AN APPROACH OF LOCAL FINANCIAL AUTONOMY AND IMPLICATION OVER SUSTAINABLE DEVELOPMENT IN THE KNOWLEDGE SOCIETY

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Abstract: Local governments play an important role in sustainable development processes based on their administrative and financial autonomy. Policies and programs undertaken to assure sustainable development by local governments produce benefits for persistence of the knowledge society. This paper will try to highlight the implication of local financial autonomy over sustainable development of local communities in a knowledge society, based especially on local financial autonomy theory approach.

Keywords: financial autonomy, sustainable development, local communities, knowledge society

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1. INTRODUCTION

World historically, “sustainable development” is omnipresent, and recently it has become an ideology in connection with “knowledge society” in a fast-changing national and international market forces context. Local governments depend upon being able to respond to new market opportunities, based on idea that every society is a knowledge society (McElhinney, 2005; Casey, 2006; Bhargava, 2007). Based on their local financial autonomy, local governments needs to identify their own economic strengths and to use own resources in the implementation of a realistic local development strategy.

The paper is structured as following: Section 2 reviews the theoretical approach of the local financial autonomy; Section 3 discusses some implication over sustainable development of financial autonomy in a knowledge society; Section 3 concludes the main ideas of the theme, as final remarks.

2. THEORETICAL APPROACH OF LOCAL FINANCIAL AUTONOMY

The process of decentralization in the public sector economy - which supposes an increase in the financial independence of local authorities, separating the functions of the local
and central government in the public sector of economy, adequately distributing the financial resources for the realization of these functions - takes the shape of so-called fiscal decentralization (Davulis, Peleckis, Slavinskaitė, 2013). The level of the fiscal decentralization characterizes the degree of independence of local government, where local government is independent as much as it has financial resources to fulfill its functions (Davulis, Peleckis, Slavinskaitė, 2013), so-called local financial autonomy. Financial side of local autonomy emerges from the definition offered by the European Charter of Local Self-Government and shall result in conferring certain powers and responsibilities to local authorities. In other words, financial autonomy is realized by disposing of sufficient resources to ensure their own expenses and at the same time to achieve the decentralized powers with the help of local public finance. The local autonomy cannot be implemented only under conditions in which local authorities have adequate financial resources as "the financial side is an important component of local autonomy, which exert an influence on the ability of local authorities decision" (Voinea, 2008, p.47) or "local autonomy implies the right of local authorities to dispose of financial resources, to use them and manage to fulfill the duties prescribed by law, to develop the budget, to pursue implementation of the budget called financial autonomy" (Voinea, 2008, p.45).

Agnes Sauviat (Pauliat, 2004) states that local financial autonomy is one of the basic conditions of a real management freedom that is not a way to manifest independence from the state, and requires to the state to guarantee a stable and enough resources that allows the local community to exercise fully and relevant the decentralized competences. In these circumstances, to support these competences at a cost, local authorities must identify their sources of income and to prepare expenditure programs. Based on these interrelations, autonomy in financial terms can be defined by combining three elements (Guengat and Uhaldeborde, 2003; Gilbert, 1999): autonomy of local expenditure, autonomy of local revenues and local budget autonomy. Local revenue autonomy implies the right and ability to determine the types of taxes, tax base, tax rate. Local expenditure autonomy implies the right and ability of local authorities to determine the nature and size of local public expenditures on public goods and services in line with demand, and the right and ability to perform expenses, manage local property. Local budget autonomy implies the right and ability of local authorities to adjust the income level of public spending severely according to the areas of competence of local authorities, based on the current generation of paying taxes, but also the next generation liable for payment of interest rate of local borrowing. Budgetary autonomy implies the right and ability of local authorities to achieve a statistically and dynamically budget over which assumes financial responsibility.

