



DOES THE SYSTEM OF MUNICIPAL FUNCTIONS AND THEIR FUNDING PROVIDE CONDITIONS FOR EFFICIENT OPERATION?

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SUMMARY

The Importance of the Audit

Public services which meet the needs of every citizen of the Republic of Lithuania are easily accessible to all regardless of place of residence or socio-economic status, and are intended for the improvement of quality of life and social cohesion¹. The division of state territory into administrative units is aimed at the development of the preconditions necessary for optimum management, improved service for residents, and more effective satisfaction of their needs. In this regard, the state and municipalities have shared goals. This leads to the need for both cooperation and for the combination of centralised state governance and decentralisation. The implementation of the cooperation principle creates the preconditions for state authorities and municipalities, both striving to perform their mandates which have been specified in the law, to seek a common goal, namely – the assurance of effective management of the state and of local communities².

When delegating the implementation of specific functions, it is imperative to assess which level of management (state or local government) and which functions (state (i.e., state-delegated) or independent) would lead to the provision of public services which best meet the needs of residents, while using public finances in the most rational manner possible.

¹ The National Progress Programme for 2014-2020 approved by Resolution No. 1428 of the Government of 28 November 2012.

² Decision of the Constitutional Court issued on 22 October 1996.

Compared to other countries of the European Union, the level of decentralisation in Lithuania is low, i.e., local government is typically given relatively few functions to perform, with the rest being reserved by central government. The lack of integration between central and local levels has a negative impact on both levels of governance – the National Audit Office hereby identifies the shortcomings related to the public services provided by state authorities and municipalities. Even though state authorities take periodic action to improve the system of municipal functions, they do not lead to desired outcomes. Therefore, in order to determine the reasons behind the aforesaid shortcomings, as well as potential measures which could initiate positive changes in the system of functions as a whole, we have made the decision to conduct a systemic audit on the functions performed by municipalities.

The Goals and Scope of the Audit

The goal of the audit is to ascertain whether the system of independent and state (delegated to municipalities by the state) functions performed by municipalities, and their funding, is capable of ensuring the effective and resultative performance of said functions.

The key questions of the audit were as follows:

- does the distribution of functions between the central and local levels of governance ensure their effective and resultative implementation?
- does the system for the funding of state (i.e., state-delegated) and independent functions motivate municipalities to operate more effectively and to strive for better performance?

Audited entities:

- the Ministry of the Interior, responsible for the development of policy at the level of local governance, as well as for the arrangement, coordination, and control of its implementation;
- the Ministry of Finance, responsible for the development of state policy in the area of public finance, as well as for the arrangement, coordination, and control of its implementation³;
- other ministries responsible for the development of policy and the arrangement, coordination, and control of its implementation in the areas where municipalities perform their state (state-delegated) and independent functions⁴;
- state authorities responsible for overseeing the implementation of state (i.e., state-delegated) functions⁵;
- 60 municipalities.

³ Page 7 of the Statutes of the Ministry of Finance approved by the Resolution No. 1088 of the Government of 8 September 1998.

⁴ The Ministries of the Environment, Finance, Energy, Culture, Health, Social Security and Labour, Transport and Communications, Education, Science and Sport, Justice, Economy and Innovation, Agriculture, and National Defence.

⁵ The Central Electoral Commission, the Competition Council, Statistics Lithuania, the State Language Inspectorate, Office of the Chief Archivist of Lithuania, and the Drug, Tobacco and Alcohol Control Department.

The audited period: the 2016 – the 2nd quarter of 2018. In order to conduct a comprehensive assessment, we have also examined the changes in the system of municipal functions which took place during earlier periods (2014-2015). The following was examined during the audit: state strategic planning documents, legislation regulating the operation and funding of local government, resolutions of the Constitutional Court of the Republic of Lithuania related to the operation and funding of municipalities, special laws and other legislation regulating the functions implemented by municipalities, and practices of other countries.

In order to assess and describe the status of functions implemented by the central government and municipal bodies, we have analysed the results of 49 public audits, performed during 2014 - the 1st quarter of 2018, related to the functions implemented by central and local government.

