

THE IMPACT OF PUBLIC MANAGEMENT ON THE EFFECTIVENESS OF PUBLIC FINANCES AT THE LOCAL LEVEL



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ABSTRACT

The main purpose of the paper is to show the relations between the management method practiced by the public authorities and the efficiency of public finances carried out at the local level. The paper has been prepared on the basis of literature and copyright research on the effectiveness of financial management in Polish local government. A descriptive method and the results of economic and statistical analyses have been used in the work. Authorities applying the administrative management model are characterized by passivity and reluctance to use innovative methods of management. They apply a one-year financial planning cycle and perform cost analyses to a very limited extent. Local governments applying the strategic management model use modern and effective methods of financial planning in financial policy, also in the multi-annual arrangement, and constantly carry out financial analyses. The practice of public financial management at the local level shows the impact of public management on the effectiveness of financial policy and budgetary economy at the local level. The paper refers to the theory of public finance and efficiency of local public financial management. The conclusions of the paper can be applicable for the practice of finances of the local self-government.

KEY WORDS

public management, local finance, local government

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INTRODUCTION

Public sector entities operate in conditions of limited budgetary resources in relation to the existing current and future development needs. In the situation of intensifying spending pressures, the reduced size of public funds, it is necessary to analyse the effectiveness of budget management, allowing for more efficient use of available resources. In such circumstances, the question is to what extent public authorities are able to skilfully use local socio-economic potential and possessed financial resources. These problems can be analysed in different planes – revenue collection, allocation of expenses, shaping the financial result and debt levels, as well as the use of property resources.

With this in mind, an important task is the search for the relationship between the decisions of local authorities, and the efficiency of their budgetary

economy. In particular, it is worthwhile to pay attention to the demonstration of the relationship between the management model practiced by public authorities, and the quality of the collection and spending of budget funds.

In recent decades new trends have appeared in public finance management focusing on the introduction of management methods aiming at directing activities to the rational and efficient forms of management. An open question is whether the new trends in public finance management, with an emphasis on improving the definition of policy objectives, detailed scheduling of tasks, monitoring the progress of their implementation and control of the achieved results, are applicable in the practice of functioning of the public sector at the local level.

In this publication, an attempt is made to show the relations between the management model practiced by Polish local public authorities and the efficiency of public expenditure carried out at the local level.

To this end, traditional and innovative methods of management in the public sector will be discussed, with the demonstration of their advantages and disadvantages, and with the analysis of the effects of their use in practice.

1. PUBLIC MANAGEMENT THEORIES AND THE EFFECTIVENESS OF MANAGEMENT

Public management is a discipline of science whose main focus is the management of public sphere organizations at different levels of their operation. It deals with the study of methods and harmonization of activities ensuring the proper setting of goals of organizations making up the public sphere and the rational use of resources for the realisation of public interest. Public management as a distinct academic discipline in theoretical approach appeared in the 80s of the twentieth century (Brudney, 2000, pp. 4-6). Its essence was an attempt to integrate elements of business and general management with elements of political science and public administration. In-depth theoretical analyses of organizations forming the public sector conducted in this field led to the formulation of recommendations for practitioners of public management.

In the economic theory, we can find the basis of the management discipline in the public sector mainly in: the public choice theory, the stakeholders theory and the transaction cost theory (Kozuch, Sułkowski, 2015, p. 25).

In the public choice theory, the most significance is given to the analysis of decision-making processes undertaken by the authorities. In particular, this approach focuses on the study of how decision makers use public property and organizational resources belonging to them.

In the light of the considerations on the problem of public sector management it is worth stressing the aspect of the presence of external effects of taken decisions. The allocation of funds to certain social and economic spheres (for example the decision-makers' focus on building technical infrastructure) has an impact on the functioning of many entities in the economy, even though they were not directly or even indirectly involved in the decision-making process (Wilkin, 2005).

The interest of the stakeholder theory is the issue of interactions between stakeholders of a given organization and benefits which are the results of these relationships. It concentrates on managerial decision making and the analysis of their effects.

