



Administrative reforms and performance of local public policies

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Abstract

Purpose – The purpose of this paper is to clarify the relationship between administrative reform in Portugal and the impacts on the dependence of local governments in the face of budgetary resources of state and local municipal revenue collection, which is understood as a form, among others, participation civil society in local public policies.

Design/methodology/approach – The study opts for an exploratory analysis using the grounded theory approach, including the use of data relating to local government structures and partnerships with the private sector, based on the main lines of the public administration reform. The data were supplemented by documentary analysis, including legislative documents and papers in specialized area of administrative decentralization and civil society participation in local public policies.

Findings – The paper provides empirical insights about how the increased participation of civil society in local public policies is associated with less reliance on state budgets and a greater number of local managerial structures.

Research limitations/implications – Due to the chosen research approach, the results cannot be generalized. A comparative study between several countries could bring several interesting insights.

Social implications – The paper includes implications for economic and social development of new public policies in the context of administrative reforms.

Originality/value – This paper makes several theoretical and empirical contributions on this research field specially about local public manager's decisions for financial resources transfers within the active policy of sustainable local development.

Keywords Public policy, Portugal, Public sector management, Decentralization, Public sector reform

Paper type Research paper

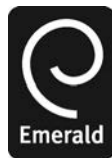
1. Introduction

This study analyses the administrative reforms impact and the public policies decentralization, particularly on the Portuguese municipalities' dependence on financial transfers from the central government budget (municipal funds) and the ability to collect local municipal revenue.

These reforms have sought to approximate the interior regions (most deprived) to the coastal regions of the country (most favored), by relocation of municipal funds.

The relevance of this issue stems from the fact that, although the principle of solidarity led to public policies that tend, according to Hertzog (1991), Hoffmann-Martinot (1992) and Debbasch (1976), to shift financial resources from more developed regions to the most deprived, the collection level of local municipal revenue is a form of civil society participation in local public policies that contributes to the financial sustainability of local public administration. However, this study shows that these reallocations did not improve the development on the affected regions.

Based on the Portuguese public administration reform started in 1974, we opted for a combination of literature review and exploratory research, crossing a theoretical



approach, seeking to understand the scientific contributions on the issue at hand, with the use of survey data for Portuguese municipalities, providing information on the relationship between municipal funds and local municipal revenues.

The municipal data were collected from official statistics, enriched by document analysis with legislative documentation, specialized articles about decentralization of public policies and on civil society participation in local public policies, seeking a good relationship between theory and practice.

Since the connection between the municipal funds and the participation of citizens in municipal management has not been discussed in national technical studies, we use exploratory research to present a view on the issue.

This document starts by presenting the theoretical background (Section 2), followed by the methodology (Section 3), results analysis and conclusions (Section 4) and suggestions for future investigation (Section 5).

2. Theoretical background

2.1 *Public administration reform*

Portuguese municipalities are traditionally presented as having jurisdiction tied to a certain land area, local development policy should be based on a process of interdependence and cooperation between central government, local communities, private sector, civil society and development agencies, as suggested by Crook and Manor (2000). Overall, these reforms seek to improve local policies performance that, according to Lamaury (2009), depend on several issues among which are financial support decisions and, according to Bouvier (2009), local finances sustainability is a limiting factor on their success.

This led to the creation of municipal associations and the local public enterprise sector with different objectives presented ahead.

2.1.1 Municipal associations. Municipal associations are understood by Amaral (2003) as public collective persons, connected to two or more municipalities, in order to carry out specific common interests and inter-municipal development. They serve broader area than municipalities they benefit from scale economy effects, allocating local resources more efficiently. In 1991, there were 35 municipal associations, mostly multi-purpose, and since then their number has not stopped growing.

Areas of intervention encompass water supply, sewage treatment, town planning, etc. Their own legal status provides them executive autonomy from their constituent local municipalities, since only projects and activities assigned and financed by the municipalities associated can be executed. The financial support given by each municipality for a project or activity is proportional to the benefit expected for the citizens served by that municipality.

