Revenues).⁴

¹ Ustawa z dnia 13 listopada 2003 r. o dochodach jednostek samorządu terytorialnego, Dz.U. nr 203, poz. 1966 [Law of November 13, 2003 on Local Government Revenues, Journal of Laws No. 203, item 1966].

² Konstytucja Rzeczypospolitej Polskiej z dnia 2 kwietnia 1997 r., Dz.U. nr 78, poz. 483 ze zm. [The Constitution of the Republic of Poland of April 2, 1997, Journal of Laws No. 78, item 483 as amended].

³ Wyrok Sądu Najwyższego z dnia 21 listopada 2003 r., sygn. akt II CK 267/02, Legalis [Supreme Court Ruling of November 21, 2003, file ref. no. II CK 267/02, Legalis].

⁴ It should be noted that the state budget procedure hardly provides any useful information on methods for determining financial allocations to similar tasks, as the state budget process operates

Unless another law stipulates otherwise, closed-end subsidies toward public tasks devolved from central government or other public tasks delegated under specific laws are distributed by regional representatives of central government known as governors or *voivodes*, on terms and conditions set forth in relevant regulations. Importantly, subsidies should be made available to LGUs within such time frames as to enable them to complete the delegated tasks to an acceptable standard and in a timely manner. If this condition is not met, an LGU may claim the amount due, plus interest at the default rate applicable to tax arrears, in court. Unless other applicable laws stipulate otherwise, closed-end subsidies toward the performance of public tasks devolved from central government or other public tasks delegated under specific laws are distributed among specific LGUs, at municipality and poviat level, by centrally appointed governors of regions/provinces known as *voivodes* (Art. 49 of Law on Local Government Revenues).

An LGU is to be provided with commensurate funding to ensure that it is capable of completing a specific public task assigned to it. Nevertheless, the terms and conditions on which the funds should be transferred to an LGU are only defined under laws delegating specific tasks or under intra-governmental agreements. As a result, an LGU does not have a say about how such tasks are determined and what amount of funding is allotted to these. In case funds are not available to an LGU in time to enable it to attend to a devolved public task, the LGU is entitled to a penalty payment based on the default interest rate applicable to tax arrears.

It is therefore easy to see that LGUs have hardly any influence on the making of laws that delegate public tasks from the central to the regional (province or district) or local (municipality) level. The only way they can engage in the law-making process is through the consultative body called the Joint Committee of Central and Local Government (*Komisja Wspólna Rządu i Samorządu Terytorialnego*). The Committee is a forum that has been created to enable central government and local government to develop a consensus on vital issues relating to the functioning of local government. It is also where national policies toward local government are discussed and attention can be given to local government matters involving, or falling within the jurisdiction of, the European Union or other international organizations of which Poland is a member state. The Committee is composed of representatives of both central and local government. The central government is represented by the minister for public administration and 11 other members appointed and recalled by the Prime Minister on a recommendation from the minister for public administration. Local governments are represented by appointees of national associations of local government units. Representatives of both sides are proportionately assigned, on appointment by the Committee's plenary assembly,

at a much higher level and, hence, central government bodies are not at all engaged in performing tasks similar to those pursued by LGUs.

to 12 task forces and 3 workgroups whose work is widely supported by domain experts.⁵

2. The Rule of Adequacy in the Costing of Delegated Tasks

In democratic and decentralized European states, the principle of adequacy between the tasks performed by LGUs and the resources available to it is seen as a cornerstone of local government finance [Ostrowska 2014: 59-78]. The European Charter of Local Self-government demands that local authorities be entitled to adequate financial resources of their own that they can use freely at their discretion, and that these financial resources be commensurate with the responsibilities assigned to local government units by the constitution and the law.⁶ This right is also enshrined in Poland's Constitution that guarantees LGUs a share of public income in proportion to their burden of tasks and responsibilities and insists that any modifications to the powers and responsibilities of local government be accompanied by corresponding shifts in the distribution of public income (Art. 167 of the Constitution).

A. Ostrowska notes that, in line with the Constitution, the distribution of income between state (i.e. central government) and local government must be based on a fixed mechanism for dynamic adjustment and compensation rather than on gradual, ad-hoc "devolvement" of the expenses incurred in the performance of public tasks delegated from central to local government. The principle of adequacy also implies that LGU income, both in terms of structure and fiscal efficiency, should correspond to the nature as well as to the expected quality and quantity of public tasks to be carried out.⁷ If so interpreted, the principle would postulate that, whilst LGU revenues should be in proportion to its responsibilities, LGUs are to carry out solely those tasks that are set out explicitly in legislative acts providing for the transfer of specific powers and responsibilities to them, rather than those tasks that local authorities themselves perceive as local and public [Ostrowska 2014: 59-78; Dębowska-Romanowska 2010: 239].

