

**LOCAL GOVERNMENT ORGANIZATION
AND FINANCE IN FRANCE¹**

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I – Introduction

There are currently at least four levels of government in France: the central government, regions, *départements*, and communes. One could add two other semi or quasi levels of government: the European Union, and groupings of communes. These institutions also have taxing, spending, borrowing and regulatory powers. However, groupings of communes, as their name indicate, do not have directly elected councils, and can be seen as creatures of communes. Similarly, the European Union can be said to be a creature of member governments. The powerful decision-making body in the Union is the council of ministers of member countries, meeting periodically in Brussels, not the directly elected European Parliament (which has only a consultative voice), nor the permanent European Commission. This paper will focus on the role, function and finance of the three sub-national governments: regions, *départements* and communes.

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Jurisdictions

Communes and *départements* date back to the French Revolution. The list and maps of communes and *départements* has not changed much since 1790. There are nearly 37,000 communes, and they were patterned after pre-revolutionary catholic parishes. Over the past two centuries, no new commune has been created, and only a few communes have merged, in spite of government efforts to induce such mergers. Close to 100 *départements* were created anew, to replace former Old Regime provinces. They all had roughly the same size (about 5,000 km²), which was said to be such that one could horse ride to the departmental seat in a day from any part of the jurisdiction. Some *départements* changed name over the course of time, a few additional *départements* were created in the Paris region in the 1950ies, former colonies or overseas territories (La Réunion, Martinique, Guadeloupe, Guyanne) were transformed into *départements* in the post World war II period, but these changes were minor. Paris is at the same time a commune and a *département*. For both communes and *départementst*, there is a worrying vocabulary ambiguity: a commune (or for that matter a *département*) is at the same time a geographical area, and the local government that administers it. In this paper, we will mostly use these words to designate the local governments, although in some cases, hopefully clearly indicated by the context, they might also designate the arezas.

In population terms, however, changes have been very substantial. Massive rural to urban migration, then suburban developments, led to a dramatic decline of the population of some communes (there are even communes with no permanent residing population any longer), and, combined with total population increase, to equally dramatic increases in the population of other communes. The same is true of

départements. The net result is that there are immense disparities between the population size or density of communes and *départements*, as shown in Table 1.

Table 1 – Area and Population Size of French *Départements*, Communes and Regions, 2002

	Communes	<i>Départements</i>	Regions
Number		96	22
Area size (km ²)			
Average	15	5,700	24,700
Median	11	5,900	25,700
Standard error	15	1,900	11,200
Minimum	□	105	8,300
Maximum	758	10,000	45,300
Dispersion coefficient	1.00	0.34	0.45
Population size (1000)			
Average	1.6	610	2,660
Median	0.2	503	2,080
Standard error	13.9	466	2,240
Minimum	-	74	260
Maximum	2,130 ^a	2,560	10,950
Dispersion coefficient	8.7	0.76	0.84

Sources and notes : Calculated by Bernard-Henri Nicot (SIRIUS, Univ. Paris XII). Excluding overseas communes, *départements* and regions. ^aParis, which is at the same time a commune and a *département*.

Regions are much more recent in France. They appeared in the 1960ies as administrative jurisdictions, with partly elected partly appointed consultative bodies, gained authority, and became full-fledged sub-national governments in 1982. There are 22 metropolitan regions (including Corsica), plus 4 overseas regions. They are very diverse in size and population.

Because communes are many and small, there is an obvious need for them to get together in one form or another. For many decades, the central government has tried to encourage mergers of communes: it has not met with much success. In the 1960ies, it created *communautés urbaines*, a form of metropolitan government in which the communes of an urban agglomeration jointly manage a number of urban public services, and levy taxes. This was made compulsory for four large agglomerations (Lyon, Strasbourg, Bordeaux, Lille)¹ and optional for other—but only nine additional

¹ And also for Le Creusot, a much smaller agglomeration.

agglomerations agreed to create *communautés urbaines*. Presently, the 14 *communautés urbaines* regroup 355 communes and 6.2 million inhabitants.

A more popular, and much softer, form of communal cooperation has consisted of “syndicates”, created either for one specific function, such as garbage collection or water supply or for several functions. There are about 15,000 one-purpose and 3,000 multi-purpose syndicates. They are financed by negotiated contributions from member communes. In the area of urban transportation, about 150 “organizing authorities” have been created; they benefit from a special and important tax.

In recent years, the central government has encouraged (through specific subsidies) communes to create *communautés d’agglomérations* in urban areas, and *communautés de communes* in more rural areas. Presently, there are more than 150 *communautés d’agglomérations* regrouping nearly 3,000 communes and 20 million inhabitants, and more than 2,000 *communautés de communes* regrouping 28,000 communes and 25 million inhabitants.

Economic Weight

How important are local governments in France ? Table 2 presents a quantitative approach to this question, based on national accounts data for 2002. National accounts data, prepared by economists, is more meaningful than public finance accounts data, prepared by accountants. In particular, national accounts data take into account income and expenditures of local governments “satellites”, that is entities formally and financially distinct from local governments but in practice controlled by them; it also “consolidates” intergovernmental transfers in order to avoid double-counting of income or expenditures. On the other hand, public finance data is more detailed than national accounts data.

Table 2 – Income and Expenditures of French Local Governments, 2002

	In G ^a euros	In % of GDP	in % of central government
Total expenditures	153	10.1	43.6
Intermediate consumption	34	2.4	170.0
Wages	46	3.0	43.0
Interest on debt	6	0.4	15.8
Services and transfers	32	2.1	18.0
Investment	33	2.2	471.4
Total income	156	10.3	53.2
Taxes	76	5.0	28.3
Other (incl. transfers)	80	5.3	333.3
Balance	+3	0.2	-

Source : National Accounts 2002 ; ^aG = giga = billion = 10⁹

Several important points emerge from this table. First, sub-national government income and expenditures represent about 10% of GDP in France. Second, in money terms, the weight of local governments is about half that of the central government¹. Third, local taxes cover about half local government expenditures, and represent therefore about 5% of GDP. Fourth, as a consequence, transfers from the central government to local governments account for about 5% of GDP and cover the other half of local government resources. Fifth, in public investment terms, local governments weight about 5 times as much as the central government. Finally, in 2002 at least, local governments ran a surplus; and their indebtedness (as measured by interests paid on debt) was only one sixth of central government indebtedness.

What is the relative importance of communes, *départements* and regions ? Table 3 provides an answer in terms of expenditures (but data on income tells exactly the same story) for 2001.

¹ In France, what is known as social security, which includes medical insurance, pensions, unemployment allowances, and maternity allowances, and which weights about as much as the central government, is not considered part of the central government.

Table 3 – Expenditures of Communes, *Départements* and Regions, France, 2001

	(G euros)	(% of total)
Communes	108.3	67.1
of which groupings of communes	31.3	18.4
<i>Départements</i>	39.2	24.3
Regions	13.7	8.5
Total, local governments	161.3	67.1

Source : DGC, using public finance accounting concepts.

It appears that the picture is largely dominated by communes, that account for two-thirds of total local governments expenditures. *Départements* account for about one fourth, and regions, although their importance is increasing fastest, still represent less than one tenth of the total. The role of groupings of communes, as entities formally (although not politically) independent of communes, is large, and is also increasing rapidly.

