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MUNICIPAL GUARANTEES – PUBLIC SUPPORT FOR WHICH INVESTMENTS?

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Simona GHERGHINA [1]

Abstract

The current regulations concerning the issuance of municipal guarantees are both unclear and limitative, therefore restricting their use by the local public authorities as an effective support measure for public investments of local interest. Whilst focusing on procedural issues and on the financial limits to the ability of local authorities to undertake public debt obligations, the law seems to define in a restrictive manner the potential beneficiaries of municipal guarantees, that excludes the concessionaires of public works, public assets or public services, the delegated administrators of utilities an the project companies operating a public-private partnership project. A redrafting of such texts to extend the list of beneficiaries of municipal guarantees to such companies would give local public authorities a significant instrument for supporting investment projects.

Keywords:

municipal guarantees, public debt, public finances, local investments, sovereign debt

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1. Preliminary considerations. Sovereign debt and generally public debt have probably never been so much close to the centre of the public attention as in the current context of the financial and economic crisis. If we extend the analysis beyond their financial aspects and the proposed solutions and focus on the legal texts regulating the undertaking and the performance of public debt obligations, it may appear that such legal texts are quite far from the sharp clarity one would expect for such subject. Where regulations should leave no place for divergent interpretations, whilst giving expression to transparently assumed public policies, vague provisions seem to allow a limited action domain for local public authorities when undertaking public debt obligations.

The architecture of the Romanian legal system addressing public debt is also divided into a visible part and one which is less visible, if not hidden, in the sense that there is no common opinion of the legal literature as concerns its existence and characteristics. The visible part comprises specific regulations concerning public debt, i.e. Emergency Government Ordinance no. 64/2007 regarding public debt (hereinafter referred to as "the Public Debt Law") and specific provisions regarding public debt assumed by administrative-territorial units included in the Law no. 273/2006 regarding local public finances (hereinafter referred to as "the Local Public Finances Law"). Both types of specific regulations – those of general application in the Public Debt Law as well as those included in the Local Public Finances Law – are integrated within the greater domain of public law. But the less visible part of the legal system regulating public debt is outside the field of public law, in the outer space of private law. The application of private law rules to public debt obligations is built on the idea that such obligations assumed by public law legal persons, as the state or the administrative-territorial units, either by loans or other types of financing or by guarantees, shall be similar in nature to those assumed under the same type of contracts by private persons. Consequently, the Civil Code rules on obligations and guarantees, on loans or credit facility agreements, shall be the general level of regulations applicable to public debt obligations, the Public Debt Law shall be the special regulation applicable to all types of public debt (thus being what may be called a first level of specificity) and the Local Public Finances Law shall be the special regulation applicable to local public debt (as a second level of specificity).

This study aims to analyse the consequences of the current form of the legal text regulating the municipal guarantees by emphasising the unreasonable limitations imposed on the possibility of local public

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authorities to efficiently use such instrument in various domains of local interest (for a special example, Pârvu, Ungureanu *et alii*, 2011, p. 203).

2. Beneficiaries of municipal guarantees. Unlike the Public Debt Law, the Public Finances Law does not include a legal definition for the beneficiary of the guarantee, but defines the „*local guarantee*" as being the obligation assumed by a local public authority, as guarantor, to pay when due the unpaid obligations of the beneficiary of the guarantee or of the subordinated economic operators or public services, within the limits provided by the law.

The definition fails to provide a clear design of the legal concepts it addresses, requiring interpretation and even corrections. One of the inadequacies in the definition is related to the issuer itself, i.e. the debtor of the obligation arising under the guarantee, which is referred to as "*local public authority*". A regrettable confusion is made between the legal person assuming the obligation, which is clearly the administrative-territorial unit, and the authorities entitled to make decisions at the local administrative level, generally named local public authorities. It is, most probably, an integrative reflex derived from the general theory of administrative acts, which assumes that they are issued, amongst others, by the local public authorities when exercising their powers conferred by law (Apostol Tofan, 2004, pp. 4-5). Given the quasi-general qualification of contracts entered by public entities as being administrative contracts (Săraru, 2009, p. 75 *et seq.*), therefore becoming part of the greater family of administrative acts, the reference to the same issuer/party – the local public authorities – is somehow explained, but, in our opinion, not justified. Unlike the unilateral administrative acts issued by the local public authorities according to their powers granted by law, the contracts entered at the local level should have as a party the legal person, as the effects of such contracts shall arise within their patrimony. The local public authorities shall exercise their powers by making the appropriate decisions related to the contract's closing, performance or termination, as the case may be.

