Making public finance public : subnational budget watch in Croatia, Macedonia, and Ukraine

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Edited by Katarina Ott

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and Public Service
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Foreword

This volume provides three fascinating case studies of subnational budgeting in Croatia, Macedonia, and Ukraine. These studies, together with an excellent cross-country synthesis, will serve as a valuable resource to those in universities, civil society organizations, parliaments, and the media who are concerned with improving transparency and accountability in public financial management.

This publication contributes to a growing international movement to improve budget transparency and broaden participation in public budgeting. While budgeting has traditionally been considered the exclusive preserve of the executive branch of government, this situation is changing. Over the past ten to fifteen years, researchers and activists, together with legislators, auditors-general, and journalists, have been working to bolster their own knowledge and capacity to participate effectively in the budget process.

THE WORLDWIDE GROWTH OF BUDGET WORK

The most impressive growth in budget analysis and advocacy capacity has been in civil society. Just a decade ago, only a handful of independent civil society researchers and organizations were working to ensure that government budgets are responsive and accountable to the public. Since then, organizations and researchers in more than sixty middle- and low-income countries in Africa, Asia, Eastern Europe, and Latin America have taken up this work.

The reasons why civil society researchers and organizations are gravitating to applied budget work are not new. The budget has for a long time been vital to the functioning of the economy, to anti-poverty and other government policies, and to open decision-making. What is new is an international environment that is much more conducive to transparent and inclusive budgetary processes.

One major catalyst for budget work has been democratization. Budget work frequently flourishes in countries that are undergoing a democratic transition, since the increased government transparency and public participation that generally accompany such a transition present greater opportunities for civil society involvement. A second catalyst has been the trend toward decentralization that may bring budgets closer to communities and make the issues more real to them.

As a result of these and other catalysts, a wide range of researchers and groups now conduct budget work, from policy-oriented think tanks to membership and community-based organizations. Some groups were established specifically to advance budget issues, while others have undertaken budget work to strengthen their existing policy and advocacy work. Several researchers and groups have been established or incubated within an academic environment, and some groups have been initiated within the public sector.

Budget work has proven to be effective in a wide range of political systems. It has flourished within commonwealth and parliamentary systems, despite the inherently closed nature of the budget process in these systems, and it has succeeded in presidential systems as well. Though budget work has taken root most easily in established and emerging democracies, it has proven resilient even when faced with an extreme paucity of data (as in Mongolia), autocratic regimes (as in Azerbaijan), extensive corruption (as in Nigeria), or political turmoil (as in Indonesia).

An important related observation is that civil society engagement in budgeting complements greater independent oversight of the budget by the legislature, media, and auditors-general. In fact, a partnership between civil society budget groups and these three actors is often the starting point for local independent budget work.

TASTES OF SUCCESS

Although the trend is relatively recent, emerging evidence shows clearly that civil society engagement can add value to public budgeting in two respects. First, broader engagement by civil society is associated with increased budget awareness and literacy, more effective participation by a number of oversight actors, and improved budget transparency. Second, civil society budget work can also lead to enhanced budget systems, shifts in pro-poor allocations, and an improvement in the effectiveness and efficiency of expenditure.

One exciting example of these impacts is the work of Fundar, an NGO based in Mexico City. In 2002, Fundar conducted research to hold the government accountable to a major policy commitment to reduce rural maternal mortality. Working with a coalition of civil society organizations on reproductive health issues, Fundar determined the real costs of eradicating maternal mortality and analyzed actual government spending on maternal mortality, contrasting the allocations for maternal and reproductive health with other areas of spending and pointing out regional imbalances in the distribution of these allocations.

Together with the coalition, Fundar arranged a series of meetings on maternal mortality with legislators, including a televised forum in which public officials took part. Along with related work to secure media coverage of maternal mortality, these efforts paid off.

The government substantially increased its funding for programs designed to improve maternal health, expanding the funding for one such program nearly tenfold.

Another recent success story comes from Uganda. An NGO coalition called the Uganda Debt Network has contributed significantly to the country's anti-corruption efforts by training and building a community network to monitor whether government and international donor funds intended for anti-poverty programs such as health and education are actually delivered. These monitors then present their findings, including any evidence of corruption or mismanagement, to local officials and community members and push for corrective action.

In a relatively brief time, this initiative has helped to reduce corruption in the flow of government resources to schools and hospitals, identify problems in funding to local governments, and obtain increased funding for anti-poverty programs. It also has led the government to invite civil society groups to participate in its budget planning discussions and anti-poverty initiatives.

TWO IMPORTANT CHALLENGES

Despite the explosive growth of civil society budget work around the world, several important challenges remain for the growing movement. The research in this volume helps to deepen our knowledge base on two of these challenges.

First, while strong examples of budget groups exist in Croatia and Poland, budget work seems to be growing more slowly in Eastern Europe than in several other developing and transitional regions. Although many of the preconditions for budget work are met in large parts of Eastern Europe, such as the existence of a literate and skilled population, several other preconditions remain challenging, such as access to data and the development of an active citizenry. Yet, many countries undergoing transition have much to learn from the Eastern European experience of transformation, and these studies help to build our understanding of the economics and politics of transition.

Second, while budget work has successfully rooted itself in a wide range of political and economic systems, the majority of the work focuses on national rather than subnational budgeting issues. There are several reasons for this, including the tendency to centralize budget processes and budget reform in national government. However, as decentralization gathers steam, it becomes more important and appropriate to focus our energies on analyzing and influencing local government budgeting. As the case studies show, while decentralization can complicate the coordination and monitoring of budgets nationally, it often creates greater opportunities for citizen and local legislature involvement.

Not surprisingly, the case studies do not provide easy solutions to these challenges, nor do they even provide generic solutions for the three countries covered. But they do help us to tease out the specific dynamics of subnational budgeting in post-central-

planning environments. Each of the authors also helps us to appreciate the specificity of projects and activities that may help to advance budget transparency and accountability within each context.

Nevertheless, in many other respects, the case studies highlight a set of challenges that are all too familiar to budget researchers and activists around the world. Access to timely, accessible, and useful information and to formal and informal opportunities to participate in the budget process remain the major obstacles to all of our efforts. We need to approach the pursuit of improvements in both of these areas as two sides of the same coin. Improved information without enhanced capacity and willingness to participate is insufficient, as is participation capacity without access to information. Governments have a critical role to play in correcting this situation. But, given the long-standing tradition of exclusive and secretive budgeting, the onus is also on researchers and activists to take the initiative and break the mould.

The Open Society Institute's Local Government and Public Service Reform Initiative and Katarina Ott deserve our gratitude for producing a much-needed and extremely useful publication. Our collective responsibility is to make sure that these materials do not simply sit on our bookshelves, but are enlivened through our actions to make public budgeting public.

Warren Krafchik
International Budget Project
2006

Making Public Finance Public
Comparing Croatia, Macedonia, and Ukraine

Katarina Ott

SUMMARY

This chapter is about making public finance public and it gives a comparative basis to the subnational budget watch project that took place in Croatia, Macedonia, and Ukraine. It is based on a grant organized and funded by the Local Government and Public Service Reform Initiative of the Open Society Institute–Budapest.

The following questions have informed the structure of this project concerned with the disbursal of funds within local government budgets and subsequent monitoring by civil society actors like nongovernmental organizations as well as private citizens who ideally form into what this project loosely calls the subnational budget watch. In short, as its basis, this study asks: (i) Are citizens participating? Does legislation enable them to participate? Are there institutional arrangements for participation? (ii) Are budget data available, reliable, and timely? Could one compare actual with planned figures? (iii) Is it clear who is accountable for what? Does the executive branch of the government take in consideration external auditors' reports and/or requests from the legislative branch?

Irrespective of the opportunities for participation, of the availability, reliability, and timeliness of data, and of the accountability of governments to citizens, all three countries show poor participation and understanding of the concepts that support such subnational budget watch initiatives that are more substantial in more mature democratic models than those present in post-communist transition states. In order to de-alienate citizens and to demystify the budget and bring it closer to the populations concerned, further research and advocacy is needed. Like this study, it should raise awareness of the importance of the transparency of the budget, accountability of governments, and the participation of citizens, particularly at lower levels of government. Models and action plans vary from the establishment of monitoring committees in Croatia and strengthening the independence of budgetary users in Ukraine, to addressing citizens with reader-friendly budget guides in Macedonia.

1. INTRODUCTION

The intention of this chapter is to give a comparative study of subnational budget watch in three countries—Croatia, Macedonia, and Ukraine—based on a one-year project organized and funded by the Local Government and Public Service Reform Initiative of the Open Society Institute–Budapest.[1]

The countries in this sample face huge democratic deficits, large and entangled governments, and inadequate levels of public services, all accompanied by inactive populations. During the post-communist transition, it was expected that governments at the local and regional levels most likely would become more influential and that citizens would become more aware of the issues and participate at the local level. Simultaneously, citizens would begin to engage in the relatively new concept of a subnational budget watch. This has yet to happen.

In connection with the above set of problems, this study has sought to ask: (i) Are citizens participating? Does the legislation enable them to participate? Are there institutional arrangements for participation? (ii) Are budget data available, reliable, and timely? Could one compare actual with planned figures? (iii) Is it clear who is accountable for what? Does the executive branch of the government take in mind external auditors' reports and/or requests from the legislative branch?

This chapter expands briefly on the findings of the country chapters and more details can be found in each chapter respectively. Irrespective of the opportunities for participation, of the availability, reliability, and timeliness of data, and of the accountability of governments to citizens, all three countries show poor participation and understanding of the concepts that support such subnational budget watch initiatives that are more substantial in more mature democratic models than those present in post-communist transition states. In order to de-alienate citizens and to demystify the budget and bring it closer to the populations concerned, further research and advocacy is needed. Like this study, it should raise awareness of the importance of the transparency of the budget, accountability of governments, and the participation of citizens, particularly at lower levels of government. Models and action plans vary from the establishment of monitoring committees in Croatia and strengthening the independence of budgetary users in Ukraine, to addressing citizens with reader-friendly budget guides in Macedonia.

The remainder of this chapter will present the problems of establishing a subnational budget watch programs on the local level; analyze the similarities and differences among three countries, Croatia, Macedonia, and Ukraine; establish common problems and possible solutions, explain situations, expectations and possible actions in the future; and finally provide some conclusions.

Box 1.
Budget watch

Budget watch is a relatively new concept. It first requires a definition: Who are the watchers? And what, why, and how do they watch?

Budget watchers are usually nonprofit, nongovernmental organizations or individuals with the mission of promoting transparency or openness of government, its accountability, and citizen participation. They usually emphasize that budget is too important a document upon which revenues are gathered and public expenditures made to be left to the discretion of government bureaucrats and elected representatives. Citizens as taxpayers contribute to the government treasury and they should also have a say in the distribution of these funds. This is why budget watchers insist on insight into the collection of revenue and distribution of expenditures, dealing with issues like equity, fairness, and efficiency. To facilitate this process, they insist on the transparency of budget documents and budgetary processes and the possibility of citizens to participate therein. The final goal is to achieve more accountable government.

Typical activities of budget watchers include budget analyses and distribution of results in form of newsletters, briefs, citizens' budget guides, and various other publications. They also participate in public hearings, public debates, and various lobbying and advocacy activities.

Budget watchers may aim at general budget transparency, accountability, and participation or may specialize in some topics like poverty, education, health, environment, or gender.

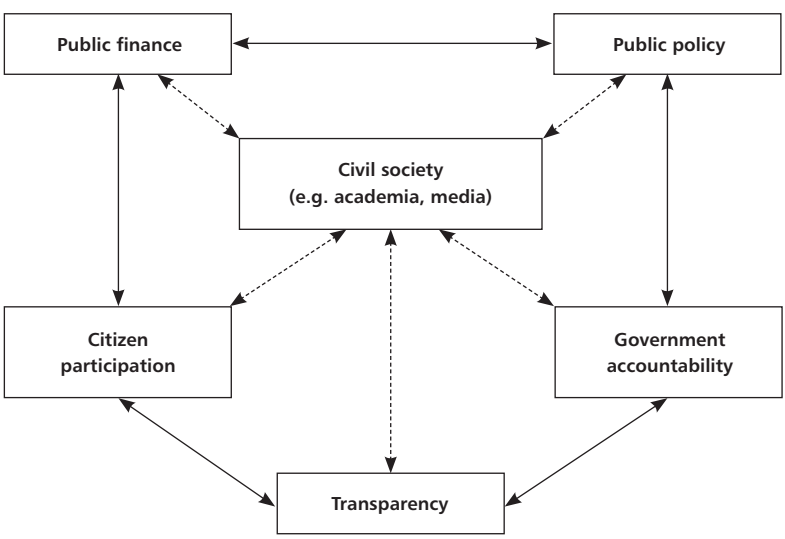
Budget watchers can concentrate their activities on national level of government, but more and more they become active at subnational levels as the majority of the issues that directly affect the life of citizens like education or welfare are under the competency of subnational authorities.

Budget watch activities in USA are particularly developed and groups are numerous both on the national and state and county levels. International Budget Project (IBP) of the Center on Budget Policy and Priorities (CBPP), Washington, D.C., is a leading group in this field. There are also very good and active budget watch groups in India (e.g., Center for Budget and Policy Studies—CBPS, Bangalore; Developing Initiatives for Social and Human Action—DISHA, Ahmedabad), South Africa (Institute for Democracy in South Africa—IDASA, Cape Town), or Mexico (Center for Research and Analysis—FUNDAR, Mexico City). However, civil society's engagement in budget watch programs in Europe is still lagging behind.

2. THE PROBLEM OF A SUBNATIONAL BUDGET WATCH

The goal of each society should be to have sound, efficient, and equitable public finances in line with the possibilities and needs of that society. To fulfill that goal a country needs to have a sound public policy. A good public policy requires government accountability at all levels. To make government accountable, the basic prerequisite is transparency. And who is able to require transparency but citizens? Citizens elect their representatives in the legislative and executive branches of the government to make decisions for them. But budgets are too important to be left only to elected representatives in governments and parliaments or to possible interplays of politicians and interest groups that they might represent. This is why citizen participation is needed. Figure 1 presents the subnational budget watch circle of actors: public finances → public policy → government accountability → transparency → citizen participation. The arrows could also point in the opposite direction, forming a full circle. In the middle of that circle we could imagine some representatives of civil society, academe, the media, or in this case our three authors trying to influence all of them.

Figure 1.
The subnational budget watch circle



In the context of the LGI's broader agenda, the authors of this volume were asked to steer their efforts to foster positive government reform. In this particular case, the term *government reform* could better be broadened to *government and social reform*. A further request was to produce analytical, policy-oriented studies, despite the fact

that the field is not rich in academic literature. Finally, the goal was to present policy options and recommendations geared towards the policymaking community in their respective countries.

In the particular context of the subnational budget watch the authors were asked to provide models of participation and monitoring for local and regional government budgeting. A further request was to create a usable subnational budget watch template by synthesizing the lessons of best practices existing in many countries at the national level. Again, one must add that while there are literature and relevant case studies about budget watch programs at the national level, they are few at the subnational level. The authors were also asked to formulate an action plan for generating momentum, highlighting issues such as access to reliable and sufficient data, the "translation" of budget lines to an understandable format, matching the rhetoric of public officials to the budget lines, and examining the role of auditing and oversight, particularly comparing the national and subnational players.

3. COMPARING CROATIA, MACEDONIA, AND UKRAINE

What do theses three countries share? First, they are all post-socialist countries coping with problems of transition from a socialist to a market economy and building a democratic society despite the strong role of the state (private sector share of GDP ranging from 60 percent in Croatia to 65 percent in Ukraine and Macedonia), a democratic deficit, weak institutions, underdeveloped civil society, and serious economic imbalances, all aggravated by the consequences of war in Croatia and serious political crises in Macedonia and Ukraine. Second, all three of them are new countries established after the collapse of bigger federations, struggling with developing new states and appropriate institutions. Third, all three countries have problems with national minorities. Macedonia has a large Albanian minority (23 percent of the population) and Ukraine has a large proportion of Russians (22 percent). Croatia has a considerable Serbian minority (around 4.5 percent of the population) and it has problems with the territories that went through tremendous changes of population during and after the war in the 1990s. These regions in Croatia are now populated by refugees from other areas of Croatia and ex-Yugoslavia territories, further complicating the issue. Minorities are important in this context because they tend to be highly regionally concentrated, and this might cause particular problems in some regions. Roma are also a significant minority facing the fewest opportunities and most discrimination in all three countries.

What are the differences among the three countries? Table 1 draws attention to the essential data. Croatia and Macedonia are dwarfed by the size and population of Ukraine. In terms of the difference in the absolute and per capita levels of GDP, Ukraine has ten times as many citizens as Croatia yet its absolute GDP is only twice the size.

While GDP per capita is at similar levels in Macedonia and Ukraine, in Croatia it is twice as large.

Table 1.
Basic facts about Croatia, Macedonia, and Ukraine

	Croatia	Macedonia	Ukraine
Population [millions]	4.4	2.0	48.4
Area [1 000 sq. km]	56.5	25.7	603.7
GDP [USD billion], 2004	34.3	5.3	65.0
GDP p.c. in 2004 at current international USD (PPP)	12,336	6,767	6,414

Source: For population and area (*Der Fischer Weltalmanach* 2006); for GDP (*Transition Report* 2005).

Third, the countries have different types of territorial organization (see Table 2). Macedonia has only one tier of subnational government—municipalities (towns, villages and communes within the capital city). Croatia has two tiers of government—counties plus municipalities (cities and communes). Ukraine has three tiers—regions, counties and municipalities (cities, urban districts, urban settlements, and rural councils). The average population of a municipality ranging from around 630 in Ukraine to 23,800 in Macedonia, with Croatia being in the middle with around 3,200. Of course, the population per municipality cannot be taken as a vital decentralization indicator (one could look into other indicators like the share of central government expenditures in total direct expenditures), but it could be indicative of the ability of citizens to participate.

Table 2.
Number of subnational units in Croatia, Macedonia, and Ukraine

Level	Croatia	Macedonia	Ukraine
Regional	None	None	27[2]
County	20 + Zagreb[3]	None	490
Municipality[4]	123 cities 429 communes	33 towns[5] 37 villages 10 communes in Skopje	456 cities 188 urban districts 886 urban settlements 28,585 rural councils
Average population of a municipality	3,198	23,800[6]	633[7]

Source: Adapted from the correspondence with Daskalovski, Maletić, and Slukhai.

Finally, irrespective of the final outcome of the processes, the three countries are in different stages regarding EU integration. While Croatia has already started negotiations with the EU, Macedonia has candidate status, and Ukraine only has a partnership and cooperation agreement and is considered as a possible partner within the European Neighborhood Policy.

The large discrepancy in the size of the countries, in terms of territory and population, the differences in their territorial organization, and to a greater degree, the differences in wealth shown by the absolute and per capita GDP, offer different possibilities for the patterns of citizen participation. The same might be concluded about the stages of the relationship with the EU.

Another key difference is that the three authors come from three very different backgrounds. All three of them engaged in this program because they are genuinely interested in promoting budgetary transparency, accountability of government, and citizen participation. But Ivana Maletić is an economist employed by the government, actually a deputy minister of finance of the Republic of Croatia, thus representing government itself. Sergii Slukhai, also an economist, is a university professor, representing the academic community. Zhidas Daskalovski is a political scientist, belonging to an NGO, representing civil society. All these differences are reflected in their topics: Ivana Maletić deals with the supervisory and monitoring role of the central government and the public in general over the local government units in Croatia; Sergii Slukhai researches budgetary oversight and accountability in secondary education in Ukraine; and Zhidas Daskalovski analyzes the role of the public in subnational budget monitoring in Macedonia.

4. COMMON PROBLEMS AND POSSIBLE SOLUTIONS

4.1 Common Problems

Despite the various approaches of the authors and the stages of decentralization and democratization of their countries, one can discern some common problems that are more or less emphasized in all three cases. They may be broadly grouped under the topics of an inappropriate or defective legislative and institutional framework, the dominant role of government bodies, and the subordinate role of the public.

4.1.1 Inappropriate or Defective Legislative and Institutional Framework

Although *Ukrainian* legislation regulates citizen participation in budget oversight in various documents from the constitution to particular laws, the procedures for obtaining information about issues of public concern are imprecise. Consequently, it is questionable whether citizens can exercise their right to influence public bodies, especially regarding budgetary issues at the local level. Ukrainian legislation also does not provide a clear framework concerning the effective use of public money, independence of local governments and budget users from the central government, and the accountability of local governments and budget users to the public.

Within the *Macedonian* legal framework there is no mention of any possibilities for citizens to be involved in the budgetary process. However, the legislature does not preclude citizen participation in general. On the contrary, from the constitution to various laws, participation of citizens in decisions about common matters is encouraged. One can conclude that although legal provisions do not directly provide for the possibility for budget participation at the local level (and the national level as well), the legal background for it has been ensured indirectly.

Among three countries *Croatia* seems to have the best legal basis for citizen participation. However, various institutional weaknesses and psychological and cultural obstacles result in: a poor supervisory and control environment for effective central government, inadequate citizen participation, and slow improvements of government accountability.

An inappropriate or deficient legislative and institutional framework is the most repeated topic in all three papers. The situation varies from country to country. Croatia has the legal preconditions but lacks the necessary democratic knowledge and tradition, in addition to psychological and cultural obstacles. Legislation exists in Ukraine too, but procedures are wanting and the result is questionable. The worst situation is in Macedonia where only an indirect legal background for citizen participation has been provided.

4.1.2 Dominant Role of Government Bodies

The government is dominant in all three countries and may be summarized as: centralism, under which all issues of public importance are supposed to be resolved at the national level; the strong role of the state, whether at national or local levels, in all aspects of life from politics to the economy and social issues; and weak, usually coalition governments that have to cope with more pressing issues of daily survival and are often unable to fasten on the processes of decentralization and the dismantling the dominant role of government bodies.

In *Ukraine* the central government bears most of the responsibility for the delivery of public services, including secondary education. Weak popular demand for independent local authorities and the long-lasting tradition of a centralized state lead to the lack of any strong desire to shift more power from the top to the bottom. Even in the rare cases of decentralization, the local authorities do not become truly accountable and fiscally independent. As a consequence transparency that has been greatly improved at the national level seems much more problematic at the local level. All these facts contribute to the weakness of the role of the citizens and government dominance, more at the national, but indirectly at the local level, too.

Local governments in *Macedonia* are hardly prepared to step beyond the former regime's behavior and accept the principles of accountability and transparency. The roles and the responsibilities in the management of public finances are not clear and in these circumstances it is difficult to hold the government accountable for budget policy and decisions. There are no specific provisions encoded in law that state clearly that documents covering the budget should be accessible to interested citizens. A lack of willingness and legal pressures for a change enable government bodies to run the show.

