

Meeting the Challenges of Public Financial Management in the Enlarged EU



By **Slawomir Zalobka***, EIPA 2006-present

Public financial management is continuously in the spotlight within the European Union and elsewhere. Given the importance of meeting these challenges, EIPA has set up a new Antenna in Warsaw in order to train a broad array of public servants by the sharing of knowledge and experience in this field. Since the Antenna has only been created in 2006, this contribution will focus on how we anticipate that it will contribute to the broader activities of the Institute.

Let us start with some broad principles. When in a private enterprise the finances and supplies are badly managed, its effectiveness decreases, operational costs grow, and resources for investment diminish. In effect, the company loses its competitiveness. If the company does not undertake actions to correct this, the harsh laws of the market will quickly eliminate it. This is reflected by the fact that the goal of commercial enterprises is to maximise profit. Financial management is therefore always judged on this criterion.

Within the public sphere, profit maximisation does not play a decisive role, and hence different criteria apply. Broadly speaking, public finance consists of all economic phenomena concerning accumulation and spending of money supplies (within the state budget and budgets of other entities of the public finance sector) in order to satisfy social needs and to fulfil the constitutional duties of the local, governmental and state power. In the case of public finance management, besides the purely rational approach to maximising the utility of the available funds, additional elements such as the preservation of social justice and political stability also have to be considered. The necessity of taking into account so many factors which are very difficult to measure and potentially unstable over time implies that public financial management is very different from managing private enterprises. Its goal is also different: public finance management focuses on achieving stable economic growth, which should be accompanied by the growth of the standard of living.

The public and private sectors frequently overlap since, for example, the state budget and other parts of the public finance sector are often significant participants in the market economy, both in terms of demand and supply. Hence, they may deliver a certain amount of services required by the citizens and they influence the financial market by receiving credits to finance a budgetary deficit.

In the case of public finance we are dealing with a stream of resources coming into the treasury from the public contributions by citizens on the one hand and, on the other, expenditure of the institutions in the public finance sector in pursuit of the tasks entrusted to them by the state. Often public finance management tends to be associated with the spending side. However, this is a simplification since an effective and efficient tax system is equally important. The aim of an effective tax system is to acquire financial sources with minimal inconveniences or negative consequences to the taxpayers, but also in a way that



Photograph taken on the occasion of the signing, in Warsaw on 30 March 2006, of the agreement between the Government of the Republic of Poland, represented by Mr Jan Pastwa, Head of the Civil Service, the National School of Public Administration (KSAP), represented by its Director, Mrs Maria Gintowt-Jankowicz, and EIPA, represented by its Director-General Prof. Dr Gérard Druesne.

keeps the costs of tax collection low. The tax system should not only fulfil its obvious fiscal functions, but it should also be designed in such a way that it supports the development of the economy. Creating (and continuously adapting) such a tax system is one of the major objectives for managers of public finance. This is not only a national issue: in our times of globalisation the level of taxes has great influence on the level of foreign investments in a given country.

The significance of global tax competition can be seen by the ongoing debates within the European Commission on the standardisation of direct taxes or, at least, a standard way of defining the tax base of the Member States. From the above it is clear that managers of public finance dealing with tax system design must possess broad knowledge of both the European regulations as well as the prevailing local conditions.

It was mentioned above that any tax system should be efficient and friendly to the taxpayer. To achieve that, a well-trained and well-managed staff is required, because the final income level of the constituent parts of the public finance sector depends on the quality of its staff.

However, the quantitatively more substantial field of operations in the realm of public finance is to be found on the spending side. In all European countries there is an overarching need to organise the rules of calculating expenditures, to limit those rules and to better utilise them, so that the effectiveness of public expenditure will be increased and overall expenditure can be reduced. In other words, it is necessary to create an effective system of public finance management while taking into account the factors characteristic to a given society. A significant complicating factor is the fact that it is extremely hard to create the right indicators of "effectiveness" of public expenditures, especially in the case of services delivered to society. Many international organisations (OECD, IMF) and academics have pointed this out. Therefore, the results of public finance management in terms of prescriptions for effectiveness are difficult to define.

But apart from those limitations we can say that the process of creating good management of public finances can be helped by basing it on the principle of the "three Es": efficiency, economy and effectiveness. In addition, a so-called performance budget can be instrumental to a more efficient attainment of the government's programmes.

Hence, for proper public finance management one should possess knowledge allowing the public servant to propose and subsequently implement systematic changes in the framework of public finance, as well as legislative changes, and to exercise activities in all spheres of social life that use public sources. The goal here is not to simply cut off spending, but to create mechanisms that will lead to more effective usage of the available sources, so that the diminished sources allow not only small, but perhaps even larger effects.

Also, one should not forget that the majority of countries have debts. It is important to manage public debt effectively since it can either stimulate economic growth or it can be a burden to it. This management is extremely important for the new and aspiring Member States of the EU. If we take Poland as an example, its accession to the EU in May 2004 had a remarkable impact on the conditions in which the management of public debt takes place. Two of the most important aspects influencing management stem from the financial flows connected with the membership of the EU and changes in the environment in which the management of public debt takes place, including the growth of Poland's credibility and the gradual integration of the internal market of stock and bonds with European ones. So, in order to effectively manage public debt, to minimise operational costs, one should possess broad knowledge in the field of public finance as well as great comprehension of the situation on the international financial markets.

Membership of the EU has helped to define the direction of development of the countries of Central and Eastern Europe, who collectively assumed the challenge of levelling the differences between themselves and the fifteen "old" Member States. They are not alone in this process however, because through its Cohesion Policy the European Union consistently strives to level the standard of living of the citizens of the individual regions of the united Europe. The budget of the Communities is created by all EU Member States and the means reserved



for the Cohesion Policy are substantial. It is therefore of no surprise that the European Commission is keenly interested in the way the EU money is spent. First of all, these means can be used only for purposes that serve the Community as a whole and especially those projects that promise advantageous multiplier effects. The next important determining condition for EU support is the co-financing of projects using Community and Member State funding. This can have positive effect on the public finance of the countries involved as well as providing them with strong incentives to find the means for socio-economic development. Naturally, those means should be managed in a way that guarantees their most effective and law-abiding use.

Hence, the most effective allocation and usage of the means available in the framework of the Cohesion Policy are of great interest for the EU. Obviously, the means we discuss here are being managed by the Member States through their public administrations who should be properly qualified for the tasks at hand.

This brief overview illustrates the range of challenges that members of public administrations face while dealing with public finance, regardless of whether they are taxes, expenditures of public debt, managing the means available for absorption of EU funds, as well as proper technical estimation and checking / auditing of all of these complicated operations. To meet these formidable challenges, the Warsaw Antenna aims both to provide specialised training and to create a centre for the exchange of knowledge and experience about public financial management. By creating this Antenna, EIPA is giving a clear signal that it is ready to take part in the difficult and long-lasting process of building a modern, competent and effective financial administration for the enlarged Europe. ::

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- * Slawomir Zalobka, Director of the European Centre for Public Financial Management, EIPA's Antenna in Warsaw.