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LOCAL PUBLIC ENTREPRENEURSHIP AND JUDICIAL INTERVENTION IN A EURO-AMERICAN AND GLOBAL PERSPECTIVE

CHRISTIAN IAIONE*

I. INTRODUCTION

Local public entrepreneurship encompasses a variety of activities carried out by local governments designed to foster local economic development. In this Article, I present local public entrepreneurship as a windfall of the right to local self-government. In Part II, I discuss the competing scholarship on the role local governments take in competing with each other by creating incentives to entice citizens and businesses into their jurisdictions. Then, in Part III, I present the concept of local public entrepreneurship and detail how local governments utilize such activism in competition with other governments. In the following three parts, I examine the intersection of local self-government and local public entrepreneurship in the Italian, European, and American legal frameworks. I explore the impact of globalization on this phenomenon in Part VII. In the following part, I present two cases—one from the European Union (EU) and one from the U.S.—in which local public entrepreneurship played a major role. I examine how the European Court of Justice (E.C.J.) has discouraged local governments from engaging in such activities, thereby undermining the right to local self-government. By contrast, the U.S. legal system actively encourages a high level of local public entrepreneurship for the production of urban services and infrastructure. Finally, I advocate for the formal recognition of the economic liberty of

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local governments and the implementation of democratic counterbalances to such liberty as an alternative to judicial intervention.

II. *TOCCATA (OR PRELUDE)*. . . : THE HAYEK-HYPOTHESIS. LOCAL GOVERNMENTS AS COMPETING QUASI-COMMERCIAL CORPORATIONS¹

Since its birth, the Tiebout model² has divided the field of local government scholarship into two main schools of thought: its supporters and its critics. I build on Charles Tiebout's hypothesis that local governments compete with each other, but analyze this phenomenon from a slightly different perspective.

Tiebout's cutting-edge study theorized that local governments compete with each other for taxpayers by offering packages of local public goods at competitive tax-prices.³ From this standpoint, local governments act like private firms that compete for consumers by offering competitively priced goods. The "full mobility" of citizens is the crucial device ensuring efficiency. Taxpayers can leave inefficient cities for cities that produce preferred public services at lower tax-prices.

In the Tiebout model, local governments are not the dynamic players in the game of interlocal competition. Richard Briffault has underscored that the "dynamic element in the public sector marketplace is the individual, or, in Tiebout's terminology, 'the consumer-voter.'"⁴ Individuals have the ability to "shop around" between local governments, and the "multiplicity of localities assures a range of choices and increases the likelihood that one locality will approximate the mobile consumer-voter's preferences."⁵

1. *Toccata* is a piece of classical music mainly for organs, composed to emphasize the dexterity of the performer. Toccatas for the organ are often followed by an independent fugue movement. The fugue begins with a theme, known as the subject, stated alone in one voice. A second voice then enters and plays the same theme, beginning on a different degree of the scale. The remaining voices enter one by one, each beginning by stating the same theme (with their first notes alternating between the same two different degrees of the scale). The remainder of the fugue develops the material further using all of the voices and, usually, multiple statements of the theme. 11 THE NEW ENCYCLOPEDIA BRITANNICA 814 (15th ed. 1986).

2. See Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416 (1956).

3. *Id.* at 421–23.

4. Richard Briffault, *Our Localism: Part II—Localism and Legal Theory*, 90 COLUM. L. REV. 346, 400 (1990) ("The central mechanism for revealing public service preferences is relocation: 'The act of moving or failing to move . . . replaces the usual market test of willingness to buy a good and reveals the consumer-voter's demand for public goods.' By settling in a particular locality, 'the consumer-voter may be viewed as picking that community which best satisfies his preference pattern for public goods.' People decide on the taxes they want to pay and the type and level of services they want to receive by 'shopping around' among the various localities in a given metropolitan area before 'purchasing' by moving to the one that best fits their needs.").

