

ACHIEVEMENTS AND PROBLEMS IN IMPLEMENTING INNOVATIONS IN MUNICIPAL FINANCE

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Abstract: *The topic of the relationship between science and practice has always been a subject of discussion, and in the absence of such, criticisms were directed either at the representatives of science, because their works are detached from real reality, or at the representatives of practice, because they do not follow and do not perceive the scientific achievements. This fully applies to the public sector, where declarations of modernization are constant, but the results are not always sufficient. This report asserts the thesis that in the field of public finances, and in particular those of municipalities, there are quite a few innovative developments that are successfully implemented in some of them, but still insufficient, making an attempt to reveal the reasons for this .*

Keywords: *public finance, innovation*

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Introduction

State administration is basically a conservative system and it should be. We cannot imagine how after every political change and the coming to power of a new government, reforms will be made in accordance with the temporary moods of the rulers. Changes in the work of public administration structures must be done carefully and for a long time. However, this does not mean that the state administration in its set of executive bodies at the central and territorial level should be immune to innovation and improvement, on the contrary, the modernization of the administration should be a constant process, just as the requirements are constant of society to her work.

What are the challenges facing public administration today? The "black box syndrome" is particularly typical. People see that the administration works, but do not know exactly how, and judge its work by the subjective criteria of how they themselves have been served. Sometimes there is a feeling that processes are not particularly efficient without reference to objective measures. The heads of the administrative units, for their part, prefer not to undertake changes in the ways of working, in order not to make mistakes and not to be reprimanded by superiors, and no one is punished for doing his job routinely. The budgets of administrative structures do not depend on the competitive environment or on innovations. If we add to all this the fact that changes require additional effort and resources with an unclear end result, one can understand why the desire to maintain the status quo is always stronger than the desire to change.

Last but not least, the great politicization of the state administration should be mentioned. Our everyday life is filled with examples of personnel reshuffles at the change of each government, which can be justified when it comes to the composition of the political cabinets or the top management of the administrative structures, but not when it is done at the lower expert levels.

However, there are good examples of innovations introduced in public administration. In this report, we will examine some innovative models developed or applied by the author in the

field of municipal finance, trying to explain the reasons for the reluctance to implement them, despite the generally recognized benefit they have for better management

1. Bond financing

Economists are still divided over the debate over which is the better option – a balanced, deficit or surplus budget. In the socialist period of our country's development, it was considered that a budget with a surplus meant great economic opportunities, but this practice continued even after the transition to a market economy, when at the end of the year there were unused budget surpluses, which were spent hastily and in a non-transparent manner. A deficit budget implies greater efforts to collect revenue and satisfy more of the public needs, but it is necessary to indicate the sources of its financing. The assumption of public debt is mainly done by issuing securities, while municipalities prefer bank loans. Issuing bonds, although still an insufficiently popular source of income in municipal budgets, already has its history in our country. After the replacement of the Law on Securities, Stock Exchanges and Investment Companies with the Law on Public Offering of Securities, and above all after the control of inflation and stabilization of the leva exchange rate, real opportunities were created for debt financing of municipalities through the issuance of municipal bonds. These were prepared and implemented by the municipalities of Varna, Sliven, Shumen, Dupnitsa, etc. The fact that the municipality of Varna has already issued three bond issues, the last of which, registered in the Central Depository (CD) on June 30, 2010, was at interest rates more favorable than those of government securities speaks for the attractiveness of municipal bonds. papers issued at the same time (5.52% yield on municipal bonds versus 6.15% on government securities on the date of their entry in the CD.)

Issuing municipal bond loans allows municipalities to overcome their financial difficulties related to:

- Financing of the current deficit of the municipal budget.
- Redemption of previously issued debts. In this way, the refinancing of the liabilities is actually carried out.
- Smoothing out fluctuations in the receipts from tax payments in the local budget.
- Attracting significant financial resources to finance local programs and capital-intensive projects without increasing the tax burden.

Despite the improved regulatory and legal environment and the obvious possibilities of bond financing to solve budget problems, municipalities still refrain from using this financial instrument. The reasons for this are rooted in the lack of experience and ignorance of the specific matter related to the operation of the capital markets.