But the main element which remains unclear in this definition relates to the identification of potential beneficiaries of the municipal guarantees. When analysing the enumeration of potential beneficiaries of municipal guarantees in the legal definition of the "*local guarantee*", it seems to provide for three distinct types of such beneficiaries. The first would be a type identified in general terms, as the "*beneficiary of the guarantee*", to include all possible beneficiaries of such public guarantees under applicable regulations, *i.e.* those of general tenure in the Public Debt Law

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as well as those of special application in the Local Public Finances Law. In addition to this general type of beneficiaries, the legal text adds two specific types that may be collectively referred to as public entities subordinated to the local public authority, namely public companies (named "*economic operators*" in the legal text) and public services, both subordinated to the issuer of the guarantee. This general denomination of "economic operator" was included by art. 8 of the Law no. 71/2011 regarding the application of the Law no. 287/2009 regarding the civil code within the broader term "professional", as part of the new Civil code's idea of uniform regulation of all private law institutions.

Certain connections with the general legal context have to be restored, in our opinion, at least for the elements of this definition which draw the limits of using public guarantees by local authorities. One of these elements requiring connection with more specific legal terms is the subordination described by such legal definition. From both economic and legal perspectives, public companies, deemed to be private law legal persons, are under the control of the local public authorities, with the respective administrative-territorial unit (village, city or county) being the main or sole shareholder. Subordination describes rather, in administrative hierarchy terms, the situation of a public authority that is not autonomous but merely under the administrative authority of another public law legal person.

Consequently, the "*subordinated economic operators*" shall be the commercial companies or the public undertakings operating a public monopoly ("*regii autonome*" in Romanian) under the control of the local authorities, according to art. 36, par. 2 lett a) and par. 3 lett. c) of Law no. 215/2001 regarding the local public administration. We believe shall not be included in this category of "*subordinated economic operators*" those companies which are not under the control of the local public authorities, either by shareholding or by significant influence on their decisions.

Another element of the legal definition requiring further clarification is the even more vague reference to public services subordinated to the local public authorities. According to the relevant regulations, public utilities services are organised either as departments of the local public administration, or as separate legal persons. Further, such legal persons may be private companies entrusted a public service or public undertakings.. Considering that the existence of a guarantee issued by a local authority for a certain beneficiary implies the existence of two distinct legal persons – the issuer and the beneficiary, the legal definition of the guarantee may be deemed to refer solely to the public utilities

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services organized as public undertakings, i.e. legal persons under the control of the local public authorities. Such public undertakings are operating the respective public utility service based on a direct administration contract, and may be also organized as commercial companies or as *regii autonome*, with the local public authorities exercising their control either by shareholding or by decisive influence on their corporate decisions.

When analyzing the characteristics of such companies subordinated to the local public authorities, they seem to be similar to those of public undertakings referred to by art. 86(1) of the EU Treaty, as they are further described in the *Transparency Directive* (Commission Directive 80/723/EEC of 25 June 1980 on the transparency of financial relations between Member States and public undertakings) and in the relevant decisions of the European Court of Justice (ECJ). As the ECJ stated in its ruling in *Cases 188-190/80 France, Italy, and the United Kingdom v. Commission*, "the expression "public undertakings' means any undertaking over which the public authorities may exercise directly or indirectly a dominant influence". The various situations falling within the scope of such influence are further detailed in the *Transparency Directive*, which was transposed into Romanian law by Competition Council Regulation as of May 21, 2004 concerning the transparency of financial realtions between public authorities and public enterprises as well as the financial transparency within certain enterprises. Moreover, the considerations applicable to public undertakings, deriving from the control exercised on their activity by the public authorities, are extended to undertakings accorded special or exclusive rights by the public authorities. Also, the existence of certain influence by the public authorities is implied by art. 86(2) of the EU Treaty in respect of undertakings entrusted with the operation of services of general economic interest or having a character of a revenue-producing monopoly, even if the are private companies, not formally controlled by public authorities.

