THE PRINCIPLE OF SUBSTANTIAL TRANSPARENCY OF PUBLIC FINANCE AND THE CREATION OF THE ACTIVE CITIZENSHIP

Joanna M. Salachna, Marcin Tyniewicki[1]

Abstract

This article endeavours to analyse what impact of substantial transparency of public finance (i.e. a reliable means of providing information on state sector finances) has on shaping active citizenship in society. The aim is based on critical question on how the public authority should inform citizens on the process of collecting and spending public sector income; moreover, the complicated nature of public finances and varying educational backgrounds of recipients who form the society need to be considered.

The authors claim that principle of substantial transparency of public finance (i.e. informing citizens on public funding) has been inadequately implemented and it might be incomprehensible from the social addressee's perspective. Currently in Poland this principle is primarily focused on a rather professional level, although its social aspect is not ignored by the doctrine either. The authors believe that reporting on the state finances should be adjusted to the educational level of the audience as they are the principals of public authority.

This paper constitutes a part of the extensive research initiated by the authors, which examines the role of moral values in distributing public

1 Joanna M. Salachna, Professor of Financial Law, Department of Public Finance and Financial Law, Faculty of Law, University of Bialystok, Poland. The author specializes in local government finance, financial legislation and theory of legal and financial accountability. The author is the member of the Regional Chamber of Account in Bialystok and the Center for Information and Research Organization in Public Finance and Tax Law of Central and Eastern Europe. Email address: salachna@uwb.edu.pl
Marcin Tyniewicki, Doctor of Financial Law, Department of Public Finance and Financial Law, Faculty of Law, University of Bialystok, Poland. The author specializes in local government finance, EU public finance and public debt management. The author is the member of the Regional Chamber of Account in Bialystok and the Center for Information and Research Organization in Public Finance and Tax Law of Central and Eastern Europe. Email address: tyniewicki@uwb.edu.pl

resources by the authorities. Non-reactive (non-empirical) research methods have been utilised in the paper, which encompass a literature review, including legal acts currently in force in Poland.

Keywords: Substantial Transparency; Public Finance; Financial Decisions; Democracy; Education; Active Citizenship; Civil Society.

JEL Classification: A13, A20, E62, H50

1 Introduction

The main aim of the article is to analyse how the principle of substantial transparency of public finance (i.e. providing proper information to society) affects the shaping of active citizenship. The aim is based on the critical question on how the public authority should inform citizens on the process of collecting and spending public sector income; moreover, the complicated nature of public finances and varying educational backgrounds of stakeholders in society need to be considered. Thus the authors hypothesise that the principle of substantial transparency has been inadequately implemented and it might be incomprehensible to its target audience. This principle in Poland is mainly focused towards a professional level i.e. people who possess relevant expertise (Kosikowski, Ruśkowski, 2008: 301); however its social aspect has also been highlighted (Kornberger-Sokołowska, 2010: 254; Malinowska-Misiąg, Misiąg, 2007: 46–47). The principle of substantial transparency of public finance as a theoretical assumption has been distorted away from the perspective of a democratic model of the functioning of the state and civil society; according to which, proper information on financial matters should be supplied by collating data appropriately, and making it publicly accessible and appropriate to their age and educational level.

The Principal – Agent theory for the public sector (Weingast, Moran, 1984: 147–192; Moe, 1984: 739–777) was considered first in order to thoroughly examine the problem of informing citizens about financial policy and financial decisions taken by the authorities. In this concept, the "principal" is society or citizenry, whereas the public authority (politicians) is the "agent".

The authors assume that the principal (society) takes responsibility for public matters, hence civil society must act as the motivation for state authority (politicians) to effectively take and reconsider their decisions. The fundamental basis of civil society in democratic states is / should be relevant education and accurate dissemination of public affairs and finance. This coincides with transparency, which includes clear and intelligible presentation of the most relevant and crucial information and data.[2] It must be highlighted that without real transparency of an authority's public finance activity, neither citizenship education nor real engaged citizenship can exist. On the other hand, a regular and accurate (transparent, intelligible) flow of information and consistent education gives rise to a gradual comprehension of the information by citizens (substantial transparency). The fact that civil society is properly, not just superficially developed, makes citizens feel responsible for public affairs, and for public finance (global responsibility of society).

In conclusion, the authors would like to highlight that this problem constitutes just one part of the extensive research initiated by the authors, examining the role of moral values in the distribution of public resources by state authorities. The research methods include, inter alia, the analysis of the data obtained from questionnaires (empirical) but also some non-reactive (non-empirical) research methods, including a literature review and the relevant legal acts which are in force now in Poland.