The main types of bonds that can be used for municipal debt financing are:

- General obligation bonds. They are guaranteed by the issuer, which is obliged to use all its tax power to make the loan payments. Because of this characteristic, they are considered risk-free and are highly rated by rating agencies. Their main direction is the financing of municipal objects that do not bring direct income, such as public buildings, streets, schools, parks, etc. The municipal budget revenues are used for debt payments.
- Bonds guaranteed by revenues from projects (revenue bonds). They are usually used for capital investment that has a certain group of users and that accumulates cash receipts (for example, commercial establishments, sports facilities, parking lots, etc.). This type of bond is

not guaranteed by the budget, but by the proceeds from the operation of the constructed object, which is why they are considered a bit more risky.

- Special tax bonds (special tax bonds). Payments under them are guaranteed with the proceeds from certain fees and service prices. These can be a household waste fee, the price of water, the price of advertising or other services. Unlike general obligation bonds, here the sources of income are limited.
- Industrial revenue bonds. They are usually issued by economic development agencies to municipalities. The purpose of the agency is to support the construction of industrial and commercial property for the benefit of private users. The funds from the issue of this type of bond are used to build new objects that are sold on lease. The security of this type of bond depends on the creditworthiness of the lessee.
- Housing bonds. This type of bond is issued to raise funds for the construction of new homes. They are guaranteed by the mortgage payments on the homes. In the USA, they are additionally guaranteed by federal subsidies for socially weak families, private insurance against mortgages, insurance from the federal housing authorities. This type of bond is extremely popular in Russia. They occupy 85% of the municipal securities market in the country.
- Bonds with mixed coverage (double barrel bonds). This type combines the security of general obligation bonds and those guaranteed by project revenues. Although they are not commonly used in the US and most European countries, in our country they offer a certain amount

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- Bonds with mixed coverage (double barrel bonds). This type combines the security of general obligation bonds and those guaranteed by project revenues. Although they are not commonly used in the US and most European countries, in our country they offer certain advantages to issuers, which is why they are preferable.
- Lease rental agreement bonds. In countries with a developed capital market, they have become increasingly popular in recent years. Typically, these bonds are issued by nonprofit corporations, community hospitals, or universities. They are most often used for the purchase of movable property (trucks, construction machinery, etc.), but are applicable to any type of property. With them, the municipality purchases the property and leases it to the relevant municipal company or institution in the form of a lease agreement. The leasing contract is structured as a revenue bond and includes all legal provisions, such as interest rates and additional requirements for the bonds.
- Bonds for the refinancing of old issues (refunded bonds). They are usually issued by municipalities when there is a change in interest rates.

What type of bonds a public institution with an independent budget will issue depends on the purpose of the bond loan and on its financial policy. The relatively limited use of municipal bond loans for debt financing of municipal budgets can be explained both by the aforementioned ignorance of the relatively complex matter of issuing securities, and by the expansive policy of banks to offer loans to municipalities with minimal risk (Борисов, 2004).

