COMPARISON ON THE STRENGTHENING OF LOCAL PUBLIC FINANCES AUTONOMY IN THE EUROPEAN UNION COUNTRIES

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This study is primarily intended to present a comparative analysis between EU Member States on the organisation and finance of local governments and to provide the stage of local financial autonomy in the context of European Union with the help of its relevant indicators and the establishments of legislation limits.

Key words: local public finances, financial autonomy, European Union, revenues, expenditures, investments

JEL classification: H7, H83

1. Introduction

In all EU countries an important part of economic activity is conducted under the responsibility of administrative, financial and legal local authorities as a result of the decentralization of decisions at the administrative-territorial units. Local public sector has undergone numerous reforms as a result of implementing the principle of local autonomy and decentralization process particularly in the municipalities or localities, corresponding to the first level of local government. These reforms in local public expenditure were adopted according to the needs of each country. Local government expenditure in the new EU Member States tends to increase as a result of the decentralization of local government. This increase powers of local and implicitly increases local public expenditure. Local tax reforms are initiated and implemented permanently in the European Union in order to identify the most effective form of local administration based on the principles stipulated by the European Charter of local autonomy. Administrative-territorial units of the Member States of the European Union have pursued continuously increase the performance of revenue that has held it in relation to five criteria: revenue adequacy, financial autonomy, fairness, transparency and simplicity, cost-effective[210].

The framework of this paper is based on a set of research programs and papers made by different Romanian and foreign institutions as Council of Europe, Central and Local public administrations, Romanian Institute for Public Policies, DEXIA – France, Universities etc.

2. The legal framework of the autonomy of local public finance

Each country has its own legislation on local public finances, but the diversity of national rules are in accord with the common legislation adopted at the European level and European Union level for its member states. So that, legislation, as a key factor in the process of implementation of local financial autonomy and decentralization process, establish the general rules for local public finances. Article 9 of the European Charter of Local Self-Government lists certain general principles concerning the financial resources of local authorities and Article 3 proposes that local authorities should have the right to regulate and manage a substantial share of public affairs. At the same time, fiscal policy has to be judged in the light of the Maastricht criteria[211], which say that candidates for the monetary union must – among other things – not run an excessive deficit (a general government deficit of more than 3% of national gross domestic product and a general

210 Comisia Europeană (1998), „Financing the European Union”, Commission Report on the Operation of Own Resources System, Brussels, p. 5.

211 Protocol No. 5 to the European Union Treaty, on the procedure concerning excessive deficits, Article 1

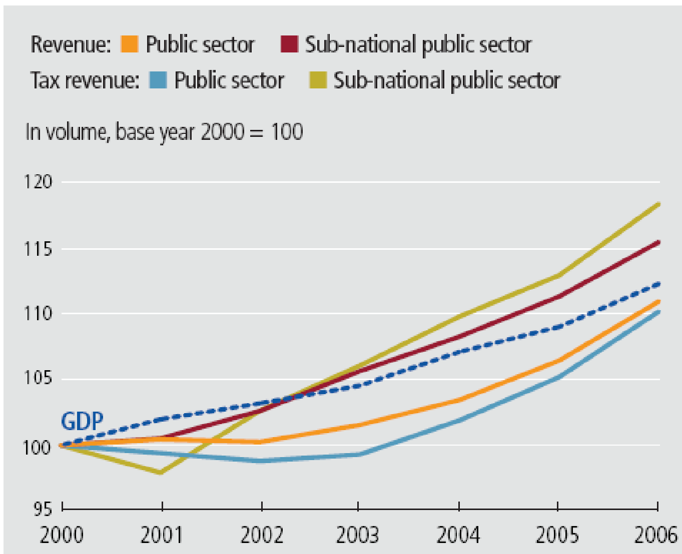
government debt of more than 60% of national gross domestic product). Where local authorities enjoy some degree of freedom in their fiscal policy and where their deficits or surpluses form a larger part of the deficit of the General State, the necessity of close coordination among the different levels of the state will arise. This might, at least in some cases, the reduction of financial autonomy of local governments.

