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The management of Government Expenditure Arrears in Spain

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Abstract

Clearance of government expenditure arrears has been one of the main goals of the Spanish economic policies in the last few years. Two key elements can be singled out in those policies: the extraordinary funding mechanisms to regions and municipalities, aimed at curbing the temporary component of late payments, and the elements of transparency and visibility of the average payment periods of public administrations. This paper provides a general presentation of the problem, with a summary of the best practices suggested by experts and describes the strategy adopted in Spain and its results.

Key words: Government expenditure arrears, Late Payments, Average Payment Period, Extraordinary Funding Mechanisms, Liquidity Fund to Autonomous Communities, Payment to Suppliers Plan, Public Financial Management, Subnational Governments, Autonomous Communities, Local Entities.

1. Introduction

The accumulation of government expenditure arrears is a problem for economic growth. It produces tensions in companies' business cycle that can eventually be unsustainable, depending on their financial position, leading to potential bankruptcies, layoffs, etc. Considering the weight of SMEs in Spain, curbing late payment in public administrations has been one of the goals of the Spanish economic policies in the last few years and has played a fundamental role in the economic recovery.

The Spanish strategy for clearing expenditure arrears starts with the reforms implemented in 2012, in the worst times of the economic crisis, within a context of severe liquidity restraint in financial markets and with public administrations whose late payments further aggravated the economic slowdown. According to the Bank of Spain, the aggregate commercial public debt grew from 57.1 billion euros (5.3% of GDP) to 87.3 billion euros (8.1% of GDP) between 2007 and 2011. Even though this rise in the stock of public debt took place at all levels of administration, it was more concentrated in subnational governments, autonomous communities and local entities, whose debt accounted for 75% of the total in 2011. Measures launched in that moment have cut down the commercial debt of those two levels of administration to the current 8.3 billion euros.

Two key elements can be singled out in those measures:

- The extraordinary funding mechanisms, such as the Fund for Payments to Suppliers and the Autonomous Communities Liquidity Fund, aimed at reducing the temporary component of the arrears and clearing the stock of commercial debt.
- The elements related to the transparency and visibility of the average payment periods (APP) of the administrations, which have played a fundamental role in creating incentives for the administrations to curb their late payments.

In this paper we provide a general overview of the problem, including the recipes suggested by experts to reduce late payments in public sector, and describe the Spanish strategy put in place in the last few years and its results.

2. CONCEPTS

We can define public expenditure arrears following Flynn and Pessoa (2014) as financial obligations that have been incurred by any level of the public sector for which payments have not been made by the due date. According to the authors, payments may be overdue based on a particular legal obligation (such as payment of social security benefits, or salaries), a specific contractual commitment (such as payment for construction of a road), or a continuing service arrangement (such as payment for electricity supply). However we will focus on commercial public debt in this paper, since it has the most important impact on economic activity, through contracts between the public sector and individuals and companies.

What constitutes a payment arrear may vary from country to country because there may be no clearly stated deadline for payment in laws, regulations, or policies. International practice on what is an acceptable delay between receipt and payment of the invoices varies from anywhere between 30 to 120 days. In the context of the European Union, *Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions* harmonized the maximum payment delays in business-to-business and business-to-administration transactions. In the latter, it established a general rule of thirty days and foresaw the payment of penalty interests in case an administration failed to comply with those deadlines.

BOX 1

Basic legal framework related to public expenditure arrears in Spain

- Law 3/2004, of 29 December, establishing measures to combat late payments in commercial transactions. In its article 4, lays down the deadline a debtor must meet, in case no other payment date has been fixed in the contract, at 30 calendar days after goods receipt or provision of services, even if the invoice or payment request has been issued before.
- *Directive 2011/7/EU of the European Parliament and the Council of 16 February 2011 on combating late payment in commercial transactions*, establishes a general rule of thirty days in business to administration transactions, computing as of the date of receipt of the invoice or the date of receipt of goods or provision of services or, when necessary, as of the date of acceptance or approval. This deadline can be extended in certain circumstances to sixty days (public corporations and public entities providing health services).
- Before the Directive saw the light of day, Spain had already adopted *Law 15/2010, of 5 July, amending Law 3/2004, of 29 December*, establishing measures to combat late payments in commercial transactions and thereby anticipated some measures laid down in the Directive, specifically, with regard to the payment deadlines.
- However, transposition of the Directive was completed through enactment of *Royal Decree-Law 4/2013, of 22 February, of measures in support of entrepreneurship, growth and job creation*, and its various reforms, the last operated through *Law 9/2017, of 8 November, of Public Sector Contracts*. This law includes the average payment period of contractors as a criterion to assess their economic and financial solvency when they concur in bids for contracts with the public sector.

When it comes to the causes of public expenditure arrears, the literature differentiates between those of a temporary and a structural nature. According to Flynn and Pessoa (2014), the temporary accumulation of government expenditure arrears is sometimes the result of acute government liquidity shortages that accompany serious economic or financial crises. Once the immediate shock of the crisis has passed, revenues recover, the government is able to access financial markets, and arrears tend to be cleared quickly and often do not re-emerge. A certain component of the Spanish problem of public expenditure arrears in the last few years was of this temporary nature, originated in the severe recession of 2009.

Persistent expenditure arrears are typically a symptom of underlying weaknesses in a country's public financial management system. Disregarding the case when the administration ignores that it is incurring in arrears, expenditure arrears can be the result of failures at any or all stages of the public financial management cycle, including inadequate legal frameworks, unrealistic budgeting, weak or cumbersome expenditure controls, inefficient cash management, lack of or problems with a financial management information system, or gaps in fiscal reporting.

Otherwise, factors related to the political cycle could also play a role in explaining late payments in public administrations. Delays can happen when governments, using cash accounting systems, postpone payments to sell a healthy financial position; similarly, in election years, the incumbent government may pass on to the next administration a large balance of outstanding payments without correspondent resources to finance them. According to the data published by the ministry of finance of Spain (MOFS) that will be commented in the section 4, there could be some evidence of these factors, since there was a rise of subnational governments' APPs as of the local and regional elections in 2015.