5. *Id.*

Interestingly, Friederich Hayek, an ardent proponent of laissez-faire economics, supports an active role for local governments in their economies.⁶ According to Hayek, competition amongst local governments would encourage those entities

to offer a combination of advantages and costs which [make] life within their territory at least as attractive as elsewhere within the reach of its potential citizens. Assuming their powers to be so limited by law as not to restrict free migration, and that they could not discriminate in taxation, their interest would be wholly to attract those who in their particular condition could make the greatest contribution to the common product.⁷

The result would be “the revival of a communal spirit which has been largely suffocated by centralization.”⁸

These differing views of the role of local governments have seemed like mere “prophecies” destined to remain unrealized. However, aspects of these theories have recently materialized due to the globalization of social, economic and legal relationships.

6. 3 FRIEDERICH A. HAYEK, LAW, LEGISLATION AND LIBERTY, THE POLITICAL ORDER OF A FREE PEOPLE 146 (1979).

7. Hayek posits that:

Most service activities now rendered by central government could be devolved to regional or local authorities which would possess the power to raise taxes at a rate they could determine but which they could levy or apportion only according to general rules laid down by central legislature.

I believe the result would be the transformation of local and even regional governments into quasi-commercial corporations competing for citizens.

... The widely felt inhumanity of the modern society is not so much the result of the impersonal character of the economic process, in which modern man of necessity works largely for aims of which he is ignorant, but of the fact that political centralization has largely deprived him of the chance to have a say in shaping the environment which he knows. The great Society can only be an abstract society—an economic order from which the individual profits by obtaining the means for all his ends, and to which he must make his anonymous contribution. This does not satisfy his emotional, personal needs. To the ordinary individual it is much more important to take part in the direction of his local affairs that are now taken largely out of the hands of men he knows and can learn to trust, and transferred to a remoter bureaucracy which to him is an inhuman machine. And while within the sphere which the individual knows, it can only be beneficial to rouse his interest and induce him to contribute his knowledge and opinion, it can produce only disdain for all politics if he is mostly called upon to express views on matters which do not recognizably concern him.

Id. at 146–47.

8. *Id.*

III. . . . AND FUGUE: LOCAL PUBLIC ENTREPRENEURSHIP AND LOCAL SELF-GOVERNMENT

At the outset, it is necessary to use a heuristic tool to guide in the investigation of Hayek's hypothesis. The tool I utilize is the concept of local public entrepreneurship.⁹ This is the "fugue,"¹⁰ and it may have interesting ramifications for the study of competition amongst local governments. My goal is to carve out a principled justification for legislative and judicial intervention on behalf of local governments who regard such interventions as excessively burdensome.

For the purposes of the present study, I define "local public entrepreneurship" as embodying all the commercial and industrial activities in which local governments engage, either directly or indirectly, for the purpose of accomplishing their mission. Primarily, this mission is to foster the well-being of their constituency and, more notably, to encourage local economic development.¹¹ Local government economic activism should generate and retain business, drawing individuals and firms through expenditures on infrastructure, capital projects, public relations, marketing, and a vast array of other business-oriented initiatives.¹² The objective is to attract citizens, firms and investment into the jurisdiction and away from similar jurisdictions.

In order to accomplish their mission, local authorities must provide goods and services to both their actual and potential constituencies. As Baker and Gillette explain, "different localities distinguish themselves by offering different packages of goods and services."¹³ This creates a market of local goods and services. Citizen-consumers choose the city that maximizes their preferences at the lowest tax-price.

I look at this phenomenon from a slightly different perspective. Tiebout and his successors offered a consumer-oriented vision of local economic

9. I adapt the terminology used in ROBIN PAUL MALLOY, *PLANNING FOR SERFDOM: LEGAL ECONOMIC DISCOURSE AND DOWNTOWN DEVELOPMENT* 10 (1991).

10. *See supra* note 1.

