A LEGAL PERSPECTIVE ON THE CREDITWORTHINESS OF THE MUNICIPALITIES

BY

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1. BACKGROUND

In the current financial crisis in Sweden, in state finances, banking and the municipalities, the creditworthiness of the municipalities is being brought into question. This issue is not new, nor exclusively Swedish. Local government legislation in Germany and Norway still bears the marks of the financial crises of the 1920s. It is of fundamental interest, therefore, to examine history and compare the legal systems of other countries. Assessment of the municipalities' creditworthiness requires knowledge and understanding of their special position. A municipality cannot be compared to the state, nor to a private corporation; it is a legal entity *sui generis*, and its special position in society is reflected in the legislation pertaining to it. A brief summary of the special legal status of the municipalities is, therefore, necessary. This paper will deal with what distinguishes a municipality from, for example, a private corporation. The similarities between municipalities and private companies—e.g. the possibility of challenging a resolution adopted at a general meeting, the fundamental similarity between company and municipal audits, and the employer/employee relationship as provided under labour law—are of no relevance in examining the creditworthiness of the municipalities from the legal angle.

2. THE SPECIAL LEGAL STATUS OF THE MUNICIPALITIES

Compared with older Swedish constitutional laws, the 1974 Constitution Act sanctions local self-government and accords it special status in the constitution. According to its Ch. 1, sec. 1, para. 2, popular government is realized, *inter alia*, by means of a representative and parliamentary constitution and through municipal self-government. Pursuant to Ch. 1, sec. 7 of the Act, the municipalities may levy taxes in order to perform their tasks. According to Ch. 8, sec. 5, the basis for the institution of municipalities and municipal taxes is determined by law, as are the municipalities' obligations and authority. How these provisions affect the issue of whether a Swedish municipality can be adjudged bankrupt or whether municipal property

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can be taken in distress will be dealt with later. Suffice it here to say that private businesses are afforded no such corresponding constitutional protection.

A municipality is a compulsory association. Private initiative did not bring it into existence. A municipality can be dissolved only in the manner and under the conditions prescribed in the Institution of Local Government Act (SFS 1979:411). Basically, municipalities may be fused or divided up. These issues are judged by state bodies, the Crown Judiciary Board and, in the final instance, by the government. The law prescribes how the municipalities' assets and liabilities are to be dealt with. According to the final paragraph of sec. 6 of the Institution of Local Government Act, responsibility for a promissory note may be transferred from one municipality to another, irrespective of whether the creditor has given his consent. Such a provision, it may be said, indirectly indicates that the creditor's legal position could hardly deteriorate as a result of one municipality taking over the debts of another. It appears that behind such a provision lies the idea that each municipality always can, and must, discharge its obligations.

As opposed to a private company, a municipality cannot be dissolved or wound up "just like that", but only as prescribed by the Institution of Local Government Act.

Other legal provisions state that the municipality's activities, in principle, are restricted to its own territory (the localization principle) and shall serve the members of its own community, see Ch 2, sec. 1 and Ch. 2, sec. 7 of the 1991 Local Government Act. Among other things, this means that the "market" for municipal business operations is limited today compared with business activities conducted by the private sector. Thus, there is no competition "on equal terms".

Many municipal duties are obligatory by law and cannot legally be discharged by parties other than the municipality. For example, this includes the municipality's responsibility for primary education, the social services, the building and planning authorities, offices of public guardianship and trusteeship and the environment protection inspectorate. Within these areas there are many activities involving the exercise of public authority with respect to the individual. This constitutes the fundamental difference between the activities of local government and those of private enterprise.

The municipalities are subject to legal regulations that are different from those applying to private enterprise. Local or administrative appeals can be lodged against local government decisions. The municipalities are subject to supervisory control by the Parliamentary Ombudsman. The

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exercise of public authority in local government activities is vested with special responsibilities that involve penalties under the law and liability in damages. The municipalities enjoy the independent, constitutional right to levy taxes. This right is slightly circumscribed, e.g. by tax ceilings, but the basic principle stands. The effects of tax ceilings or similar restrictions imposed on the municipalities' financial freedom will be considered later.

3. SPECIAL RULES RELATING TO LOCAL GOVERNMENT'S FINANCIAL TRANSACTIONS

There are also special rules governing the municipalities' financial transactions.

