USERS FEES AND LOCAL FINANCE IN TRANSITION COUNTRIES
THE CZECH AND SLOVAK CASES

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Abstract

The intent of this research is to determine what contribution is made by users fees to the local budgets of the Czech and Slovak Republics. Unfortunately, the revenues produced in the Czech and Slovak Republics from charges for public services are not considerable; they represent under 5 per cent of the receipts of local budgets. In transitional states trying to cope with a backlog of needs for local and national infrastructure and for numerous public services, one must ask whether such revenues could not be increased. Underlying this question is the more philosophical one about what the objective of user’s fees is or should be.

The paper presents the limited data available on Czech and Slovak users fees and discusses the use of such fees. The specific services are reviewed for which fees are provided in the twin republics. The revenue implications of the relevant public services for local budgets are discussed. The possibility of charging users fees is addressed not only as a means of cost recovery but also as a technique for providing budgetary relief for hard-pressed local authorities in these and other transition countries. The theory of optimal pricing is applied in this discussion. The role of users fees in the overall budget picture of the two Republics, especially in the context of the reform of public administration in the accession of the two republics to the European Union, are the concluding topic of the paper.
The transition from central planning to market orientation has already been underway in the Czech and Slovak Republics for what is now approaching a decade and a half. The path has not been an easy one for the public sector transition, since the central governments have been inclined to retain a centralist tradition. In reforms of public administration undertaken to prepare for entry into the European Union, there has been an attempt to devolve some power from the centre to the recently organized regions and the municipalities, but the effort to achieve fiscal decentralization has been difficult in the face of insufficient flows of funds from the centre to the cities and towns. The Czech central government has been more generous toward Czech municipalities than has been the case in Slovakia, but the Czech central government has managed the use of funds granted and transferred with a relatively heavy hand.

It follows, therefore, that the budgetary viability and fiscal independence of Czech and Slovak municipalities benefit greatly if independent financial sources, such as those generated by property tax and local users fees, generate robust revenue yields. This paper looks at local users fees and the possibilities they provide for financial relief for Czech and Slovak municipalities. Unfortunately, the revenues produced in the Czech and Slovak Republics from charges for public services are certainly not considerable; they represent well under 10 per cent of the receipts of local budgets. In transitional states trying to cope with a backlog of needs for local and national infrastructure and for numerous public services, one must ask whether such revenues could be increased. Underlying this question is the more philosophical one about what the objective of user’s fees is or should be.

It is a common view that the acceptable rationale for the prices of public goods and services is cost recovery. Policy may justify charging less than full cost recovery, but in some instances it may also seek more than recovery of the full cost. In transition countries users fees will be utilized for several purposes, frequently including the objective of providing a contribution to general revenue. Such is also the case for the Czech and Slovak Republics.

Municipalities receive revenue for the provision of paid public services. Some public services are provided privately, e.g., water, sewage, electricity and heat, and the consumer/citizen pays the providing private firm directly. Other public services, e.g., the use of public spaces for parking or other purposes or the approval to establish casinos or gambling, are provided to citizens for the payment of fees.

Some of the services once considered “public” are now provided privately. Such will not be the focus of this paper, since in the Czech and Slovak Republics such services have been privatized. They are subject to industrial regulation through, for example, the Czech Ministry of Industry and Trade, which is concerned with the pricing practices and other regulatory issues involved. These are simply no longer public services and cannot be counted on to generate public revenues.

The provision of public services is seen both as a duty of public administration and also, quite appropriately, as a source of public revenue. Such revenues make possible enhanced and extended goods and services for citizens and provide other desirable possibilities for scarce public funds. It was in part with this in mind that on one occasion the Czech Republic’s Ministry of Finance proposed that user’s fees be classified as taxes. The parliament declined approval of that particular proposition, but it does occasionally approve of new fees (as it did a few years ago for the fees on slot machines and casinos) and of fee increases as appropriate. Privately provided services have characteristics that suggest the use of prices, while publicly provided services have characteristics that suggest the use of taxes, even though the Czech Parliament did not grant the Finance Ministry permission to apply that label to services for which the term “fees” (poplatky) still applies.