3. The evolution of local public finances in EU

a. The evolution of local public revenues

Local revenues have increased annually between 2000 and 2006 on average of 2.4% (3.3% for the local sector only), outstripping GDP growth (2%) and that of total public revenue (1.7%). Within this revenue, tax revenues increased more faster, 3.1% on the local level.

Figure 1: Evolution of revenue and tax revenue in EU-27 countries on the period 20



0-2006

Source: ***Sub-national public finance in the European Union****, Dexia, December, 2007, p.15*

Local revenue has expanded much faster in the EU-12 (7.8%) than in the EU-15 (3.5%) due the steady economic growth which positively impacted tax revenues, but also continuing reforms aimed at providing financial compensation for the transfer of competences.

b. The evolution of local public expenditures

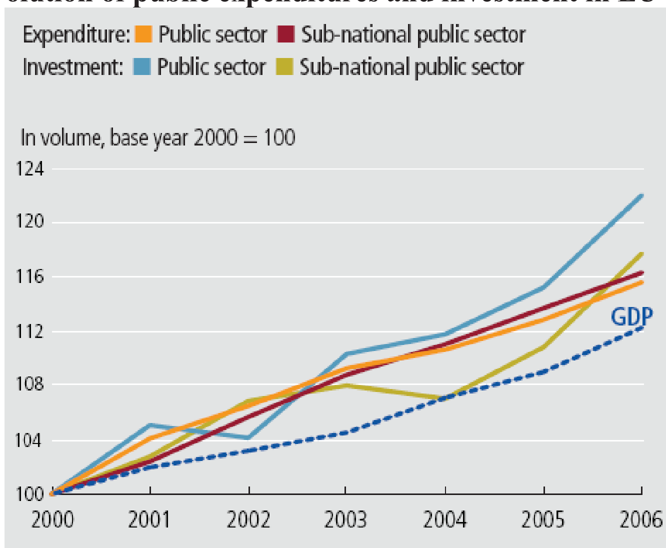
Municipal responsibilities have been extended and the impact is very strong because it has significantly increased local government expenditure. Between 2000 and 2006, local expenditure rose 2.6% per year on average, surpassing annual GDP growth over the period (2%) and slightly outpacing total public expenditure (2.5%).

Local public expenditure growth is most dynamic in the new Member States of the European Union, the EU-12 showing a growth rate of 5.4% per year versus 2.5% for the EU-15. The largest increase (22.3%) occurred to Slovakia where financing for most infrastructure and public services was transferred to municipalities and the regions which were created in 2002.

A growing number of countries are involved in structural reforms which allow them to outsource spending (through financial dealings with satellite bodies which do not appears as public expenditure), to private local public companies or to transfer certain public utilities – like water services, electricity or municipal waste – to the private sector (Austria, Belgium, Denmark, Germany, Portugal, Sweden, Spain).

Investment growth in the local public sector was 3.2% per year on average in the period 2000-2006. The growth was particularly strong in the EU-12 (9.1%) versus EU-15 (2.5) not only on account of increased expenditures linked to the decentralisation process but also because of the considerable infrastructure needs both in terms of renovation (catching up to EU standards) and construction in such key areas as transport and the environment (water, waste, management).

Figure 2: Evolution of public expenditures and investment in EU-27 on the period 20



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Source: ***Sub-national public finance in the European Union****, Dexia, December, 2007, p.12*

Local investment was particularly dynamic in 2006, progressing by 6.6%, a pace more than double that of GDP growth (3%) and heftier than 2005 (3.6%). Investment growth was remarkable in most EU-12 counties, with an average growth of 28.9% for the zone. It was over 60% in Latvia and Lithuania and 84.6% in Romania versus EU-15 which registered 5.1%

In Romania, the capital expenditures in local public budget imposed by the necessity of development of local public investments must rise as a condition of local public autonomy, but the current expenditures are still too big.

