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Capital Investment Funding in Poland

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Capital Investment Funding in Poland

Inventory of Financial Flows for Regional Development and Local Public Services

Introduction

The presented report was completed in December 2001. It does not mean that the authors were able to include all updated data. The most of information included in this report is based on data from 2000. In 1999 Poland changed the administrative structure and two new levels of self governments: counties and regions appeared. It means that self-government sector and its role has increased significantly but recently. Despite young age, new self-government units joined the process of supporting local and regional development. It was visible just in data from 2000 – the second year of counties' and regions' operation. The inventory allowed the Institute team to recognize real streams of money supporting capital investment on local and regional levels. It "opened eyes" for the critical role of infrastructure enterprises in financing capital investment in infrastructure and the modesty of foreign aid financing this sphere in Poland. The inventory reveals significant developmental effort of local governments in Poland and the role of banking industry in supporting this effort.

The report operates terminology used by the Main Statistic Office. In numerous publications the same Polish terms are interpreted into English in different ways. We prefer official statistic terminology instead of independent translations.

Important issue are names of local governments in Poland. To avoid confusions we explain our translations. We have three levels of local governments, but four types of self-government units. They are:

Gminy – (fundamental self government unit, sometimes translated into English as gminas or communes) – in this report we call them communities (rural entities) and municipalities (urban entities) or in uniformed way: *communities/municipalities*.

Powiaty – (second level of self-government with different competences; on the area of one such unit there are several communities and municipalities) – in this report we call them *counties*

Miasta na prawach powiatu - (cities with county rights - these units perform both competences of municipalities and counties; this form concerns larger cities) – in this report we call them *cities with county rights*.

Województwa - (sometimes translated into English as voivodships; there are larger territorial entities with regional competences) – in this report we call them simply: *regions*.

The report consists of four chapters: description of public finance system used at local and regional levels, presentation of statistic data on capital investment financing, description of mechanisms of capital investment financing in Poland and the evaluation how different mechanisms meet their objectives.

The authors would appreciate all comments and suggestions concerning this report.

1. Public Finance System at Local and Regional Levels¹

Budget incomes of the Municipality, County and Region are regulated by the "Law on territorial self government units incomes", dated November 26th, 1998² Accordingly to the Law, public incomes on local and regional levels are composed of the three main sources:

- Local/regional governments units own revenues. Those revenues in the year 2000 amounted to 41,7% of total incomes,
- Allocations, which amounted to 22,7% of the local regional budgets incomes,
- General subsidies, which amounted to 35,6 % of the revenues³.

Local/Regional government own revenues

Local/Regional governments own revenues are the most important source of budgetary income and constituted last year nearly half of all incomes of local governments. Own revenues are composed of the following components:

- Shares in personal and corporate income taxes. Those shares, different for each unit are as follows:

Municipality	PIT	27,6%	CIT	5%
County	PIT	1,0%	CIT	0%
Region	PIT	1,5%	CIT	0,5%

Shares in taxes collected by national budget contribute in 13,8% to revenues of local government units. Among those taxes definitely the most important are personal income taxes which contribute to 12,4% of revenues.

- Revenues from local taxes. Those taxes include real estate tax, commercial vehicle tax, legacy and gift tax, agriculture and forests taxes, flat rate tax paid by selected family micro enterprises. Among the local taxes the most important is the real estate tax, which brought 9,2% of all incomes of the local governments in Poland. Other taxes contribute between 0,1% (forest tax) up to 1% (agriculture tax) to local and regional incomes. Municipalities can decide about the level of local taxes up to legally established ceiling. Local authorities are also authorized to apply individual exemptions and incentives concerning local taxes.
- Revenues from fees, including stamp duty and administrative fees. Fees collected by local government units contributed 2,7% to the incomes in year 2000.
- Revenues on assets, especially property owned by municipalities premises. Those include especially rent on the real estate owned by municipalities (e.g. premises). Income on assets contributed last year (2000) amounted to 7 percent of the incomes.

¹ Description is based on the legal situation in 2001.

² "Dziennik Ustaw no 150 z 1998 with changes in "Dziennik ustaw" no 160, 2000 and Dziennik Ustaw no 55, 39 and 95 2001 .

³ Report on the budget execution of the territorial self governments Units in 2000. Ministry of Finance 2001.

Other revenues, including e.g. interest on financial capital, deposited in banks, income from privatization, revenues of communal companies and other enterprises owned partly by local self government units, income on fines. Those income contributed 6,8% to the incomes.

Allocations

Allocation can be defined as financial transfer, mostly from national governments to local and regional authorities to fulfill designated task, including capital investment tasks. Local and regional governments can use them only for the tasks, which are targeted by financing institution. They can be divided into two main groups, basing on the division of responsibilities between territorial self-government units and national administration.

* Allocations providing co-financing of the local governments tasks, related e.g. to social aid medical assistance, public safety - 8,2% of incomes in 2000

* Allocations covering the costs of tasks, which should be executed by the national administration, but according to mutual agreements are executed by municipality, county or region - 12, 2 % incomes in year 2000.

