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**Public Sector Transition in Post-Communist Economies:
The Struggle for Fiscal Decentralization in the Czech and Slovak Republics**

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Public Sector Transition in Post-Communist Economies: The Struggle for Fiscal Decentralization in the Slovak and Czech Republics

Introduction

Transition studies have often been studies of transitioning private sectors. How centralist governments withdraw from the business of micromanaging a nation's enterprises is a fascinating story indeed. The other side of the coin, how the public sector is to be brought to decentralization and democracy, is likewise of great moment for the peoples of the transitioning countries.

Under central planning the tradition was to provide all public goods and services under the direction of the central government and its ministries. There were no genuine subnational governments, since all policy decisions pertaining to taxation and the distribution of public services were made at the central level. The only work done at the subnational levels was "state administration," the local implementation of the central plan and will.

The process of fiscal decentralization, transitioning to a set of decentralized, democratic institutions, amounts to transforming the offices for state administration into legitimate subnational governments. It is achieved by granting local governments significant budget autonomy and some independent financial resources. It is a difficult task, given the natural tendency of the institutions, traditions and legacies of central planning to retain financial control over all levels of government.

This paper presents a comparative case study of the attempted devolution of power in the Czech and Slovak Republics. Identical institutions and traditions up to the "velvet divorce" of 1993 make them excellent subjects for comparative analysis. Their problems and experiences, moreover, are similar to those of other transitioning countries in east Europe.¹

At the end of the central planning era, transitioning countries had neither public nor private managerial elites, and they had no opposition party waiting in the wings. New managerial and political talent had to be found or developed to replace the old *nomenklatura*, the party elites and the entrenched bureaucracy, or new titles had to be found for the old faces. Only the new *Bundesländer* of

Eastern Germany could reasonably obtain new personnel from the new western partner, a possibility not available to the transitioning countries generally. So the personnel that manage the public sector transition are often those trained under previous regimes and they have a tendency to slow the devolution of power to subnational governments. As we shall see, the political environment and the centripetal forces inherent to center/periphery relationships would render decentralization extremely difficult even without the impetus of the actors and customs involved.

Initially, there was reason for optimism that fiscal decentralization would succeed in the two republics, for the Czech and Slovak people had manifest strong desires to reestablish independent local governments after the Velvet Revolution. As the transition progressed, decentralization bogged down, but after a time the prospect of accession to the European Union offered the possibility for new impetus for the process. Unfortunately, it gradually became apparent that the EU would not actually demand fiscal decentralization of the new member countries. The European Union was unconcerned that central governments were unwilling to devolve financial control.

The importance of EU membership was not lost on the Czechs and Slovaks, and they were anxious to accede. They accepted EU demands that candidates for membership develop viable democratic governments and market economies. They would also have been willing to respond to EU pressure to initiate fiscal decentralization. The Union, however, ultimately promoted an alternative to fiscal decentralization. It encouraged central governments to adopt substantive “reforms of public administration,” which established regional governments and sought to strengthen the independence of municipalities by modifying non-financial institutions.

As the accession occurs, the reforms in public administration (*reformy veřejné správy*) remain the only hope for devolution. The two republics have been convinced that regional governments should be introduced to bring government closer to the people, but the EU permits them to carry out the process according to their own inclinations. Whether fiscal decentralization can find a

worthy proxy in the establishment of the resultant institutional changes in municipal public administration remains to be seen.

Section I introduces some of the difficulties associated with the efforts of fiscal decentralization. It reviews especially some of the problems encountered in the change from local public service provision under central planning to the provision adopted by transitioning nations. The problems of local finance in the transition, *e.g.*, the use of the property tax and the provision of funds transferred to municipalities from the center, are addressed in Section II. Section III addresses the nature and potential of fiscal decentralization; it also reviews the potential moral hazard problems associated with that process. Section IV reviews some of the ways that fiscal decentralization is failing, in spite of the more hopeful transition developments. The role of the EU as a promoter of democracy and decentralization will be reviewed in Section V. This concluding section will inquire as to whether genuine local democracy can be achieved for accession states through the implementation of “reforms of public administration” rather than through fiscal decentralization.

I.

As in all other aspects of the transition from central planning to market democracy, the problem of overcoming the legacies of the former regime remains large. The problem is greater than the mere financial poverty of local governments in the region, which must wait on transfers from central governments bogged down in continual fiscal crises of their own. The problem also stems from the conditions and institutions of inter-governmental relations, which seem to guarantee a lack both of resources and of local autonomy.

In the private sector, the transition problems of central control and the soft budget constraint were generally addressed through privatization. But even with privatization, firms continued to enjoy the soft budget constraint by obtaining unjustifiable bank loans. The state tacitly supported this situation because it feared that if non-viable firms were permitted to disappear, as the

market would demand, unemployment and social unrest could undermine tender, transition governments.

In the public sector, the nascent democratic republics faced potential moral hazard problems that were partly a legacy of former planning institutions. These problems arose because the center was unwilling to inaugurate substantive change in the provision of local public services. Because certain aspects of the central planning system retain strong appeal to policy agents, they would prefer to continue to function as they did under the planning system. Specifically, policy agents preferred to keep taxes indirect and non-transparent. Non-transparent taxes allow policy agents to provide public services without political opposition. Under central planning, citizens were not aware of having to pay for services received and they are still disinclined to shoulder the fiscal burdens implied in public service provision. Thus, both citizens and public officials prefer that local public services be financed by transfers from the center rather than from taxation. Nor are central governments averse to the traditional ways; the state provides the funding for local service provision and retains complete control over the programs funded.

In the transition, the institutions of capitalist democracy represented a new philosophy and a new combination of social mechanisms for the provision of public goods. The new system obviously required relinquishing the former public sector system along with the specific menu of services and products previously provided. During the socialist period, not only public, but also several kinds of public and even quasi-private goods were provided directly to the workers through state-owned enterprises. In humanizing their formerly capitalist production units, communist governments caused state-owned enterprises to provide much of the housing, health care, nursery care, vocational training, general education, recreation, and even sports and vacation facilities for workers.² And to make this model function, the state willingly retained a soft budget constraint for such enterprises, funding their generous service provision³ while supporting their well-publicized production inefficiency.

It is not surprising that the transition's demand for hard budget constraints produced open (rather than disguised) unemployment. The state had been subsidizing its enterprises to retain superfluous workers on the payroll for many years prior to the decline of central planning. But not only were jobs lost with the advent of the transition, privatization and marketization caused the now-private firms to cease providing the goods and services once accepted almost as "entitlements." Naturally, citizens *qua* consumers were not unwilling to forego generous public goods provision at the outset of the transition, since they anticipated that their long-pent-up demands for the much richer menu of private goods common to market economies would now be satisfied. The generosity of socialism was relatively greater with respect to public goods than private goods, so consumers were expected to forego for a time such things as excellent schooling, health care, and housing. The willingness to wait, however, was predicated on more abundant provision of private goods, such as electronics and automobiles, which had been in very short supply under central planning. Nor could that willingness be expected to last indefinitely.

