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**Financing local self-government in Poland in light of the standards of the European  
Local Self-Government Charter**

**Abstract**

An adequate participation of the local government in the state's income is a fundamental value, and it should stabilize the legal status of the local government; however, a system of guarantees must be implemented to ensure that the rule of adequate participation is observed. Such a guarantee function is performed by the European Charter of Local Self-Government that should have a material effect on financial management in Polish local government. Especially, Article 9 of the ECLSG requires that local government units be provided with sufficient funds to complete their tasks and an obligation of the state to provide such funds may be derived from Article 9 paragraph 2 of the ECLSG. However, a problem exists due to the legislature's failure to adopt flexible financing systems ensuring the full implementation of Article 9 of the ECLSG. The objective of this study is to address the question of importance and effect of the European Charter of Local Self-Government for and on financial management of local government after 22 years since the ratification of the Charter.

**Keywords:** government, financial management, sufficiency of income, the European Charter of Local Self-Government.

**JEL CODE:** R58, G28.

**Finansowanie samorządu lokalnego w Polsce w świetle standardów  
Europejskiej Karty Samorządu Lokalnego**

**Abstrakt**

Adekwatność udziału samorządu lokalnego w dochodach państwa jest wartością podstawową i w sytuacji prawnej samorządu lokalnego: powinna stabilizować tę sytuację, wymaga ona jednak przyjęcia systemu gwarancji zapewniających poszanowanie owej adekwatności. Taką funkcję gwarancyjną pełni Europejska Karta Samorządu Lokalnego, która powinna mieć istotny wpływ na gospodarkę finansową samorządu lokalnego w Polsce. Zwłaszcza art. 9 EKSL i (wywiedzione z art. 9 ust. 2 EKSL) odniesienie do państwa obowiązku zapewnienia gminom i powiatom środków finansowych, które pozwalają na realizację zadań. Problemem jednak jest, brak właściwego przyjęcia przez ustawodawcę elastycznych

systemów finansowych, które gwarantowałyby pełne wdrożenie art. 9 EKSL. Opracowanie jest próbą odpowiedzi na pytanie jakie znaczenie dla gospodarki finansowej samorządu lokalnego w Polsce ma Europejska Karta Samorządu Lokalnego po 22 latach od jej ratyfikacji.

**Słowa kluczowe:** samorząd lokalny, gospodarka finansowa, adekwatność dochodów, Europejska Karta Samorządu Lokalnego.

## **Introduction**

The aim of the paper is to compare the standards set by the European Charter of Local Self-Government (ECLSG) in the field of financial management and solutions in the field of financial management of local government in Poland. The subject matter of the article is topical and important because Polish local government has been operating for over 25 years (the first local government elections were held on 27 May 1990) and representatives of local government corporations and delegations of the Congress of Local and Regional Authorities of Europe draw attention increasingly to the incomplete observance in our administrative culture of some articles of the Charter.

Nowadays, decentralisation does not only constitute independence in the sphere of the empire (as understood in the 19th century), because today local government and decentralisation are the basis for independent management of public affairs, first of all in the economic sense, in a network system rather than a hierarchical one, by achieving social and economic benefits on a local or regional scale, by acting for the development of a given local government unit, organising the provision of public services, cooperation and at the same time competing with other local governments, participation in supra-local and supra-regional markets, etc. that instead of territorial capture, cooperation with neighbours should be undertaken in order to carry out tasks on a wider scale. Effective protection of self-government's independence is a development measure, so it should be protected and supported, and not confined to the last century's stigmata. Today, self-government in the world is the most important developed form of public entrepreneurship, it is a kind of company that acts for the benefit of community members (like a commercial law company for the benefit of shareholders), and, like every company, it must have a stable economic, social and territorial potential (Kulesza 2012, pp. 7-24).

Too often local authorities, mayor or council are referred to as self-government. Whereas, self-government is something completely different. According to the European Charter of

Local Self-Government ratified by Poland, local self-government means the right and ability of the local community, within the limits defined by law, to direct and manage the essential part of public affairs with their own responsibility and in the interest of residents. This means that in order for a self-government to exist, the community must be able, and also knowhow and be willing to manage its own affairs. This requires a system that provides appropriate opportunities for this community, as well as civic awareness and the willingness to make the right decisions and take responsibility for them (Regulski LEX 2011, access: 03.10.2016).

Local government is a local community with a democratic internal organisation, which has been structurally and subjectively separated by statute in order to perform the main part of local tasks in the field of public administration with the right to use legal forms of action characteristic for public administration (Kisiel 2003, pp. 17-18).