2. Long Term Financial Planning Model

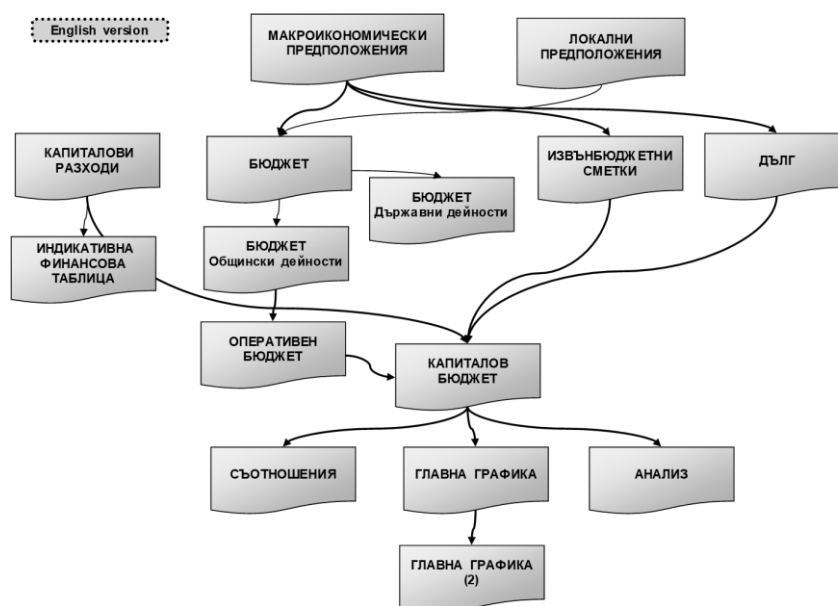
During the period 1998 - 2001, a team of Bulgarian and American experts developed a Model for long-term financial planning of municipal budgets under the "Local Government Initiative" Program of the American Agency for Development and Cooperation (USAID). It was and continues to be successfully implemented in municipalities whose financial managers take into account the long-term impact of their decisions.

The model is based on Microsoft Excel and enables:

- Extrapolation of the revenue and expenditure data of the municipality for a ten-year period, based on macroeconomic assumptions and historical data for four previous years.
- Calculation of the financial ratios that are related to the financial health of the municipality, with the determination of those that are at safe levels, the limit values and the risk values.
- Calculation of the operating budget by expenditure paragraphs and determination of the amount of operating surplus that can be set aside for investment costs.
- Ability to "play" different options for the amount of local taxes, fees and service prices and their impact on the operating budget.
- Calculation of the necessary additional funds for the implementation of the capital program of the municipality.
- Introduction of options to cover the shortfall of capital funds by taking on debt, with certain parameters.
- Assessment of the impact of various debt-taking decisions on the long-term financial health of the municipality.
- Making changes to the capital program to reduce financial risk.
- Visualization of budget values and parameters.

This model was successfully implemented in the municipalities of Sofia, Ruse, Varna, Shumen, Sevlievo, etc. when drawing up their budgets and before deciding to take on municipal debt, in order to see what the long-term consequences would be on the financial health of the municipality concerned. However, it is still not sufficiently popular and in demand, mainly due to the requirement that its application for financial forecasting be carried out by external experts who possess the relevant certificate for its use (Борисов Б. , Иновативни методи и модели за управление на общините, 2019)

Figure 1. Structure of the multi-year financial planning model



3. Business process management

It is a generally accepted finding that in the modern world the processes are dynamic and take on a risky nature. Belief in management's ability to predict future events and control them leads to the search for non-traditional solutions, flexible organization and quick adaptation to the external environment. Constant improvement of both adopted strategies and routine activities related to the achievement of specific results is sought. The dynamically developing business environment led to the emergence of qualitatively new concepts in management, perceived for some time as a model for effective management. Among them, the concepts, theories and management models developed in the last 30-40 years stand out, such as the concept of "Continuous improvement (Kaizen)", the concept of "Organizational excellence", the concept of "Total Quality Management - TQM", the concept of "Total Equipment Service" - TPM, the Six Sigma concept, the Proactive Management concept, the Lean Production concept, the Theory of Constraints (TOC), the Sustainable Development concept, the Management by Values concept, the Management of customer relations (CRM), the concept of "Supply Chain Management (SCM), management through the Balanced Scorecard (BSc), the concept of "Business Process Management - Business Process Management", etc. It is noteworthy that if the market concept that conquered the world in the 70s and 80s of the last century and was directed towards markets and customers, then in later years we observe a look inward, towards business processes, but not so much towards capacity opportunities of production technologies as much as to improve management.