To this point in time, the transition has not greatly improved the provision of public goods and services. Limited resources have affected the public sector in both republics, although the Czech Republic has done better in terms of the transfer of funds to subnational governments than have the Slovak Republic and some other countries of the region. In spite of the somewhat more copious provision, the development of genuine autonomy for local governments has not been a Czech priority.

Perhaps statist-socialism trained the peoples of east and central Europe to be very patient indeed. Perhaps supplying the municipalities of transition countries with an acceptable volume and quality of public services can be postponed almost indefinitely. But it is still not clear how countries that are anxious for association with the EU can indefinitely underfund local public services. The transition to democracy, market economics, and self-determination at the local governmental level suggests that the question of municipal finance must be addressed in a more satisfactory manner.

II.

Under central planning, local administrative offices were required only to implement state plans. Local autonomy, so highly valued by Czechs, Slovaks, and others in east Europe, was lost until the post-communist era began in 1990. This section begins a review of progress since that time, and suggests that decentralization has to this point been suboptimal.

As in other transition countries, Czechoslovakia began the attempt to decentralize its fiscal system immediately after the transition began in 1990. Legislation to establish taxation and budget systems of a more Western-European type was passed early in the transition and bore some of the flaws expected of a rush through parliament.⁴ This is at least one reason that fiscal crises in the two transitioning countries have been common since the downfall of communism and that transfers of funds from the center to the subnational governments have generally been insufficient to cover the backlog of needs. Municipalities have not been able to function with anything approaching full effectiveness. But the problem has been more than having insufficient funds for public service provision. The municipalities have also been unable to enjoy genuine autonomy, especially because they have insufficient sources of independent revenue. In the Czech and Slovak Republics, one of the primary difficulties is that the property tax, the traditional western source of independent finance, has not been modernized. Especially in the Czech Republic it remains basically the purely symbolic and ineffectual tax that it was under central planning.

The movement of the former central planning regimes to a more distinct market orientation parallels the less distinct movement of a number of developing countries away from an import-substitution model of economic development to a more open, market orientation. The general view that greater reliance should be placed on markets rather than any kind of statist activism is paralleled by the view that less power should remain in the hands of the federal government.⁵ But power devolution is not a part of the instincts of either central or municipal agents in central and eastern Europe.

Advocates of strong central government see the municipalities of transition countries such as the Czech and Slovak Republics as being either incapable of fiscal autonomy (largely due to the very small sizes of many of them), or as failing to demand or require it. It is true that many of the municipalities and townships of the Czech and Slovak Republic are very small. Within months of the Velvet Revolution of 1989, Czechoslovakia permitted villages and towns, many of which had been arbitrarily amalgamated under the previous regime, to declare their independence. This dramatically increased the numbers of independent municipalities in Slovakia, Moravia and Bohemia. Many of these towns are too small to manage self-government, lacking in technical abilities and resources, lacking a viable fiscal base, and lacking scale economies in the provision of public goods and services.

Many of these towns and villages are now seeking solutions to their resource problems by joining in strategic alliances with other small towns and sometimes even with cities in their proximity. These alliances are proliferating and are endorsed and promoted by the central government. For example, one village can provide a primary school (*mateřská škola*) for several contributing neighbor communities who will bus their children to the school site. A partner town might supply a care facility for seniors from several nearby communities. Another, similar arrangement offers an interesting example in Southern Bohemia where the mayor of *Hluboka nad Vltavou* simultaneously serves as the mayor of eight nearby towns and villages and assists them with their public service provision.

But insufficient population is only one of the problems facing the municipalities of the twin republics. Problems of horizontal and vertical fiscal imbalance confront almost all subnational governments in both developed and developing countries. Horizontal fiscal imbalance is the product of unequal resource availability in municipalities. Vertical imbalance becomes apparent where central governments capture the lion's share of the taxable sources, leaving subnational governments with insufficient "free resources" for the independent pursuit of tax revenues.

A lack of trust in government is another important problem in the transition. The processes and outcomes of decentralization will not only enhance the efficiency of public services, but will increase trust as government is brought closer to the people so that citizens participate more effectively at low cost.⁶ Trust will also increase as government processes become more transparent. The ideas supporting this view of decentralization have a long history in the public finance, public choice, and public management literatures.⁷ Successful decentralization requires effective performance of a set of complex tasks, both by those agents who relinquish and those who acquire new tasks and prerogatives. The reassignment of personnel and responsibilities, often with a reduction in services, is not always easy for citizens to understand and support.⁸ In the best of circumstances, trust takes time to be established and grow.

For fiscal decentralization to succeed, local governments must have access to an autonomous source of tax revenue, *i.e.*, they should not be dependent upon the center for all revenues.⁹ Local activity tends to be more visible, as are the policy and other choices made by elected and appointed public officials, and as visibility does, accountability increases as well.¹⁰

The literature suggests that the property tax embodies the positive characteristics required of a local tax:

- The property tax is immobile (taxpayers can't evade it by relocating their transactions beyond a relevant political border).
- The property tax is stable (it provides reliably constant revenues independent of the business cycle).
- It is potentially neutral (its imposition does not cause changes in the utilization of the services of taxed properties).
- The tax can be designed to fall on taxpayers who presumably have the means and the ability to pay (they are home owners and property holders). Excise taxes, for example, can be regressive, representing a larger portion of lower than of higher incomes.
- As local public services improve and increase property values, the beneficiaries are required to pay for the increased value.
- as a direct tax, it is visible to taxpayers¹¹

Unfortunately, because visibility is sometimes a political liability, the design and implementation of an effective property tax is challenging. Since it is direct and visible, it makes citizens and officials less comfortable than do indirect taxes such as the VAT.¹² Both citizens and officials usually prefer the pursuit of revenue through the use of excise taxes and local fees on a variety of transactions.¹³ For local officials, the property tax too often generates political problems.¹⁴

There are also administrative and practical problems with property tax implementation. Examples of the latter include the difficulty of establishing market-oriented property values in the absence of a functioning real estate market¹⁵ and coping with the uneven distribution of the property tax base.¹⁶ As a consequence of political and practical issues, the property tax remains critically under-used,¹⁷ especially in the transition countries; this can be an impediment to successful decentralization and undermine the welfare gains expected from that process.

For many reasons, transitioning countries often fail to realize substantial receipts from the property tax. Because cadastral data are generally poor and collection and enforcement efforts are weak and inconsistent, local governments in transition countries have rather consistently been under-funded and overly dependent on transfers.¹⁸ Even when local governments effectively harvest modest to meager property tax yields, inflation and time quickly erode them when they are indexed neither to inflation nor to economic growth. The services local governments provide for fees also generally fail to produce significant revenues in the face of significant resource needs. They are usually little more than nuisance levies that may cost more to collect than they yield in revenues.