In order to reduce local and regional inequalities the framework laws of metropolitan areas (AM), of Lisbon (AM Lisboa) and of Oporto (AM Porto), and the framework laws of inter-municipal communities were published in 2003 and revised in 2008. This enabled the creation of new forms of territorial organization, sharing characteristics with municipal associations, filling the lack of an intermediate government level between the central government and municipalities. In our view such entities can only replace the intermediate government level if they are assigned with powers in order to have an active role in the economic development, able to stop the exodus trend of people to larger population centers, as presented by Lobo (1989).

Metropolitan areas have several goals such as planning, investment programs, economic/social/environment development, participation in partnerships between

central government, local government, public enterprises and other entities in the definition of the area development plans (e.g. transportation, water distribution, electricity, etc.).

The legal regime for municipal associations distinguishes municipal associations as public collective persons (inter-municipal communities CIM), with multiple common goals and municipal associations as private collective persons (specific goals inter-municipal association AMFE), and created to carry out specific purposes of the municipalities connected to them. The last type cannot have profit-oriented goals, unlike other private entities, yet its operating costs should be completely supported by their revenue.

Despite criticism that may merit this type of association, the benefits from its implementation should be highlighted: a new decentralization process thrust, promoting scale economies in the management of public resources when the municipal financing scheme reveals weaknesses in the response required by their citizens as presented by Santos (1999) while studying the globalization effect on national economies. The access to information leads to new needs created through observation of new services and goods available on other communities, for example road access, computer equipments, internet access and support infrastructures.

2.1.2 Local public enterprise sector. Framework laws of 1998 and 2006 regulated the creation of municipal, inter-municipal and regional enterprises that defined the local public enterprise sector (SEL).

These enterprises are organizations that have a legal identity separate from the municipality, although subject to the supervision of its executive body. These enterprises manage municipal activities such as water distribution, sanitation and municipal transport systems.

Their creation has been done at a very fast pace, according to the Inspeção-Geral de Finanças, at 1999 there were 34 municipal and inter-municipal companies. At 2011, that number was 206, according to data from Direção-Geral das Autarquias Locais (DGAL).

This strong growth is driven by the tendency to avoid the constraints of regulations on financial management of public services, according to Amorim (2000), using tools and forms of private law to pursue their respective roles.

The current legal regime covers municipal, inter-municipal and metropolitan enterprises, as enterprises under commercial law, in which municipalities, municipal associations and metropolitan areas may exercise a dominant influence since they hold most of the capital, voting rights or the right to appoint/remove a majority of the management/supervision members.

With the need to comply with the requirements arising from global markets and especially in the European context, a set of financial rules are defined to the SEL entities, requiring rigorous financial management and positive results, under the threat of the participating municipalities being held accountable to cover the recorded deficits.

The model aims to disallow the creation of local public enterprises in order to escape legal budgetary control and the limitations of local debt or economical escape, represented by the privatization of public services without proper business support.

With these entities belonging to SEL cannot have purely administrative activities, which should be pursued by the traditional legal instruments, under penalty of inefficiency and therefore harmful to social welfare. Municipalities are usually better equipped to answer problems of that nature, due to their closer proximity and direct participation mechanisms accessible to their citizens.

2.2 Decentralization and participation

Assuming that any reform of public administration has the ultimate goal to eliminate or reduce dysfunctions, decentralization according to Carneiro (2003) and Corte-Real (2003), stands out as an essential process that seeks to answer the growing needs of society through the distribution of responsibilities between levels of administration.

As Fukuyama (2006) states, there is an optimal degree of decentralization, since the (un)success of this process is largely dependent on a complex series of technological and social factors, and particularly the institutional capacity of each country to stimulate economic growth with greater civic participation and democratic control.

