

IMPORTANCE OF TAX REVENUE CONCERNING BUDGETS OF LOCAL AND REGIONAL SELF- GOVERNMENT UNITS

Emina JERKOVIĆ, PhD

Faculty of Law, Josip Juraj Strossmayer University in Osijek
Department of Financial Law and Financial Science

ekonjic@pravos.hr

Abstract

Since its independence the Republic of Croatia has commenced a thorough reconstruction of its taxation system according to the market economy taxation policy. Essential taxation reforms have brought the system closer to EU systems i.e. it has been being harmonized with taxation systems of developed European countries.

The tax systems of modern countries are using a large number of tax forms, which differs from country to country. The Republic of Croatia has adopted solutions that are used by the majority of European countries. Current tax system of the Republic of Croatia can be viewed through three fiscal levels, but this paper deals with revenue, especially tax revenue of local and regional self-government units. The paper will present importance and a way of collecting revenue, especially tax revenue and satisfying public needs in terms of counties, cities and municipalities.

Keywords: *tax system, local and regional self-government units, local taxes, regional taxes, budget*

JEL Classification: H2, H23, H29

1. INTRODUCTION

The goal of every state decentralization is to recognize and please the public needs and to encourage local and regional development. Only by achieving those goals of decentralization can the state create motivation and satisfaction of its citizens for contributing to accomplishment of public affairs. In the Republic of Croatia decentralization presents itself through three levels of government. We talk about the highest level, i.e. the state, the middle regional level, i.e. counties (20 of them) and the third local level, i.e. cities and municipalities (556 of them). Each of the fiscal levels has its powers and responsibilities.

Certain values are specified by the legal regulation of every EU Member State, and are also declared by the European Charter of Local Self-government (hereinafter referred to as the Charter) accepted by the Council of Europe.

Article 9 – which includes eight sections – (Financial resources of local authorities), the longest part of the Charter, regulates the finances of local governments. It provides detailed guidelines on local self-governments, and contains the following financial and economic management principles:

- principle of income: the local authorities are entitled to their own financial resources, of which they may dispose freely within the framework of their powers;
- local authorities' financial resources shall be commensurate with the responsibilities provided for by the constitution and the corresponding law (the principle of entitlement to the financial resources adequate to the responsibilities);
- the principle of local taxation powers (local taxation rights, and the right to introduce other local payment obligations; part at least of the financial resources of local authorities shall derive from local taxes and charges of which, within the limits of statute, they have the power to determine the rate);
- reduction of financial disparities between the local self-government units (so-called equalization principle);
- the use of funds as per the statutory limits (the principle of expenditure);
- as far as possible, grants to local authorities shall not be earmarked for the financing of specific projects (the limitation of earmarked funds);
- the autonomy of management decisions within their own jurisdiction (principle of discretionary powers);

- participation in the central decision-making concerning local self-government finances (principle of participation).

The most important principle is the entitlement to appropriate financial resources, which means, on one hand that the volume of municipal funds shall be commensurate with the extent of local government responsibilities set forth in the corresponding law in the legislation,¹ and, on the other hand, the amount of funds allocated at the local self-governments can be considered as appropriate, if they keep pace with the cost of carrying out their tasks (Paragraph 4 of Article 9 of the Charter).

The current Croatian tax system can be examined through three fiscal levels. This paper deals especially with tax revenue of local and regional self-government units, by presenting the way of realizing tax revenue, levying and collecting taxes, furthermore satisfying public needs on state, county and city levels.

Since the declaration of its independence, the Republic of Croatia has commenced thorough reconstruction of its tax system as well, since it had to meet the requirements of the new political system terminating the war period, as well as the challenges of market economy closing the socialist character. Essential tax reforms have brought the system closer to systems of the EU Member States, through its harmonization with taxation systems of developed European countries.

2. SCOPE OF AUTHORITY OF LOCAL AND REGIONAL SELF-GOVERNMENT UNITS AND THEIR REVENUE

Law on Local and Regional Self-Government² regulates the scope of functions of municipality and city separated from the scope of functions of county. Pursuant to the provision of Article 19 of the Law, local and regional self-government units in their self-governing scope perform the tasks of local importance, and especially see to jobs that are not constitutionally or legally assigned to government bodies, relating to the planning of settlements and housing, spatial and urban planning, social welfare, primary health care, education, etc.

¹ Paragraph 2 of Article 9 of the Charter

² Law on Local and Regional Self-Government, Official Gazette 33/01, 60/01, 106/03, 129/05, 109/07, 125/08, 144/12

2.1. THE POWERS AND RESPONSIBILITIES OF COUNTIES

County conducts services of a regional importance, and which are not assigned by the Constitution and laws to the national authorities. The incidence of county can be original (self-governing) and entrusted to (services of state administration).

