



# “Future of the Workplace” project

Providing high quality, modern and sustainable jobs within local and regional government

## Theme n°1

Funding of Local and Regional Government: Key challenges, solutions to growth and alternatives

## **A very difficult economic context**

At present, local and regional government in the European Union (EU) is operating in a very difficult economic and financial context and there is little prospect that this will improve in the short term.

With the exception of Estonia, Hungary and Sweden, the budget of every government in the EU was forecasted to be in deficit in 2011. These high levels of deficit are to a large extent a consequence of the 2008 financial crisis and the recession it caused. However, the banking crisis has been followed by a sovereign debt crisis, and, under pressure from financial markets, European governments have adopted policies which aim to eliminate government deficits as rapidly as possible.

This approach has been also been enshrined at European level, as evidenced most recently by the *Treaty on Stability, Coordination and Governance in the Economic and Monetary Union*. This was initially agreed in December 2011 and signed by the governments of 25 states, those of the Euro zone states plus eight other governments on 2 March 2012. The Treaty includes a commitment that the signatory states will incorporate “*through provisions of binding force and permanent character, preferably constitutional*”, a rule under which: “*the budgetary position of the general government of [the signatory state] shall be balanced or in surplus.*”

Downward pressure on local and regional government expenditure as significant part of overall government expenditure (33.6% on average in 2010 on the basis of CEMR/Dexia figures<sup>1</sup>) will be ongoing.

### **National differences**

It is important to point out at this stage that the share of local and regional government in overall government expenditure varies widely between member states. It is higher in countries with a strong federal structure, where important powers are devolved away from national governments: the CEMR/Dexia figures show that local and regional government accounts for 41.8% of total government expenditure in Belgium, 44.1% in Germany and 53.2% in Spain. In contrast in Cyprus, this level of government only accounts for 4.8% of total government spending; in Greece, the figure is 5.6%; in Ireland 10.3%; and in Malta 1.5%. More typical values, of around 25%, are found in the Czech Republic (27.0%), in Estonia (24.7%), in Hungary (25.6%), in Latvia (25.6%), in Lithuania (27.6%), in Romania (23.9%) and in the United Kingdom (27.8%).

There are also important differences in tasks undertaken by local and regional government. In most countries, education is an important local and regional responsibility, accounting for 20.8% of total expenditure at this level. But local and regional spending on education is nil or miniscule in Cyprus, Greece and Malta, and well below average in Italy and Portugal. Health accounts for around a quarter of local and regional spending in Denmark, Finland and Sweden, as well as in Austria

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<sup>1</sup> This and subsequent figures on local and regional expenditure come from *EU subnational governments: 2010 key figures*, CEMR and Dexia, 2011

and Spain, and 44.2% in Italy, but in other states, including the Czech Republic, France, Germany, Romania and the UK, local and regional government spending on health is very small or non-existent, as the responsibility lies elsewhere.

These differences should be borne in mind in any consideration of spending trends.

### ***Local and regional government hit harder***

There are indications that, in some countries, local and regional government has been more heavily affected by cuts than the public sector as a whole.

In Italy, for example, the deficit reduction plans announced in 2010 and 2011 provided that “more than half of the expenditure reduction in 2011–2012 is to be delivered by sub-national governments,”<sup>2</sup> while the CEMR/Dexia figures show that they account for only 31.3% of total public spending. In the UK, the latest figures for public sector employment show that in the 12 months from the first quarter of 2011 to the first quarter of 2012, employment in local government fell by 202,000 or 7.1%, while employment in central government, including the health service, fell by 40,000 (1.4%).<sup>3</sup>

A study by a Council of Europe body, the European Committee on Local and Regional Democracy, found indications that this was a general trend, although it looked at a wider range of countries than EU member states. It concluded that, “in more than half of the countries for which we have data, local budgets dropped more on aggregate than the corresponding central ones, at least in one of the two years of the crisis.” It went on to point out that, “in a number of these countries [Central and Eastern European countries as well as some old member states] there is evidence that the central governments have deliberately applied pressure on local budgets in order to create fiscal space at the centre in order to deal with the effects of the crisis, either by cutting transfers and local borrowing or forcing local governments to run surpluses”.<sup>4</sup>

### ***Impact on social dialogue***

Efforts to cut spending have directly affected employees through pay cuts and pay freezes, as well as in dealing with other issues, such as pensions. These changes in terms and conditions go to the heart of issues which ideally should be resolved through social dialogue, as do the cuts in employment which have been implemented in many states.