2 Determinants of Taking Financial Decisions by Public Authority. The Role of Communication

Analysing the decisions of state authority, which are financial in character/ dimension (as they lead to far-reaching consequences), is a common and contemporary phenomenon. They frequently provoke deep emotions not only among academia, experts or politicians, but also among citizens. These types of decisions include, inter alia:

- Providing the coverage of free health benefits which are guaranteed (financed) by the state;

2 Formal transparency, on the other hand, means presenting the information and data in a free form or sequence etc. Although the information and data are provided this transparency is frequently in a specialised or *de facto* superficial nature.

- Setting out the amount and conditions for obtaining social benefits (e.g. aids, allowances etc.), which are financed from public resources;
- Formulating the rules of financing social security and determining the prerequisites (e.g. age, years of experience, the level of health detriment) which authorise a person to receive a pension or a disability pension);
- Modification of the tax system, which may also include formulation of the taxation rules in reference to the income of natural persons and corporations.

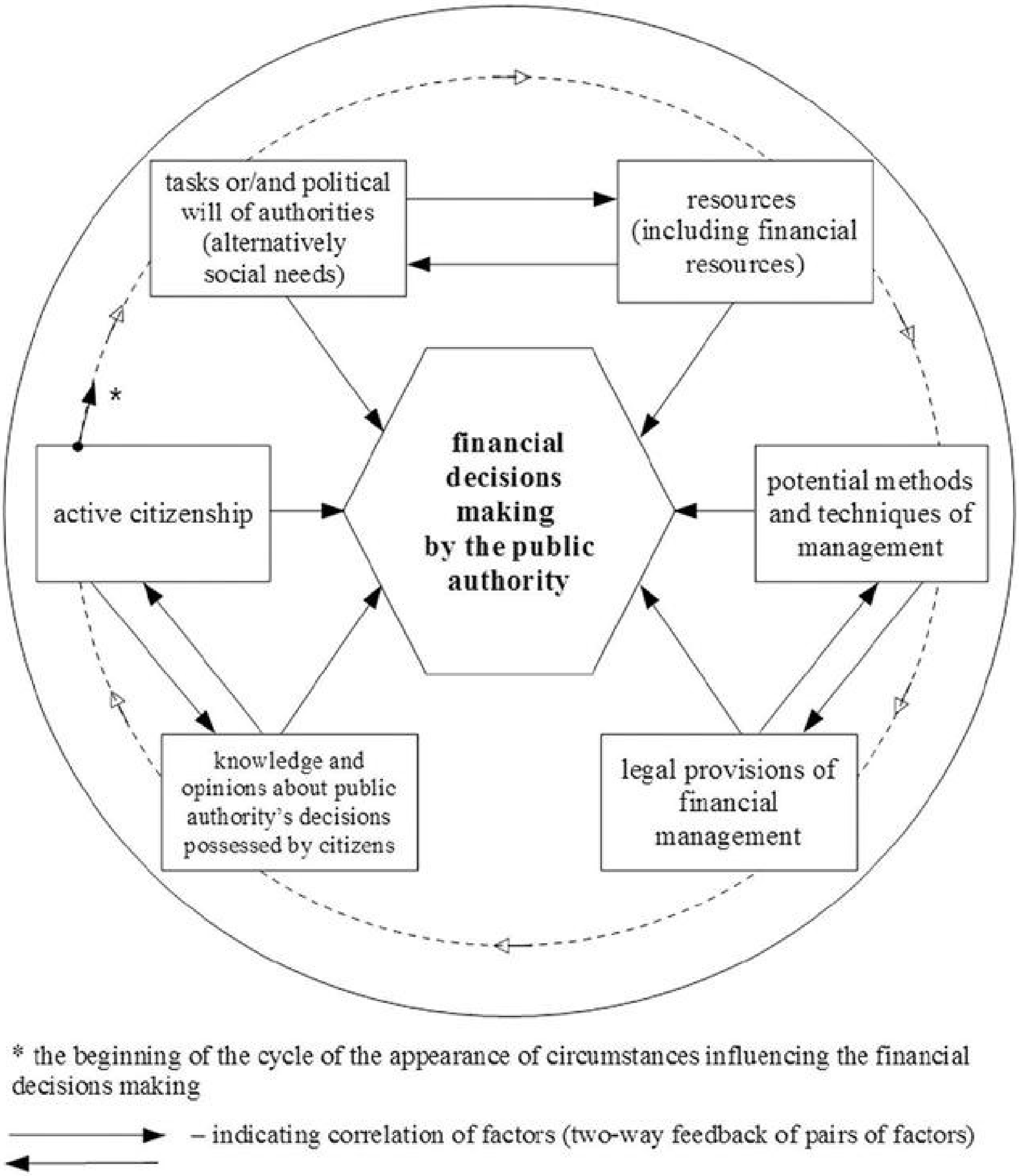
The aforementioned types of financial decisions, which are taken under particular circumstances and within a specified time frame by public authorities, in most cases cannot be assessed as either unequivocally positive or negative; this is due to the perspective of those making an assessment. Thus, for example, the social consequences of decisions are evaluated according to how they affect the standards of living (the rights and obligations of citizens and entrepreneurs) in a particular country. Nevertheless, their impact (either positive or negative) might also be different under certain categories. Financial / budgetary capacity (efficiency) of a particular country (most often, current and sometimes only prospective) is another point of reference. In this case, regardless of experts' calculations and forecasts, the consequences of the decision always differ (below/above the forecast) from the expected intentions and plans. The reform of healthcare in the USA (so-called *Obamacare*[3]) can be an example here. The consequences of the reform both for those who are covered by this healthcare and the budget of the USA, are far from the intended effects. (*c.f.* Kaiser Health Tracking Poll: December 2013. The Henry Keiser Family Foundation 2013. http://kff.org/health-reform/poll-finding/kaiser-health-tracking-poll-december-2013; Cornwell, Morgan: Obamacare website gets new tech experts; oversight pressure grows, Reuters: 2013. http://www. reuters.com/article/2013/10/31/us-usa-healthcare-surgeidUSBRE99U16R20131031).

