

Size Categories of Municipalities and Finances of Local Government in Slovakia

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1. Introduction

Local finance is one of the important factors that influence various aspects of local development. This has been particularly valid since 1990, when a new system of local government was introduced in Slovakia. Local governments have an important level of autonomy in decision-making concerning local finances. Nevertheless, the state still has strong tools available for influencing financial behaviour on the local level. The main tools are various forms of central regulation, and above all, a system of financial transfers from the state budget to the local budgets (shared taxes, state grants).

This article analyses the differences in local finances according to population size of municipalities. The great number of small municipalities in the Slovak settlement system (at present more than 2860 municipalities) is one of the problems that faces the system of local government. Particular attention will be paid to the smallest size category: rural municipalities with a population of less than 2000 inhabitants (2496 municipalities in 1995). General information concerning the development of local finance in Slovakia will also be outlined. The role of central state transfers to local budgets is documented and discussed. The main structure and two year development in local revenues and expenditures (1994-95) is evaluated. This analysis offers a better understanding of development constraints at the local level.

This type of research is determined by data availability. The most suitable documents for this type of analysis are final accounts of municipalities. These financial documents are approved by the City Council for each year, and proceed through the auditing process. This principal local finance document reveals basic financial aspects of local policy and development. Although financial data concerning municipalities are available locally without any obstacles, it would be problematic to collect a representative and standardized sample of final accounts directly from individual municipalities. The original sources of data used in this research are individual final accounts of all Slovak municipalities, as they were gathered for the Ministry of Finance of the Slovak Republic. Slovak legislation respects protection of individual data in the case of individual municipalities and their main financial records, which are collected in the central government databases. For this reason, were used aggregated data for districts (for 1994 and 1995), according to the three main population size categories of municipalities (0 to

1999, 2000 to 4999, and 5000 and more). I selected several primary items for the purposes of this analysis from available municipal final accounts aggregates. All local budgets are aggregated in two largest cities: Bratislava and Košice, taking into account the specific two-tiered structure of local government. Obviously, one can not forget the existence of large differences among financial situations of individual municipalities within one size category.

2. Local Finances and Size of Municipalities after 1989

Slovak municipalities have these main types of revenues (since 1993):

- local tax revenues (real estate tax, share on centrally collected taxes – shared taxes),
- non-tax revenues – local fees, administrative fees, other fees, credits, grants from state budget, other non-tax revenues,
- revenues from municipal property and from property of the state in municipal administration.

The state reacted to the different sizes of municipalities by applying three main approaches in Slovakia. The first approach was formulated through progressive taxation in the case of real estate tax. The second approach consisted of a different distribution of shared taxes in advance of larger municipalities. The third approach takes into account problems of smaller municipalities through specific state grants.

The entirety of the real estate tax has been a local source of revenues since its introduction in 1993. This tax has two main subtypes: a tax on buildings and a tax on land. The real estate tax is calculated by multiplying the tax base by a coefficient that takes into account the population size of the municipality and its position, or specific function (district centre, spa status) (Table 1).

Table 1. Coefficient for real estate tax calculation (1994–1995)

coefficient	size category of municipality
0.3	up to 300 inhabitants
0.6	301–600
1.0	601–1000
1.4	1001–6000
1.6	6001–10000
2.0	10001–25000
2.5	above 25 000 inhabitants
3.5	district cities, spa cities
4.5	Bratislava

Source: Bubeniková, I., 1996. Zdaňovanie nehnuteľností v praxi. Bratislava (EPOS).

