

REVENUES AND EXPENDITURES OF MUNICIPALITIES IN THE SLOVAK REPUBLIC

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Abstract

The importance of exploring the structure and characteristics of municipal financial relations contributes to the long-term sustainability and stability of the entire public sector. Municipalities' revenues and expenditures are primarily used to fulfil the aims of their policies. Original and devolved competences as well as some autonomy in decision-making are given to authorities, therefore supervision over their management is important. The expression of self-government is the management of revenues and expenditures. The correct allocation of funds reflects policy objectives. This article discusses about the structure of budgets and offers summary view on part of the financial funds of local governments. It also draws attention to the specific problems, threats and challenges to be faced in the present or in the future.

Keyword

municipalities, revenues, expenditures, COFOG, classification of financial structure

JEL classification: H 71, H 72

Introduction and literature review

Analysis of municipal management requires understanding of financial relations. The budget of municipalities can be characterized by four points, a decentralized money fund, a balance of revenue and expenditure for the certain budget period, a financial plan and an instrument for realizing an aims of municipal policy which is part of public policy. (Peková, 1997) The budget must be characterized in terms of current, capital budget and financial operations using generic, organizational, economic and functional classification. (Veverková, 2013)

The revenue generation process is carried out by utilizing of available funds from economic operators, which is at the expense of their welfare. We distinguish this reduction as temporary or permanent, voluntary or enforced. (Medved' – Nemeč et al., 2007) Municipal revenues are composed of several components. Define tax revenues is more difficult for municipalities than for the state budget, while maintaining tax justice, tax neutrality and low administrative burden. It is important to define the position of territorial self-government in the tax system of the state. The central government must avoid tax competition between municipalities with regard to the tax burden and incidence. This can also be achieved by limiting

the power of municipalities to determine the subject of tax, tax base, tax rates. These measures concern mainly local taxes. (Neubauerová, 2006)

In terms of transparency, tax collection should take into consideration principles such as simplicity because of interest pressure reduction, clarity also for better orientation and control, stability, because frequent changes in tax rules create uncertainty and unintentional elements for individual parties, visibility, having regard to taxpayers which ones feel this directly or indirectly, a clear separation of taxes from mandatory savings and address fees. (Beblavý – Švec, 2001)

In the second place are non-tax revenues such as revenue from own business. In developed countries, these revenues are becoming more traditional. Municipalities derive them from the revenues of municipal enterprises, from renting and selling their own assets, from trading with securities and others resources. Revenues from business activities of municipalities are gradually increasing. The fees represent an additional non-tax revenue, covering especially the current expenses related to the provision of public services to citizens. Administrative fees has special status. Between them we include fees for administrative acts,

penalties for example, offenses, for polluting public spaces and revenue from extra-budgetary funds such as reserve funds.

Non-tax receipts also include non-repayable cash transfers provided as specific purpose subsidies from the public budget. They are provided for specific tasks with the most common goal of supporting education, improving housing, maintaining communications, security and fire protection. Unlike special subsidies, purpose subsidies are not tied to area in which they will be used. For example, they are used to balance municipal budgets and they are usually specified by law. Other revenues include recoverable credit facilities, revenues from pooling of funds, donations and proceeds from public collections and other incidental revenues. (Neubauerová, 2006)

The existence of public expenditures is linked to the existence of the public sector, its organization, objectives and reflects the relationship with private and non-profit sectors. The part of the state's interventions, which is reflected into money, is considered as public expenditures. (Sivák, 2007)

Public expenditures also include expenditures of municipal budgets, which are intended for specific economic activities. These expenditures are non-repayable. The creation of autonomous budgets respects the principle of unity, which helps to avoid any special-purpose links between revenue and expenditure. The structure of expenditures depends primarily on