Governance

Communal (also called municipal) councils are elected every six years. People vote for lists, but the list that comes first benefits from a “premium” that gives it a majority in the council. The council elects one of its members —the leader of the winning list— as its chairman or mayor. This means that there are no post-election negotiations to form a council majority, and that there is no possibility of a conflict between the mayor and the council either. A mayor can run for mayorship as many times as he/she wants. Two consecutive mandates (12 years) are quite frequent, three mandates (18 years) are not uncommon, and some mayors have even stayed in office for four (and in exceptional cases five) mandates. Mayors are very well known, and usually command respect and popularity (many people would say: “all politicians are bad, except for my mayor”). In that sense, communes are indeed a pillar of democracy in France.

Communal groupings, by contrast, have a weak legitimacy. Their governing boards are not elected, but appointed by the (elected) mayors of the constituting communes. This is even the case when they have the power to levy taxes.

For electoral purposes, *départements* are divided into 20-30 jurisdictions, and each jurisdiction sends one member to the council for six years. Every three years, half the seats are up for re-election. The council elects one chairman amongst its members. Every three years, depending upon possible changes in the council majority, a new chairman can be elected, so as to rule out potential conflicts between a council chairman and a council majority. Here again, there are no limits on the re-election of council members or chairmen.

The electoral system for regions is now similar to that of communes. Elections are held every six years, by party lists, with a premium to the winning list, so as to ensure a clear majority in the regional council. The council elects the leader of the winning list as chairman.

For long, it was possible and in practice quite common for a politician to hold simultaneously several electoral mandates. One could at the same time be the mayor of a commune, a member (or chairman) of a département council and a member of the national assembly or of the senate, and a member of the European Parliament, or even a cabinet member. This had the advantage of giving national politicians some experience of local government problems¹, as well as obvious disadvantages. It has been restricted, however, and now a person is not allowed to have more than two electoral mandates at

¹ A more contingent reason for a locally elected politician to seek a national mandate was financial ; being a mayor is a full time job not very well paid whereas being a member of Parliament is a not so full time job very well paid.

the same time. Most members of the national assembly and of the senate, however, are also elected in a sub-national government council.

Communes and *départements* have always enjoyed a fair degree of formal autonomy. They have had elected councils, their own taxes, borrowing powers, and municipal or departmental employees¹. The central government never had the power to remove a council chairman that was not of its liking. But it is true that, at the same time, the central government imposed many constraints and exerted many controls over communes and *départements*. This was facilitated by the spatial organization of the central government, which was —and still is— patterned after the *departmental* structure. In every *département* (in the area corresponding to every *département*), there is a representative of the ministry of Interior, the prefect (who is appointed by the central government), and a representative of each of the central government ministries (equally appointed by the relevant ministry). There is for instance a representative of the ministry of Equipment (transportation, urban development, housing), or of the ministry of Agriculture.

Tax rates, for instance, were free between limits, and there was a fixed link between the rates imposed on the various local taxes. For a long time, even in the post World War II period, communes and *départements* needed a central government authorization to increase the fees charged on various services they provided. Similarly, an authorization was needed to borrow, and anyway a central government controlled entity, Caisse des Dépôts et Consignations, had a *de facto* monopoly on lending to sub-national governments. Subsidies were granted by central government ministries on a project by project basis, which made it practically impossible for a mayor to develop a

¹ The case of Paris was a noteworthy exception : from 1971 to 1976, the mayor was appointed, not elected.

particular infrastructure investment without the agreement and support of the central government. For long, communes and *départements* were treated like infants requiring supervision and guidance. In a *département*, the strong man was the prefect rather than the elected council chairman; the *département* budget was actually prepared by the prefect staff, and in many cases, council meetings were chaired by the prefect, even in the presence of the elected council chairman.

This multi-faceted control or tutelage of sub-national governments defined centralization in France as much or more than the relatively large ratios of central to local taxes and responsibilities. The history of decentralization in France, over the 1970-90 period, is largely the history of the gradual relaxation and abandonment of these controls, much more than the history of the shift of central to local taxes and responsibilities. Now, French sub-national governments enjoy a very high degree of autonomy. They do pretty much what they want with their taxes, their expenditures, their debt, their regulations, their employees. Constraints and mandates are minimal. It is in that sense that to-day's France can be considered as a relatively decentralized country.

II – Local Government Expenditure Responsibilities

The responsibilities of each type of government are not always clearly and formally defined. In some areas, they are: municipal roads are to be maintained by communes, and vocational training is to be provided by regions, for instance. But in many other areas, nothing prevents any government to intervene: a commune, or a *département*, or a region, can equally decide to subsidize an orchestra, for instance. In addition, particularly for investments, several levels of government (including the central government) can get together to finance a particular project. A table like Table

4, which indicates which governments are responsible for various public goods or services, does not throw much light on relative responsibilities, because it shows that, in most cases, all levels of government can and are involved.

Table 4 – Allocation of Responsibilities, by Levels of Government, Various Public Goods or Services

	State	Communes	Départ.	Regions
Welfare		*	*	
Education	*	*	*	*
Vocational training				*
Transportation	*	*	*	*
Economic development	*	*	*	*
Urban planning		*		
Water, sanitation, garbage		*		
Culture, Sports and leisure	*	*	*	*
Safety (fire protection, etc.)	*	*	*	

Welfare – The actual delivery of welfare transfers is in the hands of *départements*. But most transfers are decided by the central government, and the central government gives subsidies to *départements* that are calculated to meet that need (*départements* complain that such subsidies do not cover the cost of these mandated expenditures). These mandates define national minimal payment, but *départements* can be —and often are— more generous and give more. In addition, communes can also give money to people in need, and provide services for them.

Education – All four levels of government are very much involved in education. The basic division of labor is that local governments are responsible for developing and maintaining the physical stock of capital, i.e. school buildings, whereas the central government is responsible for labor, i.e. for recruiting, monitoring, promoting —and paying— teachers, and also for curriculum development. Communes are responsible for primary school buildings, *départements* for junior high school buildings (called *collèges* in French), and regions for senior high school buildings (*lycées*). Local governments are also increasingly involved in additional education expenditures, such as art schools or school canteens. In a labor-intensive activity like education, this means that the bulk of

education expenditures remains centralized, and goes a long way to explain the relatively low level of sub-national government expenditure in France. Recruitment and wages are uniform throughout the territory. This does not mean that there are no spatial disparities in school quality: the more senior and often the best teachers tend to congregate in schools located in the most “pleasant” areas. But such disparities are not as great as what can be found in countries where education is funded sub-nationally.

Vocational training – Vocational training is one of the few public services the responsibility of which is not shared. It rests with regions.

Transportation – Transportation, by contrast, is the business of all levels of government. The central government is responsible for “national roads”, for most regulation, for supervising and heavily subsidizing rail transportation, for canals (through a national agency), and for harbors. Regions are responsible for some major roads, and many road investments have been co-financed by regions and the state (and often *départements* as well). A recent development is the involvement of regions in rail transportation. It started in the mid 1990ies as an experiment in six regions, and is being extended to all regions. Regional passenger rail transport is now negotiated regionally, between each region and the regional branch of SNCF, the French national railway agency. Subsidies to SNCF are beginning to be, and will become, an important share of regional expenditures. *Départements* are responsible for “départemental” roads, and also for the organization (and subsidization) of bus transportation, including school bus transportation. The central government is presently moving roads from the national category to the *départemental* category. Finally, communes are responsible for communal roads, including streets, and also for urban public transportation.

