

FINANCIAL STRATEGIES FOR THE ROMANIAN LOCAL PUBLIC ADMINISTRATION*

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Abstract

Public administration reform at all governmental levels constitutes an important component of the transformation process from a centralized system to democratic governance. This process involved important legislative and institutional changes in order to fulfill the principles of a market economy and the European Union standards based on transparency, predictability, accountability, adaptability and effectiveness. Therefore, in a continuing extension of the citizens' needs, Romanian public administration reform, especially at local level, is concentrated on quality of public services based on citizens' needs and increased performances in the context of a necessary decrease of budget expenditure, taking into consideration the actual financial constraint. In this context, it is useful to investigate the financial strategies of the local public administration based on the Romanian experiences that consisted in important public resources decline because of the financial crisis.

1. Romanian local public administration

Starting with 1990, the Romanian economy was in a continuous transformation process from a transition country, during 1990-2003, to an emerging market and developing country, during 2004-2006, and an emerging and developed country since 2007. Important legislative and institutional changes were imposed in order to fulfill the challenges of all different periods.

The most important period was 1990-2003 when the state's role, functions and responsibilities were gradually developed. As in a transition country, policies in Romania were oriented to macroeconomic stabilization, microeconomic liberalization, institutional restructuring. The transition period was characterized by legislative and institutional instability, which were improved afterward. In addition, the responsibilities of all governmental levels were clarified. The local public administration took over many of the central responsibilities based on the fact that local authorities are more capable to identify the needs of the citizens and, therefore, to assure the necessary public services (Câmpeanu and György, 2010, p. 69). This transformation was necessary taking into consideration the fact that 'during communism, local governments (i.e. territorial divisions of central government controlled by the Ministry of Interior) were characterized by little political autonomy and high levels of social and economic responsibility' (Cepiku and Mititelu, 2010, p. 64).

Structural and institutional reforms during 1990-2003 have placed Romania in the group of emerging countries characterized by sustained economic growth, macroeconomic and financial stability in order to support the real convergence and the long-term sustainability.

The recent concerns for the Romanian local public administration are to ensure high quality services provided to the citizens and to improve the management capacity at all local structures. In order to assure these objectives important changes were made regarding the distribution of responsibilities during the decentralization process. Despite all efforts, Romania had a low degree of decentralization of almost 30.2%, on average during 2000-2008 (Câmpeanu and György, 2010, p. 70) in the context of a low degree of local financial autonomy of almost 15% based on the share of revenues determined by sub-national authorities to total revenues of local budgets (Câmpeanu and György, 2009b, p. 900).

Moreover, Romania faces new challenges regarding the economic growth, governance and policies needed to improve people's lives at both national and sub-national levels and to assist other states in the long process of transition and development according to the Millennium Development Goals (MDG).

The aim of this paper is to investigate the financial strategies of the local public administration based on the Romanian experiences considered in the context of an important decline in public resources because of the financial crisis. This paper is structured as follows: the main section addresses some aspects on Romanian financial strategies highlighting the main subsystems that we had identified (budget, revenue, procurement, human resources, disbursements, repartitions, debt management). Some

concluding remarks of our study, stressing the impact of the described strategies, are presented in the final part of the paper.

2. Financial strategies

Any financial strategy should take into account the main components of the activity that should be integrated as a whole. Due to the interdependencies between subsystems, strategy development is made in a logical way beginning with those activities which can be independently controlled by the organization. Afterwards, other subsystems will be added based on previous ones.

In order to assure the efficiency and transparency for public funds, financial systems should be reformed. Integrated financial management information systems (IFMISs) have become core components of financial reforms in developing countries (Peterson, 2007, p. 323) using latest IT facilities. Each IFMIS integrates a number of subsystems (modules) which permit on-line financial management and financial reporting. Such a system was described by Abate and Chijioko (Figure 1) taking into account their vision about the role of IFMISs. From this model, we can tailor a system nearest to the Romanian local authorities' requirements.