In the public sector, stakeholders are primarily residents, businesses and other organizations which directly or indirectly feel the effects of decisions made by public authorities. Of key importance here is the social responsibility of public decision-makers for meeting the needs of businesses located in the area of the given territorial unit. The stakeholder theory is a good prerequisite for the introduction of modern forms of governance in the public sector, such which are based on the social and economic image of the public organization. In practice, its use is often manifested in the application of instruments aimed at soliciting „stakeholders' favourable disposition". This is done for example by means of the use of simple fiscal incentives (lower taxes, exemptions), the provision of certain services, or infrastructural development of well communicated investment areas.

The third theory, constituting the background for the emergence and evolution of the discipline of public management, is the theory of transaction costs, established on the basis of management science in enterprises. Coase is considered its precursor, who in his deliberations formulated the theorem according to which the basis for determining the boundaries of a company, and thus the range of tasks performed independently, should not be technological conditions, but the amount of the costs that must be incurred in connection with carrying out transactions within the organization or between companies in the market. Coase pointed out that narrowly specialized units typically gain the benefits of economies of scale and are able to assure lower manufacturing costs of offered products in comparison with enterprises in which the majority of areas of activity needed in the business, leading to the creation of specific goods and services, is carried out independently (Coase, 1988). These deliberations were later put to the test of adaptation for the needs of improving the efficiency of public sector management.

It is worth referring to the theory of organisational configurations in the public sector concerning two main principles of efficient operation: effectiveness and efficiency. The main idea of this theory is the assertion that various parts of the organization should not be considered separately, since the whole organization gives them the correct meaning (Roberts, 2000). The public domain model focuses on the objectives of the public sphere, the conditions of its operation and its tasks. The concept of organisational publicness explains the specifics of public organizations and their relationships with the environment (Markowski, Banachowicz, 2003; Kozuch, 2004, p. 50).

It should be noted that there is a close convergence of these concepts with elements of the model of public

governance (Markowski, Banachowicz, 2003). Thanks to the introduction of public governance in the social reality the following will be obtained: the improvement of the political decision-making process, increase in the level of participation of citizens in public life, the creation of a cooperation network, ordering of the State, the improvement of the public administration efficiency and the observance of the principles of democracy and human rights.

Historically, a bureaucratic management model has developed in the public sector, which assumes that public entities should undertake only those actions that are necessary for the proper, that is conforming to the regulations, realization of their tasks. According to Weber, bureaucracy as an ideal type should be characterized primarily by: action precision, speed, flexibility, unambiguity, continuity of work, impersonality, compliance with regulations, cost savings and predictability of behaviour. In practice, in the bureaucratic model administration is focused on creating procedural frameworks of its activities and performing of activities within the framework of competence defined by the law. In the interest of bureaucratic administration is, therefore, not effective provision of services to maximize the benefits for stakeholders, but smooth, continuous, cost-effective, predictable and mechanical execution of predefined tasks and procedures. In Weberian terms, it is called upon to perform specific, mechanical activities resulting in the implementation of planned, mostly short-term objectives. Functioning, it primarily performs current tasks arising not out of the signalled needs of its stakeholders, but from pre-set work schedules. It is not oriented on tasks that go beyond a short-term time frame, therefore, its employees and managers do not wonder about the long-term consequences of their decisions.

In the twentieth century, there was a gradual change in the paradigm of management in the public sector, manifested primarily by an attempt to move away from the traditional bureaucratic model. Under the conditions of the dynamic development of the world economy and the growing social needs, public administration reform proponents more and more often took the floor. To meet these challenges, public authorities should implement new management solutions, approximating the structure and form of governance in the public sector to management of a company operating in the conditions of market competition.