The term "subordinated" is inadequate for describing potential beneficiaries of municipal guarantees, due to its lack of clarity. Its use by the successive legal provisions regulating local public debt may be a reflex of the existing situation in early '90s, when all public services were part of the administrative system and thus subordinated to the local public authorities. The current situation may not be much different, as privatization of local services remained a mere exception. But the regulations allowing for private operation of public services have significantly evolved under the influence of European rules. Today, if

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based on such regulations the operation of public services or other economic activities may be entrusted to private companies, the perception on the beneficiaries of municipal guarantees has also to evolve from subordination to a more comprehensive concept. There is no reason in principle for not allowing such guarantees for private operators if they are allowed for operators under public control. European rules on state aid and transparency of use of public funds are applicable in both cases, as the European regulations are neutral as concerns public or private ownership (Craig, de Búrca, 2008, p. 1071 *et seq*.).

The general category of guarantee beneficiaries shall also include in principle only legal persons, other than those specifically included in the other two categories of beneficiaries listed by the legal definition we are analyzing. Specific exceptions allowing for municipal guarantees to be issued for natural persons as beneficiaries may be also applicable. Although the text doesn't make any specific reference to legal persons, as in the legal definition of the guarantee beneficiary existing in the Public Finances Law (art. 2 lett. g), we believe such limitation is indirectly deriving from the cause of issuing such local public guarantees, as it is described in art. 61 par. 1 of the Local Public Finances Law, namely to secure loans exclusively directed to financing objectives of local public interest. As the beneficiaries of the municipal guarantees in this case may be either the public undertakings performing such investments or the private companies being concessionaires of the public assets, public works or public services, or a project company in case a public-private partnership is in place, it is quite hard to imagine an actual situation whereby a natural person may be the beneficiary of the local guarantee. Still, special regulations may be enacted allowing for public guarantees being issued in favour of natural persons who co-finance through a bank loan a special project addressed to a private asset in the ownership of such natural person, a project which involves also allocation of public funds. Currently, such projects are developed for the rehabilitation of private dwellings via a mixed public-private financing, secured by state guarantees.

If such exception would be provided by special regulations also for municipal guarantees, such amendment would envisage not only the extension of the beneficiaries' list, by adding natural persons to legal persons, but also a more significant change to a material limit to the use of municipal guarantees, namely the destination of the loan secured by municipal guarantees. According to art. 61 par. 1 of the Local Public Finances Law, such loan may be used only for financing public investments of local interest or for refinancing the local public debt.

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Whilst the assessment of the local public interest is within the exclusive power of the local council, as the deliberative authority, public investments are qualified as such only when referring to assets in the ownership of the administrative-territorial unit or meant to enter such ownership upon certain terms and conditions of the contracts entered by the administrative-territorial unit in respect of such assets, usually upon termination of the contract. This is the normal outcome of public works contracts, other public procurement contracts related to assets, concession contracts, delegated administration contracts or public-private partnership contracts.

Despite such general listing of beneficiaries in the legal definition, a narrower domain of the beneficiaries of the municipal guarantees may be drawn if we refer to other articles in the Local Public Finances Law. Its art. 63 par. 1 provides that may be guaranteed with the own incomes of the administrative-territorial units (i) loans undertaken by the administrative-territorial units as well as (ii) loans undertaken by the economic operators and by the public services subordinated to them. A similar but shorter list is included in art. 62 par. 3, which states that the obligations assumed by endorsing promissory notes issued by the economic operators or by the public services subordinated to the local public authorities are to be included in the local public debt. Subsequent regulations concerning the details (documents, steps etc.) of payment by the administrative-territorial units of obligations arising from the endorsement of promissory notes, namely art. 11 of the Order of Ministry of Public Finances no. 1235/2003 approving the methodological norms for the Emergency Government Ordinance no. 146/2002 regarding collection and use of funds through state treasury, are clearly referring to the promissory notes issued by economic operators and public services subordinated to the local public authorities.

Both texts in the Local Public Finances Law are unclear, especially if interpreting them in the sense of referring to specific forms of municipal guarantees, i.e. a security interest on certain incomes of the administrative-territorial unit (art. 63 par. 1) and endorsement of promissory notes (art. 62 par. 3). The main effect of such interpretation would be a strict application of these texts only for the types of municipal guarantees they are reflecting.