Finally, public expenditure arrears could be the consequence of inadequate or non-existent sanctions. Expenditure controls can be undermined by ineffective sanctions, or an unwillingness to enforce them, against officials or institutions who fail to comply with the law. The legal framework should clearly specify financial management responsibilities and sanctions for noncompliance both at personal and institutional levels with possible administrative, criminal, financial sanctions (fines), to managers or staff or to the organization, such as, for example, reducing its financial flexibility or suspending or reducing its appropriations in the budget. In this regard, the Spanish legal framework complies with this prescription, since it establishes the responsibility of internal auditors and the corresponding sanctions and even foresees, as we will see later, a regime of sanctions applicable to administrations failing to comply with the late payments legal framework.

Regarding the drivers of late payments, we can refer to the evaluation study of the late payment directive, carried out by Hausemer, Rzepecka, Lofstrom, Eparvier, Rivoire, Gallo, Maroulis, (2015). According to the authors, while late payment behavior is a multi-faceted, complex phenomenon, there are three key drivers that explain differences in the experience of late payments across sectors, countries, and over time. First, the general economic situation. Second, the prevailing business culture, which would explain that Southern European Countries such as Spain, Italy, Portugal, Greece have historically had higher average payment duration and delay than Nordic countries such as Denmark, Sweden or Estonia. Third, in the case of business-to-business trans-

actions, power imbalances in the supply chain, meaning that actors with market power tend to impose long payment periods on smaller suppliers, late payment being in practice an informal and zero cost source of borrowing for big companies, at the expense of their suppliers.

The recipes usually suggested by experts in order to control the accumulation of public expenditure arrears depend on the cause behind that accumulation. A brief summary of those recipes could include:

- A legal and regulatory framework that clearly define payment terms (and when a payment is in arrears), reporting requirements, controls at the budget authorization, commitment, and payment stages and the sanctions associated with any breach of those provisions. In this regard, the Spanish legislation is in line with this recommendation.
- Empowerment of the government to adopt measures against public contractors that do not pay in time to their suppliers. In this regard, the recent enactment in Spain of the new Law of Public Sector Contracts is a move forward in line with this recommendation.
- A credible and realistic budget, based on robust assumptions and forecasts in the fiscal framework on which the budget is based, reflecting actual spending requirements, through analysis of the historic behavior of each category of expenditure, with a particular focus on those items prone to arrears. In this respect, there is a high heterogeneity in Spanish administrations, the size and means of the administrations affecting the quality of its budgetary process and its capacity to comply with this recommendation. Nevertheless, there are some recent legislative initiatives that aim at strengthening internal control, especially at the level of local governments, which could improve compliance with this recommendation.
- Another important factor relates to cash and debt management. Reliable cash forecasting should ensure that liquidity is available to meet payment obligations as they arise. The same reasoning related to the capacity to produce a credible and reliable budget applies in general in this case, with the size and means of Spanish administrations being a factor that determines the quality of their cash and debt management.
- More generally, having a good system of fiscal reporting and fiscal accounting is a fundamental factor, and more specifically, having an information system based on technological solutions that enables the managers to have control over the stock of commercial debt and its vintage, and warns managers of risks of incurring in arrears. However, only a small number of countries (12 %, according to Flynn and Pessoa, 2014), regularly generate reliable data on the stock and vintage of arrears. The reason for the lack of awareness of arrears can be weaknesses in the fiscal reporting system or simply the lack of legal obligation to report it.

The lack of reliable data in this field is a problem not only for public managers themselves but also for citizens who should have access to this information. According to the European Commission Staff Working Document Evaluation of the late Payment Directive (2016), “Ministries in most Member States responsible for the transposition of the Directive do not collect any official data regarding the application of the legislation nor figures presenting changes in

average payment periods”. “Hard economic data on the subject (average payment periods/quantitative impact of the Directive) is scarce and when available, the different methodologies used in the calculations do not allow for direct comparisons across the board”. It is typical to use data from private credit rating companies, who base their reports on surveys of suppliers. However, this approach can have an important bias problem, since suppliers experiencing problems of public expenditure arrears may have an incentive to participate in these surveys and report longer-than-actual payment periods, if they think they can contribute to a policy change.

One of the recommendations in the report from the Commission to the European Parliament and the Council on the implementation of the Directive 2011/7/UE (2016), is to “Set up a system/procedure to monitor progress, report and publish information on average payment periods in both the public and private sectors.”

Spain has complied with this recommendation since it records the APP of all public administrations with a common calculation methodology, which, until the last change operated through Royal Decree 1040/2017, started with the receipt of electronic invoices. The information on APPs of all levels of Government is published by the MOFS, serving as a basis for the analysis to public managers and citizens. This is one of the key features of the Spanish strategy. It has played a crucial role, account taken of the impact that these publications have on regional and local media. Visibility adds an additional element of discipline to managers in subnational governments which, as we will see, has contributed to the reduction of the APP of those administrations.

- Finally, oversight of subnational governments and state-owned enterprises is also recommended. In addition to central government arrears, significant problems can appear at the subnational level and in state-owned enterprises. In this sense, the central state in Spain plays a special role in monitoring compliance and applying measures related to fiscal stability, debt sustainability and APP in other public administrations. As we will see, these measures, can even lead to withholding funds to subnational governments to pay directly their suppliers, when other measures have not succeeded in reducing their APP.

3. REFORMS IN SPAIN

Most of the measures in this field depart from year 2012, in a context of economic slowdown and severe liquidity restriction, both in the private and the public sector, with an important effect on public expenditure arrears. In that context, governments were unable to tap the financial markets to get the cash to cover even their day-to-day expenses. In that situation a specific plan to combat late payments in public administrations was enacted. That plan included a set of reforms, both of a temporary and structural nature.

3.1. Measures of a temporary nature: The extraordinary funding mechanisms¹

As from year 2012 the central state has implemented several financial instruments to provide subnational governments with the necessary liquidity they could not obtain in the financial markets, with the goal of reducing their high stock of commercial debt. Among those instruments, the Fund for Payments to Suppliers and the Autonomous Communities Liquidity Fund, have had a special importance. In these schemes, the central state paid the commercial debt of subnational governments and signed with them a 10 years-low interest rate loan, to obtain repayment.

The effect of these mechanisms on clearing public expenditure arrears operates through two channels: First, there is a direct effect, since the commercial debt, quantified on the basis of actual pending invoices submitted by subnational governments, is paid straight away and the total amount converted into a loan. Second, there is an indirect effect through the conditionality in the adjustment plans² in which the subnational governments must engage to have access to the funds. These adjustment plans are also monitored by the central state and contribute to improve the fiscal position of the administration concerned, thereby correcting the problem of late payment in the longer run.

