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CHANGES IN THE STRUCTURE OF INCOME OF POLISH MUNICIPALITIES, 2019–2021

This article is devoted to studying the detailed income structure of Polish municipalities in the years 2019–2021. The general structure of municipalities' income is examined in a broader time horizon (2004–2021). The theoretical section focuses on the characteristics of municipalities' income, with particular emphasis on tax income, the level of which depends to a large extent on the financial situation of enterprises. The research section is based on data from the Central Statistical Office. The article concludes that in the years 2019–2021, the income situation of municipalities did not deteriorate as much as was predicted. However, it is noted that the income structure of municipalities is changing, and the share of their own income is decreasing; this may lead to a significant reduction in their financial independence.

Keywords: municipality, municipalities' income, taxes.

1. INTRODUCTION

The recession caused by the spread of the SARS-CoV-2 virus was a factor strongly affecting the finances of entrepreneurs and local governments. Local governments, as direct providers of public services, have struggled to respond to the COVID-19 pandemic on an unprecedented scale, despite sometimes immediate and severe disruptions to their budgets (Dzigbede, Gehl, Willoughby, 2020; Dutta, Fischer, 2020).

It forced the need for dynamic changes and adaptation of local government units to new circumstances, especially in terms of their income. The decrease in the income of entrepreneurs translates directly into the decrease in the tax income of local government units, especially municipalities. The COVID-19 pandemic posed new challenges for local government units and made it necessary for them to adapt quickly to the new reality in connection with the implementation of the tasks imposed on local governments, as the activity at the local government level affects the economy of the entire country (Łubina, 2021). Pandemic preventive measures included, among others: suspending classes in schools, temporarily limiting various ways of moving around, temporarily limiting the functioning of certain institutions and workplaces, banning public gatherings, etc. The implemented limitations caused reorganization of various branches of economy, and some entrepreneurs suspended their business activities. This situation affected directly the financial situation of local governments, especially of Polish municipalities.

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The subject of this study is an attempt to estimate the changes in the structure of Polish municipalities' income between 2019 and 2021, as well as identifying the changes in the level of income from municipal taxes. Moreover, when estimating the structure of total income, a wider time horizon was used to illustrate better the trend of change, not only caused by the pandemic. Municipalities were selected for the study because they have the largest catalog of sources of their own income, among all local government units.

2. CHANGES IN THE STRUCTURE OF MUNICIPALITIES' INCOME

The fundamental factors specifying the conditions of functioning of the local government are financial resources and an adequately planned budget which constitutes the basic instrument in the process of efficient management and planning (Dylewski, 2007).

The system of financing municipalities should guarantee them the amount of funds appropriate to their tasks, the possibility to use them freely, and above all, it should ensure the stability of income (Wankiewicz, 2009). Unfortunately, in recent years a drastic decline of their own income has been observed in the case of municipalities, which, in connection with a simultaneous transfer of additional tasks or broadening the range of the already existing ones, has led to a financial imbalance of numerous municipalities. The COVID-19 pandemic, accompanied by legal changes in taxation system, undoubtedly contributed to the reduction of own income of municipalities, which share in the structure of the total income is decreasing.

Municipalities' income consists of three parts. Basically, these are their own incomes, subsidies and grants, which results directly from the provisions of the Act on Income of Local Government Units (Act 2003, Article 3(1)). All indicated groups of income can be of both current and property nature. Although municipal self-governments should derive the majority of their income from their own sources, it would be difficult not to notice the need to supply their budgets with a subsidy from the state budget. Large disproportions in income, with similar or sometimes even identical tasks imposed on them, mean that municipalities are often unable to carry out all these tasks from their own income. In the absence of funds, state intervention is necessary to equalize the financial situation of individual municipalities. The problem of inequality related to, for example, an uneven local tax base, means that various types of transfers from the state budget usually constitute a significant part of municipalities' budgets. The European Charter of Local Self-Government postulates that, if possible, transfers should take a general, non-target form.

The subsidy is a public benefit provided by the state to local government units. In the doctrine of public finance law, it is customary to define subsidies as a non-repayable, general, unconditional and gratuitous benefit. The generality of the subsidy means that it does not have a specific purpose, it is defined by the municipality's constitutive body. The subsidy is non-repayable because the funds transferred under it are not refundable (except for the amounts unduly collected). The free-of-charge subsidy means that the municipality, receiving public funds from the state budget, is not obliged to provide consideration to the state treasury (Kwiatkowski, Tyszkiewicz, Wójcik, 2021).

