

FINANCIAL – ACCOUNTS VIEW ON THE GOVERNMENTAL EXPENSES AND THE AUTONOMY ADMINISTRATION IN THE CONDITIONS OF THE SLOVAK REPUBLIC

Marián Kočner¹

¹ Department of Enterprise's Information Systems, Faculty of Economics and Management, Slovak University of Agriculture in Nitra, Tr. A. Hlinku 2, 949 76 Nitra, Slovak Republic

Abstract

KOČNER MARIÁN. 2014. Financial – Accounts View on the Governmental Expenses and the Autonomy Administration in the Conditions of the Slovak Republic. *Acta Universitatis Agriculturae et Silviculturae Mendelianae Brunensis*, 62(6): 1537–1543.

The extension of state activities currently raises the need to fund specific public projects in the area of the infrastructure, ecology, or the entire expenditure programs in the field of education, health and social care and culture. Into the accounts methodology of the national and autonomy administration were introduced the transfers which represent prevalent expenses, capital expenditures, grants, subsidies and contributions. From an accounting perspective views there is an important fact from which the transfer passes, respectively whether the transfer is provided by the founder, the transfer by another entity within the public administration, or the transfer goes from an entity outside of the public administration. Watching transfers is important for the subsequent preparation of consolidated financial statements and summary financial statements of the public administration. The aggregate accounts of government administration in 2012 expanded by another group of accounting entities namely the state enterprises, RSR, Eximbanka and other public entities.

INTRODUCTION

1 Theoretical Aspects of Public Expenditure

Public expenditures represent cash flows that are within the public system budget allocated for the implementation of the fiscal functions of the state. Historically, the oldest purpose has been the expenditures on defense and judiciary. Within the public expenditures, we distinguish two groups ^ of spending, namely the government spending (of the consumption and investment character) and also transfers¹.

Public expenditures =
= governmental spending (G) + transfers (Tr).

Governmental expenditures – consumption
spending + expenditures + investments.

We understand the efficiency of public spending in terms of efficiency and effectiveness (at minimal cost). As reported by a pair of economists Musgrave, the public projects are divided into divisible and indivisible, and the projects with a fixed (permanent) and intermittent (variable) budget. Public expenditures represent the flow of funds, it is

¹ Kubicová, J. et al. 2005. *Teórie vo verejných financiách: praktikum [Theory In Public Funds: practicum]*. – Bratislava: Publishing House EKONÓM, .

a financial term thus they represent funds in a given volume and structure, with certain principles of allocation, implementation and monitoring of performance. Public expenditures as a budget category are reported and funded in one budget period – a calendar year. Public projects and spending programs are often long term and represent the terms indicating material economic processes; they are funded through the programs and grants for specific production of public goods; those are socially oriented transfers. A lot of authors have been dealing with the theoretical and practical aspects of the past also today. Musgrave deals with the area of the costs and benefits. Hamerníková and Kubátová deal with Efficiency of public spending and public projects. J. Nemec deals with the methodology of evaluation of public programs and projects. J. E. Stiglitz deals with the inefficiency of the private sector in the provision of public goods. J. Rektořík and J. Šelešovský deal with a system of the financial control in public administration. G. Wright and J. Nemec dedicated their research to the issue and problems how to enhance the efficiency of public services in the book *The Management of public administration theory and practice*.

According to Stiglitz J. E. we distinguish macro – and micro economic aspects of public expenditure.

Macroeconomic relations characteristic for public spending, projects and programs are:

1. public expenditure on the purchase of goods and services constitute one of the important elements influencing the aggregate demand and production,
2. under active fiscal policy, the public expenditure, projects and programs act as a multiplying factor,
3. are an essential part of the cycle of revenue and expenditure in the economy (public sector enters the cycle, through their institutions, specific spending projects and programs),
4. growth of these expenditures and the growth of the public sector affects the overall employment and production in the economy.