Among other structural reasons, which preceded the many initiatives for reform and modernization of public administration in Europe after the 1970s, according to Mozzicafreddo (2001) is the share of governmental expenditure, primarily resulting from increased investment on social policies and, at the macro level, the introduction of new public management policies that promote economy and the quality of public expenditure.

In this sense the weight of public expenditure and financial responsibilities of different administrative levels is important in the context of administrative reform, since public decisions have to take in account the cost-efficiency ratio on the application of available resources by the local governments and entities created by them (AM, CIM, ANFE and SEL).

Thus, local government with real responsibilities in the management of local interests give expression, at different administrative levels of the State, to the participation of citizens in democratic processes and, as Martins (2001) argues, allow a closer and more efficient public management to pursue the welfare of citizens.

Through municipalities, AM, CIM, ANFE and SEL, citizens exercise their right of participation in public administration, as referred by Crook (2003), administrative decentralization leads to the creation of participation and control mechanisms used by the citizens in order to influence public policies.

Montalvo (2007) emphasizes the role of citizen participation on the municipal budget in financial resources allocation decisions, particularly on investments defined as priority (housing, social welfare and infrastructure), especially as a process of intervention by citizens in municipal management and promotion of political and social development as a way to revitalize democracy at a local level.

In Portugal this is an unusual form of citizen participation in public administration, that emphasis the selection of public investment by citizens, private enterprises, social institutions and other community participative associations. We think this kind of participation is important as it would allow combining the participatory democracy with the representative democracy. However, the optimization of this combination is always dependent on the financial sustainability of the chosen solutions, which in turn depends on the capacity of those being financed by the participant citizens.

Though due to large disparities between regions, as presented by Carvalho (1996) in the Portuguese case, this may lead to public expenditure choices whose financing oversteps the resources available on municipalities involved and require funds transfers from richer municipalities. These transfers reach such dimension that may lead to financial instability even on the richer regions, requiring the deactivation of public services and infrastructures.

Portugal taxes redistribution on local finances law is supported by income taxes and VAT, through attribution of funds to municipalities by the central government. In the last years, the criterion has set the growth of the richer municipalities to negative

percentages in order to keep some growth on the poor municipalities. This is a central government intervention to correct the perverse effects of decentralization through financial equalization mechanisms, which support the calculation of financial transfers from central government to local government.

With regards specifically to the financial aspects, the principle of solidarity led to public policies that, according to Hertzog (1991), Hoffmann-Martinot (1992) and Debbasch (1976), shift financial resources from more developed regions to the most deprived.

Rocha (2009) places the spotlight on the autonomy through the local assets and resources, in which are accounted the municipal local revenues as a form of direct participation of the citizens on public management as well as the financial transfers from central government.

Nabais (2007) and Zbyszewski (2006) defend that autonomy must be seen from the perspective of municipal powers controlling the revenue and expenses, as described by Moreira (2003) and Franco (1992), in terms of providing conditions for the creation, settlement and collection of the revenue and taking on commitments to third parties, settlement and payment of the expenses, in our understanding, wider and closer approach to reality of democratic societies.

So it is justified to analyze the ability to generate its own income and to obtain resources through transfers from central government, as the main sources of municipal funding, those directly contribute to local financial autonomy and are therefore, as presented by Matias (1987), without neglecting financial sustainability required on the local level decisions taken to answer citizens needs.

Since Portugal is currently under financial aid, the sustainability issue has special impact on the national debt and on local administration debt management, pressured by the financial deficits of AM, CIM, ANFE and SEL structures.

2.3 Sustainability of local public policies

The regional disparities reductions, development promotion and national cohesion reinforcement underlie the equalization phenomenon, embodied in financial transfers from central government to local municipal administration. These transfers can be subdivided into two main components: from central government budget are vertical redistribution; between municipalities is horizontal redistribution. In order to support its activities, municipalities also can charge fees or taxes over the goods and services provided, collect real estate taxes and borrow from financial institutions within certain limits.

