

Interventionism or Activation – Local Market Expectations Towards Local Government Units

Tomasz Kopyściański,¹ Rafał Kowalczyk²

DOI: 10.36250/00749.27

JEL Classification: H7, K2

Abstract

Representatives of economic and legal sciences very often deal with the issue of the comprehensive impact of local government units on creating local development conditions. The experiences of recent years indicate that public entities, including local government units, are active participants in the local market. This participation can take direct forms when the local government units participate in the market, but also an indirect form, when the local government units act as the regulator of this market. The main restrictions of local government's participation in the market are the law framework, the expectations of the local government community, financial condition and the risk associated with business operations.

Keywords

local government; local market; law regulations

1 Introduction

The issue of comprehensive impact of local government units on the shaping of local development conditions was a relatively rare issue at the initial stage of political change. Difficulties connected with the course of socio-economic transformation significantly

¹ PhD, Finance and Management Faculty, WSB University in Wrocław. The author specialises in local government finance. He is the author of more than 50 reviewed articles in scientific journals. Contact email: tomasz.kopyscianski@wsb.wroclaw.pl.

² PhD, Financial Law Department, University of Wrocław. The author specialises in financial law, particularly concerning local finance. He is the author of more than 60 reviewed articles in scientific journals. Contact email: rafal.kowalczyk@uwr.edu.pl.

influenced the directions of actions of local government units in the first years of their existence. Frequent changes in legal regulations, unstable solutions in the area of financing local government units, little experience in local area management, did not create a proper basis for discussions about the long-term prospects of functioning of local government units. Mainly for these reasons, local governments over the years focused more on immediate satisfaction of the collective needs of the territorial community, less attention was paid to the broader programs related to undertaking development initiatives. However, with the passage of time, symptoms of departing from this trend began to appear. It is first and foremost noticeable that by virtue of their functions, local government units induce lasting changes in the local space, which makes it necessary to reflect on changing the approach of local governments towards a multidimensional view of the problems of the local community.

Undoubtedly, the economic activity of public entities is inherently worrying due to the impact on the functioning of the local market, especially in terms of the potential use of a monopoly position or possible violation of the principles of free competition. However, recent years' experience indicates that public entities must engage directly or indirectly in local market affairs. The authors assume that any economic activity of a public entity is in fact an intervention in the local market, the identification of conditions and rules of intervention of local government units should intervene in matters of the local market taking into account current legal regulations and from the perspective of justifying the economic effectiveness of undertaken activities.

2 Economic Motives and Consequences of Intervention of Local Government Units in the Functioning of the Local Market

The area of each local government unit is a specific socio-economic system. It is created by the appropriate territory, together with the natural environment, the infrastructure base and the entire subject structure, which includes residents, units conducting economic activity, local authorities, social, cultural and religious organisations, etc. However, the essence and character of a given entity are really determined by the relations that occur between the listed positions. In this respect, local government units are often seen as a certain system in which the whole is more than a mere sum of parts (Bertalanffy, 1984: 23–24). The development of this system is connected with the process of transformation, in which the object passes from simple forms to more complex ones, more perfect in certain respects (Ziółkowski and Goleń, 2003: 44). Thus, local development cannot be identified only with quantitative growth, but it must also include a set of qualitative and structural transformations to improve the quality of life of the inhabitants. As a result, local development means a harmonised and systematic operation of the local community, local authorities and other entities functioning in

this area aimed at creating new and improving existing utility properties, creating favourable conditions for the local economy and ensuring spatial and ecological order (Brol, 1998: 11).

One of the key factors of local development is the economic development of the local government unit. Well-functioning local markets are the foundation of this process. They operate on a number of business entities such as commercial, production and service enterprises, farms, banks, other financial institutions, business organisations, business-related institutions and a whole range of others. The activity of these entities is a prerequisite for the development of local government units. They create jobs for the residents, thus providing them with a certain level of security, both financial and social (Wojciechowski, 2001: 192). Therefore, the level of prosperity of the whole local government community depends to a large extent on the economic results achieved by the sphere of private enterprises. Economic relations also have a significant impact on the shape of other components of local development, namely the social, ecological or spatial dimension. In connection with this, the question arises, what position should local government take towards these processes? Should it actively influence the course of market phenomena, or should it rather adopt a neutral attitude towards them?