11. *See, e.g.*, PAUL E. PETERSON, *CITY LIMITS* 22 (1981); Ann O'M. Bowman, *The Visible Hand: Major Issues in City Economic Policy* 7-8 (National League of Cities, Working Paper, 1987). According to Bowman's survey, 86% of mayors surveyed ranked economic development among their three top priorities and 36.5% ranked it as their highest priority. *Id.* at 8. Regarding the legal, political, and economic implications of public/private cooperation, urban development and revitalization, see also MALLOY, *supra* note 9. In the landmark case *Kelo v. City of New London*, 545 U.S. 469 (2005), the U.S. Supreme Court ruled that promoting economic development constitutes a "traditional and long accepted function of government." *Id.* at 484.

12. *See* Clayton P. Gillette, *Kelo and the Local Political Process*, 34 HOFSTRA L. REV. 13, 14 (2005).

13. LYNN A. BAKER & CLAYTON P. GILLETTE, *LOCAL GOVERNMENT LAW* 337 (3d ed. 2004).

entrepreneurship.¹⁴ In contrast, I embrace a business-oriented approach. My focus is on competition among local governments from the perspective of the supplier of public goods rather than from that of the buyer.

In dealing with the supplier's business strategies, I do not intend to cover supplier pricing policies. Therefore, I do not address how a local government's taxing power can be used when competing with other governments. That subject has been extensively discussed.¹⁵ The fiscal well-being of most cities largely depends on taxpayers—both private individuals and businesses—moving to, remaining in, or departing from the city.¹⁶ However, city taxing powers are constrained by “cross-cutting pressures to hold taxes low enough to make the city attractive to businesses and affluent residents while keeping taxes high enough to fund essential infrastructure and social welfare programs.”¹⁷ Hence, at some point, cities must use something other than fiscal incentives to influence the migration of individuals and businesses.

From this perspective, local governments seem close to fulfilling the Hayek hypothesis. Indeed, to foster economic growth, localities engage in a variety of activities aimed at creating a fertile environment for the birth of new enterprises or attracting more external investment. Not only do cities act as business operators, but they also choose the same tools that private firms utilize. Local governments rely increasingly on private corporate structures to deliver public goods. They also sign contracts and enter into complex transactions in order to build partnerships with each other or with private parties.¹⁸

Provided that localities must compete with each other, they need to be relatively free to define the bundle of goods and services offered to their constituents. Briffault explains that “a fundamental premise of the Tiebout hypothesis is that localities possess substantial discretion over local taxing, spending and regulatory decisions. Although this premise usually passes unstated, Tiebout's theory would make no sense without it, since it is this discretion that allows local governments to respond to consumer-voter preferences.”¹⁹

14. Tiebout, *supra* note 3, at 416–24.

15. See, e.g., WALLACE E. OATES, *FISCAL FEDERALISM* 126–40 (1972).

16. See PETERSON, *supra* note 11, at 32–37; Briffault, *supra* note 5, at 351.

17. Briffault, *supra* note 5, at 351.

18. Gilliam E. Metzger, *Privatization as Delegation*, 103 COLUM. L. REV. 1367, 1377–79 (2003).

19. Briffault, *supra* note 5, at 405.

Thus, as economic entrepreneurs, cities need sufficient discretion to design pro-business and business-like strategies. This includes discretion to decide how to best accomplish their mission and which instruments to utilize in reaching their goals. For example, local governments usually directly provide some public goods and services. However, for many municipalities, there is an alternative to public production: privatization. Privatization takes different forms, but in broad terms it involves private production with either public partnership, regulation or mere oversight.²⁰ There are two main reasons to choose privatization. First, it is debatable whether local governments always function the same as other public governmental entities.²¹ Second, in many cases, privatization is preferable when the service corresponds to a normal entrepreneurial activity any economic actor could engage in (e.g., debt issue) or relates to sectors where the public provision (and monopoly) could be limited to just a specific part.²²

In principle, local public entrepreneurship therefore grants localities the freedom to decide the “what” and the “how” of local economic development. However, in some legal systems such economic freedom is not fully protected, and in some it is at stake. The question then becomes “who” makes the choices about the “what” and the “how” of local government economic activism. Such authority could be found in the law, the judiciary or local governments themselves. The ultimate answer may also be greatly influenced by the role of globalization.