Microeconomic aspects of public expenditure cause substitution and pensioner effects. The essence of the substitution effect is the change in consumer behavior as a result of the provision of public expenditure. In the pensioner effect there is no effect of changing the behavior of individuals. The consumers will be able to consume more, but do not change their preferences.

The aim of this paper is to highlight the importance of financial and accounting aspects of government expenditure and the autonomy from the perspective of a transparent display of financial flows in the public sector in Slovakia. Based on the content analysis method, the amount of the collected data and expert studies the achieved results and conclusions have been formulated.

2 Financial Management of the Public Spending

Justification public spending is linked to the existence of public goods. In an efficient allocation of public expenditure, the financial management and control of public expenditure is inevitable. The very process of public goods providing is governed by the public administration (central government and autonomy) and in the view of the individual components of the management activities of the public administration, the control is necessary in the public administration. A perception of control in close connection with the control action is now common to most definitions of control. It represents a summary of activities, through which we examine whether the stated results have been reached³ and, based on the resulting findings, in case of adverse events, the measures to overcome them are suggested. The financial nature of economic activity causes that in the process of transforming of inputs (resources) into outputs the financial management is an important part of management activity. The essence of the financial management has been shown in Fig. 1.

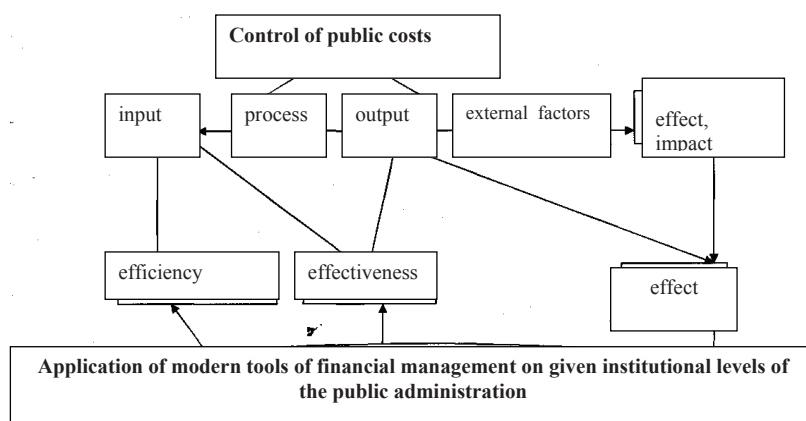
Shown approach is a consequence of the financial management of public resources, result -oriented and it is closely related to the application of the principle of value for money in public finances. The above mentioned principle has become a part of the Slovak legislation, too. The law on financial control states the need to respect the economy, efficiency and effectiveness in the management of public funds⁵. The compliance with this principle is reflected in the application of modern tools of financial management and strengthening of the economic terms in the financial control of the application of the audit. Public administration entities, as well as legal persons and natural persons to whom public funds shall be provided to, are responsible for the management with them and they it is mandatory for them when using these resources to keep up economy, efficiency and effectiveness of their use. This principle has been stated in § 19 art. 3 and 6 of the law on the public

2 Rektořík, J., Šelešovský, J. 2003. *Kontrolní systémy veřejné správy a veřejného sektoru* [Control Systems of the government administration and a public sector]. Praha: Ekopress, p. 12.

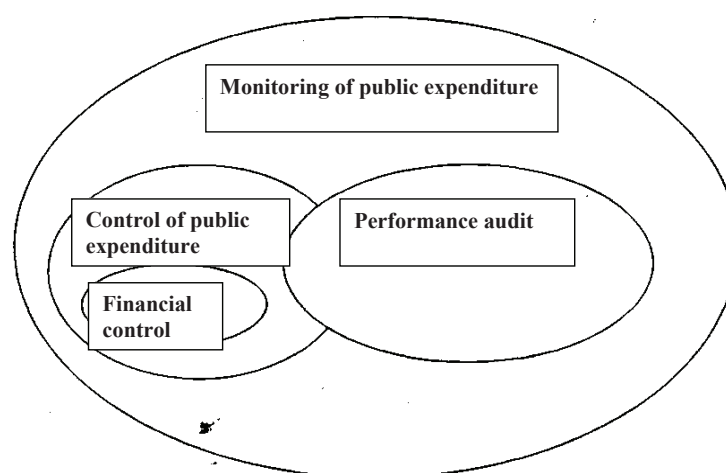
3 Dvořáček, J. 2003. *Interní audit a kontrola* [Internal Audit and Control]. 2. přepracované a doplněné vydání. Praha: C. H. Beck, s. 45.