In *Croatia* the consequences of war, occupation of a third of the country, and huge population movements have all been constraints on feeble efforts for decentralization. Excessive number of territorial units and, consequently, the inefficient, oversized administration at several levels of government, plus areas of special national concern, contribute to the slow diminishing of the dominant role of government bodies. Numerous hurried decisions necessary for eventual EU accession have further enhanced the dominance of government bodies, at both the local and the national level. Consequently, despite the nominal decentralization, a kind of centralization is actually in place, contributing to further "governmentalization" of the country.

4.1.3 Minor Role of the Public

With the dominating role of government bodies, the minor role of the public logically follows. In all three countries, and unfortunately not only in them, information and data are missing, the majority of people are alienated from the government budget and its process, and there is a strong need to demystify the budget and bring it closer to the population.

In *Ukraine*, a country with a population of almost fifty million, some vital national budget statistics are published once a year, in one hundred copies, and distributed only to high-level national authorities, but not to local authorities or citizens. No wonder the general public has little involvement in or influence on budgetary issues like the level of school funding, the topic of our study here. The problem lies in the factual formation of local budgets that gives no space to public involvement. Local budgets are formed from

top down, a virtual replica of the Soviet-type budgeting process when the Communist Party made all the decisions instead of citizens. Even today there is no reason for local officials to discuss budgets with the public because they are predetermined by the state. It is not that the public is ready or over-demanding either.

At the moment there are no institutional arrangements for citizen participation in *Macedonia*. Citizens hardly participate in the budgetary process on the subnational level and this issue is not on the agenda of citizens' groups and nongovernmental organizations. Citizens are passive and the political culture negatively influences the direct involvement of concerned citizens in the budgetary processes. Even when citizens show some initiative, responses from the local governments are not encouraging.[8] In sum, budgetary monitoring at the subnational level is very difficult to undertake in practice.

Croatia faces the problem of willingness more than a lack of possibilities. Its citizens are not organized well and they are still passive.[9] By contrast, the local media—radio, television, newspapers—are very powerful and influential. Media have been instrumental in initiating communication between the public and local governments, trying to talk openly about the problems and change the mentality of secrecy. There are also more and more local governments, particularly developed and wealthier ones, promoting the publication and distribution of citizens' budget guides and organizing public hearings and open discussions. However, this is not an obligation. Legal weaknesses do still exist, like there being no requirements for the public presentation of simplified financial reports intelligible to a wider public. This leads to a poor capacity to deal with information presented in a complicated way. The existing Association of the Towns and Municipalities is also very passive and has only narrow functions. Despite the efforts of some local governments and local media, there is still a lack of awareness of the need for participation and of changes that can be encouraged.

Briefly, in Ukraine the top-down, predetermined process of budgeting does not give space to public involvement; in Macedonia citizens hardly participate and public engagement is not on the agenda of even citizens' groups; and in Croatia citizens are poorly organized and passive, so that, despite the efforts of some local governments and local media, the awareness of the need for participation is still rather undeveloped.

Box 2.
Opening budgets to public understanding and debate

For the purpose of this text it would be interesting to have results from *Opening Budgets to Public Understanding and Debate, Results from 36 Countries* (IBP 2004). Of the three countries only Croatia participated, and unfortunately it did not fare well. As some of the issues mentioned below have been improved lately, one might expect a better evaluation in the results to be published in 2006. Keeping in mind how the other two countries—Macedonia and Ukraine—were ranked substantially worse in other indicators like press freedom, corruption, and competitiveness, one cannot have high hopes for their eventual rankings if they participated in this comparison of budget transparency.[10]

In the IBP survey, "Croatia's scores are uneven, indicating mostly positive practices in the area of 'monitoring and evaluation reports,' but negative or mostly negative practices in the other two major categories: 'executive budget documents' and 'encouraging public and legislative involvement.'"

In the "executive budget documents" category, Croatia scored only 28 percent, well below the cross-country average. The budget provides information on the budget year and the prior year, but no historical data or projections beyond the budget year. Its score of 12 percent in the "comprehensiveness" subcategory indicates that the budget presents little or no information in areas such as the macroeconomic forecast upon which the budget is based, quasi-fiscal activities, and tax expenditures.

In the area of "monitoring and evaluation reports," the country's score of 51 percent indicates slightly positive practices. The executive releases reports on a monthly basis, but does not issue a mid-year review of the budget. Year-end reports by the executive, although released in a timely manner, lack the details needed to facilitate comparisons between enacted levels and actual outcomes.

In the "encouraging public and legislative involvement" category, Croatia fares poorly. It provides *no* information highlighting policy and performance goals—that is, it provides no information about who benefits from various programs and how those programs are performing—making it difficult to assess how budgetary figures connect to desired outcomes. In the other two subcategories—"involvement of the legislature" and "facilitating public discourse and understanding"—Croatia does moderately well, with scores of 54 percent. Although Croatia issues a pre-budget statement, it does not make available a non-technical "citizens' budget" or other supplementary materials that could be used to expand public understanding of the budget.

4.2 Common Solutions

Basic recommendations in this study evolve around improving the participation of citizens, the autonomy and responsibility of local governments, and the oversight or monitoring capacities of central governments.

4.2.1 Promoting Participation of Citizens

As customers of public services, and at the same time providers of public money, citizens should be interested in participating in budgetary processes and decision-making. Thanks to the legacy of non-democratic regimes, paternalistic and highly centralized states, citizens might not be yet aware of their rights and possibilities. Unfortunately, they are often also unaware of their obligations. However, one could expect that step-by-step these ideas might become more pronounced. Works like this one are expected to move citizens closer to that goal. Promoting participation of citizens is not an easy task. There is no established academic literature, accessing data is difficult, and promoters sometimes even face open hostility. So what can be done?

In *Macedonia* a number of policy measures to strengthen the role of the civil sector in the budgetary oversight of the local governments could be recommended. First, it is necessary to have clear provisions in relevant laws guaranteeing citizens permanent access to local financial information. Second, local governments should be obliged: (i) to disseminate budget information, (ii) to organize regular quarterly open sessions and special public hearings before adopting key decisions, (iii) to publish income and expense statements and balance sheets, (iv) to have a proactive approach to transparency with information made available in reports and on websites, (v) to allocate sufficient human resources to processing information requests, and (vi) to become trained to deal courteously with the public. All that should be stated in relevant laws. For the beginning, a lot will be expected from the access to information law (passed in 2005) that might benefit citizens. It is expected to make budget monitoring of local governments much easier and to directly empower ordinary citizens in their dealings with institutions that now seem distant and all too powerful.

Whether citizens, NGOs, or media, all monitors in *Croatia* should communicate, be involved, ask questions, and actively participate; give concrete suggestions to their local governments; expand their working knowledge and ability to understand and compare local budgets; and not "vote with their feet" without trying to act and make changes. Monitorrs should be involved in all stages of budgetary process. In the preparation stage they should participate in decisions about programs. That would enable them to better understand local governments' work and intentions and might ensure better satisfaction with the provision of local services. In the execution stage they should monitor and

ask for results. This might help to prevent inefficient usages of public funds, frauds, and irregularities, and provide budget execution reports for the public. In the financial reporting stage, they should comment, ask for simplicity, and compare with other local units, so as to better understand the situation in the particular local community but also in the country as a whole and gather ideas about new possibilities.

Keeping in mind the low level of influence of the general public in *Ukraine* on the level of public expenditures, the goal of the policy proposed is to increase the public participation in the budget in order to gain more efficiency in providing public services. The problem cannot be solved just by an additional legal act (on public governance, for example), but with a complex policy mix directed mainly at the institutional strengthening of public governance. The core mechanism for securing a higher level of public inclusion could be the decentralization of educational administration, accompanied by a higher level of school self-government and responsibility of unit managers. That might mean a new schooling paradigm, devolution of functions from central to local governments, more autonomy of budget users, different money allocation, and promoting competition among budget users.

4.2.2 Promoting Autonomy and Responsibility of Local Governments

It might be concluded that greater autonomy and responsibility of local governments, usually connected with higher levels of decentralization, might improve the prerequisites for a better subnational budget watch program.

Achieving clarity of roles and responsibilities in the management of public finances in *Macedonia* is essential to the citizens' capacity to hold the government accountable for budget policy and decisions. One can only hope that after the newest reforms in 2005 subnational budgets will be drafted with more concern for accountability. The country should not be over-centralized and local governments should not be left to deal with important municipal issues without recourse to sufficient funding. The practice of many municipalities of running into debt and even finding extralegal means to manage and fund their work should be stopped. As a result, budget transparency should be an issue of concern to local governments, and central authorities should not tolerate the state of affairs by reasoning that citizens need their basic local needs filled.

As the central government in *Ukraine* bears most of the responsibility for the delivery of public services including secondary education, public policy options should be developed for enhancing local budget accountability in the education branch. Legislation should be revised to increase the independence of budgetary users, in this case educational establishments, and also to strengthen the accountability of educational establishments and authorities to the public. It could be obtained with the implementation of self-regulating mechanisms at the school level combined with a normative formula-based

approach in the allocation of public moneys. Simultaneously, the elements of competition among schools should be launched. This could raise not only school cost efficiency, but also the quality of education.

The formal 2001 decentralization of government functions in education, health, and welfare in *Croatia* was not followed with the appropriate decentralization of financing. The central government still has to decide whether it wants decentralization of both authorities and financing, or decentralization of authorities and centralization of financing. Government should also invest in solving the problems of equalization grants, fiscal capacity indicators, and shared taxation formulae. The preoccupation with the number of local governments is clearly a politically delicate and tough issue to resolve. Clear definition of powers and responsibilities at all levels of government and establishment of stable financing mechanisms based on objective criteria could affect greatly the autonomy and responsibility of local governments, making them more interested in being accountable to citizens.

4.2.3 Promoting Oversight or Monitoring Capacities of Central Governments

Decentralization means greater autonomy and responsibilities of local governments, but at the same time it requires a strong oversight or monitoring capacities of central government. Central government should enable equalized development of local communities and guarantee the appropriate level of public services to all citizens, without financial difficulties.

As local governments are assumed to perform state functions at the local level, central government in *Ukraine* is mostly interested in controlling local spending decisions. Unfortunately, state budgetary oversight is biased towards control of the legality of money usage rather than its efficiency. For any change in this practice, a redefinition of the role of the relevant ministries, in this case of education, is necessary. The relevant ministry should be responsible not only for the content of education but also for the budgets of the school entities. The ministry should establish departments capable of dealing with financial analysis and monitoring. Central government should solve the unclear processes of the formation and usage of the budgets of educational establishments and the inefficient usage of public resources. It should also enhance the usage of alternative sources of financing, competition among budget users, and free some taxpayers' money by replacing it with private sources. The goal of these changes is to obtain effective mechanisms capable of guaranteeing the best possible usage of educational budgets at both the macro and the micro level. It could also increase public interest in the issue, and consequently public participation in budgetary decisions.

There is no effective mechanism for controlling local financial management in *Macedonia* and this is why major legal and institutional changes are necessary. If the aim is successful fiscal decentralization, close monitoring of local budgets (as well as the national budget) is necessary. It should prevent the current practices by local governments of accumulating debts, owing suppliers of goods and services, and undertaking illegal financial management practices that currently cannot be easily identified, even by the state audit authorities. Getting rid of the illegal practices and non-payment culture of the government could promote a taxpayer culture and consequently positive *quid pro quo* feelings among citizens.

The absence of active central government involvement in local government activities in *Croatia* is one of obstacles in the way of their further development. It might sound contradictory to the previous claims about strong centralization in Croatia, but it could also be indicative of the real state of the affairs. Besides enhancing the autonomy and responsibilities of local governments, central government should improve external monitoring mechanisms and establish procedures for monitoring local governments. Thus they can come to understand that, as well as the state audit authorities, the central government can also monitor, control, and audit their activities.[11] On the local government side the emphasis should be on financial management, fiscal discipline, and efficient usage of resources. On the central government side it is necessary to build analytical and monitoring capacities. It will of course be difficult, considering the constant problems of attracting staff to public administration. But that is another topic.

5. SITUATION, EXPECTATIONS, AND WHAT COULD BE DONE

Like the majority of other countries in the post-communist transition, the countries in our sample—Croatia, Macedonia, and Ukraine—face huge democratic deficits. They are also confronted with large government expenditures and inadequate levels of public services, all accompanied by inactive populations. The options are smaller governments, meaning a decrease in services; larger governments, with an increase in taxes; or better governments, i.e., an increase in effectiveness. Witnessing the slow processes of restructuring of the economies and the health systems, plus the aging of population, one could expect that large governments are here to stay, meaning that citizens as taxpayers should try to promote other options.

One could also expect that governments will most likely become more influential at the local and regional levels and that citizens will become more aware of the issues and engaged to participate at local levels, and, logically, ultimately begin to actively engage in a subnational budget watch program.

In Table 3 participation, information, and accountability are compared in the three countries. Judging from the answers to the set of questions, the situation seems to be

the worst in Macedonia and much better in Ukraine and Croatia. Answers to almost all questions for Macedonia are negative, while the majority of answers for Croatia and Ukraine are positive, even though they usually are accompanied by some disclaimer like "but," "still," or "yet." Of course, this evaluation is rather subjective and cannot be used for any kind of ranking of the three countries. The most discouraging conclusion could be that citizens of all three countries participate: "hardly," "poorly," or "on a very small scale," irrespective of the possibilities for participation; the availability, reliability, and timeliness of data; and the accountability of governments.

It is obvious that we need action to de-alienate citizens and to demystify the budget and bring it closer to the population, and that the action should be based on research and advocacy. That is exactly where our case studies fit in. They are expected to raise the awareness of the importance of the transparency of the budget, the accountability of governments, and the participation of citizens, particularly at lower levels of government. The chapters propose the introduction of new models and action plans for participation and monitoring.

For Croatia, Maletić proposes concrete institutional framework in the form of a newly established monitoring committee with representatives of relevant ministries, budget users, and citizens (NGOs, local governments associations, media, etc.). She also clearly defines working plans for the committee. A functional committee could change the role and the position of citizens in the subnational budget watch program, enabling them a formal position within the process.

Slukhai proposes a practice from New Zealand for Ukraine. In that model, schools enjoy a high grade of fiscal independence and are required to perform in a fiscally sound way. The relevant ministry should be deeply involved in fiscal issues and should not relinquish their management solely to the Ministry of Finance. The model might be a good example to prove that decentralization and school autonomy are capable of providing not only very good results in the delivery of education, but also of enhancing the incentives of citizens for participation in local budgetary issues.

Bearing in mind the poor possibilities for participation and lack of information and accountability in Macedonia, Daskalovski opted for the translation of budget lines to an understandable format and for the generation of momentum in the form of a published citizens' budget guide. The intention is to use the experiences of similar publications for other countries and to consult experts in the field. A good citizens' budget guide could enable ordinary citizens, as well as politicians and the media, to better understand the basics of the budget and the budgetary processes.

Table 3.
Participation, information, and accountability in Croatia, Macedonia, and Ukraine

	Croatia	Macedonia	Ukraine
Participation			
Are citizens participating?	Poorly.	Hardly.	On a very small scale.
Does the legislation enable them to participate?	Yes.	Not directly, but some indirect encouragements exist.	Formally yes, but without clearly defined mechanisms.
Are there institutional arrangements for participation?	No, but numerous examples of arrangements in practice.	No.	Public hearings.
Information			
Are data available?	Yes, but not in citizen-friendly formats.	Only on *adhoc* basis.	On a very limited scale, without detailed information available to citizens.
Are data reliable?	Yes, quite.	No.	Mostly yes, but shadow activities of budgetary users still exist.
Are data timely?	Yes.	No.	Yes.
Could one compare actual vs. planned figures?	Yes.	No.	Yes.
Accountability			
Is it clear who is accountable for what?	In general, yes, but with some limitations.	Provided by 2004 Law on Budget.	In general, yes, but with severe problems.
Do the executives take in mind external auditors reports?	Yes.	No. Central authorities even tolerated local governments running debts until 2004.	Yes.
Does the executive bear in mind requests from legislative?	Yes, still with quite large autonomy.	Not, unless these suit the interests of central government.	Yes, still with quite large autonomy.

Source: Adapted from correspondence with Daskalovski, Maletić, and Slukhai.

6. CONCLUSIONS

For citizens budgets are too important to be relinquished to the sole stewardship of legislative and executive branches of government. Citizens should try to participate in budgetary processes from the very beginning, when governments start preparing the budgets, to the final stages when governments and auditors report on their execution. This chapter tried to explain why citizens should engage their subnational budgets, how to do so, and what questions to ask. The subnational level was emphasized because it usually provides basic education, health, or welfare services that citizens are particularly interested in. Consequently, one might expect citizens to become most easily attracted to engagement at the local level. We hope that this chapter will fill a gap in the existing literature and give some directions for possible actions of all interested parties—the legislative and executive branches of government, public servants, academia, the media, NGOs, and citizens.

Here, we should emphasize the limitations of our conclusions, based as they are on the comparison of only three countries. Although they have a lot of issues in common, these countries are different by size, wealth, territorial organization, and their current relationship with the EU. The authors of the case studies also have different backgrounds and approaches. The topic is rather new, comprehensive, experiences from other countries are rare, and we cannot claim that the approach taken was the best one. Further work would analyze a bigger sample of countries, e.g., a group of ex-Soviet or ex-Yugoslavia countries or new EU members and candidate countries. One could also concentrate on particular segments, e.g., the role of local assemblies in local budgetary decision-making or the effects of the harmonization with the EU on the possibilities for citizens' participation.

It would also be good to engage as many countries as possible in *Opening Budgets to Public Understanding and Debate*, i.e., the budget transparency index by the International Budget Project, which is expected to impact participation and accountability. Of course that impact could be looked upon in the opposite way as well, i.e., how participation and accountability could affect transparency. Besides a worldwide budget transparency index, one could easily imagine a worldwide budget participation index. Such an index might make feasible a comparison of citizen participation and enable them to have a greater influence on governments' decisions concerning revenue collection and public services provision. Of course, decisions should be in line with the possibilities and needs of these same citizens, their local communities and their countries.

ENDNOTES

[1] I would like to thank the authors of the country studies—Ivana Maletić, Sergii Slukhai, and Zhidas Daskalovski–for their contributions, OSI/LGI for giving me the opportunity to mentor the project, and Scott Abrams for both constructive and friendly cooperation since the beginning. The editor would also like to thank Ken Davey for his help with the title.

[2] Regional level includes 24 *oblasts*, Autonomous Republic of Crimea, Kyiv City and Sevastopol.

[3] As the capital Zagreb has status both of a city and a county.

[4] Basic level of local authority.

[5] Towns have more than 3,000 citizens.

[6] The biggest one is Kumanovo with 105,484 citizens and the smallest one is Vraneshtica with 1,322.

[7] In the calculation, the urban districts are excluded in order to avoid double counting.

[8] A mayor of one municipality in Macedonia was so irritated by the request of the researcher to get a copy of the municipal budget that he asked him, "Would you please leave the room?"

[9] The pilot project of our fellow could be taken as the best indicator of the role of the citizens in Croatia. She dropped the idea of surveying citizens about budget processes and their openness to the public after realizing that a group of colleagues from the pilot who are all experts in the field were as completely uninformed as citizens. None of them ever saw the budget of the local unit in which he/she is living or participated in any of the budget processes in his/her local unit.

[10] If we look at global press freedom ranking, Croatia is 82nd, Macedonia 107th, and Ukraine 123rd. All three countries are considered *partly free*. For comparison, Estonia and Latvia are considered *free* and ranked 24th, the same as the United States (Freedom House 2005). Comparing corruption perception indices, Croatia is 70th in a group with countries like Burkina Faso and Lesotho; Macedonia is 103rd with Gambia, Swaziland, and Yemen; Ukraine 107th with Eritrea, Zambia, and Zimbabwe. Some of countries in transition are much better ranked, i.e., Estonia 27th and Slovenia 31st. (Transparency International 2005). Comparing competitiveness indices, Croatia is 62nd, Ukraine 84th, and Macedonia 85th. Some of the best-placed among transition countries are Estonia 20th or Slovenia 32nd (World Economic Forum 2005).

[11] None of the respondents in Croatian survey, when asked who monitors the activities of local unit, mentioned central government, the Ministry of Finance, or some other ministry. Over 40 percent of respondents circled the State Audit Office then followed internal control, local assembly, local budget and finance committee, etc.

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Subnational Budget Watch in Croatia: Is Anybody There?

Ivana Maletić

EXECUTIVE SUMMARY

This paper is about the supervisory and monitoring role of the central government and general public over local government units in Croatia. The analysis presents the legal background and present situation regarding budget processes, their openness, and transparency. Since most studies in Croatia were done for the central government so far, we conducted a survey to analyze the openness of budget processes and mechanisms of monitoring and control at the level of local government units. The main finding shows that the lack of institutional and legal framework for a supervisory and control environment causes the absence of active central government and public involvement in the local government units' activities and, in addition, creates an obstacle for their further development. The author argues that the supervision and monitoring functions are imperative if the government wants to improve the decision-making process and to increase public confidence in government as well as to increase public participation in budget processes to achieve better transparency. Since it is not easy to develop supervisory and monitoring functions and to build the related structures, a number of recommendations, including a working plan and roadmap, are offered.

1. INTRODUCTION

This paper examines the level of development of budget monitoring in Croatian local government units. In addressing this topic, it asks: Are the budget processes at the local government units' level open enough? Is information available in order to ensure citizens' monitoring and participation? Are there institutionally and legally defined elements of the supervisory and monitoring functions? Are there control mechanisms? What control mechanisms have been established in order to ensure efficient and effective use of public financial resources?

The main results of this paper show that a comprehensive budget watch program needs to be supported by legal instruments for communication (open and transparent budget processes), monitoring, and control. It is also important to develop and establish a system of financial management and control; to set up the necessary institutions and functions; to define business procedures for all activities and processes, along with detailed job descriptions and separations of duties as well as division of responsibilities for the staff involved.

The process of decentralization in Croatia has occurred at a very slow pace. One of the most significant reasons for this was, and still is, the lack of a good monitoring system at the central government level. Additionally, communication with citizens is very weak and there is no serious information process that can explain to citizens the role of the budget and the possibility of their influence.

To support this study, a survey was conducted to analyze the openness of the current budget processes and mechanisms of monitoring and control at the level of local government units. The results are presented in this paper. Among the main findings we can stress that budget processes are not public enough and there is no well developed and established relationship between the public and local units. Second, a monitoring and control system over local units is very poor. The public practically does not participate in the monitoring of budget processes. The monitoring role of the central government over the local units is not systematically organized and weak. Factors to consider are legal weaknesses and a lack of institutions, matched with a lack of capacity and willingness to change the situation.