Before I turn to two case studies addressing this question, I need to make clear that I am assuming local public entrepreneurship is a product of the right to self-government that local governments hold in most highly decentralized legal systems. Therefore, in the next three parts, I briefly summarize how local self-government and local public entrepreneurship relate to each other in different legal frameworks.

20. The enduring debate between laissez-faire economics and public intervention is beyond the scope of this Article.

21. This public/private distinction has been increasingly blurred. See Roderick M. Hills, Jr., *The Constitutional Rights of Private Governments*, 78 N.Y.U. L. REV. 144, 150 (2003).

22. See Clayton P. Gillette, *Public Service: Opting Out of Public Provision*, 73 DENV. U. L. REV. 1185, 1186–87 (1996).

IV. THE ITALIAN LEGAL FRAMEWORK

A. *The Role of Local Governments Under the Italian Constitution After the 2001 Devolution Reform*

Recent reforms to Italian constitutional law have greatly altered the framework of local government powers.²³ In 2001, changes were made to Title V of the Italian Constitution, which defines the relationships between Italian regional and local governments, and in particular, to Article 118.²⁴

The Italian Constitution today grants autonomy to all sub-national levels of government. The entities composing the Italian Republic stand on equal footing, although they have different powers.²⁵ The most relevant innovations grant municipalities “administrative functions” and discuss the principles of subsidiarity, differentiation and adequacy. These principles serve as safeguards to prerogatives of localities and to effective and uniform standards in public goods delivery.²⁶

23. See Gian Franco Cartei & Vincenzo Ferraro, *Reform of the Fifth Title of Italian Constitution: A First Step Towards a Federal System?*, 8 EUR. PUB. L. 445 (2002); Erminio Ferrari, *Planning, Building and Environmental Law After the Recent Italian Devolution*, 8 EUR. PUB. L. 357 (2002); Gian Franco Cartei, *Devolution and the Constitution: the Italian Perspective*, 10 EUR. PUB. L. 33 (2004).

24. Constitutional Law no. 3 of Oct. 18, 2001, Gazz. Uff. no. 248 of Oct. 24, 2001, following Regional president direct election introduced by Constitutional Law no. 1 of Nov. 22, 1999, Gazz. Uff. no. 299 of Dec. 22, 1999 (ordinary Regions) and Constitutional Law no. 2 of Jan. 31, 2001, Gazz. Uff. no. 26 of Feb. 1, 2001 (special statute Regions).

25. Article 114 of the Italian Constitution states that “the Republic is constituted by Municipalities, Provinces, Metropolitan Cities, and the Regions and the State.” COST. (Italy), *reprinted in* CONSTITUTIONS OF THE COUNTRIES OF THE WORLD 25 (Gisbert H. Flanz ed., Oceana Publications, Inc. 2003). The original text, instead, stated the “the Republic is divided into Regions, Provinces and Municipalities.” MAURO CAPPELLETTI ET AL., *THE ITALIAN LEGAL SYSTEM* 306 (Stanford Univ. Press 1967). In addition, the second paragraph of Article 114 now extends to provinces, metropolitan cities and municipalities the legal status previously accorded only to regions by the repealed Article 115. Compare *id.* with COST. (Italy), *supra*. Accordingly, these entities share with the regions the same nature of autonomy with regard to their home rules and constitutionally entrenched powers and functions. Indeed, they are “autonomous entities with their own statutes, powers and functions in accordance with the principles established in the Constitution.” COST. art. 114 (Italy).

26. Article 118 provides:

The administrative functions are attributed to the Municipalities, save these which, for assuring a uniform exercise, shall be conferred to the Provinces, the Metropolitan Cities, the Regions and the State, on the basis of subsidiarity, differentiation and adequacy.

The Municipalities, the Provinces and the Metropolitan Cities are the title holders of their own administrative functions and of those conferred by State or regional law, to their respective competences.

The State law shall specify the forms of coordination between the State and the Regions in the matters referred to in letters b) and h) of the second paragraph of Article 117, and specifies other forms of agreement and coordination in the matter of the protection of the cultural heritage.

COST. art 118 (Italy).