In most cases, urban transportation is clearly a metropolitan issue and function. Because there are so many communes in France, practically all urban areas include a relatively large number of communes. A special institution, worth mentioning, has been created to solve this problem. For every urban area, in the perimeter relevant for metropolitan transportation, communes get together to create an “organizing authority”. This grouping is in principle voluntary, although it is usually “inspired” by the prefect of the *département* involved. It is very much facilitated by the creation of a specific transport tax (*versement transport*), a tax based on wages, ear-marked for public transportation, and managed by the organizing authority. The board of this authority is composed of representatives of the mayors of the constituting communes. It is the authority that defines bus lines, or tram lines, subsidizes them heavily (above 50% in most cases), and usually contracts out the service to a private enterprise¹. “Organizing authorities” are usually a creation of communes, but in certain case, a *département* may also be a member. And they receive subsidies, particularly investment subsidies, from the central government.

Economic development – Economic development is a mixed bag including the development of industrial estates, or investment subsidies to (and capital participation in) enterprises, often aiming at re-directing development to specific areas. Governments of all levels are involved in promoting economic development.

Urban planning – The preparation of master plans, sketching out the desirable future economic, social and spatial development of an urban area, and of land use maps

¹ Such institutions do not facilitate accounting ; it is frequent to see this transport tax omitted from the list of « local taxes », although it is beyond doubt that it is a local tax ; also, because the expenditures of organizing authorities do not appear in communal accounts, they are often omitted from « commune expenditures ».

that allocate different zones to different uses (and forbid certain uses in certain zones) is the responsibility of communes.

Water, sanitation, garbage collection – Environmental services such as garbage collection and disposal or water provision are the responsibilities of communes. As in the case of urban public transportation, communes can and do get together to provide such services. They create *ad hoc* groupings or “syndicates” of varying perimeters to benefit from economies of scale. In many cases, the service is contracted out to a private enterprise.

Culture, sports and leisure – All levels of governments are involved in the provision or subsidization of culture, in the form of public theater, music conservatories, museums, concert halls, etc. Sports facilities and parks are mostly provided by communes.

Safety – Fire protection is mostly the responsibility of departments. But it is the central government that intervenes in the case of forest fires or floods. Communes are responsible for road usage, and are beginning to intervene in the protection of persons. But it is the central government that is solely responsible for police.

Can data on expenditures of local governments give a more quantitative picture of this allocation of responsibilities? Unfortunately not. There is data on expenditures by type, for each level of government, as reflected in Table 5.

Table 5 – Expenditures by Type, Communes, *Départements* and Régions, 2001

	Communes	<i>Départements</i>	Regions	(In G euro) Total
Wages	25.3	4.5	0.4	30.2
Transfers	9.5	7.6	4.6	21.7
Interests	2.9	0.8	0.4	4.2
Investments	16.3	6.0	2.1	24.5
Total	69.3	34.9	11.7	116.2

Source : Ministère de l'Intérieur. 2004. *Les Collectivités locales en chiffres*. *Note* : This data is not commensurate with the national accounts data of Table 2 ; it does not include expenditures of groupings of communes, and of certain quasi local government institutions.

However, we failed to identify a meaningful breakdown of expenditures by function. We compiled Table 6 from various ministry of Finance and ministry of Interior sources, but it is not clear that the categories used for communes are similar to those used for *départements* and regions.

Table 6 – Expenditures by Function, Communes, *Départements* and Regions, 2001

	Communes	<i>Départements</i>	Regions	(in G euros) Total
Education	5.2	3.2	3.0	11.4
Vocational training	-	2.2	-	2.2
Welfare	2.7	13.7	-	16.4
Transportation	-	6.4	1.3	7.7
Economic development	11.1	3.8	0.7	15.6
Culture, Sports, leisure	7.3	-	-	7.3
Other	41.9	8.2	4.0	54.0
Total	68.4	35.3	8.7	112.4

Sources and notes : for *départements* and regions : Ministry of Interior. 2004. *Les collectivités locales en chiffres* ; for communes : ministry of Finance's site. Data on debt reimbursement has been escluded.

The excessive size of the share of “other” suggests that reporting and cost accounting is imperfect. It is hard to believe that general administration (which is not allocated to specific functions, as it should) account for half the expenditures of local governments. Nevertheless, the ranking of functions by importance of expenditures shown by Table 6 –welfare, economic development, education, transportation, and culture, sports & leisure— appears quite plausible.

III – Local Government Own Taxes and Charges

As mentioned above, French local governments collect about 5% of GDP in taxes. There are about a dozen local taxes. Table 7 presents local tax proceeds by type of tax and level of government.

Table 7 – Local Taxes, by Type and Level of Government, 2002

	Communes & groupings	<i>Départements</i>	Regions	(in G euros) Total
Housing tax	7.9	3.5	-	11.4
Property tax	9.7	4.2	1.1	15.0
Land tax	0.8	“	“	0.9
Business tax	13.6	6.4	1.9	21.9
Garbage tax	3.4	-	-	3.4
Transport tax	4.3	-	-	4.3
Property registration tax	-	4.0	-	4.0
Vehicle licence tax	-	0.2	-	0.2
Electricity tax	0.9	0.4	-	1.3
Additional ppty registr. tax	1.4	0.1	-	1.5
Vehicles registration tax	-	-	1.4	1.4
Urban development tax	0.4	0.2	0.2	0.7
Other	0.3	e	e	0.4
Total	42.9	18.9	4.7	66.5

Source: Ministry of Interior. 2004. *Les collectivités locales en chiffres*

Before discussing in turn the most important of these taxes, a few general comments are appropriate.

Shared tax bases - First, as is apparent from Table 7, for several taxes (particularly those with the highest yield) two or three different levels of government have access to the same tax bases. There are no “shared taxes” in the usual sense of taxes shared between the central government and sub-national governments, a practice common in Latin America, but also in Germany. What is shared here are not tax proceeds, but tax bases. Consider for instance the property tax (*taxe sur le foncier bâti*) to be paid on a particular building. Let us assume that the tax base is 100. The communal council will decide on a rate of 10%, the *département* council on a rate of 5% and the regional council on a rate of 1%. In principle, we do have three different taxes, and the rate of each tax has been voted upon by a legitimate elected council. The commune will raise 10, the *département* 5, and the region 1. The owner of the building

receives a tax bill that indicates this clearly. In practice however, few taxpayers bother to study their tax bill in detail, and our owner is likely not to look much beyond the 15 he/she pays as “property tax”. This is no inducement to accountability. *Départements* and even more so regions are tempted to increase their tax rates in the hope that the blame will be put on the shoulders of communes. Many yield to this temptation. Symmetrically, communes, and even more so *départements* and regions, are discouraged from lowering tax rates because they know that they will not get political credit for it, particularly if other governments increase their tax rates at the same time.

Tax assessment and collection - This anti accountability effect is aggravated, or at least favored, by another general feature of the French system: local tax assessment and collection is not done by local governments themselves, but by the central government, on their behalf. The central government ministry of Finance assesses tax bases, local governments decide on tax rates, the central government collects the money, and hands it over to local governments —minus a 4% fee for the service rendered¹. This practice does not diminish the “localness” of the taxes involved: what constitutes it is the political decision embodied in rate setting. Assessment and collection are quasi technical functions, that could even be, in theory at least, contracted out to private enterprises properly monitored. This system has several major advantages. One is that it protects tax payers from —and local officials from the temptation of— local arbitrariness or favoritism in tax assessment and collection. Another one is that there are economies of scale involved. Indeed, in the case of the numerous very small communes local tax assessment and collection would not merely be costly but in practice impossible. A third advantage is that tax assessment is uniform throughout the territory. It is done by the same institution with standardized procedures.