In case of endorsement of promissory notes, its own specificity may be deemed as sufficient argument for such strict interpretation. The text in art. 62 par. 3 seems to limit the beneficiaries of this type of municipal guarantee – endorsement of promissory notes – to public

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undertakings controlled by the local authorities. Still, the main aim of this legal text is not apparently focused on reducing the list of potential beneficiaries of municipal guarantees in case they are issued in the form of promissory notes endorsement, but on including the obligations assumed under such guarantee in the public debt. Such clarification was unnecessary since the overall features and effects of the endorsement of promissory notes were enough to unquestionably lead to such conclusion.

A significant issue is relating to the interpretation of art. 63 par. 1 – 3 of the Local Public Finances Law, especially of the legal effects of the "*guarantee on own incomes*" referred by these texts. Such interpretation is to be conducted on three levels, one meant to contribute to the determination of the list of potential beneficiaries of municipal guarantees, another aiming to determine whether the "guarantee on own incomes" is one of the many forms of municipal guarantees allowed under the applicable regulation or, to the contrary, is the only form of guarantee allowed, together with the specifically mentioned endorsement of promissory notes, and the last, which are the legal effects of such guarantee, when compared to security interests on receivables or other similar security interests created under the general regulations (i.e. Title VI of the Law no. 99/1999 or the Civil Code, as the case may be). We will analyse here only the first level, the second and the third being further developed in section 3 below.

The express statement referring to beneficiaries contained in both analysed texts, *i.e.* public undertakings controlled by the local authorities, may be regarded as being sufficient basis for a strict interpretation in the sense that no promissory notes other than those issued by such legal persons may be endorsed by the administrative-territorial units and no guarantees on own incomes may be issued for obligations assumed by other persons. In addition, art. 63 par. 1 states that such guarantees on incomes may be granted by the administrative-territorial units for their own public debt obligations. Such literal interpretation would further lead to the conclusion that all other municipal guarantees, if any, are available to all types of beneficiaries permitted by law, whilst endorsement of promissory notes and guarantees on incomes are valid only if used for securing obligations of public undertakings controlled by the local authorities or, in case of the latter, for own public debt obligations of the issuer.

Moreover, given the details for payment regulated by the Order of Ministry of Public Finances no. 1235/2003 approving the methodological norms for the Emergency Government Ordinance no. 146/2002

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regarding collection and use of funds through state treasury, any transfer ordered from the State Treasury to a bank account has chances of being refused by the clerks in the State Treasury if the endorsed promissory note is issued by another entity than those controlled by the endorser (subordinated to it, in the terms of the legal text). In the absence of a clear sense of the term "subordinated", a strict interpretation may be preferred, to include only those companies in which the public authority is a majority or sole shareholder. In this sense, a similar restrictive interpretation is contained in another secondary regulation, namely Annex 1 to the Government Decision no. 9/2007 approving the procedures for the Commission for authorization of public borrowings, which in its art. 1 par. 2 and 4 refers to municipal guarantees issued in favor of locally subordinated economic operators and public services, created by decisions of the deliberative authorities of the local public administration.

Since the guarantee assumed by endorsement is not meant to have more severe legal effects than other municipal guarantees, such solution is justified by neither economic nor legal reasons, at least for endorsement of promissory notes. As for the guarantee on own incomes, it may be deemed as having a material negative impact on the use of public funds collected from taxes and other regular sources of the local budget (but excluding those transferred from central budget) and therefore its beneficiaries be limited to the issuer itself and the public undertakings controlled by it.

In all cases, if such narrow sense is retained, the two types of municipal guarantee – guarantee on own incomes and endorsement of promissory notes - cannot be available, for example, to concessionaires of public assets, works or services, to delegated administrators of public utilities, or to project companies developing a public-private partnership, if they are not controlled by the local public authorities in terms of majority shareholding. Such solution is not at all the most appropriate for allowing local public authorities to use the instrument of municipal guarantees for credit enhancement and thus for supporting investments of local interest. Considering that the concession contracts, delegated administration contracts and public-private partnership contracts may provide for the obligation of the private contractor to complete an investment that will be transferred in the ownership of the administrative-territorial unit upon termination of such contract or at other moment agreed by the parties, such investment may be deemed as being public and of public interest and therefore benefit from the support of municipal guarantees.

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Based on these considerations, we believe a clarification of the legal definition of the municipal guarantee, in terms of issuer, forms and beneficiaries will enhance its use as public support for investments of local interest.