One of the forerunners of modern science of management in the public sector units was Peter Drucker, who claimed that the efficiency of the action is an essential attribute of the modern theory of organization and management in both the private

and public sectors (Drucker, 2003, p. 34). He introduced the concept of the three „Es” (efficiency, effectiveness, ethical) to the science of management in the public sector. According to Drucker, the assessment of the efficiency of public authority includes: the degree of implementation of planned goals (effectiveness), the positive ratio of operation results to the cost (efficiency) and compliance of operation with the adopted axiological system (ethics).

In the first place, we should point to New Public Management – NPM among modern management models. The development of this idea has become a response to the changing role of public authorities in the management and organization of socio-economic life and the growing societies’ demands in relation to government bodies. The main assumption of NPM is to transform the approach of public asset managing authorities towards increasing the effectiveness, efficiency and quality of provided services, while increasing the responsibility of decision-makers for their actions (Hughes, 2003, p. 37). New public management, therefore, proposes new solutions for assessing the effectiveness of public sector activities by targeting the authorities and decision makers on the final results of their activities. Postulating a departure from bureaucratic methods of governance, the possibilities of cooperation with the private sector and non-governmental organizations are used to a greater extent. It should significantly expand the selection of alternative mechanisms of service provision. The NPM trend also introduces significant changes in the internal structures of public organizations.

Undoubtedly, NPM, as a collection of modern methods of management in the public sector, has played a significant role in shaping directions of development of the public sector. This trend, however, has not become the dominant paradigm of management in the public sector. One of the main objections formulated against NPM is too much confidence in market mechanisms, manifested to some extent in mechanical attempts to transfer the majority of business solutions to the public sector.

Assessing the practical application of this management model it is worth pointing to Pollitt’s conclusion that, in fact, there is no „pure” model of public management in the spirit of NPM in any European country (Hughes, 2003, p. 37). It seems that NPM brings beneficial effects (in terms of improving the quality and efficiency of services), mainly in the case of simple services with measurable quantity and value, the quality of which is also relatively easy to measure. However, in the case of social services with a complex structure and multiple objectives,

NPM can, next to the positive economic effects, cause adverse social results.

From among modern management methods applicable in the public sector, we should still draw attention to entrepreneurial management. In this spirit, one of the first coherent concepts in terms of the paradigm change of governing of public affairs and transformation of the role of decision-makers was presented by American researchers Osborne and Gaebler. They present the problem of the quality and effectiveness of management in the public sector against the background of the rapidly changing socio-economic environment and rising public expectations (Osbourne, Gaebler, 1994, p. 43). The rules, which Osborne and Gaebler talk about, allow public authority to manage public affairs more effectively and more efficiently. They insist that „in order to reduce wastefulness” in the public sector, bureaucratic institutions should be transformed into entrepreneurial institutions which will not hesitate to reject useless ideas. They also point out that the administration in its nature is passive, reluctant to change, closed to the growing needs of society and cannot meet new challenges.

In recent years, much attention has been paid to the trend of „public governance”. Its message is a method or system of governing not related to the structures of power, but to the governing function (in terms of performing the tasks of power), from the point of view of modes of action and the quality of governance. In this model, governance assumes that policymakers, organizing the public service provision process, replace competition with cooperation, partnership, co-responsibility and the possibility of achieving mutual benefits on the basis of synergy. The governance trend implies, therefore, that public authority is a major player animating social and economic processes, and above all fully responsible for the proper execution of its tasks. In the model of public governance a key role is played by the governing process itself.

It seems that due to the lack of unambiguous positive effects of the implementation of NPM in the practice of public administration, the public governance approach will be applied more and more often. An important common feature of the two doctrines is the formula for exercising of public power. For both of them one of the main principles is that decision makers should focus on defining the general organizational, financial and technical framework for the functioning of the organization, the sphere of the public service performance should be as much as possible transferred outside into specialized entities.

2. THE EFFECTIVENESS OF MANAGEMENT OF PUBLIC FINANCES AT THE LOCAL LEVEL IN RELATION TO THE METHOD OF MANAGEMENT

2.1. LOCAL REVENUE POLICY

The public sector on local level is subject to an increasing pressure to increase efficiency and improve the quality of its actions. Pressure of authorities, local communities, businesses, and media stimulates its development and thereby forces the introduction of modern management methods.