The prohibition on mortgaging, set out in Ch. 8, sec. 13 of the 1991 Local Government Act, is of special interest. According to the main rule, the municipalities and county councils must not grant lien on their property as security for a debt incurred.

The rule was introduced as late as 1979, but is founded on older practices.[1] The prohibition on mortgaging applies to both real and movable property. This prohibition would appear to stem from the notion that the commitments of the municipalities and county councils are guaranteed by virtue of local government's discretionary powers of taxation and their total assets.[2]

This provision is also connected with the special provision in sec. 59 of the older Banking Companies Act (SFS 1955:183) which states that banks may issue loans without security to, inter alia, municipalities and county councils. Corresponding provisions are found in the statutes pertaining to loans of state funds.

Among other things, Ch. 2, sec. 13 of the 1987 Banking Companies Act (SFS 1987:617) states that banks may dispense with security if it is deemed unnecessary or if there are other special reasons for so doing. From the text it can be seen that an amendment on a point of substance was not intended in the case of the municipalities. The state, the municipalities and other borrowers deemed safe according to the present provisions[3] should be included among the cases where security is unnecessary when granting credit. Apparently the dubious option has been adopted of "legislating through the *travaux préparatoires*" instead of retaining the clear and explicit provision of the older Act. This point of view was also set out in the

[1] Parl. bill 1978/79:53 p. 18 ff.
[2] Kaijser-Riberdahl, *Kommunallagarna II* (Local Government Acts II) 1983, p. 549.
[3] Parl. bill 1986/87:12 p. 24.

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opinion submitted by the Swedish Association of Local Authorities of 16 November 1984 (mem. 1984:153), but was not taken into consideration by the legislator. The legal position is, however, unchanged.

The Enforcement Code (SFS 1981:774) also contains special provisions with respect to the state, the municipalities and the county councils. All the special provisions relate to the legal status of public entities as creditors, saying that during debt recovery procedure there is no need to lodge security or put up an advance payment or down payment, which is normally required of a creditor pursuant to Ch. 2, sec. 27, Ch. 10, sec. 16, Ch. 12, sec. 5 and Ch. 17, sec. 5 of the Enforcement Code. It can be assumed that behind the regulation lies, inter alia, the idea that no requirements for security, down payment or advance payment are necessary when public-sector bodies act as creditors. There are, however, no special provisions governing the role of the municipalities, the state or the county councils as debtors.

All in all, the rules outlined above rest on the premise that the municipalities and other public entities are, generally speaking, creditworthy even if they are in a difficult financial situation.

4. BANKRUPTCY LAW AND THE MUNICIPALITIES

The 1987 Bankruptcy Act, like its predecessors, contains few provisions relating to the municipalities.

A characteristic function of bankruptcy law is that if the claims of a number of creditors cannot be satisfied, the loss is to be borne proportionally, subject to modification brought about by instituting preferential rights in respect to individual debts. The adjudication order means that, with certain exceptions as prescribed by law, the debtor loses possession and control over his property. The estate is administered by a trustee in bankruptcy. The administration involves disposing of the assets and turning them into cash.

The issue of whether municipalities can be adjudged bankrupt is not dealt with in the *travaux préparatoires*, only in the principles of law derived from past decisions. Walin-Palmér[4] affirm that the new bankruptcy act does not help answer the question of what legal entities can be declared bankrupt. Walin-Palmér, without answering the question, refer to Welamson.[5] Welamson refers, *inter alia*, to older Norwegian doctrine—more of

[4] Walin-Palmér, *Konkurslagen* (The Bankruptcy Act), part I 1989 p. 10.
[5] Welamson, *Konkursrätt* (Bankruptcy Law), 1961 p. 25 ff.

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which later—in which it is assumed that a municipal association, in principle, can go bankrupt. At the same time, the difficulties involved in reconciling the application of normal bankruptcy legislation with the provisions applying to municipal operations are underscored. On occasion, this has given rise to special legislation to eliminate, or set constraints on, the possibility of instituting bankruptcy proceedings against a municipality, in which connection special rules were issued to safeguard the creditors' rights in the case of municipal insolvency. If the issue came to a head here, it would probably be regulated by the interposition of legislation. For his part, Welamson appears to rule out the idea that the state can enter into bankruptcy and declares that what applies to state activities probably also applies to the municipalities.[6] This has been understood to mean that it is fairly certain that a municipality cannot be adjudged bankrupt.[7]