Article 118 recognizes subsidiarity as a keystone of the right of self-government.²⁷ Accordingly, power is assigned “to the lowest practicable tier of social organization, public or private.”²⁸ The principle of subsidiarity calls for a flexible and dynamic distribution of powers. Powers should be assigned based on the local/non-local dimension of the collective interest and on the capability of the specific government to fulfill that interest. Therefore, an extensive degree of inter-local cooperation is required in order to reach the optimal dimension of delivery of several local services.

In my view, the principle of differentiation creates the right of local authorities to select the public responsibilities and services they provide to actual and potential residents.²⁹ This principle also recognizes the right of localities to choose how to discharge their duties.³⁰ But above all,

27. Article 118 also recognizes the principle of “horizontal subsidiarity,” pursuant to which all public authorities “shall favor the autonomous initiative of the citizens activity of general interest on the basis of the principle of subsidiarity.” *Id.*

28. Roderick M. Hills, Jr., *Is Federalism Good for Localism? The Localist Case for Federal Regimes*, 21 J. L. & POL. 187, 190 (2005).

29. This view does not match the opinion of the majority of current scholarship. Most scholars either read the principles of differentiation and adequacy as hendiadys or disregard the importance of the principle of differentiation. *See, e.g.*, Tania Groppi & Nicoletta Scatone, *Italy: The Subsidiarity Principle*, 4 INT’L J. CONST. L. 131 (2006); Beniamino Caravita Di Toritto, *Constitutional Reform: Local Government and the Recent Changes to Intergovernmental Relations in Italy*, in *THE PLACE AND ROLE OF LOCAL GOVERNMENT IN FEDERAL SYSTEMS* 149 (Nico Steytler ed., Konrad-Adenquer-Stiftung 2005); Peter Leyland et al., *Regional Government Reform in Italy: Assessing the Prospects for Devolution*, 2002 PUB. L. 242–51 (2002).

30. Article 117 provides that the Italian State has exclusive legislative competence in matters of “electoral legislation, organs of government and fundamental functions of Municipalities, Provinces and Metropolitan Cities.” COST. art 117 (Italy). Additionally, there are some services that any local government must provide to constituents in order to guarantee equal and uniform conditions of citizenship. This calls for a nationwide common denominator for public service delivery. The Italian Constitution also entrusts the central government with the legislative power to determine “the essential levels of well-being concerning civil and social rights which must be guaranteed on the entire national territory.” *Id.* Regions may decide to assign additional tasks. Central and regional governments transfer to local governments the necessary economic resources for this purpose. In addition, each local government has the power to decide whether to provide additional services and how to organize the distribution of such services. To this end, Article 119 establishes that

municipalities, the Provinces, the Metropolitan Cities and the Regions have financial autonomy of revenues and expenditures.

Municipalities, the Provinces, the Metropolitan Cities and the Regions have autonomous resources. They establish and apply their own taxes and revenues in harmony with the Constitution and according to the coordination with the principles of public finances and the tax system. They receive a share of the joint participation (*compartecipazione*) from the proceeds of the state taxes that are related to their territory.

The law of the State shall establish an equalization fund (*fondo perequativo*) without restrictions as to their destination, for (the benefit of) the territories with lesser fiscal capacity per inhabitant.

differentiation favors the right of local governments to politically and economically distinguish themselves in their mission to foster local development.

In this last regard, the 2001 reform indeed strengthened the regulatory powers and organizational autonomy of local authorities. Localities have been vested with the power to enact regulations relating to “the organization and the development of the functions attributed to them.”³¹ Thus, both national and regional laws detail what services will be provided and how local administrative functions will be exercised. A clear ruling from the Constitutional Court on this issue is still missing. States and regions should grasp the potential of these principles and promote competition and cooperation among municipalities at the local level. And, unfortunately, after more than five years, there has been little effort to implement the new constitutional principles recognizing local governments’ full-fledged status as autonomous entities.

B. Local Public Entrepreneurship in the Italian Legislation on Local Government

The Local Government Act of 2000 defines the legal status of local governments within the Italian governmental framework.³² Notwithstanding the recent constitutional reform, there have been minimal changes to this law.