As the ability to collect local revenues differs between municipalities, the law stipulates the execution of larger financial transfers to municipalities with less collection ability and reduction of financial transfers to the remaining municipalities seeking to assure sustainability of municipal finances, understood has the ability to fulfill the financial needs of the their activities.

First, through the creation of decentralized government structures (AM, CIM, ANFE and SEL) leading to a public management closer to its citizens through the election of municipality representatives and direct participation on municipal activities. In fact, the meetings of municipal councils are open to the public, budgets and investment plans are available for consultation by the public.

The participation of citizens in these activities requires their responsibility, ensuring that financial support for those choices is sustainable and choosing the best cost-benefit solutions. In this perspective the financial support diversification of

choices should be considered, taking in account the autonomy of municipalities, so that expenses do not become a burden for future generations.

Since AM, CIM, ANFE and SEL entities are created through municipalities involved, their debts have to respect the debt limits of each municipality after taking in consideration the size of municipality involved. If the debt limits are not kept, next year financial transfers have penalties, requiring the increase of local revenues cover expenses.

As presented by Mozzicafreddo *et al.* (1991) and Leibfried and Zürn (2005), decentralization as a process of change territorial organization of the State, establishes the transfer of responsibilities to entities independent from the central government, with autonomous decision powers and highlight on financial resources management.

At the municipal level that is under analysis, in an evolutionary process of interdependence and cooperation, between a centralized administrative organization and decision makers closer to the people, justifying the creation of different types of entities with different powers on the local and regional levels seeking to improve the performance of public decentralization policies of government structures, as indicated by Manor (2011).

The size of the municipal associations, metropolitan associations and public municipal enterprises also appears, at least partly, as result from the inability of each municipality by itself not having the ability to answer the challenges imposed on the 1960s and 1970s, mainly due to reasons of economic rationality, in response to the satisfaction of needs that go beyond the local nature that characterized them so far according to Oliveira (1993) and Nogueira (2001).

Such phenomena have affected territorial organization, as referred by Condesso (2005), leading to new ways of adapting old structures of local administration to the problems affecting needs that clearly exceed municipal dimension, requiring the collaboration between municipalities.

The transfers from central to local government of municipal funds are defined seeking to ensure, according to Guengant (1993) a minimum level of provision of specific goods or public services throughout the national territory (matching grants) and are translated, according to Anderson (1994) and Dahlby and Wilson (1994), on specific grants to local government entities that provide goods that generate inter-jurisdictional externalities (spillovers).

The justification of this transfers gains importance with regard to the criteria of territorial equity, questioned by Manor (2002) to the extent that schemes decentralized democracy can actually lead to unequal treatment of people involved in them. In the case of water distribution, the inequality in the funds transfers leads to highly different local prices charged for the water used by its citizens (e.g. between Castelo Branco and Torres Vedras municipalities). These criteria incorporate variables related to the participation of local government in tax revenue redistribution by these, present in most European Union countries, where the population and area indicators have greater weight.

The financial equalization system seeks to minimize the effects of fiscal disparities among municipalities (horizontal balance), which may result from different costs of providing local goods and services and unequal access to resources, and also seeks to promote the resource sharing and efficient allocation of resources goals.

These operations should have in consideration costs steaming from administrative decentralization, otherwise, the new structures are unable to pay on time their

operational costs, which leads us to the need of support from local revenue to complement funds transfers from central government.

3. Methodology

3.1 Data and information sources

To identify the nature of the relationship between the financial equalization transfers from central government and local revenues, we selected a set of variables of the Portuguese municipalities' financial activity in 2007, which were obtained from the DGAL.

The total municipal funds are the financial transfers from central government budget to municipalities and local revenues are municipal taxes, fees, fines and other penalties and from the sale of municipal goods and services.

Taking into account the territorial division of municipalities, on the appendix to this study, the presented view refers to the importance assumed by such variables, municipal funds and local revenue in relation to the respective citizens.

