



Independent Authority
for Fiscal Responsibility

Report

Report on the main budgetary lines of the Local Corporations for 2018

The mission of the AIReF, the Independent Authority for Fiscal Responsibility, is to ensure strict compliance with the principles of budgetary stability and financial sustainability contained in article 135 of the Spanish Constitution.

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Executive Summary

The aim of this report is to assess the main lines of the Local Corporations' (LC) budgets for 2018 from the viewpoint of their suitability to guarantee compliance with the budget stability and Government debt targets, as well as the year-end expenditure rule.

The evaluation has studied the probability of achieving a surplus equal to that of the previous fiscal year. It would not be of interest to evaluate the probability of achieving a stability target, traditionally fixed at equilibrium, that is known in advance to be easily achievable by the Local Corporation subsector as a whole. The AIReF has performed this analysis based on the information provided by the Ministry of Finance and Civil Service (MINHAFP) regarding the national total based on the data provided by the LCs whose population represents 77% of this total. In addition to this information, data provided by various individual LCs has been included.

The data received indicates that, in 2018, the Local Corporations can reach a surplus similar to those reached in recent years, thanks to strong guaranteed revenue from local taxes and expenses contained by the application of the spending rule. The only uncertainty present in this subsector is, precisely, the fact that compliance with this expenditure rule entails the need for a surplus beyond the one included in the annual stability target. However, in spite of its relevance, it is not possible to evaluate this since, after the 2014 modification of the order regulating the mandatory information provisions under the scope of the Organic Law of Budgetary Stability and Financial Sustainability (LOEPSF), the LCs (unlike previous years) no longer have to provide information concerning the expenditure rule during the first phases of the budget cycle. In this report, the AIReF recommends that the current rules revert to their pre-2014 state.

In its analysis, the AIReF has differentiated the largest LCs from the rest of the subsector. This is intended to reinforce the idea that the application of the LOEPSF is individual and not collective, and that each and every one of the General Government entities must comply with it, without being able to argue that the subsector as a whole is in line with the established targets.

The AIReF does not have sufficient means to analyse every one of the corporations that make up the subsector, therefore, from the outset, it has circumscribed its individual assessments to the largest corporations: 16 City Councils with a population greater than 250,000 inhabitants, 3 Provincial Councils, 1 *Cabildo* (Canary Islands Council) and 1 Island Council which are those with the largest budgets. As a whole, this group performs well in relation to the deficit and debt targets, recording surpluses that, in 2018, could reach around 1,600 million, or 9.6% of its non-financial revenue. Likewise, its debt to current revenue ratio could fall to 46%, more than 50 points below its level when the LOEPSF came into force. However, the overall contribution of this group to the subsector's surplus has fallen since 2016. This creates risk where the computable expenditure trends exceed the growth rates established by the spending rule, whose compliance is considered to be very tight for these entities in 2017. According to the closing forecasts, 8 of these 21 LCs expect non-compliance with the spending rule this year.

Regarding the stability target, the risks of non-compliance spotted in both 2017 and 2018 affect only 4 and 3 entities, respectively, and derive from the existence of an Economic and Financial Plan (EFP) and/or an Adjustment Plan (AP). As these plans have to guarantee the coherence of the fiscal rules, require a surplus in line with compliance with the expenditure rule, which had not been recognized by the time the general budgetary equilibrium target was set. It is precisely here where the dysfunctions in the application of the LOEPSF arise, to the extent that there is no agreement between the different agencies on important issues, such as what the stability target is (the general target or that committed to in the EFP/AP), if it is possible to approve an EFP that breaches a fiscal rule during the first year of validity, or if there are modifications to the EFP allowed during the years of its execution. In this report, the AIRcF recommends to approach these problems.

LOCAL CORPORATIONS	Stability Target (ST)		Expenditure Rule (ER)
	2017 year-end forecast	2018 Forecast	2017 year-end forecast
MADRID	✓	✓	✗
BARCELONA	✗	✓	✓
VALENCIA	✗	✗	✗
SEVILLA	✓	✓	✓
ZARAGOZA	✗	✓	✓
MÁLAGA	✓	✓	✓
MURCIA	✓	✗	✓
PALMA DE MALLORCA	✓	✗	✓
LAS PALMAS DE GRAN CANARIA	✓	✓	✗
BILBAO	✓	✓	✗
ALICANTE	✓	✓	✓
CÓRDOBA	✓	✓	✗
VALLADOLID	✓	✓	✓
VIGO	✓	✓	✓
GIJÓN	✓	✓	✗
L'HOSPITALET DE LLOBREGAT	✓	✓	✓
PROVINCIAL COUNCIL OF BARCELONA	✓	✓	✓
PROVINCIAL COUNCIL OF VALENCIA	✗	✓	✓
PROVINCIAL COUNCIL OF SEVILLA	✓	✓	✓
ISLAND COUNCIL OF TENERIFE	✓	✓	✗
ISLAND COUNCIL OF MALLORCA	✓	✓	✗

 Compliance
  Non-compliance

In the rest of the Local Corporations, other than the selected 21 largest, the problem is different, since in aggregate terms, they increasingly contribute to the local government subsector surplus and comply with the expenditure rule. However, when analysing the data published by the MINHAFP, it is possible to observe that in an overall positive situation, there are some Local Corporations with clear sustainability problems that manifest themselves in debt to current revenue ratios greater than 200%, negative cash balances and average payment periods widely exceeding the 30 days established in the current regulations.

The AIReF, created to ensure compliance with the principle of financial sustainability, has selected a group of 18 LCs from the group of LCs with populations greater than 20,000 inhabitants, focusing its analysis on the 9 that, according to the previous indicators and with the information received, present a more compromised situation: Jerez de la Frontera, Alcorcón, Parla, Jaén, Gandía, La Línea de la Concepción, San Andrés de Rabanedo, Totana and Navalcarnero.

Selection Criteria for City Councils with sustainability problems			
LOCAL CORPORATIONS	Debt/current revenue ratio	Average payment period	Negative cash balance (% of current revenue)
JEREZ DE LA FRONTERA	Greater than 300	More than 250 days over the legal period	NO
ALCORCÓN	Between 200-300	More than 250 days over the legal period	NO
PARLA	Greater than 300	More than 250 days over the legal period	YES: greater than 100
JAÉN	Greater than 300	More than 250 days over the legal period	YES: greater than 100
GANDÍA	Greater than 300	More than 250 days over the legal period	NO
LA LÍNEA DE LA CONCEPCIÓN	Between 200-300	Between 90-120 days over the legal period	YES: between 20-50
SAN ANDRÉS DEL RABANEDO	Greater than 300	More than 250 days over the legal period	NO
TOTANA	Between 200-300	Between 180-250 days over the legal period	YES: between 20-50
NAVALCARNERO	Greater than 300	More than 250 days over the legal period	YES: greater than 100

In these cities, the problem is very different than the one pointed out in the case of the large LCs. Here, the degree of annual compliance with the fiscal rules is of secondary importance compared to the structural and acute problem of the sustainability of their finances. For this reason, in addition to the projections on compliance with the stability targets in 2018 and 2017 and the expenditure rule in 2017, the AIReF offers comparative financial sustainability indicators that serve as a starting point to diagnose the problem in these LCs prior to the adoption of measures that could allow them to be placed on the path to sustainability in the medium term.

In this report, the AIReF makes several recommendations to the MINHAFP:

1. Establish and supervise a common framework to guarantee the homogeneous application of the LOEPSF in all LCs and throughout the country;
2. Include the expenditure rule calculations in the information that the LCs must provide on the fundamental budgetary lines, approved budgets and budgetary execution;

3. Convene and lead, for each of the City Councils of Jerez de la Frontera, Alcorcón, Parla, Jaén, Gandía, La Linea de la Concepción, San Andrés de Rabanedo, Totana and Navalcarnero, a commission of experts in line with the provisions of Articles 25.2 and 26 of the LOEPSF, with the participation of the relevant autonomous community, to analyse the causes of the sustainability problems and to propose the most appropriate solutions.

The AIRcF also recommends that the City Councils of Valencia, Murcia and Palma de Mallorca, with greater risks of non-compliance with the stability target, adapt their budgetary plans to ensure compliance by the end of 2018; and recommends that the city councils of Barcelona, Bilbao, Vigo and Gijón, with more moderate risks, adopt the necessary measures to correct possible deviations in the event of the risks occurring in 2018.

1. Object of the report, methodology, and limitations to its scope

1.1. Object of the report

The object of this report is to assess the likelihood of the main budgetary lines of the Local Corporations for 2018 to ensure compliance with the 3 fiscal rules at year-end.

For this purpose, the main budgetary lines for 2018 for the LC subsector have been analysed and, separately, given their different behaviour, budgetary weight and affected populations, the 21 largest LCs (the 16 city councils with populations greater than 250,000 inhabitants and the 5 Provincial Councils or equivalent bodies, with the greatest non-financial budgets) and the rest of the subsector.

The evaluation of the subsector has been carried out with the information on all the Local Entities provided by the Ministry of Finance and Civil Service (MINHAFP). The information on the Local Corporation subsector as a whole has been provided by the Ministry of Finance and Civil Service (MINHAFP), which incorporates the data submitted by the Local Corporations to the national data bank in compliance with the Order that establishes the duties deriving from the LEOPSF regarding the provision of information. This information, given the representativeness of the reported data, including information from almost 77% of the national population, allows the AIRcF to issue an estimate regarding the likelihood that the local subsector main budgetary lines will comply with the fiscal rules at year-end 2018. This evaluation has taken into account the execution carried out and the closing estimates for 2017 as a starting point for the following year's budgeting, as well as the main lines of the 2018 budget plans submitted by the LCs themselves to the MINHAFP in compliance with their information duties.

The AIRcF has included, as in previous reports, the individual assessment of the 16 City Councils with populations of more than 250,000 inhabitants and the 5 provincial councils or equivalent bodies with the greatest non-financial budgets. The AIRcF has performed an assessment of these entities similar to that performed in other reports for the Autonomous Regions, analysing the likelihood of compliance with the three fiscal rules: stability target, debt limit and expenditure rule at the end of 2017 and 2018. The LCs assessed were: The City Councils of Madrid, Barcelona, Valencia, Sevilla, Zaragoza, Málaga, Murcia, Palma de Mallorca, Las Palmas de Gran Canaria, Bilbao, Alicante, Córdoba, Valladolid, Vigo, Gijón and L'Hospitalet de Llobregat; the Provincial Councils of Barcelona, Valencia and Sevilla; and the Island Council of Tenerife and the Island Council of Mallorca.

This individual assessment was made chiefly on the basis of information submitted by the selected LCs, based on their 2017 performance, an estimate of the year-end close and the main budgetary lines for 2018, subsequently complemented with the information received from the MINHAFP Information Centre. All entities complied in a timely manner with the obligation to collaborate with the AIRcF.

The assessment of the rest of the LC subsector includes an analysis of the medium-term sustainability of the LCs with major structural problems. The different behaviour and situations of the medium and small LCs with respect to the large LCs demand that the evaluation of the expected compliance with the fiscal rules be performed separately. In addition, within this heterogeneous group, some LCs with financial sustainability problems have been identified, which have to be analysed with a broader and more detailed vision than that required by the evaluation of annual compliance with the aforementioned rules.

For this sustainability assessment, the AIRcF has selected the LCs with populations greater than 20,000 inhabitants that had the highest risk levels in the July report on expected compliance with the budgetary stability and public debt targets and the expenditure rule, as well as another 5 whose main sustainability ratios present values much higher than average. The AIRcF has limited this study to the 13 LCs with more than 20,000 inhabitants that presented the greatest risks in the July report, adding another 5 with very high values on one of these indicators: the level of outstanding debt to current income as an indicator of the sustainability of the financial debt, the negative cash on hand as an indicator of short-term solvency and the average period of payment to suppliers that, together with the above, warns of the existence of lags in the settlement of commercial debt¹. Trust thresholds have been set for all of them by section to rank their criticality and select those in the worst situations. These 18 City Councils have been selected: Alcorcón, Algeciras, Almonte, Aranjuez, Ayamonte, Cuenca, Gandía, Granada, Isla Cristina, Jaén, Jerez de la Frontera, La Línea de la Concepción, Navalcarnero, Parla, San Andrés del Rabanedo, Sanlúcar de Barrameda, Totana and Valdemoro.