In modern works on municipal law it has been affirmed that a Swedish municipality cannot go bankrupt. The independent right vested in the municipalities to levy taxes, and the impossibility of suspending municipal operations, that are prescribed by Local Government law are the reasons cited for this affirmation. Additionally, we have the municipalities' obligations according to special legislation. A trustee in bankruptcy cannot simply run down or wind up the activities, for example, of the primary school system or the social services, or ignore the decisions taken on planning and building matters.[8]

In connection with the appearance of the new Local Government Act, the issue was raised by the municipal law committee in their report "Financial Administration in the Municipalities and County Councils".[9] The committee states here that Swedish municipalities and county councils cannot go bankrupt, at least as long as their right to levy taxes is safeguarded by constitutional law. Hence the absence of detailed safeguard provisions for creditors of the type stipulated in the Companies Act.

The new Act also lacks special provisions to protect the rights of the municipalities' creditors. The advisory bodies to whom the act was referred for consideration did not call for such protection either. It has not been deemed necessary.

Lindquist-Losman also share the view that a municipality cannot go bankrupt, affirming that the provisions of the constitution concerning municipal administration prevent an administrator from taking over.[10]

[6] *Op cit*, p. 26.
[7] Walin-Palmér, *op.cit.*, p. 10.
[8] Kaijser-Riberdahl, *op.cit.*, p. 549, and Riberdahl in *TfR* 1987 p. 247 ff., especially p. 251).
[9] Den ekonomiska förvaltningen i kommuner och landsting, Ds C 1987:5 p. 39.
[10] Lindquist-Losman, *1991 års kommunnallag*, 1991, p. 128.

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5. OLDER DOCTRINE AND EXPERIENCE IN OTHER COUNTRIES

In older *Swedish* legal writing, it is affirmed that municipal property could be taken in distress and that a Swedish municipality could go bankrupt.[11]

The issue was debated, based on Norwegian circumstances, at the 1931 meeting of Scandinavian jurists as the matter was of burning interest for the Norwegian municipalities.[12] Some of the arguments are of current interest, while others have been overtaken by legal developments.

In *German* and *Swiss* law, these issues have been illuminated in a few older dissertations, the oldest of which is from 1885.[13] The principle involved in a German decision issued on May 3 1930 by the Oberverwaltungsgericht of Saxony is still of current interest. The town of Glashütte was declared bankrupt in the decision, but the bulk of the town's total assets were excluded as they served the interests of public law. In the case there was a special statute which allowed an exception to be made for "Objects..." that are "indispensable ... for the performance of the municipality's public duties". The point at issue in the case was how much should be withheld from the administration. In rejection of the municipality's claim, it was deemed that, inter alia, the municipality's real estate used as sports facilities and municipal allotment gardens as well as a piece of forest property should be included in the estate in bankruptcy. The situation was held to be clear in French law: state and municipal property was "inviolable" and could not be appropriated in bankruptcy proceedings nor be subject to debt recovery enforcement.

On *Danish* law at that time, the debate initiator—Professor Poul Andersen—held that bankruptcy could be accepted but with special limitations and constraints attached in respect to property used in mandatory operations, such as fire stations, court houses/town halls and waterworks. Andersen also held that the municipality's taxes receivable could not be included in the estate either. On the other hand, the question was raised as to whether municipal electric power plant property could be included in the estate assets.

The account of *Norwegian* law is primarily of interest from the point of view of legal history, as the present Norwegian Local Government Act contains special provisions on bankruptcy and debt recovery enforcement.

[11] Hagman, *Kommunallagarna*, 1926 p. 196, see also Riberdahl in *TFR*, 1987 pp. 250 f.

[12] See *Rättsliga tvångsmedel mot staten eller mot kommun* (Judicial Coercive Measures against the State or a Municipality), *Förhandlingarna å det femtonde nordiska juristmötet i Stockholm 1931* (Proceedings of the Fiftieth Meeting of Scandinavian Jurists in Stockholm 1931), p. 181 ff.

[13] Ibid p. 219.

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In a judgement of the Norwegian high court (NRt 1927 p. 529) it was established that a municipality could go bankrupt, but that this immediately led to the adoption of provisional legislation and the issue was subsequently regulated under the Norwegian Local Government Act, more of which later. The issue of whether debt recovery proceedings could be instituted against the municipalities was also debated.