As pointed out by Raczkowski, local government units should seek self-assessment and planning tools which would allow them to manage the given unit in an efficient, transparent and predictable way. An important element of management is finance, which should be managed not only on the annual but also on the long-term basis (Raczkowski, 2015, pp. 65-67). It can be also pointed out that in the context of public management it is essential to ensure activities which are harmonious, targeted and optimal from the point of view of the public sphere (Kozuch, Sułkowski, 2015, p. 42).

Management in the public sector encompasses decisions and actions of the public authority, as an entity responsible for the implementation of a wide range of municipal and social services and shaping development processes. It requires the use of instruments from the field of management, including financial management (Bitner et al., 2013, p. 20).

Managing public funds, local authorities conduct their own financial policy, which should be understood by a conscious and purposeful activity of people and institutions involving the definition and implementation of specific objectives, using available funds. (Ruśkowski, 1994, p. 17). An element of financial policy is financial planning, which is the process of determining of financial effects of planned activities within the specified time, and comparison and adjustment of these plans to the anticipated financial resources.

The practice of public financial management at the local level shows a close connection between locally conducted financial policy and the budgetary economy, and the implemented management model. This is confirmed by author analyses and forecasts of the financial situation of many Polish local governments. On this basis, it can be argued that local authorities using the bureaucratic management model limit themselves to financial administration,

but decision makers implementing innovative management methods resort to instruments of strategic management.

Authorities applying the administrative management model are characterized by passivity and reluctance to use innovative methods of management. They apply a one-year financial planning cycle, make cost analyses to a very limited extent. Strategic management is, however, the process of shaping of financial policy and budgetary economy, both on an annual as well as on many year basis. Here, a cost and benefit statement is used as well as available management tools helping to shape long-term policy of local authorities. In this model, satisfying needs is not a simple sum of the annual plans of financing of tasks, but it has a strategic character, connected with long-term local social, economic, spatial, environment protection policy. And annual budgets are a reflection of this policy and an instrument of its implementation. A very important feature of strategic management is creativity, understood as the ability of public authorities to identify and solve local problems, combined with the creative ability to apply methods and techniques of planning of current and developmental tasks. It is connected with the transfer of methods of planning and strategic management from the private sector and adapting them to the conditions and needs of public institutions (Sierak, 2013, p. 191).

The experiences of functioning of local government in Poland show that administration, as a bureaucratic management model, is a cause of many conflicts and tensions among members of local authorities, because their activities concentrate on the annual „battle for budgetary resources” which are necessary to achieve their preferred tasks. In such conditions, decisions concerning the scale and direction of budget spending (especially pertaining to investments) are subject to achieving a current compromise. They are not a result of long-term arrangements. It is disturbing that in Poland still a little more than a half of municipalities uses this passive, ineffective management model (based on the results of the author’s study in the Department of Economics and Finance, Warsaw School of Economics).

Financial management encompasses a great deal of decision-making planes. For obvious reasons, the considerations contained in this publication have been limited to selected elements of the revenue and expenditure policy-making of local authorities in Poland.

By analyzing management decisions of a large collection of local authorities, it can be argued that locally conducted revenue policy is closely linked with the adopted management model. This applies

primarily to the formation of local taxes and fees and the management of municipal property.

At this point it is worth referring to Tiebout, according to whom people move (migrate) to places where local authorities provide the appropriate relationship between the tax burden and the level of services (more Tiebout, 1956). This process is called „voting with the feet”. Residents have identified preferences pertaining to the size of taxes and the resulting number of services which they would like to receive from the local government. According to Tiebout, „voting with the feet” would lead to Pareto optimum, that is a situation in which the improvement of one’s situation cannot occur without deterioration of someone else’s. Thus, rational management can help to increase the location attractiveness of the territorial unit. A consequence of unskilful management can be depopulation and decline in the location attractiveness for businesses, which in the long run may have a negative impact on the level of budget revenues.