Fiscal decentralization can be successful only if at least the following three conditions hold. First, there must be a correspondence between the expenditure responsibilities of local governments and the necessary financial resources available to perform them. Second, the autonomy of subnational governments must be increased by permitting them to mobilize their potential resources and by providing incentives for them to do so. Third, the system for providing transfers to them

must be transparent and based on objective and consistent criteria, rather than through negotiation and ad hoc bargaining.¹⁹

III.

Because there are marked divergences between the perspectives and incentives of central and sub-national governments, principal/agent conflicts are common. Naturally, agents tend to pursue their own interests rather than those of the principal; in part, doubtless, because agents tend to regard themselves as principals and their own prerogatives as most important. In the case of local finance, municipal government can generally be considered the principal, simply because it most proximately represents the real principal of democratic political processes, the citizenry. The central government is the agent, which serves the principal; in this case the center accepts the responsibility of collecting property tax revenues for the municipalities. The local government principal receives such revenue as a result of the agent's actions, but the contractual rules do not let the agent central government share in the revenues, in spite of its collection efforts or its superior resources and position. In the Czech Republic, this specific situation applies, and as in many principle/agent relationships, moral hazard problems are the result.²⁰

The sub-national governments, desperately needing funds, can merely hope that the center will exert significant effort in administering the property tax, since they do not share in that responsibility. Nor are they in a position to monitor tax administration closely. From their perspective the outcome will be far from optimal, since the center has different incentives regarding property tax revenue and the exertion of effort and resources to generate it. Naturally, smaller property tax revenues can be offset by greater transfers from other taxes or revenue sources. To the extent that the center compensates for its lack of effect in generating property tax revenues, local governments are *financially* no worse off, but the alternative revenues consistently come with strings attached.

Clearly the central government has a role in property tax policy design, but the Czech centralization of the tax's implementation creates the potential for incentive incompatibilities and the eventual failure of the property tax. Even attractive, smart policy and administrative designs cannot assure that a tax will succeed in the face of incentive incompatibilities.²¹

An additional potential for moral hazard problems emerges when the central government transfers revenue to local governments. Fiscal redistribution is justifiable when the distribution of resources is badly skewed across subnational governments, or if subsidies encourage local governments to pursue activities of high priority to the center.²² However, if transfers from the center simply offset revenues that could have been raised locally, there is an additional twist on the moral hazard problems already described.

If the central government compensates the municipality for the property tax funds it has failed to collect, the compensating revenues are not encumbered with political transparencies dangerous for local officials. With the more transparent property tax, local officials run the risk of incurring political opposition. This is particularly true for local governments in the transition countries where central planning kept taxes both indirect and invisible. Obviously, when taxes become visible and direct, they can certainly impact local elections.

When transfers are provided by the center as an alternative to local taxation, municipalities may conveniently abdicate fiscal power, relinquishing their own autonomy because central revenue provision is so convenient. Here the local government should be functioning as the proximate agent of local citizens and is in a situation fraught with moral hazard problems. It shares responsibility for the revenues foregone, as well as for the loss of local independence as central influence on local service provision will usually accompany transfers of alternative funds. The consequence of these actions is that the importance and effect of the property tax are diminished, as is the potential for local fiscal autonomy.

IV.

Applying these theoretical considerations to the Czech and Slovak fiscal situations leads us to inquire which of the two governments has been most successful in terms of local finance, and why. The Slovak Republic has administered its property tax locally; the Czech Republic has administered it centrally. The Czech Republic, having chosen a centralized approach to property tax administration, transfers substantial amounts of funds from the national to the local governments, while the Slovak central government has been far less generous.

Budget data are presented in Table 1. Under central-planning from the late sixties onward, the Czechoslovak federation's local governments derived roughly 60% of their total receipts from subsidies. Beginning in about 1984, they experienced a gradual decline in central government subsidies, a trend that extended beyond the opening to market economics and democracy. Although there was a brief expansion of transfers from 1990-1992, the decline continued thereafter. After the mid-nineties, subsidies represented no more than about twenty-five percent of the total receipts of Czech and Slovak municipalities.²³

Table 1 shows the financial situation from the end of central planning through the year 2000. The data indicate that Slovakia's municipalities enjoy considerably less revenue than those of the Czech Republic. From 1993 on, after the Velvet Divorce, Czech municipal budgets were more than twice as large as those of Slovakia, even without considering the greater value of the Czech crown. In the Czech Republic the aggregate of local budgets is from one quarter to just over one-third of the national budget. Local budgets in Slovakia are only about fourteen percent of the total national budget.

A comparison of central government grants to municipalities reveals the reason for the relative poverty of Slovakian municipalities. Grants in Slovakia ranged from 1.5 billion Ks (Slovak Crowns) in 1993 to 1.1 billion Ks in 1994. The grants paid by the Czech central government to the

TABLE 1 here

municipalities ranged from just over 27 billion Kč (Czech crowns) in 1993, to 59.5 billion Kč in 1996. Interestingly, in the years just prior to Slovak independence (1991 and 1992), the government in Prague provided grants of 7.9 billion and 2.4 billion crowns respectively for Slovak municipalities. Independence from the Czechs turned out to be a shock for the municipalities of the Slovak Republic, for it separated them from the Czech central budget.

Slovak cities also discovered that the strange politics of the Mečiar era would not only separate them from the Czech, but also from the Slovak central budget. Mečiar was interested in the “family privatization”²⁴ of Slovak industry, but not in helping solve the problems of Slovak towns, cities, and regions. Cities recognized that they would be forced to solve their own fiscal problems, for there would be no significant resource flow from the center to the subnational governments.

In the Czech case, the central government’s ongoing efforts to fund the cities and towns include revenue sharing and financial grants. As Table 1 indicates, grants have been very nominal in the Slovak Republic. Table 2 provides data for an overview of the more significant efforts of the Czech Republic. Note especially the tax revenues accruing to local governments as a percentage of the Republic’s consolidated budget totals. Local tax revenues were only 13.6% of total budgets at the beginning of the period in 1994. From 15% in 1995, the share declined for three straight years,

Table 2 Here

reaching a low for the period of 12.8% in 1997. It increased over the next three years, reaching an all-time high in 2000 of 15%.

In the early years the Czech central government transferred to the local governments a considerable share of the personal income tax revenues that it collected. In 1994 and 1995, municipal governments received 89% and 87.6% respectively of those revenues. In 1996 the share dropped to 63% and remained at that level. Corporate income tax followed a contrasting pattern,

with the center initially transferring only a small portion to the municipalities. In 1994 only two tenths of one percent of corporate income tax revenues accrued to local budgets, increasing quickly to the level of over twenty percent. It increased only gradually up to 26% from 1996 to 1999, reaching 31% in 2000.