6. THE NORWEGIAN LOCAL GOVERNMENT ACT

The 1954 Norwegian Local Government Act (NLGA) currently in force is the only one in the Nordic countries that expressly contains special rules relating to recovery of municipal debts. This must be viewed in the light of the events of the 1920s. According to sec. 56 of the NLGA, a Norwegian municipality cannot enter into bankruptcy. If a municipality cannot meet its obligations owing to difficulties of an enduring nature, obligatory notice to this effect must be given to the Ministry of Local Government. Until order is restored in the municipality's economy, rules are issued governing the order of preference of various debts, pursuant to sec. 57 NLGA. Debt recovery enforcement is permitted only under very limited conditions as stated in sec. 54 of the NLGA. The prohibition on mortgaging previously incorporated in the NLGA was abolished in 1978. A more detailed account of the provisions can be found in Hammer, Local Government Act with Annotations.[14] In the draft proposal for a new local government act (NOU 1990:13), these rules are largely left unchanged. The legislation committee conducted a detailed discussion of both the prohibition on bankruptcy and the restraints imposed on debt recovery enforcement and concluded that municipal operations are in essence so different from those of private enterprise that the provisions should be left largely unchanged. It was also held that there was virtually no real need for rules safeguarding the rights of creditors.[15] As the provisions were perceived by the committee as being static and showing little to indicate an active way out of the crisis, the committee proposed that the state be brought more into the picture as the governing and controlling body. It is proposed that where a municipality suspends payments, a supervisory board should be set up composed of representatives from the municipality and the Ministry of Local Government. This supervisory board is to adopt a new financial plan and a new annual budget and is to approve all payments during the period of suspen-

[14] Hammer, *Kommuneloven med kommentarer*, 1984 pp. 207 ff.

[15] For further details see *Forslag till ny lov om kommuner och fylkeskommuner* (Proposal for a New Local Government Act), NOU 1990:13 p. 250 ff.

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sion. The financial plan and budget should be sanctioned by the Ministry of Local Government.

7. DEBT RECOVERY PROCEEDINGS AND MUNICIPAL PROPERTY

As stated earlier, the Enforcement Code contains special provisions pertaining to the position of the municipality as a creditor only, not as a debtor. There is no explicit prohibition on enforcement proceedings to recover a municipal debt. The issue has never been examined in modern practice. The examples of older law cited by Hagman[16] do not elucidate matters.[17]

This was another of the issues raised at the proceedings of the 1931 meeting of Scandinavian jurists. The Danish side affirmed that debt recovery enforcement was possible, but with certain limitations concerning the nature of the property. Under Norwegian law then in force, the assets of the state and municipalities could be divided into "res extra commercium" and fiscal assets. The fiscal assets could be taken in distress, but not the public property assets.

In the debate, the Danish and Swedish jurists maintained that if debt recovery proceedings were permitted, then bankruptcy must also be permitted, and vice versa. Otherwise a smart creditor would be able to safeguard his interests and recover the debt while there was no possibility for less alert creditors to achieve equal distribution of the disposable assets.

The findings of a Swedish report of 1915 were also referred to, where a division of municipal assets into two categories was proposed: financial assets that would be subject to coercive measures and administrative assets that would be exempt from such measures. According to the experts' proposal, the County Administration Board would be vested with the authority and assume powers for compulsory administration of the municipality. The experts' proposal was based on the notion that it should never be possible to adjudge a municipality bankrupt. No legislation ever resulted from this proposal.

The matter is touched upon in modern works by Lindquist-Losman[18] who assert, with no detailed analysis, that there is nothing to prevent a creditor from obtaining an injunction ordering a municipality to pay and then having the senior enforcement officer distrain upon the municipal-

[16] *Op. cit.* p. 126.
[17] Riberdahl, *op cit.* p. 250.
[18] *Op. cit.* p. 128.

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ity's property. At the same time these authors dismiss the idea that a municipality can be adjudged bankrupt.

In one case, the County Administrative Court held that it was possible for the senior enforcement officer to execute a judgement ordering special care to be rendered in the form of group accommodation for the handicapped, but the Handicap Commission considered it doubtful as to whether the provisions in the Enforcement Code could be invoked when the defending party was a municipal board and where the enforcement issue was complicated. At the same time, the Commission stated that there was nothing in the wording of the statutes to preclude this.[19]

8. ASSESSMENT

The only real argument to support the idea that municipal bankruptcy is possible is the fact that the Bankruptcy Act does not exclude any group of debtors.