1 The author is the Douglas and Effie Driggs Professor of Economics, Marriott School, Brigham Young University, Provo Utah. He would like to thank Dr. Zdenka Jiraskova and Alena Holmesova of the Ministry of Finance, Czech Republic, for helpful discussion of this topic in May, 2003 and to the Lincoln Institute of Land Studies and the Marriott School, BYU for financial support of this project.
This paper will review the current budgetary contribution of users fees as well as their potential for greater future revenue in both the Czech and Slovak Republics. The use of local fees was affirmed in Czechoslovak legislation, both in Prague and Bratislava, before the federation was abandoned. This occurred in the latter capitol November 27, 1990, before the Velvet Divorce and the establishment of two independent republics. That law remains the basis for users fees in both Slovakia and the Czech Republic to the present, so the two countries depart from an identical initial situation. Since their division in 1993, they have continued to share many of the characteristics of transitioning states struggling to develop the capacity to perform in market environments. They make an interesting comparative study now especially as their approaches to national and local finance have begun to diverge. The differences are becoming more apparent as the two nations pursue divergent approaches to the reform of their public administration systems mandated by the European Union in preparation for their accession in 2004. The Slovak Republic has undertaken a complete overhaul of public finance and a comprehensive tax reform, striving to move toward a “single tax” at the single rate of 19 per cent for the basic taxes: VAT, corporate and personal income taxes.

Section I will review the services for which fees are provided in the twin republics, after which section II will review the revenue implications of such public services for local budgets. Section III will address the question of charging users fees not as a means of cost recovery but as a technique for providing budgetary relief for hard-pressed local authorities in transition countries. The role of users fees in the overall budget picture of the two Republics, especially in the context of the reform of public administration in acceding to the European Union will be the topic of Section IV.

Chapter 1. User’s Fees Charged in the Czech and Slovak Republic

There are nine general service categories for which user’s fees are levied in the Czech Republic. Listed by Jiráskova and Šneberková (2002, p. 7) these include the following:

- Recreation and spa fees
- Fees on local housing accommodations
- Fees on the use of public properties for parking and other uses
- Permits to drive in the city centre
- Fees on admissions to ticketed entertainment
- Garbage collection
- Value-added fees for lands where water and sewage hookups have been made available by the municipality
- Dog licenses
- Fees on casino gambling and slot machines.

The same basic list is provided by the Law of the Slovak National Council on Local Fees of April 29, 1992.

Although there have been a small number of changes in these municipal fees stemming from 1990 in both the Czech and Slovak Republics, they remain very similar to the present. The right to apply users fees in both republics, which precedes their division, was granted by the national parliament through law. Each municipality has the right to decide whether or not to apply any of the fees approved by the legislation. If they decide they will charge an approved fee, they decide what (approved) rate they will charge and then post a notice on the municipal bulletin board that the users fee is to be charged.

1.1 Fees for Dog Licenses.

As one reviews the specific provisions pertaining to the users fees, their intent becomes apparent. In the case of fees for dog licenses, one intent is made explicit when reference is made to the regulatory function of this fee. When citizens in a large apartment building own a dog, the potential external effects of the pet are negative and are discouraged through the imposition of the fee. When, on the other hand, fees are exempted

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3 See Zakon Slovenskej národnej rady y 27. novembra 1990 o miestnych poplatkoch, which presents essentially the same list in section 1 of the statute.
4 This will be done on the basis of explication and commentary on the Czech law as provided by Jirásková and Šneberková, op. cit.
for specially trained dogs for the blind, helpless, or handicapped persons, other intent is apparent. Clearly, we are not talking here of price discrimination, since the elasticity of demand of handicapped individuals for canine assistance is low and the willingness to pay would be greater, were higher fees applied, than that of individuals for whom dog ownership is a form of consumption. The Municipality can also extend the exemption for dogs to other owners whose dogs have special qualification, e.g., those of guard dogs or hunting dogs.