1.2. Methodology

The AIRcF forecasts for the subsector as a whole for the different streams that make up the balances are based on all known historical data, continuously updated based on the latest information available on performance and the specific measures to be taken, taking into account the results of the AIRcF's own models for taxes, the LC financing system through State transfers and interest trends. The updated annual forecast is broken into quarterly projections, applying the same weights as assigned by the ARIMA projection for each quarter for each of these components except for the aforementioned financing system, taking into account the effect of both seasonality and the series trend. The confidence intervals are obtained in two stages. First, a VAR model is estimated for the following variables: subsector specific variables (expenditure, revenue and public debt to GDP ratio) and common variables referring to the national aggregate: Real GDP, GDP deflator and government ten-year bond yields. Second, using the projected trajectories for the different variables and forecasting the joint distribution of the VAR shocks, 1,500 probabilistic scenarios are constructed. The intervals shown are used to assess the fulfilment of the objectives according to the following probabilities:

¹ Within the principle of financial sustainability, the LOEPSF includes the debt target and the average supplier payment period (PMP).



The estimates included in the individual assessments are based on all the historical information published for each LC, as well as the unpublished information submitted by the entity itself regarding liquidated years (until 2016) and their estimates for 2017 and 2018, adjusted by the AIReF, where appropriate, taking into account the projected impact of the measures adopted and the historical trends of each item. The average values used to compare each LC with the subsector average as a whole, the average of the parent Autonomous Community, as well as its population section, have been obtained as an average of the values of each of the individual city councils where the information is available.

1.3. Limitations to the scope

There have been no relevant limitations to the scope in terms of the budgetary stability and public debt targets. On the contrary, there has been no information on the spending rule. The MINHAFP Information Centre has provided the AIReF with most of the information requested, except for the data corresponding to the business entities that are listed under Public Administrations in the national accounting and, therefore, are consolidated into the LC calculations of the stability target, debt limit and spending rule. The inclusion of this data in the AIReF forecasts on the expected compliance of the LCs with the fiscal rules by the end of 2017 and 2018 may determine variations in their conclusions, although it is estimated that it will not be particularly relevant. Moreover, information on the spending rule in 2018 has not been available as this is not part of the content of the main budgetary lines that local entities must provide to the MINHAFP in accordance with the current wording of the order that regulates the provision of information within the scope of the LOEPSF.

2. Results of the assessment

2.1. Local Corporations Subsector

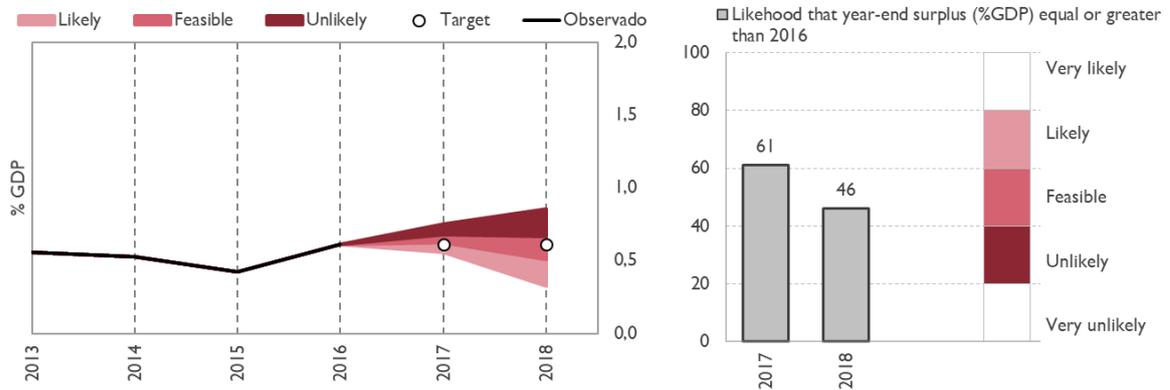
2.1.1. Budget stability target and expenditure rule

The AIReF deems it highly likely that the LC subsector will comply with the budget stability target in 2017 and 2018, it being feasible that next year the potential surplus will be similar to the 2016 surplus, around 0.6% of GDP. The information provided to the AIReF by the MINHAFP incorporates to the national total the data submitted by the entities themselves² on the 2017 performance, estimates for the close of the year, and the main budgetary lines for 2018. Based on this information, and taking into account the latest data on national accounts and financial assets and liabilities published by the IGAE and the Bank of Spain, respectively, the AIReF considers it likely that the LC Subsector will obtain a surplus similar to that of 2016, around 0.6% of GDP.

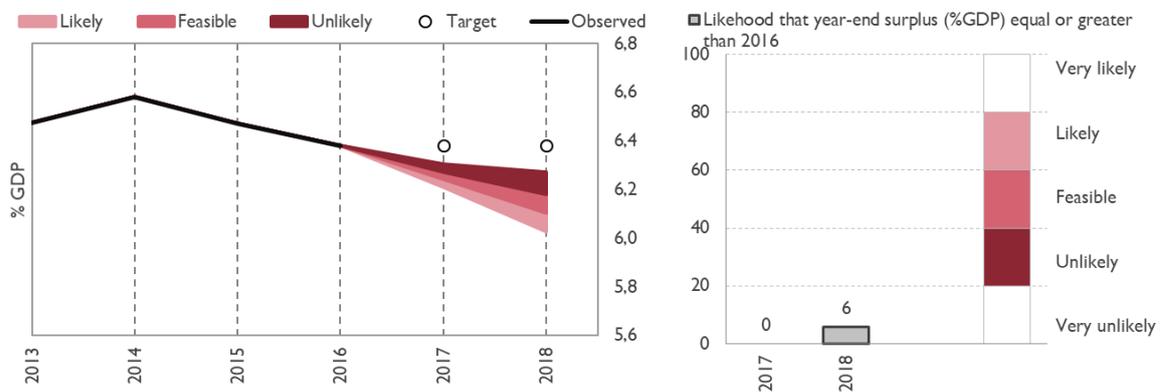
In terms of revenue, an increase of about 2% is expected in fiscal years 2017 and 2018, with growth mostly coming from increases in “other production taxes” (mainly IBI) and “value-added taxes” from the Provincial Councils. However, this increase does not compensate for the increase in GDP, which is why it is considered very unlikely that the 2016 results will be replicated in 2017 and 2018. In terms of expenditure, the AIReF forecasts a slight increase in absolute values, driven by the increase in current expenditure (average of both years about 2%) as capital decreases, although this increase does not compensate for the increase in GDP, which means that, as can be seen in figure 1 the AIReF considers it highly unlikely that 2017 and 2018 will reach 2016 levels.

² Submissions from the LCs communicated prior to 15 September of the year prior to the reference, consolidated information on the main lines of the draft budgets for the following year. Also, these submissions communicate quarterly information on performance together with estimates for year-end, with details of each entity and the consolidated result.

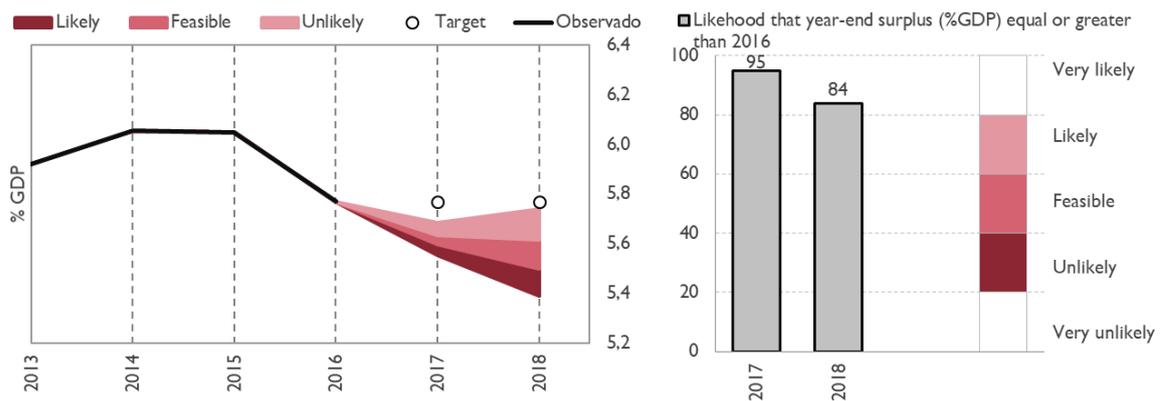
FIGURE 1. LC SUBSECTOR FINANCING CAPACITY AS % OF GDP



LC SUBSECTOR NON-FINANCIAL REVENUE AS % OF GDP



LC SUBSECTOR NON-FINANCIAL EXPENDITURE AS % OF GDP

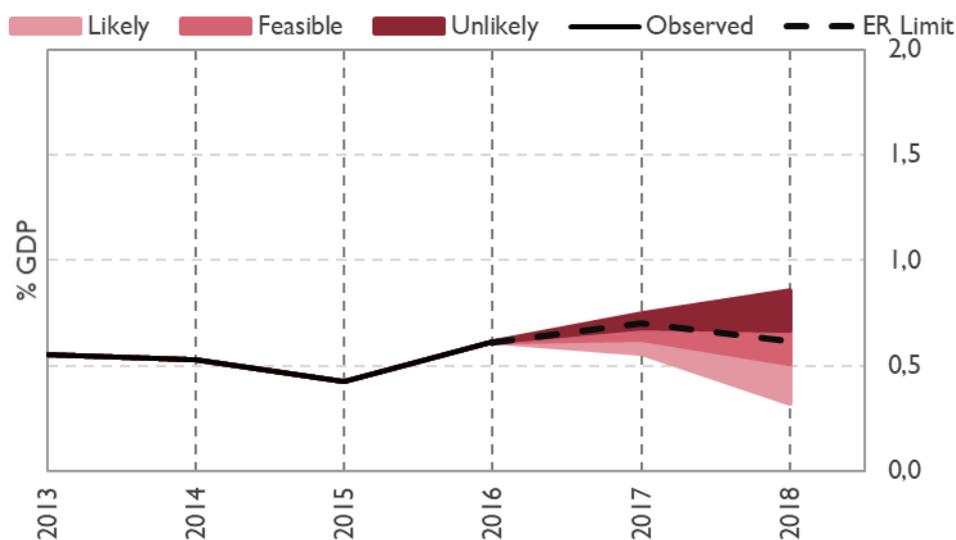


Source: MINHAFP and AIReF forecasts for 2017 and 2018.

