



# Local Authorities and Public Finances: Between Administrative Autonomy and the Demands of European Union Economic Governance

*Autarquias Locais e Finanças Públicas: Entre a Autonomia Administrativa e as Exigências da Governança Económica da União Europeia* idioma

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## Abstract

Local authorities in Portugal have played an important role in the development and dynamization of the territories. Since its constitution, through the strengthening of its powers with the revolution of April 25, 1974, to more recent times, local power has managed to adapt to the realities of the times, greatly influenced by constant popular pressure, as a result of the proximity that they have with the people. It is in this context that this study intends to develop the role of local authorities and their impact, with current legislation, particularly regarding the powers attributed at the level of local and regional finances, emphasising the need to reconcile constitutional autonomy with the financial constraints imposed by European Union economic governance. The impact of the European Union's economic governance on the fiscal responsibility of local authorities is also addressed, demanding greater budgetary rigour and compliance with EU criteria. The paper argues that strengthening legal and financial instruments for municipalities is essential to achieving a balanced multilevel governance framework in Portugal. The importance of effective coordination between levels of government is emphasised, promoting a balance between local autonomy and the financial discipline imposed by the European legal framework.

**Keywords:** Local finances; Authorities; Regional development; Territorial cohesion; Sources of financing; European Governance.

## Resumo

*As autarquias locais em Portugal têm desempenhado um papel importante no desenvolvimento e dinamização dos territórios. Desde a sua constituição, passando pelo reforço das suas competências com a revolução de 25 de abril de 1974, até aos tempos mais recentes, o poder local tem conseguido adaptar-se às realidades dos tempos, muito influenciado pela constante pressão popular, fruto da proximidade que têm com as populações. É neste contexto que o presente estudo pretende desenvolver o papel das autarquias locais e o seu impacto, com a legislação em vigor, nomeadamente no que diz respeito às competências atribuídas ao nível das finanças locais e regionais, salientando a necessidade de conciliar a autonomia constitucional com os constrangimentos financeiros impostos pela governação económica da União Europeia. É também abordado o impacto da governação económica da União Europeia na responsabilidade fiscal das autarquias locais, exigindo um maior rigor orçamental e o cumprimento dos critérios comunitários. O artigo defende que o reforço dos instrumentos jurídicos e financeiros das autarquias é essencial para alcançar um quadro de governação multinível equilibrado em Portugal. É sublinhada a importância de uma coordenação efetiva entre níveis de governo, promovendo um equilíbrio entre a autonomia local e a disciplina financeira imposta pelo quadro jurídico europeu.*

**Palavras-chave:** Finanças locais; Autarquias; Desenvolvimento regional; Coesão territorial; Fontes de financiamento; Governança europeia.

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## Summary

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## 1. Introduction

Portugal has a political-administrative structure similar to many member states of the European Union, where the role of local authorities is decisive for the development of the population (Pires, 2006, pp. 907-930; Ribeiro, 2011; Rodrigues, 2008; Monteiro, 2010, pp.39-58, Pereira & Tavares, 2007, Pinéu, 2023, p. 22).

Local and regional finances in Portugal are fundamental to understanding the role of local authorities and autonomous regions in the economic management and development of their communities, in a context of administrative decentralization (Ribeiro, 2010, pp.63-85; Pires, 2007, pp.99-119; Rodrigues, 2011, pp.45-64).

It is in this perspective that we seek to combine the autonomy of local authorities (municipalities and parishes) and the autonomous region of the Azores, in terms of revenue and resource management, taking into account the specific needs of each territory. In this respect, it seems that the matter in question raises pertinent issues for the efficient use of public resources. This article argues that strengthening the financial and legal autonomy of local authorities—particularly in insular regions like the Azores—is essential for ensuring territorial cohesion and effective public service delivery. However, this autonomy is increasingly limited by the constraints imposed by European Union economic governance. The central thesis of this paper is that a rebalancing of powers and resources is necessary to reconcile constitutional guarantees of local autonomy with the fiscal discipline required by the EU, through legal reform and coordinated multilevel governance.

Given the relevance of this topic in light of both constitutional principles and EU economic governance, the study aims to: (i) examine the current legal and financial frameworks applicable to local authorities; (ii) assess the effects of European fiscal rules on municipal autonomy; and (iii) offer recommendations for legislative reform and regional policy.

This study adopts a qualitative and interpretative approach based on the review of legal texts, public policy documents, and empirical financial data from official sources such as the Court of Auditors and the Financial Yearbook of Portuguese Municipalities. The selection of empirical references prioritised territorial relevance (particularly the Autonomous Region of the Azores), recentness of data, and institutional representativeness, aiming to ensure analytical coherence between legal norms and financial realities.

The paper is structured as follows: Section 2 addresses the fundamentals of local and regional finance; Section 3 explores financial autonomy and revenue sources; Section 4 presents management challenges; Section 5 evaluates the impact on quality of life; Section 6 outlines policy recommendations; Section 7 analyses EU economic governance and its local implications; and Section 8 concludes the study.

## 2. Fundamentals of local and regional finance

The Portuguese public sector carries out its mission of producing, providing and allocating goods and services to citizens. To this end, it is structured into various subsectors (organizational forms) with different legal and institutional frameworks (Figueiredo, 2009, pp.105-123; Viegas, 2010, pp.89-110; Rodrigues, 2011, pp.101-120; Monteiro, 2013, pp. 45-65).

The Public Administrative Sector (PAS)- the State in the broad sense – corresponds to the largest component of the public sector and ensures the functions of income redistribution, resource allocation and macroeconomic stabilization, through the provision of public goods and services (Fernandes, et al, 2024, p. 21).

The democratic organization of the Portuguese state includes the existence of local authorities, as provided for in the Constitution of the Portuguese Republic (CRP).

The principle of the autonomy of local power is enshrined in Article 6, establishing the basis for this autonomy in the section on the organization of political power, under the heading "Local Power".

According to Article 235, *"the democratic organization of the State includes the existence of local authorities"*. These are defined in Article 236 as *"territorial legal persons endowed with representative bodies, which aim to pursue the interests of their respective populations"*. On the mainland, local authorities include parishes, municipalities and administrative regions. In the autonomous regions, local authorities include parishes and municipalities.

This structure reflects a partially regionalised State, a constitutional model that combines a unitary state with elements of decentralisation, by recognising autonomous regions with specific legislative and financial powers. Unlike a fully federal system, the Portuguese model maintains national sovereignty while granting limited self-government to regions like the Azores and Madeira.

The actions of local authorities are governed by a set of principles that guarantee their legal and institutional autonomy in the pursuit of their objectives and in the management of their resources, as set out in the framework of attributions and competencies established by Law no. 75/2013, of September 12<sup>1</sup>.

The principle of local government autonomy is established in Article 6 of the Constitution of the Portuguese Republic (CRP). This is further reinforced by the European Charter of Local Self-Government<sup>2</sup>. According to Article 3 of the Charter, autonomy means the *"effective capacity of local authorities to regulate and manage, under the terms of the law, and under their responsibility and in the interests of their respective populations, an important part of public affairs"*, under the law and in the interest of their populations.

In addition, the CRP recognizes the archipelagos of the Azores and Madeira as autonomous regions, as stipulated in Article 5. These regions are considered public legal entities, endowed with political-administrative statutes and self-government bodies (Article 6), with the mission of promoting the democratic participation of citizens, economic and social development and the defense of regional interests (Article 225(3)).

Although they have political and administrative autonomy, this does not compromise the unitary nature of the state or the integrity of national sovereignty (Article 225(3)).

The statutes of the autonomous regions are approved by parliamentary law (Article 226), through the legislative initiative of the respective Regional Legislative Assemblies (Article 226(1)). The powers and competences of the autonomous regions are defined both in the CRP (Article 227) and in their statutes<sup>3</sup>.