The first element of local government financial policy relates to fiscal policy. Federowicz uses this term in the sense of „a choice of sources and methods for collecting public revenues, and also directions and methods of implementation of public expenditure in order to achieve social and economic objectives fixed by competent public authorities” (Federowicz, 1997, p. 7).

The analysis of the relationship between the management model and the effectiveness of the local government budget economy should start with the local income policy. Its object is to collect revenues to be able to execute public tasks in accordance with the established current and development objectives.

Local government income policy in Poland is pursued in the conditions of decentralization of public tasks and competencies to perform them. Unfortunately, it goes hand in hand with the decentralization of public finances to a limited extent. This is a significant external condition of shaping own financial policies of local government units. In local government budgets, this process results in an excessive increase in current expenditure, which limits the pool of funds which could be used to finance investments.

The first relationship between the shaping of income policy and the management model implemented by public authorities occurs in the shaping of local taxes and fees. A significant problem here is the optimization of tax rates, on the one hand, in relation to the possibility of taxpayers, and, on the other hand, to the scope of current and development expenditure needs reported by them.

Referring here to the decision-making processes – the bureaucratic model is characterized by low activity of authorities in shaping tax policy. In practice, setting tax rates is based on the size of the previous years, indexed with the rate of inflation. Potential changes in the size and efficiency of the tax base are not analyzed, the examination of internal and external determinants of fundraising is limited, the simulation of the impact of tax rates on the future financial situation of the municipality is missing. Local politicians often freeze tax rates, keeping them at the same level even for many years. An argument in favour of such an action is the protection of the financial status of the local community. However, the effects of such policy can be inverse. Such policy, in conditions of rising prices of energy, transport, materials, increasing wages leads gradually to increase in the share of current expenditure in total expenditure, which in turn results in a reduction of the development potential. As a final result, such policy is not conducive to the growth of potential and competitiveness of the territorial unit. In addition, when it is practiced over a longer period, it leads to the deepening of the financial gap. Very often bureaucratically managing authorities' reaction is the balancing of the budget with funds derived from the sale of municipal property. Such activities cannot be regarded as a solution to the existing problems. Property resources are in fact limited, and it is not always possible to achieve the desired level of revenues from their sale. Such a management model may eventually lead to an imbalance, even loss of liquidity.

A different approach to the financial policy is characterized by the strategic management model. In this model, it is integrated with the shaping of socio-economic development.

Griffin draws attention to the specific features of the strategic management process, such as proficiency, effectiveness, efficiency (Griffin, 1996, p. 38). He points out that achieving the goals of the organization lies in the use of existing resources in a rational way, without unnecessary wastefulness.

Strategically managing local authorities, while shaping the revenue policy, analyze the current and future implications of the decisions made within it. Here, it is necessary to highlight the problems that have a strategic impact on the level of satisfaction of the current collective needs and the scale and pace of development processes. In strategic management an important element of the shaping of the revenue policy is the orientation on the future, that is, solving of current problems from the perspective of the future and focus on results, that is the achievement of objectives through the systematic, efficient and effective implementation of pre-planned tasks. At the

same time, each territorial unit is treated as part of the environment, which constitutes a set of both opportunities and threats to its development.

Treating finances as part of integrated strategic management we should pay attention to the direct connection of the municipality's tax policy with its development strategy. Current objectives should be subordinated to operational and strategic objectives. Tax policy cannot be limited only to enforcement, differentiation and collection of revenues from local taxes. The amount of burden resulting from local taxes and fees, the level of prices for public services, rental rates for residential and commercial premises, as well as fees for the use of public facilities are dependent on the current financial needs of local government. Attractive rates and periodic tax exemptions should help to attract new investors (Patrzałek, 1994, pp. 47-51).