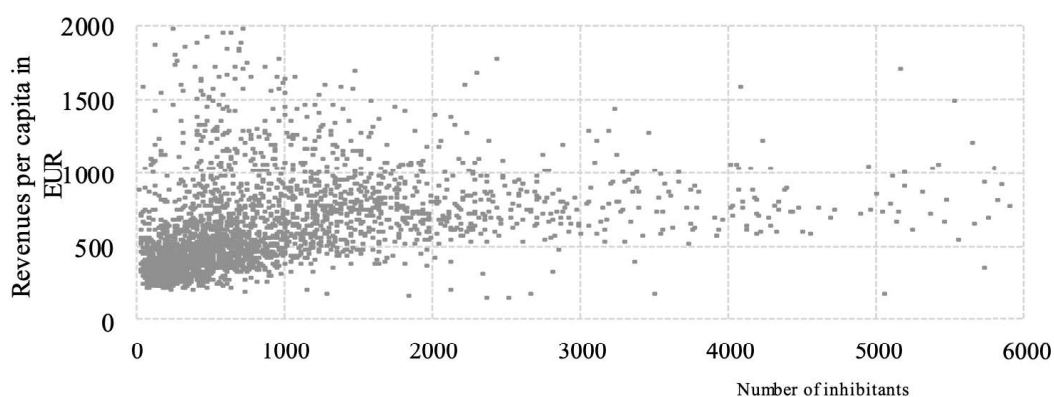
the decision of municipalities and their volume depends mainly on the revenue base. Balanced budget policy must be respected during budgeting process. Expenditures are provided for covering of the needs of the local population through public goods at the instigation of the preferences of the local population. They are affected by the scope of the responsibilities and powers of self-governments. The distribution of expenditure-financed tasks should be made with the aim of maximizing economy and efficiency. (Neubauerová, 2006)

1. Revenues of municipalities

1.1 Dependence between revenues of municipalities and quantity of population

The following chart describes the relationship between the revenues of municipalities and the number of inhabitants. There has been taken all receipts and receipts of financial operations according to the economic classification of the budget classification as well as financial operations which provide the possibility of replenishing funds. If we did not include them in the calculations, there would be no significant changes in the result. The graph only shows municipalities with less than 6 000 inhabitants, because at higher numbers there are no longer extreme values and at the same time it only captures revenues up to 2 000 EUR per capita.

Figure 1. Revenues of municipalities depending on the quantity of population in 2017



Source: own processing according to FIN 1 - 12: 2012 – 2017: Finančný výkaz o príjmoch, výdavkoch a finančných operáciách.

In municipalities, it is confirmed that with the increasing number of inhabitants the revenues grow and this is not proportional, i.e. by the same ratio. While the majority of municipalities up to 1 000 inhabitants achieve revenues in the range from 200 to 600 EUR per capita with a median of the given interval 590 EUR, but with a higher average is 712 EUR due to the more extreme values in this population range. For majority of municipalities with 1 000 to 2 000 inhabitants a range is located from 400 to 1 000 EUR per capita and an average is 792 EUR. 635 from 1894 municipalities were located in the first interval, with revenue below 400 EUR per capita and in the next range the number of municipalities decreased to 16 from 579 municipalities. (FIN 1 – 12, 2012 – 2017)

The calculation show that smaller municipalities achieve less revenue per capita. It is important for the state to regularly review the revenue structure and their availability. Possible inequalities between small and large municipalities could be avoided. Municipalities have some similarities in costs with enterprises, where fixed costs increase by jump and variable gradually. Small municipalities have a significant amount of fixed costs, such as the maintenance of municipal office

buildings, employee wages at least in such a way as to ensure minimum mandatory administration. In less numerous municipalities, the revenues of municipalities should be prevented from serving too much to cover fixed costs and current expenses. Consequently it would not be left for capital investment, which would result into slowing or stopping the development of the municipality. A solution is the merging of municipalities, if the whole system is properly defined and mechanisms are established to set a minimum amount of finance designated for smaller municipalities. This would eliminate fixed costs and generate savings of public finances.

1.2 Structure of revenues

Next table no. 1 provides a complete revenue structure for 2017 according to the economic classification of the budget classification. For the purposes of calculating the balance, budget deficit or surplus, financial operations are not taken into account under the legislation of the Slovak Republic. However, for completeness, they are presented in the table as they are also part of the budget.