The extraordinary funding mechanisms have brought in a significant liquidity to subnational governments at very low cost. Since 2012, the total amount lent to autonomous communities and local entities amounts to more than 200 billion euros. According to Téllez, Hernández de Cos, Hurtado and Pérez, (2015) these mechanisms have reduced dramatically the stock of commercial debt and the APP to suppliers in these administrations. Furthermore, different estimations confirm a positive impact on economic activity, even if it is complex to quantify its magnitude, account taken of the variety of channels through which these mechanisms operate. Nevertheless, it is clear that these measures have proven successful in providing the liquidity needed to pay an important part of the commercial debt of subnational governments' suppliers, which had grown out of control, during the crisis.

3.2. Structural Measures

- *Basic Stability and Financial Sustainability Organic Law, OL 2/2012, of 27 April, (BSOL)*, can be seen as the most important law from which subsequent reforms, originating in 2012, depart. This law brought in a new discipline in the Spanish public financial management, which would be guided henceforth by the fiscal rules of deficit, public debt and expenditure rule. It is important to highlight that, while the basic legal framework we described in box 1, establishes the “legal” payment deadlines for the public sector and the penalty interests applicable when the administrations fail to comply with those deadlines, with the BSOL and its related and implementing regulations, public administrations in Spain are subject to an additional discipline, which entails the follow-up of their APP (in a similar fashion as with the fiscal targets), and are potentially subject to measures, in case of non-compliance.

¹ http://www.minhfp.gob.es/es-ES/CDI/Paginas/EstabilidadPresupuestaria/20140410_LIQUIDEZ.aspx

² See additional provision one of the Basic Stability and Financial Sustainability organic Law, OL 2/2012, of 27 April.

- *Organic Law 9/2013, of 20 December, of public sector commercial debt*, is the first organic law devoted exclusively to public sector late payments. It broadens the sustainability principle in the BSOL to include commercial debt. This organic law introduces the concept of average payment period to suppliers, APP, as an index to follow-up payment periods and the vintage of outstanding debt. All administrations, irrespective of their size, are obliged to follow-up and report regularly their APP³, which is published by the MOFS, monthly, in the case of central state, autonomous communities and big municipalities and quarterly, in the case of smaller municipalities. This transparency element is a critical element for a successful strategy for clearance of public expenditure arrears, as we saw in the previous section.

According to this law, public administrations must include information related to the payment to suppliers in their cash plans, and must apply certain measures on their own initiative, when they detect APPs higher than certain thresholds. Moreover, if those measures fail to drive down the APP, other gradual measures apply, of a preventive, corrective and coercive nature, similar to those applying in the context of non-compliance with the fiscal and debt targets and the expenditure rule⁴. It is important to highlight that, in the last stage of application of these progressive measures, when previous measures have not succeeded in correcting the APP, the Ministry of Finance can trigger the proceeding to withhold funds from the system of regular transfers to subnational governments, in order to pay directly to suppliers, on behalf of the subnational administrations. This is a fundamental provision, taking into account the high degree of public decentralization in Spain and the fact that, subnational governments have a constitutional guarantee of budgetary autonomy.

- *Law 25/2013, of 27 December, fostering the use of electronic invoices and setting up the accounting registry of invoices in the Public Sector*. This law foresees a group of measures aiming at helping suppliers use electronic invoices. It also establishes the obligation for administrations to have a general point of entry of electronic invoices so that suppliers can submit them for an electronic processing. This way, suppliers have a reliable and credible tool to prove the date of the invoice, and they can eventually launch claims in case the administrations fail to pay in time. This element is also important, given that, until the last reform in the calculation methodology of the APP, the entry of the invoice in the point of entry was the reference for the calculation of the APP.
- *Royal Decree 635/2014 of 25 July, establishing the methodology for the calculation of the average payment period to suppliers of public administrations and the conditions and proceeding to withhold funds from the systems of regular transfers to subnational governments, foreseen in the Basic Stability and Financial Sustainability Organic Law OL, 2/2012, of 27 de April*. The main feature of this law is that it develops the common methodology for the calcu-

³ <http://www.minhafp.gob.es/es-ES/CDI/Paginas/PeriodoMedioPago/InformacionAAPPs/PMPdelasAAPP.aspx>

⁴ Examples of communications submitted from central state to autonomous communities in each phase can be found in the Ministry of Finance website:

<http://www.minhafp.gob.es/es-ES/CDI/Paginas/EstabilidadPresupuestaria/InformacionComunidadesAutonomass/ComunicacionesComunidadesAutonomasPMP.aspx>

lation of the APP, so that the resulting data can be monitored and are suitable for analysis⁵. The calculation formula of the APP of a public administration, according to this Royal Decree, is a weighted average of the APP of its entities, the weighting factor being the value of their transactions. The APP of each entity is a weighted average of the ratio of payments made and the ratio of outstanding transactions, the weighting factors being the value of the transactions settled and the pending debt. The ratio of payments made is an average of the days of payment of the transactions settled, weighted by the value of each transaction. And the ratio of outstanding transactions, the number of days elapsed to the last day of the month to which publication data are referred, weighted by the value of each debt.

The main advantage of this common methodology for calculating the APP was that it did not capture only what an administration would take to pay, (the payments made component), but also the outstanding transactions component or the vintage of the debt. If this element were to be ignored, one administration could artificially register a low payment period, were it to use a “LIFO”, *last in-first out* approach, when selecting the invoices it pays, while maintaining the oldest invoices unpaid.

Another feature of this methodology was to start computing the days of payment as from the 30 days after the entry of the invoice in the administrative registry. This element has been strongly criticized by the industry since, according to the reasoning, it artificially added 30 days as compared to the calculation established by the late payments Directive. We can contest the criticism first by taking into account that, even if Royal Decree 635/2014 started the computation of days automatically as from the 30 days after the entry of the invoice, the Directive allows for a 30 days period for approval. Therefore, application of these 30 days seems reasonable, as if it was the time for approval, and considering that the same calculation methodology has to be used for the APP of administrations as different in size and means as a municipality of 5.000 inhabitants and the social security.