We note that such a definition would require local authorities to decide absolutely free on local revenues and expenditures reflected in the local budget, which is quite difficult to achieve given that, in practice, the central public authorities in most of countries maintain a fairly high volume of public activities and mobilize the most important sources of income. Therefore, in the spirit of local autonomy, powers and responsibilities (Filip et al, 2002) in local public funds entrusted to local authorities are limited to: development and approval of local budgets deadlines; settlement, collection and follow up of taxes under the law; follow up execution of budgets and rectified during the budget year; establishing and monitoring how public services to enhance their effectiveness for citizens; efficient management of public and private assets of administrative-territorial units; management of financial resources during budget implementation in terms of efficiency; establishing options and priorities and approve the expenditures from
local budgets; development, approval, modification and implementation of development programs in view of the administrative-territorial management as the basis of the annual local budgets; organisation of the own financial control on own management, on management of subordinate institutions and on public services.

In support of financial side of autonomy and for local finance to standardize European states, the European Charter of Local Self-Government offers several guidelines (Law no.199/1997, Art.9) on formation and management of financial resources. These recommendations are framed by some authors in the category of principles underlying the formation and administration of local financial resources, since the adoption of the Charter in the national/internal law.

If it is just the financial side view of local autonomy, it is distinguished by the following features (Voinea, 2008, p.47):

- Ensure the right of local authorities to develop, approve and execute its own budget for each financial year;
- Regulation of powers of local authorities to determine and manage their own revenues from taxes, fees, contributions under the law;
- Follow up budget execution and local budgets rectification during the budget year;
- Background and approval options and priorities to finance the costs of local budgets;
- Using the financial resources of local authorities during budget execution in terms of efficiency;
- The right of local councils to establish special fees for the operation of local public services;
- The right of local authorities to decide on loans contracted under the law.

The size of the financial side of the local autonomy is dependent on the delimitation of powers of local government in providing public services, the diversity and quality of public services, the development programs of the administrative-territorial, the level of own revenues of administrative-territorial units, by improving management expenses from local budgets. Legal and financial autonomy materializes in establishing local authorities as separate legal entities, endowed with its own budget, independent financial willpower, regulatory sovereignty in the area of financial management and prevent central government control (Labie, 2005, p.7).

Local Public Finance Law (Law no.273/2006, Art.16) of Romania provides financial local autonomy as a principle that the administrative-territorial units are entitled to sufficient financial resources that local government authorities can use in the exercise of the basis and within the limits prescribed by law and that local government authorities have the power to establish levels of local taxes under the law. The financial autonomy in the administrative-territorial units should be seen through the legal element, on the one hand, and in terms of economic-material element, on the other hand. The legal implies approaching financial autonomy as discretion under the legal regulated at the national level (law, ordinance, etc.) and the level of administrative-territorial unit (Local Council Decisions, Decisions by the Mayor) and an economic element material financial implies approaching practical side of autonomy expressed by local authorities ability to maintain budget balance.
The main idea underlying the financial side of local autonomy is that revenues must cover expenditure during a fiscal year. So the amount of revenues determines the possibility of making of local public expenditures and at the same time reflects the degree of autonomy in their report appearing between revenues, transfers of funds from the state to balance local budgets and loans. If the share of own revenues in total local revenue sources is higher, the administrative-territorial unit is free to spend as they wish to ensure coverage of public needs, which translates into a large financial autonomy.

In other words, measuring the financial side of local autonomy was the subject of research as a result of the approach to measure the relationship between decentralization and different macroeconomic variables. Thus, in particular, on the financial side of autonomy, a number of qualitative and quantitative indicators have been established in recent years to measure the relative position of administrative units within the perfect sovereignty teritorial and total financial independents. Many of these indicators, however, are criticized, because not fully cover all components of autonomy.