Since 2008, 11 of the 27 EU states have directly cut public sector pay, sometimes more than once. The level of the reductions has varied from country to country, as has the way they have been imposed — sometimes hitting basic pay, sometimes pay

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<sup>2</sup> IMF Country Report No. 11/173: Italy, IMF, July 2011

<sup>3</sup> *Public Sector Employment - Q1 2012*, Office for National Statistics, 2012

<sup>4</sup> *Local government: responses to recession across Europe*, European Committee on Local and Regional Democracy (CDLR), August 2011

additions and sometimes both. The countries where pay has been cut are the Czech Republic, Estonia, Greece, Hungary, Ireland, Latvia, Lithuania, Portugal, Romania, Slovakia and Spain, and the situation in each one is set out in Table 2 in the Annex.

Seven further countries have frozen public sector pay, or significant elements of it, for at least a period since 2008. These are: Bulgaria, Cyprus, France, Italy, Poland, Slovenia and the UK. As with pay cuts there are variations in how this has been done. In Poland, for example, teachers were, for a period excluded. In France, it was the pay scales that were frozen, while other elements of pay improved for some public sector employees. In the UK, those earning less than £21,000 a year (about €25,000) got a small increase (although not in local government). A common feature in many countries is that pay freezes are set to last for a considerable time. In Italy, for example, public sector pay is being frozen from 2011 until the end of 2014. In Cyprus, the pay freeze announced in 2011 will last for three years, and in France, Poland and the UK pay freezes were planned for a two-year period.

The negative impact that these decisions have had on social dialogue has been intensified by the fact that in most cases pay cuts and freezes have not been negotiated between the social partners, but imposed, generally by central government. In some cases governments were under pressure to react quickly to pressure from the markets; in others the cuts were required by external funders (sometimes the International Monetary Fund alone, sometime in conjunction with the European Commission and the European Central Bank). However, whatever the reasons, unions and generally local and regional authorities themselves were not consulted beforehand.

There are some examples where agreements have been reached with the social partners, frequently after initial disputes. These are set out in the table below.

In **Ireland** in March 2010 the so-called Croke Park agreement guaranteed: that there would be no further pay reductions over the lifetime of the agreement – from 2010 to 2014; that there would be no compulsory redundancies; and that the 2010 pay reductions would be disregarded for the purpose of calculating pensions for those retiring in 2010 and 2011. In return the unions agreed to cooperate fully in redeployment within the public services as part of a modernisation of the public services allowing staff numbers to be reduced.<sup>5</sup>

In **Lithuania** discussions between the government, the unions and the employers led to the signing of a national agreement on 28 October 2009. As well as covering a wide range of issues, this confirmed the average 10% cut in pay for state officials and civil servants and the average 8% pay cut for those employed in other publicly funded bodies. In return, the government promised that, during the period of the national agreement, there would be no further reduction in the basic salary level in the civil service.

In **Slovenia** in December 2011 the government and the unions agreed to extend a freeze on pay in the public sector into 2012. The initial plan was for it to continue to

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<sup>5</sup> Public Service Agreement 2010-2014

be frozen throughout the whole of this year. However, following discussions with the unions, a compromise was reached limiting the freeze to the first six months.

Finally in **Spain** unions signed a wide ranging agreement with the government and the employers in February 2011. The deal did not deal with public sector pay but did introduce major changes in Spain's pension system, increasing the normal retirement age from 65 to 67.

These examples show that it is possible for social dialogue to deliver results. However, they remain the exceptions and it has not always been possible to maintain agreement, when the pacts expire. In Lithuania for example, it was not possible to reach a consensus on an extension to the national agreement when it ran out at the end of 2010. In Slovenia, pressure from the government to cut public sector pay in the second half of 2012 led initially to a major strike, although subsequently acquiescence by the unions that wages would come down.

