Country

Lisbon Portugal

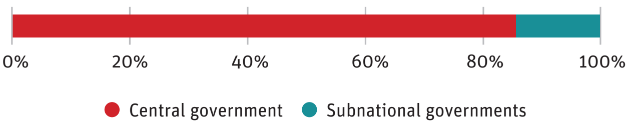
CITY:
0.5 mil. inhabitants

METROPOLITAN AREA
2.8 mil.
(-0.2% pop. change/5 years)

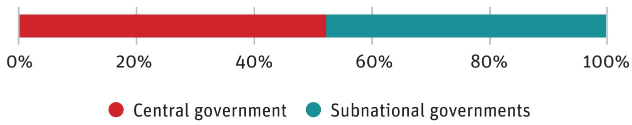
GDP: 100 % of the average EU28 GDP
(-1.7% average annual change in GDP/5 years)

How local public finance systems work in Portugal

PUBLIC REVENUE



CAPITAL EXPENDITURE



Portugal has a **three-tier system of subnational governments** (SNG) consisting of regions, municipalities and parishes. On the mainland of Portugal, however, the regional level does not exist; here only municipalities and parishes are used. The level of SNG in Portugal thus represents 308 municipalities (municipios), 3,091 parishes (freguesias) and two autonomous island regions. On mainland Portugal, there are 278 municipalities and 2,882 parishes, while in the Azores there are 19 municipalities and 155 parishes and on Madeira there are 11 municipalities and 54 parishes.

Fiscal arrangements are determined by the Portuguese constitution. Financial law reform in 2007 created the Municipal Social Fund (FSM) — with earmarks subsidies to finance specific expenditures in education, health and social care; at the same time, it provided municipalities up to a 5% share in the personal income tax. The local finance law from 2007 also simplified the intergovernmental system of transfers and reformed the municipal accounting system. The new local finance law from 2013 and an amendment in 2018 increased the transparency of the system, fiscal sustainability and individual accountability.

Subnational governments play a major role in public investment; they are responsible for 52% of all public investment (51% in OECD unitary states). However, public investment by SNGs accounts for just 0.8% of the GDP, (1.7% in OECD unitary states). SNGs in Portugal have been hit heavily by crises and between 2007 and 2017 their investment has decline by an average of 5% per year.

In 2016, government grants and transgers accounted for one-third of total SNG revenue (49% in OECD unitary states). The reform of public expenditures, beginning in 2019, will increase grants to municipalities by 1–1.2 billion, including a new municipal share in VAT revenue.

Tax revenue is a major source of income for regions and municipalities; taxes account for 41% of their revenue (39% in OECD unitary states). Nonetheless, tax revenue is relatively low and amounts to 2.5 % of GDP and 10% of public tax revenue (4% and 20% respectively in OECD unitary countries).

The two autonomous regions have a certain degree of autonomy; they retain nearly all national tax revenue collected in their territory, they set their tax rates (including VAT, personal income tax, corporate income tax, and excise tax) and can also introduce new taxes.

Municipal tax revenues include both shared and local taxes. Since 2007, municipalities have received a share of personal income taxes, with this share limited to a maximum of 5% of tax revenue, while municipalities may decide to reduce this percentage. Property tax is collected by municipalities each year on buildings and lands. To ensure the property tax had a more realistic basis, the cadastral value of 5 million properties was reassessed. **Property tax revenue makes up 32% of SNG tax revenue, 13% of total SNG revenue** and 0.8% of GDP (OECD 1.1%).

The 2013 local finance law abolished the real estate transaction tax, which had negatively contributed to the creation of extensive construction in the suburbs; this repeal, however, was never really implemented. The real estate transfer tax in 2016 accounted for 14%

of municipal tax revenue and 6% of total SNG revenue. Municipalities also collect a vehicle tax and a surcharge on corporate income tax (derrama). **Together, regional and municipal tax on personal income amounts to 0.4% of the GDP, 17.2% of SNG tax revenue and 7% of the total SNG revenue. Regional and municipal tax on corporate income accounts for 0.3% of the GDP, 10% of SNG tax revenue and 4.2% of total the SNG revenue. VAT accounts for 0.4% of the GDP, 15% of the SNG tax revenue and 6% of the total SNG revenue.**

The autonomous regions of the Azores and Madeira receive special transfers from the central government: lump-sumsubsidy, a regional cohesion fund, national co-funding with EU funding and a fund to finance common interest projects.

Transfers to municipalities from the central government correspond to 18.5% of the average revenue from three major taxes (the corporate income tax, personal income tax and VAT). These revenues are combined in the Financial Equilibrium Fund (FEF). The FEF is further divided into two funds: The General Municipal Fund (Fundo Geral Municipal, FGM) and the Municipal Cohesion Fund (Fundo de Coesáo Municipal, FCM). FGM funds are distributed based on population, area and other cost factors; their allocation takes into account the tax capacity of municipalities and the municipal index of social development. Other general subsidies fall under targeted grants from the Municipal Social Fund (Fundo Social Municipal, FSM).

Fees constitute 18% of the total SNG revenue (OECD 15%). **Property income in 2016 accounted for 3% of SNG revenue** (rent, sale of assets), which is higher than the OECD average (2% in 2016).

Source: http://www.oecd.org/cfe/regional-policy/Observatory-on- Subnational-Government-Finance-and-Investment.htm