According to the provisions of the Act of 13 November 2003 on the income of local government units (Act 2003, Article 7(1)), the general subsidy for communes consists of:

- compensating part,
- educational part,
- balancing part.

Subsidy is a form of external support for the municipality's finances guaranteed by the constitution. As a result, local government authorities have a kind of sovereignty in terms of using the subsidy. The only type of subsidy that does not give municipal authorities full freedom to dispose of it, is the education subsidy. The funds transferred to municipalities under this subsidy must be allocated to the implementation of educational tasks. The subsidies are intended to reduce the effects of unequal access to sources of income or a different burden of expenditure incurred by municipalities (Hanusz, 2015), being a permanent element supplying their budgets.

Grants are a special form of financial support for municipalities, which are subject to legal rigor and strictly defined settlement rules (they are funds for the implementation of a specific task). Grants are a permanent element of the income structure of municipalities. The essence of grants is their close connection with a specific task to be performed, after which the funds received must be accounted for. Therefore, the targeted nature of the grant significantly limits the freedom to perform activities financed in this form (Hanusz, 2015). The grant is a marked transfer. Municipalities may receive grants from many sources, in addition to the state budget, from earmarked funds, other local government units, and from foreign sources. Grants received by municipalities from various sources are subordinated to the appropriate sections of the budget classification, depending on the area of activities for which they were granted.

External transfer relocated to municipalities (subsidies and grants) are not very susceptible to the economic situation and other phenomena such as a pandemic. The most variable group of municipality's income is their own income.

Own revenues recognized in a broader context (*sensu largo*) are those that do not constitute subsidies or grants. The amount of own income determines the upper limit of the budget constraint, determining the municipality's ability to implement investment expenditures (Zioło, 2012). Taking into account the economic importance of individual sources of own income, they are clearly divided into four basic segments (Guziejewska, 2008):

- tax income, including income from taxes and local fees,
- income from the property of the municipality and revenues from the economic activity conducted by it,
- income from shares in the proceeds from state taxes, which cannot be classified as tax due to the complete lack of authority of the local government in their scope,
- other income which is not earmarked grant or general subsidy, automatically included in municipality's own income.

Own revenues of municipalities, due to the fact that they are not earmarked, can be spent in any way, i.e. both for current expenses necessary to ensure the continuity of financing the unit and for investment expenses. They determine the degree and scope of financial independence of municipalities, as they determine the level of this independence. Own revenues are collected from sources located in the area of operation of a given local government, they are made available to municipalities indefinitely by virtue of law, some of them come from sources that local government bodies can influence by deciding on their introduction or at least specifying the legal structure of these income.

An important source of own revenues of municipalities are revenues from income taxes, both from natural persons and from legal persons. The main advantages of shares based on PIT (personal income tax) are the ease of collection and cheap administration (Govinda, 2007). This is where the financial condition of enterprises and the finances of

municipalities come together. The higher the income taxes paid by natural and legal persons to the state budget, the higher the own income from the shares in these taxes is received by the municipality. Thus, the better the financial situation of enterprises in a given municipality, the higher its income.

The adoption of legal acts related to COVID-19 resulted in a decrease in revenues from personal income tax, corporate income tax, and tax on civil law transactions (Golaszewski, 2020), in the income of municipalities, a periodic decrease in outflows from stamp duty was also noticeable, as the aftermath of limiting the activities of institutions and offices. On the other hand, in the area of local taxes, the decrease in revenues was the result of the decisions of the executive authorities of the municipalities to grant exemptions, reliefs and deferrals in tax payments on the basis of applicable ordinary regulations and special acts related to the pandemic.

The structure of own revenues of municipalities in 2014–2021 is presented in Figure 1.

