

Local Governments in Portugal

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After more than three decades of democracy, local governments in Portugal face new challenges with a significant increase in their attributions as well as a new role they have to play as providers of local public goods. Portuguese local governments have now the experience and the organization to aspire to move from quantity to quality, production to management, information asymmetry to transparency and accountability, monopoly to competition, growth to sustainability and bureaucracy to simplicity. In this paper we present an overview of the way walked by Portuguese local governments in the last three decades and we characterize the present problems they face concerning their financing.

Después de más de tres décadas de democracia, los gobiernos locales en Portugal se enfrentan a muchos cambios derivados de un incremento considerable de sus atribuciones, tales como el nuevo papel que han de jugar como oferentes de bienes públicos locales. Los gobiernos locales portugueses tienen ahora la experiencia y la organización necesarias para aspirar a moverse de la cantidad a la calidad, de la producción a la administración, de la información asimétrica a la transparencia y responsabilidad, del monopolio a la competencia, creciendo en sostenibilidad, y de la burocracia a la sencillez. En este trabajo presentamos una revisión del camino andado por los gobiernos locales portugueses en las últimas tres décadas y caracterizamos los problemas presentes a lo que han de enfrentarse relacionados, sobre todo, con su financiación.

Key words: local government finances, local governments, Portugal
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1. INTRODUCTION

After more than three decades of democracy, local governments in Portugal face new challenges with a significant increase of attributions as well as a new role as providers of local public goods. We may say that local governments in Portugal reached a stage of maturity and face now

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a new task agenda. Local governments have now the experience and the organization to aspire a shift from quantity to quality, production to management, information asymmetry to transparency and accountability, monopoly to competition, growth to sustainability, and bureaucracy to simplicity.

The new agenda requires qualified human resources, an appropriate institutional framework and the financial resources to cope with an increased sophistication in the provision of utilities to residents. In this paper we will focus on the institutional framework of local governments as well as their search for new financial resources. In section two we present an overview of the path trodden by local governments since 1979 and we characterize local government finance in Portugal. In section three we do a SWOT analysis of local governments financing considering the new challenges they face. In section four we analyse the agenda of local governments in the next decade and we present a set of programs and policy measures at local level. Finally, we derive some conclusions.

2. THREE DECADES OF DEMOCRATIC LOCAL GOVERNMENTS IN PORTUGAL

Local Governments in Portugal have been conferred constitutional dignity since 1976. Their attributions and competences are established by the laws 159/99 and 169/99 modified by law 5-A/2002. Local governments have their own personnel, patrimony and finances, and their administration pertains to their political bodies. The central government only has legal inspective powers in situations established by law.

Portuguese local governments are composed by the administrative regions, two autonomous regions (Azores and Madeira), 308 municipalities and 4259 *freguesias*. The administrative regions were not yet created despite having been established by the Constitution of the Portuguese Republic.

During the last three decades the number of municipalities has been fairly stable (only three municipalities were created) despite the strong movement in favor of secessions from existing municipalities. Portuguese municipalities differ in size, and this asymmetry has increased as a consequence of emigration. As can be observed in table 1 between 1981 and 2005 the number of municipalities with less or equal to 5,000 residents has increased from 19 to 34. From 1981 to 2005 the number of municipalities with less or equal to 10,000 residents increased by twenty.

Table 1. Portuguese Municipalities by Population Size

Population	1981		1986		1996		2005	
	Number	%	Number	%	Number	%	Number	%
1 – 5,000	19	6.23	19	6.23	32	10.49	34	11.03
5,001 – 10,000	70	22.95	69	22.62	76	24.92	75	24.35
10,001 – 20,000	91	29.84	89	29.18	75	24.59	70	22.73
20,001 – 50,000	79	25.90	82	26.89	73	23.93	72	23.38
50,001 – 100,000	28	9.18	24	7.87	25	8.20	33	10.72
>100.000	18	5.90	22	7.21	24	7.87	24	7.79
Total	305	100.00	305	100.00	305	100.00	308	100.00

Source: Own calculations based on INE estimations.