County in its self-management scope performs services relating to:

- education
- health care system
- spatial and urban planning
- economic development
- transport and transport infrastructure
- maintenance of public roads
- planning and development of a network of educational, health, social and cultural institutions
- issuing construction and location permits and other documents related to construction and implementation of spatial planning documents for the county outside the big city
- other activities in accordance with special laws.

By the decision of the representative body of local self-government unit in accordance with its statute and the statute of the county, some jobs of self-government scope of the municipality or city can be transferred to the county.

Entrusted services relate to services of state administration which are carried out by a county and are defined by law. The costs of these services shall be paid from the state budget.

2.2. THE POWERS AND RESPONSIBILITIES OF CITIES AND MUNICIPALITIES

Municipalities and cities in their self-governing domain (scope) perform the services of local importance which directly actualize the needs of citizens, which are not assigned by the Constitution and laws to the national authorities and in particular services related to:

- planning of settlements and housing
- spatial and urban planning

- utility services
- childcare
- social care
- primary health care
- education and primary education
- culture, physical culture and sport
- consumer protection
- protection and enhancement of natural environment
- fire and civil protection
- traffic in their area
- other activities in accordance with special laws.

To meet its duties, counties, cities and municipalities have to find means of finance- mostly deriving from public revenue. When we talk about financing local and regional self-government units most often we talk about fiscal capacity and its strength. Fiscal strength of these units varies a lot especially when it comes to municipalities and cities.

3. REVENUE OF LOCAL AND REGIONAL SELF-GOVERNMENT UNITS

Financing of local and regional self-government units in decentralized countries is of great importance, both for the development of the overall economy, as well as for the development of local and regional self-government units which carry out the logic of polycentric development. To satisfy this postulate it is necessary to find the optimal method of financing.

Local and regional self-government units in their budgets have to ensure revenue which are proportional to expenditures, from its own sources, of shared taxes and grants from state and county budgets.

Revenue of local and regional self-government units:

1. Income from movable and immovable objects in their possession
2. Income from companies and other entities owned and revenue from concessions granted by local self-government units

3. Revenue from the sale of movable and immovable objects in their possession
4. Gifts, inheritances and legacies
5. Municipal, town and county taxes and fees and duties, whose rates, within the limits specified by law, are determined independently
6. Government assistance and grants provided by the state budget or a special law
7. Compensation from the state budget for performing services of the state administration, which were conveyed to them
8. Other revenue determined by law.(Srb & Perić, 2004:91)

Law on Financing of Local and Regional Self-Government Units determines the resources of funds and financing services from the scope of the counties, municipalities and cities.

3.1. COUNTY REVENUE³

1. Revenue from own property
 - a) Income from movable and immovable objects in the possession of the county
 - b) Income from companies and other entities owned by the county
 - c) Revenue from the sale of movable and immovable objects in the possession of the county
 - d) Gifts, inheritances and legacies
2. County taxes
 - a) Inheritance tax
 - b) Tax on motor vehicles
 - c) Tax on boats
 - d) Tax on gaming machines
3. Fines and confiscated assets for the offenses that are prescribed by the county itself
4. Other revenue determined by special law.

³ Law on Financing of Local and Regional Self-Government Units, Official Gazette 117/93, 33/00, 73/00, 59/01, 107/01, 117/01-correction 150/02, 147/03, 132/06, 73/08, 25/12, 147/14

3.2. MUNICIPAL AND CITY REVENUE⁴

1. Revenue from own property
 - a) Income from movable and immovable objects in the possession of the municipality or town
 - b) Income from companies and other entities owned by the municipality or town
 - c) Revenue from concessions granted by local self-government units
 - d) Revenue from the sale of movable and immovable objects in the possession of the municipality or town
 - e) Gifts, inheritances and legacies
2. Municipal and city taxes
 - a) Surtax to income tax
 - b) Tax on consumption
 - c) Tax on holiday homes
 - d) Tax on corporate title
 - e) Tax on public land use
3. Fines and confiscated assets for the offenses that are prescribed by the municipality or town themselves.
4. Administrative fees in accordance with a special law
5. Residence fees in accordance with a special law
6. Utility charges for the use of municipal or city facilities and institutions
7. Utility charges for the use of public or municipal urban areas
8. Other revenue determined by special law.

3.3. SHARED TAXES

There is one very important category of public revenue that we must emphasise- shared taxes.

Shared taxes are personal income tax and tax on sales of real estate. Most important remark dealing with shared taxes is revenue belonging.

When it comes to tax on sales of real estate the division is as follows:

- a) State- 40%

⁴ Law on Financing of Local and Regional Self-Government Units, Official Gazette 117/93, 33/00, 73/00, 59/01, 107/01, 117/01-correction 150/02, 147/03, 132/06, 73/08, 25/12, 147/14

b) City- 60%.⁵

But, personal income tax is the most significant revenue especially when it comes to cities and municipalities.