⁵ The work of the Joint Committee is currently regulated by the provisions of the "ustawa z dnia 6 maja 2005 r. o Komisji Wspólnej Rządu i Samorządu Terytorialnego oraz o przedstawicielach Rzeczypospolitej Polskiej w Komitecie Regionów Unii Europejskiej", Dz.U. nr 90, poz. 759 [Law of May 6, 2005 on the Joint Committee of Central and Local Government and on Representatives of the Republic of Poland in the Committee of the Regions of the European Union, Journal of Laws No. 90, item 759].

⁶ Europejska Karta Samorządu Lokalnego z dnia 15 października 1985 r., Dz.U. 1994 nr 124, poz. 607 [The European Charter of Local Self-government of October 15, 1985, Journal of Laws No. 124/1994, item 607].

⁷ Cost vs. output and outcome.

Despite the constitutional guarantee, it is for many years that we have seen the costs of public tasks repeatedly underestimated in delegating responsibilities from central to local government. As a matter of fact, the problem has not been addressed properly until today. LGUs have been reacting differently – by petitioning and appealing on one hand and, ultimately, by filing lawsuits in courts of law on the other. Attention was brought to the unresolved problem by the Polish National Association of Local Government Organizations in its statement of January 26, 2016, underscoring the fact that, over recent years, the state government has continued to impose an increasing burden on local governments while at the same time failing to provide them with adequate funding. The Association argued that, under the Law on Local Government Revenues, an LGU that is obliged to carry out public tasks devolved from central government or delegated under other legislative acts should be provided with closed-end subsidies from the state budget covering the full cost of such tasks. The actual practice is, however, that many LGUs need to earmark a significant part of their own revenues to support the performance of non-statutory duties. Importantly enough, this extra spending is not reported in the Rb-50 form (the one for reporting expenditure relating to the performance of public tasks delegated from central government or devolved under other specific laws), as it is simply not allowed under the current government regulation concerning the preparation and submission of these forms.

The problem seems to be chiefly attributable to the lack of established standards in two key areas:

- quality, concerning the expected outcomes of delegated tasks,
- methodologies for costing a delegated task in terms of its deliverables (output) and their value [NIK 2014].

Although the absence of costing methodology appears to be crucial, one should realize that without quality standards for output and outcome it would be extremely difficult to come up with a universal solution, i.e. one suitable and applicable to all types of LGUs.

The difficulties with costing methodology stem, to a large extent, from a mistaken perception of cost whereby the costs of public tasks devolved from central government are effectively identified with government spending. Insofar as the economic category of cost is known to the public finance sector and used widely in its budget recording and reporting system, it is not found at all within the public task planning and execution process. The reasons for this are manifold. Firstly, it is the so-called cash method that is adhered to in recording government revenues and expenditures. This means that it is the date of payment that matters in recording expenses rather than the actual date on which the underlying event occurred. As a result, reporting on public tasks is based on annual budget entries, and hence

on the related expenditures, instead of on costs incurred (Art. 40 § 2(1) of Law on Public Finance).⁸

It should be emphasized, however, that cost is an economic category that relates to product or service. In the sales process, the cost of each product is linked to the revenue from its sales.

Under the Accounting Law, the cost of a product (service) comprises both costs directly related to the making of this product and a reasonable proportion of indirect costs that are attributable to it (Art. 28 § 3 of Accounting Law).⁹ The broad definition of cost, on the other hand, includes:

a) costs and losses – denoting likely and measurable decreases in economic benefits over a given reporting period, such as a decrease in the value of assets or an increase in the value of liabilities such that will reduce equity or increase its shortage in any manner except through withdrawal of funds by the owners or shareholders.

b) other operating expenses – construed of as expenses related indirectly to the operating activities of a business, such as in particular:

- social (aid) activity,
- sale of fixed assets, capital work in progress, intangible assets as well as of real property and intangible assets that are accounted for as investments,
- expenses involved in the upkeep of real property and intangible assets accounted for as investments, including adjustments to the value of such investments or their conversion to, respectively, fixed assets or intangible assets, provided that their appraisal is based on market value or, otherwise determined, fair value,
- costs arising from the writing-off of time-barred, discharged or unrecoverable debts and receivables, except for non-cost-bearing debt toward the state,
- expenses related to the creation and release of provisions for liabilities, except for provisions associated with financial transactions,
- fixed asset impairment or revaluation write-downs, as well as adjustments to these, except revaluation charges bearing on financial costs,
- costs incurred due to compensation and penalty payments,
- costs related to the transfer or acquisition of assets, including cash, wherever the assets are transferred or acquired at no charge, through donation or otherwise, for use other than to subsidize sale price or to purchase or build capital goods, capital work in progress or intangible assets (Art. 3 Accounting Law).

An important ingredient of any business activity is cost accounting. It is the designation given to the ongoing process of determining the cost of production or

⁸ Ustawa z dnia 27 sierpnia 2009 r. o finansach publicznych, Dz.U. 2013 poz. 885 ze zm., art. 40 ust. 2 pkt 1 [Law of August 27, 2009 on Public Finance, Journal of Laws of 2013, item 885, as amended].

⁹ Ustawa z dnia 29 września 1994 r. o rachunkowości, Dz.U. 2013 poz. 330 ze zm., art. 28 ust. 3 [Accounting Law of September 29, 1994, Journal of Laws of 2013, item 330, as amended].

service activities. It is the cost accounting system that processes information on the value of resources used by the business in running its daily operations. The gathering of data on the costs of business operations is governed by principles allowing for the requirements of specific users of cost accounting information [Nowak et al. 2004: 13-18].

The classical and most common costing system is that of full-cost accounting, as it complies with the requirements of compulsory financial reporting. Full-cost accounting makes it possible to arrange costs by type, grouping them e.g. either by contractor or by product/service. Under this system, the key criterion for cost classification is the possibility to assign costs to products or services that are hence viewed as basic cost drivers. Using this criterion, two basic categories of cost are distinguished [Sobańska 2009: 101-102]:

- direct costs – that can be directly and individually linked to a specific product or service,
- indirect costs – that are perceived as costs shared by a number of different products or services.

A major issue involved in assigning indirect costs to products or services is that of adopting certain factors – auxiliary values representing a sort of technical-economic parameters characterized by real or conventional linkage to the costs that are to be captured for accounting purposes [Sobańska 2009: 101-102; Drury 1998: 37-54].

If the simplest available solution is adopted – that of full-cost accounting – the cost of delegated public tasks should be determined by looking at direct as well as indirect costs. Such a costing model for public tasks delegated from central to local government is shown in Fig. 1.

It should be at the same time stressed that LGUs may not opt out and, with a vast majority of delegated tasks, have to be willing and prepared to carry them out regardless of whether there is demand for a particular public service at the moment or not¹⁰. It seems to be wrong, too, to advocate an approach whereby a universal measure is sought, such as a unit cost or a factor based on the number of full-time hires, that could be applied in costing all public delegated tasks. In most cases, the method will be inappropriate to estimating the cost of a delegated public task, as it will not be able to capture all the costs, particularly indirect ones, involved in carrying it out. Cost estimation based on a linear function depending on the number of activities or the outcomes of such activities is an over-simplistic and inadequate approach, since it is oblivious of the so called fixed costs, incurred in sustaining preparedness to provide public services to an unknown number of customers and hence perform a hardly predictable number of activities, or of in-

¹⁰ This can be illustrated with the example of registry offices: whether or not there are any residents wishing to get married, municipalities may not close down any of these institutions.

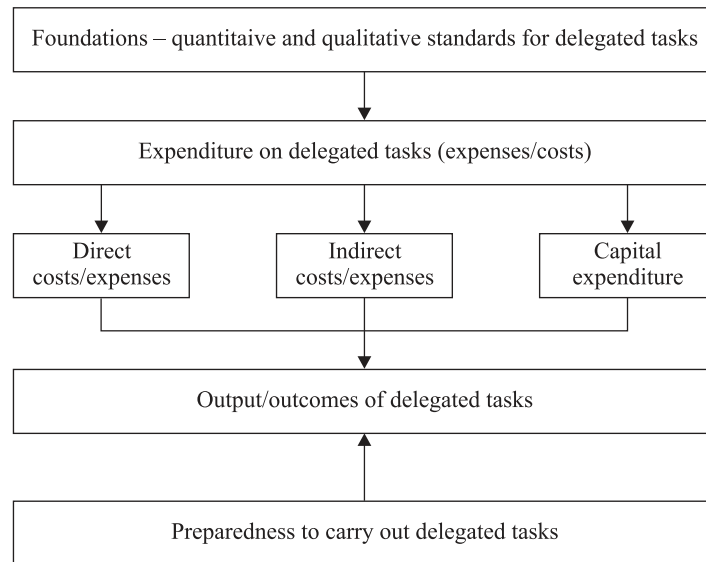


Figure 1. A costing model for delegated public tasks

Source: own elaboration.

