

## The transparency of the formula-based government grant system for social welfare and health services

Arranging social welfare and health services is one of the key tasks of local authorities. Responsibility for financing services is shared by local authorities and the state. In practice customers, employers and the social insurance system also participate in financing Finnish social welfare and health services together with local authorities and the state. The state participates in financing services primarily through the formula-based government grant system. Formula-based government grants to local authorities are a significant expense item in the budget. The budget for 2008 appropriated about 4.9 billion euros to formula-based government grants for social welfare and health services. In the budget for 2009 the figure is about 5.6 billion euros.

The purpose of the government grant system and the adjustment of government grants based on tax revenues is to ensure local authorities with differing conditions and service needs sufficiently equal possibilities to arrange services. Although government grants ensure and steer the level of municipal services, local authorities can use general-purpose formula-based government grants as they see fit.

The use of the formula-based government grant system in financing local authorities' services has been justified on the grounds of the system's simplicity, predictability and incentive effect. Development has also focused on improving the clarity and functioning of the system. The formula-based government grant system has been criticised, however, as a complicated patchwork particularly from the perspective of the municipal sector. Parliament has also drawn attention to problems involving the clarity of the system.

The present audit examined the transparency of the formula-based government grant system for social welfare and health services. In practice it sought to determine in what respects the social welfare and health services system is cumbersome and difficult to

understand. It also sought to determine in what respects the system is a clear and understandable whole. The subject was examined primarily through the quality of legislative drafting and legislation. In connection with work, matters related to the transparency of the system were also studied from the perspective of local authorities' financial management.

The reform of the municipal and service structure and the related preparation of a reform of government grants are currently under way. The National Audit Office recommends that the audit findings should be taken into consideration in this connection.

The audit found that current legislation on government grants gives a disjointed picture of the formula-based system as a whole. This is connected to the existence of different systems according to administrative sector and the numerous changes that have been made in them. Through the government grant system a considerable number of changes, arrangements and compensations have been made regarding the division of labour between local authorities and the state as well as financing, and these have complicated the criteria in the formula-based system. In most cases it is difficult to trace solutions regarding changes and the grounds for their use to legislation or related drafting documents. Shortcomings in the content of legislation also make it more difficult to understand government grant legislation. For example, the way in which factors determining the amount of government grants are expressed is not always clear or sufficiently detailed, and background information related to factors has often been expressed inadequately in legislation.

The audit also evaluated the preparation of the government grant reform that entered into force at the beginning of 2006. The broad government proposal linked to the reform (88/2005) was found to be well drafted as a rule. Some shortcomings were also observed. These primarily involved the inadequacy of the grounds for some factor changes. From the viewpoint of government grants as a whole, particularly changes in the remoteness and archipelago factors in general government grants have weakened the system's clarity and understandability. The way in which the built-up area structure coefficient is calculated has also shifted to a model including several steps, without strong grounds. Another problem was the vague nature of effectiveness evaluations related to the proposal. This especially concerns the evaluation of social impacts.

From the viewpoint of parliamentary committees, the government proposal for the reform of government grants was considered a sizable and in some respects difficult whole. Discussion in committees focused on certain aspects of the reform. Greater attention was focused on new factors determining the amount of grants for social welfare and health services. In its report the Administration Committee did not mention general factors determining the amount of grants, although changes in these were significant. Drafting work preceding the government proposal and optional models included in the early stage of drafting were not discussed by the committee.

If one compares the recommendation of the working group that prepared the reform of government grants and the government proposal, one can justifiably state that certain changes in the government grant system were based more on political expediency than on clearly studied needs for change. In the opinion of the National Audit Office, all the solutions in the government grant reform have not been justified in accordance with the principles of good legislative drafting. The government grant system should be a stable whole, in which changes should be made with care and implemented solutions should be presented and justified as openly as possible.

The audit investigated the views of office holders responsible for local authorities' financial management concerning the clarity and understandability of the government grant system. The majority of those responsible for local authorities' financial management consider the government grant system's criteria technically complicated and legislation linked to the system disjointed. According to local authorities the structure of the system and the factors determining the amount of government grants should be simplified so that principles regarding the amount of government grants are understandable and can be applied in planning individual municipalities' finances and activities. The numerous changes that have been made in the system have also hampered local authorities' financial planning and made it more difficult to compare government grants in different years. The directing and prioritising of government grant resources to certain service areas is known to some extent in local authorities' financial management, but in practice the steering effects of general-purpose formula-based government grants have been modest.