1979 is an important date for local governments in Portugal. For the first time a law regulates the finances of local governments. From then on it has been subject to additions, amendments and several changes. Presently, local government finances are regulated by the law 2/2007 changed by law 22-A/2007.

Despite the growing importance of local governments, the level of decentralization of expenditure in Portugal is still small. In table 2 we can observe that the percentage of expenditure of local governments in total expenditure of general government was in 2006 below 13%.

Table 2. Expenditures of Local Governments as a Percentage of Expenditures of General Government

Year	%
1979	12.41
1987	10.40
1996	11.52
2005	13.10
2006	12.99

Source: Government Statistics, EUROSTAT.

An important feature of local governments and, in special, of municipal activity in Portugal is the percentage of resources devoted to investment. As we can observe in table 3, comparing 1987, 1996 and 2005, we verify that annual investment is always above 32% of total annual municipal expenditure.

Table 3. Structure of Municipal Expenditures (%)

	1987	1996	2005
Current Expenditures:			
Personnel	29.1	23.7	27.2
Goods and services	14.7	14.9	19.1
Current transfers	6.7	7.6	5.9
Other current expenditures	3.9	3.5	4.2
Subtotal	54.4	49.7	56.4
Capital Expenditures:			
Investment	38.8	33.2	32.1
Capital transfers	4.1	5.6	6.0
Financial assets	0.3	2.1	1.0
Financial liabilities	2.3	9.3	4.2
Other capital expenditures	0.1	0.1	0.3
Sub-total	45.6	50.3	43.6
Total	100.0	100.0	100.0

Source: Finanças Municipais - DGAA; Finanças das Administrações Públicas, INE.

Municipalities in Portugal depend heavily on inter-governmental transfers. Despite the increase in the relative importance of direct taxes, indirect taxes and user charges, and sale of goods and services in municipal receipts, transfers (current and capital) account for more than forty-five percent of total receipts in 2005. The growing importance of debt is also a feature of the structural changes observed in the last three decades concerning municipal financing. More restrictions on municipal debt have been determined in recent years, and the decrease of the importance of this source of income between 1996 and 2005 can be noted below.

Table 4. Structure of Municipal Receipts (%)

	1987	1996	2005
Current Receipts:			
Direct taxes + indirect taxes + user charges	27.1	24.0	33.9
Sale of goods and services	7.4	12.6	9.0
Current transfers	30.4	19.2	22.3
Other current receipts	1.9	1.9	2.8
Subtotal	66.8	57.7	68.0

Capital Receipts:	1987	1996	2005
Capital transfers	26.0	26.6	21.7
Financial assets	0.1	1.4	0.4
Financial liabilities	3.7	11.6	4.8
Other capital receipts	3.4	2.7	5.1
Sub-total	33.2	42.3	32.0
Total	100.0	100.00	100.0

Source: Finanças Municipais - DGAA; Finanças das Administrações Públicas, INE.

Despite many changes introduced in the Law of Local Finance during the last three decades, municipal financing in Portugal can be characterized by five major features:

- i) The low level of municipal fiscal autonomy.
- ii) The importance of real estate property as a fiscal basis for municipal taxes and user charges.
- iii) The redistributive nature of intergovernmental grants, with poor municipalities relying mainly on transfers from central government.
- iv) The small, but increasing importance of fiscal competition among municipalities.
- v) The importance of investments in the management of the political business cycle.

2.1. LOW LEVEL OF MUNICIPAL FISCAL AUTONOMY

In table 5 below local government's fiscal autonomy is classified into eight levels.

Table 5. Levels of Local Government Fiscal Autonomy

Level 1	Fiscal basis of local taxes set by municipalities.
Level 2	Fiscal basis of local taxes is not set by municipalities. Rates set by municipalities.
Level 3	Fiscal basis of local taxes is not set by municipalities. Rates defined by municipalities from a pre-determined range.
Level 4	Municipalities have the power to set user charges.
Level 5	Municipalities collect their own taxes but do not set their fiscal basis or their rates.
Level 6	Municipalities participate in central governments tax receipts (revenue sharing).
Level 7	Municipalities receive unconditional inter-governmental grants.
Level 8	Municipalities receive conditional inter-governmental grants.