## ***Taxation***

It is beyond the scope of this report to look at the complex and very varied systems of the public financing of local and regional authorities through taxation and transfers from central government (See Box on Finland for an example of how money is raised and spent.). However, it is essential to draw attention to the view of both employers and unions in local and regional government, as set out in a series of joint statements, that simply cutting expenditure cannot be an acceptable solution to the problems of public finance. In February 2010, CEMR and EPSU pointed out that “the provision and quality of local and regional government services is largely dependent on public finances”, and went on to say that “In this context, sustainable financing requires socially just taxation and other revenue streams, sufficient to allow local and regional governments to make long term investments to meet the changing needs of local communities.”<sup>6</sup>

In a further statement in December 2010, CEMR and EPSU jointly called on the European Council to ‘realise that public spending at local and regional level is not a ‘parasite’, but aims at improving the quality of life of citizens and driving economic growth’. Finally in October 2011, CEMR and EPSU stated jointly that the current approach of government had been “to foster economic stability and balance budget deficits at the expense of the public sector without reflecting on the alternatives of public income.”<sup>7</sup>

There would certainly be differences in defining exactly what is “socially just taxation”. However, EPSU has set out a five-point plan on fair taxation, which involves: a general move to progressive taxation, rather than flat taxes, an EU-wide strategy to

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<sup>6</sup> European Sectoral Social Dialogue Committee for local and regional Government: Joint statement to the European Council meeting 11 February 2010 on the economic crisis, [http://ec.europa.eu/employment\\_social/dsw/public/actRetrieveText.do?id=8826](http://ec.europa.eu/employment_social/dsw/public/actRetrieveText.do?id=8826)

<sup>7</sup> CEMR/EPSU Joint statement, 21 October 2010, [http://ec.europa.eu/employment\\_social/dsw/public/actRetrieveText.do?id=8997](http://ec.europa.eu/employment_social/dsw/public/actRetrieveText.do?id=8997)

increase the tax paid by large companies, seeing tax compliance as part of social corporate responsibility, with greater tax transparency for major companies, a tax on financial transactions and better tax governance to tackle tax fraud.<sup>8</sup>

## ***Funding solutions***

With reduced financial support from central government and operating within a defined legislative framework, local and regional authorities have only a limited number of possible responses to make savings without reducing services.

As well as cutting costs through reducing the pay of their employees (see above), their main options are primarily to:

- increase revenue from other sources, such as charging for services;
- make savings through rationalisation and general efficiency;
- reduce costs by making greater use of technology;
- make savings through cooperation with other local and regional authorities;
- work with the private sector through public private partnerships; and
- work more closely with voluntary organisations – the third sector.

The survey undertaken jointly by European Committee on Local and Regional Democracy and CEMR in the summer of 2011, although not complete, provides an indication of the actions taken by regional and local authorities under these headings.<sup>9</sup>

## **Higher charges and using other sources of income**

The survey indicates that in a number of countries charges for services have increased but that there are often limits on how much can be raised. The response from **Estonia** for example notes that, *“There have been some cases of the water tariff going up, bus tickets becoming more expensive, or the garbage collection fee rising, but these are rather exceptional cases; this not a general trend”*. As the response from **Finland** notes some charges are *“defined quite narrowly by legislation and municipalities have limited possibilities of increasing them,”* a position echoed by the response from **Slovakia**. From **Hungary** too, it was reported at the joint CEMR-EPSU workshop in January 2012 that new legislation meant that local authorities were prohibited from increasing public sector service fees.

However, the survey also shows that higher energy charges have been passed on in **Finland**, and this also seems likely to happen in **Slovenia**. In the **Czech Republic**, the CEMR affiliate SMOCR (Union of Towns and Municipalities of the Czech Republic) reports that in some cases rents in social housing have been increased and some municipal facilities have been rented to commercial companies.

