Ref 20181108 – Speech - Heather McVEY

35th Congress Session – Congress of Local and Regional Authorities, 8 November 2018, Strasbourg

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Report "Coping with the debt burden: local authorities in financial difficulty (CG35(2018)21)"

Strasbourg, France, 8 November 2018

Dear Chairman, Dear Colleagues,

It is my honour to present to you the report on **"Coping with the debt burden: local authorities in financial difficulty."**

The right of local authorities to adequate financial resources of their own is a key principle of local autonomy, set out in Article 9 of the European Charter of Local Self-Government. This same article also introduces the principle of proportionality, which means that any transfer or delegation of additional powers must be accompanied by resources corresponding to the new powers and services to be provided.

Unfortunately, we have to admit that these principles are rarely applied or implemented in our member States.

This report "**Coping with the debt burden**" grew out of our *Resolution 372(2014)* and *Recommendation 362(2014)*, which concentrated on the scope of financial autonomy of local authorities, and their ability to raise their own revenues and finance mandatory tasks and functions.

Our previous report, unsurprisingly, revealed that many local authorities had been facing increasing difficulties since the 2008 financial crisis. As a result, the Congress itself received numerous complaints by national associations with regard to its work.

So, this made us decide to review the situation, and provide our member States with an up-to-date overview of the situation. Mr Szente, our expert, and vice-president of the Group of Independent Experts, prepared a questionnaire and sent it to our national experts. As such, the report and the conclusions which we drew up are based on what we established from the 24 replies that we received, from just over half of our member States.

We faced two difficulties. The first was the methodology. How do we determine whether finances are actually "adequate"?

The second was a lack of data. Since there is no reliable database of economic figures on the financial resources of the municipalities of each country, it proved difficult. Some national Ministries of Finance even refused to give data on local public finances to the national experts!

And of course neither the Council of Europe, nor the EU, has such a database.

So what have we found? What issues has the report flagged up? Let me take you through some of the main findings. It will come as no surprise that there are great differences between the member States in the share of the local government sector as a proportion of overall government expenditure. The share of the local government can vary from less than 1% to more than 15% of GDP.

I believe that local taxation is a key element of the financial autonomy of local authorities, as it allows municipalities to raise revenues according to their decisions and policies. The capacity of local governments to generate revenue is thus an excellent indicator of their financial autonomy.

We must also remember that there is a strong correlation between the degree of financial autonomy and the ratio of own resources to central government transfers. The greater the share of local revenues in the local authorities' total budget, the greater their financial independence and the more they can finance their activities themselves.

Similarly, the financial autonomy of municipalities is greater, when there is a higher ratio of lump sum allocations to specific allocations.

Our report also addresses the principle of proportionality, or the "adequacy principle", as it is formally known. This is crucial.

Local authorities have to manage more and more responsibilities that had previously been under the reins of national authorities. Member States should not give local authorities new responsibilities without providing them with resources: they should ensure the right of local authorities to adequate financial resources.

It has to be said – the way in which member States allocate funds to local authorities to accompany new responsibilities is far from satisfactory. Quite often, local authorities become dependent on grants and transfers from national governments, yet these revenues, are frequently changed at short notice, by national parliaments or governments, leaving local finances vulnerable to the wishes and whims of national institutions.

This is the reason why it is essential that member States recognise the principle of adequate financial resources.

But our local authorities do not always have the means to defend themselves. And if they apply to the courts, they could quickly discover that judicial remedies are often just a symbolic form of protection. This is partly due to the difficulty of defining and translating into law the principle of "adequate finances".

With regard to the political aspect – and relations between different levels of government, our report reveals clear-cut disparities between our member States on this issue. In Northern Europe, local authorities are often consulted by regional and central governments. Unfortunately, this is not the case in other member States, where consultation processes are more often than not mere formalities, leading to no real change.

It is evident that local authorities do not receive the same attention during the consultation process if the principle of adequate finance is not being respected, and the law is not being implemented.

However, let us not be too negative. Positive aspects do exist. We have witnessed progress. Our report found that many of our member States have been introducing new financial mechanisms to improve the financial management of our local governments. So, it is now down to us to explore these in more detail, as there is a lot of good practice out there.

As you know, we have also produced a new draft resolution and recommendation. The resolution briefly concentrates upon countries that do not abide by all of the principles mentioned in Article 9 of the Charter. We need to face the truth, and explicitly name these countries.

We must face reality:

- The majority of the Congress recommendations from 2014 have not been implemented.
- The fiscal capacity of local authorities is extremely limited in numerous countries.
- Some member States still do not recognise or guarantee the principle of sufficient municipal finance.
- In six member States, some local authorities are no longer able to cover the cost of services, therefore eliminating the principle of proportionality.

With regard to our recommendation, it clearly expresses that not enough is being done by member States to comply with Article 9 of the Charter. The discordance between the importance and application of Article 9 is a recurring issue, and has indeed been identified by the Congress in its monitoring of the Charter.

To make matters worse, 12 member States have witnessed no change concerning the efficient implementation of Article 9. As such, the recommendation takes up the offer made by the Committee of Ministers for dialogue of the issue of the financial difficulties of local authorities in relation with the non-implementation of Article 9.

The recommendation further invites the Committee of Ministers to call on member States to adopt a common understanding of the financial autonomy of local authorities.

Hence, this definition should ensure that local authorities can comply with their tasks and functions with the resources at their disposal; and have a certain degree of discretion in expenditure and make choices over own and transferred resources.

Dear Colleagues, there is still a lot for us to accomplish. Since there are no sanctions even in case of flagrant violations of the Charter, no positive changes can be expected in the near future in recalcitrant member States. That is why I would urge the Committee of Ministers to call on governments to increase their efforts to ensure full implementation of Article 9, as this is where the root issue lies.

Thank you for your attention.