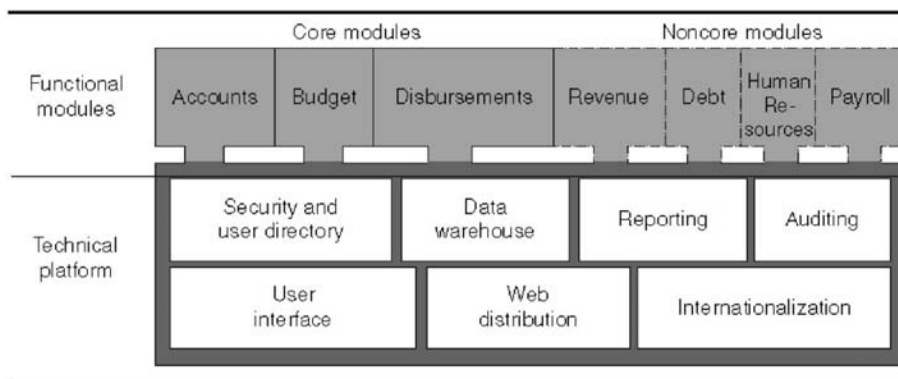


Figure 1: Features of a typical IFMIS

Source: Abate and Chijioko *apud* Peterson (2007, p. 328)

The IFMIS is a tool designated to help local authorities to manage their financial issues. However, in the same time it can offer precious data and reports to external parties which have to monitor or control the entity's financial situation. For example, in Romania, the Court of Accounts is focusing on audit in order to assess the legality of spending, in particular the ceilings for expenditures set out in the budget laws are observed (Tiron Tudor, 2007, p. 133).

The Romanian financial management was continuously reformed, especially between 2002 and 2006. The new public finance legal framework (entered into force on 1 January 2003) took a series of best financial practices from more developed EU countries. The public sector abandoned cash-based accounting by introducing the philosophy of New Public Management based on an accrual system (Ștefănescu *et al.*, 2010, p. 230).

The implementation of integrated financial management systems can be obstructed by different factors. The smaller the entity is, the easier is to achieve success. This is why IFMIS can be implemented easier in local administration where organizational structures are less complex. At the level of the decentralized public institutions, where the use of budgets is more lenient, there are more favorable conditions to achieve successfully the targets of the operational management. For example, a county council or a local council has a budget that can be the starting point in building a budget system, related to the area of management policies promoted: education, healthcare, culture, sports, entertainment, infrastructure, sanitation, sewage-water etc. (Verboncu *et al.*, 2010, p. 172).

In the Romanian local administration, the main subsystems that we had identified are budget, revenue, procurement, human resources, disbursements, repartitions, debt management. Depending on each authority's situation, some of these components could not appear (for example, those authorities that did not borrow resources do not have the debt management component).

2.1. Budget strategies

Local government has a two-tier structure with the county level consisting of 41 counties and the municipality of Bucharest, and the lower tier made up of a large number of towns and communes (Ruffner *et al.*, 2005, p. 37). From an organizational point of view local administration is structured in local authorities and subordinated public institutions. While the first category represents the power of the local authority, the latest are public service providers. The local competencies depend on the rate of decentralization admitted by the political decision system (Profiroiu and Profiroiu, 2007, p. 43).

Each local community has its own budget. Local budgetary resources consist of (in descending order): VAT amounts, shares from income tax, other local revenues, subsidies, local taxes, and donations. The Romanian local budgets are dependent on intergovernmental grants, these being used in many countries to finance sub-national spending and to implement national policies (Bergvall, 2006, p. 111).

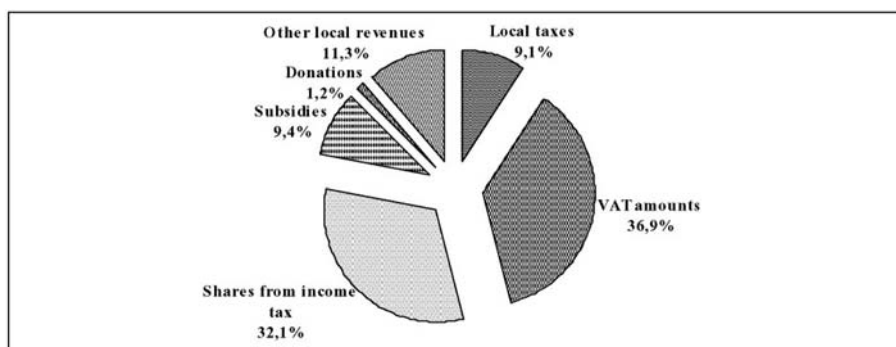


Figure 2: Structure of the local budget revenues in 2009 – The case of Romania

Source: Miricescu *et al.* (2010, p. 489).

