

# **Financial independence of commune as a determinant of local development by the example of Poland**

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*Abstract: Financial independence is one of the most important determinants of sustainable local development. It provides ability to implement commissioned and own tasks by the communes. The goal of this article is to present the essence and level of financial independence of communes in Poland. As a result of the survey, the index of communes financial independence does not exceed 50% and it is different for various types of communes.*

*Keywords: commune, local development, financial independence*

## **1. Introduction**

Be classified as a high developed country - this is a target of every state all over the world. Affiliation to this group gives a prestige on international area. Attainment this level of growth is strongly related with local development. Term of local development doesn't have one common definition. It depends on the factors that shape it. According to M. Ziółkowski and M. Goleń it can be defined as process of evolution of object from basic level to more advanced one in many ways [1]. J. Parysek claim that local development can be regarded as social-economic growth related with creation of new work places for regional society and formation of the best term of leaving in local environment connecting with development of organization, structure and functioning of local society system by using local resources of development. Other view on Local Development have R. Brol who describe it as harmonized and systematic actions of local society, local authorities and other entities functioning in commune aiming to creation and improvement of values for local economy and provides the spatial and economic order [2]. L. Wojtasiewicz consider that local development is process of positive

quantitative and qualitative changes related to needs, preferences and system of values in particular system. In relation to A. Nelson it is changes in regional productivity which are measured by number of population, employment, income and value of market production [3].

Comparing whole definitions we can conclude that local development are quantitative and qualitative changes on local territory related to standard of living of the inhabitants and functioning of economic entities.

According to definition we can define the main areas on which influence local development:

improving the competitiveness of economic entities and quality of life of inhabitants,

growth of economic potential of the region,

development of competitiveness of regions [4].

Achieving the best results of local development is very hard and time consuming because every commune has specific factors that influence on it. We can divide them into two groups: dependent and independent factors. To first group we can classify geographic localization and exterior help. To geographic localization we can include localization in rich region, distance from the board of other country, distance from agglomeration. As exterior help we understand possibility to obtain for region financing from European Union. To the second group we can classify activity of local government and society. Activity of local government is represented by how many companies are in region, municipal infrastructure, reductions for companies from region. To activity society we can include voting in elections, percentage of people with master degree.

Besides the specific factors that characterize and have an impact on local development there are also determinants which play a major role on growth of every region. To this group we can include decentralization and financial independence. First term refers to transfer of goals, competencies and funds from state government to local government to realize everything more effectively [5]. The second determinant specifies as acquisition of own resources from local economy to fund and realize important aims [6]. Financial independence of commune is described in Polish constitution as right to own assets, property and acquire income [7].

Moreover we can describe it in two ranges. In wide range financial independence is juridical possibility to decide how to manage funds of commune. In short range is defined only to funds that commune can possess by its own. On financial independence of commune not only influence the sum of funds but also possibility to shape level and scope of costs, organization of local budget, planning and execution of budget.

Possession by communes financial independence have a huge impact on local development. Funds gathering by commune government can be directed for realization of social-economic aims which lead to improving the situation of commune according to national level. Commune also receive transfers from national government but time money should be spend directly on delegated task which mostly have no impact on development of particular commune.

## **2. Methods and materials**

The aim of this article is to define the essence and level of financial independence of communes in Poland.

I assume that urban communes have higher level of financial independence than other two types of communes in Poland.

My article will consist of two parts. In first I will describe the aim of financial independence and methods how to calculate the level of it. The second part will contain the analysis the level of independence of commune.

To write this article I use descriptive and analytic method. In descriptive method is use information from scholarly books, legal acts, articles and specific literature refer to local development and public finance. In analytic method I use the reports of budget execution of polish communes published by Ministry of Finance to analyze the level of financial independence over time of 5 years.

## **3. Results**

### **3.1. Methods reflecting the financial independence of commune**

To write about financial independence of commune in Poland we need to focus previously at the administrative structure of the country, types of communes and a role which they involve. Poland have three-tier division of state in which commune is describe as basic government unit [8]. According to definition commune is community of citizens that lives on homogenous territory regarding to settlement and spatial system as well as social and economic relations that allows to realize public goals [9]. Commune have legal entity.

Communes in Poland are divided into three types according to number of citizens and type of territory. We distinguish rural commune, rural-urban commune and

urban commune. The first one is a set of dwellings that does not belong to an urban community, it is a continuous building area with less than 2000 inhabitants. Rural-urban commune is a territory which includes city and several villages. Urban commune is territory with urban sprawl and more than 100000 citizens who works in production and services [10].

Currently in relation to the report of Central Statistical Office from 2016 in Poland we have 2478 communes [11]. We involve to them 303 urban communes, 616 rural-urban communes and 1559 rural communes. Each of them have some level of financial independence.