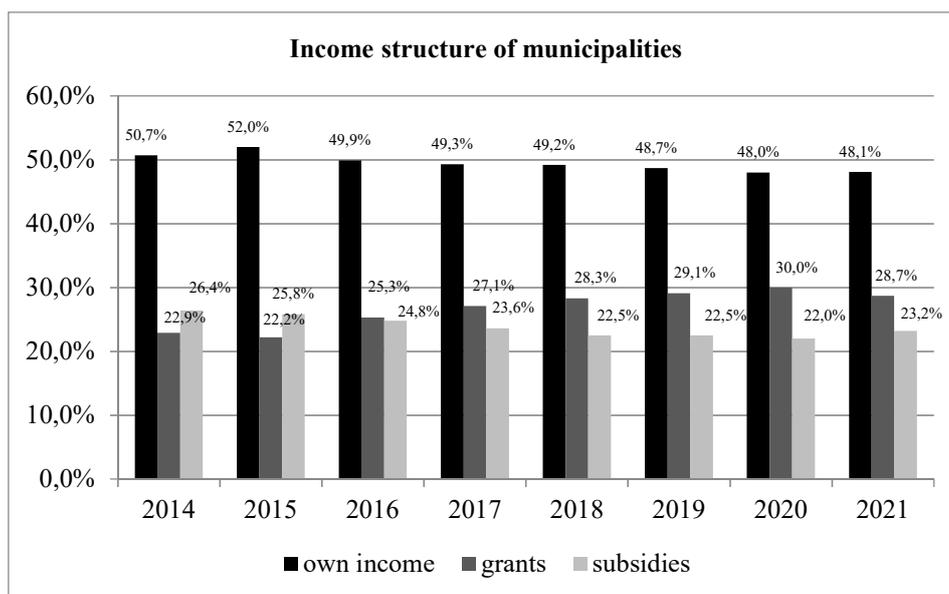


Figure 1. Structure of income of Polish communes in 2014–2021

Source: own elaboration based on Central Statistical Office.

The structure of total income shows that funds transferred from the state budget to the budgets of local government units accounted for almost 52% of their income in 2021 (compared to 2014, the share of grants and subsidies in total income increased by as much as 2.6 percentage points, the share of grants in the corresponding period increased by 5.8 p.p., and subsidies decreased by 3.2 p.p.). Characteristic for the presented years is the phenomenon of a systematic increase in the share of grants in the income structure of municipalities and a decrease in the share of own income in this structure. This proves the progressing serious limitation of the financial independence of local government units (Kwiatkowski, Tyszkiewicz, Wójcik, 2021).

The chart below presents the shaping of municipalities' income independence in 2019–2021.

Specification	Years		
	2019	2020	2021
Total income	229 128	249 413	274 527
Own income	113 329	121 294	132 149
Shares in PIT and CIT	51 750	50 935	57 878
Income independence index (own income/total income)	49,46%	48,63%	48,14%
Income independence ratio adjusted for shares in state taxes (own income - shares in PIT and CIT/total income)	27%	28%	27%

Chart 1. Municipality income independence index in 2019–2021

Source: own elaboration based on data from the Central Statistical Office.

The analysis of the data presented in Chart 1 regarding the index of income independence of municipalities shows that throughout the period under review, this index had a downward trend (a general decrease by 1.32 percentage point), which is the result of decreasing own income in the structure of total income of municipalities (data from Figure 2). On the other hand, the ratio of income independence of municipalities adjusted for outflows from shares in state taxes remains at a relatively constant level (in the analyzed period, its increase was recorded by 1 percentage point in 2020 compared to 2019, and a decrease by 1 percentage point in 2021 compared to 2020).

The situation becomes even more unfavorable for the local government when we look at the structure of own income, which also includes transferred income, even though it is classified as own income.

2.1. The structure of municipalities' own income

As previously mentioned, all those that are not grants and subsidies should be considered as own income. Thus, the catalog of own income is very extensive. According to the budget classification, own income can be divided into:

1. a share in state tax revenues
 - a) a share in personal income tax (PIT),
 - b) a share in corporate income tax (CIT).
2. taxes and fees
 - a) property tax,
 - b) agricultural tax,
 - c) forest tax,
 - d) tax on means of transport,
 - e) inheritance and gift tax,
 - f) tax on civil law transactions,
 - g) stamp charge,

- h) service charges,
 - i) other taxes and fees.
3. other own income

Figure 2 presents the structure of own income of municipalities in 2019–2021.