4 Hronec, Š., Kuvíková, H., Meričková, B., Nemec, J., Mazúreková, M. 2004. *Vybrané problémy finanční kontroly* [Selected Problems of the Financial Control]. Banská Bystrica: Ekonomická fakulta UMB, s. 38.

5 Economy means minimizing the cost of carrying out the activity or the procurement of goods, works and services while maintaining their appropriate level and quality. Efficiency is maximizing of the results in relation to disposable public funds.



1: The essence of the financial administration in the field of public sources management



2: Financial control of public expenditure

Source: OCHRANA, F. 2003. *Veřejná volba a řízení veřejných výdajů* [Public Preference and Management of Public Expenditure]. 1. vyd. Praha: Ekopress, p. 184. ISBN 80-86119-71-8.

administration budgetary rules. The management of public funds has been regulated by a considerable number of laws and failure to comply with them may result in losses to the state party.

Effect means the relationship between the planned outcome of the activity and the actual outcome with respect to used public funds.

The extension of the subject matter of the management control of public resources in an aspect of performance and results is the way to further improving of the legal norms quality.

The main objectives of financial control are:

- economical, effective and efficient performance of public administration,
- compliance with the generally binding application of laws in the management of public funds,
- observed economy, efficiency and effectiveness in the management of public funds,
- timely, reliable information to the head of the public authority on the level of management of public funds.

Based on the above objectives of the financial control, it can be stated that the most important

parts of the financial management of public finances are – planning, budgeting, accounting, reporting and financial control. In the context of interrelations between the financial management and financial control it is worth mentioning that the challenging targets which are financed by public funds require the existence of procedures for the prevention and detection of errors at various levels of management (control procedures). The control activity must therefore be associated with a control performance. A very good example of the application of financial management procedures based on the close connection between the management activities and control activities is the financial management of the Structural Funds and the Cohesion Fund. The European Commission in providing these resources requires from the individual Member States to create such approval system of allocation of the overall financial of aid per country for each applicant that is not necessary an ex ante approval of the European Commission. In this system, the managing authority of the operational program has been responsible

for creating of such a method of allocation and control of financial assistance sources, which is in line with contractual obligations made between a Member State and the European Union as well as with the laws relating to the provided financial aid. *The sources of financial assistance of the European Union significantly affect public expenditure of the individual Member States and the behavior of economic agents.*

The core of the financial assistance resources allocation of EU is based on *openness* to the entities from both the private and public sector, provided, however, that they have to *submit a project* whose activity meets the objectives and priorities stated by providers in an open call. This is called the inquiry method of funding through public expenditure programs (program funding) – the element of competition for public resources and the principle of additionality is important (the applicant is involved in co-financing of the project). The crucial importance in the development of the project is to ensure the compliance of the objectives of the project activities of the applicant to the goals of the financial assistance. The base in the project creation is the project activities budgeting, the project sources funding budgeting and the project expenditure timetable. A separate chapter within the stage of the project creation is a financial analysis. The financial analysis differs significantly according to the type of the project. For the revenue generating projects it is necessary to analyze the funding gap of the applicant and the project impact on the applicant's financial situation. In the case of the investment projects it is necessary to analyze the financial and economic return on investment. For all types of projects, it is necessary to analyze their financial sustainability. At the project implementation, it is also necessary to monitor the compliance with the stated objectives of the project. The control activity plays an important role in this stage. For example, in conditions of Slovakia, in terms of co-financing (the principle of complementarities) the problem is that most government entities (municipalities) are under funded and the resources availability of the financial assistance of the EU is thus hindered. In terms of resource allocation in the autonomy administration inefficiency arises. Most municipalities have received the funds from the EU to modify and beautify the centers of towns and villages, while those communities have not obtained the resources to build sewers (in the future it is expected that the municipalities with the number of over 2,000 inhabitants will be penalized by the EU for not built drains). In the allocation of financial assistance funds from the European Union there should be applied the principle of the preferential resources approval