Table 1: The ratio of local expenditures in EU countries in 2006

	Romania (million Lei)	EU-27 (million Euro)
Total expenditures	**28761**	**1322956**
Intermediate consumption	7076	331259
Compensation of employees	11608	453157
Interest	330	22186
Subsidies	16	44349
Social benefits	2998	196180
Other current expenditure	1061	76483
Capital transfers payable	0	29912
Capital investments	5672	168419

Source: Eurostat

Resources from Cohesion and Structural Funds represent an opportunity for the new member states, because they offer the possibility to make big investment projects, also in local infrastructure, withought using ordinary resources and without affecting the level of consolidate budgetary balance, being, at the same time, an element of local autonomy. The new EU member states and Romania in particular, don't have the capacity of absorption of these funds because of a lack of experience of management authorities and difficulty in designing projects that fulfill EU criteria and sometimes local authorities have trouble mobilising the necessary resources for co-financing of EU funds.

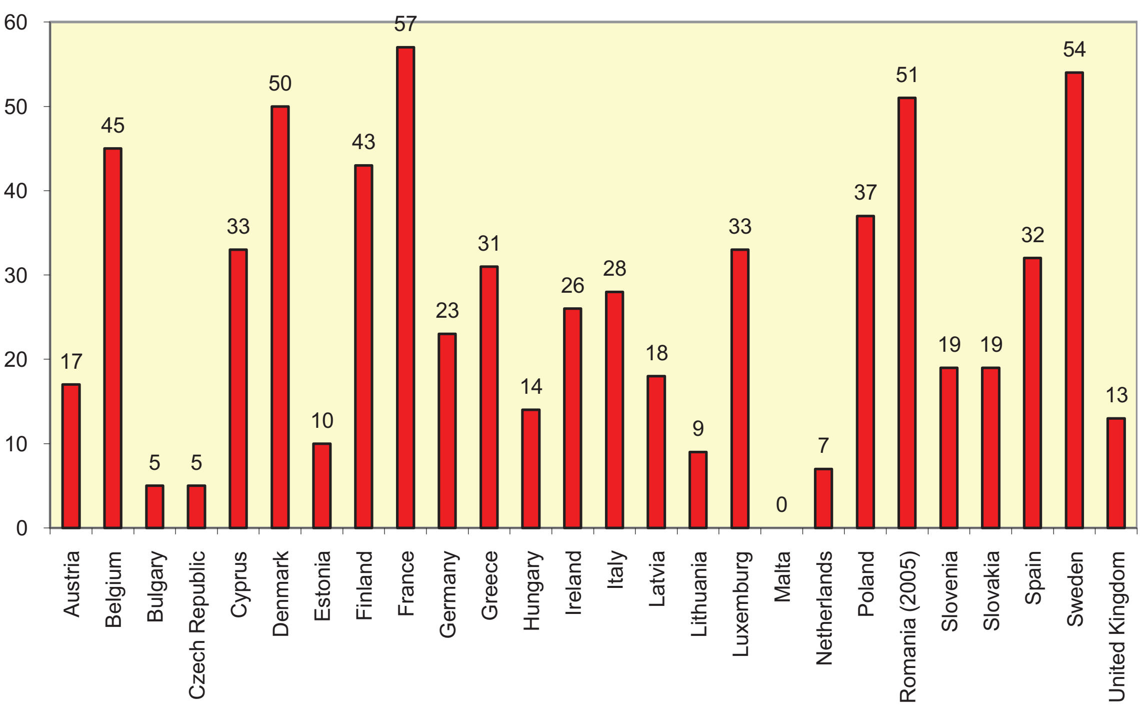
4. Indicators of financial autonomy

a. Local financial autonomy rate

The level of own revenues in total local revenues represent the most significant indicator of local autonomy because makes the position of local authorities more independent on the state. As their incomes are higher, the increasing degree of autonomy because they can cover costs of local own revenue sources. Most of the revenue derived from taxes on wealth or property, revenue from the provision of services (parking cars, gyms). Almost all countries have left it to local authorities to collect very small taxes, such as dog license fees or entertainments tax. Very few counties have provision for genuine local taxes that yield an appreciable amount and for full autonomy to collect them. In Romania, United Kingdom and France, the main taxes levied are the various forms of property tax. In most cases, the rates can be determined either freely or within specified limits by the local authorities.