Shared taxes (personal income tax, corporate tax, road tax) change almost every year in Slovakia, according to the State Budget Act. In 1993, 70 % of the revenues of the personal income tax was distributed to municipalities. This was later changed to a 29.92 % share from the physical person income tax (1994) (22.53 % in 1995; 23.6 % in 1996), and 5.87 % from corporate tax (4.51 % in 1995; 3.33 % in 1996). The amount of

these revenues was stable in absolute numbers in both years (physical persons income tax: almost 3.5 billion Sk, corporate tax: approximately 1.5 billion Sk). The relative 30 % share from the road tax has been stable since 1994. This tax is a very marginal income and must be used only for local road building, reconstruction works, etc. Later changes in respect to size category changed the distribution of shared taxes. Revenues from the personal income tax are distributed among municipalities according to the population size. The state transferred part of the yield from the corporate tax according to population size in 1994 and 1995, after multiplying by a coefficient for the particular size category of municipalities (Table 2). The share of the corporate tax allocated to the municipalities has been in the following proportion since 1996: 60 % according to the population size and 40 % according to the location of the since 1996 tax payer.

Table 2. Redistribution coefficients according to size categories (1994–1995)

Size category of community	Coefficient
up to 500 inhabitants	0.930
501 – 2000 inhabitants	0.950
2001 – 5000 inhabitants	1.000
5001 and more inhabitants	1.020
Bratislava	1.088

Source: Mikš, J., 1994. Miestne rozpočty 1994, Verejná správa, No. 3, pp. 15–16.

Small municipalities have received additional resources in the form of specific grants from the state budget. These transfers from the state budget to the small municipalities' amounted to 213 million Sk in 1993 (the total grant transfers from the state budget to the local budgets amounted to 1521 million Sk); 216 million Sk in 1994 (from total grant transfers of 1080 million Sk); and approximately 220 million Sk in 1995 (from total grant transfers of 1190 million Sk). The state distributed its support to local governments in small municipalities through non-investment subsidies, with the exact subsidy defined on a per capita basis in 1992–1993 (Table 3).

Table 3. Non-investment subsidy with respect to the size categories (1992–1993)

Size of municipality	Subsidy
communities up to 1000 inhabitants	120.– Sk per capita
communities among 1001 to 2000 inhabitants	90.– Sk per capita
communities among 2001 to 3000 inhabitants	70.– Sk per capita
communities among 3001 to 5000 inhabitants	50.– Sk per capita

Source: Buček, J., 1993. Problèmes de financement municipal en Slovaquie. Bulletin de la Societe Languedocienne de Geographie, 3–4, pp. 335–346.

This administrative system of non-investment grant redistribution to the smaller municipalities was transformed in 1994. The purpose was to compensate municipalities with poor soil quality conditions that suffered from lower real estate tax income. State

grants “for local governmental functions” were then distributed through a system combining the size/population of the municipality and a coefficient related to newly introduced soil-economic conditions as another variable that influences the level of state grant (each cadastral unit has its strictly defined average price of land for taxation purposes) (Table 4).

Table 4. Non-investment grant with respect to size category (1994)

Coefficients		Non-investment grant per capita with respect to soil-economic conditions and size of municipalities (in Sk)			
soil price scale in Sk/m ²	coefficient	Population level in municipality			
		up to 1000	1001–2000	2001–3000	3001–5000
$x \leq$	1.20	144.–	108.–	84.–	60.–
$1 < x \leq 3$	1.10	132.–	99.–	77.–	55.–
$3 < x \leq 5$	1.00	120.–	90.–	70.–	50.–
$5 < x \leq 7$	0.95	114.–	85.50	66.50	47.50
$7 < x \leq 9$	0.90	108.–	81.–	63.–	45.–
$9 < x$	0.85	102.–	76.50	59.50	42.50

Source: Mikš, J., 1994. Informácia o postupe MF SR pri rozpise neinvestičnej dotácie na krytie samosprávnych funkcií obcí v roku 1994. Verejná správa, č. 8, p. 14.

For 1996, subsidies for local government functions were planned in the amount of 250 million Sk for municipalities with a population level up to 5000 people (the proposal for 1997 is 350 million Sk with a scope changed to include only municipalities up to 3000 inhabitants). This grant helped to cover current expenditures of local government (but not wages, salaries, rewards for employees). Another typical specific grant applied in the Slovak local finance system aims to support public transport in selected large cities.