Until around the year 2000 almost all studies have used financial statistics of the International Monetary Fund as a starting point in measuring financial decentralization. The dominant pattern used compares the local expenditures / revenues with the total expenditures / revenues at national level, or alternatively, with gross domestic product (GDP). These indicators relatively simple are in use today (e.g., Eurostat), although Ebel and Yilmaz 2002, Meloche in 2004, the World Bank in 2007 showed disadvantages of these indicators such as:
- For revenue does not make a difference between different sources of local revenue. The nature and degree of local autonomy may be perceived differently depending on sources of revenue. At the same time, does not specify what percentage of transfers are allocated to general and specific objectives.
- For expenditure not distinguish between mandatory and optional expenditure. For mandatory expenditure, even if they appear as local expenditures in the decentralized local communities, local authorities are in this case only state agents who have limited powers. It also, transfers from other levels of government appear in the functional expenditure.

These deficiencies of the indicators generates an overestimation of the degree of decentralization and local financial autonomy.

Organisation for Economic Co-operation and Development (OECD) in 2001, has developed a new model for measuring revenue autonomy applied in the Member States, but did not try also a model for expenses.

3. IMPLICATION OVER SUSTAINABLE DEVELOPMENT OF FINANCIAL AUTONOMY IN A KNOWLEDGE SOCIETY

Local governments are the initiators of local sustainable development processes, because on the medium term their presence is of fundamental importance for establishing the institutions that these processes require. Local governments are the most legitimate local public authorities responsible for mobilization and participation of local actors and forming teams of leaders to ensure local sustainable development. Local sustainable development thus calls for decided action by the local public bodies, which suggest the strengthening of local autonomy. In their quality of autonomous authorities, local governments have the possibility of the enhancement of
the endogenous resources of each local area in production activities and encouraging the establishment of new local enterprises based on high quality and differentiation of products, production processes and services. Based on their financial autonomy, local government programs for sustainable development include a wide range of initiatives, as programs designed to improve the human capital of individual workers, or can be created new financing instruments to meet the needs of local micro and small enterprises. One of the main implications of local authorities based on their autonomy in sustaining the sustainable development process is the establishment of local networks among public and private actors and promoting scientific and technological development activities in order to develop production and business innovation in their local community, for facilitating the increase of the efficacy and efficiency of local development activities. Local autonomy is ‘responsible’ for identifying new sources of employment and income at the local level. In the power of local authorities is also the sustainable development component of environment, where local governments are responsible to search for strategic accords on environmental goods. The reliable incorporation of the three elements of sustainable development (economic, social and environment) using financial autonomy can create the premises for the development of knowledge cities. The approach of local investments for a sustainable development need longer lead times than electoral and political cycles (Alburquerque, 2004).

In this context, one of the main strategic objectives in the formulation of a local sustainable development strategy is the accent put on innovation as an objective itself and the identification of innovation needs of the local production system (also at the level of human resources) through the incorporation and development of management innovations strategy. Effective local management innovations strategy of sustainable development requires careful targeting of the limited public funds. In this context, an important place is according in whole process to local financial decisions because local policymakers must have sufficiently resources for the use in the exercise of the basis and within the limits prescribed by law. Effective measure that must be taken are “increasing jobs located in the city” and diversifying the local economy. Especially, expenditures for social and cultural activities have an influence on economic development as they contribute to the maintenance, restoration and development work capacity of individuals to training and raising their qualifications, the reproduction of labor (Petrișor, 2014).

Bartik (Chapter 2) shows that on average 10% reduction in state and local business taxes increases local employment and business activity in the long-run by around 3%. Lowering the tax rate on labor and production and consequently on the income tax base causes a positive economic effect (Durdureanu, 2014). Some studies find that business tax reductions, if financed by reducing spending on local education or roads, may reduce a local economy's employment (Helms, 1985; Munnell, 1990; Bartik, 1989). In our opinion, tax differentials in urban areas have large effects, because a constant in lowering property taxes in one urban area, holding bigger the property tax rates of other urban areas, may increase the business activity in that individual community. This point of view is sustained from the perspective of an individual to buy a property, to develop a business and a business to choose a location.

What is sure in practice is that countries of a high level or old decentralization which in time have developed long-term strategies of sustainable development, succeed to have a sustainable development at local level. This idea is sustained by empirical evidences. For example, Denmark local governments have considerable autonomy to operate within overall
expenditure limits and priorities in selected areas such as social services, primary education or primary health care, without reference to or interference from central government.