Local tax bases are therefore known in a comparable fashion for all local governments. This makes it possible to devise transfer systems based, at least in part, on tax bases, and aimed at reducing tax base disparities—a major goal of transfer systems.

Central government interference – Broadly speaking, local government councils enjoy a great freedom in tax matters. They cannot invent and create taxes of their own, but they can—and do—decide on tax rates. This freedom, however, is not unlimited. A given commune cannot decide overnight to quadruple the tax rate of its business tax. For the main taxes at least, there are some constraints on maximum tax rates: they cannot exceed 2 or 2.5 times the average national tax rate. There is also a compulsory link between tax rates increases on the business tax (paid by enterprises) and tax rate increases on the housing and property taxes (paid by households—and voters). The former cannot be higher than the latter, to prevent local government from increasing only taxes paid by non voting enterprises.

In a number of cases, the central government intervenes to reduce the tax burden of taxpayers, without decreasing the tax proceeds of local governments. For instance, in the name of economic development and employment, the central government sets a limit on the business tax paid by an enterprise as a proportion of its value-added : it cannot be more than 4%. If the product of the tax rate by the tax base turns out to represent 5% of the value-added of the enterprise, then the enterprise pays only 4% of this value-added. The difference, 1%, is paid by the central government to the local government. As a result, the central government has become a major, indeed the main, local tax payer. Whether this 1% should be treated as a local tax or as a subsidy is a matter for discussion.

¹ The ministry of Finance also guarantees local governments against taxpayers default, and claims that the fee charged is also in part an insurance policy premium.

Let us now turn to the five local taxes that account for more than 3 billion euros. Together, they represent more than 85% of local government tax income.

Business tax – The business tax (*taxe professionnelle*) has for long been the most important local tax in France, and still is, in spite of recent cuts in its tax base. It is paid by all enterprises, or more precisely by all “establishments” in the jurisdiction in which they are located. In other words, an enterprise with 20 branches or factories or warehouses will pay 20 different business taxes. The tax base used to be a mix of capital and wages^{1,2}. In 1999, wages have been eliminated from the calculation of the tax base. The resulting reduction in the tax base, and in tax proceeds, has been compensated by a central government subsidy. As mentioned above, there is an upper limit to the amount of business tax that a particular enterprise (or rather establishment) can be made to pay, which is 4% of its value-added.

Taxe professionnelle is an important tax in France. It is the fifth French tax, after the VAT, personal income tax, corporate income tax, and fuels tax. It represents 1.4% of GDP, and a much larger share of the value-added by private enterprises (since GDP includes a non private enterprises components). No wonder that it has been, and still is, heavily criticized in France.

The main criticism is that it is “unfair”, in the sense that it does not treat equally all enterprises; this is “demonstrated” by showing that taxes paid per worker, or per euro of value-added, differ from one sector to another. By this reasoning, any business tax is unfair. For any conceivable tax base, it will always be possible to find one or several criteria (tax per unit of capital, tax per euro of profit, etc.) for which there will

¹ For small enterprises in the service sector, eg. a lawyer, it can be turnover.

² Incidentally, this provides data on the stock of capital (and on wages paid) at the commune, *département* or region level, which is very useful for the analysis of spatial development.

be inter-sectoral or inter-enterprises disparities in taxes paid. A more serious criticism, valid for any business tax in any country, but particularly worrying in a country with small jurisdictions (such as French communes), is that a major part of the tax burden is exported out of the tax jurisdiction. A detailed study conducted on a sample of communes suggested export leakages of about 80%. The political cost of increasing tax rates in a particular commune is low, because the burden of the tax will mostly be borne by people who do not live and vote in the commune. Accountability suffers.

On the other hand, *taxe professionnelle* had, and still has, several advantages. It is a high yield local tax, and the foundation of local governments fiscal autonomy. Being a tax on production factors, it is an inducement to efficiency, rather than a punishment of efficiency. It has proven to be a useful instrument for the siting of unpleasant facilities, such as garbage incinerators or power plant. Communes, and their voters, do not like such facilities, but they like the business tax that comes with it: this facilitates negotiations and siting decisions. For many years, the business tax had another virtue: it had an equalizing effect. Businesses, particularly industrial establishments, were usually located in industrial communes inhabited by relatively low income industrial workers. Communes with low property tax bases per capita happened to be communes with high business tax bases per capita. With de-industrialization, and the development of service activities not necessarily located in low income areas, this disparity-reducing feature has lost much of its importance. But it has not disappeared: poor communes in terms of households incomes are not necessarily poor communes in terms of tax bases.

Like all business taxes, the burden of the tax is in part borne by the central government, or more precisely central government tax payers. Tax payments are

deductible from corporate income, and a reduction in corporate income means a reduction in corporate income tax, the rate of which is about 35%.

Communal groupings have an impact on the business tax. *Communautés urbaines* have the power to levy it, in addition to what is levied by member communes. An enterprise located in a *communauté urbaine* will therefore pay it four times, at the rate decided by each entity: to the commune, to the *communauté urbaine*, to the *département* and to the region. In principle, the communal rate is lower (than what it would be in the absence of *communauté urbaine*); in practice it is probably not much lower. The other groupings (*communautés d'agglomérations* and *communautés de communes*) have the option of choosing a uniform rate for their business tax, and they are encouraged to do so by central government subsidies. This has the advantage of eliminating tax competition within the grouping. Tax competition is not necessarily bad, but it has to be accompanied by “benefit competition”. This is not the case in an urban agglomeration, where the benefits of public services provided by any commune are often available to all agglomeration inhabitants and enterprises. More than 1,000 groupings, representing 38 million inhabitants (63% of total population), have opted for the grouping-wide uniform business tax rate. There remain differences between the business tax rates of different groupings, and differences between the communes of a given grouping for the rates of other taxes.

Property tax and garbage tax – The property tax, or *taxe sur le foncier bâti* (literally tax on built up land), is a tax based on the value of property. Technically, the tax base is the renting value of the property, but there is presumably a fixed relationship between sales values and renting values, so that this does not matter much. Assessment is done by the central government ministry of Finance, with the help of a cadaster (also managed by the central government), and taking into account the size, comfort,

location, etc. characteristics of each property. The views of local committees are also taken into account. Unfortunately, re-assessments are rare and unpopular, because owners of under-assessed buildings strongly oppose them, and the few courageous ministers of Finance who attempted to undertake re-assessments paid a high political price for it. As a result, and although there are no serious studies of it, it is widely believed that the ratio of assessed value to market value varies significantly from one property to another. Industrial and commercial properties are assessed and taxed just like residential properties, at similar rates. Communes, *départements*, and regions decide on the tax rate each of them applies, and the ministry of Finance does the rest, that is collects the tax from property owners and sends the proceeds to each commune, *département* and region.

How heavy is the property tax in practice? The true tax rate (the ratio of tax paid to sales value) varies greatly from commune to commune

The garbage tax, or *taxe d'enlèvement des ordures ménagères*, has exactly the same base as the property tax and can be seen as an addition or a surcharge to it. It is called garbage tax because its proceeds are ear-marked for garbage collection and disposal. It is only imposed by communes, and not even by all communes, since some prefer instead to charge fees, based on the amount of garbage collected —fees which are not recorded as taxes.