We used information provided by the Instituto Nacional de Estatística (INE) for the latest census available and by the Instituto Geográfico e Cadastral (IGP) regarding the administrative divisions in Portugal.

3.2 Data processing

The amounts per capita of the variables referred above are shown on maps with the administrative division at the municipal level for per capita municipal funds and per capita local revenue in 2007 (Figures 1 and 2), highlight the relation between citizens' benefits and efforts for different municipalities.

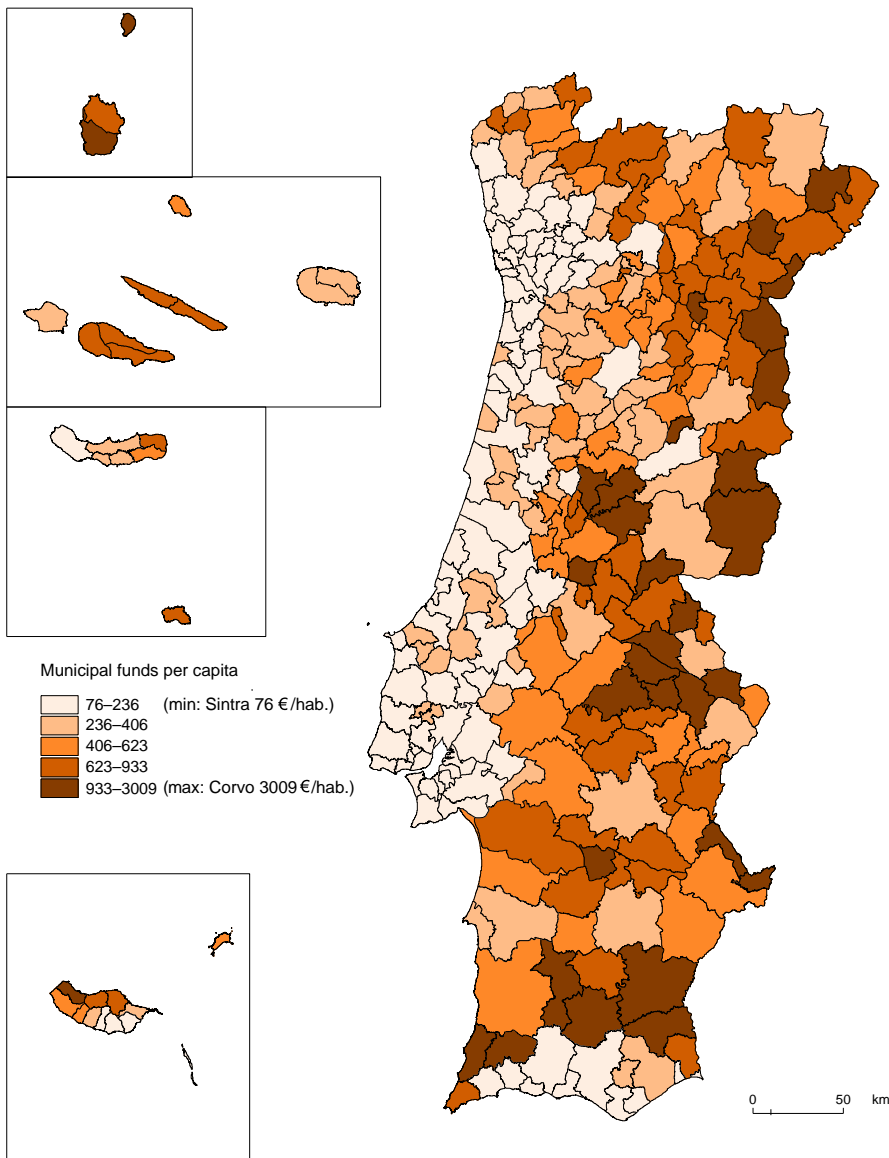
The division by classes, identified on the maps, takes into account the method of natural intervals, closed on the right and open on the left, except in first class, where the intervals are both considered closed. The ranking takes into account natural breaks through the Jenks (1967) optimization method, which forms internally homogeneous classes and ensures the heterogeneity between classes, minimizing the variance within each class.

