11. The public sector in Portugal: scope, structure and accounts[1]

Summary

This chapter examines the scope and structure of public sector in Portugal, as well as the accounts of the various sub-sectors of general government including transfers that operate between them. One difficulty in the analysis of public finances in Portugal is a certain conceptual confusion because the same term has different meanings depending on the context in which it is used (for ex. State). A second difficulty is the different forms of accounting and accounting systems used. The main concepts used here are *economic* rather than *legal*, and we clarify the distinction between them. Finally, frequent changes in organizational structure of governments, as well as changes in the actual universe of institutions within general government (*administrações públicas*) make comparative analysis difficult.

The *public sector* includes all entities that are controlled, directly or indirectly, by some political institution be it the government of the Republic, regional governments (Azores and Madeira) or local governments. Therefore, it includes the *general government* (or public administrations) comprising three levels of government (central government and social security, regional and local governments) as well as the *public sector corporations*, when there is a majority or total public capital and whether the major stakeholder is the State, a Regional Government or a municipality.

What characterizes the entities in general government, is that they are *non-market* producers of goods and services to individual and collective consumption or entities operating redistribution (pecuniary or not), in both cases being mainly financed by *compulsory contributions*. These contributions must represent at least 50% of production costs. In the case of *market producers* revenues of prices, tariffs or fees are in return for the provision of services and should cover the costs of production (at least never lower than 50%).

EUROSTAT, the Statistical Authority in the European Union, has developed the European System of Accounts ESA95, where countries have the same structure of accounts distinguishing the *central government (S.1311), state (S1312), local (S1313*) and social *security funds (S1314*). The State level is primarily used in federal countries (e.g. Germany, Belgium, Austria) and not in unitary countries (e.g. Portugal and the UK). Portuguese statistics classify the aggregate accounts of central government (S1311, which consolidates the accounts of the State (ministries) with Autonomous Funds and Services (FSA)); local government (S1313 which consolidates the accounts of regional and local government (ARL)); and finally, Social Security (SS in S1314). In federal countries (such as Germany or Austria), there are federal government accounts (S1311) state government accounts (in S1312), and local governments in (in S1313).

The general government in Portugal (S13) is therefore composed of four sub-sectors, namely: State, FSA, ARL and SS. Since three of them (State, FSA and SS) are under the political direction of government, the degree of political decentralization may be measured by the ratio of the expenditure on regional and municipal governments (the ARL) over the consolidated expenditure of general government (public administrations).

The use, in the broadest sense of the term "State", in "State Budget" or "General State Account" refers to the budget or the account of the three sub-sectors (state, FSA and SS). On the other hand, in the strict sense of the term, “State” means only the sub-sector of integrated services of each ministry (ie *Direcções-Gerais*), without a legal form and with just an administrative autonomy for the current management of appropriations from the budget state. They have no autonomous revenues or own assets. In turn the FSA (e.g. hospitals within public administration, public universities, public institutes) are entities with administrative and financial autonomy. They have a legal status, with the management of current and capital expenditures, its own assets, ability to have their own income and possibility of access to credit (with permission). The sub-sector of social security includes the institutional units which are mainly responsible for the payment of social benefits (unemployment, sickness, pensions, etc.) and are financed by compulsory contributions.

When considering the accounts of public administrations, it is important to distinguish whether to use national or public accounts. The national accounts (NA) are used for the European Union

[1] (c) Paulo Trigo Pereira. This is a slightly revised version of the summary included in the book (Pereira, P. (2013) Economia e Finanças Públicas: da Teoria à Prática) in order to adapt to the needs of Erasmus students and the diversity of their countries’ public finances .

(EUROSTAT, the excessive deficit procedure etc..) It has an economic basis, based on defining the universe of entities that belong to the government *as non-market units* and adopts a logical of *commitments* (revenues and expenses are recorded when the commitment is made and not when there is a cash flow). A public accounting (PA) is used initially in the accounts of general government entities (SPA) has a more legal definition of the entities that belong to the public administration and adopts a more imprecise logic of cash (receipts and expenses are recorded when entering or leaving the Treasury account).

In order to compute the balances of general government accounts, we use the economic classification of revenue and expenditures (i.e. non-financial). The *effective revenue* is total revenue less revenue from financial liabilities (eg loans) and financial assets (eg income from sale of shares or other financial assets). *Effective expenditure* is the total expenditure less expenditure on liabilities (eg repayment of loans) and financial assets (eg purchase of all or part of equity/capital by the state). The *current balance* (in PA) or gross savings (in NA) is the difference between effective (non financial) revenues and expenditures. It can be calculated for each sub-sector alone (state, FSA, ARL and SS) or for public administrations (general government) as a whole. In this latter case it is necessary to *consolidate* the current revenues which are equal to the sum of current revenues from all sub-sectors, less the inter-governmental transfers (revenues) that come from other sub-sectors. The capital balance is also the difference between capital revenue and capital expenditure and can be calculated with or without consolidation for each sub-sector, but has to be consolidated for the general government.[2]

The sum of current and capital balances (in NA) for all four sub-sectors *gives the overall (or global) balance of general government*, which is nothing more than the difference between effective revenues and effective expenditures.[3] If it is negative, it represents *a public deficit* and generates the need for net borrowing, ie needing to issue new debt. If it is positive, there is a surplus and generates the possibility to decrease (repay) part of the public debt.

Another important balance is the *primary balance* which is the difference between effective revenue and primary expenditure (effective expenditure less interest payments). It gives the value of the overall balance that would exist if there were no public debt (and therefore no interests).

The interpretation of the balances of each subsector should be cautious given the transfers between sub-sectors. Balances (unconsolidated) represent a simple relationship between revenues and expenditures. A sub-sector may have a surplus only because it receives transfers from another sub-sector. In this case the balance (consolidated) of the sub-sector will be negative. If transfers are the result of a law (basic law on social security, finance, regional or local, etc.) they are a legal obligation of the State. If they are not a consequence of a specific law, but they are discretionary (e.g the need to cover any deficit of Social security) the situation is different. Changes in transfers between levels of government do not change, everything equal, the global balance of general government because they are an expenditure for one sub-sector (the donor), and the same revenue for the other (the receiver).

Also transfers between general government (AP) and the public sector corporations (SPE) should be considered carefully since they may involve *off-budget* phenomena or outsourcing with the aim of reducing "artificially" the budget deficit. A financial flow between the two can be a current expense (case of compensation for "social prices"), can be a capital expenditure (capital transfer) or an increase in the equity of a public corporation. The latter, unlike the first, is clearly not an effective expenditure since it increases the financial assets of the state and in principle should not count for the deficit. However, if the company concerned is considered a non-market institution, it may count for the deficit.

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[2] Capital revenues and expenditures include revenues/expenditure from liabilities and assets. Usually when we mention capital balance we are talking about non financial (effective) revenues and expenditures.

[3] The global balance of general government can also be computed as the sum of the non-consolidated balances of each sub-sector (state, FSA, AFS and SS) given that transfers, *within public administration,*have no effects on general government balances.