1.2 Fees for visiting a spa or recreation facility

These fees are not paid by the blind, helpless, or handicapped, nor by any assisting person accompanying them. Nor is this fee paid by persons younger than 18 or older than 70, a child support recipient, or by soldiers on active duty. Since the tariff may not exceed 15 Kc per person per day of the stay, this fee is rather minimal. Rather than suspecting that the demographic groups selected for exemptions are akin to those who receive lower prices in price discrimination schemes, we recognize quite readily that these exemptions are made with the intent to avoid creating hardships.

1.3 Fee for Use of a Public Area.

This fee is represented as having a “regulative and educative” function intended for maintaining public order. It is paid for private use of public space, particularly for the placement of facilities offering services or for the use of sales or advertisement facilities, e.g., for circuses, carnivals and other attractions, for cultural or sports activities, or for film or TV work. No fee is paid for activities that charge no entrance fee or for activities providing proceeds only for charities. Public space can be utilized, in other words, only for activities of social worth, and especially educational activities are favoured. If such activities are profit-making, the municipality may share the profits for sharing its desirable locations.

Unfortunately for the revenue-seeking municipality, law stipulates that the fee for use of public space cannot exceed 10 Kc for each square meter of public area used per day, making it apparent that the legislators did not view this fee as an appropriate means of revenue generation.

1.4 Fees on Entrance Charges for Public Events.

The purpose of this fee extends beyond revenue generation. It also gives municipalities the opportunity to influence what cultural, sport, and other ticketed activities are held within the municipality. According to the legislation, the municipality may apply these fees in a manner that promotes its own interests and autonomy. As we saw earlier, law indicates that such fees shall not be paid for admission to activities where the entire proceeds are intended for a charity or public service. The tariff may not exceed 20 per cent of the total amount of the entrance charge, but if total revenues are not substantially more than 20 per cent of total costs, this permits the municipality to enjoy a good share of the net revenues.

Fees for lodging are levied in spa towns or at facilities serving as temporary residences. The fee can even be collected from owners of family homes if even a part of the house is used for paid lodgings. The fee may not be levied on lodging for students and pupils.

1.5 Motor Vehicle Fee for Restricted Areas.

Fees levied on vehicles entering into restricted places in the municipality are limited to 20 Kc per day, which can be paid in a lump sum if the municipality so chooses. The legislative purpose of this fee is to limit the movement of motor vehicles in certain locations, preserve the tranquillity of historical parts of towns, or to improve the environment in such places. The fee is not paid by property owners, persons or businesses having permanent residence in such areas; nor is it paid by their close relatives or by handicapped persons.

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5 See Ibid., p. 21.
6 See Ibid., p. 29.
7 See Ibid., p. 36.
8 See Ibid., p. 38.
9 See Ibid., p. 44.
1.6 Fee for Slot Machines.

The municipality is not required to offer exemptions from this fee, which must be paid for each machine in use. The fee is paid by the machine’s permit holder, a Czech corporation without property participation of non-citizens. The tariff for each machine ranges from 1000 to 5000 Kc for a three month period; it can be set differentially, depending *inter alia* on the machine's physical location.

1.7 Fee for Communal Waste.

The fee for gathering, collection, transport, separation, or removal of communal waste is paid by any corporate body which has permanent residence in the municipality, or by a household’s owner or the owner’s agent.

1.8 Fee for Enhanced Construction Property. A municipal fee can be levied for the enhancement of construction property by connecting it to water and sewage. The purpose of this local fee is to permit the supplying municipality to recover at least a part of its cost. It is paid by the owner of the construction property and can be collected only for the first connection to water and sewage.

In Slovakia, the fees applied are quite similar to those explained above. The following summary table will demonstrate the situation with regard to users fees in the Slovak Republic.