Those two groups of subsidies contributed in nearly 90 percent to all subsidies. Remaining are the allocations for designated tasks executed on the basis of agreement with other local self government units. According to the law, local government which executes the tasks of other unit (e.g. municipality, which executes the task of county or region should conclude the agreement and obtain the allocation at the amount included into the agreement⁴ It includes also subsidies obtained from Appropriated State Funds, like e.g. the Fund for Environmental Protection. The last item is relatively small (0,4% of incomes in year 2000) but it is in 75% used for financing capital investment.

General Subsidies

General Subsidies play important role in supplementing local/regional revenues from taxes. According to the Constitution territorial self-governments should have revenues allowing to fulfill designated tasks. Since local taxes and fees combined with share in PIT and CIT, are not sufficient, general subsidies are necessary. Contrary to allocations, they can be used more flexible by local and regional authorities. Incomes obtained as a general subsidy can be spend on the basis of the decision of the local/regional council. General subsidies can be divided into three parts, which differ amongst the levels of the governments. Municipality obtains fundamental part of general subsidy, which plays important role in diminishing disparities between units with high and low tax income. Total amount of the fundamental part of the general subsidy for all municipalities is composed of the not less than 1 percent of the national budget income and total amount paid by municipalities with tax income above 150 percent of the average⁵. The fundamental part of the general subsidy is later divided into two funds :

* Fund for diminishing disparities, which is paid to municipalities and communities with tax income, lower than 85% of average.

* Remaining amount is distributed between all municipalities on the basis of the indicator based on the number of inhabitants

⁴ Law on revenues of the territorial self government units, chapter 46.

⁵ For the year 2001. In years 1999 and 2000 these figures were different

Municipalities and communities obtain also educational part of the general subsidy for maintenance of the educational units and compensation part of the general subsidy, mostly to compensate the personal car transportation tax, which was replaced by increased excise tax. It compensates also lower income related to tax incentives.

Counties obtain educational part of the general subsidy for high schools, highway part of the general subsidy for maintenance of the roads and equalizing part of the general subsidy to diminish the difference in tax revenues, between local governments. Equalizing part of the general subsidy is transferred to the counties, which have lower *per capita* share in PIT than the highest in Poland (in Warsaw County). It is based on special indicator related to highest in Poland. Counties obtain 85% of the difference between highest *per capita* share in PIT and *per capita* share in given county multiplied by the number of inhabitants.

Regions obtain general subsidies divided into three parts: educational for college level education, highway part and equalizing part for those regions which have lower share in PIT and CIT than the highest in Polish region. Benefiting regions obtain 70 percent of the difference between the highest *per capita* share in CIT and PIT and *per capita* share in given region multiply by the number of inhabitants.

Educational and highway part of the general subsidy constitute 84 percent of all subventions transferred to municipalities, communities, counties and regions. Those subventions amounted last year to 5,38 billions of US dollars . Educational subvention, much larger amount to \$ 4,8 billions, while road subvention to \$0,58 billions.⁶

⁶ Report on the budget of territorial self government units in 2000. Ministry of Finance 2001.

2. Local and regional investment expenditures – analysis of statistical data

The presented analysis of statistic data is based on available information mostly from domestic sources. Important part of the presented information comes from the Main Statistic Office which collects statistic reports of local governments concerning budgetary plans and spending. Starting form 1999, also the Ministry of Finance collects and analyzes data on local governments budgets because of the new methodology of counting public finance system deficit. Beginning from 1996 the debt of local governments was growing more rapidly and counting only state government deficit proved to be insufficient to show the situation of the public finance system. The third source of information is the Committee for European Integration which monitors the spending of EU developmental aid.

While analyzing data on capital investment, it is necessary to underline, that in the period of 1990-1998 there was only one level of local governments in Poland – communities (municipalities). In 1999 two new levels were created: counties and regions. In fact in budgetary statistics appeared the forth category: cities with county rights. This category contains cities which have joint competences of community and county. Capital investment on local and regional levels is effected by different units. The most important are local governments and infrastructure companies. In this chapter we are not interested in capital investment of enterprises, except for infrastructure. It means that the presented expenditures of this kind could be lower than in reality because some expenditures of commercial sector and individuals could not be taken into account.

Form numerous statistic divisions of local and regional capital investment we decided to concentrate on data of the year 2000. The situation concerning this year is presented in the more detailed way. Parallely we decided to present dynamic data. All data are presented in current prices. Unfortunately it is necessary to realize that Poland was a place of significant inflation. However we decided not to present data in constant prices but to re-account data in zloty into ECU or euro on basis of the exchange rate of Polish zloty (PLN) into ECU or euro, form the last day of the given year. This is of course simplification but it allows for the presentation of data comparative to those used in the European Union. We think that this comparisons would allow for better understanding the value and significance of capital investment in Poland.

