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**THE FORMATION OF NEW PUBLIC FINANCE MANAGEMENT
SYSTEM WITHIN THE FRAMEWORK OF MODERN THEORY OF
PUBLIC FINANCE**

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The article defines the role of public finance management (hereinafter – PFM) in the system of public administration and explores the essence and features of financial management in the private and public sectors of national economy. The basic approaches of the traditional theory of fiscal federalism; the new public management theory; the theory of new institutional economics; the public choice theory; the policy network theory of governance are examined in the context of determining the specifics of financial management in the public sector. Particular focus is given to the issues of overcoming market failures and government failures that is rather important for ensuring economic efficiency of PFM. The necessity of PFM system structuring is proved in the article.

Keywords: financial system, financial resources, public goods, public finance, public administration, financial management, public finance management

Introduction. It is impossible to imagine progressive development of the country's economy without a well-functioning public finance. Being a tool for government intervention in the economy, the public finances directly affect both aggregate demand and aggregate supply. It occurs due to reallocation of existing financial resources in the country, creation of conditions for maintaining stability of national financial system, aimed at development of the economy and social processes.

PFM is part of the public administration system that interacts with other units by applying forward and backward linkages. Upon that, finances are both an object of administrative influence and management tool that determines possibilities and performance results of public administration in other sectors.

We can't but agree that today a process of blurring of lines between the public and market sectors objectively occurs, consisting in development of the state enterprise, extension of list and volumes of rendering paid services by state and local agencies, funding of private companies services from the budgets.

Conversely, in domestic economic literature the concept of «financial management» is rarely associated with PFM. This is explained by the fact that state or local self-governing authorities do not apply the mechanisms, not clearly regulated by the relevant legal acts, especially in the financial sector, in which supervisory bodies verify all decisions on public funds disbursing. Financial management should provide a more efficient and effective expenditure of budgetary funds in strict compliance with specific procedures and with maximum transparency.

It is also necessary to draw attention to the fact that financial management in the private and public sectors has significant differences (table 1), so that certain contradictions prevent the convergence of traditional content of PFM with financial management in the private sector.

Such contradictions primarily relates to the difference in management purposes. The profit can't be seen as a target of government activities, since such authorities shall take the responsibility for provision of social benefits (goods and services on a non-market basis) to society at large or separate individual households [2, p.10]. The difference in management

Table 1

Distinctive Features of the Finance Management in Public and Private Sectors of the Economy

No.	Comparison criteria	Finance Management in Private Sector	Finance Management in Public Sector
1.	Level of financial management application	level of enterprise or group of enterprises	level of industry, scope of activities of main administrators of budgetary assignments or territory
2.	Objectives of financial management	maximization of proprietors' welfare in current period and prospect by increasing market value of business	efficiency of society-owned funds utilization
3.	Financial management tasks	profit maximization	proper provision of budgetary services
4.	Risk management patterns	risk minimization along with acceptable profit level	risk management is concentrated in hands of financial bodies, the main administrators of budgetary assignments perform tasks on unconditional execution of their functions
5.	Financial resources formation	in terms of business development plan	within the budgetary allocations and limits of budgetary commitments

Source: designed by the author according to [1, p. 41-42].

purposes transforms the content of entire financial management process, therefore the rules and procedures of one sector are not suitable for another.

In modern economic literature major theoretical approaches that concentrate on a particular aspect of the financial management in the public

sector are: the traditional theory of fiscal federalism; the new public management theory; the theory of new institutional economics; the public choice theory; the policy network theory of governance [3, p.122]. We shall take a detailed look at each approach.

The traditional theory of fiscal federalism involves forming optimal number of local administrations, justifies the division of powers regarding tax collection and expenditures between different levels of PFM.

The new public management theory focuses on effective exercise of local governance. According to the theory, the citizen is a principal (the person who authorizes another person to act on its behalf as an agent). The local level of authority is seen as a community of principals and agents, intended to create a benefit, satisfying the demands of society. Only socially necessary goods are financed at the expense of budget funds. The civil servants are managers who have a certain freedom in choosing option of administrative decision and simultaneously their performance results are closely monitored by the authorities. Such approach brings features, previously inherent only to the private sector, into the PFM system – the innovative nature of management activity; the provision of sought-after services.

The theory of new institutional economics suggests the invention of transaction costs optimum and information security of principals regarding their participation in formation of structure and mechanism of public goods providing and funding.

The public choice theory implies that local governments act to achieve their own targets. It proposes to introduce competition mechanisms for overcoming opportunistic nature of the power structures functioning. In addition, the voting mechanisms and their possible impact on the structure and character of local governance are analyzed.

The policy network theory of governance specifies the interaction of local-level authority with partnerships, consisting of multi-level organizations with complex structures and focusing on application of institutional mechanisms and implementation measures to overcome both «market failures» and «government failures» (government regulation) [4, p.28].

The issues of overcoming market failures and government failures are investigated in the framework of the latter theory that is rather important to ensure the effectiveness of PFM; therefore, the matter is having our careful attention.