As confirmed by the information gathered in Figures 1 and 2, the municipalities with greater dependence on intergovernmental transfers (per capita municipal funds) have usually a very low level of per capita local revenue.

The availability of a high amount of municipal funds per capita can limit the effort to increase their local revenues and thus minimize the control by the voters on the management quality and of the level of municipal performance, with possible adverse effects, particularly on the local adoption of best practices in local governance. We would like to highlight that the municipal budget execution levels are around 70 percent since 1979 (according to data from DGAL), percentage reflected on the local debt levels and delayed payment of expenditures.

A weak systemic financial contribution of the respective citizens in the seat of municipal finance activity tends to be accompanied by a weak control of local public policies, with results perhaps less favorable in terms of future financial sustainability.

Furthermore, it is interesting to relate the information to the depopulation of the countryside studied by authors, such as Pereira (1998) and Chorincas (2003), on regional dynamics in Portugal. Pointing to the fact that municipal entities with strong population growth are concentrated in the coastal strip or in some regions of the country (medium-sized urban centers) and, leading to a low growth or even severe loss



Sources: INE, DGAL and IGP, Official Administrative Map of Portugal (CAOP 2009.0)

Figure 1.
Municipal funds
per capita (2007)

in some cases of their actual population on the country's interior. This issue, according to INE census data, continues to deteriorate pressuring the sustainability of local finances, leading also to poor usage of new infrastructures on the interior of the country built to counter this exodus.

In this confrontation we are led to believe that the central government budget transfers to municipalities of the interior, although being much more significant than to