The paper ends by proposing a division of roles and responsibilities for central and local government as well as for public. Among the number of recommendations would be the introduction of long-term planning and program budgeting with set goals and objectives. These are the necessary prerequisites for monitoring and evaluating the successfulness of budget execution.

2. BUDGET WATCH PROGRAM IN LOCAL GOVERNMENT UNITS IN CROATIA—SOMETHING IS LACKING

The Constitution of Croatia and the Local Government Act prescribe that local government units have revenues for financing expenditures derived from carrying out tasks from their scope of work. Local units generate income from their own sources (property and local taxes), from shared revenues (shared between the government, municipalities, cities, and counties), and from grants (mainly from the central government).

The fiscal decentralization process started in 2001. During this process the central government transferred part of its authority and responsibility in financing schools, healthcare, and social welfare to local units. In the first phase of decentralization local

units (counties and large cities—total of 53) primarily assumed competence only for financing material expenses and expenses for the acquisition of non-financial assets. Parallel with the expenditure, central government transferred the revenues (funds for financing) by increasing the local governments' share in income tax and ensured grants from the so-called equalization fund for local units. But progress in the decentralization process has not taken place during the period of the last four years (everything has remained at the first phase); one of the main reasons is the lack of a good monitoring system at the central government level. Although central and local government have the same aim (to provide citizens with necessary services), if the central government does not have good information on how the money transferred from the central to local level is spent, then it will not take steps to give local government more responsibilities and independence. With a good monitoring system, both sides are informed, which leads to mutual understanding and, in the end, to further progress. The basic precondition for the monitoring system is to have *timely, reliable and accurate information.* Financial information (on a quarterly basis) of all local units and their budget users are available in the database in the Ministry of Finance. The whole database is not publicly available, but only some parts, such as municipalities, towns, and counties' reports on revenue and expenditures, are published on the Ministry's website.[1]

The central government seeks to ensure macroeconomic stability, which is why it is important that local units practice discipline with regard to the set fiscal and monetary policy. As a means of achieving this objective, the central government has passed legislation aimed at controlling the borrowing of local units. Since the central government also allocates part of its resources to financing functions at the local level, it naturally wants to ensure that the functions are carried out properly and that the allocated resources are used for intended purposes. Still, its monitoring and control role is a very passive:

- budgets and financial reports are collected without feedback on correctness and quality of the data,
- limits for borrowing are given but control is performed only when local unit submits the request for approval to borrow,
- financing of the decentralized functions is monitored through the reports without on-the-spot checks and controls,
- line-ministries responsible for the decentralized functions must use financial reports (in addition, they receive quarterly local units' reports about uses of decentralized funds) as a basis for deciding about the criteria and measures to insure the minimum financial standard for every decentralized function, and define the way the equalization grants for decentralized functions are to be calculated. However, there is no review of the actual needs in comparison with minimum financial standards; of the actual output, including a local unit's co-financing, as compared to the financial plan; of the progress of a local unit's ability to manage decentralized functions.

One of the problems at the central government level is definitely *insufficient capacity for building the monitoring system.* Monitoring is a management responsibility that involves collection, analysis, communication, and the use of information about the programs' progress. It ensures the effectiveness and quality of the programs and periodically reviews their progress towards the achievements of objectives.

Communication with citizens is insufficient. Rare are the examples of local units that supply their citizens with brochures which explain, in a simple way, what has been done within a year and how, and what is planned to be done. There is no example of asking citizens about possible changes or new programs. Local units should have in mind that the citizens are users of public services and they pay for them (either directly or indirectly through the collection of fees and taxes), but they don't. Prices and qualities of the services have to correspond to the citizens' needs and requirements as taxpayers and users of those services. The local units have to contact the citizens, involve them in all of the budget processes and try to satisfy their specific local needs. However, it is society's job to ensure that every individual can actively participate in the government's activities, putting forth questions and expressing satisfaction or dissatisfaction with the level of local services.

The extent of activity of all interested parties (scientists, NGOs, media, or citizens) is best described through the fact that, from the year 2001, financial statements of local units (summarized data for counties, towns, and municipalities) have not been published until September 2005 and nobody asked why.

The participation of the *public* not only depends on its own effort and interest in active involvement in monitoring local units' performance but also on the openness of processes, and willingness of local units to integrate the public into budgetary processes.

Information is publicly available because of legal obligations. But some local units started to understand that communication with the public can help them in performing their job better. Without communication it is not possible to have a good monitoring system in practice. Communication among all interested parties is a starting point, and they have a shared aim—the progress and development of the local units in a sustainable, effective, and efficient way. Since the interested parties have different approaches on how to reach this aim, they presume that they cannot trust each other. A system of monitoring and control would alleviate this problem.

3. SURVEY ABOUT THE OPENNESS OF THE BUDGET PROCESS

The discussion that follows considers the budget process and its openness to the public with regard to how it is implemented in local units. The openness of the budget process was probed via the survey questionnaire that accompanied this project (see Annex 6.5).[2]

The questionnaire was intended for the heads of the financial divisions in the local units and it consisted of two parts: the openness of the budget process and the mechanisms of monitoring and control that insure legal adoption and execution of the budget. The aim was to check the openness of the budget processes by testing information that is publicly available and by asking about communication methods local units employ with their citizens, and to check the mechanisms of monitoring and control over the local units themselves.

The survey covered all local government units in Croatia. The questionnaire was sent to all of them: 426 municipalities, 123 towns, the city of Zagreb, and 20 counties.

Forty-four percent of the total number filled it in and sent it back. The final number of local units that responded was: 141 municipalities (40 percent of total), 61 towns (51 percent of total), and 14 counties (70 percent of total), for a total of 216 results. The number of local units was deemed satisfactory for the analysis.

The author's phone number was given with the questionnaire in case of need for additional explanation. Only five local units called, mainly to express their satisfaction with the questions and their hope that the result will be concrete incentives from the central government level for developing a system with a clear explanation of what is public, who can get what kind of information, and when.

In most cases the heads of the local unit financial departments filled in the questionnaire. Many of them circled one or more answers and they also gave a broader context with detailed explanations. Though this made for a time-consuming analysis, the results are valuable.

3.1 Budget Preparation

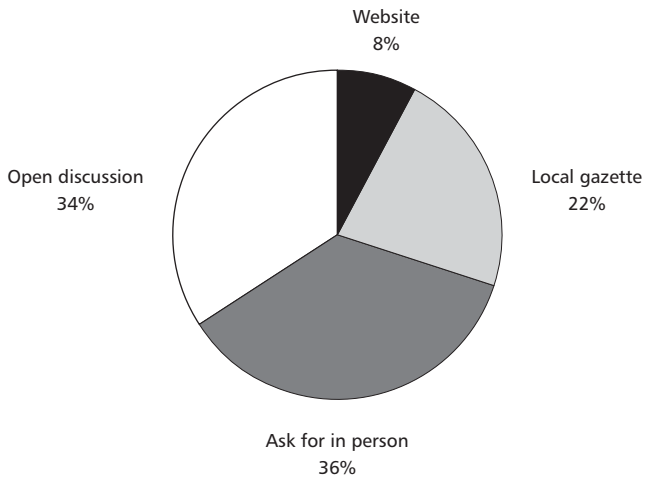
The Ministry of Finance, or for that matter any other ministry and central government institution, is not involved in the process of budget preparation at the local units' level. Central government indirectly—through the legal framework—defines the broader context of the budget through the prescribed budget methodology: program budgeting, multi-year budget, and level of detail of information.

The first two questions evaluate to what extent the public (citizens, nonprofit organizations, media, scientists, and other stakeholders) participate in the budget negotiation process.

A budget draft is publicly available in 71 percent of local units but in a very passive way because local units do not really try to involve the public in the negotiation process.

Figure 1 shows the possibilities of public insight into the budgetary draft.

Figure 1.
Public insight into the budget draft



In 29 percent of local units the budget draft is not publicly available and the distribution of given explanation is shown in Figure 2.

Some of the verbal explanations why budget draft is not publicly available are the following:

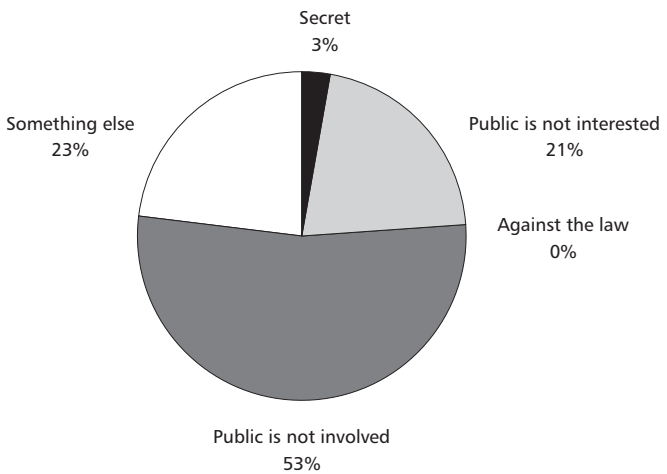
- we have discussions with social partners, towns, and municipalities but not with the public;
- the management attitude is that the public is too demanding and because of that it is better to avoid it and to prepare the budget alone;
- it is not practical and there is no time to do it;
- there is no sense to publish the budget draft. We, for example, send to all companies and other business entities in the municipality's tender for project proposals but the interest and response is very low.

According to the Budget Act, Article 32 the adopted budget must be published in the local gazette. Because of this legal obligation it was expected that nobody would answer NO to the second question (Budget adopted by the assembly is published: Yes/No) but still 11 percent (two towns and 10 municipalities) answered that the adopted budget is not published mainly because: the public is not interested in the budget (the budget is too complicated and it is not understandable) and there is no possibility to influence (to change) the budget after its adoption.

One of the explanations why the budget draft is not publicly available was that the public is too demanding and that it is better to avoid it. On the other hand, to the

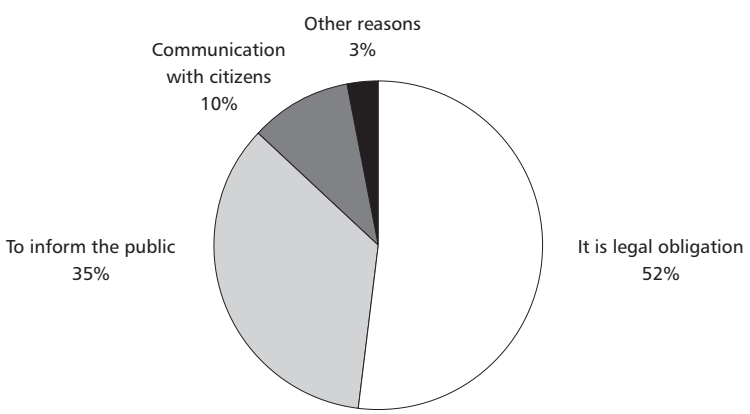
second question answers suggested that the public is not interested. With this attitude from side of the local units, the public is in a difficult situation, because in any case, interested or not, they will not get the information. This clearly shows that local units must not consider who will use the data and how, but must focus on how to present their activities and how to communicate with the public.

Figure 2.
Reasons why the public does not have an insight into the budget draft



As shown in Figure 3, 89 percent of those local governments who publish the adopted budget explain the reasons for publishing.

Figure 3.
Reasons for publishing the adopted budget



Based on the answers to the first two questions, it is possible to conclude that some local units are trying to find the mechanisms for communication with the public in order to involve it more in the budget negotiation process. Still, there are no procedures based on which local units regularly and systematically communicate with the public; communication is more *ad hoc* and depends on the willingness of the both sides. There is a certain number of local units that think that the budget preparation and adoption is an internal process and that it is too technical an issue for public involvement.

3.2 Budget Execution

Local units can disperse money to a budget user monthly, weekly, or daily, depending on the available level of the financial-information system and the relationship with the budget user.

The majority of local units transfer the money to the budget users' bank account and have to wait for the information from the budget users about what expenses the money has been used for. Local units record only the expenses that are paid but not the accrued ones. Another weakness is that data are unreliable and depend on the budget users' feedback.

The most ideal system would be the highly automated one through which the general ledgers of each budget user are connected directly with local unit's general ledger; here, budget users put accounting information (assets and liabilities, revenues and expenses) directly into the local unit's ledger accounts.

The Budget Act stipulates the obligation of providing semi-annual and annual reports on budget execution at the local level. Completed reports are submitted and published in the official gazettes of local units. If they are not written or made suitable for a wider circle of beneficiaries, they are self-serving and intended only to satisfy legal requirements.

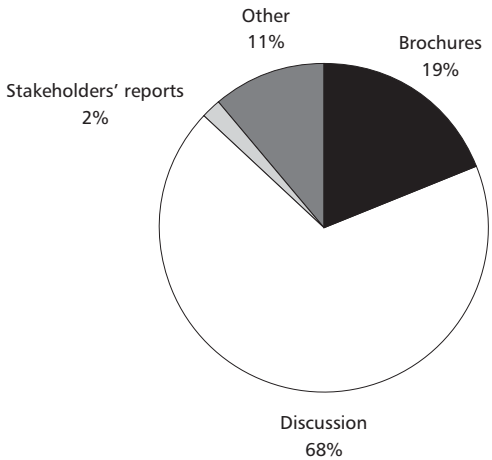
Discussion about the annual and semi-annual report on budget execution is public in 79 percent of the local units. The way the discussion about budget execution is publicly organized is shown in Figure 4.

Public satisfaction with the local units' programs and services is regularly checked in 70 percent of local units, mainly through the media: special local radio' programs and supplements in the local newspapers. Some of the local units use public web pages with the questionnaires, "coffee" with the mayor, a postal box or telephone hotline for complaints and suggestions, and meetings with local boards.

The local units that do not check the public attitude and satisfaction with their programs and services offer excuses as to why this is the case: there is no special person or department entitled to do that job, communication is *ad hoc*, there is no systematic approach, there are time limits and lack of willingness, local units analyze the feedback

and like to get the appraisals but they do not react to them, the public does not want to communicate, or it is still not aware that it can participate, influence, and change the public environment.

Figure 4.
Organization of the public discussion



3.3 Information System

An information system has to give answers to the three basic questions about government spending: what the money was spent on, how it was spent, and who spent it. It means that the data in the budget system are classified economically, functionally, and organizationally, which is one of the basic requirements for achieving fiscal transparency (IMF 2001).

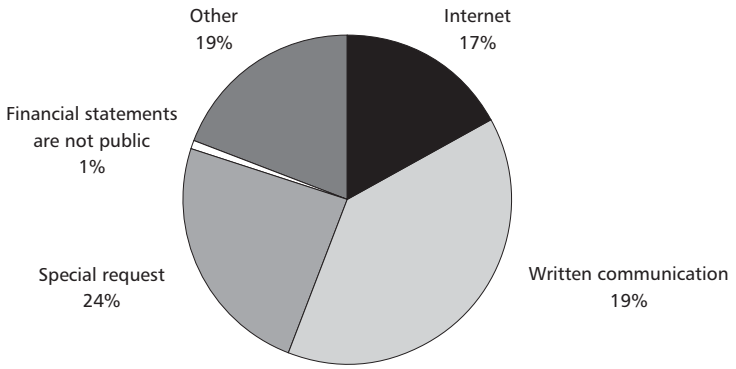
The purpose of a uniform accounting methodology and chart of accounts would be to develop an analytical framework for financial reporting that could be used for monitoring and comparing the performance of local units. Annex 6.2 gives an overview of the information system—the use of budget classifications and prescribed reporting framework.

Subnational fiscal reporting is a tool for the monitoring process, but in practice the information is used mostly by the Ministry of Finance, and even then more for statistical purposes than for suggesting corrective measures and improvements in the quality of work of local units. Other monitors rarely use financial reports.

Public availability of the financial reports was measured by the fifth question of the questionnaire. Three local units (two municipalities and one town) answered that financial statements are not for public, and in 24 percent of the cases citizens have to

submit a special request for financial information. This shows that the mentality of secrecy is still present. The answers are shown on Figure 5.

Figure 5.
Citizens' insight into the LGU's financial statements



The sixth question was asked to gauge general management's attitude towards citizens' participation during the whole budget process (preparation, execution, examination of the financial statements). Seventy-five percent of the local units think that public involvement is inevitable because the aim of a local unit's operations is to satisfy citizens' needs. If citizens are not actively involved in the budget process, then it is not possible for the local unit to know if the aim is fulfilled and what is necessary to undertake in the case of non-fulfillment. Even though this question was asked in a suggestive way, with an explanation of why the local units need good feedback from citizens, 25 percent of the local units answered that there was no need to involve the public in the budget processes because the citizens do not have enough knowledge for active participation.

Answers to the questions in the first part of the questionnaire describe the level of the openness of the budget processes. Local units are aware that the public should be informed and try to involve media in all stages of the budget process. Information is publicly available, but institutional capacities and activities taken in order to achieve active involvement and communication with the public are still very poor.

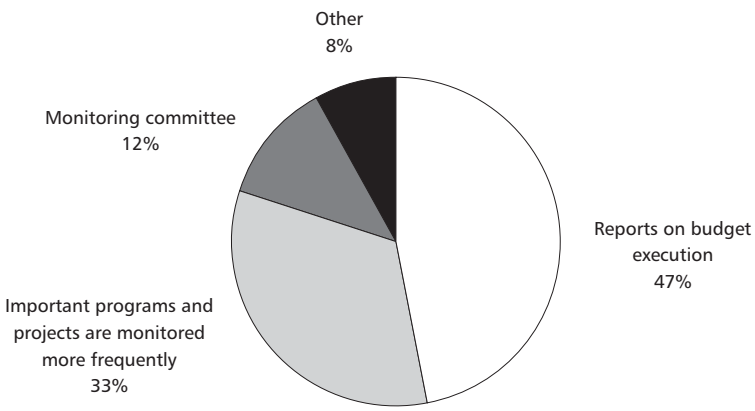
3.4 Monitoring and Control Mechanisms

After the budget adoption, the assembly monitors and controls the budget execution mainly through reports (which are semi-annual and annual). One-third of local units have established a special monitoring procedure for major programs and projects. Only some local units' assemblies feel the need for such a system and apply it at least to the

most important programs. Some local units have organized a monitoring committee appointed by the assembly with the task to inform the assembly twice (or more) a year about the efficiency and efficacy of budget execution.

The distribution of the assemblies' monitoring and control mechanisms is shown in Figure 6.

Figure 6.
Monitoring and control mechanisms over budget execution



The basic internal structure for monitoring and control exists but procedures for good functioning are undeveloped.

The procedures for discovering, preventing, and reporting irregularities are one of the basic tools of a budget watch program. The tenth question of the survey asks if such an irregularity procedure exists at the local unit level. The answers clearly show that:

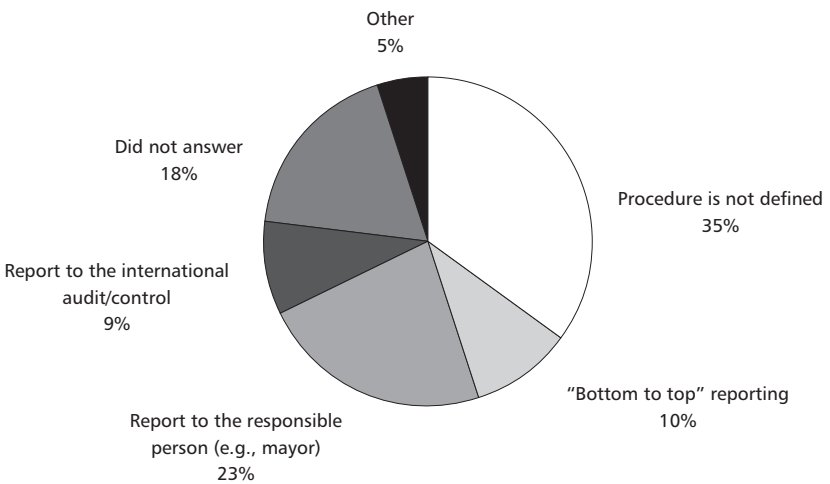
- there is no common understanding what the irregularities are (some of the local units think that irregularity is fraud; others understand irregularities as small and common mistakes),
- irregularities are still a topic that a significant number of local units try to avoid (18 percent did not answer the question);
- there are no general rules established by the central government;
- there are different approaches in the practice on discovering and reporting the irregularities, shown in Figure 7.

The following answers demonstrate how poor the understanding of irregularity procedure is:

- everybody knows everything; there are no secrets as well as the irregularities; we are only eight;

- there was no case of irregularity and because of that I cannot describe how the employees would react to it;
- all irregularities are immediately corrected.

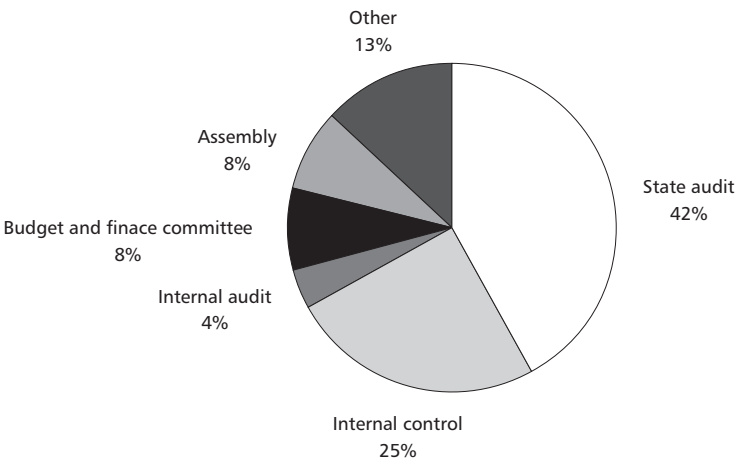
Figure 7.
Irregularity procedure



External monitoring mechanisms are poor. The eighth question checked if the local units feel that they are monitored, controlled, and audited, and what kind of monitoring, control, and audit do they recognize and meet in their everyday activities. The State Audit Office was recognized as the main external monitoring body. Others were mostly examples of internally organized functions such as internal control, internal audit, monitoring performed by the assembly, and by the budget committee. Only a few local units mentioned an additional example of an external monitoring, control, and audit body beside the State Audit Office, namely the tax department. Nobody mentioned the central government, the Ministry of Finance, or other line-ministries. This result is a reflection of the reality of no established procedures for monitoring the local units by the central government.

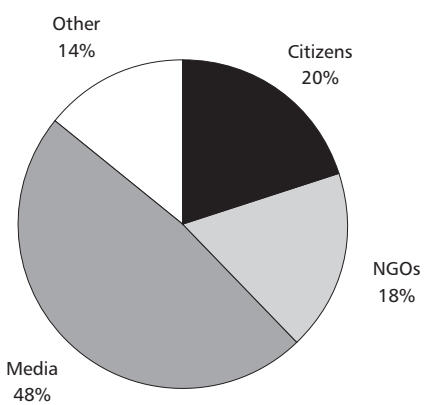
Kinds of monitoring, control, and audit mechanisms recognized by the local units are shown in Figure 8.