To define level of financial independence we need to use one of the index which was created to solve this problem. In literature they are name as [12]:

- index of participation own funds of commune in units of public sector funds,
- index of participation own funds of commune in general funds of it,
- index of participation own fund.

To define first index we need to set the sum of commune own funds and divide it by the sum of funds of units of public sectors [13].

Communes get own revenues from [14]:

- local taxes,
- local fees,
- incomes of local communities,
- assets,
- participation in PIT and CIT taxes,
- commune property,
- donations,
- penalties and fines,
- donations from other communes.

The highest income from this group of impacts commune affecting from local taxes, local fees, assets and general subsidies [15].

Receiving the sum of all revenues of commune we need to compare them to level of funds of units of public sector. Units of Public sector are describe in article 9 of the Public Finance Act[16]. Each of this entities obtain own revenues. The sum of them is necessary to calculate level of financial independence of commune. To get a level of financial independence we need to use this formula.

$$FI = \frac{OF}{EPSF} \times 100\%$$

FI - Level of financial independence, OF - Own Funds, EPSF - Sum of Public Sector Funds

According to information of own funds of communes contained of page of Bank of Local Data [17] and information of Public sector funds contained by Ministry of Finance [18] I will define financial independence of communes in Poland in 2016.

$$FI = \frac{91\,003\,803\,672,80}{190\,600\,000\,000,00} \times 100\% \approx 48\%$$

Communes in relation to Public Sector in 2016 have a finance independence level at 48% which is high indicator.

Second Indicator of financial independence of commune define relation between own revenues of commune to its total revenues. To total revenues of commune we classify own revenues and transfers from state government such as general subvention and core grant [19].

To calculate this index we need to divide own revenues by total revenues as it is write in formula.

$$FI = \frac{OR}{TR} \times 100\%$$

FI - financial independence, OR - Own Revenues, TR - Total Revenues

By example I will calculate the level of Finance independence of all communes on Poland in 2016 based on data published by Bank of Local Data [20].

$$FI = \frac{91\,003\,803\,672,80}{176\,214\,961\,241,37} \times 100\% \approx 52\%$$

Second indicator of financial independence of communes in 2016 amounted 52%. It means that whole communes in Poland have significant independence from state government. What is more according to this index communes can independently realize and spend funds for own targets.

Third index of financial independence of commune is pretty common to second one but the main difference is that own funds are reduced by value of participation in PIT and CIT taxes [21]. To calculate this indicator we compare reduced own revenues to value of total revenues of commune. This relation present formula:

$$FI = \frac{rOR}{TR} \times 100\%$$

FI - financial independence, rOR - reduced Own Revenues, TR - Total Revenues

As example I will calculate the level of Finance independence of all communes on Poland in 2016 based on data published by Bank of Local Data.

$$FI = \frac{53\,251\,547\,825}{176\,214\,961\,241,37} \times 100\% = 30\%$$

According to this method and data the indication of local independence of whole communes in Poland in 2016 is only 30%. We can interpreted it as relation with big influence of state on finances of communes. What is more this method show that participation in taxes PIT and CIT have huge impact on revenues of commune.

### 3.2. Analyze of financial independence of Communes

To analyze the financial independence of Communes in Poland we need to define the indicator based on reports of budget execution from 5 years published by Ministry of Finances. We need to calculate them for examples of rural, rural-urban and urban commune and compare them to define which kind of communes have higher financial independence. Moreover we specify which is main source of revenue in every type of commune.

Firstly I will define the financial independence of rural commune in period 2012-2016 [22].

Table 1.  
Financial independence of rural communes 2012-2016  
Source: Own elaboration based on execution of budget published by ministry of finance

Year	Own Revenues PLN	Total Revenues PLN	Level of financial independence
2012	13 267 902 225,79	34 447 857 858,47	39%
2013	14 267 081 232,23	35 367 526 259,22	40%
2014	15 534 108 334,70	37 033 034 215,01	42%
2015	16 452 231 732,09	38 507 443 422,74	43%
2016	16 785 452 078,57	44 449 694 106,42	38%

According to table level of financial independence of rural communes in Poland in period from 2012 to 2016 had level from 38% to 43%. Taking 2012 as basic year with 39% of Financial independence there was a growth of 1 percentage point in 2013. In 2014 and 2015 we can notice increase of 3 percentage points and 4 percentage points in relation to 2012. 2016 is specific years considering that there was a decrease of 1 percentage point according to 2012. In relation to

calculations rural communes in 2012-2016 had a low level of financial independence and they were dependent of transfers from state government.

Second type of commune is rural-urban commune. Its financial independence level will be define in period of 2011-2015 [23].

Table 2.