The legal provisions regulating the functioning of the local government sector do not strictly define the rules for local government units to conduct local development policy. General guidance in this regard is provided by Art. 6 of the Act on Commune Self-Government (*Journal of Laws*, 2001, no. 142, item 1591, as amended), which stipulates that the scope of the commune's activity includes all public matters of local significance, not reserved by laws for other entities. In addition, a further part of the cited article states that if the law does not provide otherwise, the settlement of matters referred to in para. 1, belongs to the competence of the commune. In these provisions, therefore, there is a presumption of the right of self-government authorities to take actions for broadly understood local development. A more exact regulation in this area is included in Art. 18 para. 2 of the said Act, stating that the sole competence of the commune council is, among others, adopting economic programs. This provision does not clearly indicate the obligation to have such programs, or the way in which they are to be developed, nevertheless the quoted provision clearly suggests such a need and indicates that the entity authorised to enact them is the municipal council. Additional obligations are imposed on the commune by the Act on Freedom of Economic Activity (*Journal of Laws*, 2004, no. 173, item 1807), among others in the scope of records or control. In addition, pursuant to Art. 8 of this Act, the commune as a public administration body is to support economic development, creating favourable conditions for undertaking and conducting business activity.

It follows from the above that there are no legal contraindications as to the impact of a local government on development processes. At the same time, there are no clear premises specifying the relation of local government units to these issues. In this situation, local government units individually determine their role in the issue of creating local development, which is reflected in the tasks carried out. Affecting the socio-

economic processes taking place on a local scale, local government units can fulfil two functions (Ziółkowski and Goleń, 2003: 63):

- a) regulatory, i.e. preventing conflicts arising between economic entities, as well as eliminating barriers to development or at least reducing the negative effects of their occurrence;
- b) real, consisting in undertaking activities stimulating and dynamising development processes in local government units.

This does not automatically mean that taking action in these areas is economically justified. Referring to the previous observations made, a local government unit is not the only participant in the processes of shaping the conditions of local social and economic development. The relationships with the private sector, which in the conditions of the market economy is the main provider of goods and services also in the local dimension, are particularly important in this case. It is worth noting that relations between economic entities in a given unit and local government authorities are often referred to in the literature as a specific game, resulting from a clearly outlined conflict of interest. Economic entities strive to maximise individual benefits, while local government authorities should safeguard the general interest of the local community. The liberal trends in economics explain this contradiction by the existence of the “invisible hand of the market”, which turns individual efforts of entrepreneurs into improving the well-being of all inhabitants. However, experience related to the functioning of the market economy prove that it often cannot cope with local problems, as evidenced, among others, by the existence of monopolies, external effects, environmental pollution, which according to some researchers raises the need for active interference in the sphere of socio-economic development. Of course, it is impossible to ignore the issue that, according to the constitutional principles, the local government is to support and not replace the operation of the market mechanism. In this situation, the local government is deprived of instruments that would allow direct manual control of local development in a directive manner. Nevertheless, through the implementation of the statutory tasks, local government units can significantly affect the behaviour of business entities, modifying them in the desired direction.

The presented reflections constitute the background of the discussion on the extent of the influence of local government units on the course of development processes in the local dimension. On the basis of theoretical considerations, the following approaches are distinguished.

- a) Radical intervention of the local government sector, manifesting itself in the development of a number of economic programs designed to create new jobs, organise offices, agencies, business promotion centres, affecting business entities located in the unit through tax or credit preferences, and mobilising organisational units of the local government sector and the private sector around the strategic objectives of the development of a given local government unit.

- b) The model of public non-intervention in the local government sector, close to conservative, orthodox liberal trends, expressing consent to marginalisation of the role of local authorities in the economic and social sphere. This approach is dominated by the belief that any intervention may mean a distortion of the market mechanism, inefficient spending of public funds in the local government sector and consolidation of traditional structures.
- c) The model of traditional public intervention that does not call into question the need to involve public funds in the economic and social spheres, but recognises the dominant importance in this area of market mechanisms.

The approach based on the local intervention model assumes that the market mechanism alone is not able to maintain the proper course of socio-economic development. In this situation, there is a need for local authorities to manage this process. This concept, therefore, sees in local government units the main source of creating initiatives for local development. The effect of such a policy is a wide range of activities, among others application of tax preferences, subsidies, support programs from public funds, infrastructure investments. They are to stimulate the behaviour of business entities in order to achieve the assumed directions of development. In an extreme variation, this trend perceives the role of local government units as a translation of the doctrine of the welfare state into the local dimension (local socialism).

Proponents of active interference in development processes emphasise that this approach enables comprehensive coordination of all aspects of local development. However, conducting such a policy entails a number of side effects. The main threats include:

- a) too many priorities result in scattering of funds, which makes it difficult to effectively implement plans;
- b) excessive involvement in the sphere of local economy threatens to repress private entities from the market; this often leads to monopoly in certain areas by local government units, such as waste management, heat, gas, etc.;
- c) large-scale intervention programs usually require large financial outlays; the implementation of such a policy can lead the local government unit into a debt trap.

