



## IMPROVING A SYSTEM OF PUBLIC FINANCE CONTROL

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**Abstract.** The article deals with current problems of the financial system of Ukraine which enable searching the ways for effective public finance control, eliminating budget process disadvantages, making fundamentals of the State Budget of Ukraine efficient control as well as other state funds and property. Special instruments of solving problems related to public finance use and state property control are offered. Also measures for stabilizing public finance and improving control system in the field of public finance are developed.

### Introduction

The state functions (such as defense, economics, society, environment) require financial resources created in the national economy, mobilized due to fiscal policy and distributed in the future among subsystems of the national economy in order to perform these functions.

Under current conditions of robust shortage of financial resources to address important issues related to the social and economic progress a modernization of control system in public finance field is required which makes research works presented an actual piece of investigation.

In modern economics there are fundamental old schools of united researchers in the field of public finance and financial markets. The most important contribution to the theory of public finance belongs to such scholars as D. Buchanan, A. Wagner, K. Wicksell, J. Keynes, E. Lindal, A. Marshall, R. McGrave, A. Pigou, P. Samuelson, E. Seligman, R. Hicks, D. Hume, K. Shoup and many others. Also these issues have been considered by Ukrainian scientists such as A. Gaidutsky, A. Galchynskyi, V. Geets, B. Danilishin, T. Yefymenko, J. Zhalilo etc. Scientists point out that effectiveness of the government strategy and economic security is determined by financial system stability and efficiency of investments and innovations.

At the same time the dynamic processes taking place in the financial and economic field, the current financial security of Ukraine require further research for finding ways of modernization of control system of public finance in order to improve functioning of the whole financial system, make it stable and sustain.

Thus, the purpose of this article is to identify the current problems of financial system of Ukraine and offer special ways for improving control system of public finance.

### Results

In economics and politics of Ukraine issues of public finance control (in terms of their formation, distribution and spending) are actively discussed as it is a fundamental for meeting social and economic needs of society.

In economic theory there is a hypothesis that the smaller share of government expenditures in GDP, the more dynamic economy is. From another point of view increasing in government spending is a worldwide trend which reflects the level of development and the concept of the social state. This concept is shared by most democratic countries, including Ukraine.

Difference in public spending across countries is caused from differences in historical, political and ideological systems influenced by sets of factors. A higher level of public expenditure is seen in those European countries where social and democratic government is in power. At the same time, other countries (including China) do not finance social sector unlike economic development.

Western economists argue that there is an "optimal size of government expenditure" (the ratio of consolidated budget expenditures to GDP) for each country. This provides an optimum between economic

growth and benefits from the provision of public goods. In turn any deviation from the optimum is undesirable and leads to an economic slowdown (Edwards S., Savastano M., 1999, p.75).

According to Keynesians if there is imbalance in the economy, the increase in government spending leads to an expansion of aggregate demand and therefore production. Increase in government spending causes an increase in output which is equal to amount of the initial government spending growth multiplied by the cost multiplier. Thus public spending can make a stabilizing or destabilizing effect on output at different stages of the economic cycle.

The opposite view is held by representatives of neo-post-Keynesians. They argue that under equilibrium conditions public spending can also influence growth through the Hicks's multiplier-accelerator mechanism (Higgs R., 1991, p.3).

Economists who represent new classical theory have shown that growth rate is endogenous not only while reaching equilibrium, but under the equilibrium. Overall relationship between government spending share in GDP and economic growth (especially in Barro's model) is nonlinear because government spending along with taxes affect economic growth. As a result, if the share of public expenditure in GDP is low (less than about 1/15), its increase has a positive effect, but if it is large (higher than 1/5), the result will be negative (Barro R., Lee J., 1993, p.25).

Up to the XX century, public expenditure in most countries had not exceeded 10% of GDP. Everything was under idea that public spending should grow along with economic growth and production increase. But its growth must comply with economic one. The rapid growth of public spending began in the early XX century which was due to the World War and the need to mobilize significant financial resources. Further industrialization, increased tax revenue and social commitments of countries led to a further increase in government spending.

According to estimates of the European Commission only because of demographic factors in the next 40 years most EU countries will have to increase public expenditure in GDP by at least 4-8%, although such increase will not actually be compensated (Mitchell D., 2005).

According to N. Illarionov and N. Pivovarova (2002, p.18) transition to a higher level of economic development will cause increase in share of public expenditure in GDP. On the other hand, there is statistical evidence that an increase of the population will cause decrease in the share of government expenditure in GDP.

Government spending of over 20% of GDP and social spending of over 4.6% of GDP will not improve social indicators. The social field is stagnant while deteriorating indicators (health, life expectancy, education) of human development (Tanzi V., Schuknecht L., 2008, p. 98). However, a number of empirical studies show that public funding of many services has a positive effect on the economy (Easterly W., Rebelo S., 1994, p.5). The most effective budget expenditures include providing general education, research and development, investment in infrastructure, so types of activities which are not profitable for private companies. Thus, economic growth is affected not only by the size of government spending but also by its structure.

Efficient solution of a wide range of public issues is determined by public finance allocated through the budget. Unfortunately the state financial system of Ukraine experiences unbalance in the State Budget and the rapid growth of public debt (Table 1, 2).

Statistics shows how the indicator of budget deficit has increased by 2010. In 2011 the budget deficit fell by almost three times, but in 2012 it doubled compared with 2011. Ratio of budget deficit to nominal GDP shows the same trend. The budget deficit is financed, in particular, due to government borrowing, which promotes the growth of public debt. In economics there are risks associated with the burden of growing debt, which cause struggles for the financial system. Any debt requires considerable transactional costs so its accumulation is extremely dangerous for the economy.