Revenue from income tax is divided between:

- a) municipality/city – 56,5%
- b) county - 16%
- c) part for decentralized functions - 12%
- d) part for position for aid of accommodation for decentralized functions - 15,5%.⁶

Decentralized functions are social care, education, health care and fire department. But it is very important to emphasize that the operational side of these functions is financed through Personal income tax. When it comes to personal income of people employed or taking care of these functions, their income derives from state budget. Operational side includes mostly material costs (buildings, equipment, furniture etc.) in connection to performing these functions.

4. UNPAID REVENUE AND THE STATE OF LOCAL FINANCES

On 31.12.2011. units of local self-government had 8,6 billion HRK of unpaid debts. With 5,4 billion HRK dominant are debts for business transactions revenue, and the other part of unpaid debt refers to debts for sales of nonfinancial asset. Biggest part of 5,4 billion HRK refers to administrative fees (about 60%) , followed by debt derived from revenue from own property (24%). When it comes to revenue collected from taxes, the debt is the smallest-only 16%. (Bajo & Primorac, 2013)

Most fiscally abundant revenue of local self-government units are tax revenue. In year 2013. they were raised in the amount of 11,4 billion HRK, which makes 72,1 % of total revenue that was raised that year. When we look at year 2012. tax revenue increased by 21.5%. When we look at the structure of col-

⁵ Tax on Sales of Real Estate, Official Gazette 69/97, 26/00, 127/00, 153/02, 22/11, 143/14

⁶ Law on Financing of Local and Regional Self-Government Units, Official Gazette 117/93, 33/00, 73/00, 59/01, 107/01, 117/01-correction 150/02, 147/03, 132/06, 73/08, 25/12, 147/14

lected tax revenue biggest share goes to revenue collected from personal income tax and surtax to personal income tax (78,2%). They are followed by property taxes in the amount of 16,5%.⁷

Problems concerning payment are related to weak cooperation regarding information exchange between Tax office and units of local self-government. Units of local self-government have empowered Tax office to collect revenue for them and Tax office charges provision in the amount of 5% of collected revenue. The problem is that Tax office delivers monthly reports about paid taxes but does not deliver information about tax payers who have not paid their debt, issuing resolutions and measures of collecting revenue. This is because Tax office is obliged to do so because of the Article 8 of Public Tax Law that concerns tax secrecy.

Also data concerning public and local revenue are not as public and transparent as it should be. Units of local self-government do not inform citizens about efficiency of revenue collecting or its purpose and influence on economic development and improvement of life conditions. These information should be available to every citizen simply by publishing them on city or county web pages.

Big part of the self-government units have their debt written off, which is not reasonable behaviour especially in these times of economic crisis. Also it has been established that 49% of 556 local self-government units did not impose all the revenue they could have by existing legal regulation and 29% of local self-government units did not undertake all the measures of ensuring the payment of existing debt. (Bajo & Primorac, 2013) The problem is more serious when we look at the big picture. Dealing with the fact that many of the self-government units have had the debt written off, they come to the state and demand help in the form of donations, financial support and grants and subventions.

5. CONCLUDING REMARKS

The autonomy of self-governments, from the conceptual point of view and particularly from the practical approach is the assessment of the economic opportunities, the amount and structure of resources, and the freedom of use of the resource. The actual operating conditions of each system depend not on the

⁷ Yearly Report of Ministry of Finances for the year of 2013.,
<http://www.mfin.hr/adminmax/docs/Godisnjak%202013.pdf>, p. 61 (access: 5-3-2015)

legal regulation, but instead on the the local economic circumstances of the self-government and their involvement of local economic development, furthermore on the economic and fiscal policy of the state.

As current tax systems of the European countries show many similarities and much less differences, the principles of taxation and the trends are quite similar. In recent decades, one of the most important European taxation tendencies has been the increase of the role of local and regional taxation and the Croatian legislation is in line with the EU efforts and regulatory trends. The Croatian model, due to the important county and municipality taxes, is closer to the welfare and economic development models⁸ of self-governments, in which, besides the central dependence, a structure was established with more active self-governments providing notable services.

It is a fundamental problem of the Croatian regional, and local taxation, which is also a tendency all around the world, that despite the continually expanding scope of central and local activities, new types of public revenue cannot be found neither in the central, nor within local taxation, which could improve the increasing revenue that covers the government services, therefore there is no other option, but to tune these systems carefully, and to harmonize their operational reserves, furthermore to improve tax compliance.

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⁸ In the welfare model, the self-government units fulfil their obligations within strong central dependence, they focus on providing the services, and they deal less with the development of the local economy, which is undertaken mostly by the central state. The self-governments act as undertakings in local economy, their local need of resources is higher than the central one, therefore they establish a more intense relationship with the local actors of the economy.

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