### EXHIBIT 1
LOCAL FEES IN THE SLOVAK REPUBLIC

<table>
<thead>
<tr>
<th>Fee</th>
<th>Subject of the fee</th>
<th>Maximum tariff</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>For usage of public space</td>
<td>Space</td>
</tr>
<tr>
<td>2.</td>
<td>For an apartment or part of one used for purposes other than dwelling</td>
<td>Rent</td>
</tr>
<tr>
<td>3.</td>
<td>For lodging</td>
<td>Bed</td>
</tr>
<tr>
<td>4.</td>
<td>For a spa town or tourist site</td>
<td>Person</td>
</tr>
<tr>
<td>5.</td>
<td>For a dog</td>
<td>Dog</td>
</tr>
<tr>
<td>6.</td>
<td>Entrance fee</td>
<td>Entrance fee</td>
</tr>
<tr>
<td>7.</td>
<td>Sale of alcohol or tobacco</td>
<td>Retail value</td>
</tr>
<tr>
<td>8.</td>
<td>Motor vehicle access to restricted areas</td>
<td>Motor vehicle</td>
</tr>
<tr>
<td>9.</td>
<td>Advertising in public area</td>
<td>Advertisement</td>
</tr>
<tr>
<td>10.</td>
<td>For entertainment machines</td>
<td>Machine</td>
</tr>
<tr>
<td>11.</td>
<td>For vending machines (500% extra for alcohol or tobacco)</td>
<td>Vending machine</td>
</tr>
<tr>
<td>12.</td>
<td>For placement of nuclear facility</td>
<td>Nuclear facility</td>
</tr>
<tr>
<td>13.</td>
<td>For collection, transport and processing of communal and small construction waste</td>
<td>Amount of waste</td>
</tr>
</tbody>
</table>


Local fees in Slovakia were established by law 544/1990, which came into effect on January 1, 1991. Since

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10 See *ibid.*, p. 45.  
11 See *ibid.*, p. 48.  
12 See *ibid.*, p. 61.
that time, the law has been modified in more or less minor ways on ten different occasions. Exhibit 1 shows which users fees may be levied by municipalities. Gains from these fees (not including revenues from the fee for collection of communal waste and the fee on placement of nuclear facilities) reached 940 million Sk in 2001.

1.9 The fee for the sale of alcoholic beverages and tobacco goods

This fee accounted for about 50 per cent of the total revenues derived from fees in Slovakia. Because they are in conflict with regulations of the EU, however, which allow alcohol and tobacco to bear only one tax burden, this fee will be repealed to avoid the double tax practice currently in effect.

1.10 The fee for usage of public space

This fee yields the second largest share of total receipts, the top revenue gains being generated by the fee for collection of communal waste, which yields 20 per cent of total municipal revenues.

1.11 The fee on placement of entertainment machines

This fee has had a strong tendency to yield declining revenues, largely because the municipalities are often unwilling to have them available, since they are often exposed to vandalism. Some fees are perceived as being inequitable. The fee on lodging has the character of a property tax, for example, while restaurant capacity is, in contrast, not taxed.

The gain from the principal seven national taxes is 400 times larger than the gain from Slovakia’s ten local fees. So some question whether from a strictly financial point of view it would not be better to repeal them. The significance of local fees, however, lies in the fact that the municipality independently decides which it will impose and how the revenues they yield will be utilized. They represent a small, but important part of the independence of Slovak local governments.

1.12 Recent Legislative Change on Fees in the Czech Republic

Law number 229/2003 Coll, enacted on July 31, 2003, was the first major revision of the original Law Number 565/1990 Coll on local users fees. Changes in the law were motivated in part by the desire to increase local fees and necessitated by the development of the new regional governments. The new law will have no impact at all on the following fees: 1) the fees for driving in restricted areas in the municipality, 2) for the use of slot machines, 3) fees for use of the communal waste system, and 4) for constructions sites enhanced by water and sewer connections. The new law stipulates that fees not paid on time or for the unpaid share of fees only partially paid may be increased by municipalities up to three times. In the past they could be increased only up to 50 per cent.

The most significant legislative change pertains to the fees for dog licenses. This law might almost have been entitled, „Closing the Loophole on Dog Licenses.” Apparently, too many Czechs had minimized the fee for a dog asking a friend or relative residing in a low-fee dog-license area to declare themselves the „owner“ of the animal. Thus, the license acquired by the „keeper“ of the animal was not for the place where the animal resided. The new law will no longer permit this to occur. The “owner” will no longer pay the fee for the license, but the individual in possession of the animal, which must be licensed where it resides. After the first of January, 2004, licensing fees were increased from 1,000 Kč to 1,500 Kč per year for the first dog over three (formerly six) months of age. For the second and any additional dogs, municipalities may increase the

annual fee another 50 per cent. Dogs kept for other „non-recreational“ purposes pay significantly lower rates or may be exempted.