The subsidiarity principle, although often invoked in discussions on decentralisation, must be properly contextualised. Originating in EU law (Article 5(3) of the Treaty on European Union), subsidiarity states that decisions

<sup>1</sup> Law no. 75/2013, of 12 September. Available at: [https://www.pgdlisboa.pt/leis/lei\\_mostra\\_articulado.php?nid=1990&tabela=leis](https://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=1990&tabela=leis) .Accessed on: 6 may 2025.

<sup>2</sup> European Charter of Local Self-Government. 1985. Available at: <https://rm.coe.int/european-charter-of-local-self-government-prt-a6/16808d7ea0> . Accessed on: 8 may. 2025.

<sup>3</sup> Articles 7, 8 and 9 of Law no. 2/2009, of 12 January (Approves the third revision of the Political-Administrative Statute of the Autonomous Region of the Azores). Available at: <https://diariodarepublica.pt/dr/detalhe/lei/2-2009-397322> .Accessed on: 6 may 2025.

should be taken as closely as possible to the citizens. In the Portuguese context, however, subsidiarity is not a constitutional principle *per se*, and should not be confused with administrative decentralisation or devolution of powers, which are governed by national constitutional and infra-constitutional provisions. Its application to the Azores, therefore, remains more political than legal, requiring careful doctrinal treatment.

## 2.1 Main components of regional finance : revenue, expenditure and financing

The autonomous regions of the Azores and Madeira have political-administrative statutes in force, namely Law no. 2/2009, of January 12<sup>6</sup>, and Law no. 13/91, of June 5, respectively. These aim to regulate the autonomy of the two regions within the legal framework of the Portuguese state.

In the case of the Autonomous Region of the Azores, the statute aims to define political and administrative autonomy, guaranteeing the capacity for self-government within constitutional and legal limits (articles 1 and 2); the organization of self-government bodies, defining the composition and functioning of the Regional Legislative Assembly, as well as the Regional Government and other bodies (articles 27 to 48); legislative and administrative powers (articles 49 to 63); and the relationship between the regional government bodies and sovereign bodies, including representation of the state. These include the relationship between the regional government bodies and sovereign bodies, including the representation of the state in the region (Articles 64 to 70) and the management of assets and finances through rules on financial management, such as the allocation of own revenue and transfers from the state budget (Articles 71 to 84).

To this end, Organic Law no. 2/2013<sup>8</sup> which approved the Autonomous Regions' Finance Law (LFRA), defines the rules for the financing and financial autonomy of both archipelagos, namely through their own fiscal resources; intergovernmental transfers and by resorting to credit or other forms of indebtedness.

The autonomous regions are the exclusive holders of regional tax revenue, as stipulated in Article 57 of the LFRA. In addition, they receive all the revenue from national taxes levied or generated in their respective territories, such as Personal Income Tax (IRS), Corporate Income Tax (IRC), Value Added Tax (VAT), excise duties and excise duty on gambling. This provision is laid down in Article 24(1) and Articles 25 to 32 of the LFRA, and is also confirmed by Article 19 of the Political-Administrative Statute of the Autonomous Region of the Azores (Law 39/80, revised by Law 2/2009) and Article 108 of the Political-Administrative Statute of the Autonomous Region of Madeira (Law 13/91).

Importantly, Article 227(1)(i) of the Constitution of the Portuguese Republic (CRP)<sup>4</sup> affirms that autonomous regions may exercise tax powers and adapt the national tax system to regional specificities. In accordance with this constitutional provision and Article 59 of the Finance Law of the Autonomous Regions (LFRA), the Azores currently apply a 30% reduction on personal income tax (IRS), corporate income tax (IRC), and VAT—an expression of their autonomous fiscal capacity "*[to exercise] its own tax power, under the terms of the law, as well as [to adapt] the national tax system to regional specificities, under the terms of a framework law of the Assembly of the Republic*".

In addition to tax revenue, the regions benefit from intergovernmental transfers, both compulsory and discretionary. One key instrument is the Cohesion Fund (Article 49, LFRA), dedicated exclusively to financing investment programs and projects listed in the regions' annual plans. In addition, the regions can benefit from other specific subsidies, such as: financing projects of common interest (Article 51 of the LFRA); national participation in incentive systems (Article 50 of the LFRA) and exceptional support for natural disasters (Article 8(5) of the LFRA).

In exceptional cases, financial protocols can be signed between the state and the autonomous regions, based on mutual commitments (Article 52, LFRA). These agreements, though not foreseen in the original law, must still comply with general principles of legality and proportionality.

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<sup>4</sup> Constitution of the Portuguese Republic, VII Constitutional Revision of 12 August 2005. Available at: <https://www.parlamento.pt/Legislacao/Documents/crp-2021-net.pdf>. Accessed on: 8 may. 2025.

However, according to Leite (2017, pp. 19-20), *"the Regional Finance Law, although classified as organic, neither brought stability to the financial relations between the State and the Regions nor prevented progressive indebtedness, despite the generous funds coming from Europe. The Regional Finance Law itself has been successively breached, in the name of the state's financial difficulties, increasing the instability it was intended to avoid, and has never been revised, as planned, to adapt to the circumstances."*

Current regional leaders, such as the Regional Secretary for Finance and Public Administration, Duarte Freitas, have highlighted that Azorean public services face significantly higher costs than on the mainland—22% more in health and 11% more in education. These structural differences justify calls for a revised LFRA.<sup>5</sup>

José Manuel Bolieiro, the current President of the Regional Government of the Azores, has also referred to this need, even announcing that *"the law is wrong and that the State has to look at the autonomous regions with more solidarity"*.<sup>6</sup>

In addition, the concerns shown by the Azores Regional Section of the Court of Auditors, in its report and opinion on the Autonomous Region of the Azores account for 2023,<sup>7</sup> stated that there was an overall or actual negative balance of 88.2 million euros, and that the total debt of the regional public administrative sector at the end of the 2023 budget year was 3.315.9 million, with an increase in net debt of 107.5 million euros, contrary to the limits set for 2023 in the State Budget Law and the Budget of the Autonomous Region of the Azores.

In the same opinion Leite (2017, p. 21) notes that it is also clear that current revenue (1,147,102,899 euros) is insufficient for current expenditure (1,385,939,492 euros). Given that the LFRA has remained unchanged for over a decade, the growing mismatch between regional costs and legal provisions is increasingly untenable. Calls to revise the law, particularly to reflect the true costs of insularity and demographic dispersion, appear well founded.

### 3. The importance of local authorities' financial autonomy

Local authorities have patrimonial autonomy (their own assets); budgetary autonomy (the possibility of drawing up, approving and implementing their own budget); tax autonomy (creating and collecting taxes); credit autonomy (the possibility of resorting to credit, either by taking out loans or by issuing municipal bonds or other legally prescribed legal forms); treasury autonomy (and more concrete and enforceable powers to carry out its own expenditure and collect its own revenue, without depending on authorization from any central state body) (Rocha, Cruz & Silva, 2017, p. 194).

This is reinforced by the Local Finance Law,<sup>8</sup> which materializes the financial autonomy of municipalities, namely in article 6, no. 2 of Law no. 73/2013, and by Article 238 of the Constitution of the Portuguese Republic (CRP), which explicitly guarantees local authorities the right to their own revenues, property, and budgets.

Also, the European Charter of Local Self-Government<sup>9</sup> in Article 3(1) refers to *"the right and effective capacity of local authorities to regulate and manage, in accordance with the law, under their responsibility and in the interests of their populations, an important part of public affairs."*

Financial autonomy requires that local authorities have sufficient financial means to carry out their duties, but also to incur expenditure without the need for third-party authorization (Cândido de Oliveira, 2013, p. 213).