This surplus would allow the LC subsector to comply with the spending rule in both years, albeit very tightly in 2017. The MINHAFP has not provided the requested information needed to analyse compliance with the spending rule in 2017 and 2018 at the subsector level. However, the AIReF has projected compliance with this fiscal rule based on the 2017 second quarter data published on the main components of the expenditure

rule. Given the information deficiencies, assumptions have been made about the behaviour of its components that, if not confirmed, could alter the results obtained, in particular the forecasts made for the amount of financially sustainable investments in 2018, which may vary considerably from year to year. According to these forecasts, the minimum financing capacity that would permit compliance with both fiscal rules should be around 0.6% of GDP, assuming the weight of expenses included in the same period remains constant for the year, except for the exclusions related to the financing system, interest expenses and payments to the State and the Basque Country Region by the Provincial Councils. This percentage is within the range of AIReF forecasts. See figure 2:

FIGURE 2. FINANCING CAPACITY IN THE SUBSECTOR ALLOWING COMPLIANCE WITH THE EXPENDITURE RULE

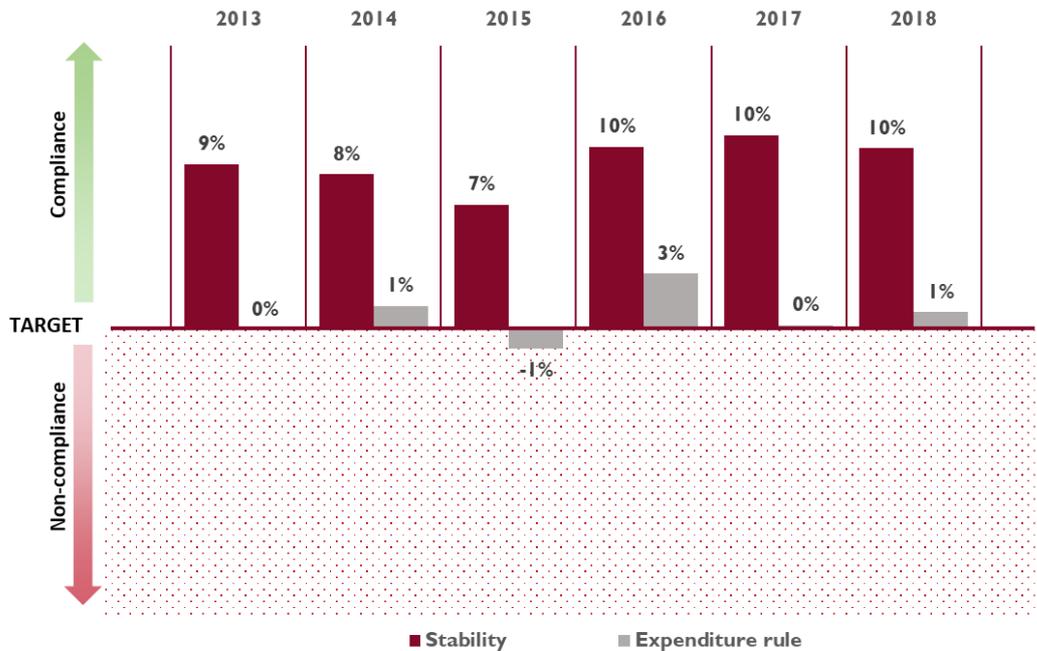


Source: MINHAFP and AIReF forecasts.

Since the entry into force of the LOEPSF, the local subsector has comfortably met the budget stability target and its expenses have been adjusted to the expenditure rule reference rate except for 2015. Since the entry into force of the LOEPSF, the LC subsector’s over-compliance with the stability target has allowed compliance with the expenditure rule every year, except for 2015, when it was breached by a narrow margin. The following factors have led to this structural surplus: greater stability of local revenues compared to those of other administrations, the moderation of spending needs as a result of the lower population growth after the crisis, the containment of spending through the application of the expenditure rule, the role of local auditors as preventive guarantors of the application of the fiscal rules and the measures contained in the law on social reform to ensure medium-term stability.

For 2017 and 2018, the AIReF estimates that exceeding the stability target would allow compliance with the expenditure rule, although very tightly. See figure 3.

FIGURE 3. COMPLIANCE WITH STABILITY TARGET AND EXPENDITURE RULE FROM 2013-2016 AND FORECASTS FOR 2017-2018



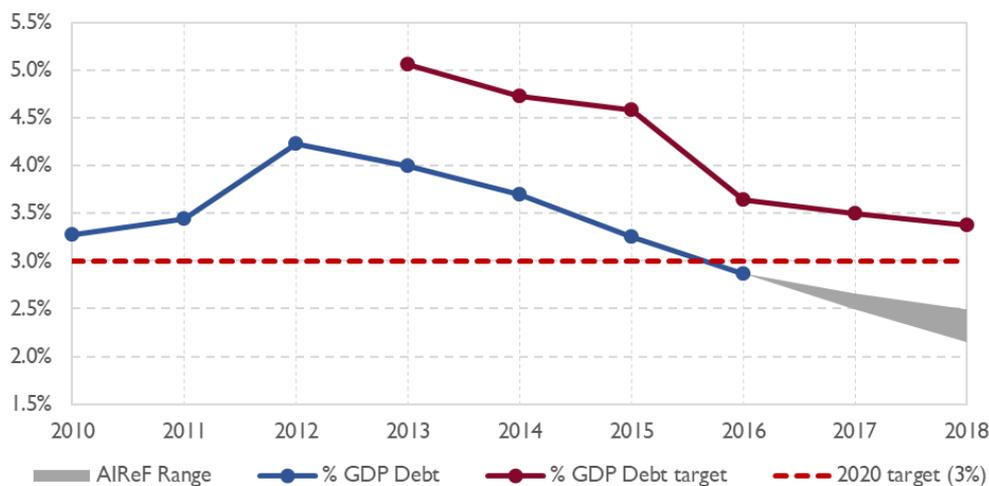
Note: Positive (compliance) or negative (breach) margin on the annual budgetary stability target and expenditure rule as a percentage of non-financial revenue and maximum computable expense, respectively.

Source: MINHAFP and AIReF forecasts

According to AIReF forecasts, in 2017 and 2018, the LC subsector could reach a debt-to-GDP level of around 2.6% and 2.3%, respectively. The LC subsector closed 2016 with a debt volume of 32,094 million euros, 2.9% of GDP, almost 9% below the 2015 level and complying, as of 2016, with the target set for 2017. The AIReF forecasts that the path to debt reduction will continue. Therefore, if the local surplus projections for 2017 and 2018 are confirmed, the local subsector outstanding debt to GDP ratio could be about 2.3% of GDP by the end of 2018.

figure 4 presents the observed live debt data trends (in % of GDP), as well as the AIReF projections for the year end 2017 and 2018 in the most favourable scenario, that is, that the surplus obtained in each year is allocated fully to debt amortization. The relative position with respect to the agreed target for the years 2013 to 2018 is also included in the graph.

FIGURE 4. DEBT IN THE SUBSECTOR (AS % OF GDP)



Note: The approved 2013-2018 targets include indebtedness deriving from extraordinary supplier payment mechanisms.

Source: Bank of Spain and AIReF projections

2.2. Individual analysis of the 21 largest LCs

The AIReF has included, as in previous reports, the individual assessment of the 16 City Councils with populations of more than 250,000 inhabitants and the 5 provincial councils or equivalent bodies with the greatest non-financial budgets, representing almost 24% of the national population and subsector expenses. In accordance with the provisions of the law ordering the AIReF's creation, the purpose of this report is to assess whether the main lines of the LC draft budgets for 2018 will allow compliance with the fiscal rules at year end. As in previous reports, similar to the treatment of the Autonomous Regions, this report includes the individual analysis of the 21 largest LCs, given the magnitude of their budgets (their expenses are almost a quarter of the whole LC subsector) and the relative population affected (almost 24% of the national total). This is based on the entities' budgetary performance during the year, the closure estimates submitted by them and the 2018 forecasts that reflect their draft budgets for the next fiscal year.

The 21 largest LCs expect to reduce their aggregate surplus by more than 25% in 2017, continuing the trend begun in 2016 with a lower contribution to the subsector surplus. In 2018, the trend could revert with the effect of the City Council of Madrid on the group. The data provided by these LEs to AIReF in April 2017 on the close of 2016 confirmed a change in their behaviour with respect to the remaining subsector entities. In 2016, while the LC subsector as a whole increased its surplus by almost 50% compared to 2015, the large city councils reduced their aggregate surplus by about 1%, which means that the rest of the LCs increased their financing capacity by more than 60%. In 2017, it is projected that this downward trend in the aggregate surplus of the large LCs will continue with respect to the 2016 results, about 26% (around 500 million euros), according to the closure forecasts provided to the AIReF from these entities.

By 2018, if the forecasts included in the main lines of the draft budgets are confirmed, this group's aggregate surplus would increase slightly (more than 3%), although this is a consequence of the weight of the City Council of Madrid, which expects to close next year with an increase in its financing capacity of 16%, while the rest of the group would continue the downward trend in their contributions to the joint surplus. See TABLE 1.

TABLE 1. VARIATION OF THE SURPLUS ADDED BY THE LARGEST LCS. (2017 AND 2018)

21 Largest Corporations							
Net Lending/Borrowing							
City Council	Importes (millones €)				% of non-financial revenue		
	Interannual variation 2017-2016(%)	2017(P)	2018(Est)	Interannual variation 2018-2017(%)	2017	2018	Variación 2018 - 2017
Alicante/Alacant	-52.2%	25	19	-26.3%	9.8%	7.5%	-2.4%
Barcelona	-94.2%	7	11	63.7%	0.2%	0.4%	0.2%
Bilbao	-362.9%	-29	4	-113.4%	-5.3%	0.7%	6.0%
Córdoba	-77.9%	16	11	-31.7%	5.5%	3.7%	-1.8%
Gijón/Xixón	-88.3%	2	5	163.0%	0.8%	2.1%	1.3%
Hospitalet de Llobregat (L')	-8.6%	34	25	-25.9%	13.8%	10.7%	-3.1%
Madrid	-21.2%	878	1,020	16.2%	17.6%	20.8%	3.2%
Málaga	3.5%	71	55	-23.0%	10.8%	8.9%	-1.9%
Murcia	-103.7%	5	23	321.1%	1.4%	5.9%	4.4%
Palma	-62.0%	18	19	3.6%	4.4%	4.6%	0.2%
Palmas de Gran Canaria (Las)	-30.0%	38	38	0.6%	10.3%	9.7%	-0.5%
Seville	44.7%	85	77	-9.7%	9.7%	8.7%	-1.0%
Valencia	-12.5%	110	79	-28.4%	13.7%	10.0%	-3.7%
Valladolid	-60.6%	11	0	-99.0%	4.0%	0.0%	-4.0%
Vigo	-56.8%	8	0	-99.8%	3.5%	0.0%	-3.5%
Zaragoza	-68.3%	35	52	49.2%	4.9%	7.1%	2.3%
Island Council of Tenerife	-22.4%	56	39	-29.8%	6.4%	4.8%	-1.6%
Island Council of Mallorca	-31.3%	47	4	-91.7%	11.6%	0.9%	-10.7%
Provincial Council of Barcelona	-7.2%	77	17	-78.0%	9.7%	2.0%	-7.7%
Provincial Council of Sevilla	-32.4%	61	99	63.4%	18.0%	29.2%	11.2%
Provincial Council of Valencia	-38.3%	18	26	41.7%	3.9%	5.4%	1.5%
Aggregate of 21 entities	-26.0%	1,573	1,622	3.1%	9.2%	9.6%	0.4%
Madrid	-21.2%	878	1,020	16.2%	17.6%	20.8%	3.2%
Other 15 city councils	-34.6%	437	417	-4.6%	4.8%	4.6%	-0.2%
Provincial and Island Councils	-24.5%	258	185	-28.5%	9.0%	6.4%	-2.6%

Source: Data provided by the City Councils and MINHAFP.

In order to assess compliance with the fiscal rules, the existence of Economic Financial Plans (EFP) and Adjustment Plans (AP) linked to extraordinary financing mechanisms have been taken into account, together with the information on the main 2018 budgetary lines submitted by the LCs and the MINHAFP Information Centre, insofar as they include tax commitments different from the general targets. In the event of non-compliance with any fiscal rule, the Plenary of each Corporation has to draft and approve a EFP, which in the case of those LCs whose Financing System, through State transfers, is the assignment model (large LCs) must be approved by the corresponding supervisory body, either the Autonomous Community, if it has assumed this competence, or if not, the MINHAFP. This plan must permit compliance with the stability and debt targets in the current year and the following year, along with the expenditure rule, with these commitments being binding for the affected administration. Similarly, in the event that an LC requests State access to extraordinary measures or additional measures to support liquidity, the MINHAFP must agree to an AP that is consistent with compliance with the

budget stability and debt targets. According to the provisions of the LOEPSF and the latest manual published by the MINHAFP to date (updated in February 2017), both shall establish the targets for the local entity, and failure to comply may result in the application of the coercive measures of Articles 25 and 26 of the LOEPSF, as established in the Law itself. Otherwise, the plans themselves would be meaningless and the measures included would be devoid of content to ensure compliance with all fiscal rules. Therefore, the stability targets included in these plans are often more demanding than the balance, in order to ensure compliance with the expenditure rule and the debt limits. This is why the AIRcF uses the commitments assumed in these EFPs or APs in all its reports.