Fees for a stay at a recreational or spa site were increased from 2 Kč per day to 4 Kč and fees for the use of public space were discussed and clarified, so that applications of and exemptions for the fees would be more uniform.

It was the intent of parliament that the new law provide some financial advantages for the municipalities. Positive changes for them include the possibilities of increasing the rates of several of the fees they may elect to implement and an extended period over which fees due under the old system would still be in force.

These changes will enhance municipal budgets and rationalize the fees system somewhat, but would not seem to provide promise for an alleviation of the problems of fiscal decentralization in the Czech Republic.

Chapter 2. Local Budget Revenues Derived from Users Fees

In this section the objective will be to make a brief review of the revenue implications of users fees. It is difficult to find data on the subject, since municipal revenues derived from users fees are not reported at the Czech or Slovak Finance Ministry sites on line. The Finance Ministries are willing to talk about them in general term and provide interesting perspectives as seen in section I, but are unable to give detailed response to requests for data. Slovakia. In Bratislava an officer of the Finance Ministry suggested that users fees represented only approximately 10 per cent of the revenues of Slovak municipal budgets. She later updated that approximation14 with the estimate that local users fees represent only 5.6 per cent of the total tax revenues of the municipalities. Czech Republic. As is apparent in Exhibit 2, in 2001 and 2002 revenues from users fees in the Czech Republic were actually larger than property tax receipts. That failed to indicate, unfortunately, that such fees represented a significant amount of revenue; rather, it comments on the insignificant property tax yield. Local fees for the years in question represented only 2.9 per cent and 3.8 per cent of total municipal receipts.

EXHIBIT 2

Municipal Revenues, Czech Republic, 2001 and 2002

<table>
<thead>
<tr>
<th>Revenue Source</th>
<th>2001</th>
<th>2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax Revenues</td>
<td>88 838</td>
<td>99 549</td>
</tr>
<tr>
<td>Users Fees</td>
<td>5 388</td>
<td>7 998</td>
</tr>
<tr>
<td>As % of Total Revenues</td>
<td>2.9%</td>
<td>3.8%</td>
</tr>
<tr>
<td>Property Tax</td>
<td>4 568</td>
<td>4 571</td>
</tr>
<tr>
<td>As % of Total Revenues</td>
<td>2.5%</td>
<td>2.2%</td>
</tr>
<tr>
<td>Users Fees + Property Tax (as % of TR)</td>
<td>5.4%</td>
<td>6.0%</td>
</tr>
<tr>
<td>Non-tax Revenue</td>
<td>23 016</td>
<td>23 809</td>
</tr>
<tr>
<td>Capital Revenues</td>
<td>10 583</td>
<td>11 588</td>
</tr>
<tr>
<td>Own Revenues</td>
<td>122 438</td>
<td>134 947</td>
</tr>
<tr>
<td>Grants</td>
<td>61 800</td>
<td>73 256</td>
</tr>
<tr>
<td>Current</td>
<td>47 198</td>
<td>55 844</td>
</tr>
<tr>
<td>Capital</td>
<td>14 602</td>
<td>17 412</td>
</tr>
<tr>
<td>Total Revenues</td>
<td>184 239</td>
<td>208 204</td>
</tr>
</tbody>
</table>


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14 Email from Mrs. Krkanová on August 11, 2003.
We observe likewise in Exhibit 2 that property tax receipts for the two years as a share of total receipts amounted to only 2.5 and 2.2 per cent respectively. The combination of both local fees and property tax, which are appropriately considered together because they are normally both the primary sources of a municipality’s “own” revenues and represent a proxy measure of a municipality’s fiscal autonomy. In an email of Dec 23, 2003 from Dr. Zdenka Jiraskova of the Czech Finance Ministry, local fees revenues for 2002 were reported to me to be a much smaller 2.2 billion Kč, but Jiraskova indicates also that the gains for local fees for communal waste, which are recorded separately, were another 2 billion Kč for 2002.