Second, it is important to highlight that the computation of days departed from an element out of the control of administrations, such as the entry of the invoice in the administrative registry, (which in turn, was traceable, since the use of electronic invoice became the norm). Therefore, it

⁵ Other examples of indicators on late payments used by sectoral associations are:

- The *Days of Sales Outstanding* (DSO) indicator, used by the medicine and healthcare industry producers, (FENIN and Farmaindustria). A financial indicator that differs from the concept of legal payment deadline or actual vintage of the invoices since it considers only the pending amount and the sales volume;
- The average time of payment to suppliers, used by the *Multisector Platform Against Late Payments*, calculated as the ratio between the accounting concept of suppliers from the balance sheet, and the value of the purchases in the profit and loss account, multiplied by 365. This ratio indicates the average number of days in which a company pays its suppliers, being again, more a financial indicator than a payment period indicator.
- The national association of self-employed workers, ATA, uses a concept of payment period based on surveys and considering the date of issuance of the invoice, regardless of the legal period allowed by the Directive for the approval of the invoice by the public administration.
- Finally, the Bank of Spain uses information on commercial credits to public administrations.

did not allow for strategic behaviors of administrations, artificially delaying the approval of the invoice to have a shorter period of payment.

Finally, it is important to take into account that the APP in Royal Decree 635/2014 was an economic indicator used to monitor late payments and impose sanctions to those non-complying administrations and its use was independent of the maximum 30 days legal deadline laid down by Royal Decree-Law 4/2013, that the suppliers could always claim in courts against public administrations. Notwithstanding the latter, the European Commission expressed concerns on the compatibility of this economic calculation with the Directive 2011/7/UE, leading it to open an infringement procedure against Spain.

This fact forced Spain to amend Royal Decree 635/2015, through *Royal Decree 1040/2017*⁶, of 22 December. This Royal Decree changed the computation method of the payments made and of the outstanding transactions, eliminating the reference to the starting point as from the 30 days since the entry of the invoice in the registry. With the new calculation method the computation of the days starts with the approval of works certificates or the documents supporting conformity with the goods or services supplied or with the date of entry of the invoice in the administrative registry, when approval or conformity are not applicable or the invoice is received after approval or conformity.

In case the current approval and conformity periods remain unchanged, this new methodology will lead, *ceteris paribus*, to longer APP in public administrations. Another possible consequence of the change in the calculation methodology is that strategic behaviors can arise in the form of artificial extensions of the approval and conformity periods, tending to maintain or reduce current APP in public administrations, since the computation starts with a fact under the control of the administrations. This problem is therefore a new challenge that will probably require monitoring closely the stages prior to approval and conformity.

4. RESULTS

4.1. Subsectors analysis

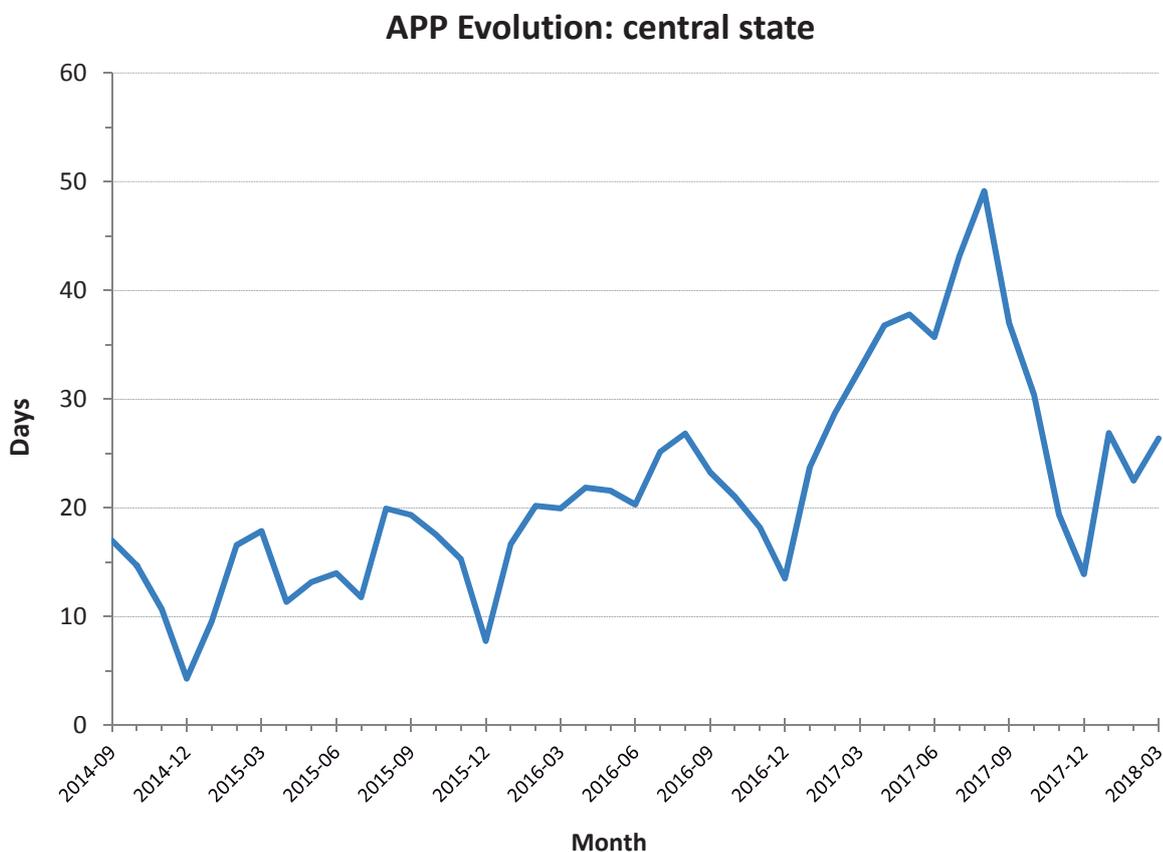
In this section we will use the statistics published in the website of the MOFS, which are classified by level of public administration or subsectors⁷. Royal Decree 635/2014 foresees computation of invoices as from 1st January 2014, date of entry into force of the obligation to account for invoices received in the official registry. The time series starts as of September 2014, date of the first publication released under methodology foreseen in Royal Decree 635/2014, and ends with the last publication under that methodology, corresponding to March 2018.