When the notion that a municipality could go bankrupt was accepted in the older doctrine, it was based on the condition that limitations were imposed in view of the municipalities' special nature. In the present author's view, the Bankruptcy Act would then need to have special provisions defining what property can be included in the estate in bankruptcy and what excluded. Expressly worded legal provisions lay behind the German decision as to what property should be included in the municipality's estate in bankruptcy. Experience from Norway teaches that whenever the issue of bankruptcy has arisen, special legislation has had to be adopted.

The fundamental difference now compared to older law is that the 1974 Constitution Act elevates the position of the municipalities. The Constitution ranks higher in the hierarchy of norms, above that of the Bankruptcy Act. In addition, the provisions concerning bankruptcy administration conflict with the performance of municipal operations as prescribed in the Local Government Act. Moreover, a municipality can only be dissolved in the manner prescribed in the Institution of Local Government Act.

The municipal right to levy tax provides another essential reason why a Swedish municipality cannot go bankrupt. There are, of course, equivalents to municipal income tax in other countries, but generally the rights conferred are not as far-reaching as in Sweden. If municipal taxes are not subject to constraints, clearly a municipality can always pay its debts. The question is, then, whether another assessment is warranted in the light of a freeze or ceiling on municipal tax.

[19] *Handikapputredningen* (Handicap Commission), SOU 1991:46 p. 448 ff.

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In earlier contexts, the Standing Committee on the Constitution has made pronouncements on the protection afforded by the constitution in relation to the municipal right to levy taxes. It has been stated that the protection afforded is not unconditional, that tax ceilings or a freeze can be imposed but that the law always provides scope for a free sector for the municipalities and a certain degree of freedom to establish municipal tax rates.[20] The constitutional latitude for imposing limitations on the right to levy tax has been debated, but the fact remains that even given the present extent of the provisional municipal tax freeze, the municipalities have recourse to an important source of income for which there is no counterpart in private enterprise. Neither can one assume that there will be a significant narrowing of the scope for municipal tax. The restraints possible relate, primarily, to municipal taxes above a given, rather high, ceiling. But provisional or permanent tax ceilings can cause significant financial difficulties for the municipalities. This may necessitate cutting back operations in real terms. However, the extent and aim of the current provisional ceiling is hardly likely to have an impact on the municipalities' capacity to pay their creditors. Faced with a financial crisis, the municipality, just like the state, would partly have to use tax revenues to pay its debts. Had municipal bankruptcy been envisaged, special rules would have been introduced in the Bankruptcy Act or the Local Government Act to regulate the conditions, as happened in Norway. The absence of regulations in this respect and the opinions reported when the 1991 Local Government Act came into being show that the necessity for such legislation was not envisaged.

Occasionally the question of municipal payment stoppage is raised. Under Ch. 2, sec. 8 of the Bankruptcy Act, the debtor is obliged to give an explicit declaration. In effect, this is a declaration of insolvency. As a Swedish municipality cannot go bankrupt and—disregarding temporary payment difficulties—can always pay its debts, it is today legally impossible for a municipality to declare a suspension of payment. Such a decision can be overturned in an appeal lodged by a member of the municipal community.

The position is somewhat more doubtful in the case of *distraint*. As opposed to bankruptcy, the execution of a distraint order involves, inter alia, merely the seizure of a particular object and not the entire assets. If, for example, a municipal agricultural property were to be taken in distress, no special administration would be required. The municipality's other operations would be unchanged.

[20] KU 1980/81:22, cf later KU 1981/82:6.

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One issue that does arise, though, is what property can be taken in distress? The exempted assets in Ch. 5 of the Enforcement Code are quite obviously not listed with distraint of Municipal property in mind. As was emphasized at the meeting of Scandinavian jurists, in such case constraints must be drafted. Property that the municipality needs for conducting its obligatory operations, e.g. schools and fire stations, should be exempted. The same idea of dividing municipal property into assets subject to, and assets exempt from, distress had been voiced by the experts in 1915. In Norwegian law, the possibilities of suing for distraint are severely limited under the NLGA.

In older legal writing, Sundberg[21] ventured a division into financial assets and administration assets, but it is debatable whether there are any legal grounds nowadays for such a division.