Romanian budgeting is based on line-item budget which is extensively used. It offers advantages such as: (i) it is comparatively easy to prepare and does not require sophisticated financial skills; (ii) it is simple to administer, facile to understand, revenues and expenditures can be easily monitored (Lazăr and Inceu, 2004a, p. 86). Line-item budgets list total departmental appropriations by items for which funds will be spent (Lazăr and Inceu, 2004b, p. 168) presenting a detailed destination map for each amount. The excessively analytical classification pattern could reduce the efficiency of the organization by imposing financial barriers to management (György and György, 2010, p. 363). We think that correlating budgets with treasury's monitoring should be made on-line by using in budgeting expenditure chapters and titles, while other classification items (subchapters, articles and paragraphs) can be used in reporting.

From the point of view of integrated financial management, the budget is the first document, which should be at the authority or institution's disposal. No expenditure should be done without a valid budget. The local budget is a financial document that is approved by county councils or local councils, the local organizations can propose the draft, but do not have any power in deciding on the final version. Budget approval is defined by the scope of budget coverage and level of documentation of requests, by the scope of approval authority and legislative discretion in budget adjustment, and by the timetable for legislative action (Mullins, 2007, p. 222). The main budget managers can approve reallocations (after July 1st) inside a chapter canceling the initial laborious line-item approval of the legislative or deliberative body. Hence, simplifying the budget pattern will lead to the same result: local budgets respect entirely the approved amounts for each chapter, while subdivisions are reallocated in accordance with managerial needs.

The challenge for local budgeting is represented by the migration to accrual budgeting. There is no official deadline established yet, but it will be mandatory in the future (possibly not in next decade). Nowadays accrual-based budgets are used on a reduced scale, but in the last years important steps have been taken to extend them. The migration from cash-based budgeting to accrual-based budgeting is done gradually, especially by completing the information from the cash-based budgets with specific information from the accrual-based budgets (György, 2010, p. 15).

A local IFMIS should have as first component the Budget module. Each entity organized as legal person should have uploaded the budget by the legislative or deliberative body's technical staff. These budgets should be consolidated and balanced with revenues in order to respect the principle of equilibrium.

2.2. Revenue collecting strategies

Local revenues can be divided into two different categories: taxes and fees collected by the local authority (including grants from central budgets) and fees collected by each local public service provider. All local revenues should be recorded in a single financial document, all the same, the institution is empowered to collect and administer revenues. Depending on the collected revenues, expenditures can be made in the limit of amounts available.

Local authorities get monthly majority of financial resources directly from the National Fiscal Administration Agency which is responsible with collecting major taxes (income tax, VAT, corporate tax etc.). Taxes administrated by local authorities are mostly property taxes (on buildings, lands, and cars) and authorizations in construction.

The strategies adopted by the local authorities in order to collect taxes and fees should be based on modern technology complementary to traditional means. The authorities should allow taxpayers to use multiple modern ways of payments: on-line payments on authority's web site, cards at tax payment desk, direct debit etc.

Access to the on-line payment system must be provided after accessing the main web page of the municipality and user identification. In addition, the user must be allowed to connect both from private and public computers. The municipality's web page must contain clear and visible information related to local taxes and imposts, the due dates, the calculation methods, the accepted banks and credit cards and a user's guide for the system (Petruşel, 2006, p. 108).

2.3. Procurement strategies

Local authorities do procurements of goods and services necessary to current activities, such as providing free of charge goods for different categories of beneficiaries (for example mothers get free milk powder bought from public resources) or developing public infrastructure (for example local authorities buy slides to offer playgrounds in parks). Procurement mainly consists in goods, but services also consolidate their position. The range of procurement is quite large and dynamic in time. Procurement strategies are reviewed annually when acquisition lists are set up. Here are also differences between visions in different institutions (Țiclău *et al.*, 2010, on a study on service procurement marketing).