Portuguese municipalities collect their own taxes and user charges, collect fines, obtain receipts from the sale of goods and services, receive intergovernmental transfers, benefit from the sale of assets, receive donations and inheritances, receive dividends and obtain loans.

Two major local taxes in Portugal have the real estate property as a fiscal basis. One (IMI) is a tax on the real estate property and another one (IMT) is a tax on the transfers of real estate property. In the former case, municipalities can choose the rate from a range of rates. In the latter case, the tax basis and the rates are not under the control of municipalities.

Other municipal taxes are a tax on corporation income (DERRAMA) and part of the receipt of a tax on automobiles (*Imposto Único de Circulação*). In the first case, municipalities may choose to collect the DERRAMA, but the rate range is defined by central government. In the second case the fiscal basis and rates are not under control of municipalities.

Portuguese municipalities have an important fiscal autonomy concerning the collection of user charges, but they have to show that there is proportionality between the user charges and the cost or benefit associated with the service that leads to the collection of those user charges.

Intergovernmental grants are mainly unconditional grants and their total amount and distribution among municipalities are defined using formulas ensuring that financial resources transferred to municipalities are not subject to political manipulation.

Considering the description above, we may conclude that Portuguese municipalities have a low level of fiscal autonomy: level 3 for some taxes; level 4 for user charges; level 5 for some taxes; level 6 and 7 for inter-governmental transfers; and level 8 for conditional inter-governmental grants.

2.2. THE IMPORTANCE OF REAL ESTATE PROPERTY AS A FISCAL BASIS FOR MUNICIPAL TAXES AND USER CHARGES

The need to ensure the neutrality principle in local government's finances determines the use of taxes based on the benefit of tax payers. The tax on real estate property (IMI) can be understood as a tax based on the benefit of tax payers if the value of property is subject to frequent updating. In such a case, municipal expenditures in amenities and public infrastructure will contribute to the increase in the value of real estate property and hence will lead to more tax receipts collected by the municipality. The growth of tax payments will not determine voting with

the feet by residents if there is proportionality between the increase in resident's benefits and the increase in resident's local taxes. This type of tax has the additional benefit of providing tax payers with the appropriate incentive to scrutinize the quality of governance at local level. Additionally, a tax on real estate property is acceptable on equity grounds.

The above arguments have been decisive to keep real estate property as an important fiscal basis of municipal taxes in Portugal. There are shortcomings, though, namely the fact that real estate property is the basis for two important municipal taxes and it is simultaneously the basis for many user charges at local level. Therefore, there is the widespread feeling that real estate property plays an excessive role on municipal finances causing two major negative effects: one is the permissive growth of construction in Portuguese cities; another is the excessive fiscal burden on housing.

In recent years municipalities benefit from the reform introduced in municipal taxes on real estate property. This effect is observable on IMI (municipal tax on real estate property) with receipts showing high rates of growth. The growth of municipal fiscal receipts has generated an opportunity for municipalities to diminish the rates of IMI, but the decrease in the rates of IMI has been insufficient to avoid the growth of the relative importance of real estate property as a fiscal basis at municipal level. This result will become more probable after the approval of the new *Law of Local Finance* that allows municipalities to give up to 5% of personnel income tax (IRS) collected from residents in their jurisdiction as a way to foster local development. With this new alternative, it is likely that the decrease in the rates of IMI will be smaller. Another consequence of the reform on local real estate taxes is the increase in inequity among Portuguese municipalities concerning their capacity to raise fiscal receipts and its implication on the design of even more redistributive inter-governmental transfers.