Specific processes take place in public sector organizations, the main ones of which can be reduced to the following:

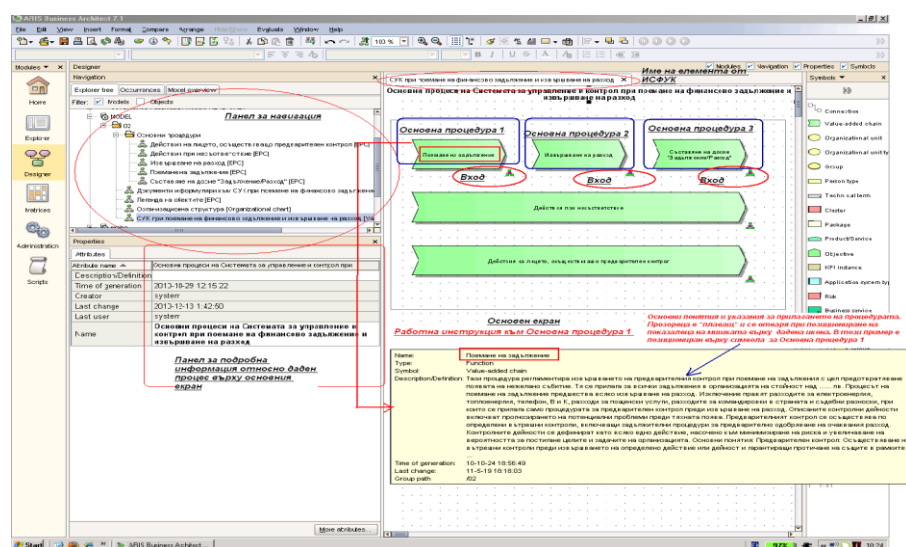
- Process of developing strategic planning documents;
- Budget process;
- Process of providing administrative and technical services;
- Investment process;
- Human resources management process;

- Public procurement management process;
- Contracts and obligations management process;
- Project management process;
- Property and asset management process;
- Information management process;
- Risk management process;
- Knowledge management process, etc.

Each of these processes includes sub-processes at lower levels. The question of their number comes down to a decision on the degree of detailing and dissection of individual processes into sub-processes. For each independent process and sub-process, written standard procedures should be developed, which describe the steps for their implementation, deadlines, responsible persons, accompanying documents, control procedures, etc.

Work processes can be described in several ways: in tabular form, in graphical format, through diagrams, or in both tabular and graphical format. Creating diagrams is an important part of the process description and analysis approach. The modeling method, also called notation, is a specific language for describing real-world objects using a special syntax that contains graphical symbols, attributes, and relationships between them. There are various technical means of notation that allow not only graphical visualization of processes, but also quick connections between processes of different hierarchical levels, connection with the organizational structure and staffing, generation and movement of various documents, retrieval of reports on deadlines, participation of officials, etc. Such tools are Casewise Corporate Modeler and ARIS Business Architecture. It is a modern software solution and methodology for description, analysis and optimization of business processes. These software products allow process tracking and detailed insight into sub-processes to the required level of detail, detailed information about each step of the process, visualization of the documents to be generated at a given stage, their filling and movement. The big difference is that they are not just pictures of a process element like drawing graphs, but have specific content that can be seen by positioning the marker over the corresponding symbol. This can be a description of a specific step, information about who performs it, when and in what way, etc.

Figure 2. Visualization of the processes related to internal control described at the high level of ARIS



In 2011, with the help of the ARIS Business Architect product, some business processes taking place in municipalities were developed, such as the process of drawing up and implementing strategic documents and that of internal control. For the municipality of Sliven, they covered not only the processes in the central administration, but also those in the town halls of the municipality and secondary budget managers. Unfortunately, during one of the changes of the municipal management, at his discretion, the use of the product was discontinued, although seminars were held and employees were trained for this.

4. WEB-based systems for financial management and control (FSMC)

One of the most important changes in the activities of public sector organizations in countries that transitioned from totalitarian to democratic governance was the decentralization of municipal finances. The new powers of the local authorities to draw up, accept, implement and report the municipal budgets also required increased attention to internal control.