<sup>5</sup> Regional Finance Law: Study reveals overcosts in Health and Education. RTP Açores. Available at: <https://acores.rtp.pt/politica/lei-de-financas-regionais-estudo-revela-sobrecustos-com-saude-e-educacao/>. Accessed on: 6 may 2025

<sup>6</sup> Regional Finance Law: Bolieiro says the State must look at Madeira and the Azores with more solidarity. RTP Açores. Available at: <https://acores.rtp.pt/politica/lei-das-financas-regionais-bolieiro-diz-que-o-estado-tem-de-olhar-a-madeira-e-os-acores-com-mais-solidariedade/>. Accessed on: 6 may 2025.

<sup>7</sup> Report and Opinion on the Accounts of the Autonomous Region of the Azores for 2023- Summary. Court of Auditors. Available at: [https://www.tcontas.pt/pt-pt/ProdutosTC/PareceresTribunalContas/pareceres-craa/Documents/2023/Parecer\\_CRAA\\_2023.pdf](https://www.tcontas.pt/pt-pt/ProdutosTC/PareceresTribunalContas/pareceres-craa/Documents/2023/Parecer_CRAA_2023.pdf). Accessed on: 6 may 2025.

<sup>8</sup> Financial Regime of Local Authorities and Intermunicipal Entities. Law 73/2013, of 3 September 2013. Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/lei/2013-105795409-116088595>. Accessed on: 8 may. 2025.

<sup>9</sup> Resolution of the Assembly of the Republic no. 28/90, of 23 October (European Charter of Local Self-Government). Available at: [https://www.pgdlisboa.pt/leis/lei\\_mostra\\_articulado.php?nid=2279&tabela=leis&ficha=1&pagina=1&so\\_miolo=](https://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=2279&tabela=leis&ficha=1&pagina=1&so_miolo=). Accessed on: 6 may 2025.



Thus, financial autonomy is directly related to the principle of local autonomy (Article 235 of the CRP), which guarantees municipalities the power of self-administration within the limits of the law, ensured by the Financial Regime of Local Authorities and Intermunicipal Entities (Law 73/2013, of September 3<sup>10</sup>), namely with regard to financing mechanisms, allocations of own revenue and transfers from the State Budget.

In addition, Article 238(2) of the CRP states that the principle of local autonomy is aimed at the fair distribution of public resources, which is where the principle of equality between municipalities of the same level comes in.

The financial autonomy of local authorities is essential for implementing public policies that meet the real needs of their citizens. This is particularly visible in peripheral or insular municipalities, such as those in the Azores, where distance from the central administration increases the importance of local fiscal capacity and rapid response. Proximity to the population, interaction with parish councils and even popular pressure mean that local authorities are able to act more quickly on the various requests made of them by law.

However, this autonomy can and must be supervised by the competent bodies, starting with the Municipal Assemblies, which is the deliberative body and is responsible for approving and supervising the main documents of the municipalities (Major Planning Options and Accountability), but also by the Court of Auditors, which is responsible for supervising the legality and regularity of public revenue and expenditure.

In short, the constitutional and legal framework offers a formal basis for autonomy, but its full realisation depends on the adequacy of financial resources and the proper functioning of oversight mechanisms

### 3.1 Sources of municipal revenue

The state needs sufficient financial resources to be able to carry out the tasks assigned to it and for this to happen, and for its existence to last, it is necessary to mobilize sufficient financial resources obtained in various ways. To ensure its sustainability, it must mobilise revenue through various means—foremost among them taxation (Pinto, 2021, p. 3).

A tax is public revenue decreed by the state (a public entity with legal powers to demand compliance with tax obligations, as is the case with local authorities) to entities, whether legal or natural, that are subject to its authority. It has a fundamentally financial function and aims to promote social justice, fair distribution of wealth, and equal opportunities, as established in Article 103(1) of the Constitution of the Portuguese Republic (CRP) and Article 5(1) of the General Tax Law (LGT).

As Sá Gomes (1980, p. 78) defines it: *"a tax as the definitive patrimonial benefit established by law in favor of an entity that is in charge of exercising public functions, for the satisfaction of public purposes, which do not constitute a sanction for illicit acts"*

The Financial Regime of Local Authorities (Law no. 73/2013 of September 3) modernised the framework for municipal revenue, enhancing accountability and coordination between central and local administration. It also sought to equip municipalities with financial tools to ensure budgetary stability and prevent imbalances (Azevedo, 2018, p. 166).

The financial activity of local authorities is carried out in compliance with the following principles (art. 3, no. 2 of Law 73/2013): a) Principle of legality; b) Principle of budgetary stability; c) Principle of financial autonomy; d) Principle of transparency; e) Principle of reciprocal national solidarity; f) Principle of intergenerational equity; g) Principle of fair distribution of public resources between the State and local authorities; h) Principle of coordination between local finances and State finances; i) Principle of inspective supervision (Azevedo, 2018, p. 167).

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<sup>10</sup> Financial Regime of Local Authorities and Intermunicipal Entities. Law 73/2013, of 3 September 2013. Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/lei/2013-105795409-116088595>. Accessed on: 8 may. 2025.

According to Article 238 (1) to (4) of the CRP,<sup>11</sup> local authorities have their own assets and finances, their own revenue must include revenue from the management of their assets and revenue collected from the use of their services, and they may have taxing powers, in the cases and under the terms of the law.

On this regard, Article 14 of Law 73/2013<sup>12</sup> refers to the various sources of municipal revenue, namely: the proceeds from the collection of municipal property tax (IMI); the proceeds from the collection of municipal property transfer tax (IMT); the proceeds from the collection of spills levied under the terms of Article 18º of Law 22- A/2007; the portion of the proceeds from the single circulation tax that falls to the municipalities, under the terms of article 3 of Law no. 22-A/2007,<sup>13</sup> of June 29; the proceeds from the collection of civil protection contributions, under the terms of the law; the proceeds from the collection of fees and prices resulting from the granting of licenses and the provision of services by the municipality, in accordance with the provisions of articles 20 and 21. The proceeds from the participation in public resources determined in accordance with the provisions of articles 25 et seq.

The proceeds from the collection of capital gains charges allocated by law to the municipality; the proceeds from fines and penalties set by law, regulation or ordinance that fall to the municipality; the income from own property, movable or immovable, administered by them, given in concession or transferred for exploitation; participation in the profits of companies and in the results of other entities in which the municipality takes part; the proceeds of inheritances, legacies donations and other donations in favor of the municipality; the proceeds of the sale of its own property, movable or immovable; the proceeds of loans, including those resulting from the issue of municipal bonds; and revenue established by law or regulation in favor of municipalities.

Municipal activity encompasses responsibilities such as urban licensing, cleaning of municipal roads, waste collection to agreements of collaboration with local institutions (Article 33 of Law 75/2013). It is therefore necessary to have revenue to cover all the needs that are legally the responsibility of a municipality.

While often insufficient, these revenues are essential to implement budgets that respond to legal mandates and public expectations. For example, Fernandes et al. (2024) report that in 2023, municipal taxes represented 35.4% of total municipal revenue nationally, but only 27.2% in Azorean municipalities, which increases their dependence on intergovernmental transfers and EU funds.

### 3.1.1 Municipal taxes and local fees

According to Azevedo (2018, p. 172nd Article 3(2) of the General Tax Law<sup>14</sup> (LGT), the Portuguese tax system includes three main types of charges: taxes (impostos), fees (taxas), and special contributions.

Taxes are unilateral and compulsory charges that do not depend on any direct consideration. They are primarily based on the taxpayer's ability to pay, typically measured by income, consumption, or property holdings (Article 4(1), LGT). Their purpose is to fund public needs in a broad and general sense.