2.3. THE REDISTRIBUTIVE NATURE OF INTERGOVERNMENTAL GRANTS

During the last three decades there has been several changes in the way transfers from central government to municipalities are calculated. Despite these changes, the general characteristics of the system have been maintained. The amount of FEF (Financial Equilibrium Fund) to be transferred to municipalities is calculated using a formula (in the present it is equal to 25.3% of the average of the annual receipts of corpo-

rate income tax, personal income tax and value added tax). FEF is then divided into two funds (a General Fund and a Cohesion Fund). In the present, each fund receives 50% of FEF.

The General Fund finances municipal expenses (provision of local public goods and services). Therefore, it is distributed according to population, area, and other cost factors. In the present 5% of the General Fund is distributed equally among all municipalities, 65% according to population considering two correction factors for non permanent population and scale economies, 20% or 25% is distributed according to area, considering a correction factor for orography, and 5% or 10% is distributed considering the area of green zones under environmental protection (the latter case is applied when green zones under environmental protection account for more than 70% of the territory of the municipality).

The Cohesion Fund is distributed with the purpose to benefit less developed municipalities contributing this way for economic and social cohesion. Presently, this fund is subject to a correction by summing or subtracting a fiscal compensation to account for differences in the municipal tax basis. Municipalities with per capita municipal taxes above 1.25 of national average have a negative fiscal compensation. Municipalities with per capita municipal taxes below 0.75 of national average have a positive fiscal compensation. The Cohesion Fund is distributed according to an index of municipal social development compared with the national average.

After the approval of the present Law of Local Finance, municipalities will receive back 5% of IRS income tax collected from local residents. Municipalities can decide to reduce this percentage benefiting tax payers. This is an important change because it induces more fiscal competition among municipalities.

As we can observe in table 6, presenting per capita central government transfers to municipalities grouped by districts, FEF benefits much more the small and less developed municipalities, located in less developed districts (compare for example the per capita transfer of FEF to municipalities in the district of Bragança with the per capita transfer of FEF to municipalities in the district of Lisbon).

FSM is a fund set to finance education competences transferred from central government to municipalities. Therefore, it has not a redistributive purpose.

Table 6. Central Government Transfers to Municipalities Aggregated by Districts - 2008 (euros)

	Per capita FEF	Per capita FSM	Per capita transfer of IRS	Per capita total transfer
Aveiro	153	16	25	195
Beja	621	14	21	657
Braga	155	18	20	193
Bragança	626	14	22	661
Castelo Branco	416	13	23	452
Coimbra	205	12	38	255
Évora	446	14	28	488
Faro	179	15	33	228
Guarda	535	14	19	569
Leiria	176	14	25	215
Lisboa	40	9	64	113
Portalegre	605	15	24	644
Porto	86	16	32	134
Santarém	249	14	25	288
Setúbal	89	14	37	139
Viana do Castelo	297	15	19	330
Vila Real	413	16	20	449
Viseu	343	17	20	380
Açores	350	23	24	396
Madeira	219	20	32	270

Source: OE2008

2.4 THE INCREASING IMPORTANCE OF FISCAL COMPETITION AMONG MUNICIPALITIES

Fiscal competition among municipalities is still low, but with the reform of municipal real estate property taxes and the approval of the new Law of Local Finance it will go up quickly. In the past, there was an implicit equilibrium and the large majority of municipalities used to set rates of IMI at their maximum. But, the increase in the value of real estate property and a new perception by local executives of the benefits of fiscal policies created an opportunity for lowering IMI and IRS to taxpayers.

Concerning the IMI, two different ranges of rates were defined depending on recent evaluation of real estate property. The pressure to lower

rates is higher for recently evaluated real estate property because IMI collected is much higher than in the case of non-evaluated real estate property. As we can observe in tables 7 and 8, in 2007 more municipalities set the maximum rate for non-evaluated property than for evaluated property. The number of municipalities that set rates below its maximum is very high for evaluated property.