Figure 8.
Monitoring, control, and audit performed in LGUs



In the ninth question local units were to state who is (among citizens, NGOs, or media) organized to monitor the local unit's activities and use of budget money, and how. Media are present the most, but citizens and NGOs are also recognized as entities that are trying to monitor what is happening in the local unit. The distribution of the answers is shown in Figure 9.

Figure 9.
Who monitors in an organized way the LGU's activities
and the use of the budget money?



Citizens are, as an organized monitoring mechanism, more present in municipalities than in towns and counties. Most of the municipalities described that citizens are organized and present in the local boards. Among NGOs, sport clubs, cultural institutions, different associations, and political parties were mentioned. They are interested in receiving financial support from the local unit and monitor carefully what the local unit spends the money on.

Media—local radio, TV and newspapers—are the most powerful and influential. Lot of examples of special shows and columns are given. Media are able to initiate communication between the public and local government, to talk openly about problems, and to change the mentality of secrecy.

4. PROPOSED REMEDIES FOR SUBNATIONAL BUDGET WATCH IN CROATIA

The problem of a subnational budget watch in Croatia should be remedied by solving legal weaknesses and the lack of institutions and human resources. The solution of any of the above-mentioned issues will vary depending on the causes for the lack of a subnational budget watch by specific groups as shown in Table 1.

Table 1.
Causes for the lack of a subnational budget watch

Causes	Central government	Citizens, media, NGOs
1	2	3
Legal weaknesses	• no mechanism for monitoring and controlling the work of local units • no financial management and control mechanisms for achieving fiscal discipline, only limits on borrowing • absence of a system for internal information exchange and monitoring the efficient use of transfers	• no statutory provisions requiring public presentation (e.g., via web pages) of budget proposals at the preparation stage • unavailability of information on budget execution • lack of simplified financial reports intelligible to wider public
Lack of institutions	• State Audit Office and Budget Supervision are the only established institutions	• association of towns and municipalities—very passive and narrow functions
Capacity	• lack of special knowledge (for monitoring and analysis) • the lack of staff	• insufficient knowledge to deal with the information presented in a complicated way
Willingness	• depends on political decision • lack of capacity causes lack of willingness	• lack of awareness of the need for participation and of changes that can be encouraged

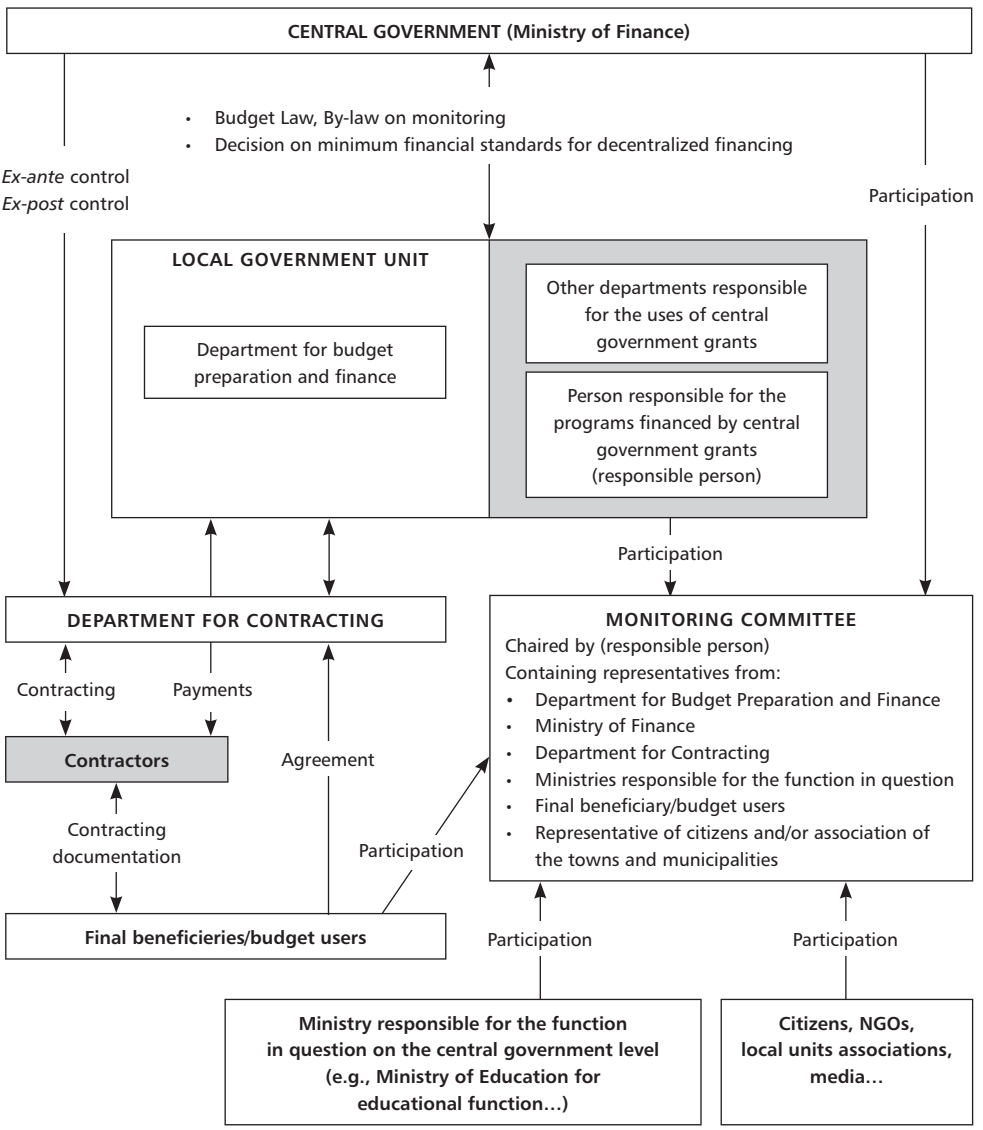
These four factors of weak budget monitoring are interwoven and mutually enforceable. Some factors are currently more important (like dependency on political decision) while some other need more time and effort (like the lack of special knowledge for monitoring and analysis and the lack of staff). Additionally, decentralization is often one of the causes of weak oversight. Decentralization benefits accrue from a closer linkage between fiscal decisions and communities, but the negative side is that administrative costs are likely to rise and decentralized activities are harder to monitor. All these weaknesses are blocking communication among all interested parties, and without communication it is not possible to have a good monitoring system in practice.

Table 2.
Who should do what and when?

Central government	Subnational governments	The public
Clearly define powers and responsibilities at each level of government.	Improve budget and accounts documentation.	Communicate, get involved, ask, and actively participate in all processes.
Establish stable transfer mechanisms based on objective criteria.	Report on risks to the legislature.	Give concrete suggestions.
Establish general government reporting procedures, accounting methodology, and politics (data standards).	Establish effective internal and external oversight mechanisms.	Expand knowledge and understand.
Develop administrative capacity at all levels of government.		Act and change before "voting with feet."
Assist subnational governments to improve transparency.		

Rather than elaborating further on what could or should everyone do, we will only single out one of the proposals for the Ministry of Finance. We propose it to establish a monitoring committee, consisting of the representatives of all entities in the system, as shown in Figure 10.

Figure 10.
Proposal for the institutional framework for subnational budget watch



We are also proposing an action plan for the monitoring committee in Table 3.

Table 3.
Monitoring committee's action plan

What	When	Treatment	Result
1	2	3	4
Proposition of the financial plans (programs)	In June	Discussion and negotiation of acceptable programs	Stakeholders agreement on programs
Execution	In July (for the first half of year) In May (for the previous year)	Discussion of objectives achieved, review of performance measurement	• cutting unsuccessful programs • better allocation of money
Financial reports	In July (for the first half of year) In March (for the previous year)	Overview of the financial situation based on financial reports	• better understanding of local unit's financial capacity • presentation to the public
			• reports to be submitted to the representative body in the local unit • reports for public presentation

That is the step that Ministry of Finance could undertake to promote participation. All other parties interested in the budget, irrespective of their status should:

- **Insist on information**
  Request information from your own local unit about what has been done over the past year. Keep a watch on other local units, compare own unit with others, and demand improvements where needed. Financial reports are not easy to understand and if a local unit has not adapted reports for its citizens, the public should insist on it and demand regular communication.
- **Ask and actively participate in the process**
  Get organized and ask to be present at the meetings and the sessions held by the governing boards of local government units. Send requests for service improvements, establish written communication with your own local unit, initiate changes, and make suggestions for improvements. Positive examples are call-in radio shows where callers put forward their questions and requests for local government officials. Journalists then seek to provide citizens with the requested information and bring local officials to discuss issues on a live radio

broadcast. This type of communication usually resolves the problem to citizens' satisfaction.

- **Cooperate with NGOs and participate in monitoring committees**
  Below, in Table 4, is the roadmap for public monitoring.

Table 4.
Roadmap for public monitoring

Process	Involvement	Time	Result
1	2	3	4
Budget preparation	• participation in decisions about programs	June–October	• better understanding of the work of local government • more satisfaction with local government services
Budget execution	• monitor, check the evidences on progress	all year	• prevention of the inefficient use of public funds • prevention of fraud and irregularities • developing budget execution reports for public
Financial reporting	• comment, require simplicity, compare statement of revenues and expenses based on functional classification with other local units	July and February	• better understanding of the situation in the local community • idea about new possibilities for development
Monitoring	• try to be formally present in all stages	all year	• institutionalized monitoring committee

5. CONCLUSIONS

There are many reasons why the monitoring of subnational budgets is deficient. We can single out the lack of an institutional and legal basis and the lack of knowledge and tradition making public finance public. The lack of knowledge is particularly pronounced in financial management control and internal audit, the functions that soon are to be introduced at the central and local government level. Under the heading of tradition, we consider the passive way of functioning and the mentality of secrecy present for far too long. Mental and cultural changes are needed in order to introduce concept of accountability and responsibility.

Effective monitoring requires that all stakeholders realize that the central government, local units, and citizens need to change their relationships and their attitudes towards public goods. Central government should the analyze information from local units, collect additional data on their activities, and regularly meet with their representatives. Local units should not be passive and just wait for the instructions from the central government. They can and have to be proactive in order to spark changes and development of their environment. Citizens, for their part should organize better, break their passivity, and start to discuss, analyze, and make well-argued proposals. They have to use their power and demand accountability. Local administration is there because of citizens and for citizens.

Reform measures for the establishment of the subnational budget watch system should include measures aimed at strengthening financial control, improving exchange of information and communication, providing managers with the required flexibility for efficient management, and developing accountability for results.

Given the author's background, her ties to the Ministry of Finance, the conclusions of this chapter are limited insofar as they focus more on the institutional framework and central government role in a subnational budget watch program.

In the future more in-depth research on local budgets' transparency could examine what kind of changes in the budget methodology are needed to make local units more open and closer to their citizens. Another subject for further research is the role of civil society in a subnational budget watch agenda.

6. ANNEX

6.1 Participation

Local units and the public are still passive. Some local units have tried to find the mechanisms for communication with the public in order to involve it more in the budget processes. Still, there are no procedures based on which a local unit regularly and systematically communicates with the public; communication is more *ad hoc* and depends on the willingness from the both sides. There are certain number of local units that think that budget preparation and adoption is an internal process and that it is too technical an issue for public involvement. The citizens are still not aware of the possibility to organize themselves and participate in the decision-making process at the local unit level. The media are very active and try to monitor local units and inform citizens. They are currently the best connection between local units and citizens, but direct communication is missing. Local radio, TV, and newspapers are the most powerful and influential. Media should continue developing communication between

the public and local government, talking openly about the problems and changing the mentality of secrecy.

6.2 Information

The information about local units' activities is available to the public even though the majority of local units still do not put much effort into making the information public. They mostly use easy and common means of communication such as Internet, TV, newspaper, and radio. Only 16 percent of local units prepare brochures and make the information more user friendly and understandable to the public. There is no organized and systematic approach with a clear goal and vision of what should be achieved through the process of improving the climate for a subnational budget watch program.

6.3 Accountability

It is not easy to talk about accountability within the system in which controlling mechanisms are not formally organized and established. Internally, accountability comes more as a consequence of a well-defined control system in which the basic operational facts are determined. The main preconditions needed to achieve the culture of responsibility and accountability within the system are still missing. We mean the strong commitment from the top management; transparent, comprehensive, and easy-to-use written procedures; a respected principle of separation of duties and powers assuring that there is no conflict of interest; an effective internal control system: an independent audit function; effective external control system: external audit, monitoring from different bodies; active stakeholders' monitoring and involvement; proper procedures for communication with the stakeholders; developed information and reporting procedures. Until these preconditions are in place, accountability will remain *ad hoc* and rare.

6.4 Basic Data about Local Finances

The data show very slow changes in finances of local units with respect to the general government. There is a slight increase in revenues and decrease in expenditures in the period 2002–2004. Local units' expenses with respect to GDP also increased slightly. This data confirms that the decentralization process did not move much further from the first step and that Croatia is still a relatively highly centralized country.

Besides the size of fiscal capacity of local units, what is also important are their functions and tasks.

- Municipalities and towns have tasks and responsibilities in housing, spatial and urban planning, utilities, social and childcare, primary healthcare, elementary education, culture and sports, consumer protection, environmental protection, fire protection, and civil service.
- Counties are in charge of education, health, spatial and urban planning, economic development, transport and traffic infrastructure, planning and development of the network of education, and health, social, and cultural institutions.

Table A1.
Local units' revenues and expenses as a part of the general government revenues and expenses

[Billion HRK]	2002		2003		2004	
	Revenues	Expenses	Revenues	Expenses	Revenues	Expenses
1	2	3	4	5	6	7
General government	75.3	75.4	81.0	80.8	88.8	87.7
Local units	11.8	9.40	13.8	10.9	14.8	11.7
Ratio (%)	15.6	12.4	17.0	13.4	16.7	13.3

Table A2.
Local units' expenses in relation to GDP

[Billion HRK]	2002	2003	2004
1	2	3	4
GDP	179.4	193.1	201.8
Local units	9.4	10.9	11.7
Ratio [%]	5.2	5.6	5.8

Decentralized functions (primary and secondary education, social welfare, healthcare, and fire protection) of counties and cities are financed from two main sources: additional share of income tax and equalization fund grants from the state budget.

Table A3.
Financing decentralized functions [thousand of kuna—HRK]

#	Function	2002			2003			2004		
		Counties and City of Zagreb	Towns	Total	Counties and City of Zagreb	Towns	Total	Counties and City of Zagreb	Towns	Total
1	Elementary schools	411.4	153.0	564.4	496.5	184.2	680.7	541.6	199.6	741.2
2	Secondary schools	317.3		317.3	382.9		382.9	368.5		368.5
3	Healthcare	384.6		384.6	394.3		394.3	397.6		397.6
4	Social welfare	244.5		244.5	215.3		215.3	227.2		227.2
5	Fire prevention				12.0	67.1	79.1	39.1	198.7	237.8
6	**Total plan of expenditure (sum 1 to 5)**	**1,357.8**	**153.0**	**1,510.8**	**1,501.0**	**251.3**	**1,752.3**	**1,574.0**	**398.3**	**1,972.3**
7	Realized from additional share in income tax	588.7	76.5	665.2	590.9	89.5	680.4	676.0	123.4	799.4
8	Allotted from equalization fund	769.1	76.5	845.6	910.1	161.8	1,071.9	898.0	274.9	1,172.9
9	**Total financing (7+8)**	**157.8**	**153.0**	**1,510.8**	**1,501.0**	**251.3**	**1,752.3**	**1,574.0**	**398.3**	**1,972.3**

Source: Financial reports of local units' budgets from 2001 to 2004.

Except for funding the decentralized functions, central government provides grants to counties, municipalities, and towns of the first and second group in territories under special state concern according to the criteria established in each fiscal year. These grants are intended for the adjustment of the budgetary fiscal capacity and investments in development programs of counties, municipalities, and towns. In addition to such direct allotments, relevant ministries transfer capital grants to local units for entrepreneurial programs, management of water, and others co-finance local units development programs.

Table A4.
Current grants from the state budget to local government units [HRK million]

Local units current subventions	2002			2003			2004	
	No. of units	Budgeted	Actual	No. of units	Budgeted	Actual	No. of units	Budgeted
Cities	29	60.5		24	48.7	46,9	11	9.8
Municipalities	82	65.8		72	54.6	53,9	55	26.3
Counties	20	74.6		20	80.6	80,6	14	39.8
Total	**131**	**201.0**	**201.0**	**116**	**183.9**	**181.4**	**80**	**75.9**

Source: Croatian State Budget for 2002, 2003, and 2004 and the Report on State Budget Execution for 2003.

Table A5.
Share of grants in central government revenues

[HRK billion]	2002	2003	2004
1	2	3	4
Central government revenues	69.6	74.7	82.3
Grants (and share in income tax) to the local units	1.5	1.7	2.0
Ratio [%]	2.2	2.3	2.4

6.5 Questionnaire about Local Government Units' Monitoring and Control System

This questionnaire is intended for the heads of the financial divisions in the local units and its aim is to analyze:

- the openness of the budget processes through testing information that is publicly available, communication methods with citizens

- mechanisms of monitoring and control that insures legal adoption and execution of the budget.

Data from the questionnaire will be used exclusively for analysis, therefore you are requested to answer the questions objectively and honestly.

I. OPENNESS OF BUDGET PROCESSES

1. **Does the public (citizens, nonprofit organizations, media, scientists and other stakeholders) have an insight in the budget draft (before the meeting of the representative body at witch it is decided about the adoption of the final budget):**

   ❑ YES
   (if your answer is YES circle one of the options below which best describes the way in which public in your local unit have an insight in the budget draft)

   a) budget draft is shown on the website,

   b) budget draft is published in the local gazette,

   c) budget draft is not published but everybody who is interested to have an insight and asks for it can get it,

   d) during the budget preparation process—from July to October, we are organizing discussions about the budget to which the representatives of the citizens, associations and other NGOs, media… are invited.

   ❑ NO
   (if your answer is NO circle one of the reasons below)

   a) publishing the budget draft is against the law,

   b) budget draft is a secret,

   c) public is not interested to be involved in the budget preparation process,

   d) publishing the budget draft would not make sense because in the negotiation process only budget users and local unit participate,

   e) anything else _____

2. Budget adopted by the assembly is published:

❑ YES
(if your answer is YES circle one or more of the options below)

a) the legal obligation of the local unit is to publish the adopted budget,

b) it is important to inform the public about programs and aims which are to be achieved during budget execution in the following year,

c) local unit needs to get feedback from the public whether the budget satisfies or not their expectations,

d) anything else _____

❑ NO
(if your answer is NO circle one or more of the options below)

a) budget is too complicated and public can not understand it,

b) public is not interested in the budget,

c) there is no possibilities to influence the budget (to change it) after its adoption and because of that communication with the public after that has no sense,

d) anything else _____

3. The discussion about the annual and semiannual report on budget execution is:

❑ PUBLIC discussion
(if you answer is PUBLIC circle one or more of the options below)

a) special simplified brochures are prepared and distributed to citizens in order to enable them to be informed about the local unit's activities and achievements,

b) representatives of citizens, media, NGOs and other organizations are invited to meetings of the assembly on which the reports on budget execution are discussed,

c) representatives of citizens, media, NGOs and other organizations prepare their reports on how their expectations have been fulfilled and these reports are also a part of the assembly discussion about budget execution,

d) anything else _____

❑ NON-PUBLIC discussion

4. **The public attitude towards the local unit's programs and their satisfaction with the services is regularly examined:**

   ❑ YES *(explain how)*

   _____

   _____

   ❑ NO *(explain why)*

   _____

   _____

5. **Citizens have an insight in the local unit's financial statements (circle one or more of the options below):**

   a) through the Internet,

   b) through brochures and other written means of communication,

   c) they have to submit a special request,

   d) financial statement are not for the public,

   e) anything else _____

6. **Management's attitude about citizens' participation in the budget processes is best described as (circle the statement which suit best):**

   a) there is no need to involve the public in the budget processes because they do not have enough knowledge for active and quality participation,

   b) public involvement is inevitable because the aim of local unit's operations is to satisfy the citizens needs. If the citizens are not actively involved in the budget processes it is not possible for the local unit to know if the aim is being fulfilled and what to undertake in the case when the aim is unfulfilled.

II. MECHANISMS OF MONITORING AND CONTROL WHICH INSURES LEGAL ADOPTION AND EXECUTION OF THE BUDGET

7. **After the budget adoption the assembly undertakes the monitoring and control mechanisms over the budget execution in the following way (circle one or more options below):**

a) based on the annual and semiannual reports on budget execution,

b) some important and major programs and projects are specially monitored and reports about their execution are prepared and given to the assembly more frequently,

c) the assembly has appointed the monitoring committee the task to inform twice (or more) a year the assembly about the efficiency and efficacy of the budget execution,

d) anything else

_____

_____

8. State all kinds of monitoring, controls, and audits which are normally preformed in your local unit:

_____

_____

_____

9. Who outside the budget system (local unit and budget users) monitor in an organized way the activities of the local unit and the use of the budget money (circle one or more of the answers below):

a) citizens (if you have circled this answer please describe how they are organized)

_____

b) NGOs (if you have circled this answer please state which ones and how they are organized)

_____

c) local radio, TV, and newspapers (if they have some special shows or editorial columns meant for the discussion of the local unit's activities and citizens' satisfaction or something similar related to the local community, state their title and shortly describe their aim)

_____

_____

d) anybody else

_____

10. If somebody among the employees notices an irregularity in the local unit's activities is there any rule for him/her how to proceed and to whom to report. If your answer is YES describe shortly the procedure.

_____

_____

_____

_____

GENERAL INFORMATION

11. The job and the position of the person who has fulfilled this questionnaire

_____

_____

12. Local unit for which the questionnaire is fulfilled is:

a) county

b) town

c) municipality

13. Number of citizens and size of the budget in the local unit:

number of citizens _____

size of the budget 2004 _____

Please mail the filled questionnaire by April 20 to the following address:

Ministarstvo financija
att. Mrs. Ivana Maletić
Katančićeva 5, 10000 Zagreb

Or by fax: 01/4591-473.

If you need to ask anything do not hesitate to call 01/4591-093.

THANK YOU FOR YOUR COOPERATION!

Date: _____

ENDNOTES

[1] www.mfin.hr → local government → counties

[2] At the beginning of the research the intention was to survey citizens too, but after a pilot project with a group of colleagues who are all experts in the field, yet completely uninformed as citizens, I realized that it made no sense. All the answers were negative because the experts from the pilot were not acquainted with the budgets of their local units. Here is a sample of the questions: Have you ever had an opportunity to see or read the budget of the local unit in which you live? Have you ever had an opportunity to participate in the process of budget adoption? Do you monitor how and with which results programs and projects preformed in your local unit are executed?