In contrast, fees are bilateral and synallagmatic: they are paid in return for a specific public service, the use of a public asset, or for the removal of a legal barrier affecting private conduct (Article 4(2), LGT). In short, fees imply a concrete benefit to the payer.

In this context, municipal taxes are: IMI (Municipal Property Tax); IMT (Municipal Property Transfer Tax) and the Municipal Surtax (Azevedo, 2018, pp. 178 to 185).

<sup>11</sup> Constitutional Law no. 1/2005, of 12 August. Available at: <https://diariodarepublica.pt/dr/detalhe/lei-constitucional/1-2005-243729>. Accessed on: 8 may. 2025.

<sup>12</sup> Financial Regime of Local Authorities and Intermunicipal Entities. Law 73/2013, of 3 September 2013. Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/lei/2013-105795409-116088595>. Accessed on: 8 may. 2025.

<sup>13</sup> Vehicle Tax Code and Single Circulation Tax Code. Law no. 22-A/2007, of 29 June. Available at: <https://diariodarepublica.pt/dr/detalhe/lei/22-a-2007-226204>. Accessed on: 6 may 2025.

<sup>14</sup> Decree-Law no. 398/98, published in the Official Gazette no. 290/1998, Series I-A of 1998-12-17. (General Tax Law). Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/decreto-lei/1998-34438775>. Accessed on: 8 may. 2025.



These taxes are regulated by specific legislation, such as the IMI code<sup>15</sup>, and referenced in Article 14(a) of Law 73/2013. Each year, municipalities can set the applicable tax rates within legal limits.

Regarding fees, it can be said that they are due for the provision of a public service, such as garbage collection or sanitation; for the use of a public asset, such as the use of or access to assets as diverse as a bridge, a road or a monument; for the occupation of spaces in fairs and markets; for the parking of vehicles in municipal parks or even for the holding of shows or concerts (Prudêncio, 2018, pp. 28 and 29).

Another noteworthy municipal tax is the tourist tax, applied when individuals stay overnight in a municipality. This tax is justified by the increased demand placed on public services (e.g., security, cleaning, waste management). Its aim is to help fund infrastructure that supports both residents and visitors (Alves, 2019, pp. 49-50).

To distinguish taxes from fees, scholars often refer to two criteria:

- the economic criterion — fees apply when no market alternative exists and the public service is indispensable, and
- the indispensability criterion — the service must respond to a concrete public need not otherwise met (Prudêncio, 2018, p. 31).

This understanding is also supported by the Portuguese Constitutional Court Ruling no. 143/2202, of April 9, 2002<sup>16</sup>, the bilateral nature of fees *"means that their payment corresponds to a specific 'consideration' on the part of the State (or other public entity). If this does not happen, we have a 'tax' (or a tax figure which, from a constitutional point of view, should at least be treated as such)"*.

Although crucial to municipal budgets, both taxes and fees are insufficient to fully support the broad scope of local responsibilities established by Law 75/2013 (Article 33). For instance, Fernandes et al. (2024) show that in 2023, these sources accounted for only 35.4% of total municipal revenue nationally, and even less in Azorean municipalities (27.2%), underscoring the need for supplementary funding.

### 3.1.2 Government transfers and cohesion funds

Law 73/2013, of September 3, which establishes the Financial Regime for Local Authorities and Intermunicipal Entities (RFALEI), outlines the legal framework for financial transfers between the State and municipalities. These transfers aim to ensure fair access to resources and reinforce the autonomy of local authorities.

According to Article 10 of the RFALEI, the distribution of public resources between the State and local authorities must be fair, ensuring that municipalities have the necessary means to fulfill the duties and responsibilities legally assigned to them (no. 1). This distribution is guided by principles of vertical and horizontal financial balance (no. 2). Vertical financial balance seeks to align the resources of each level of administration with the specific duties and powers assigned to them by law (no. 3). Horizontal financial balance aims to correct inequalities between local authorities of the same level. These inequalities often stem from differences in revenue-generating capacity or variations in local expenditure needs (no. 4).

These objectives are operationalised through various forms of participation in public revenue, defined in Articles 25–34 of Law 73/2013.

<sup>15</sup> Decree-Law no. 287/2003, published in the Official Gazette no. 262/2003, Series I-A of 2003-11-12. (Codes of Municipal Property Tax- CIMI- and Municipal Property Transfer Tax). Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/decreto-lei/2003-34499575> .Accessed on: 8 may. 2025.

<sup>16</sup> Judgement no. 143/2022. Case no. 1225/2021. 3rd Chamber. Available at: <https://www.tribunalconstitucional.pt/tc/acordaos/20220143.html> . Accessed on: 6 may 2025.

### A) General Transfers

The General Financial Equilibrium Fund (FEF) is the core mechanism through which central government transfers financial resources to municipalities. As per Article 25(a), it corresponds to 19.5% of the average national revenue from IRS, IRC, and VAT, calculated over a reference period.

In addition to the FEF, municipalities receive funds via the Municipal Social Fund (FSM), intended to finance decentralised functions in education, health, and social services. Eligible expenditures are listed in Article 30(2) of Law 73/2013.

The distribution criteria for the FSM are defined annually in the State Budget and follow objective variables laid out in Article 34, such as population, education enrolments, and socio-economic vulnerability.

### B) Participation in National Taxes

Municipalities also receive a variable share of Personal Income Tax (IRS) — up to 5% of the net collection attributed to residents in each municipality, as specified in Article 26 of the RFALEI.

They are additionally entitled to a 7.5% share of VAT revenue, under Article 26-A, distributed proportionally based on VAT collected from specific sectors (e.g., hospitality, energy, communications) within each municipality. This includes corrective mechanisms for cohesion and solidarity, defined by ministerial ordinance.

In the Azores, this VAT-sharing mechanism was implemented through Regional Legislative Decree no. 40/2023/A, of November 27,<sup>17</sup> which transfers 0.35% of total regional VAT revenue to Azorean municipalities. Distribution follows a hybrid model:

- 25% equally divided among all 19 municipalities;
- 75% distributed proportionally based on population and average daily tourist stays, per official regional statistics (Article 3(1) of the decree).

### C) Cohesion and EU Structural Funds

Beyond national transfers, cohesion policy funds from the European Union are essential to regional and municipal development — particularly in less developed regions such as the Azores.

Since Portugal's accession to the EU in 1986, successive Community Support Frameworks have channelled structural funds toward infrastructure, territorial cohesion, and public services (BOTELHO, 2022, p. 32).

Under Portugal 2020 (PT2020) — a key multiannual financial framework worth €25 billion (BOTELHO, 2022, p. 44), — the Azores 2020 Operational Programme received a budget of €1.4 billion<sup>18</sup>, financed by the ERDF and ESF distributed among the various regions of the country and according to various criteria.

According to the PO Açores 2020 monthly bulletin,<sup>19</sup> 101.39% of the budget was executed, with Azorean municipalities implementing around €85 million of projects (from a total eligible investment of €100 million), reflecting an 85% execution rate.<sup>20</sup>

It is therefore clear that government transfers and cohesion funds are essential to make up for the lack of local authority revenue. If, on the one hand, transfers such as the FEF, the FSM, the municipal surcharge and a percentage of the VAT collected help to bridge the gap in the territories, especially in municipalities where the population is small

<sup>17</sup> Regional Legislative Decree no. 40/2023/A, published on November 27, 2023 in the Diário da República, 1st series. Available at: <https://files.diariodarepublica.pt/1s/2023/11/22900/0008500087.pdf>. Accessed on: 6 may 2025.