The center of gravity of financial decisions moved to local budgets in the majority of the European Union countries, based on local financial autonomy and exclusive competences.

Even local taxes are one of the major conditions of fiscal decentralization, as well as extension of independence of self-government, grants and subsidies remain the main source of European local public sector revenue and in few EU countries (e.g. Malta, Romania and Bulgaria) accounted for over 70% of revenue. In Germany, the principles of taxation, and assessment procedure in particular, are controlled by statute; the major local taxes being on real estate and on industry.

Local public expenditure and local public revenue of the EU countries fluctuated around an average of approximately 12% of GDP over the period 2007-2013.

**Table 1 Local public expenditure (E) and revenues (R) as % of GDP in the EU countries over the period 2007-2013**

<table>
<thead>
<tr>
<th>Country/Year</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria (AT)</td>
<td>7.4</td>
<td>7.5</td>
<td>7.6</td>
<td>7.7</td>
<td>8.2</td>
<td>7.9</td>
<td>8.0</td>
</tr>
<tr>
<td>Belgium (BE)</td>
<td>6.6</td>
<td>6.8</td>
<td>6.7</td>
<td>6.9</td>
<td>7.1</td>
<td>7.2</td>
<td>7.0</td>
</tr>
<tr>
<td>Bulgaria (BG)</td>
<td>6.6</td>
<td>6.5</td>
<td>7.3</td>
<td>6.9</td>
<td>8.6</td>
<td>7.7</td>
<td>7.0</td>
</tr>
<tr>
<td>Croatia (HR)</td>
<td>11,</td>
<td>11,</td>
<td>11,</td>
<td>11,</td>
<td>12,</td>
<td>11,</td>
<td>11,</td>
</tr>
<tr>
<td>Cyprus (CY)</td>
<td>1.9</td>
<td>1.9</td>
<td>1.9</td>
<td>1.8</td>
<td>2.2</td>
<td>2.1</td>
<td>2.2</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>10,</td>
<td>11,</td>
<td>10,</td>
<td>10,</td>
<td>12,</td>
<td>11,</td>
<td>11,</td>
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<tr>
<td>Estonia (EE)</td>
<td>9.5</td>
<td>9.0</td>
<td>10,</td>
<td>9,</td>
<td>11,</td>
<td>10,</td>
<td>10,</td>
</tr>
<tr>
<td>Germany (DE)</td>
<td>7.3</td>
<td>7.7</td>
<td>7.4</td>
<td>7.8</td>
<td>8.1</td>
<td>8.0</td>
<td>7.9</td>
</tr>
<tr>
<td>Greece (EL)</td>
<td>2.7</td>
<td>2.6</td>
<td>2.9</td>
<td>2.8</td>
<td>3.3</td>
<td>3.3</td>
<td>2.9</td>
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<tr>
<td>Hungary (HU)</td>
<td>11,</td>
<td>11,</td>
<td>11,</td>
<td>11,</td>
<td>12,</td>
<td>11,</td>
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<tr>
<td>Ireland (IE)</td>
<td>7.3</td>
<td>7.1</td>
<td>7.8</td>
<td>7.4</td>
<td>7.1</td>
<td>7.1</td>
<td>6.4</td>
</tr>
<tr>
<td>Italy (IT)</td>
<td>14,</td>
<td>14,</td>
<td>15,</td>
<td>15,</td>
<td>16,</td>
<td>16,</td>
<td>15,</td>
</tr>
<tr>
<td>Latvia (LV)</td>
<td>11,</td>
<td>10,</td>
<td>12,</td>
<td>11,</td>
<td>12,</td>
<td>11,</td>
<td>10,</td>
</tr>
<tr>
<td>Lithuania (LT)</td>
<td>8.3</td>
<td>8.0</td>
<td>9.3</td>
<td>9.1</td>
<td>10,</td>
<td>10,</td>
<td>11,</td>
</tr>
<tr>
<td>Luxembourg (LU)</td>
<td>4.7</td>
<td>5.0</td>
<td>5.1</td>
<td>5.5</td>
<td>5.8</td>
<td>5.7</td>
<td>5.4</td>
</tr>
<tr>
<td>Malta (MT)</td>
<td>0.6</td>
<td>0.6</td>
<td>0.5</td>
<td>0.5</td>
<td>0.6</td>
<td>0.7</td>
<td>0.6</td>
</tr>
<tr>
<td>Netherlands (NL)</td>
<td>15,</td>
<td>15,</td>
<td>15,</td>
<td>15,</td>
<td>17,</td>
<td>16,</td>
<td>16,</td>
</tr>
</tbody>
</table>
Local public investment in the EU countries fluctuated around an average of approximately 2.22% of GDP over the period 2007-2013.