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Subnational Budget Monitoring in Macedonia: Case Studies of Municipalities of Štip and Gostivar

Zhidas Daskalovski

EXECUTIVE SUMMARY

This paper tackles the question of subnational budgetary monitoring in Macedonia. It offers a general analysis of the decentralization reforms in the country with a particular attention to the possibilities for the public oversight of budgets on the local government level. The paper argues that the legal order does not prescribe the process and that there are also no clear possibilities within the law for budgetary oversight by concerned citizens and nongovernmental organizations. Moreover, as the examples from the two municipalities of Štip and Gostivar show, budgetary monitoring on the subnational level is very difficult to undertake in practice. To change the present circumstances the author recommends a number of policy measures aimed at strengthening the role of the civil sector in the budgetary oversight of local governments.

1. INTRODUCTION

In the process of decentralization, the Government of Macedonia has committed itself to devolve the responsibilities of the central government to local government units. This may result in better governance and create more opportunities for citizens to participate in the civil society and may further democratize and stabilize the country.

Decentralization reform is supposed to provide better public inputs that ultimately aim to enhance the growth of the local communities in comparison to a centralized system that often results in concentrating power and growth in the capital city Skopje. This paper argues that, in order to ensure an effective use of public funds, the decentralization process in Macedonia should be accompanied with an adequate and close

monitoring of all the stages of the budget process at the local level to guarantee its effective execution. Citizen-driven budget monitoring is part of new efforts to introduce transparency in the democratization of the country.

The first part of the chapter provides a short overview of Macedonian decentralization where competences were transferred to local self-governments to collect taxes and reallocate funds for financing public services on the local level. This assumes that the mechanisms for monitoring the performance of the budget are not very satisfactory, largely because models of participation and monitoring for local government budgeting do not exist. Indeed, the second part of the chapter—an analysis of the related legislation and the description of the realities concerning budget monitoring in two Macedonian municipalities—Štip in the east of the country and Gostivar in the west—confirms the problem of budget monitoring on the subnational level. In fact, this chapter will reveal that achieving an effective public supervision over the municipal budgets of Gostivar and Štip is difficult, and that the local authorities hardly are prepared to step beyond regime-like behavior and accept the principles of accountability and transparency.

In the next section the chapter offers a brief description of the importance of budget monitoring and an evaluation of policy options for Macedonia. The chapter concludes that the Macedonian citizens, who are supposed to be the main beneficiaries of decentralization reform at the moment, do not participate in the monitoring of the budget cycle at the subnational level of government. With that in mind, decentralization reform should be aimed at empowering civil society and giving it the skills, knowledge, and awareness of its role in putting leaders and public officials at task to deliver and ensure effective service delivery to their constituencies as direct beneficiaries.

2. SUBNATIONAL BUDGET MONITORING IN MACEDONIA EXPLAINED AND EVALUATED

2.1 Decentralization Reform and Subnational Budget Monitoring

Before the reforms of 2004, according to one analysis, Macedonia was one of the least decentralized nations in the world when measured by the relative size of the budgets of its local governments (Rafuse 2002: 2).

Following the 2001 Ohrid Framework Agreement, Macedonia has engaged in a thorough decentralization effort, committing itself to devolve responsibilities from the central government to local government (LED) units.[1] The government aimed at correcting inadequacies in the functioning of municipalities and enhancing their capacity to create sustainable local economic development by using their own revenues.

Thus, decentralization implies the transfer of responsibilities to local self-government, in terms of tax collection and reallocation of funds for financing public services on the local level.

After the reforms of 2004, municipalities are to be financed from their own revenue sources, government grants, and other sources, including borrowing. The property, inheritance, gift, and sales taxes on real estate and property rights, as well as communal fees, will become the truly individual sources of revenues for local governments. Moreover, the municipalities will now be responsible for setting the rates on these taxes, communal fees, and charges like the hotel duty/tax and the sign fee, with maximum and minimum limits specified by the Law on Property Taxes (Levitas 2004: 10). Other revenues will include a three percent share of the personal income tax paid by people living in a given municipality[2] (Law on Craftsmanship). In addition to own revenues, the Law on Financing Local Self-Government Units envisages a number of grants given by the central budget as additional revenues for the municipalities: revenues from value added tax (general grants), block grants, earmarked grants, capital grants, and grants for delegated competencies.

The municipalities manage their budgets according to the guidelines provided by the Ministry of Finance. The mayor has full authority to make all payments as well as to authorize all procurement and is accountable to the city council. He has a legal obligation to provide a report to the council on all expenditures made during the course of the year. Municipalities do exercise their right to move expenditures among various line items during the year. Expenditures are recorded when they are paid from the account, and any funds remaining in the municipality account at the end of the year are carried forward into the next fiscal year as a surplus.

The Budget Law regulates the procedure of preparation, adoption, and execution of the municipal budget. The process begins with directions proposed by the Ministry of Finance for the estimated budget revenues and expenditures for the following budgetary year and their submissions to the government. Then, the minister circulates a letter containing the main guidelines for the preparations of municipal budgets and forwards it to the local units. The units of the local self-government, within the determined maximum amounts of expenditure, prepare a draft budget request. The draft contains the funds allocated to the municipal council, the mayor, and the administrative bodies, and to various programs (like communal regulation, street lighting, roads, parks, or forestry) and submits it to the Ministry of Finance. Thus, upon receiving the draft budget request from the municipality, the Ministry of Finance evaluates it considering its "efficiency, priority and rationality, and reconciles it with the budget beneficiaries." On the basis of the reconciliations with the budget beneficiaries, the Ministry of Finance prepares a draft budget and submits it to the government, which than adopts it, and by mid-November submits it to the Assembly for further adoption. The Parliament debates on the draft budget "not prior to 20 days from the day of its submission,"

but in practice, the budget is often adopted later than the beginning of the fiscal year, although not later than March of every year (The Macedonian Government's Answers to the EU Questionnaire on the Application for Membership: 49).

In accordance with the relevant law, the State Audit Office (SAO) performs both state audits and audits of the budgets of local self-government units. Additionally, there is a system of regular (*ex post*) internal accounting control, which monitors whether the financial transactions are executed in accordance with legal regulations, whether there is appropriate accounting documentation, and whether the financial statements provide complete, authentic, and reliable information on the year's financial changes and transactions.

According to the official government conclusions adopted on January 26, 2004, internal audit units within the local government units are to be established by the end of March 2006 (Answers to the EU Questionnaire: 15). These units are supposed to be provided with separate resources to achieve organizational and functional independence. Within units of local self-government, a certified accountant will carry out *ex ante* control of the accounting documents. This control encompasses all accounting documents and an authentic and realistic presentation of the accounting changes, i.e., transactions. Until the internal audit entities in local government units are established, the Section for Central Internal Audit within the Ministry of Finance will perform the internal audit in the units of local self-government.

2.2 Evaluation of the Current Legal Situation

Macedonian local government is in a state of flux. Thorough reforms have been envisioned, adopted, and planned in different spheres of governance on the local level.

Accordingly, the 2004 Law on Local Government gives new and increased competences to local government units in the spheres of primary health care, primary education, sport, and culture, as well as the promotion of citizens' participation. The law attempts to guarantee better services to citizens since most of the prerogatives are given to the local municipalities, and this decentralization process touches upon the issues in this chapter. In the process, the highly centralized political system will be changed so that budget formation and monitoring will be enhanced significantly at the local level. The result of the legal reform—the creation of own resources through the collection of local taxes and the allocation of three percent from the value added tax for local use—will help the local authorities develop the municipal budgets in accordance to the needs of the citizens in the locality.

The greater the degree of decentralization (fiscal, functional, and financial) is, the greater is the need for improved systems of accountability. This is a standard European

practice relevant to Macedonia. The EU accession process, for example, highlights the need to develop systems of external audit for local governments and to restrict indebtedness, measures that are both unpopular and technically demanding.

Within the legal framework there is no mention of the possibilities for citizens' involvement in the budgetary process. Budget monitoring is determined to be the obligation of the Ministry of Finance and the State Audit Office, with the future internal audit units within the local government units taking over some of the responsibilities. Indeed, these units for internal audit will give local governments greater autonomy in the process of monitoring the budget execution. The decentralization and the transfer of competences to the local authorities do not directly provide legal tools for the involvement of citizens in the budgetary process. However, the legislature does not preclude the local government's budget monitoring by concerned citizens either. Quite the contrary, a number of legal provisions from the Law on Local Self-government can be seen as encouraging such actions.

According to the Constitution and the Law on Local Self-government, local units have the right to local self-governance through direct participation of citizens in decisions about common matters. Moreover, the reformulated text of Article 115, Paragraph 1 of this law refers to the jurisdiction of units of the local self-government. This jurisdiction has been modified to read:

> In units of local self-government, *citizens directly* and through representatives participate in decision-making on issues of local relevance, particularly in the field of public services, urban and rural planning, environmental protection, local economic development, *local finances*, communal activities, culture, sport, social security and child care, education, primary health care and other fields determined by law (emphasis added).

These legal provisions, although they do not directly provide for the possibility for budget supervision on the local level, ensure the legal background for such activity. However, is budget monitoring on the citizens' groups agenda? How cooperative are municipalities in allowing supervision of budgets on a subnational level?

2.3 Practical Considerations: Municipal Debt

For fiscal decentralization to be a success, the indebtedness of local government units is a serious issue. The laws stipulate that the budgets of the local self-government units are not allowed to have a deficit. In practice, however, local governments have debts, and to manage the debts they sometimes have to undertake illegal financial management practices. One such practice is that subnational governments simply do not process incoming invoices into the accounting system, assuming, that if debt is not reported,

then it does not exist (Schlumberger 2004: 34). This very simple "strategy" of local governments cannot be easily identified by the State Audit Office or by the local council. Since within the law there is no provision for recording a commitment when expenditure is authorized, in subnational governments there is often no record of invoices that have been received by the municipality, but have not been paid (Op. cit.: 20). Another "strategy" to deal with debt is to open a second bank account. In principle, local governments are not allowed to open more than one bank account, and all the transactions of sub-accounts should be managed through this main bank account. However, for managing financial transactions, when the local government's bank account is blocked, municipalities have opened alternative accounts. This system has been tolerated by the government, "as this was the only way to keep the local governments in business and provide the basic, minimum level of public services" (Op. cit.: 35). Starting from 2004, local governments are not allowed to have more than one bank account. However, the enforcement of this new regulation is doubtful. As the former compulsory agency for payment and transfer system (*Zavod za Platen Promet*) ceased to exist, there is no effective mechanism controlling local financial management in this respect.

According to a recent study, local governments owe suppliers of goods and services more than MKD 2.6 billion without interest, and about MKD 3.2 billion with interest, respectively one-third or one-half of the entire sector's revenues in 2004 (Op. cit.: 35).[3] About 75 percent of this debt is owed to construction companies. Creditors have court orders to block money on municipal accounts to serve debts, and in 2004 around 40 municipalities have had their accounts blocked for short periods. In order to resolve the debt, a Debt Resolution Plan is currently being prepared, as a precondition for the fiscal decentralization (Answers to the EU Questionnaire: 42). Considering the circumstances, it is clear that making public finances public under a subnational watch scheme will be a sensitive issue in many Macedonian municipalities.

3. WHY IS SUBNATIONAL BUDGET MONITORING IN MACEDONIA IMPORTANT? PRACTICES FROM ŠTIP AND GOSTIVAR

This section offers an assessment of what is the situation on the ground. We ask to what extent are such common instruments of involvement—like citizen committees, polling, public opinion surveys, public hearings, information dissemination, informal meetings with community representatives and NGOs, or open houses—represented in the current budgetary practice of the local government units? Our field work seeks to answer if the data available, reliable, and of quality? Furthermore, is the data timely and is it possible to compare actual versus planned figures? We conducted the field work in the municipalities of Štip and Gostivar. The need for comparison of these two municipalities was based on the following criteria:

- Similar size (both municipalities have approximately 45,000 inhabitants)
- Ethnicity/multiethnicity (Gostivar is a truly multiethnic municipality, with Macedonians, Albanians, and Turks living there, while Štip is predominantly Macedonian municipality with a small number of Vlachs)
- Geographic location (Gostivar is located in western Macedonia, while Štip is in eastern Macedonia).

By assessing Štip and Gostivar we shall draw a picture of the current local government policy (actual practice) concerning public involvement in the budgetary process. Thus, what are the possibilities for budget monitoring in these municipalities? To ascertain this, field work was conducted over a period of nine months. The main stakeholders were interviewed and the possibilities for citizens input in the budgetary process and monitoring were evaluated. Besides public institutions and the mayors' offices, local civil society organizations also were consulted.

Our field work reveals a complex situation in both Štip and Gostivar. On the one hand, the local authorities proclaim that there are possibilities for such measures, i.e., "There is no problem with that. The citizens are informed and can monitor." On the other hand, once we checked this issue, we realized that actually there are no actions undertaken by the local authorities in this regard. Quite the contrary. Moreover, citizens and citizen associations of these municipalities seem to have little interest in the issue, remain passive regarding public involvement, and have not considered placing budget supervision on their agenda.

Let us first start with the description of the situation in the municipality of Štip.[4] Responding to the question whether the municipality can generate sufficient revenues, so that, within the framework of a fiscally decentralized system, it is able to function properly, the mayor of Štip answered positively, replying that the municipality is an entity with a strong economy to tax and that the municipality has a "sufficient technical and human capacity to cope with the challenges of fiscal decentralization" (Interview, January 14, 2005). Concerning the question of budget monitoring, the mayor pointed out that the citizens can be involved in the whole process and that the budget is freely available to the public. When asked for a copy of the budget, however, the member of the mayor's staff, who was instructed to provide us with one, delivered only very general data about this year's budget. Only when we mentioned that we would like to be given the full budget of the municipality, upon the insistence of the mayor, did the concerned person provide us with the requested data. In the first instance we were given the introductory page of the budget that only specifies the total budget revenues and expenditures. Later, we were given the additional pages that contain information on all the revenues and expenditures broken down into categories (Interview, November 10, 2004). The full budget contains data about the revenues

from different kind of taxes, expenditures on the salaries of the personnel, honoraria, per diems, travel expenses, etc., some of which might be sensitive if distributed without approval from the mayor.

This small episode indicated that budget monitoring in the municipality is not such a simple affair as stated by the mayor. We immediately asked him if the full budget is available to the citizens of Štip, and if yes, how can they get a copy of it, i.e., if there was a special procedure that might discourage them from doing so. The answer was that the whole budget is available to the citizens at the Citizens' Information Center, located in the same building (Interview, November 10, 2004). To appraise if this is so, during the next field trip to Štip, I visited the aforesaid center. The personnel in the Citizens' Information Center were nice and cooperative up to the moment when they were asked for the budget of the municipality. This kind of cooperation was out of question, and the budget could not have been given without the permission of the mayor (Meeting at the Citizens' Information Center, December 7, 2004). When I explained how the mayor approved of citizens getting copies of the budget, the responsible person retracted his position but mentioned that "in any case they did not have the budget" and that I should consult the mayor's office (Meeting at the Citizens' Information Center, December 7, 2004).

This anecdotal evidence on the possibility of budget monitoring in the municipality of Štip gave a rather bleak picture of the situation regarding citizens' involvement in the areas of local government that are of direct public interest. Interviews with stakeholders from the NGO sector in Štip and a brief analysis of the scope of their activities and mission statements confirmed that the NGO sector is engaged minimally in the supervision of the work of the local government (Interviews with Chefutov, Donski, and Longurova).[5] Neither is budget monitoring on the agenda of any NGO in Štip. On the other hand, although transparent at the first instance, the local government is hardly helpful as far as the possibilities for monitoring of the execution of the local budget are concerned. This is of a special worry when taking into consideration the upcoming reforms and the transfer of competencies and financial autonomy to the local governments throughout the country. Larger prerogatives of the municipality authorities will require an even greater need for supervision of the work of the local government and monitoring of the budget.

What looked like a manageable problem concerning the possibilities for budget monitoring in the municipality of Štip was nothing compared to the experience in the Gostivar municipality. In Gostivar, like in Štip, very few stakeholders from the civil sector take interest in the quality of work of the local authorities (Interviews with Ademi, Fetahi, and Mitro). However, if this appeared similar to Štip, the approach of the local authorities to the issue of budget monitoring was rather different in Gostivar. Namely, at the interview with the mayor of Gostivar we encountered a closeness regarding data from the budget, even hostility. The mayor, Mr. Xhemail Rexhepi, refused to give us

the budget claiming that we have no right to such information (Interview, September 23, 2004).

With such an attitude from the highest official of the municipality, it is difficult to imagine that local civil society in Gostivar would have any chance to monitor the budget. It is also problematic to understand how data from the budget can be withheld from the public by a mayor who has fully embraced international projects aimed at improving relations with the citizens of Gostivar. The opening of the UNDP-funded Gostivar Citizens' Information Center (or Municipality Information Technology Center), the help of the USAID/Local Government Reform Project in publishing the Annual Report of Activities for the Municipality of Gostivar, and a number of other similar projects were implemented in this local government unit. Even more surprising is the fact that within the Annual Report the municipality has published a detailed budget sheet for the year 2002, with a detailed commentary on the revenues gathered and the realized expenditures.[6]

In the Annual Report, there is a note in the comments on the realized expenditures that the municipality has inherited a large debt that has been growing continuously as a result of high interest rates. Surely the reason why the mayor was so sensitive about the idea of budget monitoring was related to this issue. According to the Macedonian media daily *Utrinski Vesnik,* Gostivar was one of the few municipalities in the country that ran a huge public debt. This newspaper reported that, according to a study done by the Ministry of Finance and the World Bank, the municipality of Gostivar has a debt of MKD 135 million (about EUR 2.2 million) and is third in the list of indebted local government units in Macedonia after the municipalities of Ohrid and Struga (*Utrinski Vesnik* 2005). The biggest single debt of the Gostivar municipality is to the construction company Granit. Moreover, according to one newspaper report, the mayor of the Gostivar municipality has "opened a personal account which was used for the official business of the local government unit" (*Utrinski Vesnik* 2005). Bearing in mind such reports, it would not be surprising that the mayor of this municipality was not ready to discuss budget monitoring with any interested party. The indebtedness of the Macedonian municipalities such as Gostivar and the existence of illegal subnational governments' accounts only underscore the importance of citizens' budget monitoring.

The new mayor of Gostivar, Mr. Nevzat Bejta, is a more transparent and law-abiding head of the municipality. In an interview with the author he explained that the problems of the municipality stem from the illegal practices of the previous administration and that he has successfully negotiated the debt to Granit (Interview with Nevzat Bejta, October 5, 2005). The account of the municipality has been reopened and we could immediately receive a copy of the municipality budget. While the mayor was cooperative and transparent, only a few days earlier the staff in the municipality responsible for budgeting was not. I was confronted with open disapproval when asking for a copy of the budget, comments being made such as, "When you go to the Ministry of Defense

you do not ask for secret files," and, "You make a written request, we will discuss it, and maybe we will approve giving you a copy." Considering the evidence, publicly approved and legally allowed, the possibility for a subnational budget watch program is a priority for a democratic and transparent Macedonia.

4. EVALUATING POLICY OPTIONS AND IMPROVING SUBNATIONAL BUDGET MONITORING

A partnership between the citizens and the government depends upon citizens having access to the information that impacts their lives. In our case, citizens should be included in the local budgeting process and in its supervision. They should be aware of what the budget is and have the opportunity to influence its preparation and monitor its execution. Generally speaking, budgets are instruments for mobilization, allocation, and utilization of resources. The budget represents the fundamental vehicle for articulating and delivering government policy. Typically, where budgets are not reliably implemented, policy inconsistencies will follow. One may distinguish between monitoring and budget monitoring to understand its potentially sensitive nature. *Monitoring* is a continuous process of collecting and analyzing data to compare how well a project, program, or policy is being implemented against expected results. On the other hand, *budget monitoring* is the activity of investigating the rhetoric of public officials, matching it with the budget lines, understanding what the funds are spent on, and examining the role of audit chambers.

Budget monitoring is necessary to ensure that the communities understand their rights, obligations, and entitlements. This is intended to build the confidence of the community; to encourage them to participate actively in performance monitoring using skills, information, and knowledge about budgetary processes; and to contribute to better governance at the local level. Moreover, it helps the public entities achieve their goals by applying a planned, strictly defined approach to assess and improve the performance in the processes of risk management, control, and management. Good governance dictates that government operations and decisions should be made openly, and with the active participation of those people influenced by them. Transparent systems that provide for budget monitoring have several advantages. Since the budget is the primary economic policy document of the government, its monitoring by the public is particularly important.

Indeed, it can be argued that the public has the basic right to information about the budget and to have its views considered in budget decisions. Some of the benefits of budget monitoring include: identification of the weaknesses and strengths of governmental policies, thereby promoting needed reforms; accountable government—elected office holders and public servants may be more likely to act in a responsible manner

if their decisions are open to public scrutiny; a safeguard against corruption by public officials; increased trust in governments and social cohesion—if the public can better understand what their governments are doing and why, they may have more confidence in government and be prepared to accept and trust difficult compromises; and so on (cf. Ott and Bajo 2001; International Budget Project of the Center on Budget and Policy Priorities).

Moreover, by having a clear understanding of the government's policies and actions, international and local investors are likely to be more willing to invest resources. The powers of local self-government bodies originate from local people and communities. Local self-government bodies use their powers on behalf of and for the benefit of the community residents who have the right to assess the effectiveness and efficiency of self-governments, and their ability and willingness to protect the interests of the community. Participation in the budgeting process is an opportunity for citizens to learn more about their municipality, and its financial and other limitations. Experiences show that when citizens are aware of municipal limitations regarding its competencies and finances, they more readily accept that the municipality cannot solve all their problems (Hadzhi-Vasileva 2004: 11). While budget monitoring helps build up a consensus on policy and allocation decisions, this consensus will be deepened if civil society is allowed significant inputs into the debate. Transparency and participation are mutually reinforcing and both are needed for better budgetary outcomes. In fact, the involvement of civil society actors can improve policy and budget allocation decisions by bringing different perspectives and creativity to the budget debates.

Considering the above, the following review of the policy problems and evaluation of policy options can be made. Macedonian budgetary process remains largely unaffected by input from civil society. The budget preparation is not discussed outside government or submitted to prior external review by NGOs or academics. But budget execution is not being monitored by the civil sector either. Although lawmakers have envisioned a number of mechanisms for internal and external control over the financial work of local government units, there is no explicit legal provision that involves experts or the NGO sector in the budget monitoring on a subnational level. The problem with the finance system as a whole is that it provides no mechanism for the citizens of individual municipalities to express their willingness to actively participate in the budgetary process. On the other hand, the relevant laws do not preclude such an activity either. The lack of citizens' budget monitoring on a subnational level can lead to financial irregularities that burden the normal work of local government units. For various reasons, including bad management, carelessness in the financial work of the municipalities, political influence, and so on, many of the existing Macedonian municipalities have huge public debts. Although tolerated by the central government, accumulating such debt is not legal.