Of the 21 LCs evaluated, 8 have EFPs approved by their supervisory agency and in force in 2017 (in 2 of them, the EFP also covers 2018), and 1, the City Council of Madrid, has exceeded the deadline for approval. In addition, 6 have APs with commitments for 2017 and 2018. The City Councils of Alicante, Barcelona, Bilbao, Málaga, Murcia, Palma de Mallorca, Zaragoza and the Provincial Council of Valencia, have EFPs in effect in 2017. Of these, Alicante, Malaga, Palma de Mallorca and Zaragoza, in addition to the city councils of Valencia and Cordoba, have Adjustment Plans with surplus and/or debt commitments for 2017 and 2018.

The City Council of Madrid, to date, does not have an EFP approved by its supervisory agency, the MINHAFP. This city council failed to comply with the expenditure rule in 2015 by a narrow margin (17 million euros). In September 2016, its Plenary approved an EFP for 2016-2017 that was not approved by the MINHAFP as it projected non-compliance with the 2016 and 2017 expenditure rules by 351 million and 224 million, respectively. The MINHAFP, applying Article 25 of the LOEPSF, required this City Council to adopt a Non-Availability Agreement barring credit operations for the amount of the 2015 breach.

In March 2017, due to non-compliance with the Expenditure Rule in 2016, the City Council approved a new 2017-2018 EFP which excluded, for the purpose of calculating the expenditure rule, amounts paid to the State and the Community of Madrid without associated financing (according to the LC). Again, this EFP was rejected by the MINHAFP, requiring a new Non-Availability Agreement barring credit operations for the amount of the 2016 breach.

On 16 October 2017, the City Council approved a new EFP that was again rejected by the MINHAFP, requiring the adoption of another Non-Availability Agreement, as well as the submission of weekly reports on its performance, instead of the quarterly reports generally required by the LOEPSF.

In the information provided by the City Council to the AIRcF, this Corporation expects to comply with the 2017 expenditure rule, taking as a starting point the expenditures made in previous years, which implies the consolidation of the excess expenditure originating from defaults in 2015 and 2016. It also projects financially sustainable investments for the year, amounting to 302 million euros.

The city councils of Barcelona and Bilbao have EFPs approved by their respective supervisory agencies which do not comply with current regulations. The City Council

of Barcelona has a valid EFP approved by the Generalitat of Catalonia which does not comply with the current regulations, as it allows non-compliance with the expenditure rule in its first year of validity, for which it projects non-compliance, after successive modifications not contemplated in the LOEPSF. The Bilbao City Council, for its part, approved its 2017 budget, although it fails to comply with the stability target, and has an EFP approved by the Provincial Council of Vizcaya, which covers this breach based on a regional standard. Both documents, the budget and the EFP, fail to comply with the provisions of article 135 of the Constitution and the LOEPSF. The AIReF has notified the MINHAFP of this but has not received any response on the matter.

In 2018, the year under evaluation in this report, out of the 21 LCs assessed, only the city councils of Murcia, Palma de Mallorca and Valencia present high risk of non-compliance with the stability target, and the city councils of Barcelona, Bilbao, Vigo and Gijón present moderate risk. The purpose of this report is to assess the likelihood that the LC budgetary lines for 2018 will comply with the fiscal rules at year end. It has only been possible to assess the likelihood of compliance with the stability and debt targets, and not the expenditure rule, which is the most demanding in these entities with consolidated surpluses and debt ratios generally below the legal limits. This is because the obligation to communicate the calculation of this rule in the initial phases of the budget cycle was eliminated following the 2014 modification of the development order of the LOEPSF's information obligations, which risks compliance at year end.

However, the closure forecasts provided together with the main lines of the 2018 budgets present risk of non-compliance with at least one of the fiscal rules in 2017 in all LCs assessed, except for Seville, Alicante and Vigo. The 2018 assessment begins with the 2017 performance and closure forecasts as the starting point for budgeting the following year. In this year, the AIReF projects that only the city councils of Alicante, Vigo and Seville present no risk of non-compliance with any fiscal rule, although Seville only complies with the 2017 expenditure rule as a result of the consolidation of expenditure made above the limit allowed by the spending rule in previous years.

The following tables present the projections for each LC regarding compliance with the stability target and the expenditure rule in 2017 and 2018, as well as the AIReF's conclusions for each of them.

Table 2 summarizes the situation of each LC with respect to compliance with the stability target and expenditure rule at the end of 2017 and the projected compliance with the stability target in the 2018 main budgetary lines, indicating whether there have been changes with the new information available regarding the assessment made in the report on the projected compliance with the stability and public debt targets and the expenditure rule in 2017³.

Table 3 summarizes the AIReF's main conclusions with respect to the 2017 and 2018 closure forecasts of each LC and each fiscal rule. In this table, the risk of non-compliance

³ [Report on compliance with the 2017 budget stability and debt targets and the expenditure rule by the different public administrations](#)

with one or more fiscal rules is ranked into five possible situations, from no appreciable risk of non-compliance to very high risk of non-compliance with respect to 2017.

Figure 5 presents a comparative view of these large LCs in terms of compliance with the stability target and the expenditure rule at the end of 2017, according to the data provided by the entities, as well as the AIRcF's projections for compliance at the end of this year with the stability target and the expenditure rule in the event that this forecast changes their meaning. Figure 6 presents a comparative view of compliance with the 2018 stability target according to the information provided by the LCs based on the main budgetary lines for 2018, as well as the AIRcF's forecasts for next year.

The above graphs present their results in terms of the margin over the respective target or rule and include the average performance of the group, which is highly influenced by the weight of the City Council of Madrid. Compliance, or lack thereof, with the stability target and the expenditure rule is presented as percentages above or below the target (the legal target or that established by the approved EFP or AP) for each of them. In relation to the stability target, this margin is calculated as a percentage of non-financial revenue. In relation to the expenditure rule, this margin is calculated as the expenditure limit that permits compliance.

According to these graphs, in 2017, the group's average performance ended the year complying with the stability target, about 7% over the average target. This margin is not sufficient to ensure compliance with the expenditure rule, since on average, the computable expense exceeds the expenditure limit by 1%. Moreover, in 2018, the group average is projected to comply with the stability target with a margin of around 8%. Regarding the expenditure rule, since there is no information available for 2018, it is not known if this margin would guarantee compliance with the expenditure rule next year.

Graph 7 presents the debt limit trends (ratio to current revenue) from 2012 to 2016 and the LC forecasts for the 2017-2018 period. This group has made significant efforts to reduce its debt since the entry into force of the LEPSF in 2012 until 2016. On average, the group has gone from 100% of average revenues to just 59%. This trend is expected to continue this year, with the group's average debt ratio sitting at about 46%.

TABLE 2. COMPARED OVERVIEW OF COMPLIANCE WITH THE STABILITY TARGET AND THE EXPENDITURE RULE BY THE LOCAL CORPORATIONS STUDIED (2017 AND 2018)

LOCAL CORPORATIONS	ECONOMIC FINANCIAL PLAN (EFP) and/or ADJUSTMENT PLAN (AP) APPROVED AND IN FORCE		Stability Target (OE)		Expenditure Rule (RG)
	ECONOMIC FINANCIAL PLAN	ADJUSTMENT PLAN	2017 year-end	2018 forecast	2017 year-end
MADRID	Non-compliance with RG15. 3 EFP'S 16-17 presented but not approved		✓	✓	✗
BARCELONA	EFP for non-compliance with RG15 approved for 15-16. Revised for prior non-compliance in 16. New EFP 16-17.		✗	✓	✓
VALENCIA		AP 2012 with surplus and debt commitments until at least 2022	✗	✗	✗
SEVILLA			✓	✓	✓
ZARAGOZA	EFP for non-compliance with RG15 approved for 16-17	AP 2012 with surplus and debt commitments until at least 2022	✗	✓	✓
MÁLAGA	EFP for non-compliance with RG15 approved for 16-17	AP 2013 with surplus commitments until 2017 and debt commitments until 2020	✓	✓	✓
MURCIA	EFP for non-compliance with OE and RG16 approved for 17-18		✓	✗	✓
PALMA DE MALLORCA	EFP for non-compliance with RG15 approved for 16-17	AP 2012 with surplus and debt commitments until at least 2022	✓	✗	✓
LAS PALMAS DE GRAN CANARIA			✓	✓	✗
BILBAO (*)	EFP approved by the Provincial Council in approving the 2017 budget with a deficit, noncompliance with the LEOPSF. In effect for 17-18.		✓	✓	✗
ALICANTE	EFP for non-compliance with RG15 approved for 16-17	AP (approval date not provided) with surplus and debt commitments for 2017	✓	✓	✓
CÓRDOBA		Debt refinancing plan 16 with surplus commitments in 2017	✓	✓	✗
VALLADOLID			✓	✓	✓
VIGO			✓	✓	✓
GIJÓN			✓	✓	✗
L'HOSPITALET DE LLOBREGAT			✓	✓	✓
Provincial Council of Barcelona			✓	✓	✓
Provincial Council of Valencia	EFP for non-compliance with RG15 approved for 16-17		✗	✓	✓
Provincial Council of Seville			✓	✓	✓
Island Council of Tenerife			✓	✓	✗
Island Council of Mallorca			✓	✓	✗



Compliance



Non-compliance



The measure of compliance with the targets was made in accordance with an EFP not adjusted to the LOEPSF



With changes compared to July (report on projected compliance with 2017 targets)

TABLE 3. MAIN AIREF CONCLUSIONS ON RISKS OF NON-COMPLIANCE WITH 2017 AND 2018 FISCAL RULES OF THE 21 LARGEST LOCAL CORPORATIONS

No risk of non-compliance with any fiscal rule	OE: Stability target
Low risk with possibility of correction during year	RG: Expenditure rule
Moderate risk of non-compliance with any fiscal rule	RD: Debt over consolidated current revenues ratio
High risk and/or reiterated non-compliance with any fiscal rule	PEF: Economic and financial plan
Very high risk and/or reiterated non-compliance with any fiscal rule	PA: Adjustment Plan

ENTITIES WITH VERY HIGH RISK OR REITERATED NON-COMPLIANCE WITH ANY FISCAL RULE

LOCAL CORPORATIONS	AIREF CONCLUSIONS ON COMPLIANCE WITH 2017-2018 FISCAL RULES
MADRID	<ul style="list-style-type: none"> · OE: The City Council projects a surplus at the end of 2017 14% lower than in 2016 (in the July forecast, they projected a drop of 39%) and 37% lower than in 2015. In 2018, they project to reach a surplus similar to 2016. The verification of compliance with the OE in both years will be carried out in accordance with the commitments established by the EFP pending approval · RG: It projects compliance with the RG in 2017, but only as a result of having consolidated the excess expenses from 2015 and 2016. If the excesses are not consolidated, it would be in default by more than 250 million. In the July forecast, Madrid projected an expenditure excess that doubled that of 2016. The fundamental differences in the 2017 forecasts of both dates is due to the increase now projected in financial sustainable investments, now 8 times higher, without increasing capital expenses. · RD: There is projected an RD at the end of 2017 of 70% and 62% at the end of 2018. If they meet their forecasts as of 2017, the city council would no longer need credit authorization.
BILBAO	<ul style="list-style-type: none"> · OE: The City Council expects to comply with the 2017 OE with a deficit authorized by the EFP. It expects to comply with the 2018 OE established in the EFP with a surplus of 24% of what it had in 2016 (the last year with a surplus). The AIREF appreciates some risk of non-compliance given the low margin and the revenue and expenditure trends. · RG: Projects non-compliance with the RG target for 2017 established in the EFP · RD: Maintains a debt to current revenue ratio very close to zero.