Having regard to the fact that despite our efforts to specify,⁶ in previous public audits, the shortcomings related to municipal revenue planning and distribution, there have been no systemic changes, we have decided to forego the assessment of municipal budget revenue and distribution in the present audit. We have analysed only the state budget funding of functions performed by municipalities.

During the audit, in order to identify risks, we have arranged meetings with representatives of the Ministry of Finance and other ministries responsible for overseeing the functions, the Association of Local Authorities in Lithuania, the Legal Department of the Parliament of the Republic of Lithuania, the Central Electoral Commission, the National Health Insurance Fund, the Drug, Tobacco and Alcohol Control Department, and the Central Project Management Agency. Said meetings have allowed us to learn of the key issues related to the system of municipal functions, and their potential solutions.

The audit was carried out in accordance with the Public Auditing Requirements and the International Standards of Supreme Audit Institutions. A more detailed description of the scope and methodology of the audit is provided in Annex 1 “The Scope and Methodology of the Audit” (p. 39).

Main Results of the Audit

The system of the independent and state (i.e., state-assigned) functions performed by municipalities, as well as the funding thereof, fails to ensure the effective and resultative implementation of said functions: at the national level, there is a lack of assessment regarding which functions could be best implemented by the central government, and which – by local government, and the division of municipally implemented functions into state and independent functions, as well as the separate mechanisms aimed at the implementation and funding thereof, do not lead to effective and resultative implementation of said functions, and fail to improve the quality of public services.

⁶ Public audit reports: No. VA-2017-P-20-6-16 “Actions Taken by Public Establishments and Institutions Aimed at Attracting Direct Foreign Investments” of 27 September 2017, and No. FA-P-30-1-32 “On the Results of Financial (Regularity) Audit Performed in the Municipalities of the Republic of Lithuania” of 30 September 2015.

1. The redistribution of state and municipal functions between central and local levels of governance fails to ensure their effective and resultative implementation

Functions performed by both levels of governance have shortcomings

An analysis of the 49 public and 24 financial (regularity) audits performed by the National Audit Office during the 2014 – the 1st quarter of 2018 has shown that regardless of the level of governance at which the functions are performed, shortcomings are evident both when the central government performs its functions, and when local government performs state and independent functions. Shortcomings have been identified both in the most centralised areas of state operations (e.g., defence and the assurance of public order and public safety) and the least centralised ones (e.g., accommodation and utilities).

The implementation of functions is distributed without assessing at which level the respective functions would be implemented most effectively

An analysis of the 15 changes to the functions implemented by municipalities that were taking place during 2014-2018 has shown that said functions were delegated to the central government and the independent and municipal functions were transformed into state functions. The redistribution was performed without any objective assessment of the desired outcomes or the level of governance – central or local – at which said functions would be implemented the most effectively. Therefore, as shown by the audit, the aforesaid changes did not address any issues at a fundamental level, and did not improve the quality of services.

Both levels of governance are performing similar or equivalent operations in different areas

Since there have been no assessments regarding the level of governance at which the relevant functions would be implemented the most effectively, in 9 out of 10 areas the central and local government, as well as local government when implementing state and independent functions, are both performing similar or equivalent operations. The audit results have shown that, given the above distribution of functions, both levels of government are implementing functions separately, are insufficiently cooperative, and that local government does not receive any clear instructions, goals and requirements from the central government.

Small-scale operations are attributed to the state functions

The failure to define which operations are to be regarded as functions, 11 (out of 36) state (i.e., state-delegated municipal) functions are of a temporary nature, implemented only episodically, and are either small in scale or performed only by several municipalities. During the audit, we have determined that, for the purposes of implementing some of the above functions, e.g., the assurance of the review of the state of incapacitated persons, municipalities receive less than 100 Euros per year from the state. The implementation

of, and accountability for, such functions, as well as accountability for the use of funds is subject to the same requirements as other state functions, which creates additional administrative load borne by state authorities and municipalities.

