Administrative Simplification and Local Finance
– International Compared Experiences

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You can access some of my papers and references to academic / research activities in connection with my Jean Monnet Chair at:
1. Administrative simplification and administrative reform in Portugal at local level has been for years a theme in flux, but that particularly happens at the present moment in the context arising from the Memorandum of Understanding related with the economic external assistance to Portugal [signed with the International Monetary Fund (hereinafter ‘FMI’), the European Commission (hereinafter ‘Commission’) and the European Central Bank (hereinafter ‘ECB’) in June 2011]. The basic and overall goal that has been established in this domain in the Memorandum of Understanding (quoting from its Second Update – 9 December 2011) – as part of a pillar of so called structural budgetary measures – would, in fact, imply a drastic reorganization of local government administration. As stated in point 3.44. of such Memorandum of Understanding, there are currently 308 municipalities and 4259 parishes (in Portuguese, ‘freguesias’, the smaller local units in terms of local administration) and the government should develop until July 2012 a consolidation plan to reorganise and significantly reduce the number of those entities, so that these changes would fully come into effect by the beginning of the next local elections cycle.

Furthermore, the government should carry out a study to identify potential duplication of activities and other inefficiencies between the central administration, local administration and locally based central administration services (so that the existing framework would be reformed and the identified inefficiencies eliminated).

On the basis of these overriding objectives the government has approved a (i) Resolution of the Council of Ministers (Resolution Nº 40/2011, of 22 September) and a (ii) general policy paper entitled Green Paper on the Reform of Local Administration which purported to be a starting point
for a wide discussion involving citizens in general, political parties and stakeholders in this domain so that by the end of the first semester of 2012 new guidelines could be established and developed through legislation bringing about a reformed framework for local administration in Portugal. This Green Paper put forward the idea of a true reformist shock in this area (and, as we shall observe, it is, as such, probably too ambitious in formal terms and has underestimated the practical difficulties that are to be found both in delineating in detail the reforms and particularly in actually implementing those same reforms).

Another axis of this reform movement has been (iii) the adoption of Organic Law N.º 1/2011 (of 30 November) and of Decree-Law N.º 114/2011 (of the same date) extinguishing the so-called Civil Governors (formally designated by the Government to major territorial circumscriptions – districts – all over the territory and, differently from the governing bodies of municipalities and parishes, not elected by citizens). In practice, this meant eliminating an intermediary level of de-concentrated local government administration (not a decentralised one, because this is inherently connected with direct election of the respective governing bodies by citizens), transferring its powers or functions to other de-concentrated entities of the national government (with the corresponding expect reduction of public expense).

However, what we chiefly purport to discuss here is the reform of local administration strict sensu (which does not truly comprehend the reorganization of those non-elected de-concentrated local bodies or institutions).

2.1. – In light of these instruments – in particular of the Resolution N.º 40/2011 of the Council of Ministers and of the Green Paper on the
Reform of Local Administration – this reform of local administration *strict sensu* (excluding here de-concentrated bodies) involves four essential vectors: (i) the local public undertakings; (ii) the organization of the territory; (iii) municipal, inter-municipal management and its financing and (iv) local democracy.

2.2. – The first vector comprehends various measures of a very uneven importance. We may refer here, *inter alia*, freezing every process of creation of new municipal undertakings (public undertakings owned by municipalities) and, in parallel, to develop an overall analysis of cost-benefit relation of all undertakings that are part of the sector of municipal undertakings, bearing in mind the financial sustainability of these entities, the financial flows underlying the activities of these undertakings and the structure of own proceeds of the same entities (considering the outcome generated by these entities in terms of public service or requirements of the local populations of municipalities). This overall analysis, in turn, must pave the way for the establishment of operative criteria determining the termination or merger of multiple municipal undertakings.

These, on the whole, represent corrective measures of the legal framework of municipal or local undertakings (owned or controlled by municipalities) which had allowed a process of significant expansion of this sector of municipal undertakings all over the country, based on formal safeguards which were not economically realistic. Supposedly, under the law on municipal undertakings,¹ municipalities could only establish new undertakings on the basis of economic and financial studies that demonstrated the financial sustainability of those entities and the entrepreneurial nature of the activities they would pursue. In practice, such formal requirements were rather easily downplayed and these types of

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¹ We refer here to Law n." 53-F/2006, of 29 December (that is being currently repealed).
economic studies frequently distorted towards supporting the massive creation of municipal undertakings. Accordingly, beside terminating or merging many of the current municipal undertakings, the ultimate purpose of this process is also to reform the law on local municipalities in a manner that will significantly constrain the ability of municipalities to create new public undertakings under their control. This new law will also provide for much stricter limits on indebtedness (on debt) of municipal undertakings. This represents, as far as I am concerned, a fundamental area to correct the financial imbalances of many municipalities because municipal undertakings were frequently used as rather artificial vehicles to assume more debt.