In accordance with constitutional regulations (Article 167 of the Constitution of the Republic of Poland), local government units shall be provided with a share in public revenue corresponding to the tasks assigned to them. The revenues of local government units are their own revenues and general subsidies and special purpose grants from the state budget. The sources of income of local government units are specified in the Act. Changes in the scope of tasks and competences of local government units take place together with appropriate changes in the distribution of public revenue. It should be noted that the above mentioned regulations result in a particular aspect of the independence of local government units, which can be called financial independence. Within this framework, local government units should contribute to public revenues in accordance with their respective tasks (Zimmermann 2012, p. 189).

More than 40 years ago, professor Harasimowicz pointed out that financial (budgetary) decentralisation is not an independent legal and political phenomenon, but only an instrumental reflection of the principles governing the organisation and functioning of the state (Harasimowicz 1971, p. 132). As emphasized by Professor Kulesza today also, in completely different political conditions, it should be constantly reminded that the public finance system should be a derivative of the principles governing the organization and functioning of the state, and not – as unfortunately, everyday practice shows - vice versa (Kulesza 2012, pp. 7-24).

Our current model of local government generally corresponds to contemporary international standards, especially those expressed in the European Charter of Local Self-Government (ECLSG). Unfortunately, this is not applicable to the sphere of local government

finances, where the principle of territorial self-government units' income adequacy to the tasks assigned to them, as declared in the Constitution and in the ECLSG, is still far from being implemented (Izdebski, Hausner 2013, p. 17).

In view of the above, it was justified to discuss the financial management of local government in Poland in terms of the standards set by the ECLSG and to enrich the existing scientific achievements in this area.

The discussed issue of local government income might seem to be not a doctrinal topic – the doctrine is clear here: own income for own tasks plus a subsidy, and where it is not enough: subsidies for own tasks. The problem is rather that the doctrine does not correspond to reality at all. The most expensive task for the local government is the so-called "running schools". On the financing side, it is defined parametrically (and in a political process, not in an analytical process). On the expenditure side, it is mainly defined in terms of amounts (the salaries of teachers imposed by the state in relation to the work performed). In a word, a full discrepancy between income and expenditure (Izdebski, Hausner 2013, p. 90).

### **The European Charter of Local Self-Government - Principles of Community Financing**

In its Article 3, the European Charter of Local Self-Government defines the concept of local self-government – local self-government means the rights and ability of local communities, within the limits defined by law, to direct and manage the essential part of public affairs on their own responsibility and in the interest of their inhabitants.

The doctrine emphasises that Polish solutions, despite the completely sufficient constitutional and statutory basis, in practice aim at limiting the autonomy of the commune, contrary to the provisions of the aforementioned Article 3(1) of the ECLSG, the „right”, and as a result – the "ability" of local communities to manage their affairs is radically narrowed down. This is done by displacing general legal bases and replacing them with detailed and casuistic solutions, also in those areas where there are no plans of power competences (Kulesza 2009, pp. 7-22).

The ECLSG is characterized as a model of values that shape the essence of „real” local government (Gilowska, Kieres, Sowiński 1993, p. 8).

An important element of this model are the financial principles of local communities set out in Article 9 of the ECLSG according to which. 1:

1. Within the framework of national economic policy, local communities have the right to have sufficient financial resources of their own, which they can freely dispose of in the exercise of their powers.
2. The financial resources of local communities shall be adjusted to the extent of the powers conferred on them by the Constitution or by law.
3. At least part of the financial resources of local communities should come from local fees and taxes, the amount of which these communities are entitled to set, to the extent specified by law.
4. The financial systems on which the resources at the disposal of local communities are based should be sufficiently diversified and flexible to respond as far as possible to real changes in the level of costs associated with the exercise of powers.
5. The protection of local communities that are financially weaker requires compensatory procedures or balancing measures to correct the effects of the unequal distribution of potential sources of income and the expenditure incurred by these communities. Procedures or actions of this kind should not restrict local communities' freedom of decision making within the scope of their own powers.
6. Local communities should be consulted, in an appropriate manner, on the forms in which resources derived from the redistribution of income should be allocated to them.
7. As far as possible, subsidies granted to local communities should not be used to finance specific projects. The granting of subsidies must not jeopardise the basic freedom of the local community to freely conduct its own policy within the limits of the powers conferred on it.
8. In order to finance investment outlays, local communities shall have access to the national capital market, within the limits set by law.

Art. 9 of the ECLSG explicitly grants the primacy of the general subsidy – it calls for limiting the granting of subsidies for the implementation of specific projects. The Charter explicitly states that granting subsidies cannot be used against the fundamental freedom of the self-government community to conduct its own administrative policy. Article 9(8) (access to the capital market) has the same objective of strengthening the independence of local and regional authorities (Lipowicz 1991, pp. 75-83).