Table 1. Structure of revenues and financial revenue operations by economic classification in 2017 in EUR

Tax revenues	2 341 994 460
Income and capital taxes	1 796 997 499
Property taxes	347 901 975
Taxes on goods and services	196 745 621
Sanctions imposed at tax proceedings	340 385
Non-tax revenues	572 063 455
Revenues from business and property ownership	171 542 957
Administrative fees, other fees and charges	276 922 112
Capital income	60 317 809
Interest from domestic loans, loans and deposits	1 088 298
Interest from foreign loans, loans and deposits	80 067
Other non - tax revenues	62 112 214
Grants and transfers	1 266 603 941
Domestic current grants and transfers	1 060 005 906
Domestic capital grants and transfers	199 041 299
Foreign grants	7 379 104
Foreign transfers	177 631
Revenues from transaction with financial assets and liabilities	256 486 343
Revenues from repayments of domestic loans, loans	2 361 461
Revenues from the sale of equity investments	5 586 582
Other financial operations	248 512 731
Received loans and repayable financial borrowing	157 300 962
Domestic loans and repayable financial support	151 868 429
Foreign loans and repayable financial support	5 432 533
Revenues without financial operations	4 180 661 856
TOTAL REVENUES (including financial operations)	4 594 449 161

Source: own processing according to FIN 1 - 12: 2012 – 2017: Finančný výkaz o príjmoch, výdavkoch a finančných operáciách.

Tax revenues are the most important source of financial funds. Municipalities receive 70 % of the national income tax, excluding withholding tax. In the past this percentage was lower and changed regularly. Until 2016 the share was maximally about 4,6 percentage points lower or 0,3 percentage point higher. The revenue is collected by the tax authorities and transferred to the municipalities. The remaining 30 % of the tax revenue goes to higher territorial units. (Zákon č. 564/2004)

In the second, tax revenues include property tax, which includes land, buildings, and apartments. The taxable amount for each of those taxes is broken down by type. The land is divided into arable land, gardens, built-up areas, forest and water management areas, building land etc. The buildings are subject for tax purposes and they are divided into housing,

cottages, detached garages, industrial buildings, including office buildings, warehouses, buildings serving energy etc. The flat tax also includes non-residential buildings. The law sets basic rates, which each municipality has the right to adjust according to its own decision. It can be raised from five to ten times, depending on the type of property. The tax base is set in m². Arable land, permanent grassland, gardens, courtyards, built-up areas, building plots are multiplied by their area by a coefficient set by parliament law for each municipality. (Zákon č. 582/2004)

Municipalities entrepreneurial revenues consist mainly of the sale of buildings and land rent – 154 095 756 EUR and of dividends – 9 509 076 EUR. The largest source of non-tax revenues comes from service charges, subsistence allowances and other non-industrial

sales – 244 791 152 EUR. The sale of land and capital assets reach a share more than 80% of capital income. Other non-tax revenues include e.g. funds from non-profit, contributory and budgetary organizations, claims, gambling levies.

83.69 % of grants and transfers are from domestic origin and current character. 699 499 078 EUR is intended to cover expenditures on delegated competences and comes from the state budget 314 499 876 EUR is also from the state budget, but for purposes other than those mentioned above. Domestic capital transfers have origin mainly in the state budget, excluding state special-purpose funds – 140 672 162 EUR.