These allegations underlie the alternative concept of socio-economic development consisting in refraining from interfering in market mechanisms. According to it, the system of socio-economic relations in the territory of local government units is so complicated that it is impossible to determine all the factors of its development. In this situation, modifying only some variables does not give any reasonable assurance of achieving positive effects. The most radical critics even believe that interventions can permanently dictate the functioning of the local economy system.

According to the proponents of this concept, development impulses are sent from the sphere of private enterprises, and the market mechanism translates them into

the well-being of the entire community. The role of local government units in this respect should consist in removing obstacles interfering with the free operation of market rules. In particular, it is about solving property issues in the direction of privatisation transformation of local public utilities. In addition, local government authorities should give up all forms of interference in the economic and social sphere, passing the initiative in these areas to private entities. In this situation, investment activity should not go beyond the simple reproduction of municipal property. In the light of the assumptions of this trend, the role of local government is reduced to meeting the liberal principle of the “night watchman” in the local dimension. One should therefore take into account that the orthodox realisation of the postulates will result in the marginalisation of the role of local government units by reducing their activity only to fulfilling basic regulatory functions.

Although the division is of mainly theoretical importance, it nevertheless sets out the general approach of the theory on the principles of impact on local development. Naturally, in a market economy and the existence of democratic structures, top-down management of the socio-economic development of a territorial unit is out of the question, just as arbitrary external shaping of its spatial organisation, structure and functioning. On the other hand, the previously quoted perception of local authorities as the host of a local territory is part of the trend that assumes that market mechanisms do not spontaneously create permanent forms in which an individual interest would be in line with the collective interest (Eucken, 2005: 400). Active interference in stimulating development processes also finds its theoretical foundations in the literature on the subject. It is more and more believed, that local governments cannot be limited to providing passive public services to local communities, but just like the private sector, they must compete within a global framework.

3 Legal Determinants of the Intervention of Local Government Units in the Field of Running a Business in the Local Dimension – Acceptable Intervention Limits

Bearing in mind the theoretical models of participation of a public entity (commune) in a market game and without prejudging which of these models is appropriate, an analysis of the legal environment in the scope of undertaking and conducting business activity should be made. Activity on the local market can take various dimensions and forms and can be implemented using various legal instruments. However, one should be aware that any form of public entity participation on the local market affects the behaviour of this market and its participants. To undergo further analysis, it should first be determined in which normative way economic activity can be implemented, as well as in what areas

of law there are instruments allowing local government units to intervene in the local market.

First of all, it should be pointed out that interventionism on the local market may have a direct or indirect form. An indirect form consists in stimulating appropriate behaviours or phenomena without direct involvement of a public entity in the economic activity. The direct form of interventionism consists in involvement of the local government unit in the economic activity directed by local needs.

In order to assess the legal possibilities of economic activity, it is necessary to analyse the legal provisions of both systemic and financial nature, as well as the scope of public economic law. Starting from basic legal acts, it is necessary to indicate the provisions of the Constitution of the Republic of Poland and the provisions of the European Charter of Local Self-Government. The provisions of the Constitution of the Republic of Poland do not directly refer to the economic activity of local government units, constituting only legally guaranteed freedom in the conduct of economic activity (Art. 22 of the Constitution of the Republic of Poland), referring to the system of local government units, provisions guarantee the legally protected independence of local government units (Art. 165 of the Constitution of the Republic of Poland). In addition, in the provision of Art. 166, local government units are obliged to implement public tasks consisting in satisfying the needs of the local government community. According to Art. 3 of the European Charter of Local Self-Government, the local self-government denotes the right and the ability of local authorities, within the limits of the law, to regulate and manage a substantial share of public affairs under their own responsibility and in the interests of the local population.

These seemingly content-poor systemic regulations carry a far-reaching delegation for detailed development in the provisions of ordinary laws. The Act on Commune Self-Government and the Act on Municipal Economy cited above are important for these considerations. The first of these acts in Art. 9 contains regulations on the limits of business activity carried out by the commune. Pursuant to this provision, economic activity can be divided into the one that goes beyond and the one that falls within the limits of usefulness, except that going beyond public utility is allowed only in situations provided for by the act. Conceptual determinations are necessary for further consideration. The legislator decided in this Act to interpret the authentic public utility, which is the implementation of the municipalities' own tasks in order to provide current and uninterrupted satisfaction of the collective needs of the population through the provision of publicly available services. Public utility means, therefore, the implementation of own tasks in such a way as to satisfy the widest possible needs of the community (Kalisiak and Paluch, 2000: 54). This does not mean a lack of profit in connection with the business, but it is assumed that this profit is not a priority and cannot be the goal itself. Therefore, the tasks carried out taking into account the profit in which it occupies an equal place, or goes beyond the implementation of public tasks, are referred to as going beyond the limit of public utilities. This activity is, therefore, profitable and equal to other goals that accompany undertaking activities that go