The requirement set out in Article 9(2) of the ECLSG to adjust the amount of financial resources of local communities to the scope of competences resulting from the Constitution and legal norms outside the Constitution imposes on state authorities the obligation to provide

local communities with sources of financial resources or directly with financial resources, the amount of which should at least guarantee the implementation of tasks resulting from the legal norms, including above all from the Constitution, competences (Kotulski 2004, p. 123).

The principle of proportionality of the division of public funds to the division of tasks does not allow for the formulation of an unambiguous indication as to the direction of resolving competence disputes, i.e. adjudicating for the benefit of government or self-government administration bodies. However, it points to the need for a thorough analysis of the provisions of law separating public tasks and related competences, so as to correctly „read” the intention of the legislator to delegate the implementation of a given task to the competences of government or self-government administration. This principle also implies the need to take into account the political and, above all, financial context of the division of responsibility for the performance of specific tasks between government administration bodies and self-government units (Niezgoda 2007, p. 27).

Moreover, the Charter negatively assesses the financing of own tasks from the funds transferred to local communities, subject to a specific purpose, which is characteristic of earmarked subsidies. Indication of a specific allocation of funds transferred to local government units for the performance of own tasks or determination of other conditions for their use, since it limits the possibility of conducting one's own policy within the scope of the powers granted to them. On the other hand, deciding on the scope of financing of particular tasks of local government by government administration and the need for municipalities, counties and local government voivodeships to comply with specific conditions of using the granted funds, which would involve the use of targeted subsidies from the state budget as an instrument for financing the self-government's own tasks, enables the government administration to influence the directions and manner of operation of local government units. This creates a situation similar to the situation in which government administration exercises supervision over the implementation of self-government's own tasks according to the purposefulness criterion. Then a process called managing by purse or managing golden cuvettes takes place, which seems incompatible with the independence of self-government (Niezgoda LEX 2012, access: 18.10.2016).

It is also indicated in the literature on the subject that the implementation of the principle of adequacy „(...) should consist in the necessity of an appropriate division of sources of public income between the state and local government (...)” and granting „(...) guarantees that this division will be carried out in accordance with the division of competences”. Adequacy

can be associated with „(...) the need to determine the sources of budgetary income of territorial self-government units at such a level that it is possible to finance the tasks for which these units are constitutionally and statutorily responsible”. (Filipiak 2014, pp. 32-44).

Local government units (territorial self-government units) must have financial resources appropriate to the scale of their public tasks. However, the adequacy principle does not clearly define the nature of revenues transferred to territorial self-government units by the state. As the theory of public finance and the European Charter of Local Self-Government indicate, an important part of them should be own revenue, in relation to which local communities could implement their own tax policy. A significant scope of income autonomy may increase the sense of responsibility for the financial situation of the local government community. Therefore, it is conducive to hardening the budgetary limit of territorial self-government units (Babczuk 2009, pp. 7-16).

The income system of local government units should balance two values which seem to indicate different directions of income formation. On the one hand, this value is the financial independence of self-government units. Local governments should have permanent sources of income (the so-called own income), which will not depend on secondary state interference, but only on the actions and decisions of territorial self-government units themselves (e.g. as to the level of tax rates). Moreover, ideally speaking, it is about the shaping of local government revenues which, regardless of the level of income of other units, will potentially provide income adequate to the tasks (as defined in the Constitution of the Republic of Poland), or even adequate to the scope of authority (as defined by the ESC) (Izdebski, Hausner 2013, p. 89).

### **Structure of local government revenues**

Analysing the discussed issue of revenues of local government (commune, county) from the practical point of view - the actual functioning of local administration and at the same time examining the compliance with the standards resulting from the ESLSG, the structure of revenues of communes and counties in 2013-2016 was presented, indicating the amount of total revenues in individual years (with a division into the amount of own revenues, subsidies and subsidies) and formulating conclusions in the examined area.

**Table 1. Structure of income of boroughs in 2013-2016 (in PLN million)**

Income	2013	2014	2015	2016
Amount of total income	82657,4	86763,4	88851,9	102128,7
Own income	40066,3	42539,9	44112,2	44973,7
Grants	17839,4	19636,3	19322,6	30801,4
Subsidy	24751,7	24587,2	25417,1	26353,6

Note: \* Grants are almost entirely targeted (95%)

Source: own study based on data from the Ministry of Finance.