for basic (i.e. necessary) needs of the autonomy administrations.

3. The Accounting Aspect of Public Expenditure

Through the accounting methodology valid from 1st January 2008, the concept of transfers, which are current expenses, capital expenditures, grants, subsidies and contributions, was introduced into the state and autonomy government. In case of the transfers those are mutual financial and non-financial relations which are divided among the public entities into four groups:

1. central administration – administrators of the state budget chapters (34), and their budgetary and contributory organizations,
2. regional self-government – municipalities (about 2,900) and higher territorial units (HTU – 8), and their budgetary and contributory organizations,
3. a special group of public administration – public universities (22), the Social Insurance and Health insurances (4), state funds (3), the Slovak Cadastral Fund, the National Property Fund, the Slovak National Centre for Human Rights, the Nation's Memory Institute, the Office of Health Surveillance and the Slovak Consolidation PLC, as state-owned enterprises,
4. other entities – businesses, civic associations, foundations, the European Union and the associated and jointly controlled entities, established for business purposes.

The listed division of the public administration provides separate monitoring of transfers between individual groups. Since the state and local government entities are financed through transfers (i.e. expenses), the cost accounting in the accounting group 58 is a uniqueness – The costs of transfers and the costs from the contributions revenue and income statement in the accounting group 68-Incomes from transfers and budget revenues in the state budgetary and contributory organizations, and in the account group 69 – Incomes from transfers and budget revenues in municipalities and higher territorial units and in the budgetary organizations and contributory organizations established by municipalities or regional governments.

Watching of the transfers is important for the subsequent preparation of consolidated financial statements and summary financial statements of the public administration. In terms of financial transfers to the provision of funds away from the founder and at the non-financial this is resources using by the budgetary state organizations, namely through the expenditure of the expenditure account of the state treasury⁶. The transfers (current

⁶ The government entities are mandatory clients of the State Treasury. For the state budgetary organizations (SBO) for accounting of expenditure so called drawing account of the treasury is used. On the account 225 – Account...

expenses, capital expenditures, grants, subsidies) are divided under several aspects. The main aspect is the division of the transfers into the current and capital transfers, further, a purpose transfer or non-specific transfer. From an accounting perspective views, an important fact is from where the transfer passes, or whether the transfer has been provided by the founder, the transfer provided by another entity within the public administration, or even from the entity outside the public administration.

By joining the European Union, the Slovak Republic (SR) has received the authorization for funding from the EU structural funds, which are designed to bridge the gap between economically stronger and weaker regions in the EU. The Structural Funds finance multi-annual regional development programs jointly prepared by the regions, Member States and the EU. In the accounting units of the public administration and autonomy administration, the transfer from the European Communities is treated as a transfer from an entity which is not the subject of the public administration and which is charged to the debit of accounts of the group 22 – Bank accounts and credited to the account 371 – Clearing the European Communities or the account 372 – Transfers and other settlements with other entities outside of the public administration. For example, the municipality/HTU credits in account 371 – Clearing the European Communities, charges the adoption of the sources from the EU budget in the form of grants, subsidies (221/371). In the event that an accounting entity receives funds from the state budget, municipal budget or the budget of HRU, it accounts for these funds as for the transfers by means of the account group 35 – Clearance between public administration bodies. In the period of assistance from the European Union sources, the financial control of the management of the above mentioned resources in the Slovak Republic was insufficient and particularly the effective system of financial management and control at the level of the applicant for financial support was absent. Therefore, the Ministry of Finance proceeded to the establishment of the so-called Audit Authority, which fully complies with the requirements of the Council of the European Union. From the establishment