Other important sources of revenues are yields from municipal property: profit from municipal enterprises and organizations, yields from financial investments, income from municipal bonds and particularly from the selling of municipal property (primarily real estate). This is one of the main sources of income differentiation between individual municipalities. There is also quite wide group of local fees.

It is generally accepted that Slovak local governments are in systematic financial stress, with a need for particular changes especially in central-local financial relations (e. g. M. E. S. A. 10, 1995; Čapková, 1997). Table 5 demonstrates an almost stable or slightly decreasing level of revenues and expenditures from 1992 to 1995. This was during a period of higher inflation and systematically rising costs of all activities of local governments. The decrease of transfers from the state budget to the local budgets is also very visible. Slowly declining capital expenditures are another example of financial stress of Slovak municipalities. Local governments in this situation were under strong financial tensions. While in the case of big cities, the situation concerns most particularly problems such as public transport and housing, in the case of small communities this pressure threatens the basic rational existence and functioning of local government and

self-sustaining local development. The discussions concerning economies of scale, equality, justice in distribution of public resources, combined with need to protect local identity and autonomy, are permanent.

Table 5. Basic structure of revenues and expenditures of local budgets 1991 – 1995 (in million Sk)

year	own revenues	grants from state budget	revenues total	current expenditures	capital expenditures	total expenditures	balance of revenues and expenditures
1991	8,214	7,961	16,175	–	–	14,300	1,875
1992	13,993	6,582	20,627	12,123	7,547	19,670	957
1993	19,445	1,521	20,966	12,715	6,583	19,298	1,668
1994	18,993	1,080	20,073	12,861	6,237	19,098	975
1995	21,046	1,190	22,236	12,971	5,882	18,853	3,383

– data not available

Source: Statistical Yearbook of Slovak Republic 1996. Bratislava (Veda).

3. Analysis of the Structure of Local Finances according to Size Categories of Municipalities

Different income and spending patterns related to the size of municipalities can show the real situation in local financing. A comparison of revenue patterns according to the main budget items for 1994 and 1995 shows the following principal differences concerning size categories (Table 6):

Table 6. Structure of local revenues according to size categories of municipalities (in %)

population size	0–1999		2000 to 4999		5000 and more	
	1994	1995	1994	1995	1994	1995
1. total tax revenues of which*:						
a) real estate tax	49.3	43.4	46.5	43.1	35.0	28.7
b) shared taxes	14.9	13.7	14.0	13.4	7.3	6.6
c) other tax revenues	30.3	28.9	29.4	29.1	23.9	21.8
d) other tax revenues	4.1	0.8	3.0	0.6	3.8	0.2
2. Non-tax revenues of which*:						
a) credits	45.7	51.3	47.6	50.1	49.2	44.8
b) local fees	3.2	4.1	4.5	4.9	5.2	7.8
c) local fees	4.2	4.5	4.2	4.8	4.0	4.2
c) state grants	7.7	7.5	7.0	7.0	14.1	9.8
d) other	23.8	27.0	20.8	20.5	15.4	11.1
3. Municipal property yields						
	5.0	5.3	6.0	6.8	15.8	30.1

* – percentage of total expenditures

Source: Datacentrum Ministry of Finance of Slovak Republic. 1996.

- small municipalities depend much more on local tax revenues. The real estate tax has a more important position among income items compared to larger municipalities. The role of tax revenues, due to their stagnation, decreased in 1995 compared to the year 1994 (e. g. the real estate tax was below 800 million Sk for both years),
- there is a rising share of non-tax revenues in the case of small municipalities, as observed in Table 6. This is different compared to large municipalities. Among non-tax revenues, growth of credits is higher in the case of large municipalities. This is related to the lower borrowing capacity of small municipalities (low budgets, property of low value). Local fees create almost the same share of incomes in all size categories. State grants are almost stable for small municipalities and their share decreased much more in large municipalities (for public transport). Income from “other non-tax revenues” is very high in small municipalities (mostly accumulated resources from previous years), compared to the large municipalities’ budgets,
- yields from municipal property are very low in the case of small municipalities (about 5 %) compared to the yields achieved in the category of population greater than 5000. The scope of land and buildings that small municipalities own is not comparable to the property that larger cities have. They do not have much chance to sell or rent municipal property (weaker demand, they have to accept lower prices). For example housing was concentrated mostly in the cities, so small municipalities cannot receive income from selling municipal flats. Their municipal enterprises and organizations are not profit oriented; more often they must be subsidized.