The improvement of the system of state functions is not resultative

In order to improve the quality and effectiveness of implementation of the functions delegated to municipalities, a review of state functions was carried out in 2015. The review, however, was not resultative because it was focused only on the collection of information about the legal regulation, supervision and control of the implementation of functions and the use of funds from the state budget. The Ministry of the Interior, tasked with the coordination of said review, did not set any criteria for the assessment of the effectiveness of the implementation of functions and did not raise any fundamental questions regarding the quality of implementation and alternatives to their arrangement.

2. The system for the funding of functions does not motivate municipalities to strive for improvement of their performance

State budget funds are allocated to local government without setting any desirable outcomes

In 2017, municipalities received 1,129.6 million Eur from the state budget for the purposes of implementing state (i.e., state-delegated municipal) functions, having set objectives only for 1 (out of 36) state function. 162.9 million Eur from the state budget were allocated for the implementation of independent functions without any assessment of the benefits and impact of such funding, and setting no specific and measurable objectives for municipalities to strive for. Audits have shown that insufficient cooperation between state authorities and municipalities in determining and striving for nationally significant socio-economic objectives leads to negative consequences, namely – the failure of realising said objectives.

State budget funds are allocated to municipalities without any objective assessment of how much funds they require to implement their functions

The methodologies used for calculating the need for state budget funds are not helpful in performing objective and justified calculations of the need for funds, and do not help when planning the funds necessary for the implementation of state functions: the calculation of the need for funds with regards to 10 (out of the 36) functions is not regulated, the indicators for 14 functions are not objectively justified, and only the principles for distribution of state budget funds allocated to municipalities were established for 3 functions. This leads to the allocation of differing amounts of funds for the implementation of the same state functions; municipalities lack state funds necessary for the implementation of 12 (out of 36) functions, which requires them to use their own funds to perform the necessary functions.

State authorities do not systematically control the information on how much it costs for municipalities to implement state functions, i.e., to what extent municipalities contribute

to the implementation of said functions with their own funds (information on the use of municipal funds for the purposes of implementing functions is available for only 3 (out of 36) functions).

Municipalities do not have any opportunity to direct limited state funds to more effective ways of implementing state functions

There is currently no procedure in place for the use of state budget funds in connection with 11 (out of 36) state functions. The procedures set for the use of funds in connection with 25 state functions allow municipalities to use the funds allocated to them only for specified, but different groups of expenditure. Municipalities are forced to cover expenses not specified in the aforesaid procedures from their own budgets or to implement the relevant functions only within the scope that is funded from the state budget.

Municipalities report on operations performed, rather than the results

When implementing state functions, municipalities report on performance in accordance with the procedure set by state authorities, namely – by furnishing their performance reports with quantitative information on operations performed, e.g., events organised, the number of participants in said events, the number of publications, etc., which means that such reports contain no information on qualitative results. For this reason, it is not possible for the state to assess the results achieved by municipalities with the state budget funds allocated to them.

Recommendations

To the Government of the Republic of Lithuania

1. In order the system of functions implemented by municipalities ensured their effective and resultative implementation:
 - 1.1. revise the system of functions implemented by municipalities and assess which of them are best implemented by the central government and which – by local government, and make the decisions necessary for the implementation of required changes (the 1st key audit result);
 - 1.2. assess the expediency of dividing functions into state (state-delegated municipal) and independent functions, and make the decisions necessary for the implementation of required changes (the 1st key audit result);
 - 1.3. in order to reduce the administrative costs related to the implementation of a part of the state functions, revise them and eliminate those functions which are of a temporary nature, implemented only episodically, and are either small in scale or performed only by several municipalities (the 1st key audit result).
2. In order to make the system of funding the functions implemented by municipalities motivate the latter to improve their effectiveness and strive for better performance:

- 2.1. revise the existing system for the funding of functions and assess potential alternatives to the funding of functions which could ensure the most effective way of their implementation (the 2nd key audit result);
- 2.2. establish that the allocation of funding to municipalities should be accompanied by the setting of objectives, indicators and expected outcomes (the 2nd key audit result).

To the Ministry of Finance

3. In order to ensure the uniform calculation of the total costs (remuneration, administration, etc.) related to the implementation of state functions, set uniform principles of calculation (the 2nd key audit result).

Measures and deadlines for the implementation of recommendations are provided on page 36 in “The Plan for the Implementation of Recommendations”.