In the analysed period, the role of own income (in total income) decreased, and the importance of earmarked subsidies increased, which is definitely unfavourable. In 2016, earmarked subsidies accounted for 25% of boroughs' income. The increase in the share of earmarked subsidies in the income structure of boroughs should be assessed negatively. In the case of grants, the control of their use is carried out not only from the point of view of legality, but also from the point of view of purposefulness and reliability. A similarly negative assessment should be made of the decrease in own income in 2016 (less than 50%) in total income. Bearing in mind the above, it is reasonable to state that the standards set out in Article 9 of the ECLSG concerning the appropriate amount of own resources guaranteeing financial independence of local governments or the issue of targeted subsidies are not reflected in the boroughs' financial management.

**Tabela 2. Structure of income of counties in 2013-2016 (in PLN million)**

Income	2013	2014	2015	2016
Amount of total income	23560,3	24195,8	23880,7	24 004,2
Own income	7107,6	7498,5	7954,8	8353,5
Grants	6188,1	6 517,8	5877, 2	5425,3
Subsidy	10264,6	10179,5	10048,7	10225,4

Note: \* Grants are almost entirely targeted subsidies (95%).

Source: Own elaboration based on data from the Ministry of Finance.

When analysing counties' incomes, attention should be paid to the significant share of subsidies in total income. Analyzing the above tables concerning boroughs and counties in the indicated period it is reasonable to state that in the income structure of boroughs over 50% are grants and subsidies, in the income structure of counties grants and subsidies constitute over 85% of total income. It should be emphasized that 85% of subsidies are educational subsidies. What is worse, this educational subsidy is not sufficient for the implementation of tasks in the field of education – boroughs and counties contribute from their own resources.

The analysis of the income structure of communes and counties confirms that the financial management of the local government does not meet the standards expressed in Article 9 of the ECLSG:

- too high percentage of targeted subsidies in the structure of total income,
- too small percentage of own income in the structure of total income (especially visible in the income of counties, which are slowly becoming more governmental than self-government as far as the implementation of tasks and sources of their financing are concerned),
- subsidy (education).

### **Summary**

In the municipal economy, just like in business, there are more and more areas where the business approach is concerned, such as risk assessment, benefit analysis, financial and regulatory engineering, which determines the rationality and effectiveness of a specific investment measure. The policy of central authorities towards local government must take these challenges into account. It is obvious that they cannot be met without legally guaranteed protection of the independence of local government units (Kulesza 2012, pp. 7-24), especially in the area of financial management.

Local government is not only responsible for the implementation of tasks important for local government communities (its own tasks). Their implementation is also important for the state; it is in the interest of the state to create appropriate conditions supporting the implementation of tasks by local government units, which refers not only to the tasks commissioned, but also to own tasks. Therefore, as a rule, local government units should be entitled to participate in public revenues. This share should be adequate to the „tasks assigned to them” – resources should be sufficient to finance the implementation of self-government tasks. The adequacy of the share of local government in the state's income is a basic value in the legal situation of local government; it should stabilise this situation, which requires the adoption of a system of guarantees ensuring that this adequacy is respected (Kieres 2015, pp. 96-98). Such a guarantee function (derived from Article 9(2) of the ECLSG) is a reference to the state's obligation to provide self-government units with financial resources that allow them to carry out their tasks. The problem is that the legislator has not adopted properly flexible financial systems that would guarantee full implementation of the above mentioned Article 9 of the ECLSG.

Considering that the doctrine still remains in the sphere of division into own and commissioned tasks and sources of their financing (as mentioned above) without noticing the problems the self-government and the state are faced by in practice in the discussed area, and which increasingly affect the limitation of self-government independence in the financial aspect, it is necessary for the doctrine to address the issues of local self-government financial management, taking into account not only theoretical but also practical standards resulting from the ECLSG.

The literature on the subject emphasises that the role of theory is not limited to posing research problems skilfully, but is equally based on constructing solutions for them; it cannot be so that doctrine, instead of improving the existing theories in order to even consider their implementation into the practice of law enforcement, often becomes an „intellectual game”. (Jabłoński 2011, pp. 114-115).

In line with the above mentioned need to react to the doctrine of local government's financial independence, taking into account ECLSG standards, I propose to consider the need to analyse the legal solutions adopted in the above mentioned context in selected areas (e.g. education). It is obvious that the state has certain means and an attempt to increase the revenues of local government at the expense of the state would constitute a further burden on the state, which will not be accepted, therefore, in my opinion, it is necessary to look for statutory solutions that will allow for relieving the financial burden on local governments and the state. The analysis should begin with those areas which are the greatest burden for local governments, such as the above-mentioned education, and consider whether the state (and local government) can afford to continue to apply the Teacher's Charter in an unchanged form (Teacher's Charter, which is not consistent with contemporary realities and whose regulations are a huge burden for local governments and the state).

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