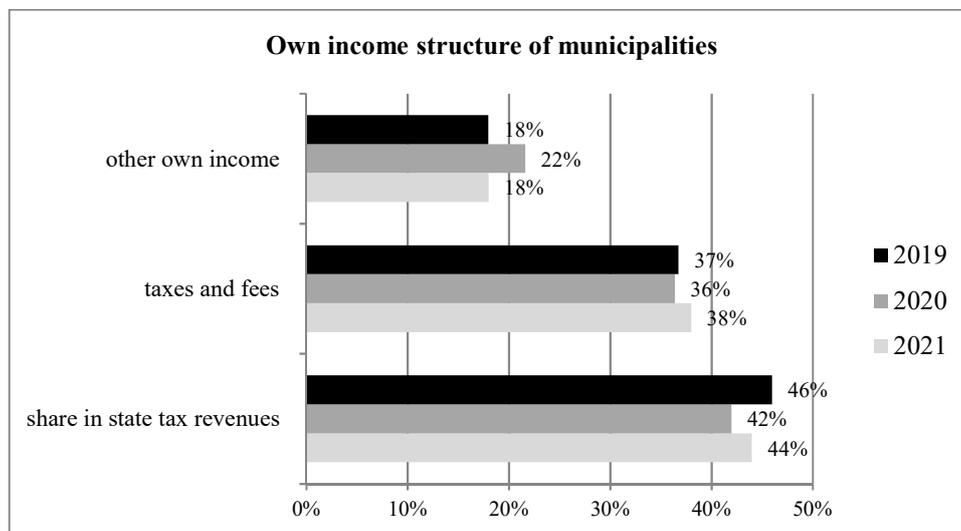


Figure 2. The structure of own income of municipalities in 2019–2021

Source: own elaboration based on data from the Central Statistical Office.

A detailed analysis of the data presented in Figure 2 allows to conclude that in the structure of own revenues of municipalities, the largest part is represented by shares in state taxes (PIT and CIT), i.e. those revenues that are transferred to municipalities' budgets from the state budget, and municipalities do not have any tax jurisdiction over them. Shares in the proceeds from state taxes constitute a group of income that is very sensitive to changes in the economic situation, moreover, the efficiency of this instrument depends on the policy of the central authorities.

The structure of own income of municipalities in the analyzed years did not change significantly. It was dominated by shares in state tax revenues (42%–46%) throughout the analyzed period, the second largest group of own revenues were taxes and fees (36%–38%), and the smallest share was held by other own revenues (18%–22%). Due to the fact that tax revenues (both direct and transferred) constitute the largest share in the own revenues of municipalities, they were analyzed in the next chapter.

3. TAXES AS A SOURCE SUPPLYING MUNICIPALITIES' BUDGETS

The tax system in Poland grants local government units a portion of tax revenue, which is a key source of financing public tasks. The performance of public tasks by municipalities depends on the availability of public funds obtained e.g. from taxes collected from households and entrepreneurs in a compulsory, non-refundable and non-equivalent manner. Tax revenues as the basic source of financing public tasks in the conditions of economic downturn are decreasing, which adversely affects the functioning of all levels of

local government, especially municipalities, which are the largest beneficiaries of shares in central taxes (Dworakowska-Raj, 2020).

The source of tax income in municipalities are local government taxes (including local taxes), as well as the shares in central taxes.

Local government taxes include:

1. Local taxes:
 - a) property tax,
 - b) agricultural tax,
 - c) forest tax,
 - d) tax on means of transport.
2. Taxes transferred to the budgets of municipalities:
 - a) personal income tax paid in the form of a tax card,
 - b) inheritance and gift tax,
 - c) tax on civil law transactions.

Shares in central taxes include:

1. shares in the income tax revenues from natural persons residing in the area of the municipality,
2. shares in income tax revenues from legal persons having their headquarters in the commune.

The tax authority in the field of local taxes is vested in the municipalities. They can freely, within the limits of applicable law, set the tax assessment and introduce reliefs and exemptions. Local taxes are less dependent on the economic situation than common income (shares in central taxes). On the other hand, the economic situation in the country has a strong impact on the amount of income of communes from shares in income taxes. The economic downturn has a negative impact on the state's finances, and this directly contributes to lower incomes of municipalities due to declining tax revenues. The instability of income from shares in central taxes makes it difficult for municipalities to pursue an effective financial policy. The effectiveness of this source of income for municipalities depends on the policy of the central authorities.

High tax revenues guarantee that municipalities strengthen their financial situation by increasing their own budgetary revenues. As a consequence, they contribute to the implementation of various budget expenditures as part of a wide catalog of public tasks performed in municipalities (Dworakowska-Raj, 2020).

Local taxes constitute the group of income over which municipalities have full tax authority. The structure and amount of revenues from local taxes are presented in Figure 3. The forest tax was deliberately omitted from the list because its share in the structure of local taxes is insignificant.