⁶ <https://www.boe.es/boe/dias/2017/12/23/pdfs/BOE-A-2017-15364.pdf>

⁷ <http://www.minhafp.gob.es/es-ES/CDI/Paginas/PeriodoMedioPago/PeriodoMedioPago.aspx#tabla73>

4.1.1. Central state

Central state covers the general administration, public entities and agencies.



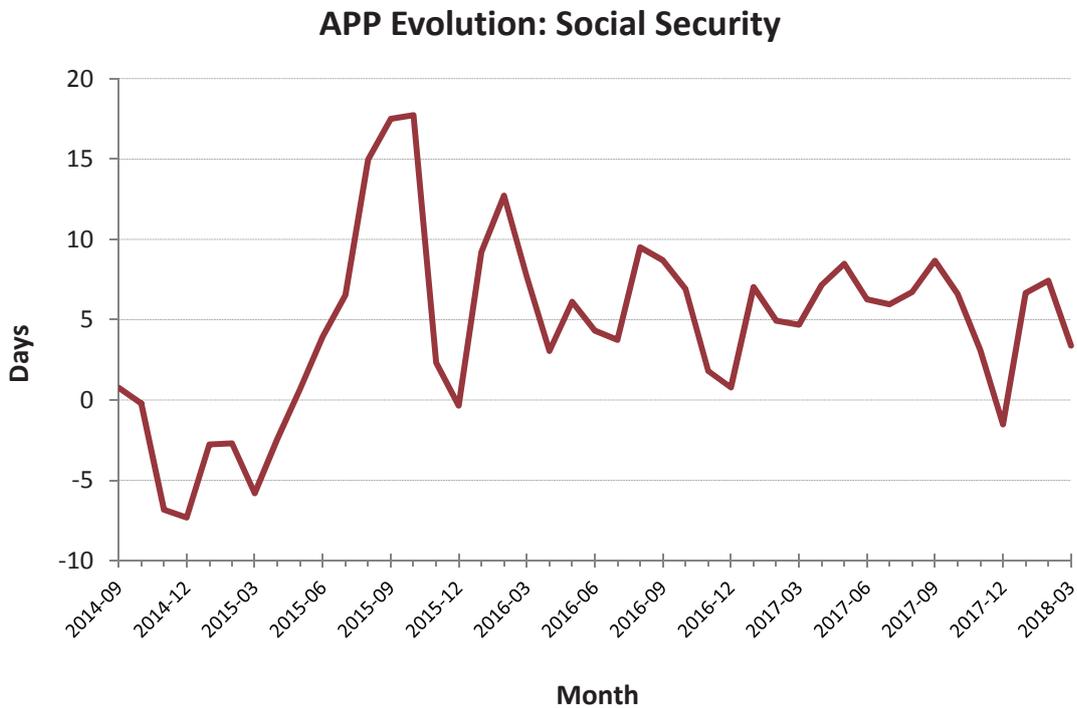
Source: Prepared by the author on the basis of data published by the Ministry of Finance.

Except the period between March and September 2017, central state's APP has always remained below 30 days. The rise in that period was due to the order enacting a general budgetary closure in the previous months, which delayed the processing of certain contracts of the central Government of high value. Since the APP calculation is an average weighted by values, those few contracts gave rise to an increase of the APP which, however, decreased once processing was unblocked.

Otherwise, we can notice, as in the case of the other subsectors, seasonal peaks in the months of August, due to the slower rhythm of payment processing and seasonal valleys and subsequent peaks in the months of December and January, due to the way the outstanding transactions ratio is computed in those months.

Despite showing an APP below 30 days in most of the months recorded, an individual examination was conducted by the internal auditors of the central state (IGAE), as from 2016, which consisted on reviewing the process for registry and handling of invoices. As a consequence of this audit, errors were detected and corrected, as for instance, the case of invoices which having been paid, remained registered as unpaid, due to lack of update.

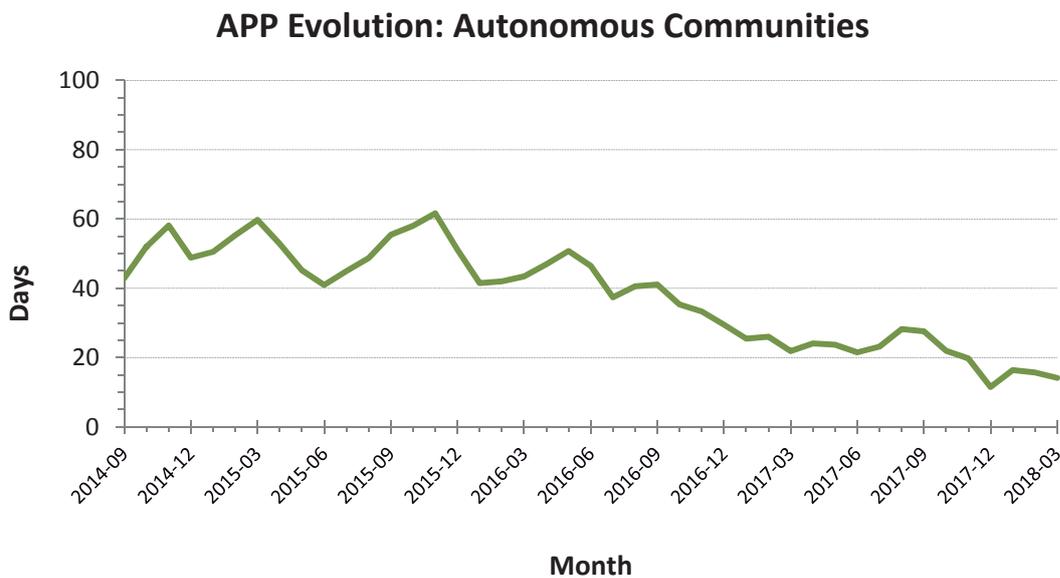
4.1.2. Social Security



Source: Prepared by the author on the basis of data published by the Ministry of Finance.

In the case of Social Security data are even better, its APP being higher than 10 days only in two short periods. As in the case with the central state, there has not been a problem of late payments in this subsector.

4.1.3. Autonomous Communities



Source: Prepared by the author on the basis of data published by the Ministry of Finance.

Even though the trend is clearly decreasing, as reflected by the time series we notice a problem of late payments, in the case of autonomous communities: by the end of 2015, the average APP was above 60 days and some autonomous communities had a much higher APP.