The correct observation is that with respect to users fees, as is the case for property tax receipts in the Czech Republic, municipalities can have no pronounced sense of fiscal autonomy. The process of fiscal decentralization has not been successful; nor have users fees contributed significantly to fiscal autonomy.

Chapter 3. Users Fees as a Supplemental Revenue Source

Although the first concern for public prices is cost recovery, policy and circumstances may also permit a municipality to charge less than the full cost of service provision or to seek the recovery of more than the full cost. It will be the assumption of this section that Czech, Slovak and other municipalities should at least consider pricing that achieves the maximum potential contribution to general revenues. There will be many instances, of course, where the national parliament and laws, or important political considerations will prohibit the municipality from implementing prices that, from its own perspective, are optimal in terms of receipts. In appropriate instances, such suggestions as offered below certainly could and would be ignored by municipal authority. But where appropriate, suggestions offered are intended to provoke thoughts on enhancing municipal receipts.

As the potential for revenue maximization is reviewed, it should also be remembered that differing prices may be needed to reflect not only differing demand elasticities in separable markets, but may also have to reflect whether the service provided meets an essential human need and whether cost differentials in diverse market segments reflect choice responsive to higher incomes. Sometimes the affluent choose to live further from the city centre and should willingly pay the higher costs of that location. If, however, the poor choose to live further from the centre because such a place is the only one where they can afford land and shelter, most would not favour charging them higher service prices to add to their financial burdens.

Such issues are sometimes difficult to resolve and they confront public housing authority when establishing rents which will vary substantially where different generations of housing construction have experienced divergent construction costs and market interest charges. These differing market segments require individual treatment. Not only will varying costs be accounted for as suggested, but varying demand elasticities will be addressed to generate greater revenues through price discrimination. Reasonable pricing would suggest that prices be responsive to the full cost of production, as well as the public’s willingness to purchase public goods or services, just as they must be in the private sector. Too often complete cost recovery is not really attempted in public service provision. Where the users are not impoverished, it is hardly appropriate to fix prices below full-cost level (not including the amortization of capital assets at their current, not historic, value) so that they must be subsidized from general revenue. The price should be comparable to what it would be for a commercial operator using the same amount of capital, since this is the test of market

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viability. The test of comparability, moreover, can be fully met only if public service prices include the
equivalent of the taxation faced by the private supplier.

There are instances, of course, where less than full cost recovery is appropriate. Where a public service is
provided with collective benefits such as would justify charging no price at all, a positive price would
nevertheless be suggested to impose discipline upon consumption. In that case, the price should be at
a level that would deter waste, but permit the desired minimum level of consumption across all incomes.
Another case is the one mentioned above: where a public good or service satisfies a basic human need for
which the impoverished are not expected to pay a full, cost-recovery price. Finally, a service may be
subsidized that primarily benefits the individual user, but the government wishes to encourage consumption
to achieve some public benefit or saving. We observe this rather frequently where municipalities subsidize
public transport to reduce traffic congestion, highway construction and repair costs, and to improve air
quality.

As is well known, subsidies tend to generate inefficiencies. Sometimes they benefit all consumers, even those
not in need of the subsidy. Sometimes they simply squander resources for a service that is not cost effective.
Such waste can be minimized by reducing prices only for low income groups, senior citizens, children, etc,
and by applying subsidies only to a minimum consumption level and market prices beyond that. In Hong
Kong and Tokyo, a minimal level of litres of water are supplied to all citizens at a nominal price. At higher
levels, consumption is priced at the full marginal cost.

In some instances pricing of public services may justifiably be based on more than full cost recovery, i.e.,
generating net revenues. Where prices are imposed with the intent to regulate consumption for which little
direct cost is involved, such as where municipalities derive revenues from licensing building or trading
activities, levying parking charges or issuing liquor licenses. Prices may also be established at greater than
cost-covering levels to enforce discipline in consumption. Telephone charges, where telecommunications
have not been privatized, may be graduated at peak-load hours to reduce congestion. Parking fees may be
established at prohibitive levels in large cities to reduce congestion in downtown areas. It should be
remembered, however, that charging above cost for public services should consider, just as taxation would,
the incidence and equity considerations that apply.