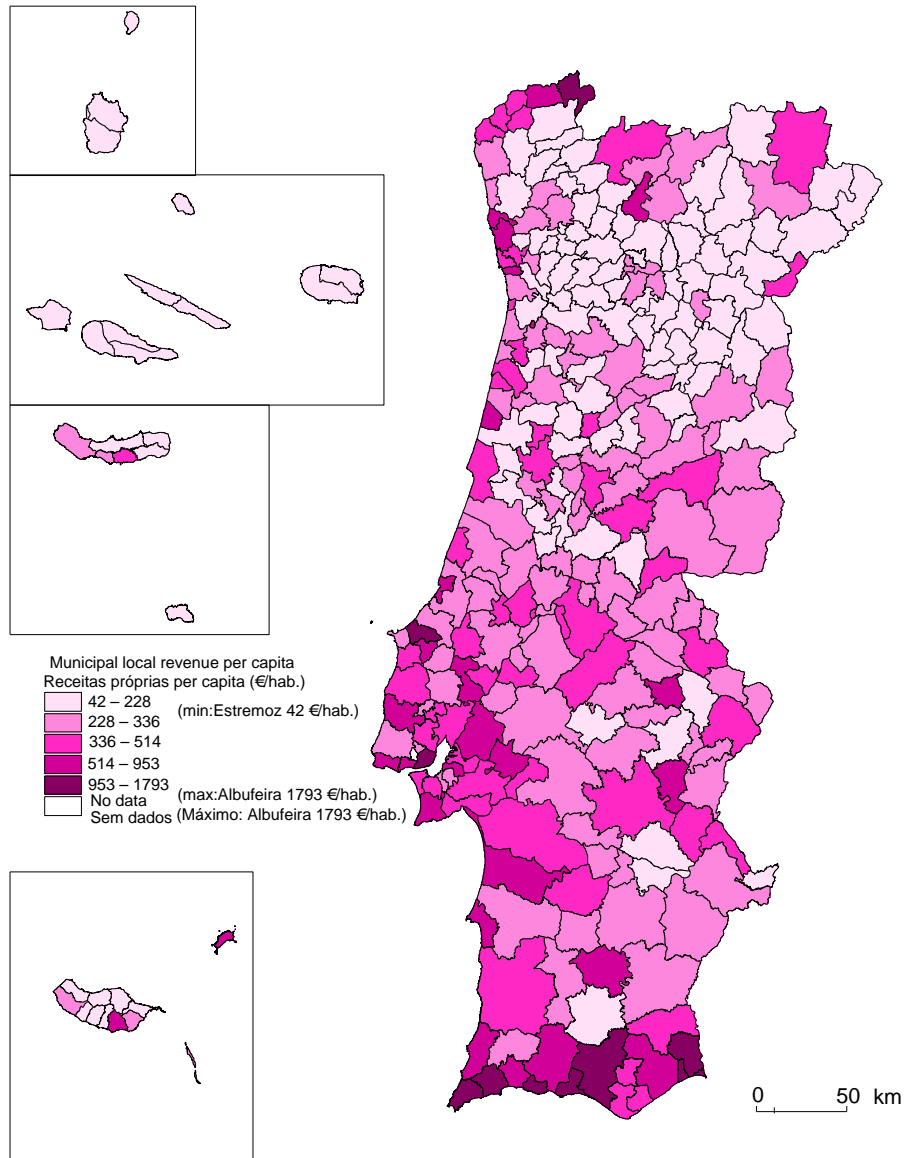


Figure 2.
Municipal local revenues
per capita (2007)

Sources: INE, DGAL and IGP, Official Administrative Map of Portugal (CAOP 2009.0)

coastal and urban areas, do not sustained economic growth or increase employment for the most disadvantaged citizens, which continue to move to regions with greater capacity to generate resources.

4. Main results and conclusions

The reform and modernization of public administration as an instrument of governance, mentioned by Cheema and Rondinelli (2007), seeks to connect the

decentralization process associated with greater civic participation that stimulates economic growth.

In the Portuguese case, the large disparities between regions required financial equalization mechanisms, which support the calculation of financial transfers to local administration redistributive objectives and efficiency concerns on the allocation of local resources. Promoting the reduction of regional asymmetries and leading to an evolutionary process of interdependence and cooperation between a centralized management and decision makers closer to the citizen. In addition to central government and local government, cooperation includes decentralized public entities that go beyond municipal borders, created by municipalities and of different municipal associations' types, metropolitan areas and public enterprises.

Private companies and organizations of social character are active participants in the municipal administration as they create jobs, contribute to economic and social development and influence choices of local public expenditures.

Despite all the reform process developed an inverse ratio between the municipalities' ability to collect local resources and dependence on transfers from central government budget continues to persist.

Public administration reform seeking to encourage local population financial participation in activities undertaken by decentralized administration led to an increase on local revenue collection and on the number municipal activities, but also on the municipal budget pressure when local revenue collection falls below the expected values for the year, aggravated by the current international crisis scenario. With this in mind, positive discrimination established in the municipal funds allocation to local administration has not proved effective at increasing the civil society level participation in local public policies.

Spatial evolution is partly demonstrative of the inability of municipal activity alone to reverse the exodus pattern from the interior to the coast and major population centers, which is expected because this phenomenon depends on other factors.

5. Limitations and futures research

The results of this study are important for the development of new policies in the scope of reform action of the State, especially regarding local finances reforms supported by the Local Autonomy European Union Charter. We are dealing with public local entities that, according to national expert literature, present a deficit at the collection of local revenues and are largely based on the performance of municipal expenditures. Recent legislative changes had no impact on this issue, a situation that should be analyzed in future research.

Analysis of administrative reforms, decentralization and good governance practices can be improved with the research of new variables, with focus on public resources redistribution taking in account civil society financial participation in local government decisions.