In fiscal legislation there is a division of real estate, in the sense that special buildings, as they are known, are not taxable under Ch. 2, sec. 2 and Ch. 3, sec. 2 of the Property Tax Assessment Act (SFS 1979:1152).

It is reasonable to assume that a similar division would be needed in the case of distraint upon municipal property. There are, however, no provisions in the Enforcement Code exempting municipal property from distraint, whereas there are special rules for the municipalities in their capacity as creditors. A reasonable interpretation, therefore, is that the Enforcement Code was not intended to be applicable to municipal property. If this were otherwise, active provisions relating to it would be found in the law. Indirectly, the prohibition on mortgaging municipal property set out in the Local Government Act can be construed as meaning that certain property may not be taken in distress to satisfy the claims of a creditor. The connection between the mortgaging prohibition and distraint is touched upon in the proposal for a new Norwegian local government act[22] which points out that after the prohibition has been lifted, creditors can bring increased pressure to bear to permit the pledging of municipal property.

Even were distraint of municipal property impossible, the municipality's creditors are hardly bereft of legal rights. To begin with, creditors can clearly obtain a writ of execution against a municipality. If a court orders a municipality to pay in a decision that has come into legal force, the municipality must abide by this decision without coercive measures needing to be adopted. The present author considers that this follows from the objectivity principle, as it is known, in Ch 1, sec. 9 of the Constitution Act governing public activities and is indirect affirmation that higher ethical

[21] Sundberg, *Allmän förvaltningsrätt*, (General Administrative Law), 1955 pp. 30 ff.
[22] NOU 1990:13 p 252.

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demands are placed on the public sector than on private enterprise. For example, if a municipal executive board in an official decision refuses to pay a debt proven in a court of law, the board's decision can be declared void in a municipal appeal. A review is to be conducted[23] of an attendant issue: that of elected representatives' personal responsibility and the sanctions applying if a municipality is in contempt of court. If such a system of sanctions were also to embrace contempt of a civil court, this would certainly be a more effective coercive remedy than the right of distraint under the Enforcement Code.

Even if someone wished to claim that it was theoretically possible for a municipality to go bankrupt, the requisite conditions would hardly arise.

According to Ch 1, sec. 2 of the Bankruptcy Act, insolvency means a situation where the debtor is unable to pay his debts and where this inability is not merely temporary. In extreme cases, a municipality may encounter payment difficulties but, for reasons outlined here, these difficulties are only temporary. The municipality has recourse to sufficient legal measures to make payment even though this may not always be immediate.

Conceivable measures are described in the following hypothetical scenario.

9. A CONCEIVABLE SCENARIO

What could happen if a municipality found itself in dire economic circumstances? An account will be given here of a conceivable scenario seen from the legal angle. The loans that have already been raised could hardly precipitate a crisis. Apart from fluctuations in interest rates, loan financing is fairly predictable. Major losses have been incurred in a few cases of the type where insurance companies or trade union organizations get involved in high-risk investments. As most municipalities do not indulge in such forms of investment, this is also atypical. It is more probable that a crisis situation would arise in a rather small municipality that has furnished guarantees not only to secure a supply of housing, but also for sport and recreation facilities. It is unpredictable when and if a guarantee needs to be discharged. At the same time, it is unreasonable to envisage a situation where all guarantees would have to be met simultaneously.

What can be done from the legal standpoint to ensure that a municipality will meet its obligations? If raising municipal taxes is out of the question, we have the theoretical possibility of raising municipal charges. Legal-

[23] KU 1990/91:38 pp. 90–92.

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ly it is possible, pursuant to sec. 35 of the Social Services Act, to charge full cost for services such as child care, home help, mobility service for the elderly and disabled etc. Were this to happen, demand would perhaps fall and consequently one could not expect a real rise in income. There would perhaps be an increase in the number of people entitled to assistance under sec. 6 of the Social Services Act. What is legally possible may perhaps not be politically possible. Normally, technical services are already charged at full cost. Therefore there is little actual scope for increased charges in areas other than the social services.

Municipal property could be sold. This would be primarily property used in the municipality's facultative operations, i.e. property not required by the municipality in order to fulfil its obligatory functions. It includes any forest or agricultural property or residential real estate. The problems involved here, as before, are financial and political, not legal.