In the structure of local taxes, property tax remains dominant, with a share in local taxes of 90% in total, in each examined year. The amount of income from property tax has increased throughout the whole examined period. The dynamics of the real estate tax, assuming that the previous year = 100, was respectively in 2020 – 104% and in 2021 – 108%, in the tax on means of transport in 2020 – 100% and in 2021 – 106%, and in the agricultural tax in 2020 – 105% and in 2021 – 102%.

Another tax group that supplies the budgets of municipalities are taxes transferred to them in full. This group includes inheritance and donation tax, tax on civil law transactions and personal income tax paid in the form of a tax card. A summary of the amount of proceeds on this account is presented in Figure 4. Personal income tax paid in the form of a tax card has not been included in the chart for its relatively low value.

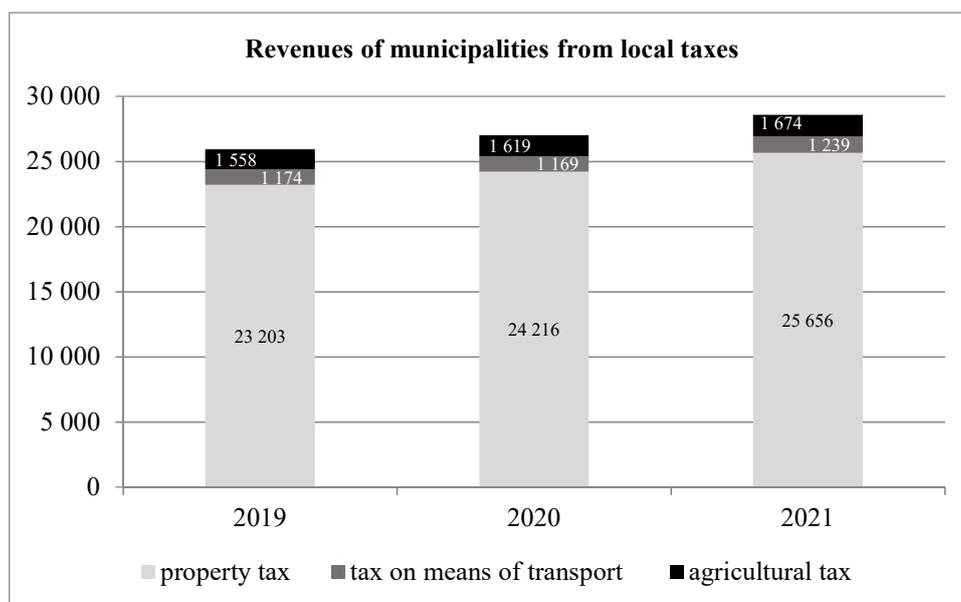


Figure 3. Income of municipalities from local taxes in 2019–2021 in PLN million

Source: own elaboration based on data from the Central Statistical Office.

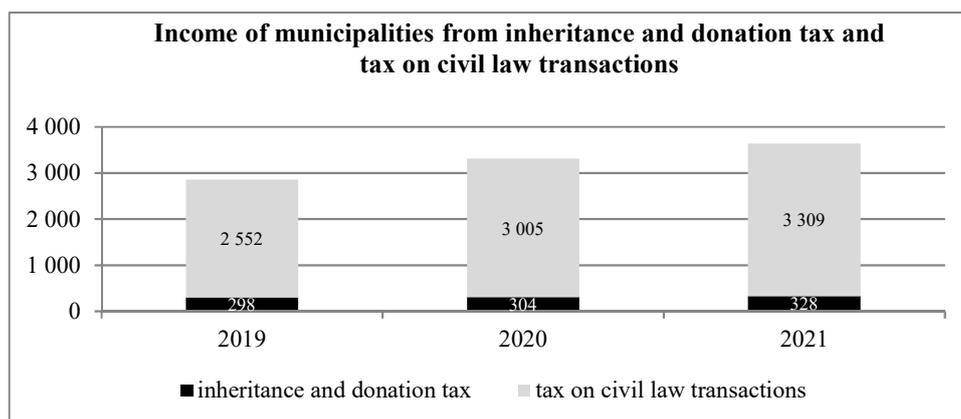


Figure 4. Income of municipalities from inheritance and donation tax and tax on civil law transactions in 2019–2021 in PLN million

Source: own elaboration based on data from the Central Statistical Office.

Budget revenues from the above-mentioned taxes in the analyzed period showed a large increase in 2021, however, their structure in 2019–2021 was very similar, and the share of the tax on civil law transactions was 90–91%. The dynamics in the inheritance and gift tax, assuming that the previous year = 100, was 93% and 138% in 2020, respectively, in the civil law transaction tax in 2020 – 103% and 149% in 2021, respectively. As a rule,

municipalities have no influence on the amount of outflows to the budget from this tax group. The analyzed taxes concern phenomena not related to local governments, and municipalities do not have the tax authority to determine the amount of tax rates. The share of these taxes in their income is not significant.