Housing tax – The housing tax, or *taxe d'habitation*, is also a form of property tax, based on the same rental value of the housing structure. It is paid by the dweller, not by the owner, on both rented or owner occupied houses. This implies that, unlike the property tax, it is not paid on non-residential structures. Tax rates are decided by communes and *départements*, since the region no longer benefits from this tax. The

housing tax is politically important because it is paid by some 25 million households, including many households who do not pay personal income tax¹. Communes can and do decide that low income households are tax exempt. Overall, the burden of the housing tax is not negligible: it represents exactly 1% of households pre-tax income.

It has been argued that the housing tax is regressive relative to income, because the ratio of housing value to income is supposed to decline when income increases. But it has also been argued that such a decline is not well established, particularly in a country where many relatively low income people live in subsidized houses of a small rental or market value. In any case, housing tax exemptions, which are common and important, reduce significantly the potential regressiveness of the housing tax.

Transport tax – As mentioned above, about 150 transport “organizing authorities” created in all important urban areas have the power to levy a tax, *versement transport*. The tax is paid by all enterprises of more than 10 employees, and is based on wages. (It is in effect a wage tax, called “transport tax” because the proceeds are earmarked for public transportation). The rate is chosen by the organizing authority, and is usually between 0.75% and 2%. The tax represents about 0.3% of GDP.

Property registration tax – *Départements* (and only *départements*) also levy a property registration tax or *droits d’enregistrement*, paid on all sales of buildings in the jurisdiction.

Evolution - How have evolved local taxes in recent years? Relative to GDP, they have declined, as shown in Table 8 that gives data for 1996 and 2002 (data for intermediate years do not add much).

¹ More than half French households do not pay personal income tax.

Table 8 – Local Taxes as % of GDP, France, 1996 & 2002

	1996	2000	□
Paid by local taxpayers	4.8	4.2	-12%
Paid by central government	0.9	0.8	-10%
Total	5.7	5.0	-12%

Source : INSEE, using national accounts concepts

Table 8 distinguishes between local taxes effectively paid by local taxpayers, and the share of local taxes contributed by the central government as a result of tax rebates or exemptions decided by the central government (the latter could alternatively be classified as subsidies). For both concepts, there was a clear and significant decline. This decline cannot be explained by a decline in tax rates. Available data suggests that for most taxes, tax rates have increased rather than decreased. The decline cannot be explained either by an elasticity of local tax bases to GDP lower than 1; the elasticity of the business tax base to GDP has for years been greater than 1, and the same is true of housing rental value. There is no reason to think that a reduced efficiency in tax collection could explain this decline. The main cause is to be found in central government decisions to eliminate some local taxes, such as the yearly vehicle licence tax (which was a *département* tax), and to downsize the base of certain taxes, particularly the business tax. Local governments received additional subsidies instead, which implies some increases in national taxation. These changes were politically rather uncontroversial. It was felt that national taxes were less distortive and/or less painful than local taxes. Politically, this counted more than the implied loss in local fiscal autonomy, which was realized and deplored.

IV — Central-Local Fiscal Transfers

As in most other countries, transfers, grants and subsidies from the central government to local governments are a very important part of local government resources and a sizable part of central government expenditures. In 2002, in France,

such transfers represented about 48% of local government income (slightly less than local taxes), and about 16% of central government expenditures. How this money is allocated is obviously of prime importance. Four general points can be made.

First, all transfers are automatic and formula-driven. There are no discretionary subsidies to local governments. No minister, not even the president of the Republic, can “favor” a particular local government of its liking. The only thing it could think of doing would be to change the allocation rules and formulae in a way that might increase the transfers received by that particular government, together with all the other local governments that have similar characteristics.

Second, nearly all transfers are block grants, coming with no strings attached. Local governments can do what they want with the subsidies they receive, even if and when they are calculated in reference to well-defined uses. There are a few specific transfers, granted by particular ministries, that are exceptions to this rule, but they account for only 3% of total transfers. This is a great change from the situation that prevailed 30 years ago, when most subsidies were ear-marked for specific usage or even projects. Official documents (followed by many analysts) continue to distinguish between operating subsidies and investment subsidies. This distinction is a mere accounting curiosity with no practical meaning¹. For a given local government, subsidies are as good as own taxes.

Third, allocation procedures are extremely complicated, and few people, if any, understand them fully². There are about 20 different subsidies. None has been

¹ The surplus on the operating budget is used to finance the investment budget. This means that a subsidy to the operating budget will make it possible to increase the internal transfer to the investment budget, and therefore investments. Symetrically, a subsidy to the investment budget makes it possible to reduce this internal transfer, and therefore to increase operating expenditures.

² It is reported that the long-standing chairman of a powerful local finance committee is about the only person who has a good command of the system ; some people claim that the commune of which he is the

introduced from scratch, with a well thought design. All have been introduced to replace a former subsidy, or to compensate for a tax eliminated or modified by the central government. Each had to take into consideration the previous situation, in order not to introduce major changes that would have been politically unacceptable (when they meant less than before). Each formula therefore embodies features of a distant past. But the central government usually took advantage of each change to introduce additional objectives—for instance, increased fairness—in the allocation formula. This produced complex formulae, planned to change over the course of time. The actual outcome of each of these formulae is hard to predict, and their combined outcome practically impossible to predict. A simple question like: “to what extent does the transfer system reduce per capita disparities in tax bases ? and how much of this reduction (if any) can be attributed to each subsidy?” remains largely unanswered.

Fourth, the system keeps changing constantly. Since, it changes by addition of new features rather than by substitution of old features by new features, this quest for improvement is one of the causes of the complexity of the system. The data and description that follows relate to 2002, but in 2003 a new system (or more precisely the first phase of a new system) has been introduced. This makes our description obsolete, but only in part, because, as mentioned year n system incorporates many features of year n-1 system.

Table 9 shows the main types of subsidies in 2002 and singles out the most important ones, that call for some additional explanations.

mayor turns out to be rather well treated by the system ; cautious analysts note that correlation is not causality.

Table 9 – Central to Local Government Transfers, France, 2002

	(G euros)	(%)	(%)
Block grants	54.3	97	100
General subsidies	24.5		45
<i>DGF</i>	18.6		
<i>FCTVA</i>	3.6		
<i>DGE</i>	0.9		
Other	1.4		
Decentralization subsidies	8.5		16
<i>DGD</i>	6.1		
Vocational training	1.3		
Education	0.8		
Other	0.3		
Compensating subsidies	21.3		39
Specific subsidies	1.7	3	
Total	56.0	100	

Source: DGCL, using public finance accounts concepts

General Subsidies

Current expenditure block grant - About 10 transfers can be categorized as general subsidies. By far the most important is the current expenditures block grant or *dotation globale de fonctionnement (DGF)*. The determination of the total amount and of the allocation criteria is done every year by Parliament. Parliament is guided by some general principles that it enacted in the past. These principles can be overruled, but this is done at a high political cost, except if there is a consensus for it.