The figure which is presented below depicts six key factors which, as the authors believe, affect the financial decision making process by public

3 *Patient Protection and Affordable Care Act* signed by the President of the USA in 2010 and progressively entered into force since 1 October 2013.

authorities, hence they create a specific environment in which management processes occur. Even more importantly, there are various correlations (two-way feedback) among particular determinants presented in the figure, which apart from different categories of determinants, is considered an additional factor which has an impact on the decision making process.

Figure 1. The determinants (environment) of financial decision making by a public authority



Source: own study

This approach can be described further. Namely, in all "pairs of factors" this marked co-variance, under certain circumstances and within a specific time frame, establishes a framework of the possible decisions. Despite the fact that the particular categories of factors might be discussed separately or jointly when viewed in the abstract, in reality, the decision making process is determined not by specific groups of factors, but the *de facto* results from the correlations existing among them. Every correlation has a different meaning in influencing the conditions i.e.:

1. Correlation: **Tasks/Political Will of Authorities vs. Resources** forces authorities to define their priority expenditures and to justify them (which may take different forms, as well as intensifying efforts aimed at increasing the financial potential (for example by obtaining new income sources). However, specific financial resources may limit both the scope of those actions or prevent their performance, despite prior declarations of politicians (political will), such as during political campaigns;
2. Correlation: **Potential Methods and Techniques of Management vs. Legal Provisions on Financial Management** determines the possible forms of actions and decisions within the scope of financial management, and its direction under certain circumstances and within a specific time frame. Although the models may serve to improve the quality of management, their application is not always possible due to legal restrictions which establish the management framework;[4]
3. Correlation: **Active Citizenship vs. Knowledge and Opinions about a Public Authority's Decisions possessed by Citizens** ultimately determines the framework of the decision making process and therefore the responsibility of public authorities. This correlation can be discussed from different viewpoints (Stiglitz, 2004: 184; Buchanan, Musgrave, 2005: 55–124, 163).[5] In respect to this consideration, however, it is worth highlighting that the authorities should not only take into consideration the preferences and attitudes of citi-

4 As a side note, a universal principle stating that public authorities act only on the basis and within the law needs to be highlighted here. It means that the principle which is applied in the private sector and which considers any acts that are not prohibited cannot be implemented in this context to be legal.

5 Management decisions might be considered, inter alia, with the application of transaction costs theory, the theory of agency and most often emphasised with the theory of public choice.

zens, (voters) but simultaneously they should effectively communicate with them through the decision making process. It is one of the conditions for social acceptance of the authorities' financial policy.