Revenues from transactions in financial assets and liabilities are no longer classified as a financial operation and are not included in the calculation of the budget balance. 137 953 575 EUR comes from municipal reserves which are the highest item in this group of financial operations. In addition municipalities also use a number of other funds. The second type of revenue financial operations are loans and repayable financial support. Long-term domestic bank loans accounted for the largest ratio of 51,48 %. Abroad the funds came mainly from international organizations and have ratio 3,45 %. (FIN 1 – 12, 2012 – 2017 et MF/010175/2004-42)

The income structure shows the high importance of tax revenues, especially personal income tax. This is an advantage at a time when the economy is growing and with it the wages of citizens, as was the case between 2012 and 2017 in our reporting period. If the economy cools, this can have a negative impact on the income tax for municipalities, because tax revenues are influenced by lower tax base of citizens and consequently it has impact on redistribution money for municipalities. It is more advantageous for the state and more cautious for municipalities if income is distributed in a different tax structure. More advantageous for the state, because any attempt to reduce the tax rate will bring a positive response from citizens, on the other hand, a great opposition from self-governments. This puts at risk the functionality of one of the instruments of state fiscal policy. For municipalities more cautiously, because if the stability of the revenue from this tax is

threatened by some influence, it may cause a loss of income. At present, municipalities are vassals of income tax. With this tax, there is a risk that the state may in certain cases with populist motives, lower its rate and thus directly raise us citizens' preferences, because the increase of own citizens' net income will feel earlier by the population than saving measures of municipalities. Based on theoretical knowledge in the first part of the thesis, it can be stated that the structure of budgets and their creation is adapted to the trends of developed countries and is heading towards decentralization.

Population migration is a natural phenomenon of open economies. The population is moving to larger settlements. If they move there and do not register for permanent residence, the income tax revenue from this person will be added to the place of official residence rather than to the actual residence. The persons cause an increase in costs for the municipality by staying in the territory of one self-government for a long time. During moving from a smaller municipality to a larger, the problem is partially alleviated by the calculation of the part of this tax for that municipality. The size coefficient multiplies the number of inhabitants and thus creates a multiplier effect. More inhabitants means the higher the coefficient. This relationship ensures an increase in income not by arithmetic series, but by geometric. Naturally, Bratislava has the highest coefficient. During preparing legislation, municipalities that are not Bratislava and Košice and have a population of over 100,000 were forgotten. The law does not set any size coefficient for them. (Zákon č. 564/2004)

Non-tax revenues are created primarily by the municipalities themselves. Their existence helps partially cover the costs of administration. Positive is also the possibility to impose fines and determine their amount and thus improve compliance with laws, generally binding regulations. Grants and transfers serve, among other things, to finance the transferred competences. The central government, in cooperation with local and regional authorities, should regularly check the balance between competence and funding. Original competences are mainly financed by taxes. Care should be taken to ensure that the original competences have ample financial resources, while transfers

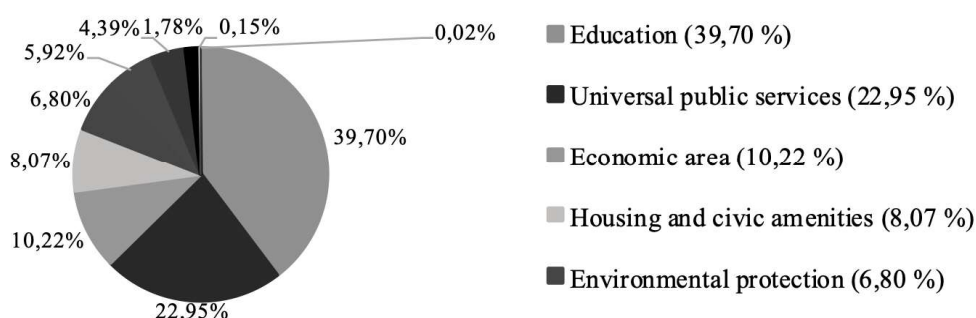
are not sufficient for the transferred competences. This also applies inversely. This problem may arise because grants and transfers have a specific use and also taxes that should be non-purpose, so the state indirectly orders them to finance certain public goods, so taxes are bound to competence. This fragmentation of sources of income may be the subject of further consideration. It has already mentioned positives and negatives.

2. Expenditures of municipalities

2.1 Expenditures of municipalities according to function classification

Expenditures of municipalities are also divided according to functional classification of budget classification. Figure no. 2 shows the proportion of individual types of expenditure according mentioned classification.