On the one hand, the central authorities have become aware of the fact that something needs to be done about the proper execution of the budgets by local government units. The Ministry of Finance has issued a tender for providing consulting services for training personnel in the local government units responsible for managing, budgeting, and administrating municipal finances (*Dnevnik* 2005). By law, it is also stipulated that internal audit units will be established in the offices of the local authorities throughout Macedonia. Therefore, the budget management of the municipalities is an important issue for the government.

However, for successful and transparent management of the local budgets, besides the state, the citizens need to become directly involved in the process of supervision of the budgetary process. It is not enough that the Law on Local Self-government defines "direct citizen participation" as the individual or collective involvement of the inhabitants of a municipality at different levels of the decision-making process of local government. It does not suffice that Article 30 of the new law states that the local government should solicit public input on municipal issues and also should involve the public in policymaking and the budgeting process. There is still a culture of passivity in Macedonia, as far as citizen involvement at the local level is concerned. A survey by Transparency International revealed that over 40 percent of the Macedonians did not know that they have a constitutional right to access to public information (A1 television interview with Zoran Jachev, October 17, 2004). Citizens are "reticent to react against the lack, insufficient, or low quality of public services, the abuse of constitutional rights and a low participation in developing and defining public policies" (Hadzhi-Vasileva 2004: 7).

Such attitudes and such passivity on the part of the citizens is highly related to the culture of public officials in the country. In a few cases, municipalities, in cooperation with the international community, have encouraged citizens to get involved in policymaking and legislation development, but many Macedonians perceive government officials as powerful, "untouchable" cliques. On the other hand, the prevailing political culture in the country is such that the decisions of the government and the policymaking process are typically done behind closed doors, without the input and consultation of a wider network of stakeholders such as citizens, civil society groups, or academic experts. A somewhat typical example was the government's decision-making process over the new territorial organization of the municipalities in Macedonia, a highly secretive and reticent affair (Daskalovski 2004b). Moreover, information is not readily given to citizens, even if they explicitly ask for it. A survey by the Macedonian chapter of Transparency International showed that 70 percent of those citizens that asked for information from state institutions have had difficulties obtaining it, and that 27 percent of them did not receive any answers from the state organs, while 33 percent were refused access to the needed information with no explanation (A1 television interview with Zoran Jachev, October 17, 2004).

Moreover, as the debate over the new Law on Territorial Division of the country showed, citizens in Macedonia remain passive concerning public life and policymaking until their direct interests are threatened. This situation has to be changed if the country is to have solid local governance and budget management. The citizens need to have a clear idea that public officials are paid by public tax money to provide requested services. The Macedonian experience in budget processing in local government units shows that the only viable policy alternative would be to engage the local population and the civil sector more directly.

5. CONCLUSION: LESSONS LEARNED FROM THE MUNICIPALITIES OF GOSTIVAR AND ŠTIP

This chapter argues in favor of an active policy for a more direct engagement of the local population and the civil sector in local governance. The goal of this policy is to have local authorities improve transparency and public involvement in the budgetary process. Thus the following recommendations aim at concrete measures for the enhancement of budgetary monitoring on the municipal level. Local governance and the budget process have been largely unchecked endeavors in Macedonian political life. Citizens are passive and the political culture discourages the direct involvement of concerned citizens in the budgetary processes. Therefore, it is vital to adopt measures to increase public information and citizen participation in the key areas of local finances and local public services. One should keep in mind that clarity in the roles and the responsibilities in the management of public finances is essential to citizens' capacity to hold government accountable for budget policy and decisions.

Recommendation 1:
Public availability of budget monitoring

A fundamental requirement of fiscal transparency is that comprehensive, reliable, and useful budget information is made available. Civil society must have the opportunity to influence budget formation and assess whether government undertook what it planned. Civil associations or nongovernmental organizations should have the opportunity to undertake monitoring of the budget's execution on the subnational level. The Law on Financing the Local Government Units should include clear provisions guaranteeing continuous and permanent access by citizens to local financial information. It should provide for clear obligations on the part of local government units to disseminate information about the budget's execution among the public, to keep a file of the budget accessible to the public in the local government unit, and to organize quarterly open

sessions for public overview of the budget's execution in the municipality. The income and the expense statements and the balance sheet should be published and made accessible to interested citizens.

Although the municipality of Gostivar has published its 2002 budget (and programs), there is no specific provision in any law that states clearly that such documents must be published and that the public must have access to this information. The assumption is that only a few of the existing municipalities have such a practice and this needs to change. Therefore, the law should stipulate that, on the part of the local authorities, there is a proactive approach to transparency, with information made available in reports and on websites. The law should provide for sufficient human resources being allocated to process information requests by interested parties in budget monitoring, that local government staff is trained to deal courteously with the public, and that there are trained officials who oversee information requests and ensure they are answered.

Recommendation 2:
Influencing the budget formation process

A key issue is whether the legislature and civil society are able to participate effectively in the budget process. Effective participation refers to the opportunities for the legislature and civil society to make their viewpoints known and to have these views taken seriously. Therefore, the law should require that the units of local self-government hold public hearings before adopting key decisions, such as the annual budget or changes in the fees for local public services. There should be ample advance notice accompanied by publication or public access to relevant documents. In fact, the possibility of public hearings was included in the draft version of the Law on Financing Local Government Units.[7] The Law was discussed at a government session on December 10, 2003, and the draft text was changed not to include the obligation for the local governments to hold public hearings for the budget. Since this was already discussed, an amendment to the law including the obligation on public hearings should not be a significant change of the legal system.

Recommendation 3:
General provisions helping budgetary oversight on the subnational level: Access to Information Law

At the moment Macedonia lacks an access to information law. Many of the problems with transparency in governance, including budget monitoring, would be solved if a freedom of information law would be adopted. The Macedonian chapter of Transparency

International, together with other local NGOs, has initiated an access to information law that is expected to be adopted by the Assembly by the end of 2005. The draft version of the law stipulates that citizens will have a right to obtain information on "the services public officials provide and the organization, the competencies and the costs of working" (Center for Research of Economic Policies 2005: 2). This implies that the financial management and the budgeting process of subnational governments will, by a specific law, become open to public scrutiny. Such a law will not only help curb corruption in Macedonia but also make budgetary monitoring of the local government units much easier as it will directly empower ordinary citizens dealing with institutions that now seem distant and all too powerful.

6. APPENDICES

6.1 Participation

At the moment Macedonian citizens hardly participate in the budgetary process on the subnational level. As examples from Štip and Gostivar show, this issue is not on the agenda of citizens groups and nongovernmental organizations. Within the legal framework, there is no mention of the possibilities for citizens' involvement in the budgetary process. Decentralization and the transfer of competencies to the local authorities do not directly provide legal tools for the involvement of citizens in the budgetary process. Budget monitoring is determined to be the obligation of the Ministry of Finance and the State Audit Office, with future internal audit units within the local government units taking over some of the responsibilities. However, the legislation does not preclude local governments' budget monitoring by concerned citizens either. On the contrary, a number of legal provisions from the Law on Local Self-government can be seen as encouraging such actions. According to the Constitution and the Law on Local Self-government, the units of local self-government have the right to local self-governance through direct participation of citizens in decisions about common matters. Moreover, Article 115, Paragraph 1 of this law stipulates that "citizens directly and through representatives *participate in decision-making* on issues of local relevance particularly in the field of public services, urban and rural planning, environmental protection, local economic development, local finances, communal activities, culture, sport, social security and child care, education, primary health care and other fields determined by law" (emphasis added). These legal provisions, although they do not directly provide for the possibility for budget supervision on a local level, ensure the legal background for such activity. At the moment there are no institutional arrangements for citizens' participation.

6.2 Information

The study reveals that data are available on *ad hoc* basis depending on the managerial vision of the local government of the municipalities. Considering the examples from Štip and Gostivar, and consulting the study of municipal debt, the data can be judged to be unreliable. Data on the budgets of local government units is not produced in a timely fashion. It is not possible to compare actual versus planned figures of the local government units at the moment.

6.3 Accountability

Until the reform of this year, budgets on the subnational level were drafted without much concern for accountability. As the country was overcentralized, the local government units were left to deal with important development issues for the municipalities without recourse to sufficient funding. Many municipalities ran into debts and had to find extralegal means to manage their work. As a result, the transparency of budget preparation and execution and accountability were not issues of concern to the local governments while the central authorities tolerated the state of affairs, aware that citizens require their basic needs to be fulfilled on the local level.

ENDNOTES

1 On the conflict and the Ohrid Agreement which ended the violence between Albanian rebels and Macedonian security forces by introducing legislative reforms improving the status of Macedonian Albanians, see Daskalovski (2004).

2 More precisely, three percent of the personal income tax on the salaries of employed people, collected in the municipality in which they are registered as having the permanent place of residence, and 100 percent of the personal income tax from individuals dealing with craftsmanship, registered on the territory of the municipality in which they are registered to perform activity.

3 EUR 1 is worth MKD 61.

4 A total of nine interviews with stakeholders within the municipality of Štip including the mayor, Mr. Dimitar Efremov, were held in the period October 2004–January 2005.

5 A list of Štip NGOs is available at http://www.ngocenters.org.mk/nvo.asp?lang=mak&grad=2. An extended list of the Štip NGOs with contact addresses and telephone numbers is on file with the author.

6 The report is on file with the author.

7 See Local Government Reform Project, Quarterly Report, 2003, Q4, by Democratic Alternatives Inc., pp. 11–13.

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Budgetary Oversight and Accountability in Ukraine: The Case of General Secondary Education

Sergii Slukhai

This paper deals with issues of budgetary oversight and accountability in the field of secondary education. Based on the case of Ukraine, the paper analyzes the state of general budgetary oversight on the local level and goes into detail concerning fiscal accountability of educational units. It is argued that the most striking feature of Ukrainian budgetary oversight on the local level is the dominant role of the state bodies involved and a very minor role attributed to the customers of educational services. In order to change this unjustified bias, a series of policies is proposed, aimed at decentralization of the educational sector, its institutionalization, and raising the level of self-governance of the school units.

1. INTRODUCTION

Education plays a growing role in the modern post-industrial society in Ukraine. It is one of the most important inputs that predetermines not only the current state of affairs in the economy, but is decisive for the country's prospect in the global economic environment and its democratic development. Because of the specific nature of education (in general, a private good that creates a huge flow of positive externalities) policy cannot be left to market forces alone because the latter cannot guarantee a sufficient level of education in society.

Secondary education is a significant cornerstone of the educational system in Ukraine.[1] As a public responsibility, it is more or less decentralized, creating one of the most extensive local government tasks. The latter fact is due to both economic and political reasons: decentralization in this field makes service provision more efficient and gives the local community more power in decision-making regarding issues of local concern to which secondary education belongs.

Thus, local authorities providing secondary education are fulfilling a very important social task. Because of this they have to be the subject of public oversight and accountable to their communities about how they use scarce public money to satisfy the public's need.

Making government accountable to the people is one of the most challenging issues in post-socialist countries. The traditions of centralism, under which all the issues of public importance should be resolved only on the national level, have gone. The most important values of local self-government like democracy (participation), autonomy (being more or less independent from the central state), and effectiveness (closest match between public good supply and demand) are spreading over the Central and East European countries or CEECs (Swianiewicz 2001). But in the post-Soviet world many obsolete traditions of the command economy in the public sector are still present. This is also true for Ukraine. These traditions persist in such an important sector of public service delivery as secondary education.

The issue of public involvement into the budgetary process has its own peculiarities in each sphere of public good provision. One of the most critical and controversial issues emerges in secondary education, which is in its essential features a local responsibility in Ukraine. Like in many other post-socialist countries,[2] Ukraine still suffers from overpowering governmental regulations of educational finance, which creates many economic distortions and interregional inequalities that require treatment (IRF/UNDP Ukraine 2001, Levitas and Gerczinski 2001, ISTC 2004b). Community involvement in forming educational budgets is very low. It is partly so because in many locations the community spirit is still weak and partly because of the extensive and direct involvement of the state in educational policy on the local level. Some compromise should be found between the demand for state supervision over mandated public spending on education, on the one hand, and possibilities of public service consumers to influence the level and quality of educational service rendering, on the other.

This paper aims to outline the effective policy concerning enhancing local accountability with special regard to secondary education. To accomplish this goal, the following objectives are stated: (i) to identify public needs for accountability in the local budgeting process; (ii) to compile an inventory of current critical issues in public policy concerning oversight over local finance in Ukraine, specifically emphasizing general secondary education; (iii) to develop public policy options intended for enhancing local budgetary accountability in the education branch.

The findings of this paper could be summarized in the following way: the public's inclusion in the oversight of educational expenditures is low in Ukraine despite the great importance of educational services for community life; the state's budgetary oversight is biased to control the legality of money usage rather than efficiency; the core mechanism of securing a higher level of public involvement could be the decentralization of educational administration accompanied by the higher level of school self-government

and responsibility of unit managers. These findings are supported by relevant studies of other researchers and proved by success stories from countries currently engaged in education decentralization (Cohen and Slukhai 2004, ISTC 2004a, Levitas and Gerczinski 2001, Lukovenko 2004).

2. CURRENT STATE AND CORE PROBLEMS OF BUDGETARY OVERSIGHT AND ACCOUNTABILITY

As school budgets are an integral part of local budgets, they are, as any other budgetary activity, the subject of budgetary control. In general, the authority for budget supervision in Ukraine is given to the central government, which has a broad range of controlling bodies at its disposal.

2.1 Budget Supervision: General Background

According to the Constitution of Ukraine, the central government bears most of the responsibility for the delivery of public services including secondary education. The majority of local authorities are still far from taking over the role of self-reliant public service providers that could meet the local voters' preferences. The most influential bodies on the local level are local state administrations responsible for the delivery of many basic public services, leaving some miscellaneous ones in the domain of locally elected bodies. As a matter of fact, weak popular demands for independent local authorities and the long-lasting traditions of a centralized state have created a very weak demand for shifting more power from the top to the bottom. Despite a piece of real power, the municipal bodies of big cities recently might have gained in the course of ongoing reforms, even in these rare cases the local authorities have not become really accountable and fiscally independent.

Since the adoption of the Budget Code in 2001, new possibilities for fostering local accountability have arisen. But there is still a long way to go before some innovations are implemented in real life and before the reform brings results: raising the efficiency of local governance and involving people in decision-making at the local level. Local governments that have gained more power need to be monitored in order to test the compliance of their policies with national ones.

As independent scholars have reported, transparency has been greatly improved on the national level since independence (Sundakov 2001), but the situation with the execution of local budgets seems to be much more problematic (IER 2003). However, empirical evidence suggests that on the local level some problems associated with transparency and public involvement in budgetary decision-making really exist. The current

composition of the local government system, characterized by the concentration of most operations of budgetary units subordinated to local governments in the central government local bureaus, moves public funding in many ways outside the influence of people who are the most interested in their operation. The main concern of the local populace is to gain more influence on public-spending decision-making and to make local governments accountable not only to the central government, but also (if not mostly) to local voters.

This is especially true for the educational budgets that comprise the dominant part of the budgets of self-governing territorial units.

2.2 Control over Local Budgetary Activity

The budget process at the local level consists of the following main stages: drafting, hearing, approval, execution, monitoring, and reporting. Formally, each stage could involve local inhabitants with budget issues. However, the real possibilities of influencing the budget process from the people's side are quite limited.

The problem here lies in the factual formation of local budgets that gives no space for public involvement. According to Article 75 of the Budget Code, local budgets are formed from top to bottom; in their main features they are replicas of the Soviet-type budgeting process. First, the local authorities should submit information concerning their fiscal capacity and fiscal needs; then the main budget money disposers should prepare the budget requests that are then submitted to the local fiscal authorities (local departments of the Ministry of Finance), which then decide upon including what requests into the budget draft of the *oblasts* (regions) or districts. The local governments of villages, settlements, and small cities have to submit the budget drafts to their respective fiscal authorities. After the state budget draft has been approved by the Cabinet of Ministers, the Ministry of Finance delivers the calculation of the main fiscal measures for drafting of their budgets to *oblast*, district, and large city authorities. Once the annual budget law has been adopted, the local authorities receive detailed information on the main parameters of their budgets; only then do the *oblast* and district authorities compose the drafts of the budgets of the local self-governments. So, we cannot speak about significant independence within the local budgeting process. The problem is aggravated by the real level of local budgetary discretion.

According to the common understanding shared by Ukrainian scholars of the public sector, the proclaimed independence of the local government budgets does not work for two main reasons: (i) a very high portion of exogenous factors determine local expenditure decisions—95 percent of local government expenditure competence belongs to the delegated powers, whose level of funding is determined by the state (Lunina 2002);

(ii) low revenue independence—the local taxes and duties comprise a very low portion of local budget revenues (around two percent in aggregated terms, see Table A1 in the Annex). Thus, explicitly, there is no reason for local officials to discuss expenditure programs of local budgets with the public because they are predetermined by the state in their chief components, both on the revenue and expenditure side.

All in all, the state bodies are mostly interested in controlling local spending decisions because local governments are assumed to perform state functions on the local level.

According to legislation, the bodies of the upper governmental level execute the obligation to oversee the execution of the subordinated governmental local budgets. The following bodies could execute external control over local government budget activities: the Accounting Office, the Ministry of Finance, the State Treasury, and the State Control and Revision Service. Their authorities in executing budgetary control are itemized in the Table A2 in the Annex.

The above-mentioned authorities, especially local State Treasury departments and the State Control and Revision Service have a broadly defined authority to directly influence the local usage of public money. Since all the accounts of local governments and budgetary units could be held exclusively in State Treasury departments, the latter ones do not only monitor the revenue side of local budgets, but also give permits to use the money even in case when they are not dedicated to the execution of delegated state functions. The funding of local expenditure programs should be done exclusively in compliance with the approved budget by a respective representative council that formally guarantees the targeted usage of money.

The misuse of public moneys could be considered to be a budget offence. As the Budget Code provides, this is the case when someone does not obey rules provided by Budget Code and other legal acts concerning composing, reading, approval, amendment, execution, and reporting of the budget. In case an offence does take place, there are reasons for the budget process participants—like the Ministry of Finance, the State Treasury, the State Control and Revision Service, local fiscal departments, heads of local authorities or key spending units—to stop budgetary appropriations for any local government. The reasons could be akin to: untimely reporting; not obeying the rules in accounting, reporting, or internal auditing; breaking the order of payments; delivering false information on budget execution; breaking the rules concerning executing budgetary obligations; and inappropriate use of budgetary costs (i.e., not in compliance with the tasks). The penalties for budget offences could range from administrative penalties for the guilty administrators and suspension of budgetary appropriations, up to criminal proceedings against the local officials involved.

The internal fiscal control of the local bodies should be performed at each stage of the budgetary process. Its main function is to secure a permanent estimate of sufficiency and compliance of budgetary institution activity to legal requirements; evaluation of relation between results, tasks, and plans; and informing the manager of a budgetary institution about results of an internal audit.

The local legislatures (*radas*) audit the execution of budgets approved by them, and the legitimacy of the usage of reserve funds. They also control compliance of the budgets, budget allocations, and cost estimates of subordinated territorial units with budget legislation.

The public participation in budgetary oversight could be estimated as quite weak. However, there exists a more or less satisfactory legislative basis for granting public influence over local spending decisions.

As one recent study of public finance transparency in Ukraine stated, the following problems illustrate the above statement:

- There is no public access to information concerning budget hearings (the budget drafts are usually neither published nor posted on the Internet);
- No disaggregated information concerning the execution of local government budgets is published;
- There is no detailed information on current budget execution delivered to the public (it is at an official's discretion to deliver some information on budget execution or not);
- No information concerning debt obligations is open (the local authorities disclose this information only to the Ministry of Finance and State Treasury);
- No information on municipal property and assets, their usage, market value, and performance of communal enterprises is available (IER 2003).

This makes us conclude the following: there is a severe problem with accountability of the state in general and of local government in particular. The current state of affairs is inherited from the Soviet past, when the citizenry was excluded from active participation in public issues, taking for granted the fact that all the issues will be dealt with correctly by the officials appointed (as a matter of fact) by the Communist Party based on ideological motives. Now, neither the public is ready to actively participate in local decision-making, nor local officials ready to allow the public to be present at each stage of the budget process (Zaharchenko 2002).

After the revolutionary events in 2004, Ukraine revealed its democratic potential. After this turning point, the issue of accountability at the local level cannot stay as before. Public participation will inevitably increase in all fields of social life.

2.3 What to Control: Educational Tasks of the Local Governments and Their Funding

As stated above, education is one of the most important responsibilities of local governments, which is delegated to them by the state. The data in Table 1 measures the local government share in educational expenditures that is as high as two-thirds of total

public expenditures on this function. According to the data presented, education looks like a shared function; the specific tasks of the local government of different level and the funding associated with those tasks are presented in Box 1.

Table 1.
Subnational expenditures by function within a sector of public administration [%]

	Year	Total	Central government	Total subnational government	*Oblast*	*Rayon*	Cities of *oblast* significance	Cities of *rayon* significance	Settlements	Villages
Total expenditures	1992	100	62.2	37.8	11.5	7.7	15.5	0.7	0.7	1.7
	2002	100	58.9	41.1	11.1	11.7	15.4	0.6	0.7	1.7
Education	1992	100	33.9	66.1	6.6	17.0	28.1	3.0	3.1	8.3
	2002	100	40.7	59.3	7.9	23.8	22.5	1.5	1.4	2.2

Source: Author's calculation based on MoF data.

The breakdown of educational expenditures shows that the expenditures on secondary education are the most important type of educational expenditures that local governments bear. As Table 2 demonstrates, they have nominally more than doubled within the last four years (with an inflation rate of about 35 percent during this time period, it implies a real growth in this expenditure category), and currently they comprise more than 60 percent of the educational budget of the aggregated local government sector.

General secondary education in Ukraine is a state function, the implementation of which is delegated to the local authorities. On the district level, the local state administration bears the responsibility for general school administration; in its structure it has local educational authorities to which all the schools are subordinated; in large cities of national and *oblast* significance, the task of secondary education delivery is performed by the educational authorities of self-government bodies (city councils). Although the Ministry of Education and Science (further referred to as the Ministry of Education) is at the top of the administrative hierarchy in school education, it has no direct influence on school funding, where the Ministry of Finance has the upper hand. The Ministry of Education deals mainly with content of education; all the fiscal issues, even the calculation of local expenditures on education, belong to the domain of the Ministry of Finance and its local departments. Concerning budgeting issues, the Ministry of Education does not play any significant role, unlike in Poland which, as a neighboring

country, serves in many cases as a relevant example for Ukraine.[3] Also significantly, it collects no information of school fiscal well-being, relying in this matter on local state administration fiscal departments.