Local government income policy is associated with the choice of sources and methods of financing (self-financing, borrowing). In the process of financial management, public authorities are faced with an important decision-making dilemma – whether to raise taxes and local fees or to borrow money to finance capital expenditures, or to do both. In the model of strategic management, decisions in this area result from the analysis of alternative scenarios of projected solutions and simulation of their future implications. Of course, local authorities are aware of the fact that taxpayers' reactions to the tax burdens may vary. What is therefore important is the parallel implementation of principles of openness of public finances, with a clear indication of financial policy objectives, including income and tax policy with respect to the feasibility of strategically and operationally assigned tasks (current and investment ones).

An important element of strategic financial management is the shaping of the revenue structure. On the basis of stable income, it is possible to forecast development scenarios which generate future budgetary income as a result of new investments. This happens, for example, when development of areas creates conditions for the location of new business entities and housing development. Taxes play the role of local policy instruments, their skilful shaping is conducive to the creation of conditions of socio-economic development. A much less favourable situation occurs when the budget structure is dominated by grants and subsidies.

Public authorities can pursue income policy objectives also by means of the sale of assets (due to the limited resources, all decision in this regard should be taken with caution), their rent, tenancy, lease, and other forms of real estate management. The

effects of income policy in this area are diverse and largely depend on the ability of effective property management. Rational management of municipal property requires the adoption of local strategies of managing its components which clearly define the principles and directions of its use. Another source of own income for local government units are also their capital revenues from shares in commercial companies and benefits derived from this and the possible sale of the acquired property rights. Also in this respect, specific goals of income policy of local government units should be formulated and implemented, so that the undertaken actions are conscious and rational.

2.2. LOCAL EXPENDITURE POLICY

The other important element of financial policy is the policy of expenditure. It involves a conscious and deliberate formulation of directions of distribution of public funds in order to carry out tasks serving the satisfaction of collective public utility needs. As part of the expenditure policy, the directions of spending of funds and the criteria for their allocation are determined. Moreover, entities to carry out specific tasks (obligatorily and optionally) are selected.

As mentioned in the introduction, a commonly occurring problem of local finances in Poland is the scarcity of financial resources in relation to the range of tasks to be implemented and the size of investment needs handed over to local governments. In such conditions, the budget economy must be characterised by as high as possible efficiency of resource management. The more so because with the development of society, the demand for public funds rises. This dependence was noted by Wagner, German representative of science of finance, who perceived and described the phenomenon of continued growth in public spending, noting that with the development of society, public authorities report demand for growing revenues, which are determined by increasing public spending (Wagner, 1893, p. 916).

Economic efficiency is expressed in constant pursuit of economic operators to maximize the effects of incurred expenses. However, measuring the efficiency of public spending in practice has some limitations, because the connection of specific categories of expenditure with the indicators describing their results is often difficult. This problem is pointed out, among others, by Stiglitz, who states that it is extremely difficult to ensure consistency between equality of access to public goods and services, and efficiency (Stiglitz, 2004, p. 136). Due to the specificity of public sector services, public

sector institutions often have other priorities than maximizing efficiency in financial terms, because social and environmental factors are equally important. The assessment of the expenditure effectiveness is further hampered by the time gap between expenditures and the effects appearing as their consequence. For example, when planning to build a network of municipal infrastructure, as wide range of recipients as possible is covered by it, even if the financial statement suggests that the investment pays off when realized only in larger population clusters.

The assessment of the effectiveness of any organization is closely related to the concept of productivity (Pawlak, 1995, p. 13). Looking for the optimization of economic, public and administrative activities, the DEA parameter assessment of efficiency can be used (Data Envelopment Analysis). The DEA method is based on the concept of the best practice frontier in which it is assumed that all entities should be able to operate at a given expected level of productivity, determined by the effective entities in the given sector. Entities which achieve productivity lower than the border level operate inefficiently. The scope of improvement of their effectiveness is determined by reference of their results to the results of efficient entities (Nazarko et al., 2008, pp. 34-35).