The disbursements of the Liquidity Fund to Autonomous Communities (FLA) have had an impact in the evolution of the APP of the subsector, explaining important valleys in the months following those disbursements. In those disbursements, a concept of a particular importance, due to the volume of funds transferred, has been the “extra-FLA”, or the funds lent to cover the non-funded deviation of the fiscal deficit incurred by autonomous communities with respect to the previous years’ fiscal targets. Experts have been critical of this lending, due to the moral hazard it could create in autonomous communities’ fiscal performance. Despite this problem, the goal of the extra-FLA was to help autonomous communities clear their expenditure arrears by lending them what they could not borrow in markets, so that they could reduce their APPs.

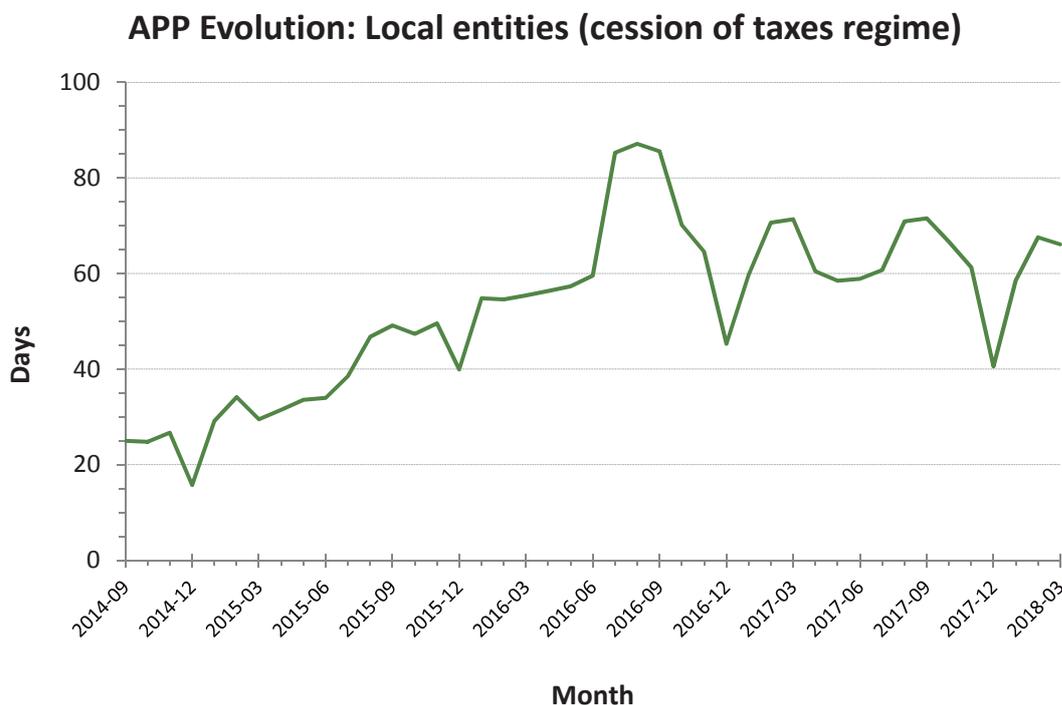
Another important driver of the evolution of the APP in autonomous communities has been the activation of progressive measures foreseen in the BSOL, which has reached the last stage, withholding funds from the regular transfers from the central state, in the case of Aragon and Extremadura.

Due to those measures, as from 2017 the APP has decreased to less than 30 days and the trend is clearly downwards. The last figures published using the methodology of Royal Decree 635/2014 (related to March 2018), show an APP of 14,3 days, leading to the conclusion that the problem of late payments in autonomous communities has been corrected.

4.1.4. *Local Entities.*

The data we consider now are those related to the big municipalities (“cession regime”, or those with a population of more than 75.000 inhabitants, and/or capital of province⁸), although the results are, in general, the same if we were to consider the whole subsector.

⁸ There are differences in the information requirements for those municipalities in the “cession of taxes” regime and the municipalities with less than 75.000 inhabitants, in the “variables” regime. The main difference is that the first group report data monthly, whereas the second reports data quarterly.



Source: Prepared by the author on the basis of data published by the Ministry of Finance

As reflected by the time series, the trend is upwards and starts to register APPs over 30 days systematically as of mid-2015. In spite of these data, however, one cannot conclude that there is a problem of late payments in the subsector, since these excessive APPs, higher than 60 days, are registered in a short list of municipalities (currently, 21). Since data for the whole subsector is a weighted average, the weighting factor being the volume of debt, and provided the high amount of debt in those few indebted municipalities, the APP of the subsector is high.

Indeed, considering the municipalities in the “variables” regime (with less than 75.000 inhabitants), the APP of the subsector is 67,87 days, according to the last publication of the MOFS⁹. However, 83,92 % of the municipalities in the variables regime and 72,97 % of those in the cession regime show currently an APP of equal to or less than 30 days.

If we disregard those municipalities with an APP higher than 60 days (14,9 % in the cession regime and 9 % in the variables regime), the APP would decrease to 13,38 days.

Therefore, we can conclude that the late payments problem in the local entities seems to be concentrated in a short list of municipalities.

In this respect, the fiscal responsibility independent authority (AIREF), has recommended the MOFS to adopt individual actions with regard to those entities, even activating the measure laid down in the BSOL that foresees sending a team of experts to audit the local governments and

⁹ Publication of data of month of March 2018 for local entities in the cession regime and 1st quarter 2018 for the local entities in the variables regime.

propose measures¹⁰, in the understanding that these entities are in such a difficult financial position that they will not be able to redress it by themselves. The MOFS, however, has preferred to enact the previous progressive measures foreseen in the BSOL, that would lead, in the case of persistent APP above 60 days, to withhold funds from the regular transfers from the central state, in order to pay directly to suppliers, and in a second stage, resort to the faculty foreseen in Art. 39.2 of Royal Decree Law 17/2014, by which, these entities would have to adhere to the Restructuring Fund (Fondo de Ordenación)¹¹, and therefore would have to sign a loan with the central state with a special conditionality.