Consider now the kinds of techniques that should be applied as municipalities implement users fees, if they
wish to do so with an eye toward revenue maximization. There are two basic situations to be considered with
this tax. First, the municipality becomes a silent but important partner of private firms, which often provide
lodging or entertainment and whose revenues the municipality will essentially tax through the users fee. Here
the municipality attaches a fee to private sector activities. Examples are the recreation and spa fees utilized in
the Czech and Slovak Republics, the fees on local housing accommodations, fees on admissions to ticketed
entertainment, and those on gambling and slot machines.

In the other case, the municipality itself provides a service and can price as a monopolist would. There are
instances in which, for social and political considerations, it will provide an essential service also to low
income groups whose consumption it wishes to subsidize. Let us consider the kinds of services that officials
can dare to provide with revenue optimization in mind. Fees (qua taxes) charged for dog licenses, for garbage
collection, parking, and rents for public housing are examples where the municipality acts as a monopolistic
provider of services.

3.1 Fees Attached to Private Activities.

If a municipality establishes a unit or ad valorem fee that is too low, it will fall short of the revenues it could
have obtained. If the fee is excessive, it can drive away the entertainment or other activity it would tax; if the
municipality’s revenue yield is so great that it removes from the private activity the revenues that would have
represented profit or even have covered cost, the fee will prove destructive. Even if these kinds of fees are
not extreme, they will distort resource allocation.

The fee should optimally reflect the characteristics of a lump-sum tax. The firm providing gambling or slot
machine revenues, or selling tickets to a concert or other form of entertainment, may be assumed to establish
ticket prices so as to maximize net revenues. The municipality then simply lays claim to its share of the take
without causing the firm to change its optimal price and quantity results. If the firm were to try to “pass the
fee” on to the consumer, raising its price would merely reduce ticket sales and generate a smaller profit pool, from which the pre-determined amount would still have to be turned over to the municipality.

Ideally, the municipality would determine or estimate the net revenues the project would generate on municipal property, and decide what share of the net revenues it would appropriate for public coffers as a lump-sum tax. It would then levy the fee as a lump sum in the form, say, of a license to perform. If the municipality felt constrained to simulate the more traditional per-ticket fee, it should divide the total revenue anticipated by the number of tickets sold ex post, and collect an average revenue per ticket. In any case, the private firm should know a revenue total that it will have to turn over from the ticket sales and not think of it as a per ticket amount that must be attached to each ticket sold. If the fee is incorrectly treated as an excise or unit tax, it would increase the price of each ticket, forcing the price higher and resulting in a sub-optimal quantity of ticket sales.

Where the objective of such action is fee-maximization, pricing should follow this pricing strategy. Assume that local authorities needed to calculate potential revenues for a circus requesting permission to perform in the city. Consider the calculation of the maximum potential net revenue (NR) at the optimal quantity of sales. For simplicity, let us assume that the circus has a fixed cost for the delivery of a single night’s performance. All of the normal “variable” costs for a given evening are determined by the cost of a single performance, and so can be treated as fixed. The municipal entertainment fee will simply appropriate revenues by reducing the net revenues of the circus for each performance by the amount of what is equivalent to a lump-sum tax. If properly applied, this methodology will change neither the price of a ticket or the number of tickets sold.

Compare this with an “excise” fee that would cause after-tax total costs to increase with each unit ticket sale by the amount of the fee. Here, increased sales imply increased per-unit costs by the amount of the tax. In this case, the firm would optimize its returns by equating marginal costs and marginal revenues, but at the higher price implied, sales will be at a lower level, below the level at which the MC = MR equality coincides with higher, optimum sales and revenues. This results in reduced, suboptimal ticket sales, smaller net revenues, smaller tax take, and smaller profits.