All of these relations, despite the fact that correlations of the elements (pairs of factors) are different, form a somewhat closed and recurrent cycle, creating the decision making process in question, which is represented in the figure by the dotted line following a clockwise direction. Recurrence of the cycles does not, however, denote that they are identical as every pair of the determinants, as a result of preceding decision making process, may be modified, which means that also subsequent financial decisions will differ. This is natural if the volatility of both citizens' political choices and financial policy is taken into consideration.

It is worth highlighting that the cycle itself commences with active citizenship, which is specifically manifested by citizens' participation in the electoral process of choosing their representatives in local and general elections (i.e. public authorities). These public authorities most frequently analyse/evaluate financial decisions, mainly taking into account the possibility of shaping and exploiting the financial potential to perform a steadily increasing number of public tasks (Correlation: Tasks/Political Will of Authorities vs. Resources). This is a natural consequence, as financial resources accompanied by an efficient and effective management system, and legal provisions (Correlation: potential methods and techniques of management vs. legal provisions on financial management) primarily determine the possibility of achieving their objectives. The authors, however, will further focus on the issues concerning the problem of communication between public authorities and citizens, particularly on its substantial transparency. Unfortunately, this question has not been widely researched in the area of public finance to date,[6] although the authors believe that this matter is an indispensable element of the functioning of contemporary (modern) democratic society, which also includes shaping (and changing) of active citizenship. Consequently this active citizenship should have an impact on the accountability of public authorities, as well as motivating the authorities to take certain actions.

6 Academics (who indicated support for the need to regulate the issue) have concentrated on the analysis of the formal/legal principles of transparency of public finance cf. point 4 of the article.

3 The Information Flow between a Public Authority and Citizens (Transparency of Intentions and Activities) – Reasons, Role, Distorting Effects

As mentioned above, an appropriate flow of information is of key importance for shaping adequate active citizenship under certain conditions and within a specified time frame. It means that a public authority should truly (not just superficially) communicate with society, because only then can active citizenship be shaped, and a civil society will exist. In addition, society may more consciously (on the basis of knowledge and opinions) affect public authority (politicians). In other words, public authorities should provide transparent (i.e. intelligible) information (this is discussed in more detail in section 4) about their intentions, anticipated effects, as well as current or prospective (also financial) outcomes of the actions taken. However, in practice this does not happen because public authorities (politicians), for various reasons, lack sufficient determination to take decisions which may rationalise the financial management of the state (this problem is more described by: Buchanan, Tollison, 1972).

Citizens are not properly informed about other matters due to the fact that the flow of information is distorted. This stems from both objective and subjective factors. In accordance with the aforesaid theory of agency, the objective factors of an incomplete and non-transparent information flow between a public authority and citizens (principal) relate to the fact that an entity that provides information possesses only limited knowledge on a particular matter.[7] "Non-transparency" is understood here, *inter alia*, as providing copious, fragmented bits of information, therefore the most important issues are not mentioned at all or, less frequently, "disappear" in the wealth of information provided. The subjective factors encompass intentional non-disclosure (non-publication) of information, which is frequently based on the fact that such disclosure might generate a negative rating of a public authority's performance by citizens (voters) – thus it might result in increasing their political accountability before voters (principal).

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7 This state might result both from a lack or a distortion of information provided to the authority from the lower levels of management, or result from a lack of sufficient awareness of the importance of given data by the authorities.

Without any doubt it can be stated that efficiency incentives of a public authority (politicians) will not and cannot coincide completely with the interests of their principal (society), but regardless of that, the scrutiny of public authorities' (politicians') activities is necessary and undisputed. In addition, this transparency of information and shaping citizens' knowledge and awareness results in a partial devolution of power (Fukuyama, 2005: 69), as the indicated correlations between accurate information and active citizenship are indeed reciprocal. The decisions of public authorities (politicians), including financial decisions, have an impact on politicians' accountability, on the shaping of citizens' responsibility and on the reinforcement of the institution of civil society (Salachna, Tyniewicki, 2016: 16–17).

4 The Principle of Substantial Transparency in Poland – Information or Disinformation?

The principle of transparency of public finance *sensu largo,* which includes the principle of substantial transparency, has been anchored in the doctrine and it is also reflected in the legal acts in Poland currently in force. It is expressly stated under Art. 33/1 of the Public Finance Act of the 27 August 2009, and its formal application is considered as the obligation to publish particular data or to follow transparent financial procedures is grounded in Art. 34–38c of the said Act. Moreover, transparency is a value protected by the Constitution (Art. 61 of the Polish Constitution).