2.3. – The second vector concerning the organization of the territory comprehends, inter alia, a full review of the current administrative map aiming towards the substantial reduction of parishes (‘freguesias’), obtaining a better scale and dimension more adequate to their different typologies (e.g., rural areas, urban areas, transition areas, etc). In parallel, at the level of municipalities, that may be regarded under Portuguese law as the paradigmatic local entity, the overriding goals is to stimulate the process of integration of municipalities, although bearing in mind the specificities and own territorial identity of some of these entities.

I am referring to municipalities as the archetypical local entity\(^2\) because although the Portuguese Constitution envisages since 1976 the creation of larger Administrative Regions – somehow succeeding to the current districts although with the fundamental difference that such Regions would involve a higher qualitative level or more intense level of decentralisation

\(^2\) See emphasizing such paradigmatic role of municipalities under Portuguese law as regards local government, the influential position of Sousa Franco, the late Prof of public finance and former Minister of Finance at the time of Portugal’s accession to the Euro, in Finanças Públicas e Direito Financeiro, vol 1, 4 th edition, 13 th reprinted, Coimbra, Almedina, 2010, pp 278.
since their respective governing bodies would be elected – the so called
regionalisation process has never been launched (a few years ago a
referendum was held about the possible start of a regionalisation process
but its outcome was a majority of votes against the initiation of the
regionalisation process and so this option has been ‘de facto ‘ frozen or
blocked from that time onwards and will predictably remain so for the
coming years).
I should add, for the sake of clarity and also of brevity, that we may, to a
large extent, anticipate already at the end of the first semester of 2012 that
these goals enshrined in the second vector of administrative reform and
simplification of local law (concerning the organization of the territory)
have not been extensively fulfilled. The reduction of the number of smaller
territorial circumscriptions (parishes or ‘freguesias’) will apparently be
very limited and there has been widespread political opposition, albeit a
rather diffuse one, from the major parties, including the ones involved in
the governmental coalition (which control a significant part of
municipalities), to the actual integration of municipalities.

2.4. – The third vector that I have referred (municipal, inter-municipal
management and its financing) involves an assessment of the impact of the
joint exercise of competences of associative municipal structures, using as
benchmark two already existent Inter-Municipal Communities (one
predominantly rural and the other predominantly urban), aiming towards a
possible rationalization of public resources.
It must be briefly referred here that the Portuguese Constitution
contemplates the possibility of municipalities establishing between
themselves associations and federations of municipalities. What is at stake
is, therefore, a possible cooperative process between municipalities –
alternative to horizontal merger of these entities – bringing about a level of
local supra-municipal administration based on competences that have been transferred from municipalities (under various institutional forms but normally leading to the creation of a new collective entity or institution of public law (still basically subject to a 1999 legal framework\(^3\)). Under the so called territorial reorganization of 2003,\(^4\) were established in this field the so called Metropolitan Areas, as collective entities of public law and of territorial scope oriented towards the pursuit of joint interests of municipalities comprehended in such areas, of two different types, the big urban areas and the urban communities. At the same time were created the inter-municipal communities of public law whose scope is also twofold – on the one hand, inter-municipal communities pursuing general goals and, on the other hand, associations of municipalities pursuing a narrower set of some specific interests common to the participating municipalities.

We do not have here time to enter into the details of this **cooperative level of supra-municipal local administration**, largely enhanced by the 2003 territorial reorganization. What is relevant here is to emphasize that the 2011-2012 movement of reform of local administration – involving both its simplification and rationalization – is aiming to bring about a reinforced **status of supra-municipal local administration** (if necessary combining cooperative or voluntary elements with legal mandatory elements dependent on certain objective criteria based on specific parameters of economic rationalization of the activity of municipalities). In the end, it is clearly envisaged to ensure the materialization of these goals a comprehensive reform of the legal framework for associations of municipalities.

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\(^3\) We refer here to Decree-Law n.º 412/99, of 29 November).

