
REVIEWS

BASICS OF PUBLIC FINANCE (ZÁKLADY VEŘEJNÝCH FINANČÍ)

Jozef Medved' and Juraj Nemeč et al.
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The development of the public policy theory is informed by many impulses from other scientific branches. Public finance is one of them. The public finance theory is one of the important sources of comprehensive analysis of the public sector. Therefore the students of public sector issues definitely should not miss the book under this review, written by a team of authors from the Economic Faculty of Matej Bel University of Banská Bystrica. This is a second reworked and updated edition of the book "Verejné financie" (first edition published by Vydavateľstvo SPRINT, Bratislava, April 2005. ISBN 80–89085–32–2).

Its authors implicitly presume that the current public finance theory works with two variant approaches to the analysis of public funding. One of them is "traditionalist" and considers public finance a subsystem of the theory of finance. Without pushing the analogy too far, this approach could be called a "narrower concept of public finance". Its methodology is based mainly on the finance and accounting theory. Some of the topical authors (J. M. Buchanan) analyze public finance from the vantage point of the public choice theory. They approach public finance within a broader context, as a subject and instrument of public choice. Although these are two different approaches, both of them view public finance as a tool of public policy. The authors introduce the reader to both approaches. From the angle of theory and practice of public policy,

the book under review is a masterpiece contribution not only to the advancement of the public finance theory but also the definition, outline and solution of interdisciplinary issues of public finance and public policy. Public finance as seen by public policy may be considered a (financial) instrument of public policy or an instrument of implementation (and financial support) of public policy decisions.

The book has nine chapters. The first chapter (written by J. Medved' and B. Meričková) examines the function and scope of public finance. The authors critically analyze a number of definitions of the "public sector" and "public finance". Each of the analyzed definitions accentuates a facet of the phenomenon under scrutiny. Instead of providing a radical new definition, the authors rather seek their inspiration in that the "public sector" can be defined from the angle of funding, management, decision making, and control.

The key problem discussed in the first chapter is the size (extent) of the public sector. The root causes of the growth of the public sector are examined (p. 20–21), including those described by literature as the causes of the growth of public expenditure. It should be noted, in relation with public policy, that the root causes of public service growth are political factors that have to do namely with the normative analysis of policy. This remark chiefly applies to the analysis of the regulatory function of public finances, to which the final paragraph of the first chapter is devoted. If the aim of the regulatory function of public finance is to create conditions for the functioning of a law-abiding state (p. 25), then, by virtue of touching upon the very functioning of state administration, the regulatory function of public finance directly impacts also the efficiency of public policies.

The second chapter (written by J. Nemeč) examines the allocation function of public finance. This chapter is a well-informed analysis of individual approaches of the economic theory to the allocation function of public finance. On the basis of comparative analysis, it brings a comparison of social economy (presented in the Czech Republic – as J. Nemeč notes – For instance by R. Duben, Y. Strecková and Martin Potůček), the liberal school, and the details of the neo-classical market failure theory. The mission of the allocation function is to allocate resources as an allocation dilemma of "use of resources" from the viewpoint of allocation choice between the private and public sectors. This dilemma is basically a normative decision. Its consequences are based on the implication ensuing from the accepted axiom (or liberal or social paradigm). Criticism is therefore leveled on the effects (impact) of such decisions in the field of public policies. The same applies to the impact of state interventions in the event of market failure, whereby it is theoretically possible to "correct" the "failure" of market forces by means of state intervention... while "the state cer-

tainly should not intervene in every case of disruption of the market regulatory mechanism” (p. 49). One cannot but agree with that. However, the question is how much the term “market failure” really denotes the phenomenon of market failure. Although the term “market failure” is routinely used, the authors, by analyzing the extent of this term, explicitly expose a serious methodological problem, namely whether it is appropriate to apply the “market failure” term to the areas where the market inherently cannot fail (see net public goods), since it is naturally absent from certain areas. The question arises whether it is not better, in such cases, to say “market absence” rather than “market failure”. This note is also in line with the exposure and solution of the problem of public and private sector partnership (PPP), presented as a modern approach in the event of existence of collective goods.

The third chapter (written by J. Nemeč and B. Meričková) provides an analysis of the (re)distributive function of public finance. The content of this function is examined from both “the purely economic angle” (in connection with the economic implications of “welfare economics”) and the vantage point of social aspects of redistribution (i.e. chiefly vis-à-vis public policy in general and social policy in particular). Naturally, the redistribution issue is connected with the issue of efficiency. The authors point out that the neoclassical view of the redistribution problem leads to inefficiency but “maximizing efficiency at a high level of inequality leads to substantial economic and social problems” (p. 66). This is a weighty material comment, from which it is possible to imply that adverse microeconomic impacts do not necessarily make public policy abandon its redistributive role. This is underscored by a well-informed analysis of social policy, interpreted here as a component part of economic policy. From the institutional point of view, social policy is described as an instrument used by the state to safeguard the rights of its citizens. Social policy is defined as an intervention instrument of the state, which, from the methodical viewpoint, may be either active (preventative) or passive (retrospective), and which reacts to social problems after they occur. The publication thoroughly analyzes the main forms of social policy, namely social security schemes, social relief and social services, whose impact on Slovak conditions are examined using specific cases.