Below presented tables contain data on the following issues:

- 1) Changes in capital expenditures of local governments and infrastructure companies within the period of 1993-2000,
- 2) Capital investment expenditures of local governments and sources of their financing in 2000,
- 3) Budgetary situation of local governments in 2000,
- 4) Comparison of capital investment of local governments per capita in different regions and different local government levels in 2000.

Much more statistic information is contained in particular chapters concerning detailed sources of financing. The first table contains data on the value of capital investment expenditures of local governments and infrastructure companies within the period of 1993-2000 in constant prices in PLN and ECU/euro.

Table 1
Capital Investment Expenditures of Local Governments and Infrastructure Companies in million PLN and ECU/euro (current prices)

Capital investment expenditures	1993	1994	1995	1996	1997	1998	1999	2000
Local governments	2435	3364	4658	7056	9680	8176	12562	13532
ECU/Euro equivalent	1018	1131	1473	1983	2496	1991	3013	3497
Supply of electricity, gas, heat and hot water, Water supply and purification	3570	4869	6768	8770	10026	10255	10606	9138
ECU/Euro equivalent	1492	1637	2140	2464	2586	2497	2544	2361
Post and telecommunications	1482	1723	2590	3938	6474	8402	9446	10320
ECU/Euro equivalent	619	579	819	1107	1670	2046	2266	2667
TOTAL domestic in M PLN	7487	9956	14016	19764	26180	26833	32614	32990
ECU/Euro equivalent	3129	3347	4432	5554	6752	6534	7823	8525
Exchange rate PLN/Euro	2,393	2,974	3,162	3,558	3,877	4,107	4,169	3,870

Source: Ministry of Finance, Main Statistic Office

The data included in the above table show that within the period of 1993-2000 the capital investment expenditures of local governments and infrastructure companies increased by 172,5% in euro values. Especially fast increase was observed in capital expenditures of local governments (by 243,5%). The increase of capital investment in supplies of electricity, water, gas heat and sewage purification amounted to 58,2%. The increase of capital investment in post and telecommunications amounted to 330,9%. The presented data show that capital investment expenditures used for local and regional development increased significantly. For year 2000 the total approved for Poland PHARE assistance amounted to 490 million euro⁷. This assistance constitutes about 5,7% of total developmental expenditures on local levels in Poland. However not the whole EU assistance had regional character. The presented data show that local governments and infrastructure companies in Poland have significant financial potential for capital investment.

Especially important part of capital investment is effected by local governments as their budgetary expenditures. In Poland there are not secondary data on methods of financing capital investment in local governments. To count the proportions in which particular sources are used to finance capital investment of local government we used the following procedure.

1. Several budgetary incomes are dedicated in concrete amounts to capital investment or long-term uses: executed allocations for capital investment, increase of long-term bank credits, increase of long-term non-bank loans, increase of issued municipality bonds (new sales minus repayments). We accepted that all sums which were dedicated as long term as serving capital investment financing.

⁷ It does not mean that this amount was spent on local capital investment.

2. Secondly, we accepted the rule that all remaining local government incomes with no specific direction of spending contribute to capital investment financing in the same way as they contribute to all expenditures. It means that incomes with non dedicated direction of spending contributed to the capital investment in the proportional way to their size.

The results of counting how particular sources of financing of local governments contribute to capital investment are presented in the below table. Data for counting were take form the Ministry of Finance.

Table 2
Capital Investment Expenditures of Local Governments and Estimations of Financing Sources in Poland in 2000

Item	In 000 PLN	In %
Capital Investment Expenditures	13.532.028	100,00
Sources of Financing	-	-
Own Revenues	4.421.580	32,65
General Subsidies	3.735.690	27,61
Allocations for Capital Investment *	2.717.510	20,10
Long-term Bank credits*	1.647.637	12,18
Long-term Loans*	502.868	3,72
Municipal Bonds*	227.494	1,68
Surplus form Previous Years	161.981	1,21
Other Incomes	107.144	0,79
Privatization Incomes	8.437	0,06
Sales of Securities	1.687	0,01
Total Sources of Financing	13.532.028	100,00

Source: Ministry of Finance and own estimations, * - incomes with dedicated direction of spending

Accordingly to data included in the above table, the No 1 source of capital investment financing in 2000 of local governments were their own revenues. On basis of the accepted rule, they financed 32,65% of all capital investment of local governments. The second source of financing were general subsidies (coming from the central budget and supporting own revenues). They financed 27,61% of total capital investment of local governments in Poland in 2000. Both sources had non dedicated direction of spending. It means that local governments in Poland had relatively high preference of increasing capital investment from their incomes with non-dedicated direction of spending. The debt instruments allowed for 17,58% capital investment financing in 2000. In debt instruments critical role was played by bank credits. The other sources of capital investment financing were less important.

Because debt sources are becoming the third most important sources of capital investment financing it seems to be important to present the level of deficit of different levels of local governments. These data are included in the below table.