**Table 1**

GDP and Indicators of the State Budget of Ukraine, in million Ukrainian grivnas

	2008	2009	2010	2011	2012
GDP	948056	913345	1082569	1302079	1408889
Income	231686,3	209700,3	240615,2	314616,9	346025,5
Expenditure	241454,5	242437,2	303588,7	333459,5	395661,8
Credits	2732,5	2780,3	1292,0	4515,0	3751,1

Budget deficit	12500,7	35517,2	64265,5	23557,6	53387,4
Budget deficit, % in GDP	1,32	3,89	5,94	1,81	3,78

**Table 2**

State Debt and Debt Guaranteed by the State (Ukraine), in billion Ukrainian grivnas

	2008	2009	2010	2011	2012
State Debt	130,7	227,0	323,5	357,3	399,2
Debt Guaranteed by the State	58,7	90,9	108,8	115,8	116,3
Total	189,4	317,9	432,3	473,1	515,5
Total, % in GDP	20,0	34,8	39,9	36,3	36,6

Government attempts to cover budget deficit employing other financial sources are not successful, although economic environment also affected the state fundraising. Government debt introduced by the Cabinet of Ministers of Ukraine and contained government bonds with indexed value and denominated in foreign currency did not significantly pushed the demand for government bonds, however, increased the foreign currency risk of public debt.

While maintaining the current macroeconomic development trends a set of indicators showing economic default will be in 2014. In fact, some experts believe that in 2013 Ukraine's budget deficit will be 104 billion grivnas (3).

According to V. Geets Ukraine will not suffer from budget deficit while economic growth being 7%. But if it is 3% the state will not be able to avoid robust budget deficit (1).

In our opinion, the government declaring goals of economic growth should make much effort to shape a balanced budget. All expenditures should be equal to incomes.

For these reasons, understanding a threat of uncovered government liabilities enables reasonable and effective policy of public finance control, eliminating disadvantages of budget process, providing fundamentals for effective control of the State Budget of Ukraine as well as other funds and state property.

Analyzing the current state of non-budget funds revealed that they are in a crisis. Especially it concerns the Pension Fund of Ukraine, which in recent years has lost certain amount of autonomy through revenues and expenditures being critically imbalanced. Increasing of pensions overtakes salaries rising. Failure to expand the legal sources and amounts of income flowing to the Pension Fund has led to its budget misbalancing. Consequently, there is a chronic shortage of the Pension Fund which is covered from the State Budget.

One of the problems in economy of Ukraine is state-owned enterprises which require significant funding. The Register of State Corporate Rights as of 01.07.2012 contains 674 companies with a state share (6). However, according to inventory of state property initiated by the government data represented above are incomplete. The state property is sometime not registered and uncontrolled. About 5.9 thousand companies operate as private firms using state property. However, public sector enterprises are generally unprofitable and not able to adhere to any financial plans. Functions of the state property control are dispersed among ministries and other government bodies. There are no effective mechanism coordinating functions of Fund of the State Property, other ministries and the State Agency of the State Corporate Rights Control.

The scope and scale of the public sector in the economy of Ukraine is currently focused on stimulating and social fields (social services, support for specific sectors of the economy due to low tariffs for public companies). So the public sector finances, in principle, do not encourage Ukraine in strengthening investment and innovation model of social and economic development.

Under these conditions, improving current situation is enabled by taking measures for the rational use of resources, coupled with the involvement of private sector resources, the development of public and private partnership to address social and economic problems in Ukraine.

Analysis of problems related to budget funds and property use points out the following ways of their solving:

- Removing inconsistencies in the regulations, resulting in loss of budget revenues;
- Improving government expenditures plans;
- Prevention of infringements of the law in government spending for goods and services;
- Ensuring revenue generated from shares owned by the state and preventing from selling state property with less price than market one;

- Cutting privileges for payments on budget credits;
- Prevention of budget loss caused from illegal administrative decisions and unjustified reserved funds allocation;
- Prevention of making budget funds receivables without their registration and further use by subordinate organizations;
- Prevention of financing state institutions through involving different budgets;
- Avoid inefficient using of the State Budget funds for goals which are not in priority.

To improve system of public finance control, ensuring its stability under conditions of challenges and fragile stability of the international financial market it is offered to take the next measures:

- through cutting budget deficit, rationalizing public spending by supporting the production sector, reducing the state debt it is possible to consolidate the State Budget of Ukraine and reserve economic spending exceeding social expenditures in law;
- improving formation of budget revenues by expanding fiscal tools and the efficient and targeted use of budget resources based on implementation of program budgeting and planning and project budgeting at all levels of the budgetary process, which in turn will contribute to the transparency of the budget process, improve financial reporting and internal financial audit;
- improving financial health of state funds as well as leading state and private corporations due to reducing level of losses and increasing domestic resource base, rationalizing expenditure, reducing the borrowing and involving the state funds for recapitalization.

## Discussion

Worsening economic conditions while crisis embracing the world economy, led to insufficient formation of budget revenues, shaping other state funds and results of activities of financial and non-financial corporations.

Inefficient public finance control while negative impact of external factors have led to a significant increase in public debt and debt guaranteed by the state, increasing internal and external borrowing and spending on keeping government debt. In the current environment policy focused on borrowing does not solve social and economic problems in Ukraine, by contrast, is a factor that significantly increases the risks of a financial system. According to said above a requirement to find additional opportunities to gain financial resources has been transferred from the category of "current" in the category of "vital" need for the state and the whole financial system.

Addressing problems of the state financial system and promoting investment and innovation way of country development can be done only through the rational allocation of the state financial resources, development of public and private partnership to involve private capital in financing innovation and sustainable social and economic development of the country.

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