ENTITIES WITH HIGH RISK OR REITERATED NON-COMPLIANCE WITH ANY FISCAL RULE

LOCAL CORPORATIONS	AIREF CONCLUSIONS ON COMPLIANCE WITH 2017-2018 FISCAL RULES
BARCELONA	<ul style="list-style-type: none"> · OE: The City Council projects compliance with the 2018 OE with a financing capacity that is 10% of that in 2016 (with no 2018 EFP in place, the 2018 OE would be 0). The AIREF projects that there is a certain risk of non-compliance. On the other hand, the City projects non-compliance with the 2017 OE foreseen in the EFP when estimating a financing capacity of 5% over the one included in the EFP. · RG: Projects compliance with the 2017 RG included in the EFP, although it will be tight. · RD: Maintains a debt to current revenue ratio of about 30%.
VALENCIA	<ul style="list-style-type: none"> · OE: The City Council projects non-compliance with the OE commitments for 2018 and the close of 2017 included in the PA. In 2018, the surplus projected by the City Council is 37% lower than that committed to. · RG: Projected non-compliance with the 2017 RG with expenditure 2% over the limit. · RD: In 2018, the Council projects a debt ratio of less than 72%, 10 percentage points below the 2017 forecast. However, they will not comply with the debt limits established in the AP for 2017 and 2018. If they met their forecasts, they would no longer need credit authorization.
PROVINCIAL COUNCIL OF VALENCIA	<ul style="list-style-type: none"> · OE: Projects non-compliance with the OE established in the EFP at year-end 2017, with a capacity close to 50% of that required. They expect to reach the 2018 OE by increasing the projected 2017 surplus by 42% · RG: Projects compliance with the RG included in the EFP at year-end 2017, although as a result of the consolidation of the excess expenditure from 2015. · RD: Maintains a debt ratio around 35%, projecting to decrease to 29% by the end of 2018.

ENTITIES WITH MODERATE RISK OF NON-COMPLIANCE WITH ANY FISCAL RULE

LOCAL CORPORATIONS	AIREF CONCLUSIONS ON COMPLIANCE WITH 2017-2018 FISCAL RULES
PALMA DE MALLORCA	<ul style="list-style-type: none"> · OE: The City Council projects non-compliance with the 2018 OE established in the AP with a surplus of 44% of that required. It is expected to comply with the 2017 surplus commitments established in the EFP and the AP. · RG: Projects compliance with the 2017 RG target established in the EFP. · RD: Its RD is less than 75%, predicting that it will reach 64% by year-end 2018, but it will not meet its AP targets in 2017 or 2018.
ZARAGOZA	<ul style="list-style-type: none"> · OE: Projects non-compliance with the EFP OE at year-end 2017, with an expected surplus of just 64% of that included in the EFP (at the end of 2016, it had a surplus 80% higher than that included in the EFP). Projects compliance with the 2018 OE with a surplus 86% higher than the AP target. · RG: Will comply with the RG target included in the EFP at the end of 2017. · RD: Has maintained an RD above 110% since at least 2012. This ratio increased after 2015 due to the loan for the construction of the city's tram. For this reason, the city fails to meet the AP targets for all years since 2015.
ISLAND COUNCIL OF TENERIFE	<ul style="list-style-type: none"> · OE: Projects compliance with OE at end of 2017, although with a surplus lower than that projected in July. Also projects compliance with the 2018 OE. · RG: Projects non-compliance with the RG at year-end 2017 by an amount much higher than projected in July. Consequently, they project a 9% growth in expenditure with respect to the July notification. · RD: Maintains a RD of about 40%, projected to reach 30% by year-end 2018.
ISLAND COUNCIL OF MALLORCA	<ul style="list-style-type: none"> · OE: Projects compliance with the 2017 and 2018 stability targets, although with surpluses 32% lower than the 2016 figures in 2017 and 94% lower in 2018. · RG: Projects non-compliance with the RG at year-end 2017 with expenditure 11% over the limit (excess expenditure is slightly lower than that predicted in July). · RD: Maintains an RD of less than 75%, projecting a substantial reduction in the 2016 debt, from 32% to 6% by the end of 2017 and 5% by the end of 2018.

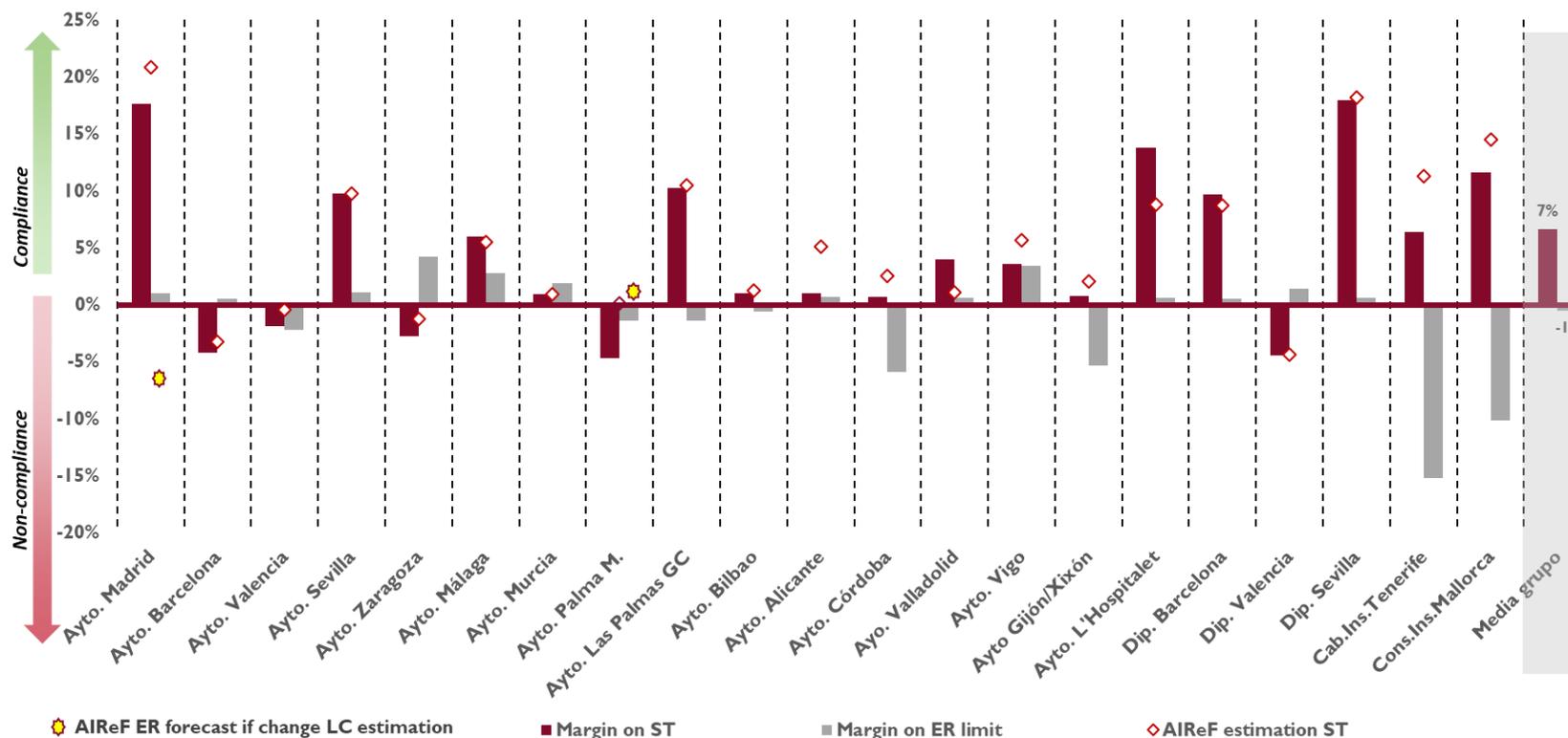
ENTITIES WITH LOW RISK OF NON-COMPLIANCE WITH ANY FISCAL RULE WITH POSSIBILITY OF CORRECTION DURING THE YEAR

LOCAL CORPORATIONS	AIREF CONCLUSIONS ON COMPLIANCE WITH 2017-2018 FISCAL RULES
MÁLAGA	<ul style="list-style-type: none"> · OE: Projects compliance with the 2018 OE. Also projects compliance with the stability commitments established in both the EFP and the AP. · RG: Also projects compliance with the computable expenditure limit included in the EFP. · RD: Maintains a debt ratio of over 75% and less than 110%, although the City projects to end 2018 at about 77%. The projected debts levels for year-end 2017 and 2018 meet the commitments included in the AP.
MURCIA	<ul style="list-style-type: none"> · OE: Projects non-compliance with the 2018 surplus commitment established in the EFP, but in an adjusted manner. In 2017, very tight compliance is projected. · RG: Projects compliance with the 2017 RG established in the EFP · RD: Prior to 2016, it maintained a debt ratio of less than 75%. In 2016, due to the loan for the tram, its ratio increased to 100%. It is projected to end 2017 at about 91% and end 2018 at about 80%.
LAS PALMAS DE GRAN CANARIA	<ul style="list-style-type: none"> · OE: Projects compliance with the 2017 and 2018 OEs, although with surpluses at 70% of those projected in recent years. · RG: Projects non-compliance with the 2017 RD as a result of a lower valuation of the revenue · RD: Maintains a RD much lower than 75%, which they expect will be reduced considerably, going
VALLADOLID	<ul style="list-style-type: none"> · OE: The City Council projects compliance with the EO at year-end 2017, although with a surplus of 39%, as in 2016. It also projects compliance with the 2018 OE with a surplus very close to the balance as a result of projected current expenditure increases close to 9% while revenue will only increase 2%. · RG: Projects compliance with the RG at year-end 2017, although it will be tight, as a consequence of significant growth in projected financially sustainable investments (5% of 2017 expenditure when they were just 1% in 2016) · RD: Maintains a RD lower than 75%. The 2017 year-end forecast will be around 36%, projecting an increase to 41% by the end of 2018.
L'HOSPITALET DE LLOBREGAT	<ul style="list-style-type: none"> · OE: Projects compliance with the OE at year-end 2017 and 2018 · RG: Projects compliance with the RG at year-end 2017, although it will be tight. The July information has varied, now including the financially sustainable investments (accounting for 11% of expenditure) · RD: Maintains a RD of around 40%, projected to decrease to 33% by the end of 2018.
PROVINCIAL COUNCIL OF BARCELONA	<ul style="list-style-type: none"> · OE: Projects compliance with the OE at year-end 2017 and 2018, although the surplus will drop 78% this year. · RG: Projects compliance with the RG at year-end 2017, although it will be tight. Compared to the July projections, which did not expect to comply with the RG, expenditure has been reduced in order to comply. · RD: Maintains an RD of about 20% that they intend to reduce 13% by the end of 2018.
CÓRDOBA	<ul style="list-style-type: none"> · OE: The City Council projects to comply with its surplus commitments for year-end 2017 established in the debt refinancing plan it signed. The 2018 OE is also expected to be met, although with a 33% decrease from the 2017 projections. · RG: It continues to project non-compliance with the RG at year-end 2017, as it had in July, although it has already reduced expenditure, albeit by a lower amount than planned. · RD: The City Council plans to reduce the RD from 76% in 2016 to 74% at year-end 2017 and to 69% at year-end 2018. If it meets its forecasts, it would no longer need credit authorization.
GIJÓN	<ul style="list-style-type: none"> · OE: Projects compliance with the OE by the end of 2018, although it will be tight, with a 70% drop in its surplus (the 2016 surplus was already 50% lower than previous years). The AIReF projects some risk of compliance. It also projects compliance with the 2017 OE, with a drop of more than 80% from the 2016 level. · RG: Projects non-compliance with the RG at year-end 2017 given computable expenditure growth forecasts of 8%. · RD: Maintains an RD of about 50%.
PROVINCIAL COUNCIL OF SEVILLE	<ul style="list-style-type: none"> · OE: Projects compliance with the 2017 and 2018 OEs. · RG: Projects compliance with the RG at year-end 2017 although it will be tight. · RD: Maintains a debt ratio of about 20%, projected to end 2018 at about 18%.