Table 3
Incomes and Outcomes of Local Governments in 2000 in Poland in million PLN

Item	Total Local Governments	Communities/Municipalities	Counties	Cities with County Rights	Regions
Incomes	72610	34584	12555	21766	3705
Own Revenues	30290 (41,7%)	18165 (52,5%)	992 (7,9%)	10541 (48,5%)	592 (16,0%)
General Subsidies	25858	11669	5989	6800	1400
Target Donations	16462	4750	5574	4426	1713
Outcomes	75747	36211	12664	23084	3787
Current Expenditures	62215	28667	11719	19142	2687
Capital Investments	13532	7544	945	3943	1100
Incomes - Outcomes	-3137	-1627	-110	-1318	-83
Deficit as % of incomes	4,32	4,70	0,87	6,06	2,24

Source: Ministry of Finance

The highest rate of deficit was observed in cities with county rights 6,06%. Communities (municipalities) were on the second position. The lowest rates were observed in counties and in regions. It was caused by the fact that these levels of local government have short life experience (they were created on January 1st 1999). The data above present also the power of different levels of local governments in collecting their own revenues (ratio: own revenues/total incomes). The highest revenues ratio had communities/municipalities (52,5%) and cities with county rights (48,5%). The lowest ratios were observed in counties and regions.

Capital investment expenditures of local governments are very diversified by regions and by level of local government. In Poland there are 16 regions. They are listed in table below. In the second column we listed the number of population in the particular regions. In the following four columns there are listed values of capital investment per capita in different levels of local governments.

Table 4
Capital investment expenditures of local governments per capita in local governments in Poland in 2000 in PLN

Region (capital)	Population	Communities/ Municipalities	Counties	Cities with County Rights	Regions
Lower Silesia (Wrocław)	2 975 074	317,5	37,6	442,6	38,2
Kujawsko-Pomorski (Toruń)	2 101 068	210,7	19,9	335,9	12,7
Lubelski (Lublin)	2 233 271	172,7	33,1	243,0	25,5
Lubuski Zielona Góra)	1 023 829	232,4	26,5	474,0	37,0
Łódzki (Łódź)	2 647 783	205,2	33,0	253,5	6,6
Małopolski (Cracow)	3 226 611	201,9	34,1	408,5	27,0
Mazovia (Warsaw)	5 068 677	543,0	25,7	378,1	16,7
Opolski (Opole)	1 086 608	181,6	27,4	407,2	14,3
Podkarpacki (Rzeszów)	2 127 859	218,7	47,9	342,2	16,1
Podlaski (Białystok)	1 222 011	208,5	46,9	293,7	17,3
Pomerania (Gdansk)	2 194 628	247,0	57,3	476,8	24,0
Silesia (Katowice)	4 857 848	187,1	34,4	296,5	71,1
Saint Cross (Kielce)	1 323 719	217,2	51,9	300,1	75,6
Warminsko-Mazurski (Olsztyn)	1 466 248	190,6	41,5	216,2	11,0
Wielkopolski (Poznan)	3 357 541	259,0	28,2	339,5	19,6
West Pomerania (Szczecin)	1 733 446	269,3	37,7	388,8	13,9
TOTAL	38 646 201	277,6	34,8	342,8	28,5

Source: Ministry of Finance

The data presented in the above table show that communities (municipalities) in two regions have the highest average capital investment expenditures per capita. There are Mazovia (with capitol of Warsaw) and Lower Silesia (Wrocław). Other regions have results below the average. The difference in per capita investment between region with the highest and lowest per capita amounts equals to 3,14. The lowest per capita capital investment is observed in rural Lubelski, Opolski and Warminsko-Mazurski regions and heavily industrialized Silesia. In counties the highest per capita expenditures are observed in Pomerania 57,3 PLN, Saint Cross 51,9 PLN and the lowest in Kujawsko-Pomorski 19,9 PLN. The difference between the highest and the lowest regions equals to 2,88. There are not so significant discrepancies between cities with county rights throughout regions. The highest per capita expenditures are observed in Pomerania 476,8 PLN and the lowest in neighboring Warminsko-Mazurski Region 216,2 PLN. The difference between the highest and the lowest average expenditures equals to 2,21.

Huge differences were observed in capital investment expenditures of regional level of self-governments. The highest per capita expenditures were observed in Saint Cross 75,6 PLN and in Silesia 71,1 PLN. The lowest expenditures were observed in Łódzki Region (only 6,6 PLN per person). Huge differences between regions are mostly based on the fact that new regions were created only one year before the beginning of analyzed period. The presented data show that differentiation in effecting capital investment among regions within particular groups of

local governments are not so significant. However it is necessary to realize that the analyzed data are the average data. Real differences between communities, counties and cities are higher.

The differences in capital investment expenditures between regions, counties, cities and communities are the final result of changing regional disparities in Poland in 90-ties. The process of increasing regional disparities in Poland in the area of capital investment expenditures, employment and income distribution was described in the chapter 4.3.

