

Auditing economic activities of regional and local authorities. Current challenges in Poland

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- ❑ The role of local and regional authorities in the state consists in performing, in their own name and on their own behalf, a substantial part of public duties.
- ❑ The scope of public duties entrusted to the local and regional authorities is roughly defined in Article 163 of the Constitution, in accordance with which they are to perform any public government's tasks not otherwise reserved by the Constitution or Parliamentary acts to other public authorities.

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- ❑ The commune (*gmina*) constitutes the basic unit of local government (Article 164(1) of the Constitution).
- ❑ The legislator has established district authorities (local authorities entrusted with the tasks of supra-communal nature) and provincial (regional) authorities.
- ❑ The commune enjoys a special role in the local and regional government system of the Republic of Poland since, under Article 164(3) of the Constitution, this type of local authority „shall perform all tasks of local and regional government not reserved to other units of local and regional government”. The constitution-makers have thus established the principle of the commune’s implied competence.

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- ❑ In performance of their responsibilities, the local authorities are empowered not only to establish their own organizational units but also to conclude agreements with other entities.
- ❑ A substantial part of the local and regional government's responsibilities is, however, carried out by the organisational units of local and regional authorities.
- ❑ A vast majority of them operate under the umbrella of the legal personality of a local and regional government unit (*statio municipi*) – as its budgetary unit or budgetary enterprise (organizational units of the local or regional authority).

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- ❑ Among the organizational units run by local and regional authorities there are also entities with a legal person status of their own (incorporated entities of local and regional self-government), in particular, the independent public healthcare institutions as well as the cultural institutions.
- ❑ In performance of their responsibilities, the local and regional authorities may also establish or become shareholders in commercial companies, join cooperatives or water management companies.
- ❑ Moreover, there are also other legal entities run by regional government, established under the Law itself (Regional Advisory Centres for Farming) or in line with the procedures specified therein (Regional Driver Training Centres).

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The normative catalogue of commercial company types that the local authorities may establish or join is given in Article 9 of the Municipal Management Law dated 20th December 1996. These are mainly limited liability companies and joint-stock companies, but also limited partnerships or limited joint-stock companies referred to in Article 14(1) of the Public-Private Partnership Law dated 19th December 2008 (Dz.U. [*Journal of Laws*] of 2009 No. 19, item 100 as subsequently amended), i.e. companies established in performance of public-private partnership agreements.

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- ❑ The concept of economic activity of the local and regional government relates on one hand to provision of paid services by organizational units of regional and local authorities and management of public goods, and on the other hand to acquisition of goods and services by those units, particularly under the Public Procurement Law.
- ❑ It is worth noting that the payment for services provided by the local and regional government's organizational units may come either directly from the beneficiaries (consumers) of those services or from special-purpose public funds, in particular the compulsory public health insurance funds.

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Regional Chambers of Audit in Poland carry out audits of financial management and public procurement process at:

- units of regional and local government (communes, districts and provinces),
- unions of communes and unions of districts,
- inter-communal associations, associations of communes and districts and associations of districts,
- organizational units of regional and local authorities, including those with legal personalities,
- other entities which have received grants originating from the local and regional government's budgets.

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Regional Chambers of Audit carry out audits of financial management and public procurement in units of regional and local government and their organizational units with regard to **legality and conformity of documentation and factual findings**.

These criteria, however, seem inadequate with regard to the economic activity of local and regional government.

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The only, and limited, possibility of expanding upon them is provided by the current wording of Article 44 (3)(1) of the Public Finance Law, which stipulates that **public spending should be carried out in an expedient and prudent manner**, in compliance with the following rules:

- achieving the best possible results from any given expenditure,
- selecting the best available methods and means to achieve established goals.

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It seems, however, that ensuring that local and regional communities have access to information on the relative costs and benefits of fulfilling the tasks of local and regional government is of most importance to the proper functioning of civil and open society.

In consequence, it seems important to grant the Regional Chambers of Audit the power to audit the economic activity of local and regional government using the criterion of economy of financial management (good management).

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The assessment of self – government's economic activities should focus on whether the established goals were achieved and what costs were created in the process. **An analysis of the economy of financial management would make it possible to determine whether the activities of the audited entity are expedient and prudent and whether it would have been possible to complete the tasks assigned with lesser expenditures or in a more effective manner.**

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The development of local and regional government's economic activity in Poland relates in particular to the increasing use of the incorporated company model for performing the tasks of local and regional government.

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It must also be noted that the Medical Activity Law dated 15th April 2011 stipulates that regional and local authorities must either cover the losses incurred by the independent public health care centres (SP ZOZ) managed by them or transform the centres into incorporated health care providers. Therefore, it is expected that in 2014 there will be a sharp rise in the number of health care providers operating as commercial companies. It is worth noting that there are currently nearly 600 hospitals and 1,700 outpatient clinics operating as independent public health care providers.

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- ❑ In this context, it is especially important to define the category of organizational units of local and regional government, and particularly of local and regional government's legal entity.
- ❑ In the judicial doctrine and case law, there are disparate views on whether it is possible to treat incorporated companies whose dominant or sole owner is a local and regional government as local and regional government legal entities.
- ❑ In accordance with the principle of legality, however, the powers of public auditing authorities should be expressly defined by the law. It is therefore not possible to presume auditing powers.

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As mentioned above, a significant proportion of local and regional government's tasks in Poland is carried out through incorporated companies. Furthermore, a significant portion of communal property has been transferred to such companies. Also significant is the process of 'debudgetisation of communal debt', whereby debt is incurred by municipal companies instead of local or regional government units.

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Municipal companies' debt is not taken into account when assessing whether local and regional government units' debt is within legal limits. Furthermore, as there are no reporting requirements, municipal companies' debt cannot be precisely assessed and currently is subject to estimations only. According to the author's research, in 2009-2012 municipal companies' debt was equal to approximately 20%-25% of the official debt of local government units in Poland.

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Including local and regional government commercial companies, particularly those created by transforming independent public health care centres, expressly in the remit of audits carried out by Regional Chambers of Audit would be an important step towards ensuring the transparency of public finance.

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Some of the other most important challenges in auditing the economic activity of local and regional governments in Poland are also the provision of an appropriate level of financing for the auditing activities of Regional Chambers of Audit and the provision of required knowledge and skills to the auditors.

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Including local and regional governments' economic activity carried out as commercial companies within the remit of audits by Regional Chambers of Audit would require a significant increase in the number of auditors and the costs of their activity. Meanwhile, Regional Chambers of Audit, along with all public administration in Poland, must be prepared to limit their cost levels in the coming years.

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Auditing the economic activity of local and regional governments' units requires different knowledge and skills from those required by auditing their administrative activity. This is particularly true of entities operating as commercial companies. Municipal companies are covered by private sector regulations. These entities also usually exhibit a different organizational culture. This may cause problems for auditors used to principles of operation employed in bureaucratic organisations.