Table 7. Structure of local expenditures according to size categories of municipalities (in %)

population category	0–1999		2000 to 4999		5000 and more	
	1994	1995	1994	1995	1994	1995
1. current expenditures:						
of which*:	68.4	70.1	64.0	68.6	67.6	68.3
a) budgetary organization	31.8	29.2	34.1	32.8	28.9	24.4
b) subsidized organization	2.4	2.3	4.9	5.8	12.6	12.7
c) self-government	31.2	34.9	20.5	23.8	12.4	15.1
d) financial operations	2.5	3.5	3.4	4.9	6.1	7.3
2. capital expenditures:						
of which*:	31.6	29.9	36.0	31.4	32.4	31.7
a) development programmes	30.4	29.1	33.5	28.4	20.7	21.3
b) housing	0.7	0.4	1.9	2.7	6.4	4.5
c) grants to legal entities	0.0	0.0	0.0	0.0	2.5	3.7

* – percentage of total expenditures

Source: Datacentrum Ministry of Finance of Slovak Republic. 1996.

There are also significant differences in expenditure patterns according to the size categories of municipalities (Table 7). The findings can be summarized in the following points:

- current expenditures are almost the same in all size categories and are growing slightly towards the level of 70% of all expenditures,
- the internal structure of current expenditures is quite different between the size categories. Small municipalities spent more on budgetary organizations (almost fully dependent on subsidies from local budgets). The most important difference is the very high and growing level of spending on the basic functioning of local government (about one-third), i.e. running of their offices, wages, paying basic services etc. in small municipalities,
- capital expenditures create almost one-third of total expenditures in all categories. Small municipalities spent only a marginal share on housing and grants to other legal entities, compared to the large ones. In this category capital expenditures are slightly decreasing.

Table 8 offers a chance to add a more realistic dimension to the previous structural comparisons of local revenues and expenditures. In the case of small municipalities the general structure of expenditures consists of one-third spent on budgetary and subsidized organization, one-third on local government and one-third on capital expenditures. In a hypothetical (average) municipality with 500 inhabitants, the average annual expenditures are approximately 1.5 million Sk (average expenditure per capita is about 3 thousand Sk, see Table 8). We can hardly speak about "development" in this situation,

Table 8. Balance of local revenues and expenditures according to size categories (in thousand Sk)

population category	0-1999		2000 to 4999		5000 and more	
	1994	1995	1994	1995	1994	1995
Total revenues	5,377,118	5,711,686	2,447,579	2,522,766	12,247,873	14,001,502
average revenues per capita	3.311	3.542	3.475	3.539	5.252	5.985
average revenues per municipality	2,156	2,288	10,241	10,297	101,222	115,715
Total expenditures	4,885,876	4,932,774	2,310,399	2,291,661	11,901,441	11,628,527
average expenditures per capita	3.009	3.059	3.280	3.215	5.103	4.971
average expenditures per municipality	1,959	1,976	9,667	9,354	98,359	96,104
Balance (revenues-expenditures)	+ 491,242	+ 778,912	+ 137,180	+ 231,105	+ 346,432	+ 2,372,975

when 0.5 million Sk is spent on local government, 0.5 million Sk is spent on municipal organizations (mostly those that are unavoidable for local life, such as kindergarden, or library etc.), and only 0.5 million Sk goes to capital expenditures, e. g. development investments (currently in Slovakia, e.g. an average new family house costs approximately 1.5 million Sk).