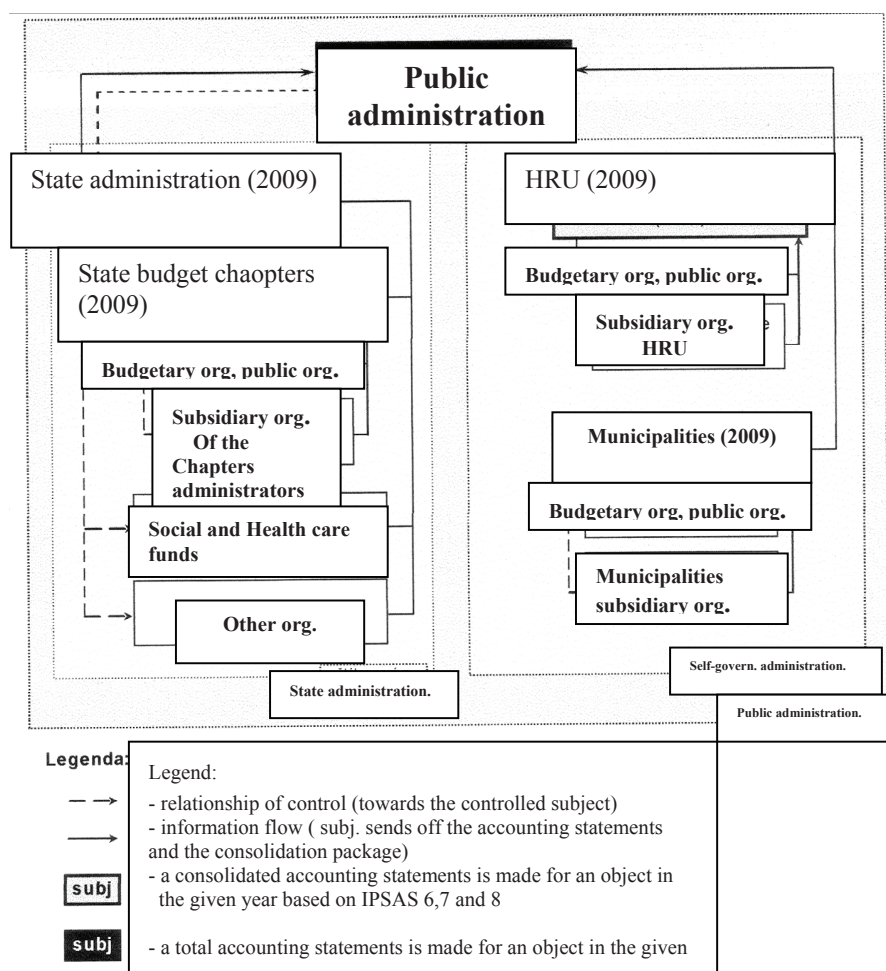
of the audit transparency increase and fair presentation of financial flows in the public sector for the implementation of accrual accounting in the public sector can be expected. Also, when drawing up individual and consolidated account balances it is necessary to apply the current accounting principle⁷ because the key challenges in fiscal reporting are:

- recognition of the fiscal position of the government sector in the ESA 95 methodology,
- formation of the consolidated fiscal accounts under GFSM2001 methodology (methodology requires consolidated reporting of statistical sectors which means the elimination of transactions within a single statistical sector).