What is happening here is illustrated in Exhibit 3. In the left column the circus in Slovakia sells 1,250 tickets for the performance of a single evening at 320 Ks per ticket. This is an optimal quantity and price resulting in TR of 400,000 Ks with net revenues of 80,000 after deducting the total cost of 320,000 to pay the cast and expenses. The municipality takes the 50,000 it had targeted for its fee, leaving the circus 30,000 Ks.

| EXHIBIT 3 |
| Entertainment Fee: Lump Sum vs Excise Tax |

<table>
<thead>
<tr>
<th>(Fixed) Total Cost of Performance</th>
<th>Lump Sum</th>
<th>Excise Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>TC = 320,000 Ks</td>
<td>TC = 320,000 Ks</td>
<td></td>
</tr>
<tr>
<td>Number tickets sold</td>
<td>Q = 1250</td>
<td>Qat = 1050</td>
</tr>
<tr>
<td>Price of ticket</td>
<td>P = 320 Ks</td>
<td>P = 320 + 40 Ks</td>
</tr>
<tr>
<td>Total Revenue</td>
<td>TR = 400,000</td>
<td>TR = 378,000</td>
</tr>
<tr>
<td>Net Revenue</td>
<td>NR = 80,000</td>
<td>NR = 58,000</td>
</tr>
<tr>
<td>Target Municipal Revenues</td>
<td>Fee = 50,000</td>
<td>Fee = 50,000</td>
</tr>
<tr>
<td>Net Revenue before Fee</td>
<td>NRbf  = 80,000 Ks</td>
<td>NRbf = 50,000</td>
</tr>
<tr>
<td>Actual Fee received</td>
<td>40 Ks(1250) -50,000 Ks</td>
<td>40 Ks(1050) - 42,000</td>
</tr>
<tr>
<td>Net Revenue after Fee</td>
<td>NRaf = 30,000 Ks</td>
<td>NRaf = 16,000</td>
</tr>
</tbody>
</table>

The right column demonstrates the inadequacy of the excise-type fee. The 40 Ks fee is attached to each ticket so that the total ticket price becomes 400 Kc, reducing ticket sales to 1,050 and yielding total revenues of
378,000 and NRbf = 58,000. But the circus must still pay 40 Ks (1,050) = 42,000 Ks to the municipality, leaving the post-fee take at NRaf = 16,000 Ks for the circus. The higher ticket price (including the municipality’s fee cut) reduced ticket sales, fee revenues, and the net revenues of the circus after imposition of the fee.

3.2 Fees Applied to Public Service Provision.

In the case where the municipality supplies a service or sells a licensing fee, it can act as a monopolist and maximize revenue. Assume a city wanted to charge for dog licenses and legislation were passed to allow that city to establish its own price. The city would not forget, of course, that the license has a regulatory function and that it is levied primarily against dog ownership as entertainment. As we saw above, dogs used to assist the handicapped or perform other professional functions are licensed at a reduced fee.

The municipality would maximize revenues by operating at the centre of its demand curve extended from axis to axis at the point where demand elasticity is unitary, since at that point MC = MR = 0 in an essentially no-cost activity for the municipality. It could attempt to determine its demand curve econometrically or through questionnaires to potential consumers, but if it had doubts whether it were enjoying maximal revenues it would be easiest to experiment at the margin, observing whether price increases would reduce the quantity of licenses demanded and cause net revenues to decline.

A somewhat more sophisticated revenue effort would obviously incorporate price discrimination, charging somewhat lesser fees for senior citizens, low-income groups etc. Attention paid to demand elasticities would likely result in lower fees to rural citizens where possession of animals is less an expression of demand for “entertainment.” It is possible that where dogs in rural areas perform no work function, their maintenance for entertainment purposes might be in less demand than it would be in urban settings. Here we would be concerned with third degree price discrimination in which individual market segments would command their own individual licensing fee, roughly taken from demand curves directly above the point where MR curves intersect the quantity axis.

It is imperative, of course, that municipal officers (and the national officers and lawmakers who have usurped local governance in hyper-centralized transition economies and who control legislation constraining municipal prerogatives) take into account the social considerations that may take priority over the municipal’s revenue yields. Once that has been done, however, it is only reasonable that Czech and Slovak municipalities (not to mention other financially stressed subnational governments in transition) apply methodologies in the application of local users fees that will permit them to enjoy the greater revenues that are desperately needed.
References


Zakon Slovenskej národnej rady y 27. novembra 1990 o miestnych poplatkoch