In a broader context, transparency of public finances ensures parliamentary and social control over the collection and spending of public resources (Gaudemet, Molinier, 2000: 238–239; Weralski, 1981: 65–71, 183–184). As it is highlighted *"social pressure seems to be a more powerful instrument than a very thorough internal audit"* (Malinowska-Misiąg, Misiąg, 2007: 46–47). This transparency safeguards the actual functioning of a democratic state based on the rule of law, whose important element is civil society.

Nevertheless, the fact that some obligations to publish (i.e. public disclosure of the state's finances and its financial management) are imposed on a public authority does guarantee that this authority will implement this transparency directive effectively. In this context, the effectiveness of transparency (substantial transparency) should refer to an accurate (clear) flow of information between the authority and various stakeholders. Western scholars, however, exploit the notion of the principle of specification more frequently (Strasser, 1992: 55; Gaudemet, 2000: 238).

Although the financial doctrine also highlights the principle of substantial transparency, apart from formal transparency, and emphasises its social and audit roles, one might have an impression that these are merely conjectures rather than practical actions. The legislator itself and the authorities seem to underestimate the social dimension of the principle of substantial transparency. Moreover, instruction on public finances at law, economic or administrative studies leaves much to be desired as it is essentially limited to the presentation of legal acts including instruments of its implementation, which is in fact done by the representatives of the doctrine. These instruments encompass:

1. The appropriate details of public income and expenditure allocation;
2. Keeping budgetary accountancy;
3. Submitting relevant reports on public finance operations.

The issue of effectiveness (comprehension) of the published data has not been much explored by the doctrine.

As a consequence, the principle of substantial transparency is applied rather from the perspective of professional recipients (i.e. people who possess some expertise on public finance) even though they, given the way the data is presented, might have problems to accurately identify and assess the financial situation and policy of the country.

Thus, this flow of information leads to the situation that a stakeholder who has a different level of education and knowledge, and bears public burdens is somehow deprived of the access to public information. Paradoxically, s/he has access to information on public finance, but the obtained data is incomprehensible to them due to various reasons. It is worth noting that stakeholders also include non-governmental organisations, who are interested in receiving public expenditure for their activities, and who might be much more efficient than individuals in scrutinising public authorities.

From the perspective of the interests of a citizen who lacks professional knowledge on the financial management process, it is possible to indicate certain barriers which distort the efficient and accurate flow of information (i.e. the application of the principle of substantial transparency of public finance) although some of these might be objective in character:

- The concentration and wealth of published data, which is frequently very detailed, and selected without taking into consideration the stakeholder's perspective;
- Non-transparent method of data presentation which makes obtaining the information, on for example, total expenditure to fund some key projects (programmes) carried out by the state, difficult;
- Application of diverse terms to publish the same statistical data, for example, public debt vs. the state treasury debt.

5 The Impact of Substantial Transparency of Public Finance on Moral Attitudes. The Essence of the Mechanism and Prerequisites of Its Proper Functioning

The abovementioned correlations between informing society (also on public finances) and shaping citizens' responsibility and reinforcing the institution of civil society, are based on the feedback effect. It is a kind of interaction between these two factors that makes the whole system dynamic and subject to constant changes. It cannot be stated, however, that if informing/educating society on financial management was at a sufficient level (how to measure the level of sufficiency is another question), it would generate active citizenship among all citizens. It can, perversely, be stated that "the dynamics of the system is constant", which results from continuous changes occurring in the area of public finances.

The feedback effect in the context of the correlation: active citizenship vs. knowledge on public finance, will be discussed further but it is worth noting that this effect also occurs in the other pairs of factors which determine financial decisions taken by public authorities.

Particular moral values should also determine the reliability (transparency) of information provided to society. It needs to be highlighted that substantial transparency of public finance will not only constitute an element of the decision making process but, apart from moral values, will be the background (indicator) for all stages of proper functioning of the public sector, whose model was suggested by Salachna and Tyniewicki (2016: 12).[8] This model proves that the basis of the proper functioning of the public sector are the methods deployed, the quality of educational services, together with the information supplied to society, and that these should be provided on the basis of moral values; hence the condition of real (not only apparent/ formal) transparency, includingthe area of public finance, is met. In this case interactions occur not only between morality and education, but also between morality and substantial transparency.