<sup>18</sup> Inforegio - Azores Regional Operational Programme 2014-2020. Language selection | European Commission. Available at: [https://ec.europa.eu/regional\\_policy/in-your-country/programmes/2014-2020/pt/2014pt16m2op004\\_pt](https://ec.europa.eu/regional_policy/in-your-country/programmes/2014-2020/pt/2014pt16m2op004_pt). Accessed on: 6 may 2025.

<sup>19</sup> Monthly Bulletin- June 2024. Azores 2020. Regional Directorate for Planning and Structural Funds. Available at: <https://poacores2020.azores.gov.pt/wp-content/uploads/2024/07/Boletim-Mensal-JUN--24.pdf>. Accessed on: 6 may 2025.

<sup>20</sup> Azores 2020 Operational Programme Information Bulletin- 1st Quarter 2024. Regional Directorate for Planning and Structural Funds. Available at: [https://www.adcoesao.pt/wp-content/uploads/acores\\_bt\\_1t2024.pdf](https://www.adcoesao.pt/wp-content/uploads/acores_bt_1t2024.pdf). Accessed on: 8 may. 2025.

compared to large urban areas, cohesion funds can be considered extra revenue for structuring projects for the territories.

Currently, the region is implementing Azores 2030, funded by ERDF and ESF+, with a total allocation of €1.134 billion. Of this, €161 million<sup>21</sup> is earmarked for municipalities, supporting areas such as:

- economic competitiveness,
- social inclusion,
- sustainable mobility,
- climate adaptation, and
- digital transformation.

Thus, European funds continue to play a structuring role in strengthening the financial capacity of Azorean municipalities, enabling them to respond more effectively and sustainably to the contemporary challenges of territorial development.

#### D) Significance

These national and European transfers are critical to municipalities with limited own-revenue capacity.

- On the one hand, FEF, FSM, and VAT/IRS share structural imbalances and enable municipalities to deliver legally assigned services.
- On the other hand, EU cohesion funds provide a complementary source of financing for long-term, transformative projects.

As the example of Azores 2020 illustrates, these resources have enabled major investments that would otherwise be unaffordable, helping bridge development gaps between mainland and island territories.

### 3.1.3 Loans and external financing

Local authorities may also access credit as a supplementary source of financing. This mechanism is essential when own revenues and public transfers are insufficient to meet investment needs, especially for long-term infrastructure or emergency liquidity support.

The credit regime for municipalities is regulated in articles 49 to 51 of the RFALEI, i.e., municipalities can take out loans, including credit facilities, from any institutions authorized by law to grant credit. Short-term loans are taken out only to deal with cash-flow difficulties, while medium- and long-term loans can be taken out for investment or to proceed in accordance with municipal financial recovery mechanisms.

Municipal indebtedness, which can result from the use of credit, is an important financial instrument, as it enables municipalities not only to obtain revenue to carry out the duties for which they are responsible but also provides greater stability for local finances (Lobo & Ramos, 2011).

This assumption is further corroborated by Article 9(8) of the European Charter of Local Self-Government, which states that local authorities must have access to the national capital market, under the terms of the law, to finance their investment expenditure.

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<sup>21</sup> Azorean local authorities to benefit from 161M€ from the Azores 2030 Community Framework. RTP Açores. Available at: <https://acores.rtp.pt/local/autarquias-acorianas-vao-beneficiar-de-161me-do-quadro-comunitario-acores-2030/>. Accessed on: 8 may. 2025.

In order to avoid heavy indebtedness, according to article 52 of the RFALEI, the municipality's total debt from budgetary operations may not exceed 1.5 times the average net current revenue collected (by the municipality) in the previous three financial years.

Total debt from budgetary operations in municipalities includes loans, leasing contracts and any other forms of indebtedness, at the initiative of the municipalities, from financial institutions, as well as all other debts to third parties arising from budgetary operations and is calculated as the sum of liabilities due and debts from non-budgetary operations.

### 3.1.4 Public-private partnerships and fundraising

In order to carry out their duties and competencies, given the current legal framework, municipalities can resort to different organizational and financing models, such as Public-Private Partnerships (PPPs).

Both the Legal Framework for Local Authorities (RJAL), approved by Law no. 75/2013, of September 12, and the Financial Legal Framework for Local Authorities and Intermunicipal Entities (RFALEI), approved by Law no. 73/2013, of September 3, as well as Law no. 43/2012, of August 28 (Creates the Local Economy Support Program), expressly mention the admissibility of public-private partnerships. 43/2012, of August 28 (Creates the Local Economy Support Program), several provisions expressly allude to the admissibility of municipalities launching public-private partnerships (articles 7, no. 2, 9, 10 and 11). Articles 7(2), 9(2)(f) and 79(1)(d) of the RFALEI; articles 33(1)(f); 81(2)(a) of the RJAL; article 10(1)(c) of Law 43/2012 of August 28).

The preamble to the first law on PPPs (Decree-Law 86/2003 of April 26<sup>22</sup>) stated: "[in this] context, the state and other public entities have been developing alternative models and innovative experiences of relationships with private entities." From this it can be deduced that the law intended to cover all public entities, including local authorities<sup>23</sup>.

Given the legislation in force, several municipalities have PPPs, particularly in municipal services, municipal companies, municipal associations and inter-municipal companies.

A clear example is found on the island of São Miguel, in the Azores, where the municipalities of Ribeira Grande, Vila Franca do Campo, Lagoa, and Ponta Delgada operate through an inter-municipal company (MUSAMI) that contracted a private company to collect waste, thus forming part of a PPP<sup>24</sup>.

The entry of private companies into public services has the following advantages: additional capital; management skills; added value for the end customer; optimization of resources (EUROPEAN COMMISSION, 2003, p. 4)

According to Sarmento (2013), the role of Public-Private Partnerships is not just the financial components of savings, financing or the transfer of risk to an entity other than the Public Administration, but the gains in efficiency in the provision of the service, which is the factor that brings a common benefit to the partners.

Nonetheless, PPPs also have disadvantages: the risk is not always fully transferred, the public sector may lose control of operations, and the contracts are often long-term and rigid (PRICEWATERHOUSECOOPERS, 2005a, p. 4).

Despite these challenges, PPPs remain important tools for the daily management of municipal resources. They allow private entities to provide essential public services that significantly impact quality of life — such as water distribution and waste collection.

<sup>22</sup> Decree-Law no. 86/2003, of April 26. Official Gazette no. 97/2003, Series I-A of 2003-04-26, pages 2682- 2686. (Defines special rules applicable to public-private partnerships). Available at: <https://diariodarepublica.pt/dr/detalhe/decreto-lei/86-2003-240646>. Accessed on: 8 may. 2025.

<sup>23</sup> Judgment No. 18, Section 1 S/PL, p. 11. Court of Auditors. Available at: <https://www.tcontas.pt/pt-pt/ProdutosTC/acordaos/1spl/Documents/2020/ac018-2020-1spl.pdf>. Accessed on: 6 may 2025.

<sup>24</sup> Contract for the acquisition of urban waste collection and transport services for the municipalities of Ponta Delgada, Lagoa, Ribeira Grande and Vila Franca do Campo. Portal Base.gov. Available at: [https://www.base.gov.pt/Base4/pt/resultados/?type=doc\\_documentos&id=1855122&ext=.pdf](https://www.base.gov.pt/Base4/pt/resultados/?type=doc_documentos&id=1855122&ext=.pdf). Accessed on: 8 may. 2025.

## 4. Challenges and opportunities in municipal financial management

As previously discussed, local authority revenues are heavily dependent on state transfers, thus limiting the administrative and financial autonomy of local authorities. In addition, current legislation—namely Law 73/2013 of September 3—imposes very strict restrictions on the debt capacity of local authorities and on the use of revenues, thus reducing flexibility in managing local projects.