Between 2007 and 2008, 30 municipalities lowered IMI rates for non-evaluated real estate property (17 had in 2007 the maximum rate) and 8 municipalities increased IMI rates. Concerning evaluated real estate property, 49 municipalities lowered IMI rates (25 had in 2007 the maximum rate) and 6 increased IMI rates. So, more and more municipalities understand the importance of fiscal decisions to foster municipal competitiveness and consequently fiscal competition is increasing.

2.5. THE IMPORTANCE OF INVESTMENT IN THE MANAGEMENT OF THE POLITICAL BUSINESS CYCLE

Many studies have been published concerning the political business cycle at local level in Portugal. There is a solid empirical evidence that local executives manage the political business cycle and that local voters are more responsive to local investments rather than to quality of management indicators. The political pay-off of investments created the conditions for an excessive orientation of local executives to invest on infra-structures and social equipments without assuring the adequate operation conditions. If we consider this behavior and the lack of scale of many municipalities, it is no surprise that many local facilities have now low rates of use and some are short of funds to operate.

The last amendment to the Law of Local Finance considered this diagnosis and new requirements on provision of information to local voters and on accountability were established. Additionally, the new restrictions on municipal debt have been raising public concern on the financial soundness of municipal management, and consequently in the last local election (2005), a few executives used the value for money argument, providing extensive information on debt and quality of management. The electoral results obtained by those executives seem to confirm that such strategy worked out, and therefore it is predictable that more local executives follow this strategy in the future.

Table 7. Rates of IMI - Non-Evaluated Real Estate Property (2007)

Rates of IMI	Non-Evaluated real estate	
	Number of municipalities	%
50% of maximum rate	25	8.1
62.5% of maximum rate	6	2.0
68.75% of maximum rate	1	0.3
75% of maximum rate	50	16.2
80% of maximum rate	2	0.6
87.5% of maximum rate	80	26.0
90% of maximum rate	5	1.6
91.25% of maximum rate	1	0.3
95% of maximum rate	3	1.0
97.5% of maximum rate	2	0.6
Maximum rate	133	43.3
Total	308	100.0

Source : Jornal de Negócios (base de dados)

Table 8. Rates of IMI - Evaluated Real Estate Property (2007)

Rates of IMI	Evaluated real estate	
	Number of municipalities	%
40% of maximum rate	33	10.7
50% of maximum rate	1	0.3
60% of maximum rate	48	15.9
70% of maximum rate	18	5.9
75% of maximum rate	1	0.3
76% of maximum rate	1	0.3
80% of maximum rate	88	28.6
85% of maximum rate	3	1.0
86% of maximum rate	1	0.3
90% of maximum rate	19	6.2
94% of maximum rate	2	0.6
95% of maximum rate	3	1.0
96% of maximum rate	1	0.3
Maximum rate	88	28.6
Total	308	100.0

Source : Jornal de Negócios (base de dados)

The central government, understanding the need to set the required incentives, is adopting a strategy to promote inter-municipal investment. In what concerns proximity public services, the *National Strategic Reference Framework* (NSRF) imposed candidacies to be prepared by groups of municipalities (at a NUTIII level).

The adoption of quality of management strategies by local executives is also a logical move because the basic needs concerning infrastructure and social equipments are fairly satisfied. In table 9 we present the number of municipalities without social equipments for 2001 (consider that since then many other investments were promoted). As we can observe in this table, only a small percentage of municipalities do not have equipments such as sports pavilions, swimming pools or libraries.

Table 9. Municipalities without equipments (2001)

Equipment	Municipalities without at least one equipment	% of total
Sports pavilion	69	22.4
Sports Field	27	8.8
Swimming pool	38	12.4
Children playground	45	14.6
Auditorium	77	25.0
Library	46	14.9
Museum	136	44.1
Market	27	8.8
Camping	191	62.0
Multipurpose Pavilion	135	43.8

Source : A Administração Local em Números, DGAA.

3. SWOT ANALYSIS OF MUNICIPAL FINANCES

Diversity is a general characteristic of local government finances in Portugal. Portuguese municipalities are very different concerning size, economic basis, dependence on intergovernmental transfers and problems they face.