For the financial year 2009, state budget chapter administrators, municipalities and higher territorial units passed to making of the consolidated financial statements according to the international accounting standards for the public sector (IPSAS – International Public Sector Accounting Standards). Total 1,130 accounting units of the state administration and local governments showed consolidated financial statement (1,100 municipalities, 8 HTU, about 20 chapter administrators of the state budget). When making a consolidated financial statement, the entities of the state and local governments comply with the law No. 431/2002 Coll. about accounting and measurements of the Ministry of Finance No. 27526/2008-31, which provides specific details on methods and procedures of consolidation in the public sector. To the Accounting Act the concepts of the parent accounting entity and subsidiary accounting entity have been introduced. The Accounting Act imposes to the parent accounting entity the obligation to draw up consolidated accounts. On the compilation process itself also the subsidiary accounting entities participate (i.e. state budgetary organizations, state subsidized organizations, budgetary organizations established by municipalities, contributory organizations established by municipalities, budgetary organizations established by the higher territorial units, subsidized established higher territorial units, business companies with a share of state municipalities and higher territorial units). The difference in preparing of the consolidated financial statements is in the number and type of the consolidated

6 ...of government budgetary expenditure is accounted on the disbursement of funds provided to the state budgetary organization in accordance with the binding indicator of the spending limit. Account 222 – Expenditure budgetary account is aimed for a budgetary organization established by the municipality or the higher regional unit. In the account 222 shall be accounted about the funds supplied by the finance provided to the budgetary organization of the municipality or organization HRU.

7 In Slovakia the account units of the state administration and local governments account using the methodology based on an current principle (i.e., based on a comparison of timely accrued expenses and revenues). The advantages of the accrual accounting are: accounting for timely accrued expenses and income (account group 38), accounting for transfers, implementing of the accounting for revenue in the accounting class 6 – Revenue, profit survey comparing costs and benefits, multi-annual outlook in the financial statements and the audit more efficient thanks to the creation of an integrated information system.



3: Total financial statement of the public administration

Source: Sabiková, L. 2009. Aktuálny princíp v reforme riadenia verejných financií na Slovensku (Accrual Principle in the Reform of the Public Finance Management in Slovakia). *Ekonomické rozhlady*, 2: 263–272.

entities. For example, the consolidation units of small communities usually contain only a few accounting entities, while the Bratislava Autonomy Region (HTU) has in 58 organizations and 28 subsidized organizations its institutional authority. Furthermore, the self-governing region has shares in four trading companies and it also establishes social care facilities such as nursing homes, cultural institutions: i.e. theaters and libraries. In Slovakia, there are also the municipalities that have neither any budgetary organization nor an organization or any subsidiary of a company established. These municipalities will prepare and submit only their individual financial statements, which are counted into a comprehensive whole for the purposes of compiling of the aggregate financial statement of the government administration.

For the accounting period of the year 2010 the following entities were parts of the whole for the compilation of the summary financial statements,

1. government, consisting of the budgetary organizations and subsidized organizations

founded by the state and the companies owned by the state,

2. self-government, consisting of the budgetary organizations and subsidized organizations in the institutional competence of municipalities, cities and autonomous regions and business companies on equity on municipalities, towns and higher territorial units.

For reporting of the aggregate accounts statement of the public administration in the year 2012 (i.e. for the accounting period of the year 2011) a substantial change is the expansion of the total whole (changes published by the Decree MoF on 23 Dec. 2011 No. MF/24141/2011-31 "Accounting policies" and by the amendment of the Act no. 431/2002 Coll. concerning accounting, i.e. the law of 1 December 2011 No. 547/2011 Coll.). In 2012, the total whole will consist of the entities of the state administration and local governments, other government entities, state businesses, RSR and Eximbank. By applying the accrual basis of accounting in the state it will be possible to use the accounts outputs for the fiscal reporting.

SUMMARY

Justification of the public spending is linked to the existence of public goods. In an efficient allocation of public expenditure, the financial management and control of public expenditure is inevitable. From the establishment of the Audit Authority we can expect increase of the transparent display of the financial flows in the public sector in connection with the implementation of accrual accounting in the public sector. Accounting about transfers has been introduced into the accounts methodology of the state and local government. Watching of the transfers is important for the subsequent preparation of the consolidated financial statements and the summary financial statements of the public administration.

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Contact information

Marián Kočner: marian.kocner@uniag.sk