In the scientific field, the issue of financial sustainability of municipal public policies would gain if the municipal funds and local revenues were crossed with the analysis of municipal debt levels. As it may lead to an analysis in the field of equitable cost distribution associated with sustainable municipal policies development.

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Further reading

Local Finance in the Twenty Five Countries of the European Union (2004), Dexia Editions, Paris.

Appendix

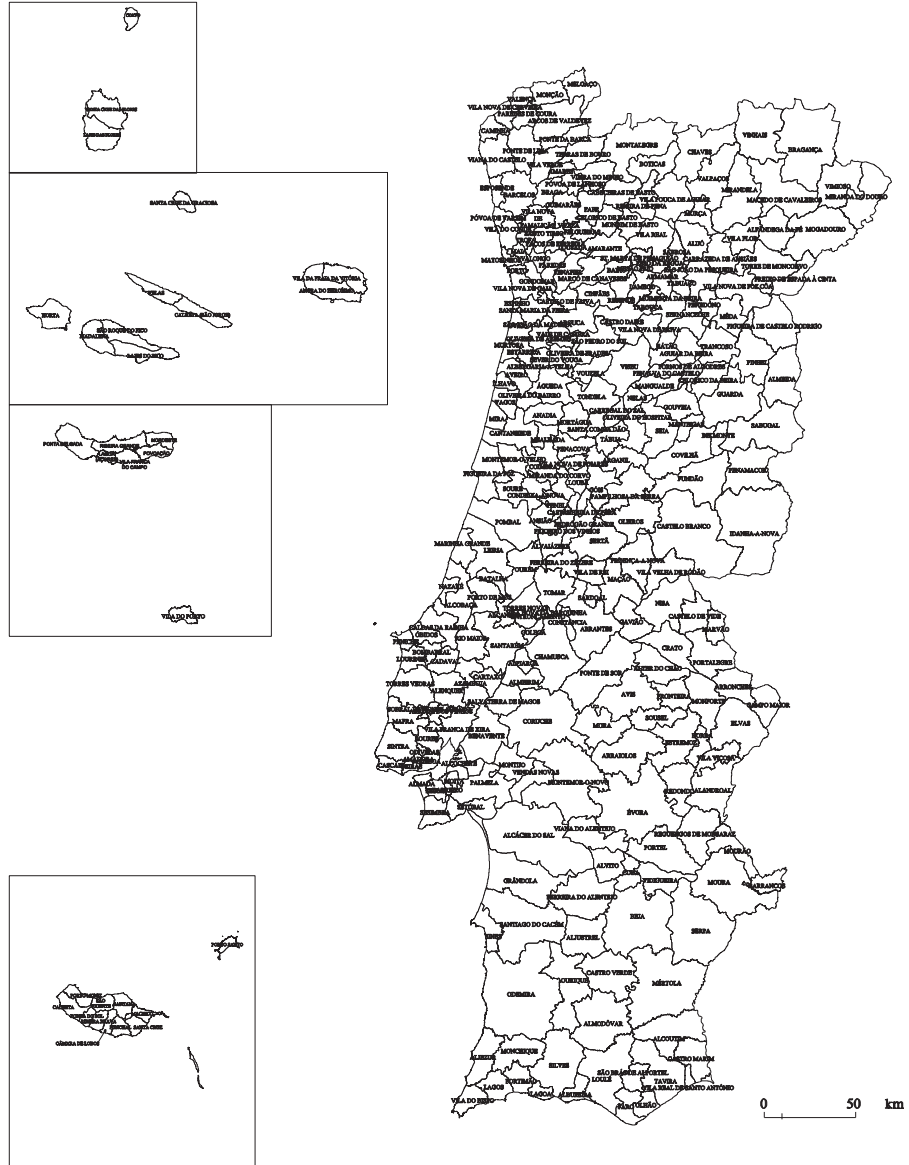


Figure A1.
Administrative divisions
by municipality (2011)

Sources: IGP, Official Administrative Map of Portugal (CAOP 2009.0)

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