For many municipalities, most of them located in the Interior of Continental Portugal, the overall picture is a loss of population and, therefore, a loss of fiscal basis, incapacity to attract residents despite the better conditions of access to social equipments they offer, and difficulties to cope with the reorganization of central government services in areas such as health, education, justice, safety, etc.

For some municipalities, major difficulties are associated with new problems mainly generated by suburbanization of large cities, such as crime, poverty, social exclusion, urban mismanagement, etc. For Lisbon and Porto the difficulties are associated with loss of population, urban decay, crime and social exclusion, urban sprawling, or others. Portuguese municipalities, as a matter of fact, can be organized using the typology presented by Ferrão (2003). There is a sleepy Portugal, a serene Portugal, and a Portugal under pressure.

Many municipalities depend heavily on intergovernmental transfers and such dependence will not change in the near future. Their efforts will be mainly devoted to obtain gains by rationalizing expenditures and by entering inter-municipal partnerships. Many others can act both in the income and expenditure side.

In the income side there is room for an increase in fiscal efficiency (user charges) and for a growth of tax and user charges receipts (especially on IMI and new environmental user charges). In order to overcome debt restrictions, the importance of public-private partnerships is going to increase and therefore special attention has to be devoted to risk management. Voter's scrutiny is going to increase and consequently more efforts will be targeted by municipal executives to quality of management and to communication with local residents. New taxes may emerge, especially those with an environmental purpose. Special attention will be given by municipal executives to front-desk services and to bureaucracy reduction. The generalisation of "*municipal shops*", e-government, and the impact of the so-called SIMPLEX, a de-bureaucratization programme, at local level may create better conditions for higher fiscal efficiency and productivity.

But many threats lie in the horizon of Portuguese local governments. Economic restructuring may erode even more the economic basis of traditional industrial municipalities. Costs with maintenance and renewal of equipments will increase in the future. European funds generated in the past an opportunity for a high level of public investment. In the near future (till 2013) NSRF will allow an identical level of public investment, but is it not foreseeable that such level of financial boosting can be maintained from then on. Municipalities will have to incur in high renewal and maintenance expenditures and do without this large amount of financial aid.

Because of new restrictions on public debt, public-private partnerships have been one of the solutions to finance new investments. The main

problem is that municipalities lack experience on this area and the signed contracts do not ensure an adequate share of project risks between municipalities and private investors.

Another solution was to use existing current expenditures as a warranty for payment of new investments. This risk has been addressed in the last amendment to the Law of Local Finances, and such practice is today forbidden.

Small municipalities face an increased risk because of their past and present inadequate policy concerning user charges. For example, user charges for water supply are very low covering only a small part of costs. These services are now in a process of reorganization. Supra-municipal companies organized on a river-based logic sell or will sell water to municipalities, (*serviço em alta*) and then municipalities provide the distribution to local consumers (*serviço em baixa*) with the municipal option to transfer this service to the supra-municipal company. In any case the user charge is very low and has to be increased steadily creating a political problem for those municipalities.

Table 10. Strengths and Weaknesses of Local Government Financing

Strengths	Weaknesses
Richer municipalities have a large fiscal basis.	Diffuse urbanization in many municipalities in the Littoral North and Littoral Centre of Continental Portugal.
Municipalities in the littoral North Littoral Centre still have a young population.	Tax base insufficient in many low populated municipalities.
Growth of receipts in consequence of the real estate property.	Low levels of productivity of civil servants.
	Low level of user charges.
	High level of municipal debt.
	Urban growth can no more be the major motivation for municipal receipts growth.
	Increasing costs with the renewal of infrastructures and equipments.
	Increasing costs with aging population.
	Structural weakness of the Portuguese economy.