3. Guarantee on own incomes of the administrative-territorial unit. Security agreement. It is debatable if the legal provisions concerning the guarantee on own incomes in art. 63 par. 1 of the Local Public Finances Law intends to restrict the possibility of the local public authority to grant any other guarantees according to applicable laws or it only grants to such creditor a supplementary right, compared to other creditors of such local public authority, i.e. to obtain a guarantee on the public revenues of the respective local public authority (according to art. 5 par. 1 lett.a of this law, "*own incomes*" of the administrative-territorial units are including taxes, contributions, other amounts and quotas distributed from the income tax collected from natural persons).

A literal interpretation of art 63 par. 1 of the Local Public Finances Law would lead to the conclusion that this article purports to provide supplementary guarantee to the creditor and does not have a restrictive character, since it provides that the local public authority "may" create guarantees on its own incomes. *Per a contrario*, it may be held that the local public authority may also grant other guarantees, as provided by applicable law. Another argument may be that, according to article 2.324 (1) of the Civil Code, any person undertaking an obligation shall be liable with all its movable and immovable assets, either existing or future. In the absence of an explicit limitation, all general principles concerning the obligations shall apply to the local public authority in respect of its loan, guarantee or similar contracts.

Still, it is possible to argue that this provision intends to have a restrictive character since it is a measure of protection of the local public authority which is not able to engage its assets in order to guarantee such claim and, taking into account the amount of such public debts, to compromise its possibility to render public services or otherwise perform its activity.

We believe that the general provisions in the Civil Code concerning obligations should apply to public debt obligations, since the administrative-territorial unit appears as a party in a contract and undertakes obligations of civil nature. In this perspective, the Public Debt Law and the Public Local Finances Law are specific regulations, although having different degrees of specificity, and therefore shall apply as such,

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following the principle *specialia generalibus derogant*. Furthermore, the Local Public Finances Law concerns exclusively the local public finances and art. 63 par. 1 refers only to the guarantees on certain public revenues, having thus a precise object. Being a special law, it should not preclude the local public authority from granting any supplementary guarantees for the performance of its obligations. Therefore, the public authority should be able to grant to a certain creditor any contractual preference or priority allowed by law in respect of its assets in the private domain or of its revenues, provided such preference or priority are assimilated to guarantees and submitted to the specific limitations and rules provided by the Local Public Finances Law.

In accordance with the provisions of art. 63 par. 1 of the Local Public Finances Law, the local public authorities may secure their obligations under a loan agreement or the obligations assumed under a loan by the public undertakings under its control by creating a security interest on the public revenues of the respective local budget qualified as own incomes by art. 5 par. 1 lett.a. Such public revenues include taxes, contributions, other amounts and quotas distributed from the income tax collected from natural persons but are excluding the funds transferred from the state budget or other budgets, such as distributions from VAT collected at the central budget, transfers for a specific destination (completion of a public investment objective partially financed from central budget funds or other funds, remedy measures after a natural disaster etc.), as well as donations and sponsorship or any amounts received from the European Union or other donors. The special destination of such funds transferred from the state budget takes them out of the revenues of the local budget in respect of which the local public authority may decide the creation of a security interest.

The security interest created on such public revenues – own incomes of the administrative-territorial unit - shall follow the general rules in respect of its publicity with the Electronic Archive for Security Interests as well as the general rules in the Civil Code relating to security interests. From this perspective, the effect of the provisions in art. 63 par. 2 of the Local Public Finances Law remains unclear, being probably meant to create a privilege, as a preference cause, in the sense of art. 2.333 *et seq* of the Civil Code. Still, considering the new regulations in the Civil Code concerning privileges and the conflict amongst them and with other security interests, a further and much clear description of such cause of preference attached to the right of the creditor benefitting from a municipal guarantee on own incomes would be necessary.

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Moreover, we have to emphasize that the security interest on certain public revenues, payable under a general legal provision (*i.e.* budgetary debts, such as taxes, fines, and any amount not due under a contract) is not an assignment of receivables in the sense used in the commercial transaction, as the right of the state of or of the administrative-territorial unit to collect the public revenues may not be assigned to any person. Such security interest created by the state or the administrative-territorial unit on the public revenues arising from budgetary debts is a security interest on actual amounts, *i.e.* after they were collected by the state or by the administrative-territorial unit in accordance with the applicable rules.