Almost twenty years since the beginning of the changes in the regulatory framework of financial control and the setting of a requirement for the introduction of financial management and control systems (FMCS) in public sector organizations, the situation is not clear-cut. There are such institutions that have introduced and implement effective systems, constantly taking care of their updating and improvement. In others, they were introduced formally, either due to a misunderstanding of the nature of the systems, or due to an underestimation of their necessity, and in others there are none at all. External audit authorities are sufficiently consistent in their efforts to carry out inspections and sanction those managers who do not comply with the requirements of the legislation. The state of SFUK that they describe in their annual reports to the Ministry of Finance does not always correspond to the actual situation. Respectively, the Consolidated annual report on the internal control in the public sector in the Republic of Bulgaria of the Ministry of Finance, which is issued every year, represents a true summary of not entirely true findings.

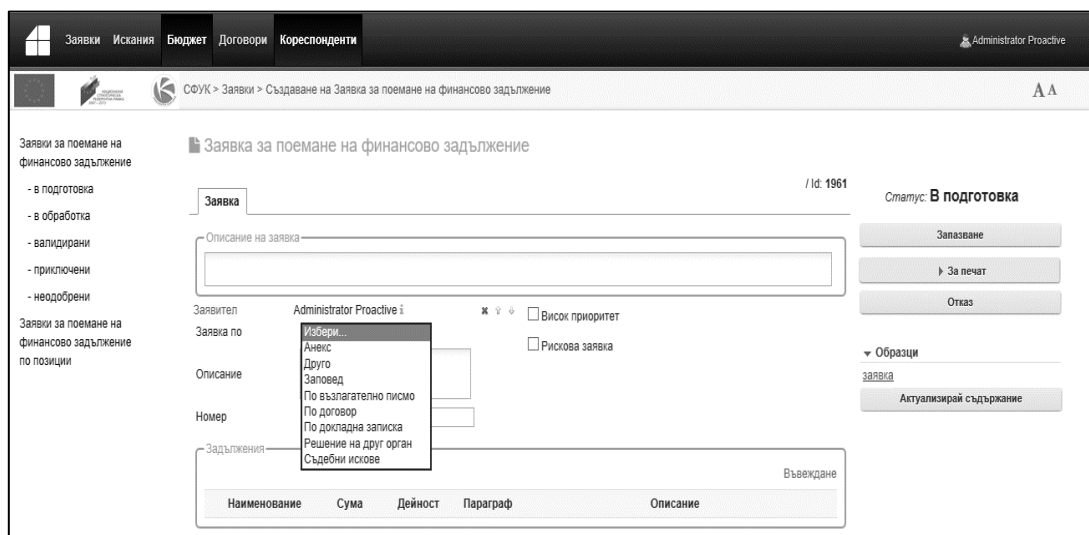
These conclusions are not frivolous, but are based on the author's long-term experience in the development and implementation of financial management and control systems in a number of organizations. More than half of the municipalities in the country, as well as some ministries and other central departments, work according to a model developed by a team under his leadership. However, if 15 years ago certain methods and technical means were used in the development of the SFC, now information and communication technologies provide new opportunities that should be used to modernize the SFC and increase their effectiveness.

As a result of the implementation of the project "New model for internal control, based on cloud technologies", financed by the Operational Program "Development of the competitiveness of the Bulgarian economy 2007-2013", a WEB-based specialized software for electronic document flow of procedures was created under the author's leadership when assuming obligations and making expenses, as an element of the Financial Management and Control Systems, called Cross Control (Борисов Б. и., 2019). It achieves:

- Instant correspondence between available, requested and spent funds under the organization's budget;
- Warning information when reaching certain critical levels of expenses on budget paragraphs, functions or those related to contracts with external contractors;

- Traceability of the performed control activities when assuming financial obligations or when making expenses;
- Full management of the internal document flow in the organization;
- Coverage of all levels in the management structure of the administration, including but not limited to outsourced units;
- Organization of a complete electronic archive, that is, archiving and copying/scanning of documents, preservation of original documents, working with archival ones and convenience in working with them;
- Easy access to information arrays;
- Convenient and lightweight interface with network and local scanning and printing tools;
- Quickly find all registered documents and extract reference information about them;
- Provides up-to-date information on the movement and actions on the documents at each stage of the work, according to the access rights;
- Has the ability to generate any reports related to the spending of public funds.