Another challenge has to do with the low qualifications of local government employees, at a time marked by new social demands and the need to solve increasingly complex problems, which, according to Canário et al. (2002, p. 31): *"The levels of schooling and professional qualifications of all Local Government staff configure an unacceptable situation and correspond to one of the structural aspects in which an intervention of a training nature proves to be indispensable"*.

In a society that is increasingly alert to social and economic issues—largely amplified by the immediacy of social media—public pressure to meet citizens' expectations is also growing. This challenge is particularly intense in local government, given its proximity and accessibility to the population.

However, there are also clear opportunities. Municipalities have the financial autonomy to manage their own revenues, which have been increasing every year, in particular the IMT (Municipal Transfer Tax), as a result of the recent real estate dynamics, whose market has appreciated significantly.<sup>25</sup>

Innovation and sustainability likewise offer an opportunity to improve quality of life and increase resource efficiency. In this respect, the Covid-19 pandemic has encouraged local authorities to adapt quickly to new working methods, which are still used today and have proved important for the efficiency of services. An example of this was the dematerialization of administrative processes, such as urban licensing; public procurement and electronic invoicing or teleworking, which according to Fontinha (2022, p. 26): *"has the conditions to perpetuate itself over time, and should be seen as an opportunity to extract the potential of workers in providing a better public service to the country"*.

Despite social pressure, as evidenced by social media, many municipalities have participatory budgets in place that encourage civic and democratic participation by the population, and are therefore a good opportunity to bring voters closer to elected representatives on a regular basis (Silva, 2017, p. 40).

In addition, PPPs (public-private partnerships) can also be seen as opportunities because they aim to attract private companies to public services, highlighting various advantages, such as risk sharing, transfer of responsibilities, more agile financing that allows the construction of more infrastructure, and lower overall project costs for the public entity. This can lead to more innovative solutions and efficiency gains, with quality and value for money (Sousa, 2015, p. 42).

It is therefore up to the top management (municipal executive) to define a mode of governance to be followed, with a political stance that defines a real strategic plan for local development. If there is no visible strategy in the organization, no meaningful direction and no solid leadership, this only increases states of discouragement, promotes disenchantment with the organization, weakens leadership, reduces organizational performance and weakens its own public mission (Caldeira, 2015).

In view of current trends—such as the growing importance of tourism in the local economy—strategic planning is crucial to ensuring balanced development that responds to the real needs of each territory.

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<sup>25</sup> IMT was the main direct tax revenue for municipalities in 2023. Notícias de Coimbra with Lusa on 13-11-2024. Available at: <https://www.noticiasdecoimbra.pt/imt-foi-a-principal-receita-de-impostos-diretos-para-os-municipios-em-2023/>. Accessed on: 6 may 2025.

## 5. The impact of local finances on people's quality of life

Quality of life can be defined as *"an individual's perception of their position in life, in the context of the culture and value systems in which they live, and in relation to their goals, expectations, standards and concerns"* (Linhares, 2019, p. 34).

According to Gonçalves (2012), measuring the quality of life in Portuguese municipalities is complex due to the many elements that affect it, whether qualitative or quantitative. They therefore advocate the quantification of economic and social development in order to clearly identify and interpret regional inequalities and thus design and implement public regional development policies capable of reversing this trend.

Municipalities with a higher quality of life are typically those that offer a broader range of goods and services. From a public policy, being efficient means allocating inputs in such a way that there is no waste and that benefits are maximized in relation to spending (Silva & Kuwahara, 2011).

Linhares (2019, p. 82) states that there are significant differences between municipalities when organized by size (small, medium and large), with large municipalities having the highest average municipal financial efficiency index due to the greater financial independence they have over smaller municipalities (which depend on transfers from the state budget).

Also, according to the same author, sociodemographic determinants such as size, location, purchasing power and unemployment rate are key to financial efficiency, with unemployment and tourism having a negative effect on this efficiency. At the political level, it was also found that ideology and the alternation of government do not influence the financial efficiency of municipalities, showing instead a negative relationship between municipal financial efficiency and the quality of life of citizens.

In practical terms, municipalities are dependent on revenue in order to be able to invest in new infrastructures that can improve the quality of life of their citizens. As revenue varies according to the size of the municipality, the larger it is, the more revenue it has, so it can channel resources into investment spending.

It should also be borne in mind that in 2023, expenditure by Portuguese municipalities was broken down into 67.8% current expenditure (including staff costs) and 32.2% capital expenditure, which means that out of a total of 13,847.7 million euros spent by municipalities, only 4,454.2 million euros went on investment (Fernandes et al., 2024, p. 136).

In the case of the Azorean municipalities, there are significant discrepancies between the 19 municipalities when it comes to current expenditure. For example, in Santa Cruz das Flores, staff costs represented 50.4% of total expenditure, while in Nordeste they represented only 15.5% in 2023. The regional average was 28.8%, below the national average of 31.1% (Fernandes et al., 2024, p. 149).

This is borne out by Rocha (2009, p. 13), who states that *"the local financial system is a deficit-ridden system, in which local authorities live in permanent difficulties, either because the revenues that are abstractly predicted do not generate the income that is expected of them, or because the expenses they incur are sometimes out of step with reality, exaggerated and without concern for their legal and financial appropriateness. Hence the constant dependence on aid from the central state, with the result that their financial autonomy is practically limited. In short, and in our opinion, financial autonomy is only a tendency."*

In other words, despite the independence and financial resources available to local authorities, a large part of their income is committed to current expenses, leaving little for the investments needed to improve the quality of life of their citizens.



## 6. Policies and recommendations to strengthen regional finances

Local authorities are directly dependent on the Government of the Republic, according to Law no. 27/96, of August 1, Article 5<sup>26</sup>, including those of the autonomous regions (art. 16): "[t]he *regime of this law shall apply to the Autonomous Regions, without prejudice to the publication of a statute defining the competent bodies for the exercise of administrative supervision.*"

Despite this, the Political-Administrative Statute of the Azores establishes, in Article 90(1)(g)<sup>27</sup> that one of the executive powers of the Regional Government is to "*exercise powers of supervision over local authorities*". Article 113 of the same Statute also states that the Regional Government "*may establish special coordination, collaboration or cooperation relations, including through the signing of agreements, with other public entities, namely the Autonomous Region of Madeira, the administrative regions and other local authorities or their associations, and that the rules governing the signing of cooperation agreements with the State shall apply, with the necessary adaptations.*"

However, these agreements are made on a case-by-case basis, and there is no common rule for the 19 local authorities in the Azores. In this regard, Regional Legislative Decree no. 5/2020/A of January 24<sup>28</sup> was adopted establishing the system of technical and financial cooperation between the regional administration and the local administration and is therefore specific and focused on very specific actions.

In addition, the local authorities in the Azores do not currently benefit from a policy of decentralisation of powers from the State. According to Law no. 50/2018 of August 16<sup>29</sup>, which establishes the framework for the transfer of powers to local authorities and intermunicipal entities, Article 9(1) states: "*The provisions of this law do not cover the powers and duties of the autonomous regions*" and Article 9(2) mentions that "*The transfer of powers and duties to local authorities in the Autonomous Regions of the Azores does not cover the powers and duties of the autonomous regions*". Article 9(2) mentions that "*The transfer of powers and competences to local authorities in the Autonomous Regions of the Azores and Madeira shall be regulated by a separate statute, on the legislative initiative of the respective legislative assemblies (...).*"

The fact is that to date, no concrete legislative initiative has been undertaken in the Azores on this matter, unlike most municipalities on the Portuguese mainland — despite the Association of Municipalities of the Autonomous Region of the Azores having already expressed its concern.<sup>30</sup>

In practice, it would be timely and appropriate to take advantage of the forthcoming revision of the Regional Finance Law to reinforce the financial resources of local authorities, while simultaneously attributing new competences to municipalities. This would give concrete effect to Article 67 of the current law<sup>31</sup>, which provides: "*[any] form of regional financial support to local authorities beyond that already provided for in the law must be aimed at strengthening the investment capacity of local authorities*".