Articles 3, 13, 112 and 113 are of prominent relevance. Articles 3 and 13 set forth the general scope of local government autonomy and require safeguards for local interests, as well as promotion of social and economic

The resources that are derived from the sources referred to in the previous paragraphs, are to enable the Municipalities, Provinces, the Metropolitan Cities and Regions to finance integrally the public functions attributed to them.

In order to promote economic development, the social cohesion and the social solidarity, to remove the economic and social inequalities (*squilibri*), to promote the effective exercise of human rights (*dirritti della persona*), or to pursue goals diverse from the normal exercise of their functions, the State allocates (*destina*) additional (*aggiuntive*) resources and effects special interventions in favor of specific Municipalities, Provinces, metropolitan Cities and Regions.

The Municipalities, Provinces, Metropolitan Cities and Regions have their own partimony, attributed according to the general principles, determined by State law. They may incur indebtedness only in order to finance expenditures for investment. Any guarantee by the State for such loans is excluded.

Id. art 119.

31. CONSTITUTIONS OF THE COUNTRIES OF THE WORLD, *supra* note 25, at 27.

32. Legislative Decree 267/2000 (Aug. 18, 2000); GAZZ. UFF. 277 (ordinary supplement) (Sept. 28, 2000).

development in local communities.³³ In particular, under Article 112, local governments are to provide “public services having as their object the production of goods and activities aiming at fulfilling social ends and to promote the civic and economic development of local communities.”³⁴

Article 113(5) provides that local public services of economic relevance, such as the operation and maintenance of methane gas, electric power, water distribution networks, public transportation networks and sanitation, are to be provided alternatively through: (a) a limited liability company selected through a competitive tendering procedure; (b) a limited liability company held jointly by the local government and a private partner selected through a competitive tendering procedure in compliance with national and EU competition law and in accordance with the guidelines enacted by the competent regulatory authorities; or (c) a wholly public-owned limited liability company, provided that “the local authority exercises over the person concerned a control which is similar to that which it exercises over its own departments and, at the same time, that person carries out the essential part of its activities with the controlling local authority or authorities.”³⁵ Overall, this legislation allows self-determination in the selection of local public goods and services as well as in the organization of services.

V. THE EUROPEAN LEGAL FRAMEWORK

Decentralization is a common denominator connecting several European countries. This focus on decentralization explains the attention paid to local government involvement in the European supranational context and in the ongoing discussion on EU governance reform. There appears to be a trend towards the promotion of local self-government and local public entrepreneurship.

A. *The Role of Sub-State Bodies in the European Charter of Local Self-Government*

The Council of Europe first recognized the basic concept of local actors in 1961, when it gave permanent status to the European Conference of Local Authorities. The Charter of this Conference was amended in 1975

33. *Id.* arts. 3, 31.

34. *Id.* art. 112.

35. *Id.* art. 113(5).

to define a “region” as a political entity.³⁶ The Conference’s working sessions led to the European Charter of Local Self-Government (European Charter)³⁷ and the Draft Charter of Regional Self-Government.³⁸

Article 2 of the European Charter provides the basic legal foundation for local self-government. Under the European Charter, “local self-government shall be recognised in domestic legislation, and where practicable in the constitution.”³⁹ This right to local self-government “denotes the right and the ability of local authorities, within the limits of the law, to regulate and manage *a substantial share of public affairs under their own responsibility and in the interests of the local population.*”⁴⁰

The European Charter specifies that the constitution or statutes of Member States should prescribe “basic powers and responsibilities of local authorities.”⁴¹ Beyond the basic constitutionally entrenched powers, the European Charter recognizes the right of local authorities to self-determination and to differentiate themselves from neighboring localities. Indeed, local authorities have “full discretion to exercise their initiative with regard to any matter which is not excluded from their competence nor assigned to any other authority.”⁴² Moreover, “[p]ublic responsibilities shall generally be exercised, in preference, by those authorities which are closest to the citizen. Allocation of responsibility to another authority should weigh up the extent and nature of the task and requirements of efficiency and economy.”⁴³ And, with regard to powers delegated by a

36. Resolution 61/20 of the Comm. of Ministers, Sept. 13, 1961 (Council of Eur.). Regions were added as members in 1975 by Resolution 75/4 of Feb. 19, 1975 (Council of Eur.). These resolutions are available at http://www.coe.int/T/CM/WCD/advSearch_en.asp#.