4.2. Aggregate analysis

There is no aggregation of the data of subsectors of public administrations in official figures. However, we can aggregate those figures and obtain a weighted average using the addition of amounts of payments made and outstanding transactions, as the weighting factor. Using this aggregation, the data would be as follows:

¹⁰ http://www.airef.es/informes/-/asset_publisher/lj3Zi6KgDH3f/content/informe-sobre-las-lineas-fundamentales-de-los-presupuestos-de-2018-de-las-entidades-locales

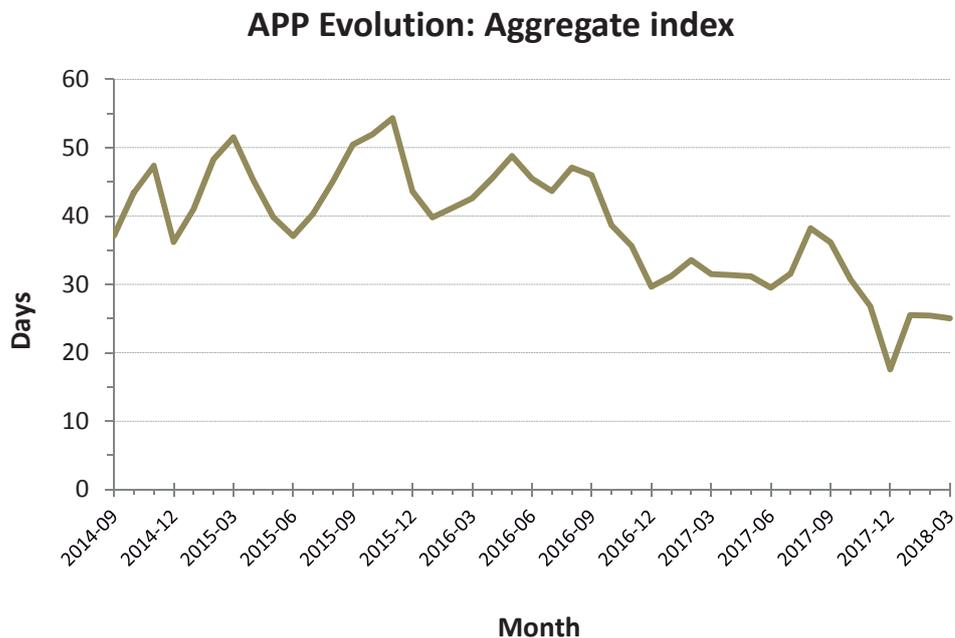
¹¹ [http://www.minhafp.gob.es/es-ES/CDI/Paginas/EstabilidadPresupuestaria/InformacionCORPORACIONES LOCALESs/ComunicacionesCORPORACIONES LOCALES.aspx](http://www.minhafp.gob.es/es-ES/CDI/Paginas/EstabilidadPresupuestaria/InformacionCORPORACIONES_LOCALESs/ComunicacionesCORPORACIONES_LOCALES.aspx)