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<sup>8</sup> EPSU Tax Justice Charter, Why fair taxation is part of the solution to the global economic and financial crisis, May 2010 (EN/FR/DE/ES/SV) <http://www.epsu.org/a/6595>

<sup>9</sup> <https://wcd.coe.int/ViewDoc.jsp?Ref=Qu/2011/fin&Language=lanEnglish&Site=DG1-CDLR&BackColorInternet=B9BDEE&BackColorIntranet=FFCD4F&BackColorLogged=FFC679>

## Rationalisation and efficiencies

Here much more has been done, although often the process started before the current crisis. The survey shows that in **Bulgaria**, a programme of schools restructuring (closing or merging some and creating new larger schools with better conditions for students) began in 2007. In **Denmark** merging schools is part of an efficiency drive, which cut costs by some 1.3 billion DKK (€175m) in 2010 and an expected 2.2 billion DKK (€295m) in 2011. This also involves amalgamating day-care centres and centres for the elderly, joint municipal partnerships around shopping areas, digitalisation and benchmarking. Overall reports to the CEMR-EPSU workshop suggested that there could be a cut of up to 4% in local authority employment in Denmark. Although there was an attempt to concentrate these cuts on so-called “cold hands” (administrative staff) and protect “warm hands” (those dealing directly with the public), in practice this distinction was often difficult to make.

Benchmarking as a way of reducing costs is also used in **Sweden** and **Slovenia**. Also, more generalised approaches have been taken in **Greece**, where an auditing service, specialised in municipalities and regions has been created to keep a tight control on local and regional government spending.

In the **UK**, the CEMR member, the LGA, reports that some councils, rather than simply making cuts or merging operations (see below), have taken steps to re-engineer processes, so that redundant stages can be removed, increasing efficiencies and cutting costs.

It is also clear that in a number of countries savings have been sought by merging local authorities themselves. In Portugal, for example, the government published proposals in 2011, which involved a 35% reduction in the number of parishes (the lowest level of local administration).<sup>10</sup> In Finland too, where there has already been a programme of municipal mergers, with the number of municipalities falling from 432 in 2005 to 336 in 2011, the government is planning major reforms which will see a further reduction.<sup>11</sup>

## The greater use of technology

Here, the European Committee survey suggests that the main focus has been in cutting energy costs. **Austria, Cyprus, the Czech Republic, Denmark and Slovakia** all refer to this in their responses to the survey. The Danish reply points out that, *“Several municipalities are leaders in the cleantech race for technological advancement and job creation. Every year the Danish Ministry of Climate and Energy gives out an award to the municipality who does the most to mitigate climate change and promote cleantech. So there is fierce but friendly competition between the municipalities to receive this award.”*

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<sup>10</sup> Portugal: Second review under the extended arrangement, IMF, December 2011

<sup>11</sup> Finnish Local Government, Association of Finnish Local and Regional Authorities, <http://www.localfinland.fi/en/authorities/newmunicipality2017/Pages/default.aspx>

## Cooperation with other local and regional authorities

This is also an area where a number of countries have been active, as the European Committee survey makes clear. In **Austria**, a new model of regional cooperation is being introduced in Styria. In the **Czech Republic**, local governments are free to cooperate among themselves and also to form partnerships with the private sector. However, the number of associations between municipalities has declined slightly recently from 779 in 2009 to 766 in 2011. They mostly cover water supply and waste water treatment, communal services, collection of household waste, local road construction and maintenance and territorial planning. **Danish** municipalities have a long tradition of inter-municipal cooperation in a number of different policy fields. In **France** new legislation, adopted in December 2010 makes cooperation between local authorities easier. They can now share services and responsibilities, although as contributors to the joint CEMR-EPSU Workshop pointed out, this has not been without problems, as in the short term cooperation may lead to a loss of jobs.

In **Ireland** local authorities are now sharing services in areas such as regional waste management strategies, water services and the collection of rents, rates, fees and fines on behalf of the town authorities. The larger local authorities are also processing salaries and wages and planning applications on behalf of smaller local authorities within their area. One particularly interesting development in Ireland is the online annual quotation solution ([www.laquotes.ie](http://www.laquotes.ie)) to make it easier for local authorities to obtain quotations from suppliers in plant hire, haulage, tool hire and supplies and services. Suppliers can now submit a quotation online to all participating authorities rather than submitting paper based quotations individually to each local authority. In **Portugal**, there is a general stimulus for municipalities to cooperate in order to make economies of scale. In **Slovenia**, the Local self-government Act provides several forms of inter-municipal cooperation, some of which are also subsidised by the government. Municipalities can merge, organise associations of municipalities or set up joint management bodies.