Figure 3. Request screen for assuming a financial obligation of the WEB-based financial control system Cross Control



The Cross Control product has been successfully used for more than 8 years in the Lukovit municipality administration and other public organizations. However, the formal attitude towards control procedures in many administrations is an obstacle to the implementation of any innovations in the field of internal control.

5. Strategic planning and program budgeting

The development of strategic documents - concepts, strategies, plans and programs, not only legitimizes the policy of a public institution in a given area, but also provides an opportunity for control and accountability, for the inclusion of interested parties in achieving the strategic goals of development, for risk assessment and from there – for more effective management. The Council of Ministers' 2023 State of Administration Report states that “an effective strategic planning process is a key condition for achieving good governance. One of the main functions

of the "management center", according to the definition of the Organization for Economic Cooperation and Development (OECD), is related to the provision of a clear strategic vision for development, planning and prioritization of goals and measures, coordination in the process of development and implementation of policies as well as subsequent monitoring and evaluation of progress" (Министерски съвет на Република България, 2023). The report concludes that there are over 200 national strategic documents that have no connection with each other, much less with the budgets of the relevant administrative structures. The review of a number of national, regional and municipal plans and programs shows that a large part of them contain large and meaningless analytical parts, and their prospective part is dominated by good wishes for the future, not supported by the necessary resources. A large part of them do not have measurable performance indicators, which prevents effective monitoring and civil control.

Linking the strategic documents and policy goals with the possibilities for their financial provision through the budget is a basic guarantee for transparency and accountability of the state administration. Taxpayers have the right to know and control what the objectives of each budget program are, what measures and actions the institutions want to finance and whether they actually lead to the achievement of these objectives. In the international comparative index "Open Budget Bulgaria shows a number of weaknesses precisely in the full use of program budgeting - lack of connection between strategic goals and the activities carried out, lack of clear and measurable indicators of the success or failure of individual programs, lack of analysis of past results periods and closing or reforming failed programs, etc.

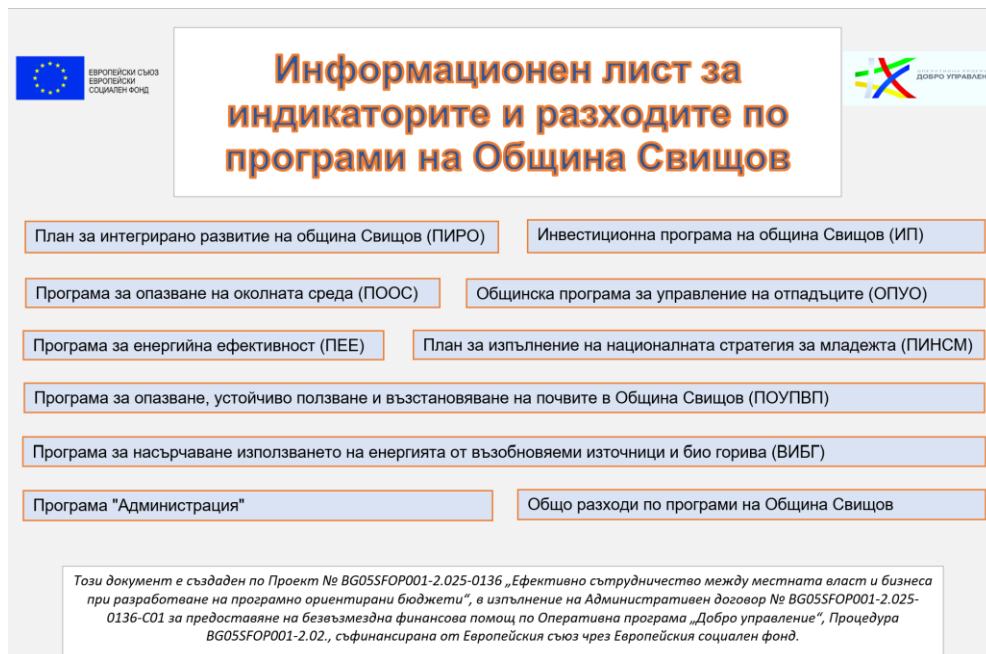
The normative regulation of the development of program budgets in our country is contained in the Law on Public Finances. In Art. 18. (2) of this law it is said that "The primary budget managers under the budgets of the Council of Ministers, of the ministries and of the state agencies also apply a program budget format", and in paragraph 4 it is specified that "The Council of Ministers approves a classification of policy areas/functional areas and budget programs under para. 3. With the classification, other indicators can be determined, which are elements of the budget structure in a program format". In Art. 67. (4) with the budget procedure, the Council of Ministers is given the opportunity to determine primary budget managers, other than those under Art. 18, para. 2 to implement a program budget format. Specifically for program budgeting in municipalities in Art. 82. (1) it is stated that "The Municipal Council adopts an ordinance on the conditions and procedures for drawing up the budget forecast for local activities for the next three years, for drawing up, adopting, implementing and reporting the municipal budget, developed in compliance with the principles, rules and the procedures under this law. With the ordinance, it can be determined that the municipality's budget is drawn up, adopted, implemented and reported in a program format as well."