Applying this method in the measurement of effectiveness, one can, for example, enter one input variable (for example the size of expenditures on education) and several output variables showing the effects of these expenses (for example relating to the conditions and effects of teaching in schools). The described method of efficiency testing is only used in the model of strategic management. Because in the bureaucratic model there is no or is very limited range of cost analyzes of public service provision.

Another feature of strategic management of the expenditure side of the budget (which does not appear in the administrative model), aimed to improve the efficiency of management of public funds, are cost analyses. They include the study of the total cost and their unit breakdown. Especially, the latter approach gives wide possibilities of application and indication of expenditure rationalization planes. Calculations may concern own resources (for example comparing costs of operation of several educational, cultural institutions), as well as comparisons of similar institutions existing in other territorial units (and differently managed).

For comparative purposes, an objectively important task here is to establish a rational standard of costs of providing of various types of municipal and social services. This requires detailed financial and economic analyses, taking into account the

impact of various factors on the cost of operation of various settlement units. For example, operating costs of a big city and a small settlement are different. However, in any case, funding of reasonable costs should be pursued, preventing the occurring forms of mismanagement. In the case of large cities it is also important to keep in mind the periodically emerging needs for overcoming developmental thresholds. In these conditions it is necessary to calculate for each service the justified, average cost of its provision, with reference to the present local and regional conditions.

Rational management contributes to achieving the desired efficiency effects. The concept is one of the basic premises of modern methods of strategic management in the public sector. In line with the philosophical tradition, the action is considered reasonable only if the operator chooses – on the basis of his/her knowledge – the most effective means to achieve the objective (such a definition of rationality refers to the philosophical tradition, already adopted by the French rationalists in the eighteenth century, which proclaimed that the main determinant of human action is the reason). According to Lange, a rationally acting operator pursues the realisation of a specific function of the objective, guided in his/her economic choices by the general principle of rational management (Lange, 1959, p. 207). This principle imperfectly formulated by Quesney, was reconstructed by Lange, according to whom it should be considered in two terms. A procedure aimed at achieving the maximum degree of the goal realisation with the given outlay is the principle of maximum productivity, which is the principle of the greatest effect; a procedure which allows to obtain a given degree of the objective realisation with the minimum outlay is called the principle of the least outlay of funds (funds saving), (more Lange, 1959, p. 207; Zagórski, 1963). In summary, it can be said that the rationalization of current expenditure should aim at minimizing the cost of meeting of public needs belonging to the tasks of local government, while maintaining a certain standard of provided services.

In expenditure policy of units managed according to the previously described innovative methods of public management we should point out two important instruments for efficient public spending. The former is rational planning, the latter is skilful allocation of resources.

The basis for the construction of financial plans is the knowledge of laws governing economic processes. There are different time horizons – short, medium and long term. Individual activities should be planned in such a way that it should be possible to use the existing resources in the most rational way

in specific periods of time.

The effectiveness of financial planning depends to a large extent on the applied methods and planning tools. The method of extrapolation is the simplest, but often used (Kaleta, 1982, p. 28). It involves planning of the budget revenue and expenditure on the basis of the implementation of the budget in previous years. It cannot be, however, a static process. Its element must be based on an analysis and assessment of historical trends and on drawing conclusions for the future financial policy.

In building financial plans, two basic methods can be used: revenue and expenditure ones. In the first of them, the size of the expenditure, subject to the continued rationalization, is adjusted to the level of income. In the other method, the basis is the implementation of a predetermined range of expenditure, financed with budgetary revenues, and in the event of a financial gap – with other sources of funding, mainly – debt instruments. Practice shows that this method is less conducive to the rationalization of budget expenditures. Financial policy adopted by the local authority determines the use of one of the above methods. The revenue method is usually used in the strategic model of management of the local unit government, and the expenditure method in the administrative model.