ENTITIES WITH NO RISK OF NON-COMPLIANCE WITH ANY FISCAL RULE

LOCAL CORPORATIONS	AIREF CONCLUSIONS ON COMPLIANCE WITH 2017-2018 FISCAL RULES
SEVILLA	<ul style="list-style-type: none"> · OE: Projects compliance with the 2018 OE. Also projects compliance with the 2017 OE. In both cases, the projected surpluses are more than 50% higher than the previous closed fiscal year. · RG: Projects compliance with the RG at close of 2017, although tight, as a result of having consolidated the 2016 RD non-compliance. · RD: Since 2009, it has maintained a debt ratio under 75% of current revenue.
ALICANTE	<ul style="list-style-type: none"> · OE: Projects compliance with the OE included in the EFP and in the AP at close of 2017. Also projects compliance with the 2018 OE, but with a 26% reduction compared to the end of 2017. · RG: Also projects compliance with the EFP computable expenditure limit, although with a very low margin (2% of the previous year and 4% of the July projections). · RD: Maintains a RD of less than 75%. The forecast for the end of 2017 will be about 33%, in compliance with the limit committed to in the AP with plans to reduce this ratio to 27% in 2018.
VIGO	<ul style="list-style-type: none"> · OE: Projects compliance with OE at end of 2017 although with a decrease from the 2016 surplus of 57%. Projects compliance with the 2018 OE, but with some risk, with a 100% drop from the 2017 levels. · RG: Projects compliance with the RG at close of 2017. · RD: Expects to continue being debt-free at the end of 2017 and 2018

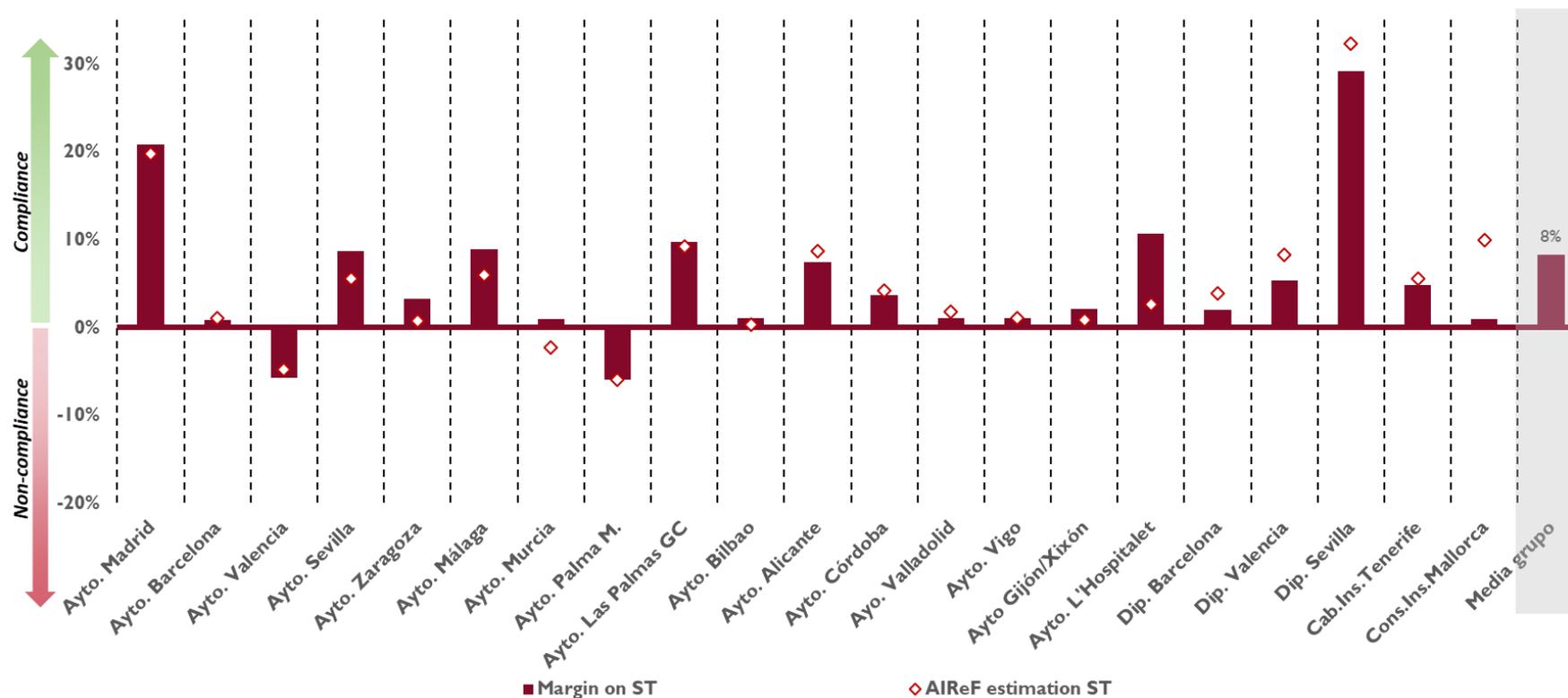
FIGURE 5. 21 LARGEST LCS. PROJECTED DEGREE OF COMPLIANCE WITH THE STABILITY TARGET AND EXPENDITURE RULE IN 2017



Note:

Margin over Stability Target (OE): Difference between net spending/borrowing projected at year-end 2017 and the target as a percentage of non-financial revenue.
 Margin over Expenditure Rule (RG) limit: Difference between the computable expense projected in 2017 and the limit of the RG as a percentage over the indicated limit.

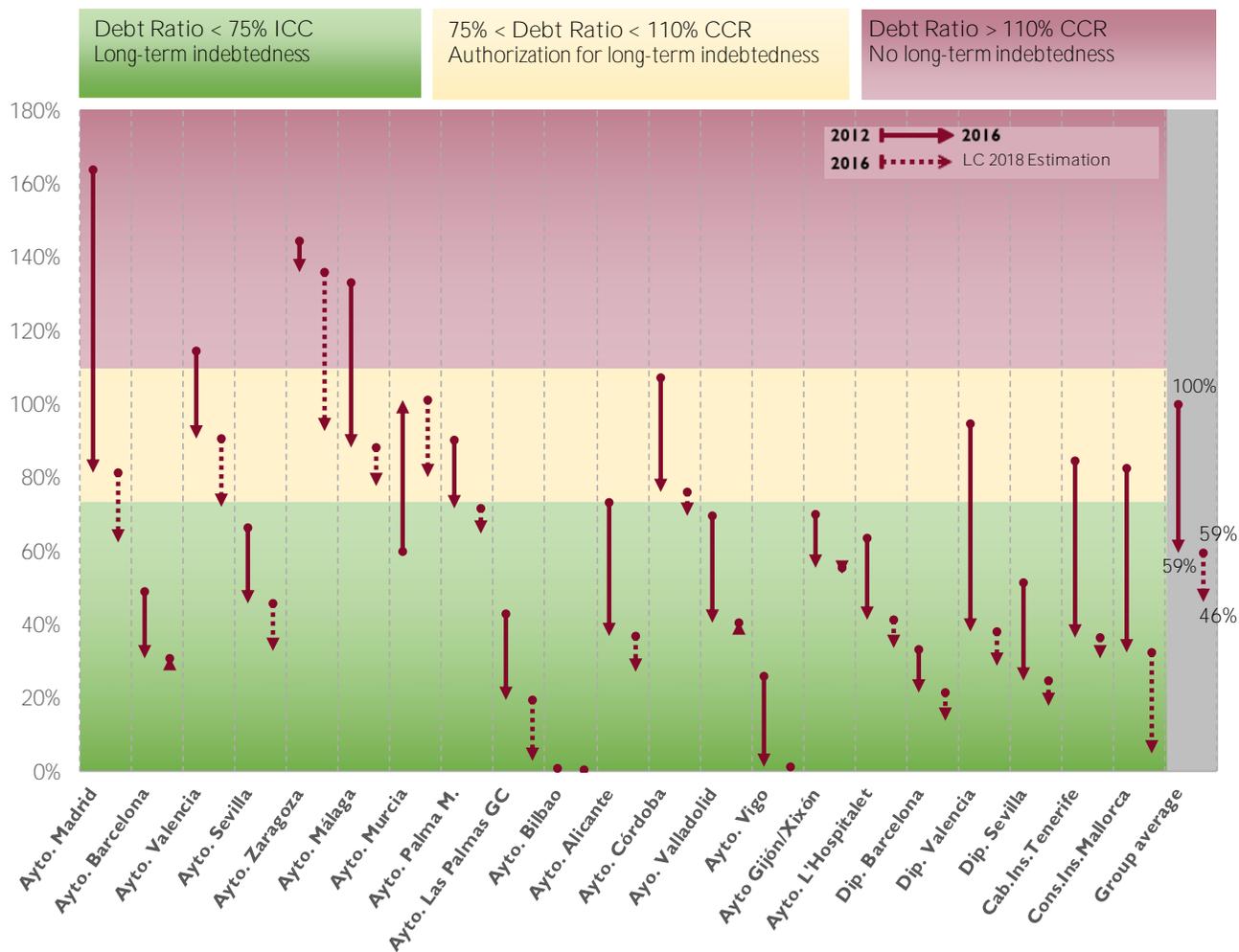
FIGURE 6. 21 LARGEST LCS. PROJECTED DEGREE OF COMPLIANCE WITH THE STABILITY TARGET AND EXPENDITURE RULE IN 2018



Note:

Margin over OE: Difference between net spending/borrowing projected in the 2018 main budgetary lines and the target as a percentage of non-financial revenue.

FIGURE 7. 21 LARGEST LCS. OUTSTANDING DEBT 2012-2016 AND FORECAST FOR 2017-2018
(PERCENTAGE OF DEBT OVER CONSOLIDATED CURRENT REVENUE (CCR))





2.3. Analysis of the rest of the LC subsector

It is estimated that in 2018 and 2017, this group of small and medium LCs will continue to make positive contributions to the Local subsector surplus. According to the IGAE publication of April 2017 on the Public Administration's fourth quarter 2016, while the LC group increased its surplus by 40% compared to 2015, the large City Councils reduced it by around 1%. In 2017, if the forecasts provided by the 21 largest LCs are confirmed and the surplus continues to reduce, 25% below the 2016 figures, the small and medium cities would need to contribute the same surplus to maintain the overall results, although to a lesser extent than in 2016 as the financing capacity of the largest LCs has decreased. By the end of 2018, if the forecasts included in the main lines of the draft budgets of the largest LCs are confirmed, the 2017 trends will continue.

In terms of the debt, the group of small and medium LCs is responsible for more than 70% of the global subsector debt (around 2% of GDP). This group of LCs represent almost 75% of total LC expenditure and their policies affect more than 70% of the national population. The group is characterized by its great breadth and heterogeneity, since it includes not only 8,112 LCs out of the 8,124 that exist but also most of the rest of the LEs within the supra or infra-local scope with different competences and financing systems. In net terms, this group of LCs follows the subsector's debt reduction trend started in 2012.

Despite the favourable net results of the small and medium LC group, there are individual situations with sustainability problems. The AIReF has been working since December 2016 on the individuality of the application of the LOEPSF and, therefore, on the need to shine light on the situation of those LEs where it is not sufficient to simply verify compliance with certain annual rules, since these rules, by themselves do not guarantee their future sustainability given their starting situation.

For this reason, in its December 2016 report, the AIReF made clear the need to deepen the analysis of the LC sustainability, including in its individual assessment of those LEs with recurrent negative indicators in this matter, which reveal the existence of structural problems. In the individualized analysis of the LCs carried out by AIReF, the group of evaluated LEs has been successively expanded, including not only the group of agents formed by those largest LCs, with larger budgets and populations, for which the AIReF performs a detailed analysis, but also to another group of entities with sustainability problems in the medium term which present very high negative indicators in their main ratios.

At the end of 2016, during the analysis of entities with sustainability risks, the AIReF began by conducting a first assessment of the criticality of the LEs in terms of debt, identifying 90 with problems placing them within the 75% limit of the ICC in a period less than 20 years and rating their situation.

Later, in the July 2017 report, the AIReF extended this analysis to the 32 city councils with more than 5,000 inhabitants with negative results in some relevant economic-financial indicator. These indicators included, in addition to the debt to current income ratio (the preferred indicator), negative non-financial budget balance, negative cash surplus, average



payment period above the legal limits, and non-compliance with the supply of information obligations.