Inter-governmental grants have been an important and increasing source of funding for Czech municipalities. Because of the greater importance of such grants, it will be helpful briefly to document them here. Grants have represented roughly a quarter of the budgets of the local governments since 1994. They constituted 22% of total accessible funds in 1994 and 29.8% in 1997, declining to around a quarter of the total for the remainder of the decade, holding at 25.7% in 2000. Over the past decade, the joint contribution of transfers and shared taxes has remained at roughly 70 percent of local government revenues, but it remained true that a “meaningful degree of tax autonomy for local authorities was still missing”.²⁵

As compared to most other European countries, including other transition countries, the Czech Republic is unique in that it offers no equalization grants to districts or municipalities. Nor did reforms in 2000 make any provision for such grants. There is instead a complex system of conditional grants or subsidies which transfers funds to promote central government policy objectives. Since such funds are targeted for specific purposes, local governments must follow directives and report on the specific uses for which moneys were spent.²⁶ It should be noted, however, that the relative importance of earmarked subsidies is declining; they provided only 24 percent of all sub-national government revenues in 1999.

Currently, earmarked grants are of two types. Categorical grants are the first of these; they fund tasks delegated by the center to municipalities. They must be spent on specific, well-defined programs and require no matching funds from the municipalities. Distributed generally on a "per head" basis, they cover outlays for social assistance, early education, hospital and assistance institutions, fire brigades, and the execution of general government services including registration

and permits. Categorical transfers are used by central governments *inter alia* for redistributing fiscal resources, countering externalities, adjusting for vertical imbalances, and promoting local government expenditures in support of national programs. If unconditional grants were used rather than categorical transfers, central authority would demonstrate greater respect for the decision-making autonomy of local government officials. The nearly exclusive use of earmarked grants suggests the central authorities' belief that they have identified all local level priorities and that they possess better information on local needs than local officials do.

Capital transfers represent the second type of earmarked grant. They originate from the central government general budget and from the State Environmental Fund to accomplish a variety of purposes, including *inter alia* fire protection, natural gas distribution, schools, development of industrial zones, hospitals, water and sewerage treatment plants, and public transport. Matching funds are required of the municipalities for all centrally supported capital infrastructure projects, except for the building of new social care institutions.

Capital transfers from the State Environmental Fund are for environmental purposes, *e.g.*, to fund water supply systems or to introduce gas, flood control, and energy conservation measures. Matching funds of at least 20 percent are required of the subnational governments at rates set by the state agency. In 2001 the State Environmental Fund transferred a share of about 7 percent of the Republic's total capital transfers for that year.

Specific transfers have been funded in such a way as to supply a negative incentive for municipal revenue generation. The central government apparently reduces the level of discretionary transfers systematically as local governments increase their own revenues. The allocation of grants conditionally and at the discretion of central authorities tends to be less efficient and fair than through the use of objective formulas or well-publicized legislative procedures and criteria. Discretionary central systems can be distorted by pressures from lobbyists representing local governments or by parliamentary members defending or lobbying for local interests. Oliveira and

Martinez-Vazquez suggest, as an alternative to project by project application processes, that local governments develop comprehensive expenditure plans for evaluation and funding to the extent of the center's budget possibilities.²⁷

Clearly, budget transfers from the center give the Czech subnational governments considerably more fiscal and governing options than are available to those of Slovakia. Nevertheless, because such a large share of Czech municipal funding comes from the state, Czech municipalities enjoy less budget autonomy. Although local independence brought poverty to Slovak municipalities, it also placed them under a hard budget constraint with a large measure of budget autonomy from the center. By forcing them to be more responsible for their own revenues, the Slovak Republic caused its municipalities to pursue increased property tax yields for their revenue needs. They needed no instruction that this revenue source should be a primary one anyway. Probably as a result of these developments, there is more of a spirit of autonomy at the municipal level. Čapková confirms that Slovakia's local governments have substantial powers, including the right to enter contracts with private or public partners, buy and sell property, borrow money, and establish various kinds of businesses.²⁸

In contrast, the Czech Republic has tapped resources other than the property tax to fund municipal services. More generous provision of fiscal grants and transfers to Czech municipalities appears to avoid the need to develop the property tax as a revenue source. But in the meantime, the Czech government has failed to provide any foundation for genuine local autonomy.

Over time, local governments in both republics will face substantially greater revenue needs for current operations and a heavy backlog of needed investments. To this point, local governments in both countries have sold off the public housing and commercial properties transferred to them by the central government early in the transition. This has been the source of considerable revenue, but a disappearing one as assets capable of being privatized become increasingly scarce. Even this source

of funds has not permitted municipalities to avoid ongoing revenue shortfalls. The problem will continue to become more serious until the municipalities are vouchsafed more adequate sources of revenue.

Since the transition period began, both republics have struggled with periodical fiscal crises. A natural response from the central government has been to reduce revenues to the municipalities, while assigning additional service provision responsibilities to the local governments. Numerous unfunded federal mandates merely reflect this kind of transfer of responsibility from the center. In fairness, the Czechs have not been as guilty of that offense as Slovakia and most other transition countries. But even when the Czech government funds centrally mandated programs, the consistent retention of strong influence over the use of those funds undermines the development of local autonomy.

In Slovakia, further development of the property tax could help provide the fiscal resources that will produce strong local autonomy, and it is apparent to specialists that the Republic does intend to move in that direction.²⁹

Given the relative largesse of the Czech Republic toward its subnational governments, one might view the lack of a serious property tax as being of no large consequence. The European Union has accepted the Czech level of funding as evidence that the Czech Republic is developing satisfactorily as a modern democracy and should be admitted as a full member of the EU.

In our view, this perception is too narrow. In the first place, the fiscal needs of the municipalities are not properly taken care of, even though the needs are not as great as those of Slovakia and numerous other transition countries. And there are other significant problems in the fiscal decentralization process of the Czech Republic, the primary one being that the central government fails to promote local autonomy.³⁰ The center has not gotten far beyond the tendency of the central planning era to rely on local agents only for state administration (*přenesena působnost* in

Czech, similar in Slovak). The center generally establishes the policies, allocates the funds, and gives very specific directions on how local officers are to utilize the funds.

The spirit of intergovernmental relations can be observed from the administration of public housing. After the Velvet Revolution in 1989, the central government turned public housing over to the municipalities. The buildings were of notoriously poor quality and in need of major expenditures, but they were transferred without the funds to maintain or repair them. Housing units have been privatized to some extent, and that provides a supplementary revenue source for the municipalities, but housing rents and tariffs on such public utilities as water and gas are still regulated by the central government, and they are held at levels below full cost recovery. Likewise, the salaries of local government employees are controlled by central government,³¹ so central policy preferences for under-collecting fees and over-paying employees can force the municipalities to operate in the red.