3. Mechanisms for financing of capital investment for local and regional development

The chapter 3 is aimed at the presentation of all important capital investment funding mechanisms used in Poland. The described mechanisms include:

1. General subsidies and appropriated allocations for local governments
2. Local governments own revenues and shares in central taxation
3. Local government borrowing
4. State budget donations for sector purposes
5. State agencies donations, loans and grants
6. Regional Contracts
7. Capital investment financed through service fees
8. European Union programs

Apart from descriptions of particular funding mechanisms the chapter contains also assessment of the compatibility of different funding mechanisms with the present key four principles of operating Structural Funds. These principles included:

Concentration - focus on the main priorities

Programming - operating on basis of integrated programs to ensure better coordination of measures

Partnership - linked with subsidiarity principle, bases on including to the cooperation different partners: European authorities, Member State, subnational authorities and broad spectrum of economic and social partners.

Additionality – co financing the projects by program partners

Besides, we decided also to include into assessment a principle of transparency. We understood transparency principle as using clear procedures providing honest treatment and open for public criteria for appropriating funds.

3.1. General subsidies and appropriated allocations for local governments

There are two most important forms of transferring central budgetary sources to local and regional governments. The first one is constituted of general subsidies, which are provided to all levels of local and regional government. The second form is constituted of appropriated allocations.

Using general subsidies for financing capital investment

General subsidies are direct transfers form the central budget to communities, counties and regions. General subsidies are considered as addition to own revenues of local governments

and can be used for all own tasks (competences of self governments)⁸. In communities general subsidies are counted separately for three divided parts: fundamental, educational and compensating. Fundamental part of general subsidies for communities contains mechanism equalizing diversified tax power of different communities. Therefore fiscally weaker communities are supported. In counties and regions general subsidies consist of 3 parts: educational, highways and equalizing⁹. There are different percentage formulas used for counting general subsidies for each kind of unit but the most important factor is the number of citizens living in each unit. Summarizing:

1. Each community receives general subsidy consisting of three independent counted parts: fundamental, educational and compensating.
2. Fundamental part of general subsidy for communities is counted as 1% of total planned incomes of the central budget
3. From the total sum of general subsidies 4% is subtracted as central reserve
4. Each community with tax incomes less than 85% of the average tax incomes per person in the nation receives 90% of difference between per capita amounts (given and the average)
5. The remaining amount is divided amongst all communities in relation to the number of citizens and value of the remaining sum.
6. The educational part of the general subsidy is established as 12,8% of the total planned central budget incomes and divided accordingly to the rules established by Minister of Education. These rules are based on complicated formulas including such positions as number of students and former expenditures.
7. Similar equalizing rules exist in relation to counties and regions.
8. Equalizing in counties and regions is effected trough equalizing part of general subsidies.
9. The objective of so called compensating part of the general subsidies is to compensate the liquidation of transport tax on personal cars (former own revenue of communities)

Despite of the fact that the value of general subsidy is created using three different mechanisms, there is not provision what is the detailed purpose of transferred money. Local governments are obliged to fulfill all their tasks (originated form the particular self governance acts for each level of local governments). However it is not decided what part of general subsidies should be spent on current expenditures and what part for capital investment. Below we present mechanism in what way general subsidies are used for financing capital investment.

As it was mentioned in the first paragraph, general subsidies are considered as addition to own revenues and the other financial inflows which could be used for financing current activities and capital investment. The procedure of using general subsidies for capital investment is following:

1. The first step is to estimate all financial obligations of local government connected with so-called current activities (e.g. running public schools, children day cares, local transportation, highways maintenance etc.)

⁸ In this chapter we present regulations for 2000, because we have data form this year. Unfortunately methods of counting general subventions are changing very often.

⁹ The fundamental and educational parts of general subsidies are subordinated to real budgetary incomes. Because central budgetary incomes are fluctuating, it is necessary to change local budgets many times in the fiscal year.

2. The second step is to estimate all obligations connected with the necessity of financing of ongoing capital investments as the first priority and capital investment needs for the following year as the second priority.
3. The following move is the creation of local government income forecast including: general subsidies, allocations, own revenues, allocations and donations form funds, loans and the other resources.
4. The next step is balancing planned expenditures and planned incomes. It shows surplus or deficit. In the last situation the local government is obliged either to cut expenditures or to indicate additional sources of financing e.g. taking loans or issuance of municipal bonds.

In fact the whole procedure is very complicated. In 2000 the Gdynia Municipality had to change the annual budget for 2000 12 times, in this 7 times with regard for changes in the central budget incomes. The last change was executed in December 2000. Similar situation took place in other local governments.

In 2000 the general subsidies constituted 35,6% of the total budgetary incomes of local governments and amounted to 25.858 million of Polish Zlotys (PLN). Accordingly to our estimations they financed 27,61% of total capital investment expenditures, which are, included in local budgets, what amounted to 3.735 million PLN.