The analysis of the aforementioned feedback effect can be commenced both with the process of communication/ information and active citizenship performed by members of society. The interaction which occurs between these factors makes this system complete in the sense that the determinants continuously affect one another; however, they are subject to constant change. Namely, proper (comprehensible) instruction and informing on public finance have an impact on citizens' awareness and their assessment concerning these finances. Non-governmental organisations, who are both beneficiaries of the information and who serve an educational role in society, are of key importance in this process too.

Disseminating knowledge (information and data) in its broad meaning, *inter alia*, the knowledge on the finances of the state and local governmental units or taxes as well as the impact (possibilities, outcomes) that citizens might have on public expenditure through social control stimulates, shapes, or changes active citizenship of the individuals. In this case we may say that some kind of stimulation of active citizenship occurs, for example, by:

- Mobilising citizens to take part in elections (it is worth noting that lack of approval for the state financial policy may lead to changes in political preferences);
- Willingness to actively participate in the process of social scrutiny by involvement in non-governmental organisations;
- A sense of obligation to shoulder public (tax) burdens in the event of the approval for financial policy implemented by the authorities;
- Concern for the public good, identifying with the goals pursued by the state (solidarity with the country and taking patriotic attitudes).

8 The model was developed by J.M. Salachna, M. Tyniewicki, U. Zawadzka-Pąk and E. Lotko.

One question might be posed in this context. How should these processes of informing and instructing citizens be conducted in order to implement the principle of substantial transparency of public finance? The issue in question is extremely broad and definitely goes beyond the present paper, but it is worth noting that the principle of adequacy should be applied here. Firstly, this principle should be implemented taking into account various educational and attainment levels (educational adequacy) hence it should not be merely limited to tertiary or universal education for social organisations to play a key role in this process as well. Secondly, the information should be provided with consideration to the educational level of various non-professional stakeholders i.e. people who do not have broad knowledge of public finances (adequacy of addressees), which means providing data of varying scope and degree of detail.

6 Conclusion

It is also important to stress that the analysed correlation between the principle of substantial transparency of public finance (providing proper instruction / information on these finances) and active citizenship might create a kind of cognitive dissonance. In theory the said correlation (the feedback effect) seems to raise no reservations – at least the authors endeavoured to prove its existence. This seems "obvious", given the fact that we agree with the statement that knowledge shapes an individual's awareness and behaviour. In practice, however, in the face of excessive amount of data on, for example, financial management of the country, as well as the complexity of the issue in question (multiplicity of terms, elaborateness of mechanisms of collecting and spending public resources, abundance of legal acts etc.), the shaping of active citizenship is effectively extremely difficult or practically does not occur, which, as the authors highlight, does not discredit the whole mechanism of the interactions but exposes the underlying problem, which is reflected in two main and interrelated issues:

- How should the information on public finances be provided?
- How should the financial decisions taken by public authorities be properly interpreted?

One should bear in mind, however, that the reluctance of public authorities, who are directly authorised to manage public resources and who derive some advantages therefrom, might present a certain barrier to properly informing the public on public finance as well. Paradoxically, the authority itself might be a beneficiary of the proper application of the principle of substantial transparency. Even though the pressure of society's awareness in assessing the way the public resources are spent forces the authority to justify (convince) that their financial decisions were appropriate, it promotes social acceptance of these decisions and subsequently provides approval of the implemented policy and ensures a continuity in holding office.

On the basis of the assumptions presented above, the authors believe that, instead of examining the correlation between substantial transparency of public finance and active citizenship, the methods and instruments implementing this principle should be researched in more detail. In other words the question of how knowledge on financial mechanism in the state should be provided becomes of key importance. The hitherto functioning of the principle of substantial transparency, focusing only on its formal/legal aspect, as well as targeting it at less or more professional stakeholders who have certain knowledge on the issue of public finances, needs to be modified. Namely, this principle, which was at the core of the theoretical dimension, should take into account the social aspect of scrutinising public resource management. In addition, as indicated above, even professionals tend to encounter problems with the appropriate interpretation of published financial data.

The question which has been posed above i.e. how to provide proper (accurate) information on public finance raises the need to completely re-define the principle of substantial transparency in the area of public finance. It seems that the fundamental condition for its effective application, from the citizen's point of view, is the motion to maintain adequacy i.e. to supply information appropriate to a stakeholder's educational level so that this information is comprehensible to them, which again raises the need to preserve the relevant scope and degree of detail, hence the need for financial education at various educational levels, as well as the education provided by non-governmental organisations.

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