Table 2.
Composition of local educational expenditures in Ukraine

Type of expenditures	1999		2003	
	[UAH million]	[%]	[UAH million]	[%]
Education total	3,471	100.0	8,985	100.0
Preschool education	567	16.3	1,636	18.2
General secondary education	2,156	62.1	5,457	60.7
Educational institutions for those who need social care and rehabilitation	321	9.2	815	9.1
Extracurricular education	113	3.3	300	3.3
Vocational schools	19	0.5	36	0.4
Higher education	106	3.1	262	2.9
Post-diploma training	23	0.7	60	0.7

Source: MoF 2002, 2004.

Small cities and rural settlements run preschool education and elementary schools (schools, kindergartens); they are also responsible for funding these institutions. In some districts secondary schools are also funded by local urban and rural communities, and despite the Budget Code provisions, there is no uniformity in practice. In rural areas, the district educational authorities bear responsibility for secondary education services. The detailed information on assignment of expenditures on education is shown in Box 1. Here, it is obvious that the educational expenditure assignment is supposed to benefit areas of each type of service in order to minimize spillovers. In order to make fiscal flows more transparent, funding educational establishments from the budgets of different levels is prohibited; so only one channel of funding is available for a separate school unit.

The funding of secondary education is performed by district governments (or by the city government in case of a big city) from the bunch of national state revenues ceded to them. Standardized expenditures on secondary education are also subjected to fiscal equalization, included in the equalization formula since fiscal year 2001 (CMU 2000, items 40–46).

Box 1.
Local government responsibilities for carrying out the educational expenditures, according to the Budget Code

Regional (oblast) level: specialized secondary education for disadvantaged students; secondary boarding schools; vocational and higher education establishments.

Cities of district significance and rural districts: general secondary education.

Towns, villages, and settlements: preschool education.

Cities of Kyiv and Sevastopol undertake all of the expenditure responsibilities that have been assigned to *oblasts*, cities and districts, towns, villages and settlements with regard to the special status of these territorial-administrative units.

Notes: All these educational expenditures will be included while calculating the sums of intergovernmental cash transfers.
Own expenditures of local governments (to be excluded while calculating intergovernmental cash transfers) extend over extracurricular education.

The planning of school funding occurs in conformity with educational norms (academic programs for each grade) set by the Ministry of Education and budgetary norms fixed by the national Cabinet of Ministers for each year. School headmasters comprise a cost estimate for the running of their schools for the budget year based on current funding norms; district authorities review the estimate, and after approval it becomes a part of the district budget. In fact, official school budgets consist mainly of two secured items—staff salaries and heating expenditures (about 90 percent of the total). The other expenditures are usually discretional ones—the district educational authority distributes them among school units according to *ad hoc* arrangements.

The budgets of schools, granted to them by district authorities, are very tight and compel school managers to seek extra-budgetary funding; but the most important part of extra-budgetary sources comes through informal arrangements, like parental cash payments and in-kind contributions which, according to some studies, could comprise up to 15 percent of an effective school's budget (ISTC 2004b).

In general, the level of school autonomy in Ukraine is strictly limited: most schools have no accountants (even utility bills are paid by district authorities), and thus have no special interest in attracting off-budget funding in an official way according to the list approved by the government (CMU 1997).

As budgetary units, school establishments are the subjects of budgetary control and supervision. The school outlays, being a part of district budget, are strictly controlled by the fiscal authorities on the district level and by the State Control and Revision Service.

The local fiscal authorities endorse only the outlays that are recorded in the school cost estimate for the running year. Even if a school master managed to get additional private support to cover some urgent outlays, he cannot deliberately adjust the school estimate, in case this money and expenses are not planned for this year. Changing a school cost estimate could be possible only after making adjustments in the district budget and will take a lot of time because only a session of the district council has the authority to adopt any changes in its budget.

Being a part of district budget, school budgets are subjected to general fiscal control according to the criteria indicated above. The regulation of revisions in educational establishments emphasizes the following subjects of special treatment:

- cost of additional educational services, revenues from property lease;
- cost calculation on production of goods and services, calculation of revenues from commercial activities of educational establishments;
- recording, accounting, and usage of humanitarian aid;
- accounting of parental payments;
- targeted usage of money for children's health improvement;
- targeted usage of money for school computerization;
- usage of money for children's nourishment (SCRS 2004).

From this list it has become obvious that the State Control and Revision Service is strongly motivated to monitor the legality of money usage by schools. But it is out of its responsibility to check whether public funding is spent in the most efficient way. This formal approach is also characteristic for other state agencies involved in budget supervision.

Summarizing the above, one could state that local governments have a very small opportunity and a low capacity to do something in order to meet local demand. Local governments' responsibilities in secondary education are very high in terms of obligations, and very low in terms of rights. Article 11 of the Law on Education defends the monopoly of the Ministry of Education in decision-making and policy-making, but at the same time vests a great part of responsibilities onto local governments. Municipalities fulfill delegated responsibilities of the central government and maintain school infrastructure, while the Ministry of Education determines academic load, teaching material, salaries, and hires and fires administrative staff (see detailed information in Table A3). School entities are seriously limited in their right to use public money and have no possibility to be flexible and responsive to changes in local demands for educational services because they even cannot change the funds allotment between cost estimate articles (it requires some changes in the *rayon* budget and cannot be done easily or quickly).

2.4 Who is who in school education funding?

From the point of view of economic efficiency, the intensity of public concern in using money on public services is determined by the allocation of benefits and costs between stakeholders. The best result in using public money will be observed in a situation when the beneficiaries are the same persons as the cost-bearers. The more differences are observed between beneficiaries and payers, the farther service delivery will be from an efficient amount.

The main participants on the supply side of educational service are the state (which is obliged to guarantee the access to secondary education for each citizen); the state educational authorities (mainly state administrations of the district level); and the schools (primarily service providers). The state authorities are interested in receiving a due amount of money to fund public services on the territory of their jurisdiction. But there may be several obstacles that make the budgeting process ineffective.

At the moment, on the national level the trade-off between educational expenditures and other types of expenditures like social benefits does not favor school education. Real school expenditures have significantly decreased during the last decade; the portion of educational expenditures in GDP—5.7 percent (MoF 2004)—is below the level necessary for remaining a well-educated nation, because educational expenditures are dedicated to (almost exclusively) salary payments. It looks like education does not yet belong to the top priorities of the state.

The state distributes educational money in the following way. The normative per student educational expenditures are included in the calculation of normative expenditures of local government and are taken into account while calculating equalization transfers. On the district and city level, the bunch of ceded state revenues dedicated to funding delegated functions is then allocated between these functions. There exists some minimum of educational expenditures determined by the so-called "secured budget items" that should be funded in any case: teacher salaries and school heating expenditures belong to these.

According to information gained from our previous field research (AUF 2003), in general, the total amount of delegated function or earmarked funding is not sufficient for maintaining an appropriate public service level. This is especially the case on the district level, where the total budget money is apportioned among separate needs. The evidence from mayors of small cities that are subordinated to the district authorities shows that the latter ones are not eager to allocate public money in favor of education; school education belongs to underfinanced branches of delegated functions at this governmental level. As we can see from the Table A4, which contains the estimates on actual funding rates as compared to fiscal need, on average, the percentage of actual secondary education funding extends only 68 percent in a sample of the cities surveyed.

The lobbying power of local educational departments of state administration and teachers' community is not strong enough to defend the interests of the educational branch on the district level. That is why we can have widely varying amounts of actual per student expenditures throughout the country.

State educational authorities, upon receiving the educational budget adopted by the district council, adjust the schools' cost estimates submitted for the preparation of the district budget. They have to fund fixed items of these estimates (first of all, teacher salaries and heating costs), but the residuum of state funding (about 10 percent of the educational budget) is assigned among schools in a very non-transparent way.

We may conclude that district educational authorities joined with teacher communities and local communities in order to defend the existing level of funding without regard to cost efficiency. On the macro level, it is reflected in the following facts: during the last decade, despite declining student enrollment, the number of teachers has increased (which resulted in an improved student/teacher ratio), and the number of secondary schools has remained almost the same (IPT 2002).

The school administration is supposed to be responsible for the quality of educational services, but in the current situation concerning teaching staff and physical assets, it is almost impossible to guarantee high-quality services. For example, even some schools of the third level in Sokal district do not have PCs; none out of 70 schools have Internet access. Thus administrators' activity in terms of funding concentrates mainly on lobbying interests of the school they administer; whoever has better connections to the district authorities receives more generous funding and better equipment.

The local communities in small cities, settlements, and villages seem to have a long-term interest in school education—the graduates will work for the prosperity of the locality. But from the short-term perspective, they usually do not care too much about schools because they do not belong directly to their jurisdiction.

The business community is interested in a pool of better-educated school graduates, but as the best students tend to go to universities and leave their communities, their interest in supporting education is quite low. Only large companies can afford investing significant money into schools; in general, the activity of local businesses in school support depends on the school headmaster's image and persistence.

Parents have their interest primarily in the effective use of money allocated because they wish to have their children educated at the best level possible. This is especially true for the high school level. But, in general, they try to achieve this goal through personal efforts that mostly are not directly connected to what is going on at school.

The above observations result in a very specific point of view that school headmasters have of the main factors exerting an influence on school performance. As Table A6 demonstrates, the local community and parental participation are not the top priorities. They are not taken seriously as factors that can support school development. And the school headmasters are not to blame here—the problem is

rooted in a centralistic approach to the administrating and funding of secondary education.

The most important sphere, supported by polling results, is conducting classes and improving physical infrastructure, and the latter priorities are interests of parents and the local community and interaction with the local environment (including the business community). This reflects the common view of the school administration on external factors influencing school performance. Interestingly, of all the concerns, the most prioritized areas are the subjects of centralized funding and control. So in case of some problem, an administrator sees no sense in going public; the most efficient way for him is to appeal to district authorities.

3. BUDGETARY OVERSIGHT AND ACCOUNTABILITY IN SECONDARY EDUCATION: IS IT OF ANY VALUE?

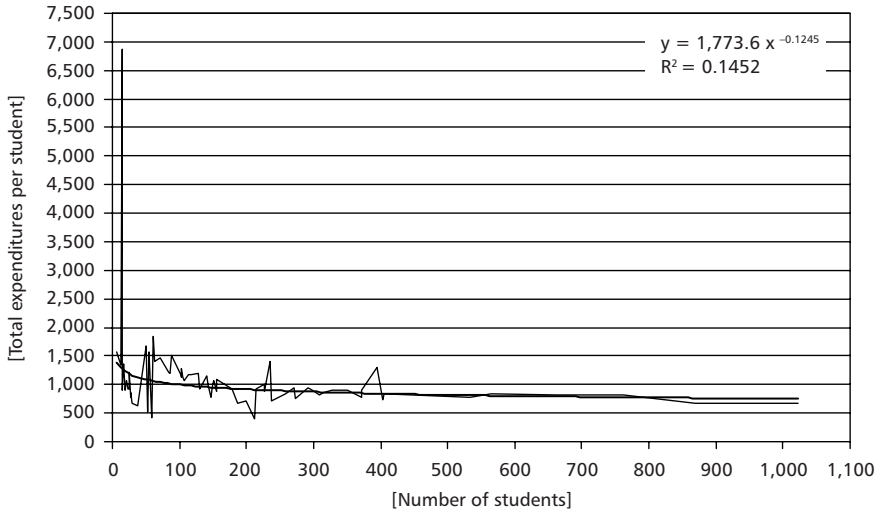
The issue of budgetary oversight in secondary education from the point of view of civic society is undeveloped. One could ask a question here: well, the public is not involved, but the state is, so maybe we do not need to change the situation?

To answer this question requires pragmatism. If public oversight makes the local government and school unit more accountable, then some benefits are gained in terms of better covering the local demand and more efficient usage of public money. Since the degree of meeting the local demand is hardly measurable, economic efficiency becomes an issue. Some useful conclusions could prove the necessity of raising the standards of accountability.

Foreign experts have found a high difference in per student expenditures in Ukraine despite the fact that educational expenditures are calculated according to a formula-based approach. These differentials cannot be attributed to any feasible factor (Levitas and Gerczinski 2001). Our own observations illustrated by Table A5 and Figure 1 below show very significant differences in per student school funding in the rural and urban areas.

From this figure it is evident that there are quite significant fluctuations of expenditures per student, especially in small schools. The problem is that the funds are distributed according to the individualized estimates of fiscal need for each school. And the fact is that cost efficiency is not taken into consideration. The educational authorities do not care too much about economic efficiency in service delivery and the state auditing bodies do the same. They are merely interested in spending money according to approved local budgets. As a result, each school receives enough money to maintain itself on a more or less sufficient level; the deviations are due to a low willingness on behalf of educational authorities to encourage efficiency and competition among educational units.

Figure 1.
Correlation between total expenditures per student and school size in Sokal district, Lviv *oblast*



Source: Cohen and Slukhai (2004).

Secondly, there is some correlation between educational costs per student and school size: the bigger a school is the lower per student expenditures are. In other words, amalgamating schools could bring significant cost economy that could be used for improving secondary education and enhancing the quality of education.

Could these issues be resolved through some political measures on the local level? The answer is positive. If some arrangements will make local authorities more publicly responsible in spending public money, if school principals are given incentives to economize the educational expenditures, then sooner or later the positive results will be evident. Being accountable, local educational authorities will try to achieve better results given the funding amount. The school network would become more coherent and efficient and the quality of education will be raised.

To understand the current situation we must see how the most motivated actors in education, parents and the local community, who should seek (from a logical point of view) a deeper insight into the budgeting of education, behave. The observation so far presumed indifference concerning budget oversight. Why?

In order to effectively perform oversight over the school budget, there should be at least two prerequisites: formal arrangements to control the school budget and a strong motivation to execute the control function.

Concerning the first point, Ukrainian legislation creates formal grounds to control the fiscal activities of the school from the public side. The school board includes representatives of parental committees, the student community, and teaching staff; the board has a right to control the fiscal activities performed by the school headmaster. But in reality, the school principal acts out of public control: a lot of his or her transactions belong to shadowy activities, and in fact he or she personally decides upon the usage of school money (of what extends over mandatory payments).

Concerning the second point, we must admit that parents have few possibilities of monitoring the school budget because they must be knowledgeable about school finance and have time to be involved in this issue. But the most important issue that prevents them from doing so is a common argument of economic theory concerning the public good. Public oversight is a public good for the parental community, but each parent who is involved must decide: whether it is worth trying to control the school principal concerning fiscal matters because there exists a high probability of conflict that will endanger their child's prospects at the school, or it is better to be silent and merely nod in reflection to the headmaster's "good" reports?

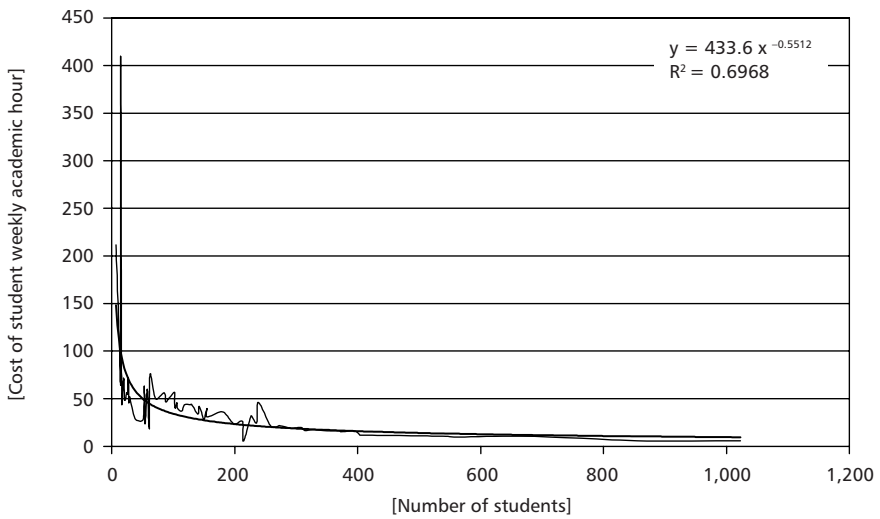
So, the main issues of public empowerment at the school level, like securing access to information, launching consultation, and securing participation in school policy-making—the general issues of civil society functioning (Huntington 2002)—are at the moment not relevant for the vast majority of school establishments because of both objective and subjective reasons.

The local community might have more effective control over the school budget because it represents a politically stronger group interest in comparison to the parental one. However, at the moment, its main concern is not the effective use of scarce funds, but pushing local authorities to maintain the school establishment regardless of efficiency. Ministry of Education officially proclaimed that "No school will be closed," so local authorities are very sensitive to the community voice in this matter. Closing a school has a high political cost, so it is in fact impossible to close a school with a decision based on economic reasons. The result of such policy is illustrated in Figure 2.

Here, the school service unit—student weekly academic hour—is regressed to school size. As it turns out, the cost of educational service unit varies widely amongst schools of the same *rayon*—from UAH 400 to UAH 10. This is a true cost of "social fairness" in the field of secondary education that really limits society's possibilities of improving the state of secondary education. The highest service unit cost is observed in small schools of the first level, which as a rule have bad conditions for rendering educational services. The most efficient are the integrated schools combining educational levels from the first though third. This calls for some policy of schools net optimization that should be performed on the *rayon* level.

On the macro level, the problem is that educational authorities do not collect any information concerning school economy and have no idea about the amount of the existing schools' net maintenance costs and whether this could be improved in any way. As a result, with educational capacities used, on average, at the level of 50 percent in rural localities, the *rayon* and *oblast* authorities each year apply for the building of new schools (and usually receive investment subsidies).

Figure 2.
Correlation between total cost to student weekly academic hour and school size in Sokal district, Lviv *oblast*



Source: Cohen and Slukhai (2004).

The answer to what is the main reason for both direct consumers of education and local communities shying away from budget monitoring is easy: these expenditures are not paid directly from people's wallets or community budget. If you do not pay, you have no choice but to get what is supplied, nothing more or less.

4. HOW TO STRENGTHEN BUDGETARY OVERSIGHT AND ACCOUNTABILITY OF SECONDARY EDUCATION IN UKRAINE?

As the research in the previous chapters has shown, on the national level, there exists no policy concerning public empowerment in executing budget control in education

in Ukraine. The existing legal acts state the formal rights, but establish no mechanism for their realization. Also, the problem could not be solved by an additional legal act, let us say, "On public governance in education." So, a complex policy should be developed that is directed mainly at the institutional strengthening of public governance in this sphere.

As the experience of some countries has shown, in order to build a better secondary education system, we need to change the old system, making school finance more transparent and accountable. This could be done based on principles enforced in the United Kingdom. These are: "per pupil funding, self-management by school boards and directors, highly publicized comparisons of examination performances and parental choice" (Davey 2002: 30). As a result of the implementation of such an approach in the UK, which launched intensive competition among schools, the overall quality of secondary education has been increased and even the schools with the worst performance have improved.

Another good example which proves that decentralization and school autonomy could bring very good results is delivered by New Zealand (Box 2). One can see that schools in New Zealand enjoy a high degree of fiscal independence and are required to perform in a fiscally sound way; the Ministry of Education is deeply involved in fiscal issues and does not give this responsibility away to the Ministry of Finance.

Box 2.

Secondary public school fiscal status and accountability in New Zealand

Each public school in this country holds its *own bank account* (it is free to choose bank institutions and change them) and receives its money *directly* from the government as well as from local sources (fees, community education fees, hire of facilities, trade, fundraising, and similar sources). The operational funding is decided on by the board of trustees, which is accountable for money usage before the national government. These funds consist of a per-pupil-grant (59 percent in total operational funding granted by the state) that has four funding levels according to cost of curriculum delivery and a bulk of earmarked subsidies (like relief teacher grant, Maori-language grant, facility maintenance grant, and others). Hence, the funding is based mainly on school enrollment, and that makes schools very sensitive to the number of students they have. This makes them compete and propose better curricula and better educational conditions.

The board of trustees is responsible for *setting priorities* and *managing the total funding*. In doing so, "the board must meet the requirements of the National Education Guidelines, the National Administration Guidelines, their obligations as good employers and any legislative and contractual requirements to which they are subject." They are also responsible for achieving the objectives specified in the school charter. The amount of state funding depends on the "School's Decile Rating" which basically relates the funding to socio-economic development of the location to which the school belongs.

The board is fully and publicly accountable for the school's financial and physical resources (for allocation of funding among school priorities, control over school expenditures, and preparation and auditing of school reports) and reporting before the community and government. What is important here is the *flexibility* of the budget: in the course of a year the budget appropriations could be changed due to the emerging needs of a school. The school board has discretion to change the appropriations and the total school budget within a budgetary year.

Schools are provided with a set of fiscal indicators, according to which the board and the school principal could monitor the financial status of the school and take the necessary steps in order to improve it. In case the school cannot manage the situation, the Ministry of Education intervenes.

The board of trustees and senior school staff receive financial reports on a *monthly* basis prepared by accounting office. The school's principal receives a detailed monthly report in order to take steps to improve the fiscal situation. Schools are supposed to prepare a report according to guidelines that are basically very similar to those for private entities.

Each year the school is required to submit an *annual* report to the Ministry of Education which is the subject of external auditing provided by the Office of the Auditor General.

Adapted from: New Zealand Ministry of Education 2005.

There is no question as to the fact that a key issue in achieving better budget monitoring in Ukrainian secondary education lies in the field of its decentralization and restructuring of state oversight. So far, the policies proposed were never implemented. The following options below concerning the strengthening of budget oversight and public accountability seem feasible for secondary education.

4.1 New Paradigm of State Budgetary Oversight over Education

The current state oversight is mainly concerned with formal control and monitoring over school finance. Under such an approach, it is almost impossible for schools to have flexibility and strive for efficiency. The state controlling agencies should be concentrated on efficiency and long-term sound fiscal management rather then formal oversight: whether the school fiscal transactions are done in line with legal requirements. This new paradigm requires changes in the current budgetary legislation and the passing of legislation on public finance reporting and auditing. The main function of state controlling bodies should be to assist in improving budget execution rather than searching for budget offenses and punishing school managers.

A significant role in fiscal planning, budgeting, and monitoring should be assigned to the Ministry of Education. The current passiveness in this field seems to be unjustified.

It should have a financial department, a bureau of economic analysis, and staff dealing with the monitoring and evaluation of schools' fiscal performance.