Under democratic governments, municipalities generally have the responsibility to develop their own capital infrastructure. In the Czech Republic, however, local governments remain fully dependent upon the central government to fund capital expenditures. Such funding takes the form of various grants and subsidized loans. Municipalities can often suggest projects they would like to see funded, but the center will determine which projects are selected and establish the terms and conditions upon which the funding is contingent. This practice, too, could be described as state administration.

It should be observed that this situation is mitigated to some extent as the Czech Republic has avoided the imposition of substantial unfunded mandates on local governments.³² Delegated functions usually obligate the Czech central government to guarantee full funding and to transfer adequate resources for any new projects. There have been exceptions to these rules, *e.g.*, when a recent transfer of the responsibility for issuing personal identification cards and passports was transferred to local governments without funds for the project. A more high-profile case was the

transfer of public housing referred to above. In a sense, retention of control over the pricing of transferred service responsibilities is also an unfunded mandate. The center's unwillingness in such cases to demand normally appropriate fiscal performance, when their own policies make that impossible, explains why soft budget constraints develop for local governments and why there is an occasional need for bailouts. Subnational governments cannot be expected to meet financial obligations if the financial requirements of assigned tasks exceed the available funds. The municipalities become hostage to their administrative directors in central government, but avoid full financial responsibility by partnering in their administrative practices.

V.

The European Union could easily place pressure on the Czech and Slovak Republics to engage in a more sweeping process of fiscal decentralization. These systems retained aspects of their centralized character beyond the era of central planning. Both the Czech and Slovak governments respond willingly to instruction and pressure from the European Union.

Basically, the EU is in a position to dictate reforms to countries aspiring to membership. Indeed, EU membership requires that a country achieve stability of institutions guaranteeing democracy, a functioning market economy and the capacity to cope with competitive pressure and market forces within the Union. Clearly, a guarantee of democracy's implicit demands for local autonomy would be an appropriate EU requirement for prospective accession countries. To expect fiscal reforms of aspiring transition members is appropriate for the EU, and one would likewise expect willing compliance both from Bratislava and Prague.

Unfortunately, it cannot be said that the EU requires fiscal decentralization. In its initial country report recommending the Czech Republic for ultimate accession, the budgetary and finance systems were addressed, but questions about them were limited to the financial control system. Concern was expressed only about the Supreme Audit Office which the Czechs had created in 1993;

the system of internal financial control did not correspond to EC provisions for member states. When the Czech government expressed its intention to improve budgetary control, the EC declared itself satisfied.³³

In the 2000 Regular Report³⁴ by the Commission on the Czech Republic's Progress towards Accession, the ongoing failure to enable the development of local autonomy is not mentioned by the EU as a subject of concern.³⁵ The problems of general funding levels, the nature of financial transfers from the center to local governments with extensive strings attached, and disinterest in local government capacity to generate any autonomous revenues, are all testimony to the failure to take seriously the problem of local autonomy. On the basis of a continental, traditional bias toward centralization, the EU does not find the Czech fiscal system a barrier to membership.

In fairness, it must be recognized that the EU has used its influence in the sister republics to seek greater local autonomy through a different initiative – an organizational “reform of public administration.” A brief review of some of the principal endeavors to effect these reforms might demonstrate that they represent a legitimate alternative to fiscal decentralization. It is obvious that the intent is to enhance the efforts to achieve genuine democracy and local autonomy.

The main thrust of organizational change is the reorganization of subnational territories. The former districts (*okresy*) have been eliminated and new regional governments (*kraje*) have recently been established in both republics, which had previously been two-tier systems of government. The *kraje* are currently being phased in, and for a transition period will be funded by transfers from the state budget. It is intended that the regions inherit some of the state's former responsibilities, *e.g.*, secondary education, regional planning and inter-city transport.³⁶ The functioning of the new regions will likely become an important part of subnational government activity.

As the new millennium began, the Czech and Slovak Republics were feeling the chaos³⁷ of a comprehensive reorganization of subnational governments. As a part of a reform of public administration anticipatory of accession to the EU, both countries were moving from two-level to

four-level governments. Regional governments were established between the traditional municipal and central government levels. This entire national structure was also to be subjected to a fourth tier, that of the European Union in Brussels. The latter step is not the topic of this section, the intent of which is merely to consider some of the implications of the establishment of the regional governments for the sister republics. Fortunately, painting with a broad brush obviates the necessity of separate explanations for quite similar public administration reforms in the Czech and Slovak Republics. Accuracy can be retained by indicating the more important, distinctive properties of the one or other republic's reform endeavors.

The goal is to modernize central administration and provide "territorial public administration" to improve the quality of the public sector's products as a whole.³⁸ Regional governments are ostensibly to "bring state administration to the people" (*přiblížit státní správu občanům*)³⁹, to involve rank and file citizens in subnational governance processes. It is implicitly, sometimes explicitly admitted that what has gone on before has been the functioning of hyper-centralized governments.

Having decision processes regarding regional schools, health-care centers, land-use policies, etc., move away from Prague or Bratislava and closer to the citizens affected implies a devolution of central powers. The question that must be asked of the reform effort is whether an institutional reorganization of governance in the Czech and Slovak Republics will obviate the need for fiscal decentralization. Can the process of bringing the institutions of policy decision-making closer to the people substitute for providing the municipalities of these countries with fiscal autonomy?

One thing the reforms did imply was that a lot of reorganization would be necessary. Previous to the reforms, the state implemented its policies not only indirectly through cooperation with self-governing municipalities, but directly as well. It implemented its own policies at the top level of the hierarchy directly, through district offices at the middle level, and with work contracted

out to municipalities authorized and more-or-less compensated to perform “state administration” (*přenesená působnost*) at the bottom level.

On January 1, 2003, the Czech Republic closed 73 district offices (*Okresy*), transferring most of their activities to 205 newly designated “cities with expanded functions” (*obce s rozšířenou působností*).⁴⁰ These cities had already been authorized to assume the functions of the old District Offices. They had received new office space, information equipment, furniture, contractual compensation for the performance of expanded functions, and training for the public officials involved. Many of the latter had been transferred from the now defunct *okresy*. Never mind that the furniture and computers hadn’t all been delivered yet, that the space acquired from district offices was badly dilapidated, that the training remained incomplete, and that the prospective compensation was somewhat less than the anticipated costs.⁴¹ As officials had pointed out, there had been no transition period and a better reckoning of costs would be achieved with experience.

A significant menu of activities was transferred. Specific tasks assigned to the cities with expanded functions included the issuing of permits, IDs and driver’s licenses, decisions concerning historical buildings, conscription duties, alimony payments, state social and unemployment support, and on and on.⁴² While the 205 towns carry out these tasks of “state administration” in their role as agents for the central government, they still have to perform their own tasks of “public administration” in their role as agents of self-government (*samospráva*). For state administration they receive compensation in part through user fees paid by citizen recipients of public services, but mostly from the central government, which also retains the responsibility for the quality of the services provided.