beyond public utility (Wojciechowski, 1997: 13). The implementation of own tasks is therefore a priority in undertaking business activities, however, the scope of these tasks, the intensity of their implementation, and finally the manner of their implementation should be treated in a flexible and, above all, evolutionary manner, taking into account the changing socio-economic conditions. The Supreme Court has a similar opinion, as in a decision of 18 May 2011 it stated: The catalogue of tasks, provided for in Art. 9 para. 4 of the Act on Commune Self-Government of 1990 and Art. 1 para. 2 of the Act on Municipal Economy of 1996, is open and variable, conditioned by the life cycle of residents, external conditions and the general socio-economic situation, which requires adjusting the provision of services to these changes. Determining whether specific services provided meet the above premises should be made in the circumstances of a specific case, by referring to the distinguished features of these tasks, indicating their importance to the commune's community (Ref. no. III CZP 22/11 SIP LEX). Therefore, it should be stated that the analysed provisions of the Act on Commune Self-Government concern the general permit for running business activity of communes, in order to implement widely understood public tasks, in a way that does not go beyond public utility, or that goes beyond these limits.

Another act regulating the admissibility of economic activity by local government units is the Act on Municipal Economy, which apart from repeating the definition of municipal economy and tasks of public utility, also indicates acceptable forms and situations in which local government units may go beyond the tasks of a public utility nature. According to Art. 10 of the Act, it is possible to go beyond public utility tasks only in the forms of commercial law companies and only if the premises are met, which are the unsatisfied needs of the local government community on the local market, and, in the situation of unemployment in the municipality, negatively affecting the standard of living, if other funds failed to improve the local labour market. It should be emphasised that the mentioned provisions indicate the priorities in the activities of local government units, which include a continuous and uninterrupted satisfying of the needs of the local government community. Therefore, any activity not related to satisfying the needs of the community is allowed only if it is provided for by law. Thus, in case of tasks that do not exceed public utility, there is a freedom to choose both forms of implementation of these tasks, while there is no justification for undertaking such activities, while in the case of going beyond public utility, the legislator controls the possibility of undertaking such activities (Banasiński and Jaroszyński, 2017: 156). It is worth referring to the category of profit, which accompanies business activity, but also activities within the municipal economy. The profit category is not a legal category, but economic category. The mentioned provisions in no way relate to the circumstances of a profit within the framework of a municipal economy or broadly understood economic activity, which does not mean that it is not done by the doctrine or judicial decisions. According to the ruling of the Supreme Administrative Court in Gdańsk of 9 January 2003, the fundamental difference between the municipal economy and business activity lies mainly in the fact that the municipal economy has no commercial purpose

to gain profits. It must lie within the framework of communal activity, and its obligatory goal is performance of the municipality's own tasks, including the satisfaction of the collective needs of the community (public utility tasks). The commune is first and foremost a body of public authority, and so, by implication, it must perform certain intervention functions in the economy. This is particularly about the areas of socially necessary activities in which private entities are not interested (e.g. lack of profitability), creating new jobs, sustaining local traditions and local centres of economic and cultural activity. Whereas the activity of municipalities directed at social needs and public utility (the necessity to obtain financial resources necessary to carry out tasks) is desired or at least acceptable; pure commercial activity of municipalities may result in monopolisation of certain activities by the municipality and distract its attention from real social needs (SA/Gd 1968/02 SIP LEX).

Another type of intervention of local government units on the local market is stimulation of specific behaviours, not through own activity, but through other instruments – primarily financial ones. And here, paradoxically, the same provisions will apply, which were mentioned when discussing direct involvement of local government units in economic activities. Both the provisions on municipal government (Arts. 7 and 9, as well as Art. 1 of the Act on Municipal Economy) indicate the premises of this activity, which are primarily the unsatisfied needs of the local government community, which fall within the broadly understood own tasks. Municipal authorities are responsible for reading these needs and deciding on ways to satisfy them.

Among the instruments of indirect impact on the local market, we should mention those, which are related to actions and involvement of public funds for economic activation, and those related to other forms of impact on the local market. The first group should first of all indicate the methods and instruments provided for in the Public Finance Act. The second group includes regulations resulting from the broadly understood tax law.