From the legal standpoint, only the municipality's facultative operations can be wound up. A municipality need not provide consumer advice services, for example, nor any other activities concerning the arts or recreation. A municipality can cut off all allowances to organizations involved in, e.g., sports or the arts. If such allowances have been granted for a budget year, it is not certain that they can be done away with during a current budget year, cf. RÅ 1974 ref. 108 (proposed revision of study circle grants for the study year under review, held: lawful), but they can be scrapped the following year.

Concerning cut-backs in obligatory services, e.g. schools or the social services, the possibilities are narrower but are not ruled out. These services can be pruned to the "minimum standard" required under the respective special provisions.

The municipalities can also impose a freeze on investment in all projects where they are not legally bound under civil law to fulfil their commitments with respect to contractors or other parties to agreements.

The municipalities can also decide not to take on any guarantee commitments whatsoever, not even to secure housing. They are not legally obliged to furnish surety, not even for housing, but a decision to this effect would remove a foundation stone from the state housing loan system. Under the system, however, it is possible for the municipalities to take such a drastic step.

The Local Government Act stipulations requiring sound, economical management of municipal affairs embrace the idea that the municipalities should normally not borrow to finance the running of operations.[24] All in

[24] Parl. bill 1990/91:117.

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all, from the purely legal standpoint the municipalities have a wide range of options available to put their economy back on a sound basis. Under such circumstances municipal planning can, however, be ravaged by inconstancy on the part of the state, for example, over state contributions, or as a result of changes in the credit market. The legal measures available vary in effectiveness. In addition, they are not the decisive factors; the financial and political effects of various retrenchment systems must also be taken into account.

From the lender's point of view, it should be of no consequence *how* the municipalities conduct themselves in a crisis situation in order to pay their debts. Like the state, the municipalities are able to use a greater or lesser part of their funds to pay their liabilities or interest. From the self-government perspective, however, it is important that the municipalities reach these decisions themselves and do not have them imposed by the state, a trustee in bankruptcy or an enforcement officer. De lege ferenda there is no reason, therefore, to tighten legislation to allow the state authority—with its own economy in the doldrums—to impose some form of "compulsory administration" on the municipalities during a financial crisis.

One interesting observation is that if the municipalities form companies, there is no obstacle to having the companies declared bankrupt.

The possibilities of forming municipal-owned companies are, however, circumscribed under Ch. 3, sec. 16 of the Local Government Act.

10. CONCLUDING GENERAL REFLECTIONS

In conclusion, from the legal standpoint a Swedish municipality cannot go bankrupt and municipal property probably cannot be taken in distress. For distraint, however, the situation is more uncertain. As long as the municipalities, themselves, possess the legal means to put their affairs back on an even keel, there is no need for legislation or special rules.

It is erroneous to equate a weak municipal economy with a poor credit rating. Seen from the perspective of the legal system—and also from the purely factual perspective—all the municipalities are creditworthy, irrespective of their financial states. On this basis, there is no justification for imposing tighter credit restrictions with respect to the municipalities. As the losses incurred by the banks over the last few years relate to private borrowers and not to the municipalities, it would be more appropriate to adopt tighter restrictions in other cases.

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The present author considers that the banks and other credit institutes would be well advised to familiarize themselves with, and take regard to, the special status the municipalities enjoy in Swedish society. In the light of the arguments presented above, it is unreasonable to require higher interest or risk premiums and the like based on the view that some municipalities are deemed to have a low credit rating. This is an unreasonable stance and must stem from ignorance of the special status accorded the municipalities.

In a really extreme crisis—which is hardly the case at present—one cannot ignore the fact that the state actually has ultimate responsibility for the economy, a responsibility which also embraces local government finances. In a crisis, the state has recourse to remedies that, from the purely legal angle, are even wider than those open to the municipalities.

Firstly there is no ceiling on state taxation. Secondly the state has a monopoly on legislation. Thus changes in legislation could be made to permit a relaxation on some of the municipalities' obligatory duties, given the political will to do so. The municipal sector can be cut back or extended through legislation issuing from majority decisions in the Swedish parliament. However, unpleasant financial and political consequences can arise as a result of maximum utilization of these remedies. When the state is prepared to step in, with no formal obligation to do so, to help banks that have become enmeshed in financial difficulties, the municipalities and their creditors have even greater reason to assume that the state will shoulder joint responsibility during extreme crises in local affairs.

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