The last tax group contributing to the budgets of municipalities are shares in personal and corporate income taxes. As indicated in Figure 2, they constitute the largest part of the own income of municipalities. The amount of income and the structure of shares in PIT and CIT are presented in Figure 5.

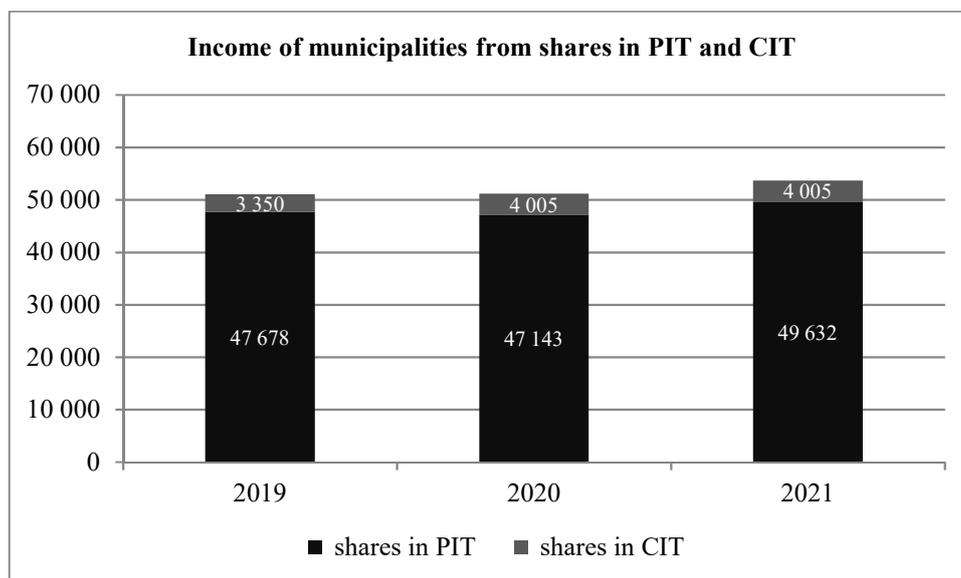


Figure 5. Income of municipalities from shares in PIT and CIT in 2019–2021 in PLN million

Source: own elaboration based on data from the Central Statistical Office

As can be seen, the structure of revenues to the budget of communes in 2019–2021 from shares in state taxes did not show significant differences, shares in PIT in the entire period under review accounted for over 91% of the total income from the shares.

The dynamics of shares in income taxes, assuming that the previous year = 100, was respectively for shares in PIT in 2020 – 98% and 2021 – 113%, and for shares in CIT in 2020 – 104% and in 2021 – 124%.

4. SUMMARY

The conducted research showed an increase in the share of grants in the income structure of municipalities and a decrease in the share of own income in this structure. This proves the progressing serious limitation of the financial independence of local government units, even though the scale of financial problems of local governments during the pandemic turned out to be smaller than expected (a large decrease in the income of municipalities was assumed). The research in this article was conducted on the basis of aggregate data for all municipalities in Poland, however, it should be remembered that the

pandemic crisis affected all local governments to an unequal extent. It had the most negative impact on the largest cities, where a significant decrease in revenues from shares in central taxes was recorded. On the basis of the presented data, apart from the decrease in the share of own income in the structure of the total income, it was indicated that a significant part of the structure of own income is represented by shares in central taxes, over which municipalities do not have any tax authority. That is why the years 2019–2020 were characterized by a high uncertainty in local governments as to the amount of possible income (mainly tax), both due to the pandemic and legislative changes in the tax law. In addition, the aggregate data is slightly distorted because the structure of own (other) income includes funds from the Government Local Investment Fund and from the Government Fund of Polish Order transferred to communes for investment tasks, although in fact they have all the characteristics of a grant. The carried out research provides the basis for formulating a postulate regarding the improvement of the income situation of local governments by providing municipalities with their own, stable income, the use of which they will be able to decide for themselves.

During the deliberations, it was confirmed that a major problem for municipalities and communes is the constantly decreasing own revenues and a very high share of funds transferred from the state budget, which requires urgent intervention to restore the income independence of municipalities.

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