Interestingly, in pre-reform Slovakia *samospráva* was performed by elected municipal officials while, under a separate roof, local state administration was performed by agents of the central government. Some indication as to the volume of resources committed by central government to local state administration can be inferred from employment figures. Before the implementation of

the public administration reform in 2000, no less than 287,817 Slovak citizens were employed in state administration (84.7% of total government employment), while only 52,100 (15.3% of the total) were employed in self-governments. After the reform was implemented, the share employed in state administration declined to 37.1%, while the number employed in self-governments increased to 62.9%.⁴³ Expressed in terms of Slovak crowns in public budgets, the contrast is even starker. In 2001 the combined expenditures of local state administration offices were 58 billion Ks. The aggregate spending of the self-government offices in that same year amounted to only 30.6 billion Ks.⁴⁴ Thus, expenditures for the tasks of the center at the local level were nearly twice as great as those for the tasks of the independent municipal governments.

In a government paper issued by Bratislava on the conception and design of reform institutions, a preference was expressed that state administration performed at the local level *after* the reform should still include the following: the police force, criminal investigation, military administration, the state veterinary office, the state hygienist office, the environmental office, the cadastral office, the land and forest office, the social office and the tax office.⁴⁵ This is an impressive list of activities for which, even after the implementation of the reform, the Slovak municipality was to have neither management nor responsibility. The Slovak municipality, as expressed in a previous section of this paper, received little funding but rather liberal managerial authority. Unfortunately, many traditional municipal functions were performed as state administration by central government agents. The municipal governments were largely left alone, but only within the very restricted sphere of public service tasks the center chose to assign them.

The Slovak national government intends for this situation to change⁴⁶ and the reforms will certainly move the cities and towns in the direction of change. The Slovaks have likewise recognized what real change will require. That recognition provides an answer to the question that introduced this section: can a reorganization of institutions be an effective substitute for fiscal decentralization? Of course the answer is no, since the effective governmental organization and fiscal decentralization

are complements rather than substitutes. The Slovak central government indicates that decentralization of public affairs has three dimensions: “decentralization of functional responsibilities, decentralization of finances, decentralization of political power.” Moreover, “decentralization can only bring benefit for the citizen if it is implemented in all three dimensions at the same time. The implementation of only one of the areas, for example, the decentralization of competencies without financial decentralization, will have a reverse effect. Therefore the process of decentralization must be complex.”⁴⁷

To establish regional self-government to exercise political choice through freely elected representatives does indeed move government closer to the people. Lacking the empowering fiscal capacity to finance local choices, however, severely constrains the freedom of action of subnational governments.

A high-profile Czech government document provides ample hints that insufficient fiscal autonomy will remain a problem. Bureš *et al* tell us in behalf of the Ministry of the Interior (*Ministerstvo Vnitra*) that municipal “own revenues” are critical in fiscal decentralization and that the biggest issue in that area is local fees, which admittedly “do not fit the actual needs of municipal economic regulation.” They admit likewise that apart from taxes, “municipalities and regions have also at their disposal other own revenues” stemming from the privatization of their own properties and from the property tax. The fiscal problem is addressed⁴⁸ because it is recognized that there is an unavoidable fiscal dimension to the reform of public administration as mentioned by the Slovak Ministry of the Interior. But the Czech Ministry of the Interior has no answer to the implicit question as to whence the financial resources will come. When mentioning that local governments are “temporarily financed mostly by subsidies (grants)”⁴⁹, it is asserted that “the aim is to strengthen their own tax revenues. Presently, the rate of regional own revenues to subsidies is circa 1:6.” No more is said about how this task is to be accomplished.

One notes that this statement is made by the Interior Ministry, not Finance. In the latter, which has the responsibility for fiscal decentralization, discussion between the Ministry and the parliament about possible changes in the property tax will need to find closure. Such an attempt was made several years ago, but failed. The parliament is currently also considering whether municipalities should be given permission to increase the fees charged for some local public services. This action, however, would provide no more than a nominal increase in local fees, which represent well under five percent of local budget receipts, and would not provide any substantive enhancement of fiscal autonomy.

In Slovakia, the Finance Ministry has announced plans to make adjustments *inter alia* to the real estate transfer tax.⁵⁰ As is well known, this may be among the least of Slovakia's unique taxation initiatives. This is not the place to elaborate on Slovakia's adoption of a flat tax such as that recently adopted in Russia and widely discussed in eastern and central Europe.⁵¹ But the Ministry does refer to the flat tax plan by observing that "progressive taxation should change to taxation by unified rate."⁵² Most significant is the observation that the share of revenues from property taxes is considerably lower than in the OECD or EU countries. As a result, the ministry intends to "focus on their strengthening."⁵³ Once again, although the Czechs usually seem to achieve bigger and better things, in the case of fiscal decentralization the Slovaks keep threatening to get it right.

TABLE 1
National and Local Budgets: Czech and Slovak Republics
Slovak Republic

	1993	1994	1995	1996	1997	1998	1999	2000	2001
Public Budget TR*	238.03	221.71	258.22	273.30	284.43	292.67	332.38	344.47	353.36
National Budget*	224.79	207.56	242.54	253.76	264.32	273.76	314.56	324.40	330.40
Local Budgets*	13.24	14.15	15.68	19.54	20.11	18.91	17.83	20.08	22.96
Local Budget as % of National Budget	5.89	6.82	6.46	7.70	7.61	6.91	5.67	6.19	6.95
State Grants to Local Budgets*	1.521	1.08	1.19	1.266	1.785	2.079	2.235	2.77	3.82
Grants as % of Local Budgets	11.48	7.63	7.59	6.48	8.88	11.0	12.54	13.78	16.63
Total Local Revenues*	15.41	14.73	16.32	19.54	20.13	18.92	17.85	20.15	23.06
Real Estate Tax*	1.61	2.03	2.05	2.88	3.14	3.21	3.36	3.61	3.69
RE Tax as % of Local Revs (%)	10.45	13.81	12.57	14.73	15.60	16.97	18.81	17.89	16.00

#Provisional

*Billions skk, czk

*Slovak State Grants in 1991: 7.961, 1992: 2385

Czech Republic

	1993	1994	1995	1996	1997	1998	1999	2000	2001
Public Budget TR*	422.00	470.20	522.00	562.80	592.50	637.70	666.80	707.80	852.90
National Budget*	358.00	389.10	428.40	464.20	487.70	518.10	549.00	568.50	732.70
Local Budgets*	91.10	112.00	130.00	163.80	145.30	157.20	165.60	181.80	192.40
Local Budget as % of National Budget	25.45	28.78	30.35	35.29	29.79	30.34	30.16	31.98	26.26
State Grants to Local Budgets*	27.03	31.00	34.80	61.50	35.90	37.40	41.40	46.10	67.30
Grants as % of Local Budgets	29.67	27.68	26.77	37.55	24.71	23.79	25.00	25.36	34.98
Total Local Revenues*	63.00	81.30	95.20	102.30	109.50	119.80	124.20	135.80	125.00
Real Estate Tax*	3.02	3.85	3.82	4.02	3.94	4.11	4.25	4.45	4.60
RE Tax as % of Local Revs (%)	4.80	4.74	4.01	3.93	3.60	3.43	3.42	3.28	3.68

Source: Federal Ministry of Finance, Czech and Slovak Republics, numerous issues of the *Statistická Ročenky* of both the Czech and Slovak Republics, and own calculations.