As the principle, the local governments have freedom in spending resources coming from general subsidies after fulfilling obligations connected with current activities. The incomes from general subsidies are matched with the other incomes and they all can be used for capital investment. Investment expenditures of local governments should be included in local budgets. In the most of local governments special capital investment plans are prepared (but it is not obligatory). Budget information is freely presented and available to all interested. Spending is governed by the Act of Public Procurement of 1995, which imposes the use of rules of transparent and honest procedures. Participants of the procurement procedures are allowed to place complaints.

Below there are presented data on the size of general subsidies for Polish local governments in 2000. These subsidies constituted 35,6% of all incomes of local governments (which totally amounted to 72.609 million PLN).

Table 5
General subsidies of local and regional governments w mln PLN in 2000

Subsidies (Parts)	Total	Communities	Counties	Cities with county rights	Regions
Fundamental	1.771	1.765	-	6	-
Educational	19.367	8.676	4.689	5.578	424
Compensating	1.743	1.228	-	515	-
Highways	2.316	-	966	602	748
Equalizing	661	-	333	100	228
Total	25.858	11.669	5.988	6.801	1.400

Source: Ministry of Finance

Summing up, the mechanisms used in calculating general subsidies allow for equalizing the differentiated tax bases of different local governments in Poland. It is important that 2.432 million of PLN were used in different forms to equalize local development conditions.

General subsidies, as capital investment funding mechanism, generally meet the criteria of compliance with EU standards. Local governments decide what are their main priorities (concentration), include capital expenditures in investment plans (programming), are trying to apply partnership and additionality principle (mostly through matching funds with the other partners). The procedures of using general subsidies for capital investment are also transparent.

Allocations for capital investment

Appropriated allocations are aimed at financing concrete tasks, which are listed in the Acts of Incomes of Local Governments (for 1999-2000, 2001). The Acts list two categories of appropriated allocations:

1) Allocations due to each local government

- They are targeted at tasks of governmental administration contracted to local governments and the other central government tasks provided by the legislation.

2) Allocations potentially available for local governments; they include:

- Allocations for subsidizing own tasks of local governments
- Allocations for eliminating dangers for security and public order
- Allocations from public target funds
- Allocations for tasks agreed with governmental administration or other levels of administration
- Allocations for social assistance and housing aid
- Allocations for capital investment connected with own tasks of local governments¹⁰

In general, there are not complaints about the first group of appropriated allocations. When local governments are contracted to perform tasks of central administration they have to receive suitable compensation for this performance. In some cases local governments can overtake some central government tasks in return for donation for this purpose (tasks agreed). Also allocations for social assistance and housing aid do not create too many problems (unfortunately they do not cover all expenditures and the central coverage ratio is scaling down).

More difficult situation exists when the problem of allocations from public funds is concerned. All public funds have very detailed criteria of distributing allocations (it will be described in chapter 3.4.). Serious doubts appear when central government allocations are used for effecting capital investment, which are considered as own tasks of local governments. The criteria included in the Act of Incomes of Local Governments provide for:

- Allocation may not exceed 50% of the total cost of capital investment (80% in education and 75% in high unemployment units) and,
- Unused allocations should be returned.

Unfortunately, apart from shares' criteria, there are not any provisions considering eligibility, maximum sizes of allocations, procedures of applying, selection criteria etc. It means that

¹⁰ Gilowska Zyta: *Sources of Financing Local Governments in Poland*, Warsaw 1999, p. 10 (in Polish). This also a functional division of capital investment allocations granted by the central government to local governments. Allocations from target public funds are described in the chapter 3.5.

criteria are discretionary and strongly depend on political decisions. Some authors¹¹ maintain that allocations financing own tasks of local governments require political decisions. In this context such allocation could be considered as awards for electoral support. The only positive side of such target donations is the fact that they cannot be used for other purposes.

Table 6
Target Allocations for Local Governments in Poland in 2000 in million PLN

Item	Total Local Governments	Communities/ Municipalities	Counties	Cities with County Rights	Regions
Allocations for tasks of governmental administration performed by LG	8839	2501	3071	2912	354
In this for capital investment	348	34	43	22	250
Allocations for own tasks of LG	5928	1530	1982	1286	1129
In this for capital investment	1825	483	449	352	541
Allocations for tasks agreed with governmental administration	759	120	432	158	49
In this for capital investment	111	85	0	0	26
Allocations for tasks agreed between Local Governments	678	417	57	40	165
In this for capital investment	246	53	15	29	149
Allocations from Public Funds	258	182	33	30	16
In this for capital investment	187	132	22	21	12
Total allocations	16462	4750	5573	4426	1712
In this total capital investment	2717	787	529	424	978

Source: Ministry of Finance

Accordingly to the presented data the total amount of appropriated allocations was equal to 16462 million PLN and total capital investment executed from these donations was about 2717 million PLN what constituted about 16,5% of the total value of donations. Appropriated allocations financed capital investment of local governments in 20,1% in 2000. The highest rate of capital investment in total allocations was observed in regions 57,1% and the lowest in counties and cities with county law (below 10%). The highest rate of capital investment was observed in allocations for own task of local governments (which was considered as discretionary).