The total amount of the block grant is determined in relation to what it was for the previous year. If B_n is the grant for year n ; B_{n-1} the grant for year $n-1$; r the inflation rate in year n , and t the GDP growth rate during year $n-1$:

$$B_n = B_{n-1} * 1+r * 1+t/2$$

Local government as a whole are guaranteed to have a block grant at least equal to what it was the previous year in real terms, and to see it increase at half the GDP growth rate.

The block grant is then divided between communes and *départements*, prorata their share during the previous year, that is 72.5% for communes and 27.5% for *départements*. Beginning in 2004, regions will also have a share of *DGF*.

The communal block grant is then divided into two parts: a “standard” part (for 81%), and a “policy” part (for 19%).

The standard part (*dotation forfaitaire*) reflects the situation in 1993. Every year each commune gets what it obtained in 1993 on a per capita basis, multiplied by a coefficient which is the same for all communes. The next question, therefore, is: how were the grants given to each commune determined in 1993. They were mostly determined on the basis of four criteria: (i) tax bases, (ii) expenditures needs, (iii) tax effort, and (iv) past grants.

Tax bases played an important role: communes with low tax bases would, all other things equal, obtain more. The problem created by the multiplicity of tax bases was solved with the notion of “tax potential” (*potentiel fiscal*) defined as follows. Let $B_{i,k}$ be the tax base of commune i for tax k . Let T_k be the average tax rate for tax k for all communes of France. Let, B_i the tax potential of commune i . We had:

$$B_i = \sum_k B_{i,k} * T_k$$

In simpler terms, the fiscal potential of a commune is what the commune would collect if it applied for each of its taxes the average national tax rate.

“Needs” also played an important role, in several ways. The commune size was taken into account, with (again all other things equal) larger commune getting more, on a per capita basis, than smaller commune, to reflect the idea that needs increase with commune size. Some special categories of communes, such as city center communes

and resort communes, were also favored. Finally, criteria such as the length of the communal road network, the number of school age children and the share of low income houses, were also taken into account.

The tax effort of a commune, defined as the ratio of taxes collected to taxes that would be collected if average tax rates were applied had also been introduced (in 1985) and played a relatively minor role.

Finally, the past situation of the commune also played a role. The global grant had been introduced as a replacement of particular local taxes that were eliminated in a distant past (1969), and new allocation criteria were supposed to replace only gradually previous communal income. In the 1993 situation, there was still an echo of this distant time.

The “policy” part (*dotation d'aménagement*) of the communal block grant is used to further specific goals. The bulk of it goes to sponsor communal groupings, which are considered desirable by the central government. Communes that get together in *communautés d'agglomérations* or *communautés de communes* get more transfers than communes that do not. This incentive is not foreign to the rapid development of communal groupings in recent years. The rest goes to “needy” communes in urban areas (*dotation de solidarité urbaine*) or in rural areas (*dotation de solidarité rurale*). The criteria used to define these communes and to allocate the grant are complex, but it is interesting to note that they refer to socio-economic characteristics (income, share of low income housing, etc.) rather than to fiscal and financial characteristics (tax bases).

Value-added compensation grant - The other important general subsidy is the value-added compensation grant. Consider a given investment (the purchase of a computer, or the construction of a building, for instance) of 100 undertaken by a private

enterprise and by a local government. Both will pay a price that includes a value-added tax of about 20. The private enterprise will use the computer or the building to produce goods or services that will be sold at a price that will include a value-added tax of, let us say, 50. The enterprise will deduct the 20 paid on its investment, and send the fisc a check of only 30. The local government will also use the computer or the building to produce goods or services which are usually not sold, and have no VAT attached. The local government cannot deduct the 20 already paid. The VAT system therefore discriminates against local governments. To eliminate or correct this distortion, the VAT paid by local governments on their investments is reimbursed to them. The amount involved is not negligible, and represents more than 5% of total local government taxes.

Investment grant – There is also an investment grant (*dotation globale d'équipement, or DGF*) for communes and départements. For communes, it is first allocated to the département level (prorata communal tax bases, or tax potential, population, length of communal roads, number of communes), then allocated by each prefect assisted by a committee of mayors to communes as a function of their investments; richer communes, i.e.e. communes with a tax potential above a certain threshold, are excluded.

Decentralization Subsidies

A second group of subsidies can be categorized as “decentralization subsidies”. They were introduced in the 1980ies, when some expenditures responsibilities were shifted from the central government to sub-national governments. Estimates were made of the cost savings this shift implied for the central government, and equivalent transfers to the various local governments were decided. Some are specific and well

identified, such as subsidies to cover the cost of vocational training (a responsibility transferred to regions) or the cost of construction and maintenance of school buildings (transferred to *départements* and regions); other are global. The process continues. Presently, the responsibility for relationships with SNCF, the rail company, for regional passenger transport —and the heavy subsidies to rail transport they imply— are being shifted to regions. This is accompanied by another specific decentralization subsidy. As can be expected, local governments, when they obtain a new responsibility (that they demanded), complain that the decentralization subsidy that comes with it does not cover the additional cost. They are usually right.

Compensating Subsidies

As mentioned above, the central government tends to intervene in local taxation and to grant deductions and allowances of all sorts. Local governments, who are usually happy with it because it reduces the taxes paid by their electorate, systematically protest that the central government cannot be generous with someone else's money, and ask for a compensation. They usually get it. Local governments thus have the best of both worlds: same revenues for their coffers and less taxes for their taxpayers.

The most recent (and important in money terms) example is the elimination of the wages component from the base of the business tax. The business tax base consisted of capital (for about two thirds) and wages (for about one third). In 1999, the central government decided to eliminate the wages component, in order to reduce labor costs in France. This implied, all other things equal, a decline of one third of revenues generated by the most important local tax in France. The central government immediately pledged

to compensate local government for this enormous revenue loss, thus creating a new subsidy that now amounts to 8 billion euros¹.

The subsidy system is therefore very complex, and its outcomes are haphazard. Most of the changes introduced in recent years aim at giving more to some local governments while at the same time not giving less to any, without increasing total subsidies. The current expenditures block grant (*DGF*) does have a redistributive effect, in the sense that it reduce disparities in tax bases. But it is not sure that most of the other subsidies have the same effect. The value-added compensation grant, for instance, is allocated prorata investments per capita, and there are reasons to expect investments per capita to be higher in high tax base jurisdictions. Similarly, the subsidy that compensates the elimination of the wage component of the business tax base benefits primarily those local governments that had enterprises with high wage bills: they are unlikely to be the poorest local governments, be it in terms of income of inhabitants or of tax bases. Overall, the system is likely to be redistributive. The Gini coefficient measuring the inequality of after-transfers local government income is lower than the one measuring the inequality of before-transfers local government income (or tax bases). But a similar result would be achieved by an equal per capita transfer.

Current Reform

In 2003, it has been decided to “simplify” the system just described. A number of the grants and subsidies classified as decentralization or compensating subsidies are shifted to the current expenditures grant (*DGF*). In the 2004 budget, the importance of *DGF* practically doubles, to 36.7 billion euros.. Regions, as well as communes and *départements*, will benefit from it. Most of the new *DGF* will be used to give each local

¹ In practice, such changes are not made overnight ; they are planned to be gradual, with sliding formula extending over many years.

government (i) the grants it received before, increased by less than the nominal increase of GDP, and (ii) a redistributive grant, mostly based on the tax bases or fiscal potential of each sub-national government.

V – Local Government Borrowing

Local governments in France do not borrow much, and consequently are not very much indebted, particularly when compared with the central government. This is illustrated in Table 10, that presents national accounts data, with a broad but meaningful definition of “local governments”.