Consequently, the public revenues arising from budgetary debts shall be always collected by their creditor, *i.e.* the state or the administrative-territorial unit and the lender shall have a security interest on such amounts. There is no legal possibility for the right of the state or of the administrative-territorial unit to collect public revenues arising from budgetary debts to be transferred to the secured lender, *i.e.* the lender cannot, in any case, collect directly taxes.

On the other hand, public revenues due under a contract, such as concession fees or rent under leases of the property of the administrative territorial unit, dividends etc., shall follow the general legal regime of an assignable claim, therefore a security interest may be constituted on the claim itself, *i.e.* on receivables and not only on the actual cashed amounts. Furthermore, the lender as assignee shall be entitled, upon default of the administrative-territorial unit under the loan agreement, to enforce such security interest and collect any payable amounts directly from the debtor (*i.e.* the concessionaire, the lessor etc.)

Still, considering the fact that the public revenues are cashed in the treasury accounts and not in commercial banks, practical problems may arise when trying to enforce such security interest on public revenues by seizure of such treasury accounts, given the special rules governing the functioning of the State Treasury and the enforcement procedures conducted against public authorities.

An issue to be further analyzed refers to the possibility of a creditor having a security interest on public revenues to assign such security interest or further create a security interest on it. Considering the absence of any legal provisions in this respect as well as, to our knowledge, the absence of any relevant practice, we believe that such assignment shall not be permitted under the general principles governing the public finances, for several arguments. The security interest on public

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revenues is an accessory to the loan agreement, which is a contract entered by the administrative-territorial unit following a competitive selection procedure, in consideration of the specific quality of the lender, i.e. an "*intuitu personae*" contract. Consequently, the security agreements, as accessories, shall follow the legal regime of the principal loan agreement, therefore shall not be assignable. Moreover, in case of enforcement of any claim against the administrative territorial unit for the release of public funds from the State Treasury, no payment will be possible to be made to a creditor and for a destination that are not specified in the relevant annual budget. Or, any assignee of a claim for payment against the administrative-territorial unit shall not be able to obtain such payment as it is not referred to in any relevant budgetary documents, including the local budget. The assignment of receivables due from the public budgets to private entities, regulated in art. 6^1 of the Emergency Government Ordinance no. 146/2002 regarding collection and use of funds through state treasury (this being a new article introduced in June 2011 by the Law no. 125/2011), is valid only if such receivables are arising from the operations described therein, *i.e.* from sale of assets, performance of services or of works to the benefit of the public authority.

3. Pre-conditions and limitations for issuance of municipal guarantees. According to the provisions in art. 61 par. 1 of the Local Public Finances Law, the local public authorities may issue guarantees for loans made exclusively for financing public investments of local interest performed by economic operators or public services subordinated to the local public authorities, irrespective if such loans are contracted with domestic or foreign creditors.

Considering such general legal provisions, it may be deemed that local guarantees may be issued upon cumulative existence of at least three preconditions: aim, being issued solely for securing a loan, beneficiary, being limited to public undertakings controlled by the issuer of the guarantee, and cause, being the loan destination, limited to financing a public investment of local interest. Such limitations allegedly derived from the general text of par. 1 of art. 61 of the Local Public Finances Law are not entirely aligned with those expressed in other texts of this law, therefore imposing a necessary interpretative effort in a domain where clarity should be the prevailing principle.

The first limitation refers to the underlying obligation secured by the public guarantee, whereby the text presented above expressly states that local guarantees may be issued for securing a loan. The same

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connection between the local guarantee and the loan it secures is restated by several other articles of the Local Public Finances Law, such as art. 62 par. 1, par. 9, par. 10, or art. 63. On the other hand, certain provisions of the same law, such as paragraphs 4, 10, 11, 12 of art. 63 are referring to "reimbursable financing". This is a defined term introduced as point 40 of the definitions' list in art. 2 of the Local Public Finance Law by the Emergency Government Ordinance no. 28/2008, and meant to cover "obligations of local public institutions arising from financing undertaken by local public debt instruments, on contractual basis or guaranteed by the local public administration authorities". The main consequence that may be directly derived from this apparently limitative reference to "loans" is that the local public authorities would not be entitled to issue guarantees for other types of financing.