Provisions of the Public Finance Act (*Journal of Laws*, 2017, no. 2077, as amended) contain a number of legal regulations important for business entities operating on the local market. These are primarily provisions regarding access to the implementation of public tasks financed from public funds, available to all entities in principle, without the preference of public entities (Art. 43 of the Act). Also provisions on the provision of budget subsidies (Arts. 218–219, 221 of the Act) do not exclude the provision of these sources of funding to private entities operating on the local market, although their availability is limited by specific provisions (specific subsidy, earmarked subsidy) and the exclusion of entities operating to gain profit (designated subsidy).

Another measure affecting the situation on the local market is conducting a specific tax policy that may stimulate business behaviour in a positive or negative way. The use of instruments belonging to tax authorities may take various forms from shaping tax rates, to introducing certain tax reliefs, to assistance provided in individual tax matters. Undoubtedly, running a liberal tax policy reduces budget revenues from this basic source of income, however, in the medium- or long-term perspective, it

should bring the expected effects in the form of economic recovery on the local market (Gonet, 2013: 131).

4 Conclusions

The involvement of local government units as an active participant in the local market is a universal and desirable phenomenon, whenever the local community experiences a lack of accessibility of services, or directed to the recipients of these services or indirectly affecting the quality of life of the local government community. Additionally, due to the fact that the market does not provide or provides insufficient amounts of certain types of goods desired by the local community, the interference of local government units finds its economic justification. The choice of tools for this interference is a secondary issue, assuming that they will be applied within the limits provided for by law. Nevertheless, since the presence of local government in the public administration system is a practical expression of the principle of subsidiarity, it is desirable to set clear criteria for the division of tasks between the state and local government in terms of influencing market mechanisms, including in particular economies of scale, flow-on effects, consumer preferences, and above all, the ability to monitor and evaluate the effects achieved through interventions.

This publication is a part of the project funded by the National Science Centre, Poland, based on the decision no. DEC-2016/23/B/HSS/00870.

References

- Banasiński, C. and Jaroszyński, K. *Ustawa o gospodarce komunalnej. Komentarz* [Act on Municipal Economy. Commentary.] Warszawa: Wolters Kluwer, 2017. ISBN 978-83-8107-118-5.
- Bertalanffy, L. *Ogólna teoria systemów* [General System Theory]. Warszawa: PWN, 1984. ISBN 8301057165.
- Brol, R. *Rozwój lokalny – nowa logika rozwoju gospodarczego* [New Logic of Economic Development]. In: *Gospodarka lokalna w teorii i w praktyce* [Local Economy in Theory and Practice]. Wrocław: Prace Naukowe AE, 1998, no. 785. ISSN 03248445.
- Eucken, W. *Podstawy polityki gospodarczej* [Basics of Economic Politics]. Poznań: Wyd. Poznańskie, 2005. ISBN 83-7177-216-5.
- Gonet, W. *Naprawa finansów jednostki samorządu terytorialnego* [Repairing the Finances of the Local Government Unit]. Warszawa: Difin, 2013. ISBN 978-83-7930-049-5.
- Kalisiak, M. and Paluch, W. *Działalność gospodarcza gminy i powiatu* [Business Activity of a Commune and a District]. Zielona Góra: Zachodnie Centrum Organizacji, 2000. ISBN 8387161403.

- Wojciechowski, E. *Samorząd terytorialny w warunkach gospodarki rynkowej* [Local Government in the Conditions of a Market Economy]. Warszawa: PWN, 1997. ISBN 83-01-12434-2.
- Wojciechowski, E. *Zarządzanie w samorządzie terytorialnym* [Management in Local Governments]. Warszawa: Difin, 2001. ISBN 978-83-7641-714-1.
- Zięty, J. J. *Ustawa o gospodarce komunalnej. Komentarz* [Act on Municipal Economy. Commentary]. Warszawa: C. H. Beck, 2012. ISBN 978-83-255-4034-0.
- Ziółkowski, M. and Goleń, M. Zarządzanie strategiczne rozwojem lokalnym [Strategic Management of Local Development]. In Sochacka-Krysiak, H. ed., *Zarządzanie rozwojem lokalnym* [Management of Local Development]. Warszawa: SGH, 2003. ISSN 2543-9170.
- Journal of Laws*, 2001, no. 142, item 1591, as amended, Art. 6.
- Journal of Laws*, 2004, no. 173, item 1807.
- Ref. no. III CZP 22/11 SIP LEX.
- SA/Gd 1968/02 SIP LEX.