Allocations for capital investment meet EU standards only partly. Especially difficult situation exists in relation to allocations for capital investment connected with own tasks of local governments. The selection of beneficiaries in local governments seems to be not transparent. The criteria of including investment expenditures of the given local government to the central budget are discretionary and base on political decisions. These criteria are not known. All other types of allocations generally meet EU standards.

It is important to underline that the central government can appropriate also allocations for sector purposes. Most of them are distributed on the principle of reducing social costs of economic reforms within the framework of special governmental programs of restructuring mining, steel industry etc. These allocations are only in a slight size used by local governments (3,4% of total sector allocations for capital investment). This issue is addressed in chapter 3.4.

¹¹ E.g. Zyta Gilowska.

3.2. Local government own revenues and shares in central taxation

Rules of collecting local and regional revenues

Local taxes, like other taxes in Poland are collected by state tax offices. Tax office has 14 days to transfer the due amount of local taxes to Municipality bank account, starting from the day the taxes were paid. Local Authorities (Chairmen of the Board) are authorized to request the quarterly report on the tax revenues, to find out if the taxes were transferred properly. In case of delay, local authorities should be compensated with “penalty interests”, similar to those applied to delayed taxpayers. In case of legacy and gift tax revenues are also collected by tax offices and later transferred to municipality where the property is located. If legacy include property located in different municipalities, revenues are transferred to municipality of testator. Similar solutions are applied to gifts.

Shares in national taxes are transferred from the tax offices to central budget and later to local governments. Those transfers should be completed till the 10th day of the next month, after those in which the income taxes were paid. The amount due to municipality is set up on the basis of two indicators.- 0,276 (27,6 share in national taxes) and indicator of compensated share of the all municipal units revenues from national taxes. This allows for scaling down disparities in tax revenues. Mentioned indicator is set the following way:

A/ Total amount of PIT revenues in given region in the previous year is multiplied by 0,276 and by the percentage of the municipality community inhabitants in the number of the region inhabitants on June 30th, previous year.

B/Total amount of PIT revenues in the previous year is multiplied by 0,276 and later by the indicator showing the share of PIT paid by municipality inhabitants in total amount of PIT

C/ Difference between point B and point A is multiplied by 0,75

D/ The amount set up in point B is later compensated by the amount set up in point C

E/ The quotient of the amount set up in point D and total amount of municipality share in PIT revenues is finally calculated.

Shares in Corporate income tax are not calculated that way. Municipalities obtain 5% of the CIT from the companies located on their territory. However not only location of the head office is considered but also location of all plants. If part of the plants is located in different municipalities, also part of CIT goes to these municipalities. The share for each municipality is set on basis of the share of the number of employees in given plant as compared to the total number of company employees.

Stamp duty fees are collected by designated point and later transferred directly to the bank account of the municipality. Administrative fees are paid in cash or by bank transfers directly to municipalities or communities.

Criteria and procedures

Own revenues remain the main source of capital investment , covering 32,65% of its costs. Local self-government units, own revenues and shares in national taxes can be spend accordingly to the budget plan, which has the form of the local law. Law on public finances, dated November 26th, 1998 precise the procedures for the budget construction. Project of the

regional/local budget should be prepared by the unit board and send for opinion to Regional Accounting Chamber, which supervises finances of regional/local authorities till November 15th each year. Opinion of the Chamber should be presented to local council, which accepts the budget in the form of resolution. The whole procedure of passing the Budget Resolution should be completed till the end of the year and in some special cases not later till the end of March next year. Local/regional council (Rada or Sejmik) has limited possibilities to implement the changes. It can not introduce the changes, which decrease the revenues or increase the expenses without acceptance of the local government Board.

Budget Resolution precise incomes divided by main sources and expenses divided by designated groups of expenses, like e.g. transportation, communal services, housing, health care, social assistance, public safety and others. Besides short-term investment expenses included in given group of expenses. Budget precise also long-term investment programs, with specification of all planned programs. Supplement to Budget Resolution should describe name of the investment program, its objectives and tasks which would be financed from the budget, name of the administrative unit responsible for the program, time schedule and total cost of the program, cost of the program in next two years. Budget resolutions in next years should include financial resources in the amount necessary for its execution and timely accomplishments. Investment program can be reduced or postponed by resolution of the local/regional parliament.

Accordingly to the Polish law, investment spending, like all other spending should be made efficiently, with achieving best results, comparing to expenditures, in a way which allows for timely accomplishments of investment program and fulfillment of the obligations.¹² The last statement is especially important for companies, involvement in investment program of the local authorities. According to the law, investment program should have not been started without assuring financial resources for its execution. However in practice this obligation is not always meet.