When describing the local public debt instruments, art. 62 refers to local guarantees in two texts: art. 62 par. 2 lists in a general manner the local guarantee alongside the instruments of local public debt, whilst par. 3 of the same article includes in the public debt the endorsement by public authorities of promissory notes issued by the public undertakings controlled by the local authorities. But the alleged strict separation between loans, on one side, and all other forms of financing listed as local public debt instruments by art. 62 par. 2, namely bonds, commercial credit or financial leasing, is contradicted by the text of par. 1 of the same art. 62, which seems to allow equivalence between loan and all types of obligations included in the local public debt. According to the text, "The local public debt represents a general obligation which has to be repaid, according to the agreements concluded, from the own incomes of the administrative-territorial unit who borrowed the funds, as provided by art. 5 par. 1 lett.a, as well as from the incomes of the beneficiaries of the loans guaranteed by the local public authorities, as the case may be." [*author's underline*]. Also in a confusing manner, art. 63 par. 4 makes reference to both loans and reimbursable financings in the same phrase, but the terms seem to have equivalent sense.

The reading of the first part of art. 62 par.1 is that if the administrative-territorial unit undertakes financing via bonds, or commercial credit or financial leasing, all being specifically allowed forms of public debt, it becomes a borrower having an obligation to repay, and such obligation is part of the local public debt. If "borrower" may be a general term in case the administrative-territorial unit is a debtor of the principal obligation, to include all forms of financing, the same level of interpretation should be applicable in case the debtor is a public

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undertaking under its control and the administrative-territorial unit is a guarantor for such repayment obligation. Along the lines of this reasoning, the financing in any permitted form of a administrative-territorial unit as well as the issuance of guarantees for similar financing undertaken by undertakings under its control, should be included in the term "loan" as used by the Local Public Finances Law, which thus receives a broader sense. Such extended sense is in no way contrary to the economic or legal structure of such financing, irrespective of its form. Basically, funds are disbursed by a financier (creditor) to a debtor, in any of the forms described by art. 62 par. 2 and 3, thus generating a corresponding repayment obligation and the administrative-territorial unit may be a guarantor for such obligation, irrespective if such repayment obligation derives from a loan as such or from bonds, commercial credit or financial leasing.

In order for the local public authorities to start the procedure for undertaking a loan as a private source for the local budget, the precise destination of such funds has to be established and approved in advance.

Considering the legal limitations for the undertaking by a local public authority of a loan, a double decision of the local or county council, as the case may be, has to be made. First, the local or county council has to approve the use of the public funds resulting from the proceeds of the loan (*i.e.* public investments or repayment of the local public debt) and the loan as a source for such expenses. Usually such decision is made within the approval procedure of the local budget, considering that the destination of the funds in fact consists of expenses from the local budget and the loan is a source for the local budget. Moreover, no expense may be included in the local budget without the reference to the sources for its financing. As regards the public investments, the list of public investments objectives has to be approved by the local council as an annex to the local budget. Second, following the selection procedure for the lender, the local council has to approve the loan agreement as well as any related security agreements. Within its general powers and competences of control in respect of all issues related to public funds and their use, the Court of Audit shall be entitled to perform a control of the respective local public authority undertaking the loan for verifying the compliance with the applicable legal provisions.

The rights and obligations arising under any loan agreement for the administrative-territorial unit (as a contracting party) and for the lender shall not be in any way affected by the breach by the local public authority of the legal limitation in respect of the use of the proceeds of

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the loan. Furthermore, in accordance with the applicable budgetary principles under Romanian law, the repayment obligations under the loan shall have to be included as expenses in the local public budget for the respective years. In any case, even in the absence of a budget expression of such expenses, the permanent budgetary authorisation stated by art. 63 par. 9 of the Local Public Finances Law shall allow the enforcement of the due amounts under a public debt obligation even if such public expense is not expressly provided in the applicable local budget.

Formally, the issuance of municipal guarantees has to follow the special rules provided by art. 61, 62 and 63 of the Local Public Finances Law. The proposal for such issuance is to be made by the mayor, as the principal manager of public funds, has to be further advised upon by the Commission for authorization of local borrowing and finally approved by the local council with a majority of appointed local counselors.