\(^4\) The territorial reorganization of 2003 was essentially based in legislative terms on Law n.º 10/2003, of 13 of May, ando n Law n.º 11/2003 of the same date.
2.5. – Finally the fourth (aforementioned) vector of the envisaged reform (concerning local democracy) involves a reform of the electoral law of the bodies of local entities (commonly designated as comprehending both municipalities and parishes as local ‘autarquias’ under the influence that curiously the 1933 Constitution prior to the 1974-75 revolution received from Italian law, in connection with the idea of ‘autarchia’ – an entity which is self-sufficient in economic terms). Prospective legislative reform in this domain also is expected to deal with the missions attributed to municipalities and their corresponding powers and competences and with the institutional structures and organization of the bodies and services of municipalities (in order to reduce for efficiency and budgetary constraints the number and type of top officials of these bodies and services). To a certain extent, and regardless of the specific constraints of the Memorandum of Understanding in the context of external economic assistance to Portugal, we may admit that the driving force behind these purposes of legislative reform under the general ‘leit motif’ of enhancement of local democracy and dealing with a full scale overhaul of missions and power attributed to municipalities and the corresponding organizational structures has to do with a larger perception of widespread imbalances in local administration in OECD countries.

In fact, in these OECD countries a growing mismatch has been perceived or observed between the functional competencies and fiscal responsibility of local government⁵ (which, as such require a full scale overhaul of these local administrations in connection with

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⁵ See on this mismatch LOCAL GOVERNMENT FINANCE IN OECD COUNTRIES, Janice Caulfield, University of New South Wales - Paper presented to ‘Local Government at the Millennium’ International Seminar - February 19th, 2000, University of New South Wales.
corresponding reforms of the central administration in a context of administrative simplification determined by objectives of economic efficiency deeply intertwined with the growing scarcity of public resources and a drastic change which has probably come for years, as a structural change, of the conditions of indebtedness of States arising from the new patterns of functioning of sovereign debt markets).

3.1. – Considering in general these four fundamental vectors of the 2011-2012 reform of local administration in Portugal, supposedly aiming at simplification and greater economic efficiency and rationalization, I believe that their level of densification, conception and, consequently their predictable level of fulfillment, is very uneven. There is a clear lack of diagnosis of the main problems and blocking factors or intrinsic obstacles to reform and, furthermore, many of the very diverse, ambitious and rhetoric objectives delineated in the policy papers and master-documents embodying this reform are contradictory. We may question, inter alia, the statement of an ambitious objective of analyzing the current administrative local map, promoting the reduction of parishes and setting criteria for a growing integration of municipalities, in a context of drastic reduction of public resources that may be channeled to local entities, without assuming as a starting point the definition of a new model for the relations of the various levels of public administration, central, local (and the various sub-levels at the local sphere).

As far as I am concerned, clearly the more matured and consequent vector of reform of local administration is this first one, concerning the drastic reorganization of the sector of municipal undertakings, preventing abusive uses of the entrepreneurial forms and entities by municipalities and the not duly scrutinized recourse by those municipal undertakings to public-private partnerships (PPPs), for new public investments at local
level with ruinous financial consequences for local administration and with negative repercussions for Portuguese public finance on the whole (many of these to public-private partnerships corresponding actually to project-finance initiatives in which the private partner does not truly bring capital to the project but banking finance that it has previously ensured on the assumption of a very uneven distribution of the risks of the project between the public and the private partner, frequently unfavorable to the former one).

3.2. – On the whole, I acknowledge that within a set of too broad and largely contradictory objectives for administrative reform and simplification of local administration four key goals stand out:⁶ (i) as I have been mentioning, the rationalization of the sector of municipal undertakings; (ii) the appreciable reduction of the number of the smaller territorial circumscriptions (parishes or ‘freguesias’); (iii) reinforcement of inter-municipalism and (iv) a growing and more demanding interplay between, on the one hand, a new pluri-annual logic of financial programming at State/central level, determining a medium and even longer term budgetary strategy and a new qualitative form of scrutiny of budgetary management not so dependent on the political day-to-day debate, and, on the other hand, the local level of administration in spite of the autonomy guaranteed by the 1976 Constitution to local entities (‘autarquias’) and to local finance. Ultimately, what this new qualitative interplay between the central level of administration – gradually more influenced and determined by supranational economic governance requirements arising from EU integration (particularly in the Euro Area) – and the local level of administration requires is a recreation of the concept and functional basis of

⁶ See on these goals, but largely underplaying or not contemplating the fourth one which we regard of paramount importance see José de Melo Alexandrino, ‘Contexto e sentido da reforma do poder local’ (Paper, in Portuguese – no English version available - 4 November 2011).
grounds of the autonomy of local entities and of decentralization guaranteed in the 1976 Constitution. I would contend here that this constitutional principle of autonomy of local entities – shared under very diverse institutional formats by several unitary (non federal) EU Member States – has to be globally re-thought and without being called into question in its fundamental assumptions its evolutionary nature should be acknowledge in a context of structural transformation of public finance in the EU and elsewhere.