Financial independence of rural urban communes 2012-2016

Source: Own Elaboration based on execution of budget published by ministry of finance

Year	Own Revenues PLN	Total Revenues PLN	Level of financial independence
2012	12 717 465 176,29	26 323 708 630,50	48%
2013	13 468 934 207,78	26 868 274 490,43	50%
2014	14 534 889 706,15	28 454 985 453,18	51%
2015	15 192 091 591,70	29 628 892 098,85	51%
2016	15 835 075 436,59	34 669 046 082,51	46%

In relation to table we can define that level of financial independence of rural-urban communes in 2012-2016 had level from 46% to 51%. Taking 2012 as basic year with 48% of Financial independence there was a growth of 2 percentage points in 2013. In 2014 and 2015 we can notice increase of 3 percentage points in relation to 2012. In 2016 we can observe decrease of 2 percentage points according to 2012. In reference to date rural-urban communes in period of 2012-2016 had an average level of financial independence, so they had possibility to financial some of their own aims.

To define the financial independence level of urban commune I will use information of revenues in period 2012-2016 [24].

Table 3.

Financial independence of urban communes 2012-2016

Source: Own elaboration based on execution of budget published by ministry of finance

Year	Own Revenues PLN	Total Revenues PLN	Level of financial independence
2012	10 537 572 690,58	17 635 910 561,24	60%
2013	10 809 953 133,72	17 807 617 495,55	61%
2014	11 641 724 903,89	19 060 961 994,32	61%
2015	11 929 000 664,26	19 530 899 622,66	61%
2016	12 514 101 452,61	22 676 091 210,00	55%

According to table urban communes had in period from 2012 to 2016 independence level from 55% to 61%. Taking 2012 as basic year with 60% of Financial independence there was noticed growth of 1percentage point in 2013, 2014 and 2015. 2016 is specific years considering that there was a decrease of 5 percentage points according to 2012. This date demonstrates how huge

independence from state government urban communes have. According to this they can decide how and on which aims they will spend revenues.

Defined the financial independence level in every type of commune in Poland, there is a necessity to compare this date to determine percentage relation between communes and specify which of them have the highest independence level.

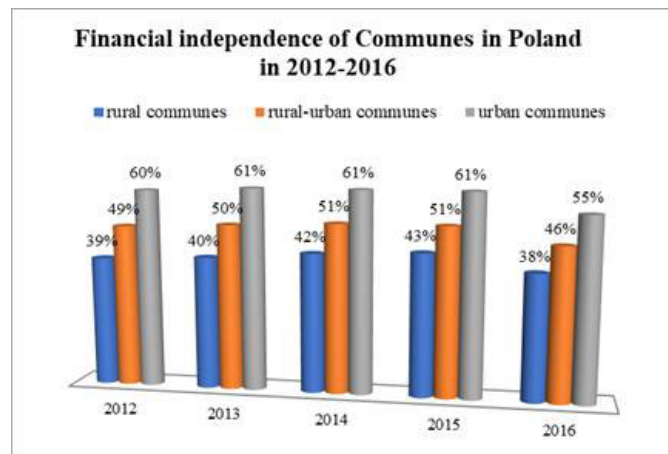


Chart 1.

Financial independence of Communes in Poland in 2012-2016

Source: Own elaboration based on execution of budget published by ministry of finance

In relation to diagram of financial independence Communes in Poland in 2012-2016 we can notice that the highest level have urban communes. The highest urban communes had in 2013, 2014 and 2015. In relation to this outcome rural-urban communes had a 10 percentage points less result and rural communes almost 20 percentage points less. This provides that urban communes have higher level of development than other two types of communes.

### Conclusion

Financial independence is one of the most important determinant of local development of communes. It can be defined as possibility to decide which aims local government is going to finance to influence on social- economic growth. What is more financial development can be specify as possession of sufficient own revenues by communes to finance aims.

In Poland we can define financial independence as relation between own revenues of whole communes in Poland to sum of revenues of unities of public sector. Also it can be specify as relation between own revenues to total revenues each of three types of communes: rural, rural-urban and urban communes. In relation to first factor polish communes have 48% of financial independence. It means that they have moderate independence in realization of own aims.



By the defining the financial independence of urban, rural-urban and rural communes in relation to data from Ministry of Finance I confirmed my hypothesis that urban communes have the highest level of financial independence in relation to other two types of communes. To approve it in 2015 urban communes have 61% of financial independence which was greater by 10 percentage points from rural-urban and by 22 percentage points from rural communes.

Thanks to this level of financial independence urban communes can decide about spending own revenues on important aims which have a huge impact on social-development growth of this commune. What is more urban communes are more developed than rural and rural urban communes.

To sum up financial Independence can influence on improvement of social and economic development of every commune. In Poland only urban communes have a sufficient level of financial independence to influence on its development by realizing own aims. Rural-urban communes have moderate level of financial independence so in some way they may influence on development. Rural communes have low level of financial independence, so they are dependent on transfers from state government and they need realize commissioned aims which not always have impact of commune development.

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