Conditions of financial nature are requested to be fulfilled in order for an administrative territorial unit to be allowed to undertake public debt obligations, and therefore to issue guarantees. The first condition enables such undertaking only if the issuer's total annual outstanding debt, including the obligations under the proposed guarantee that may fall due within that year is below the threshold calculated according to the formulae in art. 63 par. 4 of the Local Public Finances Law. A second additional condition of financial nature was inserted in 2010, when a new paragraph 4^1 was added to art. 63, stating that shall not be allowed to undertake new public debt obligations those administrative-territorial units which (i) have not paid their outstanding obligations as of December 31 of the preceding year until the date they submit their request for advice to the Commission for authorization of local borrowing, or (ii) have ended the preceding year with a deficit of the operational section of their budget.

Both the threshold and the absence of unpaid obligations and of the operational deficit, shall not be applicable in case the public debt obligations are undertaken for ensuring pre-financing or co-financing of projects benefiting from pre-adhesion or post-adhesion nor reimbursable funds from the European Union. Also, the interdiction to undertake public debt in case of unpaid obligations or operational deficit shall not apply if public debt is assumed by administrative-territorial units which opened a financial crisis or insolvency procedure for refinancing purposes according to the recovery or insolvency plan.

In addition to such pre-conditions for assuming public debt obligations, the law provides for two specific limitations concerning the

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assumption of obligations to be included in the local public debt, therefore applicable for issuance of municipal guarantees: (i) an administrative limitation to the powers of the local council, represented by the prior approval (advice, in the language of art. 61 par. 3 of the Local Public Finance Law) of the Commission for authorization of local borrowing, appointed by the Government, and (ii) a financial limitation, whereby annual indebtness and disbursement ceilings are approved by the Government (following proposal by the Ministry of Public Finances, according to art. 63 par. 10 and par. 11 of the Local Public Finances Law). Both these limitations may be qualified as expressions of administrative tutorship (Dragoş, 2001, p. 77).

Once issued, municipal guarantees are to be registered in the special registry of the administrative-territorial unit and further reported for information purposes to the Ministry of Public Finances.

4. Legal effects of municipal guarantees. The obligations undertaken by the administrative-territorial unit by issuing municipal guarantees shall be public debt obligations, having the legal regime generally provided by the Civil Code for personal guarantees. The rules in the Public Debt Law for such obligations and in the Local Public Finances Law shall be of special application, in this order.

By issuing such municipal guarantees, the administrative-territorial unit becomes a party (subject) to a legal relationship generating obligations (Gaudemet, 2008, p. 478 *et seq*.). The administrative-territorial unit shall be a guarantor and its obligation to pay the principal debtor's (i.e. the beneficiary of the municipal guarantee) obligation if the latter fails to pay it shall be ancillary (Wadsley, Penn, 2000, p. 515 *et seq*., Ellinger, Lomnicka, Hooley, 2006, p. 849 *et seq*.) to the principal debtor's obligation.

In case the municipal guarantees are issued as promissory notes or as an endorsement of promissory notes issued by public undertakings under the control of the local public authorities, the issuer or the endorser has to be the administrative-territorial unit itself (city, county, etc.) having legal personality in accordance with the provisions of Law no. 215/2001 regarding local public administration. As representative of the issuer, the promissory note has to be signed by the mayor or, in case of a county, by the president of the county council, as a principal manager of public funds or another person to whom such powers were specially and expressly transferred in accordance with art. 21 (3) of the Local Public Finances Law. The promissory notes have to bear the stamp of the municipality.

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7. Conclusions. Considering the importance of the legal regime and effects of the public debt obligations undertaken by the administrative-territorial units, either by loans or other forms of financing or by guarantees, we believe a redrafting of the current provisions in the Local Public Finances Law is necessary. Currently, the existing provisions are focused on the decisional and procedural aspects of undertaking public debt obligations and their further administration and registration.

Although necessary, this approach does not cover all aspects entailed by the issuance of municipal guarantees. In our opinion the aim of a redrafting should be to add to existing procedural provisions clear regulations concerning the beneficiaries of the municipal guarantees and the forms such guarantees may take. These regulations have to be a reflexion of adequate public policies, allowing local public authorities to support local investments by municipal guarantees, subject to compliance with the procedures and limitations provided by law, including those concerning state aid. For this purpose, the beneficiaries of municipal guarantees should include concessionaires, public utilities operators entrusted with a delegated administration of such services, project companies within a public-private partnership and other private companies not subordinated or under the control of the local public authorities. Also, flexibility should be allowed to local authorities, under the supervision of the Commission for authorisation of local borrowing, in selecting and using the most adequate forms of municipal guarantees.

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