In order to use efficiently the public money, procurement legislation sets up rules that encourage transparency and competition between bidders. From public institutions' point of view, these new rules contributed to the reduction of the expenditures, but also caused a supplementary cumbersome bureaucratic procedure (György and Câmpeanu, 2010, pp. 115-116).

Investments are a special category of procurement. These have a significantly higher value, are implemented in a certain period of time, and require special financial treatment. In some cases, investments can be implemented in more than one fiscal year, so public institutions should be consequent in finishing all projects they initiated. Risks are higher in case of investments, so financial management should be more careful in monitoring it.

Public institutions' procurements can be replaced with public-private partnerships (PPPs) when financial resources are not enough or when private management can assure better outputs. PPP contracts are increasing although there is no consensus in this issue. This increase in PPP contracts is often attributed less to the intrinsic qualities of such contracts than to governments' attempts to evade budget constraints (Maskin and Tirole, 2007, p. 3).

A new tendency in Romanian public institution's activity is outsourcing. Use of outsourcing in public institutions aims (primarily) to reduce public spending, along with the increased sensitivity of governments, to increase the labor productivity of public institutions and public officials, with fewer resources at hand, and to optimize their business (Lazăr *et al.*, 2010, p. 144). Outsourcing is a good option when administrations have to follow strict rules in limiting the number of employees or is in impossibility to pay motivating wages. Outsourcing is not necessarily the result of calculations that lead to increased efficiency in the use of public money, but may be an expensive saving solution. Usually outsourcing generates fewer employees fact which shows well in statistics. New trends indicate a shift to civil conventions that tackle the duties from job descriptions (for example in theatres actors are paid more on copyright contracts).

Procurement financial management should stress the efficiency, consisting in providing all the goods and services appropriately, quantitatively, and on time. Alternative solutions should be taken into account when efficiency is expected.

2.4. Human resources strategies

Human resource management should focus on quality. Public institutions need sufficient employees, properly prepared and motivated professionals. Human resources capacity is critical to the quality of public administration in any country. Capacity development of human capital requires effective implementation of a holistic and homegrown strategy, underpinned by long-term political commitment (United Nations, 2004, p. 16).

From a financial point of view, employers should encourage incentive systems in order to motivate employees to do their job in the best way they can. In some cases, abuses happened because professional criteria did not represent the unique parameter taken into account. Recently the Romanian legislation restricted salary bonuses for public sector employees. For a limited timespan, salaries have been reduced drastically with a quarter.

Human resource management should deal with two types of employees: public servants and contractual employees. The first category cannot be the object of outsourcing because they represent the relation between the public authority and citizens. The second category of employees could offer their services also as experts. Persons who choose to be employees in public administration also seek stability and job security. Those who accept to deliver services as experts can obtain larger revenues than the salary usually paid for similar activities, but their relation is related to the length of collaboration.

In public administration, human investments are performed using the following methods: (i) training of employees; (ii) continuous learning (at least one program every three years); (iii) specialization on interest field; (iv) well-known training institutions and quality programs; (v) programs recommended by specialized institutions (Câmpeanu and György, 2009a, p. 119).

2.5. Disbursements and repartitions strategies

Cash management is a core issue in any financial management strategy. Disbursements can be made only when resources are available. Correlation between encashment and disbursements are mandatory because short-term borrowing is impossible. If there is insufficient encashment, disbursements are delayed until sufficient money is cashed.

Public institutions use the services of a single bank, respectively those offered by the State Treasury. Institutions are captive consumers; a unique mandatory assignation to a certain unit of the Treasury exists. Commercial banking services can be used only in a small range of cases: foreign currency payments, borrowings, foreign amount management etc.

Wage payments can be done only between the 5th and the 15th of each month when are rewarded the activities of the previous month. Goods and services can be paid in the last week of each month, beginning with the 24th of the month. EU project payments can be made during the entire month without supplementary restrictions.

Repartitions are made by local authorities to subordinated institutions which do not have own revenues. Repartitions are made from local budget encashment; allotted amounts reduce the resources remained at the authority's disposal. Repartitions are distinctly made on destinations, using separate accounts for each expenditure title: wages, goods and services, EU projects, transfers, social security, investments. If resources are not enough, usually repartitions for salaries are made first, while the rest of repartitions are made in the last decade of the month.