Furthermore, within a global rethinking of the basic foundations of the constitutional principle of autonomy of local entities – in parallel with the global reform of the role and means available to the central administration – requirements of economic rationalization and inherent simplification (to some extent or at some instances) of local administration should involve a further qualitative differentiation of local entities even within the same legal categories. That would imply, for instance, conceiving and implementing forms of classification of the archetypical local entity in Portugal (the municipality), on the basis of a legal and economic typology based on objective criteria. Just to exemplify, under Portuguese law state-owned undertakings and its managers are classified under different categories (periodically reviewed) in accordance with the economic level of complexity of their activities or the relative importance of the economic sectors in which they operate or of the tasks they perform. That, in turn, determines some degree of differentiation of the duties and also of the rights (e.g. in terms of remuneration) of the managers of these undertakings. Mutatis mutandis, without multiplying different legal categories of local entities – for reasons of administrative simplification – and keeping the municipalities as the paradigmatic local entity under
Portuguese law, this would ensure a flexible and differentiated treatment of municipalities in accordance with some overriding economic realities.

4. – We have no time to deal here with ongoing reform of local finance and also, beside these time constraints, such reform is still taking shape at this very right moment (therefore being premature to anticipate its main features). Suffice is to add that the Portuguese government empowered at the beginning of 2012 a Working Group with the mandate to present a proposal of comprehensive reform of the law on local finance (or law on the finance of local entities) until the middle/end of June 2012. We, therefore, purport to present an expanded version of this DRAFT PAPER incorporating a development of this point 4, and of the essential topics and guidelines underlying this prospective reform of local finance (actually taking place and to be developed in the coming days).

What we may anticipate – as results from the proceedings of this Working Group on the reform of local finance and, particularly, from the Law which approved the Portuguese State Budget for 2012 – are, inter alia, changes concerning:

- Adjustments to the Law on local finance – which in turn was still recent and resulted from the 2006-2007 reform of local finance (culminating in the adoption of Law n.º 2/2007 of 15 January\(^7\)) – with purposes of consolidation of public finance, ensuring that in exceptional and transitory situations, and in spite of the autonomy constitutionally guaranteed to local entities, new legislative acts may limit the practice of acts by these local entities determining new financial charges with impact in national public finance, e.g. as

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\(^7\) Which had already been partially reviewed in 2007 and 2010 – we are not going into this kind of detailed comment of the legislative evolution in this domain.
regards the recruitment of new personnel, entering into contracts for the acquisition of goods or services;

- Adjustments to the Law on local finance, allowing for the establishment through future laws of extensive duties of the local entities to provide information and reporting on their financial management in order to ensure the collection and analysis of aggregated financial information concerning the organization, management of bodies and other aspects of financial management of local entities;

- Adjustments to the Law on local finance concerning new stricter limits to the growth of debt or to ability to contract debt by local entities;

- The inclusion of all relevant public entities controlled by local entities in the perimeter of financial consolidation of the local level of governance;

- Articulation with the reform of the framework law on budgetary process and budgetary management at central level, contemplating a greater emphasis on pluri-annual programming and on the pluri-annual identification of public expenses and, above all, involving a greater interaction with a new body created at central level which is the Council of Public Finance.

This latter aspect is particularly relevant, because such new body which has started operating in the course of this year of 2012 is purported to be
an autonomous body – with full technical autonomy – with the mandate of scrutinizing budgetary policy option and, especially, budgetary management in order to identify in a timely manner any major deviations of budgetary execution and also to identify pluri-annual consequences of certain policy options of governments and public administration (something that tends to be underplayed by governments on their day-to-day management frequently constrained by the electoral cycle). Here the overriding goal is to ensure that the Council of Public Finance will also to some extent scrutinize financial options and management of local administration, which, in turn, involves a re-evaluation of the financial autonomy of local entities, particularly municipalities (as I mentioned before) – a topic which is institutionally and legally very sensitive.