4. Conclusion

There are clear signs of financial difficulties at the local level: the rising level of credits and subsequent rising debt payments, decreasing subsidies to the budgetary and subsidized organizations, decreasing level of capital expenditures. Decreasing expenditures and rising surpluses of all municipal budgets emphasize the rising need for long term accumulation of finances and influence of occasional incomes (selling municipal property). Basic financial problems concern all Slovak municipalities and the core issue is the level of transfers between central state and local budgets (almost 7,5 billion Sk of shared taxes and grants in 1995) and central state regulation of many other local taxes and fees (slowly changing maximum limits defined by state legislation).

The state reacted to the huge size differences between municipalities by taking into account different problems at each pole of the settlement system. The response of the Slovak state in 1994–95 (which has not changed very much since that time) to the problems was not sufficient. In the case of small municipalities, it is necessary to protect the existence of a crucial local institution: local government. Although the financial situation of small municipalities looks positive (higher surplus, lower credits), there are signs that are not so easy to assert. Small absolute size of budgets of these tiny municipalities in absolute terms forced them to accumulate financial resources for more years for each eventual larger investment, e.g. in municipal infrastructure (and even then to combine their own resources with bank credits and eventual specific state grants). The capacity for particular aspects of development are very limited in the case of small municipalities. The state protects the institution of local government to a limited degree, but has not created suitable conditions for more autonomous, self-sustained development of small municipalities. Real estate taxes and state subsidies (shared taxes, grants) can not remain unchanged in absolute terms and their growth is needed (e.g. the inflation rate was not respected through eventual valorization of subsidies). The situation in which local governmental institutions and administrations operate in almost each village leads towards an unreasonably high portion of spending on “operational” costs. More reasonable spending, particularly in the case of current expenditures, is also needed (e. g. decrease of expenditure by means of intermunicipal cooperation in the field of administration and deliverance of public services).

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VEĽKOSTNÉ KATEGÓRIE OBCÍ A FINANČIE MIESTNYCH SAMOSPRÁV NA SLOVENSKU

R é s u m é

Slovenský sídelný systém typický veľkým počtom menších obcí sa odráža vo veľkom počte samosprávnych obcí. Príspevok sa venuje rozdielnej situácii v miestnych financiách podľa troch veľkostných kategórií obcí (0–1999, 2000–4999, 5000 a viac obyvateľov) v r. 1994 a 1995, so zvýšenou pozornosťou malým obciam do 2000 obyv. Po charakteristike hlavných položiek miestnych rozpočtov, predstavuje tri základné prístupy štátu zohľadňujúce veľkostné kategórie obcí, ktoré sa prejavujú v príjmoch obcí – podporu väčších obcí v oblasti podielových daní, progresívne zdanenie daňou z nehnuteľností s rastom veľkosti sídla a štátnu neinvestičnú dotáciu na výkon samosprávnych funkcií v menších obciach do 5000 obyvateľov.

Štruktúra miestnych rozpočtov (sledovaná podľa záverečných účtov) upozorňuje na rozdiely medzi veľkostnými kategóriami obcí. Malé obce viac závisia na transferoch od štátu (vyšší podiel daňových príjmov) a zaoštvávajú v podiele výnosov z obecného majetku, oproti väčším obciam. U výdajov je významný vysoký podiel bežných výdavkov. V ich rámci zaujal vysoký podiel výdajov na samotný chod samosprávy obcí. Výsledky analýzy vedú k záveru, že štát síce podporuje existenciu samospráv malých obcí, ale nevytvára dostatočný priestor na ich autonómny, systematický a sebestačný rozvoj. Pre zlepšenie efektívnosti financovania malých obcí je potrebné zvýšiť rozsah štátnych subvencií (vo viacerých formách), s doplnením o racionalizáciu miestnych výdajov (napr. prostredníctvom interkomunálnej spolupráce).