2.6. Debt management strategies

The financial strategies indicated above involve financial resources of local budgets. In order to finance all the local budget expenditure and local investments, local public authorities are able to borrow important amounts from domestic and foreign creditors. Those local public loans are components of public debt. In order to avoid an irresponsible comportment of local public authorities, those financial obligations are limited by the Local Public Finance Law no. 273/2006. According to article no. 63, the administrative-territorial units are not allowed to access loans or to guarantee any loan if the total annual debt due to contracted loans and/or guaranteed, interest and commissions, including the future loan to be contracted and/or guaranteed in that year, exceeds 30% of their total own income (taxes, fees, contributions, other payments, other income and allowances deducted from income tax). Therefore, a direct relationship between local financial autonomy and local loans is established (Inceu, Lazăr and Zai, 2005, p. 53). This restriction is necessary in order to assure the sustainability of local public finance on the long term.

Despite of this limit, many local public authorities had encountered some difficulties regarding the payments for local public debt services especially for municipality bonds. In order to assure the necessary financial resources, the authorities proceeded to a new issue of municipality bonds in order to finance other bonds. This is a common practice for the government that refinances important parts of its debt. Therefore,

this method was extended from central to local government. In addition, the local public debt involves activities such as: (i) issuing loans; (ii) registering the loans; (iii) payments of interest, rates for local loans; (iv) reducing the effects of local public debt risks. An important aspect of local public debt management consists in the evaluation of those risks, especially for the credit risk (Lazăr, Inceu and Zai, 2005, p. 67).

Local public authorities are capable to use specific instruments such as swaps on interest rate, currency, in order to reduce the magnitude of many of the local public debt risks. Consequently, local authorities use public loans in order to finance important objectives capable to assure the local development taking into consideration the advantages of public loans at the general and specific level (Inceu, Lazăr and Zai, 2005, p. 56). This conducted to a continuous increase of local public debt from an almost inexistent level during 2000-2004 to almost 10% of total public debt in 2008 based on the data from the Romanian Ministry of Finance.

Local public debt is used to assure finance support for investments because local budgets are balanced (Câmpeanu and György, 2009b, p. 901) according to the restriction imposed by the equilibrium principle defined in Local Public Finance Law no. 273/2006. The effects of those investments at local level are capable to sustain local development and to contribute to the improvement of the financial and budgetary indicators that quantify the quality of public finance at local governmental levels. Those are more evident because the financing capital investments should assure the principles of fairness, promptness and efficiency (Lazăr, Inceu and Zai, 2005, p. 72).

The increase of local public debt highlights the important role of local public finance in public economy. In this context, the impact of local public debt could be more serious. The dynamic of local public debt expresses the migration from central to local financing of different public interest areas in order to assure the supplementations of local resources (although central budgets remain in deficits). However, the evolution of this variable indicates that there are important differences across countries. For instance, on average during 2000-2008, the Romanian local public debt is almost 1.9% of GDP compared with 5.1% of GDP for EU-27.

3. Conclusions

Public institutions need to implement integrated financial management strategies in order to optimize and coordinate the activities related to core financial modules: budget, revenue, procurement, human resources, disbursements, repartitions, and/or debt management. A well-designed integrated financial management system should allow a well-prepared budget, high level of revenue collection, efficient spending of public money, motivated employees, and good cash management (own and borrowed resources). An integrated financial management system offers equilibrium between the institution's internal and external environment from a financial point of view.

To meet the challenges, integrated financial management system should be dynamic in order to be changed each time: economic environment permits to deal with alternatives, outputs are not satisfactory, and legislation introduces new rules or

restrictions. Adaptation of the system should be made also when periodic assessments (including audits) point malfunctions.

The integrated financial strategies should influence the internal activities, on one hand, and the relations with the economic setting, on the other hand. Internal impact is felt by employees who benefit from decent working conditions, on time paid wages, simplified and automated processes with financial documents. External impact is felt by beneficiaries who get quality services on time, find motivated and content servants, and get on time cashed bills for deliveries.

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