By way of example, competences such as the management and maintenance of school buildings could be transferred to municipalities, especially given that primary education facilities are already largely managed locally. Other

<sup>26</sup>Administrative Guardianship Law. Law no. 27/96, of 1st August. Available at: [https://www.pgdlisboa.pt/leis/lei\\_mostra\\_articulado.php?nid=282&tabela=leis&so\\_miolo=](https://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=282&tabela=leis&so_miolo=). Accessed on: 8 may. 2025.

<sup>27</sup> Political and Administrative Statute of the Autonomous Region of the Azores. Law 39/80 of 5 August. Available at: [https://www.alra.pt/documentos/estatuto\\_pt.pdf](https://www.alra.pt/documentos/estatuto_pt.pdf). Accessed on: 6 may 2025.

<sup>28</sup> Technical and financial co-operation between the regional administration and the local administration. Regional Legislative Decree no. 5/2020/A, of 24 January. Regional Legislative Assembly of the Azores. Available at: [https://portal.azores.gov.pt/documents/2514154/16235774/Decreto+Legislativo+Regional+n.%C2%BA+5\\_2020\\_A.pdf/6b115156-1485-de46-8c66-36d2029e40a2?t=1727172194635](https://portal.azores.gov.pt/documents/2514154/16235774/Decreto+Legislativo+Regional+n.%C2%BA+5_2020_A.pdf/6b115156-1485-de46-8c66-36d2029e40a2?t=1727172194635). Accessed on: 6 may 2025.

<sup>29</sup> Framework Law on the transfer of competences to local authorities and intermunicipal entities. Law no. 50/2018, of 16 August. Available at: [https://www.pgdlisboa.pt/leis/lei\\_mostra\\_articulado.php?nid=2932&tabela=leis&ficha=1&pagina=1&so\\_miolo=S](https://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=2932&tabela=leis&ficha=1&pagina=1&so_miolo=S). Accessed on: 6 may 2025.

<sup>30</sup> Azorean municipalities want 'greater articulation' in housing supply. Açoriano Oriental newspaper, 4 April 2024. Available at: <https://www.acorianooriental.pt/noticia/municipios-acorianos-querem-maior-articulacao-na-oferta-de-habitacao-358941>. Accessed on: 8 may. 2025.

<sup>31</sup> Finance Law of the Autonomous Regions. Organic Law no. 2/2013, of 2 September. Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/lei-organica/2013-73431772>. Accessed on: 8 may. 2025.

possibilities include the management and maintenance of regional public roads, leisure areas, scenic viewpoints, and parts of the region's cultural heritage.

The advantages of decentralization are, according to Pinho (2012, p. 136): "*Proximity allows the municipality to assess the real scale of the problems and make a local adaptation of the responses to be given*" thus reinforcing the intention that local power has a more efficient and effective management. Rebelo de Sousa (1994/95) also states that "*Decentralization brings public administration closer to citizens, to local initiatives, as well as increasing social ties and fostering public sensitivity to citizens' problems and needs.*"

However, it is also essential to revisit the current Local Finance Law (Law no. 73/2013),<sup>32</sup> in force since 2013 — adopted during the period of financial assistance to Portugal by the Troika, which imposed austerity policies and strict limitations on municipal indebtedness.

To this end, the National Association of Municipalities (ANMP) has advocated for the approval of a new Local Finance Law, citing the complexity, outdatedness and incoherence of the current framework. Its proposal includes strengthening the financial capacity of municipalities through:

- An increase in the IRS municipal share from 5% to 10%;
- A progressive reformulation of the VAT share to 1.5% of the total national revenue from this tax;
- The assignment to municipalities of additional IMI (property tax) and IUC (single circulation tax) revenues;
- A 5% share of ISP (fuel tax);
- And a 10% share of the Environmental Fund's revenue, distributed according to performance in sustainability metrics.

Taking advantage of the current economic momentum in the Azores — where the tourism sector represents 17% of regional GDP, having grown by 57% since 2017<sup>33</sup> — municipalities should also create and strengthen municipal tourism taxes. In 2023, fifteen municipalities nationwide applied this tax, generating €70,197,911, or approximately 2.7% of total local revenue.<sup>34</sup> In the Azores, only the six municipalities on the island of São Miguel have announced that they will begin collecting this tax from January 1, 2025.<sup>35</sup>

Another complementary measure, particularly relevant in a regional context, would involve the charging of fees for public services in municipal tourist areas — such as entry to viewpoints, walking trails, or bathing areas. This would allow municipalities to finance the maintenance and conservation of these spaces while improving the visitor experience. At present, many of the region's most visited public places — including Caldeira Velha, or the ascent to Pico Mountain — are managed by the Regional Government and subject to access charges through the Azores Natural Parks. This model could be replicated at the municipal level, for spaces managed by local authorities.

While strengthening local financial autonomy and decentralisation is essential, these efforts cannot be considered in isolation. They must be understood within the broader framework of European economic governance, which imposes fiscal constraints and coordination obligations that directly affect local authorities. The following section examines how EU rules shape — and sometimes limit — the scope of local financial self-determination, particularly in contexts such as the Azores.

<sup>32</sup> Financial Regime of Local Authorities and Intermunicipal Entities. Law 73/2013, of 3 September 2013. Available at: <https://diariodarepublica.pt/dr/legislacao-consolidada/lei/2013-105795409-116088595>. Accessed on: 8 may. 2025.

<sup>33</sup> What is the macroeconomic impact of tourism in the Azores? Azores Tourism Summit 2024. Government of the Azores and EY Parthenon. Available at: [https://turismo.azores.gov.pt/wp-content/uploads/2024/11/EY\\_Impacto\\_Azores-Tourism-Summit-2024.pdf](https://turismo.azores.gov.pt/wp-content/uploads/2024/11/EY_Impacto_Azores-Tourism-Summit-2024.pdf). Accessed on: 6 may 2025.

<sup>34</sup> Financial Yearbook of Portuguese Municipalities 2023 - Presentation and main conclusions. Order of Certified Accountants. Available at: <https://www.occ.pt/pt-pt/noticias/apresentacao-do-anuario-financeiro-dos-municipios-portugueses-2023>. Accessed on: 6 may 2025.

<sup>35</sup> São Miguel municipalities to apply tourist tax from 1st January. Açoriano Oriental newspaper, 2 December 2024. Available at: <https://www.acorianooriental.pt/noticia/municipios-de-sao-miguel-vao-aplicar-taxa-turistica-a-partir-de-01-de-janeiro-365903>. Accessed on: 6 may 2025.

Finally, while decentralisation is often framed only in administrative terms, it must be distinguished from the broader principle of subsidiarity, as established under EU law (Article 5(3) of the Treaty on European Union). Subsidiarity emphasises that decisions should be taken at the level closest to citizens, unless better achieved at a higher level. A true reform of Azorean local governance should embrace this principle — not merely by delegating tasks, but by aligning resources, competences, and fiscal responsibility.

## 7. The Fiscal Responsibility of Local Authorities in the Context of European Union Economic Governance

Having analysed the local and regional situation, it is also worth analysing the integration of local authorities into the European Union (EU) framework, since this has required them to increasingly adapt to the rules of fiscal responsibility and budgetary discipline imposed by the treaties and the EU's economic governance.