TABLE 2
LOCAL AND STATE TAX REVENUE SHARING, CZECH REPUBLIC

	1994	1995	1996	1997	1998	1999	2000
Tax Revenues, State	349,027	391,228	439,186	464,087	495,23	524,765	544,142
Tax Revenues, Local	54,428	68,167	70,000	76,091	83,319	87,011	95,807
Consolidated budgets, Local Share in %	401,503 13.5	457,022 14.9	506,202 13.8	592,474 12.8	575,83 14.5	608,585 14.3	636,618 15.0
Local PI Tax Revenues	48,716	60,096	50,818	54,503	58,581	60,078	63,501
National PI Tax	5,804	8,491	29,726	33,378	36,339	35,224	34,771
Total PI Tax Revenues	54,520	68,587	80,544	87,881	94,920	95,302	98,272
Local as % of Total	89.3	87.6	63.1	62.0	61.7	63.0	64.6
Local CI Tax Revenues	128	3,145	14,139	13,361	16,232	18,773	23,470
State CI Tax Revenues	63,624	63,337	47,676	42,202	51,324	51,343	52,322
Total CI Tax Revenues	63,752	66,482	61,815	55,563	67,556	70,116	75,792
Local as % of Total	0.20	4.7	22.9	24.0	24.0	26.8	31.0
National Government	30,980	34,803	61,504	35,839	37,355	41,374	45,939
Current	24,003	21,747	48,882	23,958	24,982	27,658	30,429
Capital	6,977	13,056	12,622	11,881	12,373	13,716	15,510
Local Rev & Grants	112,241	130,041	163,831	145,342	157,17	187,700	181,814
Consolidated Public	504,283	522,753	562,792	487,655	637,65	688,844	707,844
Local Share	22.3	24.9	29.1	29.8	24.7	27.3	25.7

Source: *Government Financial Statistics: Fiscal Data for the Czech Republic*.
Ministry of Finance, Czech Republic, and authors' calculations.
See the web site, <http://www.mfcr.cz/scripts/hpe/default.asp?VlfinSta>.

NOTES

¹ An excellent review of the process of fiscal decentralization in Russia, Poland, Czech Republic, Slovak Republic, Armenia and Estonia is provided by Jane H. Malme and Joan M. Youngman (eds.), *The Development of Property Taxation in Economies in Transition: Case Studies from Central and Eastern Europe* (Washington, D.C., 2001).

² Interviewing directors of state-owned enterprises in the spring of 1984 and again in 1989 I was impressed with the extensive set of facilities, e.g., *crèches*, cafeterias, classroom buildings, vacation homes and private apartments provided by those enterprises for their workers. We in market economies would classify the goods and services in this impressive list as private, quasi-private and public.

³For further information on this point, see Phillip J. Bryson, *The Consumer Under Socialist Planning: The East German Case* (New York, 1984).

⁴ Robert Holzman, 'Tax Reform in Countries in Transition: Central Policy Issues', *Public Finance/Finance Publiques*, 47, 3, 1992, p. 234.

⁵This view is well represented by Vito Tanzi, *Public Finance in Developing Countries* (Aldershot, 1996).

⁶See Wallace E. Oates, 'Introduction' in Wallace E. Oates (ed.), *The Economics of Fiscal Federalism and Local Finance* (North Hampton, Mass., 1998), pp. xiii-xix.

⁷See e.g., Charles M. Tiebout, 'A Pure Theory of Local Expenditures'. *Journal of Political Economy*, 54, 5, 1956, pp. 416-424 and Robert L. Bish and Robert J. Kirk, *Economic Principles and Urban Economics* (Englewood Cliffs, NJ, 1974).

⁸ See Alice Amsden, Jacek Kochanowicz & Lance Taylor, 1994. *The Market Meets Its Match. Restructuring the Economies of Eastern Europe* (Cambridge, Mass., 1994).

⁹ See Richard M. Bird, Robert D. Ebel & Christine I. Wallich 'Fiscal Decentralization: From Command to Market', in Richard M. Bird, Robert D. Ebel & Christine I. Wallich (eds.), *Decentralization of the Socialist State: Intergovernmental Finance in Transition Economies* (Washington, D.C., 1998), pp. 1-67.

¹⁰ See Jennie I. Litvak, Richard M. Bird & Junaid Ahmand, *Rethinking Decentralization in Developing Countries* (Washington, D.C., 1998).

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- ¹¹See Richard A. Musgrave, 'Who Should Tax, Where, and What?' in Charles E. McLure, Jr. (ed.), *Tax Assignment in Federal Countries* (Canberra: Centre for Research on Federal Financial Relations, Australian National University, 1993) pp. 2-19 and Wallace E. Oates, 'Taxation in a Federal System: The Tax-Assignment Problem', *Public Economics Review*, 1, 1, 1996, pp. 35-60.
- ¹²See Joan M. Youngman & Jane H. Malme, *An International Survey of Taxes on Land and Buildings*, Kluwer Law and Taxation Publishers, 1994).
- ¹³ See Andrei Shleifer & Robert W. Vishny, *The Grabbing Hand: Government Pathologies and Their Cures* (Cambridge Massachusetts, 1998).
- ¹⁴ See Anne Paugam, 'Ad Valorem Property Taxation and Transition Economies', *ECSIN, Infrastructure Unit Europe and Central Asia Region*, World Bank, Working Paper No. 9 (Washington, D.C., 1999).
- ¹⁵ See Alain Bertaud & Bertrand Renaud *Cities without land markets: Lessons of the Failed Socialist Experiment* (Washington, D.C., 1994).
- ¹⁶ See D. Netzer, *The Economics of the Property Tax* (Washington D.C., 1966).
- ¹⁷Jonathan Dunn & Deborah Wetzel, *Fiscal Decentralization in Former Socialist Economies: Progress and Prospects* (Washington, D.C., 2000).
- ¹⁸ See Bird, Ebel & Wallich, 'Fiscal Decentralization?'
- ¹⁹ *Ibid.*, p. 59.
- ²⁰ See Phillip J. Bryson & Gary Cornia, 'Moral Hazard in Property Tax Administration: A Comparative Analysis of the Czech and Slovak Republics', *Comparative Economic Studies*, 45, 1, 2003.
- ²¹ See Tanzi, *Public Finance*.
- ²² See Richard A. Musgrave, 'Approaches to a Fiscal Theory of Political Federalism,' in *Public Finance: Needs Sources and Utilization*, National Bureau of Economic Research, (New York, 1961), pp. 97-122.
- ²³ Jitka Peková, 'Obce a dotace', *Obec & Finance*, 1, 1, 1996, pp. 28-31.
- ²⁴Anton Marcincin, 'Slovakia: The Family Circles Privatization,' in Anton Marcincin, Daniela Zemanovičová, & Lubos Vagač, (eds.), *Privatization Methods and Development in Slovakia*, (Bratislava, 1996), pp. 6-39. The tenor of the Mečiar regime has been well summarized as follows: "The activities of the government of the Slovak