Table 10 – Borrowing and Indebtedness, Central and Local Governments, France, 2001

	Central government	Local governments
Revenues (G e)	295	150
Expenditures (G e)	329	147
Balance (G e)	-34	+3
Balance/revenues (%)	-11%	+2%
Indebtdness (G e)	671	111
Indebtedness/revenues (%)	227%	74%
Indebtedness/GDP (%)	45%	7%

Source : DGCL, using national accounts concepts.

When the central government budget is heavily unbalanced, with expenditures greater than revenues by more than 10%, local governments budgets (taken together) are basically balanced. The data given in Table 10 for one year (2001) is representative of the past decades. Central government accounts have always been in deficit. Local governments accounts have been in deficit or in surplus, but always by a small margin.

Consequently, the debt of the central government is heavy, relative to its revenues, and is increasing, whereas the debt of local governments is modest, and declining. Local governments debt represents only three-fourth of local governments

yearly income, and one seventh of the combined public debt of the country. It is not, at least for the moment, a serious macro-economic issue.

Net numbers do not give a full picture of the scene, and Table 11 that presents gross numbers is a useful complement. It suggests that, for a given year, new loans account for nearly 10% of total revenues, even though reimbursements represent a flow of a similar order of magnitude (actually slightly higher in 2000, the year for which this data is available). It also shows the magnitude of interest payments relative to total expenditures: slightly more than 3%.

Table 11 – Local Governments Borrowing Related Flows, France, 2000

	(in G euros)
Resources	126.1
of which: borrowing	11.5
Expenditures	126.0
of which: reimbursements	13.2
interests paid	4.2
Net borrowing	-1.7
	(in %)
Interests/expenditures	3.3%
Borrowing/resources	9.1%
Reimbursements/expenditures	10.5%
Net borrowing/resources	1.3%

Source: DGCL, using public finance accounts concepts.

All types of local governments borrow, in roughly similar proportions relative to their income, as shown in Table 12. Regions are slightly more in debt than communes or *département*. This reflects the fact that investments are a larger part of their expenditures.

Table 12 – Indebtedness of Local Governments, by Type, France, 2002

	G euros	% of resources	% of GDP
Communes	51.0	47%	3.4%
<i>Départements</i>	18.2	46%	1.2%
Regions	7.7	56%	0.5%
Total	76.9	48%	5.1%

Source : DGCL ; the total differs from the total in Table 10, because the source is public finance accounts as opposed to national accounts

Who lends to local governments? The answer to this question is given in Table 13. First, it appears that bonds floated on the market play only a minor role. They account only for 2-4% of total debt for communes and *départements*. The share is much higher (about 18%) for regions, but overall it remains very modest.

Second, most (60-80%) of the loans to local governments are made by private banks. Third, the private bank picture is dominated by Dexia (about 40% of total lending). Dexia started in the 1980ies, under the name of Crédit Local de France, as a subsidiary of the powerful and publicly owned Caisse des Dépôts et Consignations, with a long experience in dealing with local governments, but in a semi-monopolistic position. It was later privatized. It then merged with Crédit communal de Belgique, a — or rather the— Belgian bank for local governments, to create Dexia. When the quasi-monopoly it enjoyed in France was broken, and when competition for lending to local governments became open, many people thought that Dexia's share of the market would decline. It did not, and Dexia expanded in other areas, such as public finance initiatives and international lending. This would tend to suggest that lending to local governments is a fairly specialized type of banking, requiring specific expertise that is not necessarily available in the ordinary banking sector.

Table 13 – Local Government Debt, by Lenders and Levels of Government, France, late 1990ies

	Communes (1996) (%)	Départements (2000) (%)	Regions (2000) (%)
Bonds floated on the market	2.1	3.6	17.7
Public & quasi-public institutions ^a	34.8	17.2	20.1
Private banks	63.9	79.2	62.2
of which: Dexia	38.5	41.2	30.3
Total	100.0	100.0	100.0

Source: DGCI. *Notes:* ^aCaisse des Dépôts et Consignation, Caisses d'épargne, Crédit Foncier.

How explain the relative “moderation” of local governments in borrowing? It does not result from central government imposed constraints. Local governments are practically free to borrow from whoever they want, to float bonds on the market, to obtain loans from French and foreign banks, as they please or as they can. This is a sharp contrast with the situation that prevailed in the 1970ies and early 1980ies. Then, local governments could only borrow from State-owned institutions such as Caisse des Dépôts et Consignations or Caisses d'épargne, and for amounts decided by the ministry of Finance. Originally, loans were even granted only on a project by project basis. On the other hand, such loans were made at concessionary rates, significantly below market rates. All of these constraints were progressively relaxed.

Moderation does not result either from the market discipline associated with a bond market, and facilitated by the influence of rating agencies. This US-type model, which was much favored by the World Bank for its client countries, does not function in France, at least presently. The international rating agencies (plus a couple of French ones) do operate in France, and have rated some regions and *départements* and a few large cities as well. But the share of the bond market, as mentioned above, is too small for this model to function, at least for the time being.

The constraints on borrowing are financial and political. Banks are reluctant to lend to over-indebted local governments. They know what ratios of interests to

revenues are socially and politically sustainable, and refuse to make loans that would lead to significantly higher ratios. But local governments themselves are prudent. They realize that loan financing is costly. They fear that their political image would be affected by excessive indebtedness. Debt to revenues or interest to revenues ratios are part of the public debate, and they are available on the net. The long tenure of municipal governments (at least 6 years, usually 12 years, and in many cases more) encourages borrowing responsibility.

Would the central government bail out a failing local government? In principle, no. In practice, to a certain extent. There was a case of a relatively large commune (Angoulême) that nearly went bankrupt in the 1980ies. The mayor fled to Argentina. The ministry of Finance, the lending banks, and the local politicians got together, and reached an agreement that implied (a) a serious loss for the banks, (b) very high tax rates for local taxpayers, and (c) some central government subsidies. This was not very clearly stated, but banks learned that irresponsible loans to local governments could be very costly, and politicians that excessive indebtedness could lead to lasting high taxes and a damaging image.

A related interesting feature is that local governments financial balances are not held by private banks, but by the Treasury. Each local government has an account with the Treasury. It is credited of the taxes which are collected, as mentioned above, by the Treasury, not when they are actually collected, but every month (for 1/12); and also of the subsidies granted to the local government. This account is debited of all expenditures, which are actually done by the Treasury, on order from the local government.

VI - Local Government Administration

Traditionally, a local mandate (as council member, mayor, chairperson) was considered an honor, and was not paid. This was at a time when it did not take too much time (and also when such mandates were often held by people who did not need money). This is no longer the case. Being a mayor, for instance is a full-time job, even in a relatively small commune. Locally elected officials are now paid, but their wages, or compensation, are decided by the central government, and are not very high. Wages are a function of the jurisdiction size. The mayor of a 40,000 people commune, for instance, earns about 27,000 euros per year. The mayors of Paris, Marseille, Lyons (the three largest communes) get about twice as much (but in addition they can be —and actually are— MPs). Departement and region council members remunerations are in the 20-30,000 euros range. But these functions are not full-time.