The practical application of the principle of subsidiarity has been widely debated in academic literature. Hooghe and Marks (2003) argue that subsidiarity is often used strategically by member states to justify either recentralisation or selective decentralisation, rather than as a consistent framework for empowering local governance. Teles (2021) highlights that the lack of clear criteria for applying subsidiarity leads to uneven and incoherent multilevel governance, particularly in peripheral or insular regions such as the Azores. These critiques underscore the need to reconsider how EU-level principles align with regional realities.

This process is particularly relevant in the context of budgetary consolidation, financial transparency and compliance with the criteria of the Stability and Growth Pact (SGP). Although traditionally excluded from the main macroeconomic decisions, local authorities have become important players in implementing public policies that directly impact aggregate public finances (Barca & Vammalle, 2022).

With the 2008 financial crisis, and more recently with the effects of the COVID-19 pandemic, the EU has strengthened fiscal surveillance mechanisms, extending their reach to all levels of government. In this context, local authorities have become subject to stricter control mechanisms, including balanced budget rules and debt limits, which often condition their financial autonomy (OECD, 2023).

Regulation (EU) No 473/2013, which establishes common provisions for monitoring and evaluating the budgets of eurozone member states, includes the obligation to submit budget plans that also cover sub-national administrations. This reinforces the requirement for vertical coordination between the different levels of government, with a particular focus on local authorities (EUROPEAN COMMISSION, 2024).

In this framework, the fiscal responsibility of local authorities becomes not just a matter of administrative management, but a legal and political imperative imposed by EU law. This new paradigm poses increased challenges for local financial management, requiring more sophisticated technical skills and planning and monitoring mechanisms to ensure compliance with European objectives (Teles, 2021).

Despite these demands, the EU has also promoted mechanisms to support and incentivise good fiscal performance by municipalities, particularly through access to structural and investment funds. The Recovery and Resilience Facility (RRF), for example, represents an opportunity for municipalities to strengthen their investment capacity without jeopardising budgetary balances, provided they meet the agreed targets and reforms (EUROPEAN COURT OF AUDITORS, 2023).

In addition, good practices in local fiscal governance are encouraged by the EU Committee of the Regions, which promotes the sharing of experiences and continuous training in areas such as debt management, budgetary transparency, and the evaluation of financial performance (COMMITTEE OF THE REGIONS, 2023).

It is also important to consider the role of national and European courts of auditors in assessing the conformity and efficiency of public spending at local level. These institutions have strengthened their oversight of local authorities' financial acts, contributing to a culture of responsibility and accountability (COURT OF AUDITORS, 2022).

On a legal level, national constitutions and local finance laws have been adjusted to accommodate the new parameters imposed by European integration. In Portugal, for example, the Local Finance Law (Law 73/2013) already reflects a concern with budgetary consolidation and articulation with EU standards (Teles, 2021).

The current challenge is therefore to find a balance between the autonomy of local authorities — which is essential to the application of the principle of subsidiarity — and the need for budgetary discipline imposed by the European legal and economic order. While subsidiarity (as set out in Article 5(3) of the Treaty on European Union) affirms that decisions should be made at the level closest to citizens, this principle must now be interpreted alongside the supranational demands of economic coordination and fiscal sustainability. Achieving this balance requires effective multi-level governance, based on inter-institutional cooperation and the strengthening of local administrative capacity (Barca & Vammalle, 2022)

Despite the benefits of fiscal coordination at the EU level, applying the same budgetary rules across highly diverse regions can exacerbate structural inequalities. As Barca and Vammalle (2022) point out, one-size-fits-all fiscal rules often fail to account for geographic disadvantages, demographic dispersion, and higher service delivery costs in outermost regions. In the case of the Azores, rigid limits on deficit and debt may hinder the necessary investment in infrastructure, health, and education. A more flexible and asymmetry-sensitive application of EU fiscal rules would better support the Union's goals of territorial cohesion and balanced development.

Finally, it is essential that the European Union fosters a framework that acknowledges the unique role and limitations of local authorities, enabling them to deliver essential public services while upholding fiscal sustainability. The construction of a more cohesive and integrated Union depends largely on the strength, autonomy, and resilience of its local institutions.

## 5. Conclusion

To improve citizens' quality of life, local authorities increasingly adopt private-sector-inspired management models that focus on cost-efficiency, measurable results and resource optimisation. At the same time, citizens have become increasingly aware of the weight of their vote and, moving away from a passive stance, have begun to evaluate quality of services in relation to their cost — much like in ordinary commercial relationships. They have become conscious of their sovereignty as consumers of public goods (Bilhim, 2004, p. 42).

Today, local authorities in mainland Portugal have the power to make claims on the central government and the capacity to intervene like never before in the history of Portuguese municipalism. This wave of decentralization of responsibilities and funding to local authorities is clearly a positive aspect that deserves recognition (BILHIM, 2004, p.42).

However, the fact that the decentralization of competences is not yet a reality in the Azores is a reason for urgent action on this legitimate demand, already publicly expressed by the Association of Municipalities of the Autonomous Region of the Azores,<sup>36</sup> under penalty of losing the capacity to advocate on equal footing with mainland municipalities.

Added to this is the dependence on and budgetary constraints imposed by Law 73/2013, of September 3, which defines the financial regime for local authorities. In this regard, the concerns expressed by the National Association of Portuguese Municipalities (ANMP) should be highlighted, particularly its call for a new law, given that the current regime was enacted during Portugal's period of financial assistance under the Troika and continues to impose restrictive rules.

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<sup>36</sup>Azorean local authorities to benefit from 161M€ from the Azores 2030 Community Framework. RTP Açores. Available at: <https://acores.rtp.pt/local/autarquias-acorianas-vao-beneficiar-de-161me-do-quadro-comunitario-acores-2030/>. Accessed on: 8 may. 2025.

In short, given the relevance of revising the Regional Finance Law as defended by the current regional leaders,<sup>37</sup> and the urgency of adapting the decentralisation of competences to the regional context, it is in the interest of all — and particularly of citizens — that local authorities be granted greater financial autonomy. This must go hand in hand with the appropriate transfer of competences and, critically, the corresponding allocation of financial resources.<sup>38</sup>

As discussed throughout this study, decentralisation offers numerous advantages — not only in terms of the efficiency and effectiveness of local public policy implementation, but also in addressing a fundamental issue in Azorean local finances: the persistent dependence on transfers from the State Budget, which undermines the very autonomy enshrined in the Political-Administrative Statute of the Azores.

Furthermore, in the current European context, there is a growing demand for fiscal responsibility on the part of local authorities, promoted by the European Union's economic governance. The integration of municipalities and autonomous regions into the macroeconomic goals of the Member States, through budgetary rules and principles of financial discipline, requires municipalities to manage rigorously, transparently and in line with European objectives. This reality imposes additional challenges on local financial autonomy, requiring greater vertical coordination between levels of government and technical capacity building for local bodies.

It is therefore essential to rethink the legal and financial instruments available to local authorities, strengthening not only their autonomy but also their responsible integration into a multi-level governance model. The sustainability of local finances, in the light of European guidelines, should not be seen as a limitation on the actions of local authorities, but rather as an opportunity to consolidate a culture of effective public management, guided by principles of balance, transparency and proximity to citizens.

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<sup>37</sup> Regional Finance Law: Bolieiro says the State must look at Madeira and the Azores with more solidarity. RTP Açores. Available at: <https://acores.rtp.pt/politica/lei-das-financas-regionais-bolieiro-diz-que-o-estado-tem-de-olhar-a-madeira-e-os-acores-com-mais-solidariedade/>. Accessed on: 6 may 2025.

<sup>38</sup> Organic Law no. 2/2013, of September 2 (Autonomous Regions Finance Law). Available at: <https://diariodarepublica.pt/dr/detalhe/lei-organica/2-2013-499567>. Accessed on: 6 may 2025.

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