In a number of countries, e.g. France (taxe d'habitation) and the UK (council tax), citizens, who are responsible for a considerable proportion of the expenses incurred by the local authority, have had to pay a separate tax, owing to the limited possibilities of distinguishing between one payer and another, only yields a relatively small amount or else provokes a great deal of resistance.

Figure 3: Local financial autonomy rate in EU countries in 2005 (%)



Source: World Local Authorities

Analyzing data from the table is a trend towards greater decentralization in the old EU countries, suggesting a greater local autonomy. In 2005, local financial autonomy rate is under 30% in majority of ex-communist countries (Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Slovenia, Hungary, Slovakia), and, also, in countries as Austria, Germany, Ireland, United Kingdom. The local financial autonomy rate between 30% and 50% is in Cyprus, Greece, Luxemburg, Poland, Portugal, Spain, and Finland.
The biggest rates of own revenues in total local revenues are in Finland (57%), followed by Sweden (54%), Romania (51%) and Finland (50%). Romania has a high local financial autonomy rate because in local financial law is mentioned as own revenue of local budget the income tax rate share.

b. Local public revenues and local public expenditures as percentage of gross domestic product (GDP)

Identifying local public revenues and local public expenditures as percentage of gross domestic product (GDP) and the surplus or the deficit is important for to see how local authorities can cover with their revenues the local public expenditures due of their exclusive, share or delegate competences.

Table 2: Local public revenues and expenditures/GDP in 2007

Country 2005 I	Total local government revenue % of GDP II	Total local government expenditures % of GDP III	II-III
EU27	11.3	11.3	0
EU25	11.3	11.3	0
EU15	11.3	11.3	0
BE - Belgium	6.6	6.7	-0.1
BG - Bulgaria	7.2	7.2	0
CZ - Czech Republic	11.7	11.2	0.5
DK - Denmark	31.8	32.0	-0.2
DE - Germany	7.5	7.2	0.3
EE - Estonia	9.3	9.8	-0.5
IE - Ireland	6.9	7.1	-0.2
GR - Greece	2.6	2.6	0
ES - Spain	6.1	6.4	-0.3
FR - France	10.8	11.2	-0.4
IT - Italy	15.2	15.0	0.2
CY - Cyprus	1.9	2.0	-0.1
LV - Latvia	10.0	10.6	-0.6
LT - Lithuania	8.0	8.4	-0.4
LU - Luxemburg	5.1	5.0	0.1
HU - Hungary	11.7	11.7	0
MT - Malta	0.6	0.6	0
NL - Netherlands	15.3	15.3	0
AT - Austria	7.6	7.4	0.2
PL - Poland	13.4	13.3	0.1

PT - Portugal	6.0	6.1	-0.1
RO - Romania	9.6	9.8	-0.2
SI - Slovenia	8.3	8.4	-0.1
SK - Slovakia	6.0	6.1	-0.1
FI - Finland	19.1	19.3	-0.2
SE - Sweden	24.8	24.5	0.3
UK - United Kingdom	12.8	12.9	-0.1
EA11 – Euro Area	10.1	10.1	0
EA12 – Euro Area	9.9	9.9	0
EA15 – Euro Area	9.8	9.9	-0.1

Source: Eurostat

The examination of local public expenditures and local public revenues in relation to GDP highlights significant discrepancies between the countries, partly due to their varying level of decentralization and also to the varying financial weight of the responsibilities devolved to local public administrations tiers.
As data table shows, in the majority of European Union members budgets fluctuated moderately around balance point in 2007, the biggest being in Estonia (- 0.5%). The biggest surplus was registered in Czech Republic (0.5%). Only five countries succeeded to have a balance budget.

4. Conclusion

The local financial autonomy represents an important issue in the global context of economic development and a result of implementation of local autonomy principle and decentralization process. The legislation of European Union and the evolution of European Union society are oriented to raise the local financial autonomy. Local tax reforms are initiated and implemented permanently in the European Union in order to identify the most effective form of local administration based on the principles stipulated by the European Charter of local autonomy. However, there are differences between countries even the convergence criteria are applied to the states and both to the state and to the local communities until the total economic integration, the last step in the European Union integration process.

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