However, despite these many positive examples, it is essential that local authorities act within the European Union rules on public procurement. The **Belgian** case study (see Box) indicates how the rules apply and how they have affected cooperation between local authorities in Wallonia in Belgium. It also makes it clear how important it is that in the reform of the public procurement directives, which is currently underway, to have regard to the need for flexible forms of public-public cooperation and not to make effective joint working between local authorities and other public bodies more difficult.

## Working with the private sector through public private partnerships

The responses to the European Committee survey indicate that this option has been taken up in some countries. These include: **Denmark**, where local authorities have a joint agreement with central government with a target of increasing the level of competition and use of private suppliers, **France**, where longer term public private contracts are being developed, and **Latvia**, where it is considered necessary “*to stimulate projects implemented by public and private partnership, because in the*



*future it will reduce maintenance costs of local governments*”, but currently this is not being done properly. , Finally in **Slovenia** a Public Private Act was adopted in 2006, regulating partnerships between public and private sector. This legislation provides for transparency between the public and private sector and the Slovenian Ministry of Finance provides professional advice to municipalities preparing to cooperate with the private sector and manages a list of PPP cases. In the **UK** too public private partnerships have been widely used for many major capital projects. However, they remain controversial.<sup>12</sup>

## **Working more closely with voluntary organisations – the third sector**

The European Committee survey provides little evidence that this option is being widely taken up, although the response from **Slovenia** specifically mentions the possibility. However, information provided to the CEMR-EPSU workshop indicates that in the **UK** voluntary organisations and local authorities have worked closely together for some time in the provision of services, although there are some indications that cuts in budgets are putting that relationship under strain. In **Hungary** too, voluntary bodies are increasingly being used to carry out tasks previously undertaken by the public sector. In these circumstances, it is not surprising that there are also union fears that voluntary organisations are being used to undercut the pay and conditions of existing employees and in some cases to replace them.

## **Simply cutting and reducing access**

As well as these mechanisms for dealing with the funding crisis, there are also others, which in terms of the impact on service provision are much less satisfactory. These include: cutting the services provided and reducing access to local public services, through measures such as means testing, cutting hours or limiting use to certain groups of users.

The boundaries between these less positive solutions and rationalisation or increases in charges may not always be clear, but the European Committee report identifies some changes which seem in part to fall into this more negative category. In **Latvia** for example, many hospitals have been closed: in 2006 there were 106 hospitals, in 2010 only 39 are left. In **Romania**, “the school and hospital networks are in full process of rationalisation, which means closing down or merging facilities,” although the closure of hospitals or their downgrading to social care facilities, with a consequent loss of funding has produced local protests.

## ***The way forward***

These developments indicate that local and regional authorities are taking a range of measures to improve their financial position at a time when the demand for their services is growing. Indeed in the longer term the challenges faced by local and

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<sup>12</sup> See *EPSU Briefing on Public-Private Partnerships (PPPs), “10 facts about public-private partnerships (PPPs)”*, November 2011

regional government can only increase with an ageing population, as analysis undertaken by the Swedish Association of Local Authorities and Regions has shown. (This suggests that the number of inhabitants in Sweden aged over 85 will increase from around 250,000 to 450,000 between 2020 and 2035.)

CEMR and EPSU pointed out in a joint statement in October 2011, the policy of austerity has “only contributed to the negative developments in growth and employment”, while “risking a race to the bottom” in the provision of quality local public services. The way forward is for government and European institutions to “take a long-term perspective” and it is clear social dialogue is vital for successful long-term planning and innovative ways of cooperation.

Social dialogue can play a crucial role in developing and implementing new ways of working. However, it is clear that it has been damaged by the way that national governments, under pressure from the markets and in some cases under instruction from international institutions, have introduced cuts and freezes in pay affecting regional and local government without adequate consultation.

