

THE GRANTING OF DISCRETIONARY FINANCIAL ASSISTANCE TO MUNICIPALITIES AND ITS USE

The main question in the audit was to investigate the grounds on which discretionary financial assistance is granted to municipalities and whether they correspond to the objectives in the Act on Central Government Transfers to Local Government and also how the Ministry of the Interior has ensured the proper use of assistance.

As a whole discretionary financial assistance forms only a small part of the grants and assistance received by municipalities from the state. For certain municipalities the significance of discretionary financial assistance is quite large, however.

During the audit enquiries were sent to 60 municipalities and visits were made to 10 municipalities. These municipalities had applied for discretionary financial assistance for 2004. Consequently the matters that came to light in responses and visits cannot be interpreted as covering the views of all municipalities.

Statistical analyses were also made in the audit, based on financial information concerning all municipalities in 2000-2003 and application and grant information in 2000-2004. The analyses indicated that applications and grants depended on municipalities' financial situation and whether assistance had been received the year before.

According to the results a municipality was more likely to apply for discretionary financial assistance (adjusting for other factors)

- the smaller the amount of financial assets per inhabitant the year before
- the larger the amount of expenditure on social services and health per inhabitant the year before
- the smaller the annual margin the year before
- if discretionary financial assistance had been granted to a municipality the year before
- the smaller the municipality's tax revenues the year before

- the smaller investments per inhabitant the year before
- the smaller the municipality's population.

The analysis of applications is based on information concerning all municipalities. The results seem logical. The worse a municipality's financial situation, the more likely it is to apply for discretionary financial assistance.

In investigating factors influencing the granting of assistance, only municipalities that applied for assistance were included. The results indicate that the granting of assistance is more likely

- the greater indebtedness per inhabitant the year before
- the smaller financial assets per inhabitant the year before
- the smaller the annual margin per inhabitant the year before
- the larger net expenditure on social services and health per inhabitant the year before
- if assistance had been granted to a municipality the year before
- the smaller the rate of growth of operating expenses the year before.

These results also seem logical. The worse the financial situation, the more likely assistance will be granted. The results also indicate that even after factors describing a municipal's financial situation have been taken into account, whether or not assistance was granted the year before is a significant factor.

Assume that we have two municipalities A and B, which are in an equally poor financial situation according to the above indicators and apply for assistance in year t . Municipality A has received assistance in year $t-1$ while municipality B has not. According to the results, municipality A is about 10% more likely to receive assistance than municipality B. This does not seem fair.

In examining the amount of assistance granted (euros/inhabitant) and the relation between the factors used in the analyses, only municipalities to which assistance had been granted were included. An additional factor was the amount of assistance requested by municipalities (euros/inhabitant).

According to the results the size of assistance per inhabitant was directly related to the annual margin per inhabitant the year before. The relation was inverted, which means the larger the annual mar-

gin, the less assistance was granted. In other words, the more the annual margin ± 1 was negative, the more assistance was granted. The amount of assistance requested did not appear to have an influence on how much assistance was granted.

To summarize, the application for and granting of discretionary financial assistance depend on a municipality's financial situation and whether a municipality has received assistance in previous years, even when factors describing the financial situation have been taken into account.

On the basis of section 13 paragraph 1 of the Act on Central Government Transfers to Local Government, the primary reason for granting discretionary financial assistance is an exceptional or temporary difficulty in municipal finances. The Government Bill did not specify what an exceptional or temporary difficulty in municipal finances means or when such a difficulty is great enough to call for additional financial assistance.

According to the same paragraph, a municipality's special conditions can be taken into consideration in assessing the need for financial assistance. In 1997-1999 and 2001-2002 special financial difficulties resulting from the implementation of the Act on Central Government Transfers to Local Government could also be taken into consideration in granting financial assistance. In 2003-2005 there was no such provision.

In notifying the possibility to apply for assistance or deciding on the granting of assistance, specific information has not been given concerning the factors on which decisions have been based and what weight these factors have been given in granting assistance. Since a large number of criteria have been used, the procedure is not transparent. Nor has it been in compliance with the Administrative Procedure Act, since the Act requires that grounds must be given for this type of decisions. In the opinion of the State Audit Office, the broadness and vagueness of section 13 paragraph 1 of the Act on Central Government Transfers to Local Government and the fair treatment of municipalities require that all municipalities' financial information should be handled using the same criteria, which should be published in connection with decisions at the latest, and that in connection with decisions information should be supplied concerning what weight has been given to a municipality's special conditions and these should also be spelled out. The State

Audit Office considers the Ministry of the Interior's information on municipalities' financial situation and the tools used to analyse it adequate for preparing decisions.

The audit indicated that there are differences of opinion between the Ministry of the Interior and the Ministry of Finance concerning the reasons for municipalities' long-term financial difficulties. In the Ministry of the Interior's view, the reason for the financial problems of the municipalities receiving discretionary financial assistance is basically insufficient income financing. In the Ministry of Finance's view, insufficient income financing is not the cause of municipalities' financial problems to such a large extent, since the levelling of tax revenues raises municipalities' income level to 90% of the average tax revenue calculated according to the average tax rate.

On the basis of the responses received in the audit, municipalities have carried out many economy measures. The financial effect of these measures remained open, however. A positive thing is that one factor linked to the granting of assistance has been a lower than average rate of growth of operating expenses.

In recent years the Ministry of the Interior has imposed conditions on municipalities receiving assistance, but according to the audit it has not properly monitored compliance with them. Furthermore conditions do not include any sanctions in case they are not met. The State Audit Office emphasizes that in granting discretionary financial assistance the granting authority can impose a condition concerning the repayment of assistance even if this is not specifically provided in legislation. Therefore a condition requiring that discretionary financial assistance be repaid if a municipality fails to take the measures to improve the municipality's finances that are a condition for receiving assistance does not require the amendment of legislation. Although discretionary financial assistance forms only a small part of the assistance received by municipalities from the state, the amount of money involved is still significant and the Ministry of the Interior should make sure that assistance is used to produce the desired effects. For this purpose conditions must be realizable and sufficiently concrete, they must include sanctions and compliance with them must be monitored. This naturally requires that the ministry should have adequate resources for this purpose.

A significant portion of assistance has been granted repeatedly or almost repeatedly to the same municipalities. In the opinion of the

State Audit Office, this is justified if a municipality's conditions are constantly exceptional. In such cases the Ministry of the Interior should especially make sure that exceptional conditions are not due to the municipality's own measures or the fact that the municipality has not complied with conditions, however. In the opinion of the State Audit Office, placing a municipality's finances on a healthier basis should be the main goal in granting discretionary financial assistance. Accordingly it should also be possible to demand repayment if a municipality fails to take measures to improve its own finances.