Staff members, numbering about 1.5 million, are civil servants. They are recruited on the basis of competitive exams, and once recruited cannot be fired. This has benefits as well as costs. On the one hand, it protects local government employees from political arbitrariness, and ensures a much welcome continuity in the operation of local government administration. On the other hand, it can make it difficult for politicians to introduce new policies. How is this potential conflict solved?

First, in many cases, local civil servants will be loyal to the newly elected politician, and do their best to follow his/her directives. Second, particularly in large communes and in *départements* and regions, a new mayor or chairperson will bring with him/her a “private office” of his choosing and of his/her political persuasion. This might consist of 10-15 persons, usually technically well qualified, but also politically reliable, whose task will be to oversee the permanent staff, to help take delicate and important decisions, and more generally to make sure that the mayor’s directives will prevail. When the mayor quits, so does the entire private office. Third, the mayor or

the chairperson can put aside key staff members who do not want (or with whom he/she does not want) to cooperate. They will keep their salary, but will be constantly short-circuited, and deprived of any real responsibility. Some might be happy to be paid at doing nothing. But most will look for another position in another politically more friendly local government. This is often the case with the secretary-general of a commune, the most senior civil servant, who has often worked closely with the previous mayor, on topics that were partly technical and partly political.

There are complex links between the central civil service and the local civil service. The two are distinct, but similar. Under some conditions, members of one “body” can be “lent” to the other, which means that they keep the option of going back to their original “body”. When regions were created, in the 1980ies, a number of people from the national civil service were recruited by regions, often on senior positions, with regions offering very substantial bonuses, in addition to the standard civil service wages.

There is an additional element of flexibility worth mentioning. Local governments, particularly communes, do create and control a number of “satellites”, such as a development agency, or a garbage collection company, or a public transport agency. These satellites are formally private enterprises, even if their capital is 100% controlled by the commune and their board chaired by the mayor. These boards can staff these enterprises with whoever they want, and pay them at market rates.

VII – Conclusion

It is difficult to pass a judgement on the efficiency and accountability of the system of local government just described, particularly because it has changed much in

the past decades, and continues to change. A few tentative points can nevertheless be made.

First, the new tasks allocated to local governments in recent years seem to be reasonably well undertaken, as well or better than before, when they were in the hands of the central government. School buildings are better maintained by regions and *départements* than they were by the ministry of Education; but regions and *départements* spend more money on it than the ministry of Education did. It is reported that welfare money is better spent by *départements* than it was by the central government. Regions are most probably better equipped than the central government to discuss with the railroad company what regional passenger lines should be subsidized and for how much (the central government was unable to do it anyway). In that sense, the decentralization of responsibilities is generally considered successful.

Second, there are accountability mechanisms, but they are relatively weak. One such mechanism is the desire of politicians to be re-elected, and the fact they can be re-elected. This mechanism, however, functions much better at the commune level than at the *département* or region level. People know (or think they know) whether their mayor is good or bad, and they take it into account at election time, as much or more than his party affiliation. Not so at the level of the region or the *département*, where people usually vote as they would in a national election, for the party of their liking.

Another accountability mechanism is the relatively large share of local taxes in local government resources, and the fact that two of these taxes, the housing tax and (to a lesser extent) the property tax, are paid by most voters. This standard and effective mechanism, unfortunately, is weakened by several factors. It does not work for the business tax (*taxe professionnelle*) which is exported out of the jurisdiction where it is

levied. The fact that several levels of governments levy the same taxes dilutes responsibility in the eyes of taxpayers-voters. The rapid development of groupings of communes, which are not led by directly elected people, is also eroding accountability. Finally, the ratio of taxes to subsidies has dangerously declined in recent years.

Third, there are presently no macro-economic problems associated with increased decentralization. Local governments have not misused the freedom they were given, in tax or in borrowing matters. They have behaved very responsibly.

Fourth, in France as in most countries, decentralization has been driven by political considerations more than by economic efficiency considerations. New institutions have been created, at least in part, to distribute more widely power—and income—to politicians and their clients. This is done at an economic cost. To merely function, any institution, be it a government or an enterprise, has fixed costs. Part of the money spent is spent to cover these fixed costs, not to produce public goods and services. In the past years, most *départements* and regions constructed costly *départements* and region “buildings” or “houses” which are examples of such fixed costs. The multiplication of governments increases these fixed costs, not to mention the coordination costs it implies. The lack of cost accounting makes it difficult to examine this issue in depth, but one must fear that too large a share of local public expenditures goes into mere “administration”. This is exacerbated by the co-existence of regions and *départements*. Many people believe that there is one too many level of government. Eliminating one would reduce these fixed costs, but this is precisely the reason why it is politically strongly opposed and next to impossible.

Developing countries can learn several things from the French experience. One is that the standard measures of decentralization (local expenditures/total public

expenditures, local taxes/total taxes) are much too crude to be meaningful. Changing them is unlikely to achieve much. The key parameters of features of a local government organization and finance system are often details of the election system or the subsidy system.

Second, changes in the degree, nature, and significance of a decentralization system should be gradual. It took France 30 years to move from a highly centralized system to a fairly decentralized one. The idea that a decentralization reform can be conducted in a few years, or by a single law, is not very realistic, and might be counterproductive.

A third lesson is that no system is ideal and definitive. Reforming and “improving” the system of multi-level government is constantly on the agenda in France —and in most other countries as well. The reason is that such a system targets too many goals at the same time: redistribute political power, improve economic efficiency, reduce inter-jurisdiction and inter-personal disparities, facilitate macro-economic management, etc. A weakness in one of these objectives is spotted. Changes are made to improve matters on this score. But these changes are likely to worsen matters in regard to another —also perfectly legitimate— objective. These new weaknesses will in turn call for additional changes. This must be accepted. System should not be frozen, but should remain reasonably flexible, and able to accommodate changes easily. Constitutions, in particular, should not attempt to define a detailed system for ever.

Fourth, the number of jurisdictions and their map are not major issues. The very large number of communes in France (37,000) is often presented as a serious issue. It is not. It does present problems, but they have found solutions, in the form of groupings of

various types. If France was starting from scratch, it would not create the present map of 37,000 communes. But because it has existed for more than two centuries, the costs of redesigning a completely new (and better) map would outweigh the benefits of it. In this area, outcomes are path dependent.

Fifth, strong local autonomy does not imply complete local independence. There are no local governments worth the name without a high degree of autonomy. But it does not mean that they could or should be completely separated from the central government. Local taxes in France are administered, assessed and collected by the central government: this does not seriously affect local autonomy, and most probably improves the efficiency of local tax collection. Another example is given by the wages of local government officials. In some countries, in the name of local autonomy, locally elected councils decide as they please on the level of wages of the mayor. This has resulted in some politicians in relatively small (and usually very poor) municipalities or provinces voting themselves salaries much higher than the salary of the chairman of the US Federal Reserve Board. In France, such salaries are determined by a central government law, and nobody sees it as an infringement of local autonomy.

A final lesson might be that in decentralization, the better can be the enemy of the good. Four levels of government (five if one counts groupings as a level of government, and six if one considers the European Union) is a lot, even in a relatively rich country like France. For each level of government, there are justifications, and benefits. But there are costs, too. In France, they barely balance each other. But in a poorer country, it is doubtful that they would. The costs of the marginal level of government would outweigh its benefits.

References

Much of the information used in this paper, particularly numbers, come from the specialized web sites of the French ministries of Interior (www.dgcl.interieur.gouv.fr) and of Finance (www.colloc.minefi.gouv.fr).