This report takes another step forward in the LC sustainability analysis in the medium term, limiting the assessment to those LEs with major structural problems. In this report, the AIReF focuses the LC sustainability analysis on the structural problems, therefore the assessment is not limited to compliance with the fiscal rules in a given year, but focused mainly on the analysis of the elements that determine their risk in terms of sustainability in the medium and long term. The goal is to go deeper in the future in the work carried out by the various competent bodies in implementing correction measures (the Corporation itself, the financial supervisory body and/or MINHAFP in its power to approve and monitor adjustment plans).

The AIReF has selected for this sustainability assessment those LCs with more than 20,000 inhabitants that were rated with the highest risk in the July report and another 5 whose main structural financial and commercial sustainability ratios have values much higher than the average. In this report, the AIReF has limited the study to those LCs with sustainability problems with a certain population size (greater than 20,000 inhabitants) that were rated with the greatest risk in the July report. 13 entities, and another 5 entities that represent higher values in a structural sustainability indicator.

The indicators considered for the selection of the entities included: the level of outstanding debt over current revenue as an indicator of the sustainability of the financial debt; the negative cash surplus as an indicator of short-term solvency; and the average payment periods to suppliers as a warning of delinquency in commercial debt. For all these indicators, trust thresholds have been set, in order to rate the critical situation of each LC and select only those in the worst situations. The following 18 City Councils were selected: Alcorcón, Algeciras, Almonte, Aranjuez, Ayamonte, Cuenca, Gandía, Granada, Isla Cristina, Jaén, Jerez de la Frontera, La Línea de la Concepción, Navalcarnero, Parla, San Andrés del Rabanedo, Sanlúcar de Barrameda, Totana and Valdemoro. The criteria by which they have been selected and their level in each of the indicators in the last settlement (2016) are presented in Table 4 below.

The AIReF has requested the necessary information to assess the medium-term sustainability of the affected City Councils and from the MINHAFP Information Centre. All those listed above have complied with the duty to collaborate, except for Ayamonte. The AIReF has performed the analysis based on the historical information of each LE since at least 2012 (the year of the LOEPSF's entry into force), quarterly performance and the closing forecasts available for this year submitted to the MINHAFP, as well as the information on the fundamental budgetary lines for 2018 reported by each City Council. All except Ayamonte have complied with the duty to collaborate with the AIReF. Almost a month after the initial request, a written request for information was sent to the aforementioned city council, in which it was notified that failure to comply with the duty to cooperate could give rise to the warning provided in article 4.3 of Organic Law 6/2013. No response was received. This led to the publication on the AIReF website of a warning for breach of the duty to cooperate, according to the aforementioned procedure.



TABLE 4. SELECTION CRITERIA FOR CITY COUNCILS WITH STRUCTURAL PROBLEMS. (2016 SETTLEMENT DATA)

Criteria for selecting city councils with structural problems			
City Council	Debt/Current Revenue ratio	Average payment period	Negative cash balance (% of current revenue)
Granada	75-110	90-120	20-50
Jerez de la Frontera	>300	>250	
Alcorcón	200-300	>250	
Parla	>300	>250	>100
Algeciras	150-200	>250	
Jaen	>300	>250	>100
Gandia	>300	>250	
Valdemoro	150-200	>250	50-75
Sanlucar de Barrameda	75-110	60-90	>100
Línea de la Concepción (La)	200-300	90-120	20-50
Aranjuez	110-150	>250	75-100
Cuenca	110-150	60-90	
San Andrés del Rabanedo	>300	>250	
Totana	200-300	180-250	20-50
Navalcarnero	>300	>250	>100
Almonte	75-110	120-180	
Isla Cristina	110-150	>250	50-75
Ayamonte	150-200	>250	

Figure 8 below presents a comparative look at the main conclusions about the net liability position (level of financial debt and negative cash surplus, both as a percentage of current income) upon the LOEPSF's entry into force in 2012, and the last settled fiscal year, 2016, for the 18 LEs selected, as well as the improvement efforts made during the period.

On the other hand, Figure 9 presents a comparative look at compliance with the stability target at year-end 2017 and 2018, according to the information provided by the LE, as well as the AIRcF projections for 2017. Compliance (or not) is shown as the percentage of their non-financial revenue over or under the target (the legal target or that established in the approved EFP in each case).

Figure 10 presents, with respect to the debt limit (ratio over current revenues), the trends from 2012 to 2016 and the AIRcF forecasts for the 2017-2018 period. Most of the City Councils in this group have increased their debt ratio between 2012 and 2016.

FIGURE 8. NET LIABILITY POSITION OF THE 19 LOCAL ENTITIES WITH STRUCTURAL PROBLEMS (% OVER CURRENT CONSOLIDATED REVENUE)

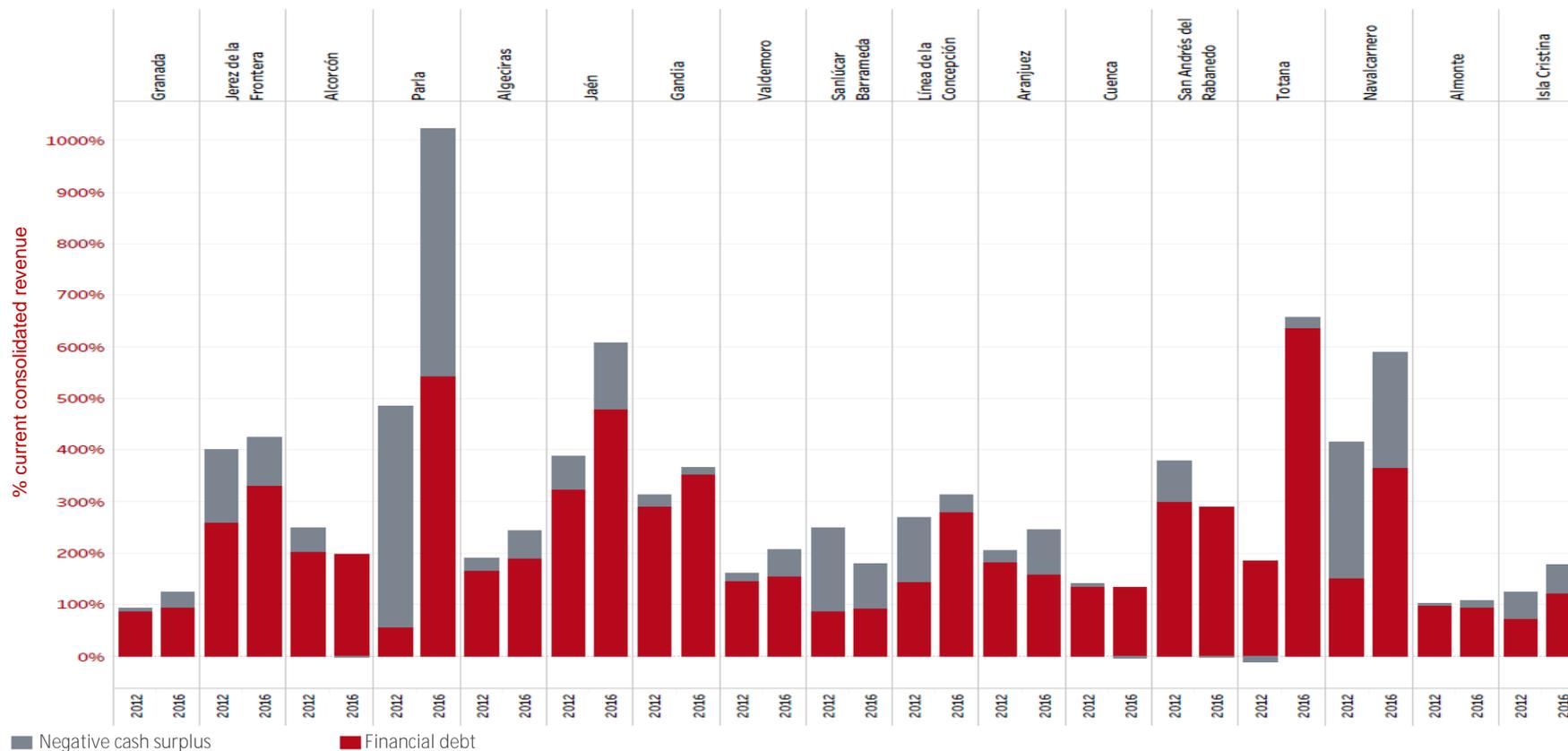


FIGURE 9. 18 LOCAL ENTITIES WITH STRUCTURAL PROBLEMS. ESTIMATION OF DEGREE OF COMPLIANCE WITH THE STABILITY TARGET IN 2017 AND 2018 (% NON-FINANCIAL REVENUE)