Investment expenditures should be made on the basis of the Law on public procurement According to the last amendments to the Law only relatively low expenditures, up to 3000 EUR are excluded from the tender procedures. Companies executing larger investment contracts should be selected in open tenders. If the investment contracts do not exceed 30 000 EUR contractor can be selected in so call limited tender, where only selected number of organizations are invited. This procedure can be also applied, if the specific character of investment is limiting the potential number of companies, which can accomplish it. If the open tender procedure not selected executing company, special, two phases tender can be organized. During the first phase companies can provide the offer without price. During the second phase negotiations are conducted with limited number of companies. In case the tender was canceled due to the lack of sufficient number of offers or if there is urgent request for contracting good or services tender procedure can be replaced with negotiations, assuring competitive conditions.¹³ Offers of the companies interested in participating at the public procurement process are selected by Committees, composed of the representatives of local administration. In many cases, lack of experience of its members create the problems with selection of the most appropriate offer. Thus lead to lower effectiveness of public spending on investment on local and regional level.

¹² Law on public finances, Nov.26, 1998 with further changes, § 27 p.3 , 2001.

¹³ Law on public procurement with changes dated June 22nd, 2001, Dz.Ust nr 76, 2001.

Fixed and flexible expenditures

Local and regional budget should reflect first of all its functions and should include the sources for covering the costs of designated tasks. In case of municipality/community the list of tasks includes:

- social assistance including care for disabled and poor persons, assistance to homeless,
- primary healthcare services, medical care to elderly persons, medical care during maternity,
- land management and planning,
- elementary education,
- local public transportation, maintenance of municipality roads, bridges and squares,
- water mains, sewage systems, electricity and heat supply,
- housing,
- support to local culture and sport,
- public safety, functioning of the local guards, voluntary fire departments,
- public markets,
- maintenance of municipal buildings and public facilities.

Generally municipality is responsible for responding to basic needs of the citizens.

Counties are responsible for the tasks, which due to their complexity or costs can not be efficiently fulfilled by municipality or community. They are responsible for:

- The functioning of the Family Assistance Centers, Social Care Houses
- Maintenance of county roads,
- Construction supervision, land and building register, water management, environmental protection issues
- High school education, running of the orphanages,
- Support to disabled persons,
- In the area of public safety, maintenance of police and fire stations,
- Support to cultural institutions, with activities focused on larger area than municipality. Maintenance of historical monuments,
- functioning of the public health care institutions financed by Health Funds,
- Protection of wild life,
- Functioning of the labor market and assistance to unemployed,
- Protection of the consumers rights.
- Maintenance of county public facilities

Regions are responsible for regional economic development, and thus include expenditures for elaboration of the regional development strategy, development of the regional infrastructure, investment promotion, support to businesses.

Fulfillment of the designated tasks and development of community wellbeing, besides covering current expenses, require also investment program. Some of the municipalities and counties have elaborated local development strategies, which show the directions of the local development, like e.g. tourism, which requires investments in sewage treatment system, development of local infrastructure, necessary for building, construction of the public baths, pools etc. Focus on e.g. food processing industry requires investment in infrastructure, development of agriculture commodity exchange, water sewage system etc. Elaboration of the

local development strategy is not required by the Law, however it is very useful for planning further investment.

Local/regional authorities are independent in their budgetary decision and it is up to their discretion to decide what part of the revenues would be spend on investment. Since the municipality budgets in Poland vary between less than \$ 100 000 and \$400 millions, the amount, which can be spend on investment depend also on the size of the budget. Larger municipalities have also long term investment program, like e.g. Poznań, which reserved nearly 50 million dollars for long term investment programs. Small municipalities, with poor population spend only a few percent of the budget on investment and do not plan long term investment programs. In every case decision is made by local council on the basis of materials, elaborated by the unit board.

Main problems in effecting capital investment

The main problems in effecting capital investment from local governments incomes are too low revenues comparing to the needs. Local authorities are obliged to cover currents expenses, related to designated and described above tasks, including especially salaries and other personal costs. During first six month of current year (2001) salaries and related social tax costs amounted to 51,1% of all current costs in municipalities budgets. The cost of salaries amounted also to 79,9% of the municipalities own revenues in first half of 2001.¹⁴ After covering current expenses, local governments are free to decide, what kind of investment would be included into the budget.

Besides the lack of sufficient funds, after covering current expenses, some problems are created by the lack of development strategies and long term investment programs. Strategies generally include vision of the municipality, county or region in the perspective of 10-20 years. Elaboration of the strategy is not compulsory for municipality and county¹⁵ and its related to significant costs (\$10 000 and up). Therefore only part of the local governments elaborated development strategies. Municipalities have also limited knowledge how to prepare long-term (4-6) years investment programs, which should include identification of investment needs, list of investment priorities with estimated costs. Lack of development strategies and investment programs for all local government units results in lower interest in capital investment and in lower effectiveness of investments.

We can say that local/regional governments use the EU Structural Funds principles to some extend. Their legal duties and situation of the particular community/municipality or region determine their criteria, procedures and decisions for investment spending. Whole process is more transparent and conformable to programming and partnership principles if the regional strategy exists. As we stated above, there is no obligatory for the local authority.

¹⁴ Finanse Samorządów. Ministry of Finance www.mofnet.pl.

¹⁵ It is however compulsory for regions