Table 11. Opportunities and Threats for Local Government Financing

Opportunities	Threats
Increasing receipts from IMI.	Increasing restrictions on public debt.
New taxes (environmental taxes).	Compromising future current receipts with the financing of present capital expenditures
Increase in fiscal efficiency.	
Public-private partnership.	Inadequate risk share in public-private partnerships.
New public management.	Economic restructuring longer than expected and structural unemployment.
Gains of productivity in public services.	Increased sophistication of consumers of public goods and services.
E-government and modern front-desk services.	Increasing costs with maintenance and renewal of infrastructures and equipments.
	Aging and loss of population.
	Transfer of new competences to local governments without the appropriate financing.

4. AN AGENDA TO INCREASE MUNICIPAL EFFICIENCY AND ACCOUNTABILITY.

A democracy of over three decades furnished local governments in Portugal with the appropriate experience, organization and human resources to face a new agenda of problems. Most municipalities in Portugal can now aspire to move from quantity to quality, production to management, information asymmetry to transparency and accountability, monopoly to competition, growth to sustainability, and bureaucracy to simplicity. This new agenda is consistent with innovation changes occurring in Portugal namely the reform of public administration, the SIMPLEX program, the Plano Tecnológico and others.

An important change is now under way concerning urban management at municipal level. With the purpose of simplifying the process of approval of new construction, a new law has been approved. The major change introduced by this new law is the possibility of promoters, in pre-arranged cases, to assume responsibility for following municipal and urban rules and to start works after a mere presentation of a pre-communication (*comunicação prévia*). This is an important change for Portuguese standards because it involves *a posteriori* instead of the tradi-

tional *a priori* verification of compliance with urban rules. Some analysts doubt the capacity of the judicial system to answer adequately to a potential increase of situations of non-compliance with urban rules.

Another major change is a consequence of the approval of the new General Regulation on User Charges where any change in user charges has to be accompanied by an economic and financial study showing the proportionality of user charges with the costs of services or with the benefit of user charge payers.

Concerning the political process at local level, conversations between the two major political parties (Socialist Party and Social Democratic Party) have been under way in order that municipal executive councils must be constituted only by members of the most voted party. In Portugal, municipal executives have been composed by councillors from different parties, depending on electoral results (Hondt method) and some authors argue that such device is unfit concerning efficiency and efficacy of governance. Empirical studies show that the existence or not of a majority and the need to obtain an absolute majority with a party from the right or from the left influences the political business cycle and the type of expenditures (current and capital expenditures), but there is no clear evidence on the efficiency and efficacy superiority of absolute majorities, comparing with relative majorities. This change in the design of local executives does not benefit small parties. Nevertheless, recent difficulties in the negotiations between the two major parties may jeopardise this political reform at local level.

An important shortcoming for municipal action is the lack of a regional level in Continental Portugal. In a recent past, the solution was the creation of municipal associations (great metropolitan areas, urban communities and special-purpose municipal associations). This model is now in a process of change because only the metropolitan areas of Lisbon and Porto as well as municipal associations with special purposes will remain in the future. The central government is adopting the NUT II and the NUT III map to organize central government services and to induce municipalities to use this spatial organization in their candidacies to NSRF funds. Regionalization is not a consensus idea in Portugal, although more and more politicians and specialists see this reform as a way for less developed regions to overcome their difficulties (the North region is a good example). Analysts see the reorganization of central governments using these two maps as an intelligent way to create better conditions for a future regionalization process of Continental Portugal.

A controversial issue in Portugal is municipal size. As can be inferred from this paper, many municipalities are sparsely populated despite the large jurisdiction areas. In large municipalities the size of urban centres also creates movements of secession and in three cases they were successful. To reorganize municipalities according to size is not an easy task because of an emotional attachment of population to their municipalities or *freguesias* and because of the recognition that identity often overlaps with individual relations to territory. Moreover, the concept that for politicians only vote counts matter is open to criticism. In under-populated areas an important role can be played by new forms of public service organization. For example, the adequate scale of services is, in a first stage, obtained by concentrating the same type of service and, in a second stage, by concentrating related services. An important role can also be played by new technologies. In large municipalities a new role can be played by *freguesias* in order to avoid secession movements.