4.2 Devolution of Secondary Education Function

The ultimate approach could be full decentralization of school education by making it a local responsibility with mixed funding from local revenues and state grants. Such an approach is, in general, compliant with the theoretical treatment of secondary education as a local public good, and, in general, gives far greater possibilities to communities to oversee the fiscal issues of school entities and to direct their function according to locally set priorities. But this contradicts the current constitutional provisions that assign this function to the state. Hence, it sounds quite good in theory, but is rather problematic to implement.

Another possibility is the creation of separate school governments (school districts) that are accountable in fiscal issues both to the government and the local taxpayers. Then it will be natural for local community to decide whether they need two schools or only one in order to get more cost efficiency and a better quality of education. Thus, the creation of school districts, and granting them a significant array of powers, could improve the situation with accountability.

There have been some steps in this direction since the Ministry of Education issued an order to experiment in creating school districts in several *oblasts* in 2004. However, in their current form these school districts look more like some additional administrative body with no special rights in managing finance. If implemented, such institution will not improve the fiscal soundness of the school system. The more promising approach is proposed by some NGOs, where the comprehensive system of administration, organization, communication, and finance measures is put on the agenda (Lukovenko 2004).

It may be argued that the decentralization process, the components of which have been proposed above, would create some problems for educational service delivery. Of course, there exists the risk that, under the condition of devolution, local governments will try to "cheat" and lower the funding of the educational function. This, in turn, may cause the further deterioration of secondary education. But this kind of behavior hardly seems possible. The case studies on educational funding performed in several CEECs have proved the opposite outcome of the decentralization process. It turns out that, under devolution, the expenditures on education grew in real terms and the schools became better funded and maintained in comparison to centralized systems still practiced in some CEECs (Davey 2002).

A favorable sign is the prospective territorial and administrative reform prepared by Ukrainian government that could be passed in the course of the year 2006, the essence of which advocates enlarging and integrating local government units. Such a develop-

ment will improve the budgetary position of local governments and will allow devolving educational functions from *rayon* to the community level in rural areas.

4.3 School Autonomy

Proclaimed in the National Doctrine of Education Development (2002), school autonomy still remains only a declaration. According to interviews with school administrators, most of them are willing to have more fiscal autonomy (i.e., to have an accountant, a bank account, to attract off-budget money to fund school outlays, to motivate teachers with performance bonuses from extra money the school attracts or saves), but the current administrative pressure and tight state fiscal control make this almost impossible. This is why most school directors are afraid to be autonomous. Similarly, *rayon* authorities would be unhappy to be freed from the previous functions in funding schools and managing fiscal flows. According to common arguments of the economic theory of bureaucracy, each administrator does not seek to fulfill public expectations concerning service supply, but to get more command over the budget (Niskanen 1968).

Raising the level of school autonomy will bring immediate economic results because schools will become motivated to use funds more efficiently. Simultaneously, they need to become accountable for the money they use. To achieve this, we need to bring about some policy changes in both directions.

Regarding the first course of action, schools should be granted budget autonomy and flexibility. It involves giving them a right to choose a bank institution, to have an accounting office, to make reallocations among the budget articles within the budgetary year without the approval of the local government. Of course, not all schools are in the position to execute the above rights. The network of schools, especially in rural areas, is very fragmented and therefore needs some treatment. The institutionalization of school districts with a broad range of responsibilities could be a remedy here. But some integrated schools of first through third educational level could execute these rights just now, without changing the school administration scheme.

Simple institutional measures could increase the accountability of the autonomous school units. The most important one could be changing the status of the school board and substituting it for a board of trustees, like in New Zealand. The board should be an independent body that consists mainly of highly respected citizens that have no personal concern in a particular school, have a degree of knowledge in the domain of public finance, and are willing to contribute to school performance. They could be representatives of universities, local governments, and the business community. The rights of this board could be strengthened up to the dismissal of the school headmaster in the case

of the misuse of moneys or assets and deciding upon hiring and extra remuneration of teaching and service staff as a result of school efficiency.

The creation of school districts could be combined with the strengthening of school autonomy. It would be a mistake to merely substitute school district for *rayon* educational authority. Even if we leave the current administrative hierarchy, there are well-addressed courses of action to achieve a better use of public money through granting more discretion to the schools. If the funds among schools on the district level were allocated through a formula-based approach, then schools would have more freedom in the allocation of money according to their needs. It is necessary to develop certain methodological guidelines and to formulate rules for distributing funds for educational institutions at the local level. In this case, huge incentives will emerge for the school administration to efficiently use the money. This, in turn, together with granting broader rights in the use of budget money, might increase cost efficiency and stimulate everybody employed to look for possibilities to economize outlays.

4.4 Mode of Money Allocation

The current approach to formula-based allocation of school money does not give much possibility to secure the appropriate funding of secondary education. The educational expenditures are only calculation measures that involve no funding obligations for the local government side except for mandatory outlays on teacher salaries, heating, and some miscellaneous needs like board for some categories of pupils. These items are funded in most cases. But a large difference among schools in terms of per-student expenditures and per-service-unit expenditures is caused to a great extent by this approach, currently in use in many countries. Here, it is worth mentioning that the Polish experience in school funding, similar to that of Ukraine, reveals a lot of problems and is criticized by experts.

In order to secure more adequate funding to schools and to make them more independent from the good will of the respective local government, the following two steps could be taken: (1) allocate money for education at the *rayon* level as targeted funds, calculated on a formula basis, and that cannot be spent for other functions; (2) allocate money directly to schools based on some formulae. The latter approach seems to be more problematic since no institutional change will be undertaken. The former one has been introduced partly—the educational expenditures are calculated on a formula basis—but the problem is that this calculation remains only a calculation, not real funds. However, the second approach has been successfully practiced in some countries; the information on New Zealand above gives some guidelines of what might be done here.

4.5 Inter-school Competition

Launching competition could be a very attractive measure to improve performance of public sector units. This is also true for educational services. Such quasi-competition does exist now in urban areas where schools with better teaching staff and equipment naturally attract more students, which causes the application of selection procedures and "voluntary" contributions to the school's off-budget funds. In rural areas, such a possibility is highly restricted due to a small number of schools in a given location and the poor development of the transportation network. But there exist some measures to enforce competition through creating a mechanism of students' "voting with their feet." One such possible policy could be the introduction of tuition fees that will make schools try to attract more students by offering better services.

An efficient way of reaching the highest benefits from public money without introducing direct tuition in public schools could be a voucher system. At least in large cities where parents have a choice, it could create some kind of competition that automatically will make a school try to propose educational services of higher quality and better conditions for learning. Mainly consumers will decide upon how much money to give to this school, not the educational authority.

5. WHO SHOULD DO WHAT AND WHEN REGARDING THE BUDGETARY OVERSIGHT AND ACCOUNTABILITY OF SECONDARY EDUCATION?

In order to improve the situation, the following policy measures could be proposed:

- Changing the role of the Ministry of Education and Science. It should be responsible not only for the content of secondary education, but also for budgeting for the school entities. That is why it needs a structure with departments dealing with financial analysis and monitoring.
- The state controlling bodies should switch from monitoring the legality of fiscal transactions to fiscal analysis aimed at achieving a higher efficiency of resource usage. The functions of controlling and auditing state authorities also might be reassigned. The inspections should be performed on the basis of the annual school report submitted to a respective administrative body and should stress the development of a methodology of internal fiscal control and audit performed by schools themselves.
- The community should be more involved in decision-making at the school level. The main instrument should be the board of trustees who will be required to monitor school performance on a permanent basis. The community and school board should have access to financial information in order to control the school

budgets. This calls for accountant offices on the school level. In schools combining the first through third level such a possibility already exists.

- The school budgets should be published in local media and subjected to internal and external audit. This will enable communities and local NGOs to be well informed about the fiscal state of their respective educational establishments.
- The functions of the *rayon* educational authority should be rearranged from the viewpoint of devolution of most of their power to school districts and autonomous schools. Their responsibility should be mostly limited to educational inspections (mainly annual tests) and assistance to schools in improving the teaching process.

6. CONCLUSION

Present-day Ukrainian legislation does not provide a clear framework concerning the effective use of public money. Schools are almost fully financially sustained by district state authorities and have a cost-estimate instead of an independent budget.

The most important problems facing the financing of the general education network are:

- an unclear process regarding the formation and usage of budgets of educational establishments,
- an inefficient use of public resources,
- the impossibility to use alternative sources of financing to their full extent because of imperfections in the legislation,
- schools and society in general are not ready for changes in the economic and political sphere, and they have not adapted themselves to the competitive environment,
- the state is not yet in the position to grant sufficient stimuli for the alternative financing of educational establishments, e.g., freeing private costs given away for education, of taxation.

The current legislation should be revised in order to increase the independence of educational establishments and also to strengthen the accountability of educational establishments and authorities to the public.

The core issue of budget oversight in Ukraine is the dominant role of the state bodies and the minor role of the public. The former is due to very high portion of delegated functions in local government activities; the latter is due to a low level of influence of general public on the level of school funding.

The main concern of state oversight is the "right" usage (from the point of view of the state) of public money rather than efficiency of its usage.

Under the current conditions, there is no effective mechanism that could guarantee the best possible usage of educational budgets both on the macro and micro levels.

The goal of the policy proposed in this paper is to increase the public participation in the school budget in order to gain more efficiency in educational service delivery. These policies are based on increasing the autonomy and responsibility of school units and change in the oversight functions of the state bodies.

The better choice for enhancing budgetary accountability would be the implementation of self-regulating mechanism on the school level combined with a normative formula-based approach in allocation of public money, as well as launching the elements of competition among schools, especially in large cities. This will raise not only school cost efficiency, but also the quality of education.

ENDNOTES

1 Secondary education in this paper stands for pupils from 6 to 17 years old. It combines three basic levels: elementary—first level (grades 1 through 4), secondary—second level (5 through 9) and high—third level (10 through 12). Usually, urban schools have all three levels combined in one school unit; in rural areas one can find schools of first, first and second, and first through third level.

2 A good overview of transitional educational economics is provided in Davey (2002).

3 In Poland, the Ministry of Education is very active in formation of educational budgets, performing annually calculations of fiscal needs of the schools. Due to the nature of educational funding in Poland, the level of funding is formally not secured; but as a matter of fact, Polish local governments spend more on school education than is allocated to them in a process of fiscal equalization for this function (Rado 2004).

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ANNEX

7A Statistical Information on Local Budgets and Oversight in Ukraine

Table A1.
Composition of subnational government revenues in Ukraine

Revenue type	1999			2003		
	[Million UAH]	[Million USD]	[Percent]	[Million UAH]	[Million USD]	[Percent]
Tax revenues	10,962	2,654	55.26	18,195	3,414	54.6
Taxes on revenue, profit, market value increase, including	7,935	1,921	40.0	13,369	2,508	40.1
Personal income tax	3,111	753	15.7	13,210	2,478	39.6
Enterprise profit tax	4,824	1,168	24.3	159	30	0.5
Property taxes	296	72	1.5	604	113	1.8
Local taxes and duties	442	107	2.2	595	112	1.8
Unified tax for small businesses	62	15	0.3	818	153	2.5
Non-tax revenues	552	134	2.8	2,231	419	6.7
Capital revenues	7	2	0.04	998	187	3.0
Earmarked funds	1,631	395	8.2	543	102	1.6
Revenues without transfers	13,152	3,185	66.3	21,968	4,122	65.9
Official transfers	2,942	712	33.7	11,355	2,130	34.1
Total revenues	16,095	3,897	100.0	33,323	6,252	100.0

Source: MoF 2000, 2004.

Note: Official exchange rate UAH/USD for 1999 was 4.13, and for 2003 was 5.33. These rates are based on current exchange market rates that have been stable through the last three years.

Table A2.
Powers of public agencies involved into external control over local government fiscal activities

Accounting Office	Ministry of Finance
Audits use of budgetary funds dedicated to funding delegated responsibilities of local self-government concerning both expenditures and revenues	Audits the compliance of local authorities' decisions with budget legislation on each stage of budget process
State Treasury	**State Control and Revision Service**
Performs accounting of proceeds and outlays of local budgets; enacts the unified rules of accounting and reporting concerning execution of local budgets and cost estimates, issues instructions on these matters and controls their implementation; controls the compliance of payments, obligations, and budget appropriations	Controls the targeting and effective usage of budgetary moneys on the local level; controls earmarked usage and timely repay of loans received under security of the Ukrainian Government; checks the obeying of rules of accounting performed and the reliability of reports concerning budget and cost-estimate execution; delivers information to local fiscal authorities concerning audits performed

Adapted from: SEFR 2002, p. 150.

Table A3.

Ukrainian legal provisions concerning administration and funding of general secondary schools

Legal act	On administration	On funding
Law on Education (1991)	Determines the administrative authorities and their functions.	Educational establishments are funded through respective budget and other sources. The extra sources include: payments for additional educational services; revenues from selling; subventions from local budgets; bank loans; voluntary contributions. The off-budget funding could not decrease the public sources. The extra revenues are not subject to profit tax in the case they are dedicated to educational purposes.
Law on General Secondary Education (1999)	Delineates authority between state bodies and self-government concerning school administration.	Refers to other legislative acts.
Law on Local Self-government (1997)	Very generally formulates the powers of local authorities concerning education.	Does not contain.
Law on Local State Administrations (1999)	Determines the sphere of responsibility of state administrations in education: they administer educational establishments as delegated function.	The state administration provides funding of delegated (by local self-government) powers in field of education.
Regulation on General Education Establishment (1999)	The school is administered by an appointed (by MoES department) headmaster. The headmaster is in charge of school assets and costs. Other bodies of school administration: teachers' council, staff meetings, school board, supervision board, parental committees.	Identifies the shortened list of additional services, approved by Ministry of Finance; determines school board's authority in control over school finance and facilities. Financial and economic activity is conducted on the basis of school budget. Sources of the school budget are—the state budget; sources of private donors, moneys for delivering other services by schools, revenues from selling products, and rent from school facilities; banks' loans and charity donations. It is permitted to create a foundation from budget and other sources.

Table A3. (continued)

Ukrainian legal provisions concerning administration and funding of general secondary schools

Legal act	On administration	On funding
Budget Code (2001)	Does not contain.	Delimitates educational expenditures between different tiers of intergovernmental budget relations system; introduces formula-based approach to the accounting of the educational expenditures for the territory (local governments)
National Doctrine of Education Development of Ukraine in 21st Century (2002)	Decentralization, function reallocations between different tiers of government. School autonomy. Community participation in education management.	Differentiation of sources of school financing and provision, its priority for the education. Incentives for the charity donations. Not-for-profit activity of schools, grants and credits, loans are supported.

Table A4.

Funding of delegated responsibilities in separate spheres as percentage of the need, according to the estimates of small city mayors, 2003

City (settlement)	*Oblast*	Function		
		Education	Healthcare	Social security
Bakhchisarai	AR Crimea	58		
Borzna	Chernihiv	70	70	
Boyarka	Kyiv	46		30
Chervonozavodske	Poltava	75	60	
Dolyna	Ivano-Frankivsk	70		
Halych	Ivano-Frankivsk	64		100
Hlobyne	Poltava	62	100	85
Hola Prystan	Kherson	75		
Horodenka	Ivano-Frankivsk	64		100
Horodok	Khmelnicki	74		2
Inkerman	AR Crimea	50		40-50
Irshava	Zakarpatska	90	70	50
Kaharlyk	Kyiv	50		
Kalanchak	Kherson	50		
Kobeliaky	Poltava	85	90	95
Komarno	Lviv	100	100	100
Kossiv	Ivano-Frankivsk	100	80	90
Kostopil	Rivne	95		
Nadvirna	Ivano-Frankivsk	90		
Ovruch	Zhytomyr	50		40
Petrovske	Luhansk	90	80	
Pology	Zaporizhzhia	50		50
Prymorsk	Zaporizhzhia	70	70	50
Radomyshl	Zhytomyr	75		50
Rohatyn	Ivano-Frankivsk	50		
Sarny	Rivne	52		60
Sniatyn	Ivano-Frankivsk	65		

Table A4 (continued)

Funding of delegated responsibilities in separate spheres as percentage of the need, according to the estimates of small city mayors, 2003

City (settlement)	Oblast	Function		
		Education	Healthcare	Social security
Tlumach	Ivano-Frankivsk	70		
Tsiurupinsk	Kherson	50	100	20
Tysmenycia	Ivano-Frankivsk	100		
Valky	Kharkiv	52		
Vashkivci	Chernivci	61	80	
Verkhnia Lanna	Poltava	100	100	100
Vovchansk	Kharkiv	60	99	33
Vyshgorod	Kyiv	35		25
Zelenodolsk	Dnipropetrovsk	60		
Zhydachiv	Lviv	70		
Average		**68**	**83**	**60**

Source: AUF 2003.

Table A5.
Efficiency measures for urban schools combining the first through third level, Sokal district, Lviv *oblast*

School	Number of students	Total expenditures per student, UAH	Total expenditures per student relative to average level, percent	Total expenditures per student-academic hour per week, UAH	Total expenditures per student-academic hour per week relative to average level, percent
No. 4, Sokal	763	814.68	102	8.61	101
No. 2, Sokal	870	650.80	82	5.55	65
No. 3, Sokal	663	829.86	104	10.86	127
No. 5, Sokal	259	705.79	88	21.11	247
Sokal gymnasium	404	1,309.16	164	11.71	137
V. Mosty	1,023	669.40	84	5.87	69
Belz	533	829.64	104	10.75	126
Ugniv	226	911.95	114	30.54	358
Average		**797.89**	**100**	**8.54**	**100**

Source: Field study in Sokal district, Lviv *oblast*.

Table A6.
Average importance of activities determined by school headmasters in Velyki Mosty school cluster, Sokal district, Lviv *oblast*, 2004

Activities	Respondents / Ratings										Total	Weight
	1	2	3	4	5	6	7	8	9	10		
Classes	5	6	6	6	5	6	6	5	6	6	57	0.27
Extracurricular activity	6	4	4	2	3	2	4	1	4	2	32	0.15
Personnel	4	3	3	5	2	4	1	4	5	5	36	0.17
Physical infrastructure	1	5	5	4	6	3	5	6	3	4	42	0.20
Interaction with environment	3	1	1	1	1	1	3	2	1	3	17	0.08
Parental and communal concern	2	2	2	3	4	5	2	3	2	1	26	0.12
Total	**21**	**21**	**21**	**21**	**21**	**21**	**21**	**21**	**21**	**21**	**210**	**1.00**

Source: ISTS 2004c.

7B Citizens' Participation in Budget Oversight

Citizens' participation in matters of local concern is regulated by a set of national legislative acts: the Constitution (1996), the Law on Local Self-government (1997), and the Law on Bodies of Self-organization (2001) that proclaims the right to participate in issues of public importance. Article 5 of the Constitution says: "The people shall be the only source of power and sovereignty of Ukraine. The people shall exercise power directly and through state power bodies and local self-government bodies." As some legal experts concluded, there exists also a problem of practical implementation of these constitutional norms into real life (Denisenko 2004).

The Law on Local Self-government vested to the local populace a right to issue initiatives that should be taken into consideration by the respective local government, to initiate public hearings (at least once a year), and to create self-organizing bodies with vested powers extending also over spending of budgetary moneys. Article 75 stipulates that the local bodies and officials *should be accountable to local community* and are obliged to inform people about their activities, including budget execution at least twice a year, and delivering respective reports. The local community can stop at any time the authority of the bodies or officials, if they do not perform the vested obligations efficiently.

The Law on Bodies of Self-organization is especially important, since it institutionalizes popular participation in governing local issues. The self-organizing bodies have an aim to make the inhabitants active in fostering socio-economic and cultural development of the territorial unit. They have a right to represent the popular stake in official local public bodies and to activate direct forms of democracy through polling, meetings, local initiatives, and public hearings.

The analysis of the legal basis of popular participation in issues of local concern makes some scholars conclude that "this legislation is the most advanced one in Ukraine because in addition to the constitutional right to participation in public governance, citizens have an actual mechanism for exercising this right" (Denisenko 2004: 26). But, at the same time, *the procedures of obtaining information about issues of public concern are not precisely stated*, so the question arises whether citizens can realize their right to influence the public bodies concerning fiscal issues. This is especially true for budgetary issues at the local level.

7C Information

In general, the access to information on educational budgets is quite limited. The data on the school fiscal performance is collected only on the *rayon* level. The Ministry of Education does not collect and generalize the data because it is not involved in the budgeting process.

The *rayon* education department of the local state administration has access to data because it is mainly concerned with economic and fiscal issues related to secondary education. Usually the fiscal data is collected on an annual basis with no special reflection to the cost-efficiency and quality of services.

The data on school budget execution concerning the part granted by the local government and *rayon* educational department is quite reliable. But there exists no reliable information concerning off-budget funding—most of such activities are done in an unofficial way. According to estimates, up to 15 percent of school budgets belong to informal transactions. Schools are motivated to hide and not to report off-budget activities in order to avoid paying taxes or being subjected to control from the State Control and Revision Service.

There are possibilities to access data on budget plans (estimates) and their execution in *rayons*, but usually the *rayon* educational department reports a 100 percent match between these numbers. Some mismatch could occur only in case if there was a *rayon* budget sequester. But this relates only to so-called "non-secured" budget items (the secured ones are teacher salaries, board, and heating).

7D Accountability

Since school establishments in Ukraine do not have separate budgets (they have only cost estimates) relying in fiscal issues on the *rayon* authorities (financial departments of the local state administration), they are mostly accountable to superior bodies, not to the local community. This creates severe problems both with the content of education (it usually does not take into account the local demand for special qualifications of the school graduates) and with cost efficiency. Schools do not care much about efficiency because they must spend the whole amount they are granted by the authorities.

Rayon educational authorities belong to local state administration and are also accountable to the superior administrative body. *Rayon* councils do not have executive bodies and are not in position to overview the performance of educational entities. Although in some localities local councils try to assist in secondary education according to legislation, they are prohibited to contribute to school funding directly. All of this accounts for the low accountability of educational administration to the final consumers of educational services.

The Ministry of Education is indeed not accountable for the spending of public funds because the funding occurs through local financial departments of the Ministry of Finance.

Index of Terms

Making Public Finance Public traces the development of fiscal transparency and accountability in the field of public finance in three post-communist European states yet to qualify for membership in the secure and prosperous borders of the European Union: Croatia, Macedonia, and Ukraine.

These case studies focus not on transparency at the national level as many studies have in the past, but seek the answers to essential questions that require immediate redress: how can local governments and their constituents in these countries cooperate to make local budgets understandable and accountable to the general public; how can national legislation be amended to enshrine the principles of accountability in law; and how can citizens arm themselves with the skills and tools necessary to ensure the efficacy and transparency of local government budgets at risk from corruption, mismanagement, and closed decision-making.

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After well over a decade of higher priorities in these transition states, it is time to reprioritize the agenda and look for the improvements that will guarantee better fiscal governance at the local level if both democratization and decentralization are to succeed.

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