Figure 2. Expenditures of municipalities by function classification in 2017 in %



Source: own processing according to FIN 1 - 12: 2012 – 2017: Finančný výkaz o príjmoch, výdavkoch a finančných operáciách.

The largest share, over three quarters, is spent on education, amounting to 1 704 036 175,59 EUR. In the second place, the volume of funds goes to universal public services in the amount of 985 149 056,91 EUR. (FIN 1 – 12, 2012 – 2017) In the case of municipalities, this class should be understood as administrative expenses and staff, material provision for municipal institutions. It does not include those institutions that are engaged in activities specified by another class of functional classification, such as schools. (Legend for COFOG) In this category 81.13% expenditures are intended for the municipality authority and office, 12.52% for public debt transactions, 6.35% for financial budgetary matters and other general public services.

The third class in terms of municipal expenditures is the economic area with a volume of 438 671 971,88 EUR. 80,87 % of this class goes to roads and rail transport. (FIN 1 – 12, 2012 – 2017) This concerns road management and supervision over roads. This includes grants,

loans and subsidies for construction and maintenance. (Legend for COFOG) The other less than 20 % are different constructions and care for the general labour area. (FIN 1 – 12, 2012 – 2017) The term constructions does not mean expenditures related to the constructions itself, but the costs associated with supervision of constructions, regulation, standardization and certification. The concept of general working area is the expression of labour affairs, cooperation with other levels of government and the private sector. (Legend for COFOG) Agriculture, forestry, hunting, fisheries have only a minimal impact on municipal budgets.

346 206 307,44 EUR was budgeted for housing and civic amenities. Of these, 45,07 % were categorized as municipal development (FIN 1 – 12, 2012 – 2017) with the aim of administration and development of services, planning, improvement of facilities, development of public utility facilities, maintenance of parks, orchards, playgrounds. (Legend for COFOG) Development expenditures

no longer include the construction itself. 54.93 % was earmarked for housing development, public lighting and other civic amenities and housing.

The fifth class is environmental protection with a reserved finance amount of 291 780 238,37 EUR. Of this amount, 72,98 % is waste management, 16,36 % is wastewater management and 10,66 % is pollution reduction, nature and landscape protection and other environmental activities. (FIN 1 – 12, 2012 – 2017) Waste management combines transport of waste, its collection, sorting, recovery and disposal. Within the waste water the sewerage system is managed, sewer networks are built, water is cleaned by valid methods such as mechanical, biological, chemical etc. (Legend for COFOG)

254 007 571,41 EUR was earmarked for recreation, culture and religion. Recreation-sports services and cultural services, each receiving over 40% of that amount. 15% was divided between publishing, religious and other cultural services. (FIN 1 – 12, 2012 – 2017) This kind of service is provided to individuals or groups on a collective basis. Culture for municipalities consists especially from the operation of cultural and sports facilities such as

playgrounds, sports halls, swimming pools, gymnasiums, libraries, galleries, museums, memorials, but also from the support of people, i.e. athletes, artists, grants. In addition, municipalities prepare strategies, implement laws, apply research in recreation, culture, religion and perform other tasks. (Legend for COFOG)

The social security area with a volume of 188 307 166,97 EUR was placed below 5% of total expenditures. The largest part in the amount of money – 70,45 % head for old-age people. It is followed by social assistance to citizens in material and social need with a share of 14,4 % and 15,15 % is directed mainly to the areas of family and disability. A small amount around 1 percentage point was provided to solve unemployment, illness. (FIN 1 – 12, 2012 – 2017) As regards the category of old-age, it also includes, inter alia, the provision of nursing services for old-age pensioners, who are dependent on the assistance of another person, for the purposes of necessary household work and basic life activities, the provision of funds to nursing facilities. (Legend for COFOG)

2.2 Structure of expenditures

Table 2. Structure of expenditures and financial expenditure operations by economic classification in 2017 in EUR

Current expenditures	3 491 758
	464
Wages, salaries	1 333 185
	002
Insurance	485 119 019
Goods and services	1 188 343
	578
Current transfers	467 784 887
Interest payments (loans, repayable financial support)	17 325 978
Capital expenditures	636 539 031
Acquisition of capital assets	598 636 898
Capital transfers	37 902 133
Expenditures from transactions with financial assets and liabilities	163 667 418
Loans, repayable fin. assistance and other expenditure operations	25 362 239
Principal repayment	138 305 18
Expenditures without financial operations	4 128 297
	495
TOTAL EXPENDITURES (including financial operations)	4 291 964
	913

Source: own processing according to FIN 1 - 12: 2012 – 2017: Finančný výkaz o príjmoch, výdavkoch a finančných operáciách.