The management of Government Expenditure Arrears in Spain

| Months | Average Payment to Suppliers (days) | | | | | Subsectors weight in the aggregate APP (%) | | | | |
|---------|-------------------------------------|-----------------|--------------------|---------------------------------|-----------|--|-----------------|--------------------|---------------------------------|-----------|
| | Central State | Social Security | Autonomous Regions | Local Entities (cession regime) | Aggregate | Central State | Social Security | Autonomous Regions | Local Entities (cession regime) | Aggregate |
| 2014-09 | 17,00 | 0,77 | 42,89 | 24,96 | 37,13 | 11,1 | 0,5 | 73,5 | 14,8 | 100,0 |
| 2014-10 | 14,70 | -0,21 | 52,01 | 24,78 | 43,41 | 12,3 | 0,6 | 73,5 | 13,6 | 100,0 |
| 2014-11 | 10,68 | -6,83 | 58,15 | 26,70 | 47,36 | 13,4 | 0,7 | 73,2 | 12,7 | 100,0 |
| 2014-12 | 4,29 | -7,31 | 48,84 | 15,74 | 36,20 | 16,0 | 0,9 | 68,0 | 15,2 | 100,0 |
| 2015-01 | 9,54 | -2,77 | 50,55 | 29,14 | 41,00 | 15,2 | 0,8 | 70,5 | 13,6 | 100,0 |
| 2015-02 | 16,58 | -2,69 | 55,31 | 34,16 | 48,28 | 10,0 | 0,7 | 76,3 | 13,0 | 100,0 |
| 2015-03 | 17,87 | -5,80 | 59,73 | 29,50 | 51,50 | 8,6 | 0,7 | 76,9 | 13,8 | 100,0 |
| 2015-04 | 11,36 | -2,41 | 52,83 | 31,47 | 45,26 | 9,0 | 0,9 | 74,5 | 15,6 | 100,0 |
| 2015-05 | 13,17 | 0,69 | 45,20 | 33,57 | 39,85 | 9,4 | 1,0 | 73,2 | 16,5 | 100,0 |
| 2015-06 | 14,00 | 3,94 | 40,96 | 33,96 | 37,06 | 9,3 | 0,9 | 74,5 | 15,3 | 100,0 |
| 2015-07 | 11,78 | 6,54 | 44,95 | 38,53 | 40,30 | 10,0 | 1,0 | 74,0 | 15,0 | 100,0 |
| 2015-08 | 19,94 | 14,97 | 48,71 | 46,76 | 45,07 | 10,7 | 0,9 | 73,5 | 15,0 | 100,0 |
| 2015-09 | 19,36 | 17,50 | 55,48 | 49,12 | 50,43 | 10,5 | 0,8 | 73,8 | 14,9 | 100,0 |
| 2015-10 | 17,55 | 17,73 | 58,06 | 47,35 | 51,95 | 10,5 | 0,8 | 74,3 | 14,4 | 100,0 |
| 2015-11 | 15,29 | 2,32 | 61,62 | 49,57 | 54,32 | 11,4 | 0,7 | 74,8 | 13,0 | 100,0 |
| 2015-12 | 7,76 | -0,35 | 51,12 | 39,91 | 43,59 | 13,1 | 0,9 | 73,3 | 12,7 | 100,0 |
| 2016-01 | 16,67 | 9,21 | 41,52 | 54,80 | 39,79 | 13,6 | 0,9 | 70,9 | 14,6 | 100,0 |
| 2016-02 | 20,18 | 12,72 | 41,98 | 54,56 | 41,18 | 11,6 | 0,7 | 72,2 | 15,5 | 100,0 |
| 2016-03 | 19,95 | 7,67 | 43,44 | 55,42 | 42,58 | 9,9 | 0,8 | 74,5 | 14,7 | 100,0 |
| 2016-04 | 21,86 | 3,05 | 46,92 | 56,33 | 45,51 | 9,6 | 0,9 | 75,1 | 14,5 | 100,0 |
| 2016-05 | 21,58 | 6,12 | 50,76 | 57,32 | 48,78 | 8,7 | 0,8 | 76,4 | 14,1 | 100,0 |
| 2016-06 | 20,31 | 4,32 | 46,49 | 59,55 | 45,49 | 9,2 | 0,9 | 76,2 | 13,7 | 100,0 |
| 2016-07 | 25,16 | 3,74 | 37,41 | 85,24 | 43,63 | 10,2 | 1,0 | 72,5 | 16,3 | 100,0 |
| 2016-08 | 26,83 | 9,51 | 40,59 | 87,11 | 47,08 | 11,2 | 1,0 | 69,8 | 18,0 | 100,0 |
| 2016-09 | 23,29 | 8,70 | 41,09 | 85,56 | 45,98 | 11,2 | 1,0 | 71,5 | 16,2 | 100,0 |
| 2016-10 | 21,01 | 6,92 | 35,34 | 70,12 | 38,65 | 12,6 | 1,0 | 70,9 | 15,5 | 100,0 |
| 2016-11 | 18,19 | 1,80 | 33,31 | 64,57 | 35,64 | 13,5 | 1,1 | 70,4 | 15,0 | 100,0 |
| 2016-12 | 13,52 | 0,79 | 29,46 | 45,29 | 29,66 | 14,4 | 1,0 | 67,1 | 17,6 | 100,0 |
| 2017-01 | 23,74 | 7,03 | 25,45 | 59,71 | 31,19 | 11,9 | 1,0 | 69,1 | 17,9 | 100,0 |
| 2017-02 | 28,69 | 4,93 | 26,01 | 70,62 | 33,56 | 11,3 | 0,9 | 71,1 | 16,7 | 100,0 |
| 2017-03 | 32,73 | 4,69 | 21,86 | 71,34 | 31,50 | 11,8 | 1,0 | 69,9 | 17,2 | 100,0 |
| 2017-04 | 36,78 | 7,16 | 24,09 | 60,45 | 31,37 | 11,6 | 1,1 | 70,8 | 16,5 | 100,0 |
| 2017-05 | 37,79 | 8,48 | 23,71 | 58,47 | 31,18 | 11,9 | 1,1 | 69,8 | 17,1 | 100,0 |
| 2017-06 | 35,70 | 6,26 | 21,51 | 58,89 | 29,52 | 13,6 | 1,1 | 68,7 | 16,7 | 100,0 |
| 2017-07 | 43,13 | 5,96 | 23,16 | 60,71 | 31,57 | 12,6 | 0,9 | 70,3 | 16,1 | 100,0 |
| 2017-08 | 49,13 | 6,73 | 28,25 | 70,91 | 38,21 | 14,2 | 0,9 | 68,0 | 16,9 | 100,0 |
| 2017-09 | 36,99 | 8,67 | 27,56 | 71,54 | 36,15 | 12,8 | 0,9 | 69,1 | 17,2 | 100,0 |
| 2017-10 | 30,40 | 6,61 | 21,98 | 66,62 | 30,73 | 13,4 | 1,1 | 68,0 | 17,5 | 100,0 |
| 2017-11 | 19,38 | 3,11 | 19,73 | 61,28 | 26,82 | 15,9 | 1,0 | 65,5 | 17,6 | 100,0 |
| 2017-12 | 13,90 | -1,52 | 11,50 | 40,56 | 17,57 | 16,9 | 1,2 | 61,9 | 20,0 | 100,0 |
| 2018-01 | 26,88 | 6,66 | 16,40 | 58,50 | 25,51 | 12,2 | 1,1 | 67,8 | 18,9 | 100,0 |
| 2018-02 | 22,50 | 7,43 | 15,70 | 67,57 | 25,44 | 12,6 | 1,0 | 69,1 | 17,3 | 100,0 |
| 2018-03 | 26,38 | 3,39 | 14,13 | 66,10 | 25,05 | 14,8 | 1,1 | 66,3 | 17,7 | 100,0 |

Source: Prepared by the author on the basis of data published by the Ministry of Finance .

And the resulting trend:



Source: Prepared by the author on the basis of data published by the Ministry of Finance.

Be it with important fluctuations, this constructed aggregate APP shows a clearly decreasing trend, from the 37,13 days recorded at the beginning of the series to the 25,05 at the end, thereby showing that the reforms have been effective in decreasing the APPs of the different levels of administration.

5. CONCLUSION

The presented reforms have therefore been successful in managing public expenditure arrears. Not only has the APP decreased, around a third, using the aggregate APP in the previous section, but also the commercial debt has tended to shrink significantly, especially in the subnational levels of government, from around 65,5 billion euros to the current 8,3 billion.

We can highlight two key elements in this strategy: on the one hand, the extraordinary funding mechanisms have played a key role in clearing the stock of invoices in arrears accumulated during the crisis. On the other hand, the elements of transparency and visibility in the monitoring and follow-up of the APP of public administrations, has fostered a new discipline and a change in the public financial management of administrations.

Despite the good results explained, important challenges lie ahead. For example, the question on the future of the extraordinary funding mechanisms. Since their inception, public administrations have improved significantly their financial position and are therefore returning or want to return progressively to the financial markets, making them less necessary. Their role would possibly evolve, therefore, from being the central element of the temporary measures put in place to reduce late payments in public sector to becoming a last resort facility, to autonomous communities facing important liquidity shocks or to the municipalities in the worst financial situation.

In this latter case, the procedure to withhold resources from the regular transfers from the central state to pay directly to suppliers of the short list of municipalities that in a way “distort” the APP of the whole sector is underway and it will probably lead to a reduction of the subsector’s APP.

Finally, regarding the structural measures of the plan, it is also worth mentioning the challenge posed by the new methodology of calculation of the APP, introduced through Royal Decree 1040/2017. The first publication of data calculated according to the new methodology is due in the month of June 2018. As said above, the new methodology might require a stronger control of the stages prior to approval and conformity, in order to avoid strategic behaviors in public administrations that may try to show an artificially low APP.

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