direct costs associated with institutional management, financial and accounting services, rent, electricity, office space maintenance and utilities, etc.

Another question that arises is that of capital investments, i.e. when and how much it is reasonable to spend on capital goods. This is directly dependent on the desirable quality of output and outcome to be delivered by a delegated task. Unless output and its qualitative properties are defined, alongside the definition of outcome vis-à-vis social expectations, any estimate of required capital outlay is bound to be characterized by a large margin of error, i.e. the expenditure is going to be considerably overestimated or underestimated.¹¹

Given the above, it seems advisable to take the following steps in order to address the issue of adequate funding for public tasks delegated from central government to LGUs:

- a review of delegated public tasks to verify the rationale for their devolution to local government along with a proportion of local government revenues (share in tax revenues, computation of open-end subsidy, etc.),
- delineating standards for the output and outcome of delegated public tasks to inform estimates of funding required to carry out these tasks (relevant models

¹¹ There is no such approach. If this approach were adopted, it would not matter where and how a citizen is provided with a public service, which means, for example, that a municipality could organize weddings in hallways or wherever in their office space, as this would be a neutral factor in terms of capital investment.

can be derived from the implementation experience with task budgeting in central government institutions),

- determining the costing methodology, where the full-cost accounting method seems to be, arguably, the simplest and therefore best suited to relevant requirements,

- amending the reporting requirements to capture the full cost of delegated tasks, including any necessary capital investment.

Unless these steps are taken, it will be impossible to produce any fair estimate of the costs involved in the performance of delegated public tasks. Nevertheless, considering the fact that the state budget has been running a deficit for a number of years, the government cannot be expected to be ready to make easy concessions. On the contrary, it should be supposed that the awareness of the enormous amounts that need to be diverted to support the performance of delegated tasks will hamper the process of their correct and adequate estimation.

Summary

The processes of delegation and performance of public tasks devolved from central to local government are characterized by a number of dysfunctions in organization and funding. In theory (and in law as well), closed-end subsidies that are awarded to local government units ought to fully cover the costs involved in carrying out these tasks. It is therefore hard to understand why that they do not and why the problem has not yet been addressed by implementing an appropriate costing method and establishing quantitative and qualitative standards for desirable output and outcome, i.e. for what and how should be expected from LGUs carrying out such tasks.

It is high time the deadlock were broken and efforts were initiated to adopt a single methodology for standardizing the quantity and quality requirements for public tasks devolved from central to local government as well as for costing such tasks in a way that will embrace the rule of adequacy. In market settings, a service that is provided at no charge would be unthinkable. Of course, what is at stake with public delegated tasks is not a charge *per se* but mere compensation or reimbursement for the expenses reasonably borne in performing these tasks. In a developed democracy, the fact that LGUs are unable to recover these expenses otherwise than by bringing their claims before the court cannot be regarded as something to be proud of and, obviously enough, brings no benefits to the state and its citizens.

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Finansowanie zadań zleconych jednostkom samorządu terytorialnego – nierozwiązany problem systemowy

Streszczenie. Poruszone w artykule problemy dotyczą dysfunkcyjnych obszarów w zakresie realizacji zadań zleconych jednostkom samorządu terytorialnego z zakresu administracji rządowej. Celem artykułu jest identyfikacja przyczyn tych dysfunkcji. Na podstawie prowadzonych rozważań zaproponowano systemowe zmiany w tym zakresie. Ponadto podjęto próbę identyfikacji tych elementów, które powinny być brane pod uwagę w procesie kalkulacji kosztów realizacji zadań zleconych z zakresu administracji rządowej. Rozważania oparto głównie na analizie rozwiązań prawnych, krytycznej analizie literatury przedmiotu i zakończono je elementami aplikacyjnymi.

Słowa kluczowe: zadania zlecone, jednostki samorządu terytorialnego, finanse publiczne