Regardless of the legal possibility for municipalities to implement a program format of the budget, no such attempts have been made so far. The draft budget for 2007 of the Municipality of Mezdra, but this practice was not continued.

Only in the current year 2024, in the successful implementation of the project "Effective cooperation between local authorities and business in the development of program-oriented budgets", carried out with the financial support of the Operational Program "Good Governance", a team under the leadership of the author developed a Methodology for compiling a program oriented budgets of municipalities, which was implemented in the municipality of Svishtov (Borisov, 2023). The methodology describes the procedures for developing the strategic planning and program documents of the municipality and their relationship with the

budget expenditures, and it is envisaged that reporting forms for the funds spent on programs and the results achieved should also be filled in when reporting the budget.

Figure 4. Navigation screen of the information sheet for the indicators and costs under programs of the municipality of Svishtov



The real reasons for the municipal administrations' reluctance to introduce program budgeting is that it is not mandatory, but optional, and that it requires additional efforts to prepare statements of expenditures under budget programs. However, the benefits of program budgeting are incomparably more significant than the need for a little more effort from the financial specialists in the municipalities.

6. Other innovative developments for the benefit of municipal finances

We will briefly dwell on several other innovations in the field of public finance, and in particular municipal ones, which have been successfully implemented in some of them, but which are not yet widely used, due to the reasons stated above. Among them are:

6.1. Methodology for determining the prices of local fees and prices of services based on the actual costs of providing them.

In contrast to the well-known method of calculating the costs of the production of a given product or the provision of a given service through direct costing, called Direct costing, the activity based costing method is more suitable for public services. By using this method and in accordance with the requirements of Art. 8 of the Law on Local Taxes and Fees, the amounts of fees and the prices of services in the municipalities of Svishtov and Sozopol were determined, tens of financial specialists were trained and methodologies were issued for the application of this method (Борисов, Определяне на разходите за публичните услуги чрез остойността на база дейности., 2001). However, the municipalities are the units that can

prove and justify the amount of the fees and prices of services accepted by them with the real costs of providing them, as required by the Law.

6.2. Methodology for determining the actual amount of the "Household waste" fee through activity-based valuation

Municipalities in Bulgaria accept the amount of the largest fee - that for garbage collection, garbage removal and disposal of solid household waste and cleaning of public places on the basis of the so-called a plan-account, in which the necessary expenses for the individual types of activities and the per milles for taxation of enterprises and households are indicated. The problem is that these plan-accounts do not contain a calculation of the actual costs for the cleanliness of populated areas. Such a methodology for calculating all associated costs was developed by the "Local Self-Government Initiative" Program of the US Agency for International Development back in 2000. The discussions on determining a new basis for taxing the users of this service, which currently do not corresponds to the "user pays" principle, but despite this, neither the necessary regulatory changes nor an attempt to create a new organization for the collection of household waste have yet been made.