Republic manifested above all a strengthening of clientelism and statism in public life.” See Grigorij Mesez’nikov, ‘Vnu’tropoliticky’ vy’voy a politicka’ sce’na,’ in Martin Bu’tora (ed.), *Slovensko 1996:su’brna’ sprava o stave spoločnosti a trendoch na rok 1997* (Bratislava: Institut pre Verejne Otazky, 1997), p. 21.

²⁵See Joao do Carmo Oliveira & Jorge Martinez-Vazquez, *Czech Republic: Intergovernmental Fiscal Relations in the Transition* (Washington, D.C., 2001), p. xiii. Also in the introduction, these authors observe (p. xi) “local governments have only a marginal influence on fiscal matters” and (p. vii) that there is “weak grassroots demand for authentic local autonomy.” As capabilities, possibilities, and vision increase, however, the demand becomes very strong.

²⁶ *Ibid*, p. 48.

²⁷ *Ibid*, pp, 84, 85.

²⁸See Soňa Čapková, ‘Local Authorities and Economic Development in Slovakia’, in Andrew Coulson (ed.), *Local Government in East Europe Establishing Democracy at the Grassroots* (Hents, 1995), pp. 198-213.

²⁹ This became apparent in interviews in Slovakia in the spring of 2003.

³⁰See Phillip J. Bryson and Gary C. Cornia, ‘Fiscal Decentralisation in Economic Transformation: The Czech and Slovak Cases’, *Europe-Asia Studies*, 52, 3, pp. 507-22.

³¹ See Jorge Martinez-Vasques & Robert McNab, *Tax Systems in Transition Economies*, International Studies Program, Working Paper 1 - 97, Georgia State University School of Policy Studies, 1997, p. xv.

³²See Oliveira and Martinez-Vazquez, *Czech Republic: Intergovernmental Fiscal Relations*, p. 26.

³³Agenda 2000, *Commission Opinion on the Czech Republic’s Application for Membership of the European Union*, DOC/97/17, (Brussels, 15th July 1997).

³⁴ See EC 2000 Regular Report from the Commission on The Czech Republic’s Progress towards Accession. Online at http://www.europa.eu.int/comm/enlargement/report_11_00/pdf/en/cz_en.pdf accessed January, 2002.

³⁵A little research in Berlin and some online reading were enough to clarify the EU’s lack of concern with strong centralization, unfunded mandates, and the lack of a viable property tax or other significant revenues for subnational governments. The EU cannot ask of prospective members what most current members

likewise fail to do.

³⁶ Martinez-Vasques & McNab, *Tax Systems in Transition Economies*, p. 6.

³⁷ See Gabriela Bártíková, Ministerstvo vnitra, 'Informační servis k reformě veřejné správy' (Prague, January 23, 2003). <http://www.mvcr.cz/aktualit/sdeleni/2003/reforma.html>. Last accessed July 22, 2003.

³⁸ Pavel Bureš, *et al*, *Public Administration Reform in the Czech Republic*, (Prague, 2002), p. 8.

³⁹ Bártíková, 'Informační servis' *ibid*.

⁴⁰ Josef Postránecký, 'Obce s rozšířenou působností (Soulad správních obvodů a standardizace veřejných služeb)', *Deník Veřejné Správy*, <http://denik.obce.cz/go/clanek.asp?id=5520002>. Last accessed July 08, 2003.

⁴¹ Josef Postránecký, 'Obce s rozšířenou působností zahájily', *Deník Veřejné Správy*, <http://denik.obce.cz/go/clanek.asp?id=5383122> (Prague, 19. 3. 2003) Last accessed July 8, 2003.

⁴² See Gabriela Bártíková, 'Změny v územní veřejné správě od 1. 1. 2003', *Deník Veřejné Správy* <http://denik.obce.cz/go/clanek.asp?id=5279535> (Prague, 20. 12. 2002). Last accessed July 8, 2003.

⁴³ See Viktor Nižňanský & Jaroslav Kling, 'Veřejná Správa Public Administration,' in *Slovensko 2002 Súbrnná správa o stave spoločnosti Verejná správa*, (Bratislava, 2002), p. 252. Note that of 161,839 workers transferred out of regional state administration offices, 117,548 were assigned to municipal self-government offices and 44,291 were transferred to regional self-government offices.

⁴⁴ *Ibid*, p. 257.

⁴⁵ The Government Office of the Slovak Republic, *The Concept for Decentralisation and Modernisation of Public Administration* (Bratislava, 2000), p. 11.

⁴⁶ In a forthcoming document, the Slovak Republic admits somewhat graphically the origins and scope of the problems motivating reform. One reads:

In the current public administration of the Slovak Republic, conditions prevail that result from decades of totalitarian system when the public administration was constituted for totally different tasks and it functioned under different framework conditions than are those existing in present Slovakia. The partial changes effected following 1989, and, particularly

continuing efforts to take public administration for an instrument of power rather than service to the citizen, have not stripped public administration of many deficiencies.

See *ibid*, p. 3.

⁴⁷*Ibid*, p. 4.

⁴⁸See Bureš, et al, *Public Administration Reform*, p. 21.

⁴⁹ *Ibid*.

⁵⁰ Miroslav Kňako, *Daňová reforma 2002*, (Bratislava, 2002). Available online at <http://www.mesa10.sk/vs/index.asp>.

⁵¹ See ‘Flat Tax Fever’ *Wall Street Journal*, July 11, 2003, p. A8. The Slovak plan is to implement a 19% personal income tax, 19% corporate income tax, and a 19% VAT tax. The lack of progressivity makes it simple and eliminates the need for an army of tax lawyers and legislators to set up the myriad exemptions designed to restore “fairness” to progressivity and to reduce the strong post-communist incentive to evade taxes altogether.

⁵²See Kňako, *Daňová reforma*, p. 1.

⁵³*Ibid*. It is also mentioned that “in the last two years excessive increase was recorded in the share of indirect tax in the total revenues of the state, affecting mostly the socially weaker classes. Thus, shift to a wider extent of revenues from property taxes might moderate the imbalance arising from the transformation of economy. Let me note here, that the increase of property taxes without relevant lowering of income taxes or payments to social security funds is impossible.”