The fourth chapter (written by M. Orviská) provides an analysis of public finance and macroeconomic controls. This problem is part of the content of the so-called stabilizing function of public finance. If budgetary policy has to do mainly with the allocation and redistributive function of public finance, then fiscal and monetary policies are the two fundamental types of “financial policy” on its macro level. In the context of the public choice theory, the government may choose to apply either fiscal policy controls (public budget income and spending) or a monetary policy. The authors warn in this connection that

macroeconomic balance is one of the chief tasks of the state’s economic policy whereby public finance is the instrument of impacting that balance. Public finance impacts the balance by virtue of both the expense and income chapters of public budgets (or their balance). Actually, it is the system of public policies that, by its demand that public goods be financially covered, exerts pressure on the give-and-take of the public budgets and influences both spending and the final balance (such as a deficit budget), as well as a long-term public finance imbalance (public debt).

The publication under review defines and analyzes manifestations of both short-term (budget deficit) and long-term (state and public debt) fiscal imbalance. The authors point out that the reform of debt and liquidity management is associated with the transition towards the active control of public debt, streamlining spending connected with the financing of a public debt, and minimizing the risks associated with financial assets. If fiscal policy is used as an economic policy tool, it is necessary to presume (examine) the likely role of the multiplication effects of the various fiscal instruments. Economics being a dynamically evolving system, it is never quite possible to preview all fiscal-policy impacts down to the nitty-gritty. It would therefore appear more suitable, within the context of the analysis presented, to approach economic policy as a mix of monetary and fiscal policy instruments. Public policy subjects are likely to prefer the fiscal policy instruments, especially when the budgeting rules allow them a freedom of decision. This follows from the very essence of public choice, the subject theme of the fifth chapter (J. Nemeč, M. Orviská). This chapter is devoted to the analysis of decision-making in the public sector, where individual preferences get transformed into collective decisions. In the context of the Downs analysis, public choice is understood to be a “junction” of the economic and political markets, whereby three approaches to the role of the state are defined: the classical liberal approach driven by monetarism; the Keynesian activist approach; and the socialist approach. The said approaches influence the position of the state in the public policy system, running the gamut from “non state intervention” (liberalism) to state paternalism (see state socialism).

The key problem of making decisions about public matters is, what decision-making rules should be applied? Practical case studies prove that no such rules exist (Arrow’s theorem). In this connection, a thorough analysis is made of the role of bureaucracy in public choice. Weber presumes that bureaucracy functions optimally; in contrast, the neoclassical economic theory proves that bureaucracy is inefficient. This is a serious finding, as if it is true, it would explain also the inefficiency of public funds allocated by public policy schemes. This has an adverse impact on budgets (sixth chapter, written by J. Medved’). Budgetary policy in relation to public policy is actually the “financial image” of

the goals pursued by the latter. In view of this, the authors define the basic requirements for an efficient budgeting policy: to maintain aggregate fiscal discipline, to allocate resources in line with public policy priorities, and to encourage an effective and economical use of public resources. The example of the Slovak Republic serves to analyze budgetary principles, to characterize the budgetary system, and to show examples of writing and evaluating a national budget.

The seventh chapter (M. Orviská, P. Čižmárik) brings an analysis of public incomes as a source of funding and covering public expenditure. Inasmuch taxes are the main type of public income, due attention is devoted to this field. The publication provides an analytical survey of tax classification criteria and borrows from Stieglitz's criteria of optimal tax system (economic efficiency, streamlined administrative process, flexibility, political transparency and fairness). In the analysis of tax fairness, the principles of usefulness and ability to pay taxes are applied. In addition to fairness, due attention is paid also to effective taxation. This issue is treated within the context of the modern theory of administrative costs and excessive tax burden. The analysis offered by this chapter is suitably concluded by the application problem of determining an effective tax rate.

The eighth chapter is an analysis of public expenditure. Written by J. Nemeč, it (together with the second chapter) is one of the most valuable contributions of the book under review. It is not only a well-informed analysis of the current state of scientific knowledge in the field of public spending but also a creative breakdown of methods of evaluation of public expenditure and spending programs. Evaluation of the efficiency of public outlays is doubtless a serious issue. As the publication proves, developed countries redistribute almost 50% of their GDP through their public budget systems. It is therefore desirable to establish how cost-effectively, efficiently and purposefully the public expenditure is realized for the good of public policy goals. The publication under review presents and applies cost-output methods (CMA, CEA, CBA and CUA) and "corporate" methods of evaluation of the effectiveness of public programs. These methods can be used both to formulate spending activity plans (ex ante verification) and to monitor the spending done (ex post verification).

The final chapter (J. Meved', J. Šebo) deals with European and local public funds. It is a survey of the basic principles of EU budgeting, legal rules of financial management, and the issue of income and spending. This analysis comes complete with practical data. It is followed by a probe into the problem of fiscal decentralization in Slovak conditions. The analysis proves that delegating state powers to local governments leads to a better and more efficient management of public goods. The impacts of decentralization are documented by indicators measuring fiscal decentralization.

The book under review is a brilliant editorial project. It is a well-informed body of work supported by the analysis of a wealth of sources, their critical analysis, and ensuing creative synthesis. Its innovative (system-based and analytical-synthetic) approach to matters under investigation by means of public finance functions sets it quite apart from other "traditional" public finance textbooks. It is a worthy contribution to the theory of public finance and could become an important methodological guide for the hands-on creation of public finance and public policies. Its value is further enhanced by case studies and problem analyses in the context of international public finance. It is a very worthy publication on the European level.