Regarding local budget autonomy, theory (Beer-Tóth, 2009) specifies that a weak local budget policy can seriously compromise the stability of the national economy. Against the background of economic growth, perspectives of financial stability, steady prices, low unemployment rate, the currency displays an appreciation tendency (Toderașcu, 2014).

One of the relevant elements of weaknesses is indebtedness without limits, on inadequate structures and for covering state’s unproductive expenditure, while promoting with caution and on appropriate destinations, public indebtedness can prove to be an enhancing factor for national economy’s growth and development (Bilan, Roman, 2014). The indebtedness in excess may affect the economic growth rate, while budgetary expenditure on interests can affect local public authorities’ ability to carry out other types of public expenditure, with negative social consequences (Bilan, Roman, 2014).

Regarding borrowings as extraordinary income and their contribution to strengthening local autonomy, we find as defining for their reflection in this direction, the prudential rules which set limits of the indicators such as public debt service, indebtedness, fiscal pressure, and macro and microeconomic other indicators that determine compliance with the convergence criteria of the Maastricht Treaty. In this context, the autonomy of local authorities to contract and manage loans is higher as these prudential rules are less restrictive and leaves local authorities to borrow "rational" in terms of efficiency by realizing the "golden rule" of budget balance that local authorities should not be in debt to cover current costs, but can borrow prudently to achieve capital expenditure. Also, to support a high degree of local autonomy, freedom to contract and guarantee loans must be accompanied by a completed specialized external control reports as a recommendation (Cigu, 2011).

4. FINAL REMARKS

In the last years is highlighted a reform process towards decentralization and emphasized the strengthening of financial autonomy, the obvious tendency to increase the share of own revenues in total revenues of local budgets, and the predominance of unconditional transfers than
conditional transfers. Also note that in most countries the first level of local government (municipalities) has exclusive competence as regards rural development and urban planning (except Greece, Luxembourg, Portugal), water and sewage (except Italy, the Netherlands), household waste (excluding Greece, Ireland), social services (except France), sports and leisure (except the Czech Republic, Greece, Luxembourg). We find that the majority of EU states exercising shared competences in education and health sector, which is a reflection of manifestation framework of the rule of law, where the major powers need to be addressed in a national context. On the second level of local government structures, powers are exercised in terms of health, education, culture, roads and highways, and economic development. In countries where there are third tier of local governments, they have functions in terms of education, roads, culture and economic development. Also, we find that an area of national importance, such as defense, is a competence which implies the involvement of the central authorities, without creating an exclusive competence of local authorities in any EU country.

In this context, it is necessary to finalize the reform of local government finances in terms of local autonomy for ensuring local sustainable development. Thus, the implementation of local autonomy must be clearly delineated responsibilities of operating and financial management at every level of local administration, creation of stable local tax revenues, supported by a framework of fiscal relations transparent, efficient and compatible with the objectives of macroeconomic stability. A viable solution would be to build a local financial system that have the elasticity needed to allow permanent adaptation to the changes that will occur in terms of the economy in the coming years and the progressive reduction of restrictions on local authorities in matters of local finance management, encouraging them to rationalize the use of revenues and enhance political accountability for performance in managing their finances.

References