A set of further organizational changes are under way or are still in need to polish the agenda towards efficiency, to reduce bureaucracy and to increase accountability. The following table shows a list of possible changes, many of which are already in the agenda of innovative Portuguese municipalities. The implementation of mandate budgets, the change in budget equilibrium rules, the creation of new taxes and the introduction of a fiscal effort index in the distribution of the cohesion fund are initiatives that require legislative changes and may raise counter-arguments. The generality of the other initiatives, in our view, benefits from a generalized consensus, although some may be difficult to implement (cases of the zero-based budgets and the use of present value of costs when deciding on contracts). Our view is that municipal executives leading the agenda will pass to voters a sign of competence and will be rewarded in local elections.

Table 12. Initiatives to Increase Municipal Efficiency and Accountability

Initiatives	Need of legislative changes
1. To improve budget procedures	
1.1. Mandate budgets.	Yes
1.2. New budget equilibrium rules.	Yes

1.3. Specialized commissions at Municipal Assembly level to analyse budget and to control budget execution.	Yes
1.4. Public debates on the municipal budget	Yes
1.5. Zero-based budgets.	No
1.6. To use the present value of costs in the selection of contractors.	No
2. To increase management transparency	
2.1. To evaluate in kind transfers.	No
2.2. To quantify non financial compromises.	No
2.3. To publish management indicators	No
2.4. To promote benchmarking studies of local services.	No
2.5. To facilitate the understanding of municipal financial data.	No
3. To reduce costs and bureaucracy	
3.1. Re-engineering of internal procedures	No
3.2. To favour a posteriori verification of rules	No
3.3. Integration of municipal information systems.	No
3.4. To modernize front-desk services	No
4. To increase fiscal receipts	
4.1. To update user charges	No
4.2. To control receipts of user charges (dividing into categories A/B/C)	No
4.3. Use of opportunity costs when defining user charges	No
4.4. To increase municipal fiscal competitiveness	No
4.5. Harmonization of tax rates and user charges at NUT III level to avoid zero or negative sum games.	No
4.6. To study the costs and benefits of tax collecting by municipality.	No
4.7. To create taxes for environmental protection and other risks coverage	Yes
4.8. To create user charges to fight traffic congestion	No
5. To increase other municipal receipts	
5.1. Correct use of public-private partnerships	No
6. Municipal Debt	
6.1. Use of public bonds.	Yes
7. Changes in the Law Local Finances	
7.1. Introduction of an index of fiscal effort in the estimation of the cohesion fund transfer	Yes
8. Protection of tax-payers	
8.1. Definition of quality standards for local public goods and services	Depend on the services
8.2. To avoid export of user charges	No

5. CONCLUSION

Local governments in Portugal play an increasing role in the provision of local public goods and services. Along the areas of traditional municipal competence, an important role is now played by local governments on child-care and basic education (such as non-teaching staff, school transports, food, curricula enrichment). But new areas of intervention are expected to be added, namely basic health (non-medical staff of health centers, maintenance expenditures of health centers, patient transportation, special health programs in health centers and schools). Costs of these new attributions is financed by the fund FSM and the appropriate financial resources will predictably be at the disposal of local governments. These are areas of intervention where central government usually showed difficulties and consequently represent an important step-up in expectations on the capacity of local governments to deliver good public services to local residents.

The referred step-up becomes even more ambitious when we consider that simultaneously there is an increase in local resident demands as well as in costs of operation and maintenance of infrastructure and equipments. There is a window of opportunity for municipalities to face this challenge with success. This window implies that during the present period of EU funds, till 2013, municipalities may promote a new agenda of initiatives to assure cost rationalization, transparency of management and accountability. After 2013 the expected increase in maintenance and operating costs has to be addressed by modern and efficient local governments without the present substantial amount of financial help. It is crucial that municipal executives understand the strategic value of involvement in inter-municipal cooperation that in the long-run may be instrumental in keeping autonomy and self-government, given the evident lack of scale of many municipalities now.

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