The implementation of investment programmes, in amounts exceeding their own financial potential, requires incurring debt. In this situation, an important part of financial planning is the assessment of the creditworthiness of the local government unit and the determination of a safe level of debt. Equally important is the skilful selection of debt instruments (a loan, a credit, municipal bonds) and the determination of the repayment terms and debt service costs, according to the existing financial potential. Uncontrolled indebtedness is a dangerous phenomenon, which can lead to disequilibrium, and even loss of liquidity. According to the „golden rule” of balanced budget, local government should not borrow money for the current purposes, it is possible to incur a debt for investment programmes.

In implementing budgetary expenditure, their rational allocation should be prepared. This function of public finances determines proper functioning of society and local economy. This allocation has a dimension of effective budget distribution to different spheres of the territorial unit operation.

The first of the dilemmas faced by public authorities relates to the issue of the budget allocation for the current and capital expenditures. The former determines the correctness of everyday functioning of the territorial unit, the latter influences the direction and intensity of development processes.

The relative proportions between the two groups of expenditure are information about the preferred policy direction of local authorities.

Properly implemented expenditure policy should ensure proper functioning and development of the territorial unit. Under conditions of limited resources, all expenses are mutually competitive, and any decision to allocate a certain amount of public revenue to a specified target automatically limits the amount of funds available for other purposes. Therefore, the preparation of the expenditure side of the budget should be preceded by a number of consultations and arrangements, including through direct meetings with residents and representatives of local entrepreneurs.

Budget allocation is also a dilemma relating to the sector structure of expenditures and decisions with regard to their distribution to: administration, public utilities, education, social services, transport, housing management and other areas of the territorial unit operation. Proper allocation is here also determined by rationality of the management process, because in expenditure policy, pursuit of a steady increase in budget expenditures is more and more visible. However, this increase is not always justified. Public spending cannot grow without limit, so continued rationalization efforts are necessary in budget economy.

One of the functions of public expenditure is the stimulation of economic growth. Expenditure on infrastructure is important, which is connected with the occurrence of external effects. Theoretical basis for such a statement is provided, among others, by Barro's model (Barro, 1990), according to which expenditure on infrastructure or, broadly speaking, capital expenditures that make up the public capital, may belong to expenditure increasing the productivity of private capital. Kneller and co-authors come to similar conclusions stating that public investments accelerate economic development (more Keller et al., 1990).

A similar argument can also pertain to public investment in human capital, primarily subsidizing of education, health, culture, sport and recreation (it is confirmed by growth models, for example Romer, 1990). This results from the fact that the growth of technology, and therefore economic growth depends on the level of human capital – the higher it is, the quicker technology develops. So, if public authorities are able to effectively increase human capital, they can thus also affect economic growth. Lukas draws attention to the relationship, according to him the accumulation of human capital may therefore be an important factor explaining economic growth (more Lucas, 1988).

In summary, we can conclude that the requirement of effective financial management is closely linked to the implemented management model. The benefits of application of modern management methods are seen in practice. Their use, however, is quite difficult – it requires knowledge, skills and consequence of the proceedings.

CONCLUSIONS

Management in the public sector is a complex process and is conditioned by many internal and external factors. The quality of this process has a significant impact on the conditions of functioning of territorial units as well as on the pace and direction of local and regional development.

The practice of public management at the local level shows two models of financial management – administrative – related to the bureaucratic management model and strategic management – used in units capable of applying modern methods of management.

Comparing local government units using administrative and strategic financial management models we can indicate that they are differentiated by the following elements of financial policy:

- strategically managing units strive to maintain a diversified but relatively stable income structure, trying to prevent a situation in which there is a large fluctuation of various sources of income;
- these units establish local fees and taxes and prices for municipal services at a level corresponding to the cost of their provision and also apply active policy of exacting their income;
- local governments applying the strategic management model use modern and effective methods of financial planning in financial policy, also in the multi-annual arrangement, and constantly carry out financial analyses;
- every financial decision is considered from the point of view of its impact on current and future budgets, with a constant analysis of its potential effects on the future liquidity of the local government unit.

The application of strategic financial management methods should lead to an increase in the efficiency of management of public funds.

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