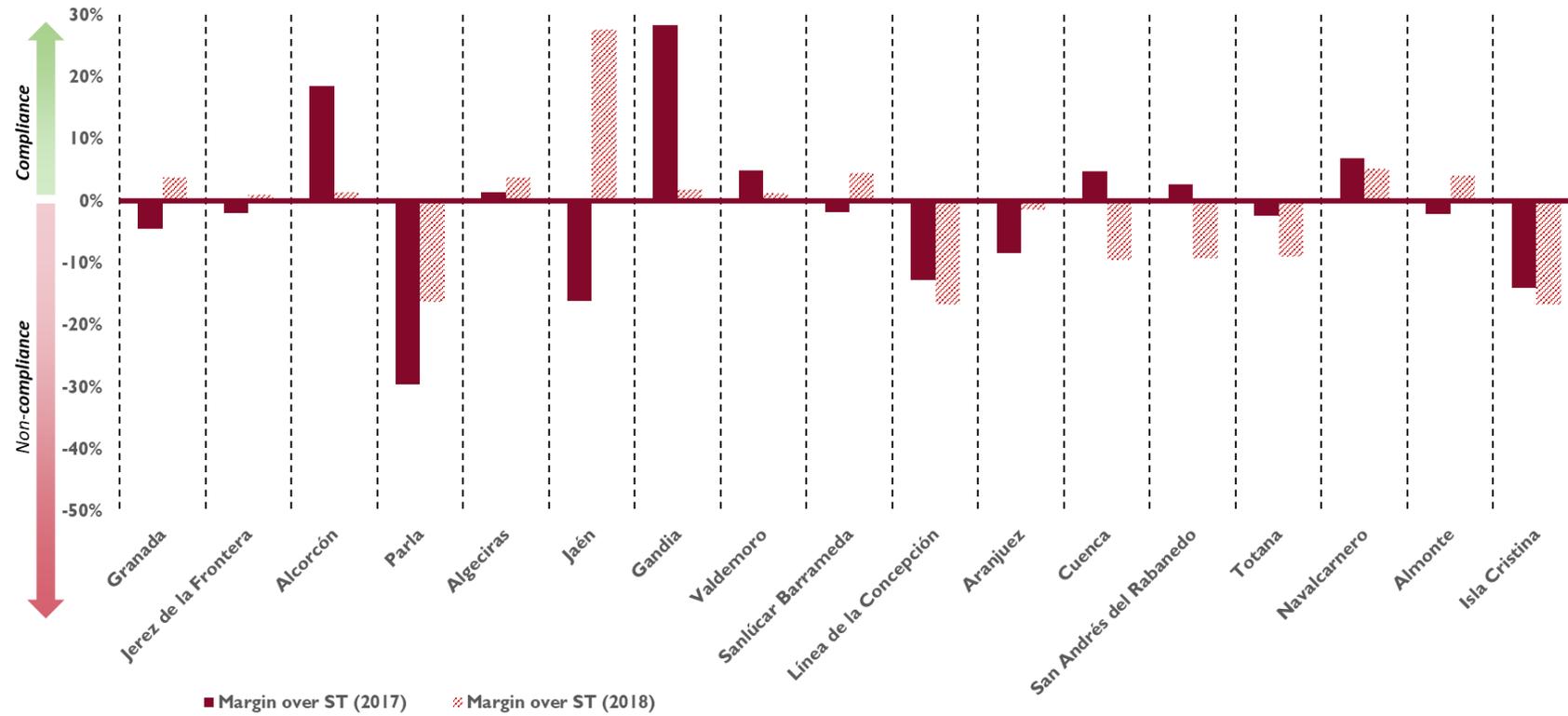
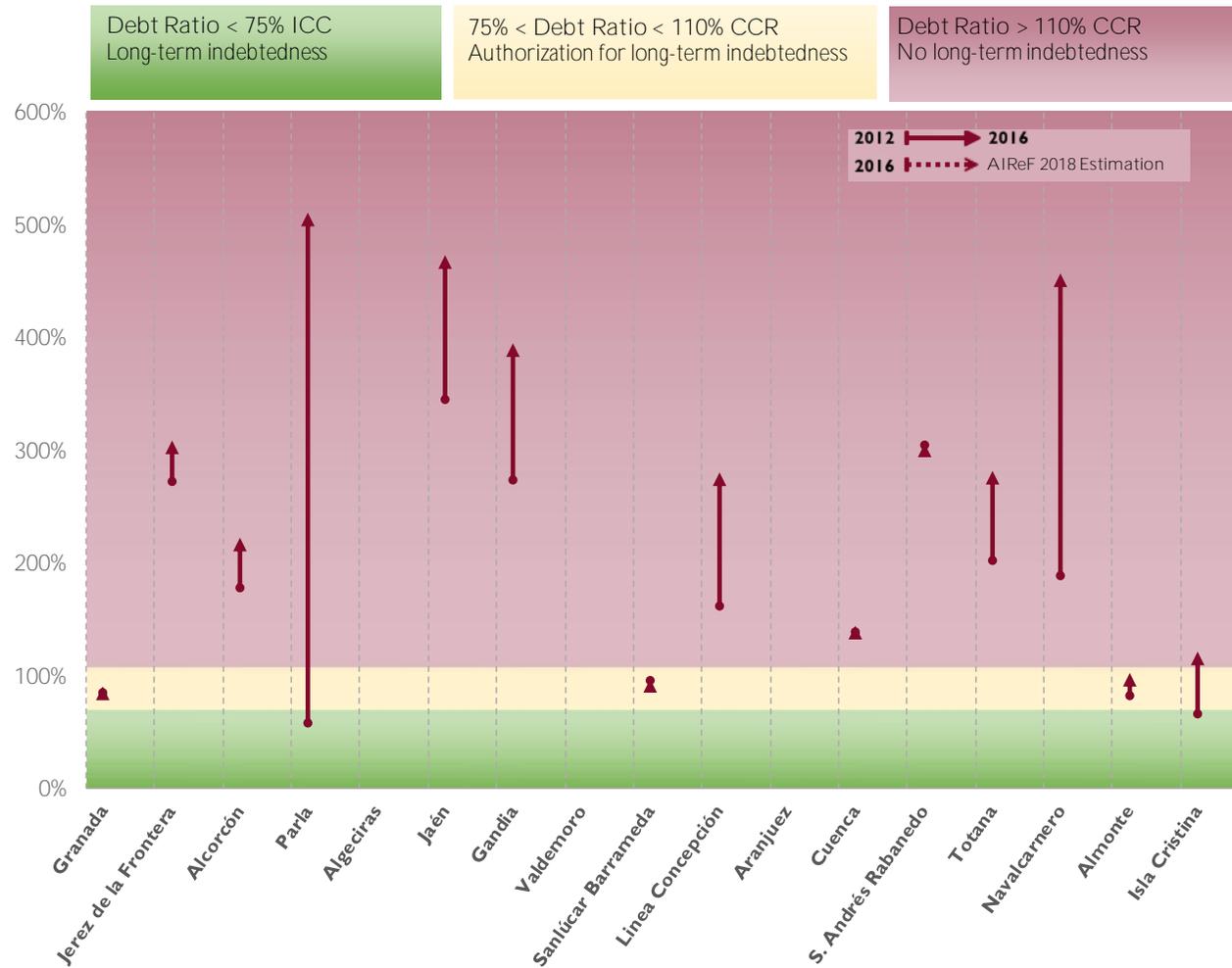


FIGURE 10. EVOLUTION OF THE INDEBTEDNESS OF THE 18 LOCAL CORPORATIONS 2012-2016 AND FORECASTS FOR 2017-2018 (PERCENTAGE OF DEBT OVER CONSOLIDATED CURRENT REVENUE)



The AIReF has rated the 8 City Councils of Algeciras, Almonte, Aranjuez, Cuenca, Granada, Isla Cristina, Sanlúcar de Barrameda and Valdemoro as being at moderate risk of medium-term sustainability. The analysis of the historical information on these cities until 2016, as well as the closing projections for 2017 and the 2018 surplus forecasts, have led the AIReF to rate these cities as moderate risk, since the detailed analysis of their situations allows the AIReF to estimate that reversion is feasible in less than 20 years. For this reason, although the AIReF will continue to monitor these LCs, the medium-term sustainability analysis in this report will focus on the other LCs whose debt ratios (the preferred indicator) is 200% of their current revenue and there are risks in assessing the possibility of reversal in the cited period.

The AIReF has rated the following city councils as high risk: Jerez de la Frontera, Alcorcón, Parla, Jaén, Gandia, La Linea de la Concepcion, San Andrés de Rabanedo, Totana and Navalcarnero. For those city councils with debt to current income ratios of more than 200% in the last financial year (preferential in terms of sustainability) and an average payment period more than 3 times the legal limit, AIReF has made a detailed study of their situations and their trends in successive fiscal years, based on the main sustainability ratios, whose results are presented in the individual files included in the annex.

Each Local Entity file contains comparisons of its situation with the group average, the average of the LCs in its Region, and the average of the city councils with similar population sizes. The files have the following structure:

- **Local Corporation financial sustainability indicators:** A look at the trends since 2014 (2013 in the case of debt) in relation to the three main structural indicators: debt and cash surplus over current revenue, as well as the average payment period. Likewise, the files include the AIReF debt forecasts for 2017 and the latest data published in 2017 on the average payment period.
- **Revenue/Expenditure per inhabitant of the Local Corporation:** A look at the trends for the same period of the non-financial revenue, expenditure and balance per inhabitant, including the AIReF forecasts for 2017.
- **Comparison between revenues, expenditures and balances of the Local Corporation budgets and settled fiscal years:** A look at the trends from 2012 to 2016 for revenue, expenditure and balances budgeted and settled each year, as well as any gaps between the two.
- **Evolution of budgetary stability and computable spending in the expenditure rule:** A look at the trends from 2013-2016 in the Local Corporations net financing need or capacity, as well as the computable expense observed each year of the period and the maximum permitted under article 12 of the LOEPSF; including the AIReF projections for 2017.

Recommendations

A. General recommendations

• ***Implementation of the LOEPSF***

The interpretation and specification of the LEOPSF in some aspects with open regulation, as well as the criteria and procedures for its application, must be clearly established and be widely known. This general premise is particularly important at the local level as the large number of entities and their heterogeneity could be said to have led to the “decentralization” of the LOEPSF since it became the local auditor and not the MINHAFP who verifies compliance or non-compliance with the fiscal rules. It should also be noted that more than half of the Autonomous Regions have assumed the financial protection of the LCs within their territorial scope, in such a way that the Economic Financial Plans in those cases are not approved by the MINHAFP but by the respective Autonomous Community.

For this reason, the AIRcF is recommending in successive reports the essential coordination of all financial protection bodies, and that the MINHAFP leads this coordination, guaranteeing the homogeneous application of the stability regulations and ensuring that unequal treatments do not occur in similar situations. The Ministry believes that there is a stable framework for institutional dialogue through the meetings held with the regional supervisory agency, to which the AIRcF has been invited this year.

However, in the course of drafting this report, the AIRcF has been able to confirm that there are still discrepancies in the criteria that must be resolved and that, as indicated in this report, city councils have been permitted to fail to comply with the targets without the coverage of an EFP, while other city councils modify their EFPs during their validity, thus avoiding non-compliance. Some city councils have budgets and EFPs approved with deficits although the Spanish Constitution and the LOEPSF demand balanced budgets.

Therefore, the AIRcF **reiterates the recommendation made in previous reports:**

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- 1. MINHAFP should establish and supervise a common framework for the exercising of the competences granted to the Local Corporations' supervisory agencies in which the criteria and procedures for taking action are clearly defined to ensure the homogeneous application of the LOEPSF in all Local Entities throughout the country.***
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- **Expenditure rule**

Throughout this report, the importance of the expenditure rule in the LC subsector and, especially, in the largest city councils has been highlighted, insofar as it is the only fiscal rule in which there are significant risks of non-compliance. In addition, there are several documents containing deficit and debt forecasts by subsector, that project LC surpluses reaching at least 0.5% GDP, despite a target set at equilibrium.

For this reason, it is not understood why the information to be provided to the MINHAFFP by the LCs on the main budgetary lines does not include the evaluation of the expenditure rule, as it does with the budget stability and public debt targets. It has been like this since the 2014 modification of Order HP/2105/2012, which developed the information provision obligations established in the LOEPSF, so that, currently, the first time data on the components and calculations of the annual expenditure rule are provided is at the end of January of the following year, since during the quarterly reports, the local auditor only has to communicate whether he expects to comply with said rule or not.

Therefore, **the AIRcF recommends:**

2. MINHAFFP should include the calculations of the expenditure rule in the information that the LCs must communicate on the main budgetary lines, approved budgets and performance, as well as an analysis of the consistency of this rule with the balance or surplus that can be deduced from the planned revenue and expenditure scenario, valued in terms of national accounts.

- **Transparency**

The stability regulation establishes the MINHAFFP's obligation to publish the relevant information related to compliance with these regulations. This information is not updated once the MINHAFFP deems it final, regardless of whether the Local Corporation later provides information, which in practice means that the published information is not always the most current.

Therefore, **the AIRcF recommends:**

3. MINHAFFP review the publications on its website on the economic financial information of the Local Corporations and periodically update all data to reflect the most recent information.

B. Individual recommendations

• **Local Corporations subject to individual analysis**

The purpose of this report is to assess the main budgetary lines for the Local Corporations for 2018 from the point of view of compliance with the fiscal rules. The AIReF does not have information on the expenditure rule, but within the scope of the stability target, it has detected the existence of risks of non-compliance in some of the Local Corporations analysed individually.

Moreover, there are clear risks of non-compliance in 2017, so it would be appropriate to make recommendations for the MINHAFP to implement warnings of the risk of non-compliance. However, the AIReF considers that, given the report's date of issuance, and the deadlines required by the Law for the application of this preventive mechanism, the formulation of recommendations in this sense is not operative. When the corresponding non-compliances are discovered, in the near future, the intervention agencies will have to initiate the application of the corresponding corrective measures.

Therefore, given the existence of risks of non-compliance with the budgetary stability rule in 2018, **the AIReF recommends:**

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- 4. That the city councils of Valencia, Murcia and Palma de Mallorca, given their high risk of non-compliance with the stability target, adapt their draft budgets to guarantee compliance by the end of 2018.***
 - 5. That the city councils of Barcelona, Bilbao, Vigo and Gijón, given their moderate risk of non-compliance with the stability target, adopt the necessary measures to guarantee compliance by the end of the year. Also, the supervisory agencies of these city councils must monitor the performance of these Local Entities to ensure compliance.***
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• **Local Corporations with sustainability problems**

The AIReF has detected financial sustainability problems in some LCs that can be classified as structural and acute due to their size and persistence over time. In these cases, it is necessary to perform an in-depth analysis of the causes that make it possible to diagnose the problem in these city councils prior to the adoption of measures that place them on the path to sustainability in the medium-term.

In this analysis, all agencies with competence in the matter must participate, which is why **the AIReF recommends:**

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- 6. MINHAFP convene and lead, for the city councils of Jerez de la Frontera, Alcorcón, Parla, Jaen, Gandía, La Linea de la Concepción, San Andrés de Rabanedo, Totana and Navalcarnero, an expert commission, in line with the one established in articles 25.2 and 26 of the LOEPSF with the participation of the supervisory Autonomous Community, when appropriate, to analyse the causes of sustainability problems in these City Councils and propose the most appropriate solutions.**
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