6.3. Methods for evaluating financial management

One of the well-known methodologies for evaluating the financial management of public institutions is the PEFA Framework for the Evaluation of Public Expenditure and Financial Accountability, created in 2001 by seven international development partners: the European Commission, the International Monetary Fund, the World Bank and the governments of France, Norway, Switzerland and the United Kingdom. The framework was created to establish a standard methodology and reference tool for evaluating the management of budget funds. PEFA is a model for evaluating the management of public finances, which should provide a basis for dialogue on strategies and priorities for their reform, as well as a set of information that could contribute to deepening research and analysis of their management. Since 2001, PEFA has become the recognized standard for evaluating public finances. As of 31 December 2015, more than 500 reports have been produced by 149 countries to assess public sector financial management (PEFA Secretariat, 2016). The performance evaluation system includes a set of general indicators that allow monitoring the effectiveness of public finance management systems, the relevant procedures and institutions responsible for their management and a report that presents the results of the evaluation of the effectiveness of the use of budget funds . As a result of the evaluation, a general report on the state of public finances is prepared, with the following structure:

1. Realism of the budget
2. Transparency and completeness
3. Budgeting in line with policy objectives
4. Predictability and control in the budget execution process
5. Accounting, documentation and reporting
6. External control and audit
7. Donor practices
8. Country-specific issues (if applicable).

TADAT (from Tax Administration Diagnostic Assessment Tool) is also an assessment framework or matrix, but it further narrows the object of assessment which is the tax administration system. TADAT is designed to give an objective assessment of the health of the main components of a country's tax administration system. This framework targets nine key enablers (POAs) that cover most tax administrations, functions, processes and institutions. The

evaluation of the results is based on 28 high-level indicators, each of which is built from 1 to 4 dimensions, or a total of 47 dimensions.

As of the end of 2024, there is no data on the implementation of PEFA and TADAT in Bulgarian practice, which is a challenge for scientists and financiers, as it is also recommended by the European Commission. The Commission's 2016 document, „Communication from the Commission to the European Parliament and the Council on an external strategy for effective taxation“, said: „Other areas the EU will focus on will include ensuring capacity building in the field of tax policy and tax administration through direct technical assistance or through partnership programs; supporting international initiatives to strengthen legislation and regulation, particularly in the area of transfer pricing; and assisting in the development and implementation of fiscal assessment tools such as the Tax Administration Assessment Diagnostic Tool (TADAT) or the Public Expenditure and Financial Accountability Tool (PEFA)“ (Европейска комисија, 2016).

In several Bulgarian municipalities, a simpler and adapted to Bulgarian practice model for the assessment of financial practice, called the Financial Management Assessment Framework, was used. The following 10 elements are analyzed, the condition of which is assessed with specific indicators. These are:

1. Financial planning
2. Budgeting
3. The collection of local revenues
4. Debt management
5. The assumption of financial obligations
6. Making financial expenses
7. Property and Asset Management
8. The investment process
9. The financial provision of projects
10. Financial control and audit.

The financial management assessment framework was successfully used in the preparation of functional analyzes of the municipalities of Silistra, Lovech, etc.

Conclusion

Discussed in this report, cutting-edge practices in managing municipal finances are not the only ones. Under the author's leadership alone, a number of methods and methodologies supporting financial management were developed, such as a risk management methodology, a methodology for subsequent performance control, an economic-mathematical model of a public-private partnership, a system for the management and control of public property and assets, contract management and control system, knowledge and information management and control system, etc. All of them have found their practical application in certain Bulgarian municipal administrations, but despite the proven effect of improving financial management, their application is limited. The reasons for this basically boil down to two:

1. Lack of an active marketing policy to promote innovative practices among public administration structures.
2. The well-known conservatism of public authorities and especially of public finances, which does not stimulate them to implement innovations. These are mainly done when regulatory requirements are introduced.

If we accept as true the statement that science without practice is useless, and practice without science is blind, then it is necessary to make more efforts to "examine" the Bulgarian institutions from the public sphere in terms of innovations. This can be done by introducing regulatory requirements for implementing innovative approaches in the work of public sector organizations, developing and popularizing typical innovative methodologies, attracting external specialists, introducing standards for certain work processes and certifying public organizations for their compliance .

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