Most funds went to paying wages and salaries. In the case of municipalities, there are mainly tariff, basic and personal salaries with a volume of 1 100 973 460,12 EUR. Health insurance is paid mainly to the General Health Insurance Company, where 68,8 % of it is directed. 340 742 776,72 EUR went to the Social Insurance Agency for all types of social insurance, including contributions to the Solidarity Fund. Employees contributed to the third pillar of old-age savings 10 728 915,36 EUR. Expenditures on goods and services include part of 21,64 % of general municipal services, 15,35 % of routine maintenance of buildings, 14,11 % of energy payments, 8,01 % of food, 6,18 % of material. Other types of expenditure such as meals, water, sewerage, off-job wages, fees, interior furnishings and others were below 5 % in this group of current expenses. Current transfers to contributory organizations with a 24,97 % portion in current transfers have a significant weight. 19,95 % of transfers was directed to the transport companies. Other types of transfers did not exceed 10%.

Acquisition of capital assets consists of 43,65 % of expenditure on reconstruction and modernization, 30,98 % is determined for the revitalization of new buildings, 6,81 % for the purchase of buildings. The preparation of project documentation, purchase of land, tools, technology, vehicles and other groups of capital expenditures take less than 5 %. The main contributors to the expenditure financing operation were repayments of long-term bank loans – 96 558 681,27 EUR, short-term bank loans – 9 240 239,62 EUR and other debt instruments – 26 967 036,62 EUR. (FIN 1 – 12, 2012 – 2017)

During categorizing of expenditures according to functional classification the most resources goes to education, which is also under pressure. Municipalities are trying to change the funding of this competence. A high share of funding for schools should not endanger the financing of other areas of public goods. As it is known from practice that capital investment depends primarily on income from parties other than the municipal's own revenues, therefore their fluctuation is linked to the announcement of possibilities to draw funds from, e. g. the

European Union Structural Funds. The increase of current expenditures may be related to the increase in municipal revenues, especially tax revenues.

Conclusions

The data are from year 2017, because at the time of the solution the data were not available for year 2018. In the area of revenues it was found that the total revenues of municipalities increased with the increase of the population. Municipalities under 1 000 inhabitants achieved an average income – 712 EUR, while municipalities between 1 000 and 2 000 inhabitants had an average income – 792 EUR. It has been shown that tax revenues have reached the highest ratio on total revenue. Grants and transfers followed their non-tax revenues. Fourth, with approximately the same share were the proceeds from transactions in financial assets and liabilities and loans and repayable financial support.

The selection of expenditure by function showed that 39,70 % went to education, i.e. regional education, especially at kindergartens and primary schools, 22,95 % to general public services, 10,22 % to economic, 8,07 % for housing and civic amenities, 6,80 % for environmental protection. Other areas ended up below 5 %. Current expenditures reached the highest share of total expenditure. Capital expenditures were ranked second in the share of total expenditures.

The correct structure of revenues and expenditures and their stability over time ensure the proper functioning of the public sector along with other factors. It is important that the original and delegated competences of the local authorities are always supervised and the financial structure of the budgets is adapted to them. Justice must be taken in mind when allocating funds to municipalities and small municipalities must not be disadvantaged. When allocating tax revenues, it is necessary to respect a certain autonomy of local governments, but they must not be misused as a result of which certain competences will be neglected. Expenditures must be sustainable and authorities

should respect interdependence of current and capital expenditures.

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