It is also clear that local and regional government has been willing to find new ways of working to reduce costs and safeguard services, with increased joint working between individual local authorities being one of the best examples. However, as the Belgian case study makes clear, the room for this cooperation is tightly circumscribed by EU public procurement rules.

### **Recommendations for Social Partners**

#### **1. Major strengthening of social dialogue**

National governments should be using the route of social dialogue to deliver new methods of working and to cope with the financial crisis, including providing the financial support to enable social dialogue to take place. At the same time European institutions should not simply pay lip service to social dialogue in the recommendations to member states but should allow it to function effectively.

#### **2. A flexible approach to public procurement**

In its reform of the public procurement directives it is essential that flexible forms of public-public cooperation continue to be permitted.

## **WORKSHOP CASE STUDIES**

### ***Public procurement rules and their impact on local government in Belgium***

EU public procurement rules, requiring work to be put out to competitive tender, have the potential to make joint working between local authorities much more difficult. This is because the basic principle is that the rules apply where the provider is distinct from the contracting authority, even if the provider itself is also a public entity.

However, local authorities in Belgium have adapted their practices to reflect decisions by the European Court of Justice (ECJ) on the circumstances when the public procurement rules do not apply. One change of practice relates to so-called “in house” arrangements<sup>13</sup>, where the ECJ has ruled that the rules do not apply providing, among other things, that the contracting authority is able to exercise a controlling influence over the provider’s decisions, even though the provider is a legally separate body.

In Belgium, the consequences of this have been seen clearly in the operation of inter-municipal associations, known as “intercommunales”. They are often involved in waste collection and waste management, water distribution, hospital management and economic development over a wider area than a single local authority. Their main formal characteristics are that they involve cooperation between municipalities (at least two) and that they have a separate legal personality. They can be both purely public, “intercommunales pures”, or have some private stakeholders, “intercommunales mixtes”.

As the “intercommunales pures”, those with no private sector involvement, are not affected by the public procurement rules, as interpreted by the ECJ, there has been a shift towards them and away from “intercommunales mixtes” which have private sector involvement.

For the future, Walloon local authorities hope that their supervisory authority (the Walloon Region) will allow them to take full advantage of the opportunities for efficient cooperation that the ECJ decisions have opened. It is also very important in drawing up new legislation at European level to have regard to the need for flexible forms of public-public cooperation, along the lines of those permitted by the ECJ. Imposing stricter conditions could only be damaging.

Source and further information from:

Union des Villes et Communes de Wallonie asbl

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<sup>13</sup> This is where the contracting authority exercises over the provider a control that is similar to that which the authority exercises over its own departments, and at the same time, that provider carries out the essential part of its activities with the controlling authority or authorities. See inter alia cases ‘Teckal’ (C-107/98) and ‘Coditel’ (C-324/07)

## **WORKSHOP CASE STUDIES**

### ***Income and expenditure in local government in Finland***

In Finland, local authorities have the main responsibility for social welfare, health care, education and culture. They also provide infrastructure for the road, power, water and sewage networks and have responsibility for waste management, public transport and environmental protection, although these services may also be delivered by joint municipal authorities or municipal companies and corporations.

Local authorities have a considerable freedom in deciding how to spend their money as well as how it is raised.

Just over half of all expenditure (51%) is on social welfare and healthcare followed by education and culture (24%), with other activities taking up the rest (figures for 2010).

Income is raised from local taxes (47%), sales of goods and services (27%), central government transfers (19%), borrowing (4%) and other sources (3%). Local taxes come in the form of a local income tax paid by residents – by far the most important source of tax income for local authorities, a property tax and a 22% share of corporate tax. Local authorities are free to decide their own rates of income tax, and the average local tax rate is 18.5%.

The largest single element of expenditure is wages (39%), and social insurance contributions and pensions account for a further 12%. Buying in services accounts for another 18% and buying in materials a further 10%.

In total Finnish local authorities employ some 430,000 people, some 20% of the country's workforce.

Source: Finnish Local Government, Association of Finnish Local and Regional Authorities

<http://www.localfinland.fi/en/authorities/newmunicipality2017/Pages/default.aspx>