It is beyond argument that there are spheres of activity, in which the government operates more efficiently than other mechanisms. By ensuring the economic performance, the government compensates for what is referred to as «**market failures**» [5, p. 20], where the free market mechanism of competition, supply and demand does not exist or is ineffective. Therefore, the mechanism of government regulation of economy and operation of the public sector serve to offset the market failure.

Hence, the following functions are traditionally assigned to the state [6, p.12]:

- protection of institution of law and public order, localization of conflicts;
- defense of private property rights, its specification and registration;
- provision of opportunities and paths free exchange of goods and services;
- creation and security of information-sharing systems;
- preservation and development of measurement standards, including standards of length, weight, unit, and also money;
- public goods production.

It is assumed that government may deliver a certain range of services in specific sectors of the economy, where government spending per unit of benefits provided is lower than the private costs of providing such services.

The performance of public functions generates the following **«government failures»** [5, p.21]:

High probability of achievements different from the performance targets. The state follows a historical tendency of increasing its participation in economic processes through the socialization of production. For this reason, transaction costs, associated with the collection and processing of information, control and monitoring of the economic situation, are increasing. The growth of spending creates grounds for deviation of the results of tasks execution, which were designated, from actually accomplished tasks.

Possible mismatch of revenues and expenditures of the State Budget. Contrary to the traditional firm, operating in the free market, the degree of rigidity of budget constraints for the government is not absolute, i.e. the budget constraints for the state are «soft». Furthermore, some economists suggest that, at certain stages of the economic cycle, government deficit can fulfill a positive stimulating role for the entire social development. Given that, it is almost impossible to recognize the state an absolute bankrupt, even if it is unable to meet its liabilities. Even being legally declared a bankrupt, the state will continue to exist and carry out its functions, i.e. it can't be dismantled from the perspective of corporate law.

Lack of legally binding performance criteria for national economy. In the absence of clear measures of performance for government activities, such as profit for firms, government agencies substitute such criteria with self-developed standards. Thus, the government activities are often measured by the criteria of budget revenue growth and the expansion of state control. The Government bears most notably political rather than legal

liability to society. Furthermore, the presence of political cycle in democratic countries considerably adjusts criteria of its activity according to the phase of the cycle, where not economic, but political expediency of actions, plays a key role.

«*Crowding-out effect*». The efficiency of public funds utilization depends on the so-termed "crowding-out effect", essentially implying that increased government spending may result in economic slowdown of private sector.

Implementation of ***the newest public finance theory*** assumes minimization of the negative effects of both types of economic «failures» (market and government alike).

Current environment mainstreams tenets of ***the public choice theory***, pursuant to which citizens delegate powers to the state. Specifically, the state operates by virtue of the social contract. The State Constitution is acknowledged as such contract, which stipulates what fall within competence of the state and what rights of citizens can't be violated. Certain countries introduced contractual relations between authorities and the public into the practice of public administration in a literal sense [1, p.43].

It is also essential to employ mechanisms of public-private partnership, involving formation of certain alliance between public authorities and business structures for implementation of projects in the major spheres of government and its subjects' activities.

A.M. Baltyna [7] identifies three levels of PFM-related decision-making and implementation of the outcomes – political, administrative and executive. Practical results of policy-level decision-making are ordinarily embodied in the strategy, the concept, the message – the documents that define the vector of future development, but do not contain a mechanism for its implementation, the formation of which is a condition for achieving

political goals. At the political level of decision-making, assignment of tasks and attainment of goals not only define the vector of social development, but also are formulated as intended results, the mechanism of their achievement must be created as a system of complementary institutions.

The content of administrative level of governance consists in organization of the process of public goods and individual services production, from functional point of view, bringing the public authorities (local government) and public (municipal) institutions together. In the performance statistics of such institutions are recorded in the public administration sector. Feasibility to combine the public control and administration authorities and the public (municipal) institutions in one sector is based on the premise that the activities of such institutions is a continuation of performing functions by the ministries, as a result, services will be provided to the final consumer.

The public administration sector is dominated by transfer operations that do not involve the equivalent exchange of money to the goods, works or services.

The authorities exercise their powers in establishing the rules for provision of services and, at the same time, some of them independently provide services, and the state (municipal) institutions have rights and obligations to produce public goods on behalf of the public law entities.

Hence, the structuring of PFM system allows us to identify a set of interacting elements of its internal structure, to evaluate and improve the effectiveness of the interaction of these elements *inter se*.

Conclusions. The comparison results of models indicate the advantages of the model of new theory of finance over the traditional model. Meanwhile, an important problem of practical application of new approaches to the PFM is measurement of results, because in public administration sector it is difficult to be guided by the level of profitability, it

is necessary to determine what impact the measure will have in public meaning, whether a social effect will occur. Certain public goods have a number of characteristics, for which it is impossible to evaluate the performance as the cost-benefit ratio. Introduction of the concept of effective PFM becomes the way out, according to it in the public sector the attention should be paid not to the economic benefit, but to compliance of the results with the objectives determined in the financial management plans, as the degree of execution of the strategic and tactical tasks.

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