37. European Charter of Local Self-Government, *opened for signature* Oct. 15, 1985, Europ. T.S. No. 122, available at <http://conventions.coe.int/treaty/commun/QueVoulezVous.asp?NT=122&CL=ENG> [hereinafter Charter of Local Self-Government].

38. Draft European Charter of Regional Self-Government, June 5, 1997, available at www.ena.lu/Europe/council-europe/European-charter-regional-self-government-1997.htm. At least equal attention should go to the Assembly of European Regions, the purpose of which, under Chapter I, Article 1, para. 3 of its Statute, is

[t]o promote the institutional participation of the Regions in decision making processes and in order to do this increase their active role in the construction of Europe, especially in the work of the Council of Europe, of the Organisation for Security and Cooperation in Europe and of the European Union.

Statute of the Assembly of European Regions, June 14, 1985, available at http://www.a-e-r.org/fileadmin/user_upload/GoverningBodies/GeneralAssembly/Statutes/Statutes-200x/EN-statuts_naples2002.pdf.

39. Charter of Local Self-Government, *supra* note 37, art. 2.

40. *Id.* art. 3 (emphasis added).

41. *Id.* art. 4.

42. *Id.*

43. *Id.*

central or regional authority, “local authorities shall, insofar as possible, be allowed discretion in adapting their exercise to local conditions.”⁴⁴

Local governments are also given the right to determine the organizational means best suited to accomplish their goals: “local authorities shall be able to determine their own internal administrative structures in order to adapt them to local needs and ensure effective management.”⁴⁵ In addition, under Article 10 local governments can choose, “in exercising their powers, to co-operate and, within the framework of the law, to form consortia with other local authorities in order to carry out tasks of common interest.”⁴⁶ On a more international level, the European Charter specifies that local governments be able “to co-operate with their counterparts in other States.”⁴⁷

The European Charter includes principles regarding the administrative supervision of local authorities and, in particular, ensures that “the intervention of the controlling authority is kept in proportion to the importance of the interests which it is intended to protect.”⁴⁸ In addition, the European Charter also promotes the financial autonomy of local authorities. Pursuant to Article 9, local governments shall have

adequate financial resources of their own, of which they may dispose freely within the framework of their powers. Local authorities’ financial resources shall be commensurate with the responsibilities provided for by the constitution and the law. Part at least of the financial resources of local authorities shall derive from local taxes and charges of which, within the limits of statute, they have the power to determine the rate.⁴⁹

Finally, local authorities have “the right of recourse to a judicial remedy in order to secure free exercise of their powers and respect for such principles of local self-government as are enshrined in the constitution or domestic legislation.”⁵⁰

44. *Id.*

45. *Id.* art. 6.

46. *Id.* art. 10.

47. *Id.*

48. *Id.* art. 8.

49. *Id.* art. 9.

50. *Id.* art. 11.

B. The Role of Sub-State Bodies in EU Primary Law and EU Secondary Legislation and the Role of Regional and Local Governments in EU Soft Law and Policy Guidelines

Initially, local and regional authorities were completely cut out of the European integration process. This neglect stems from the absence of any reference to local actors in the European Community (E.C.) Treaties. On the E.C. secondary law level, the creation of the Consultative Council of Regional and Local Authorities (the Council) was an initial step towards the involvement of local governments in the EU decision-making process. In its directive creating the Council, the European Commission (the Commission) stated that it was necessary for regional and local authorities to become active “in the formulation and implementation of EU regional policy.”⁵¹ The goal was to create a decision-making body at the sub-state levels which had only consultative powers⁵² and was to meet only when convened by the Commission itself.⁵³

This Council represented the keystone of decentralization in EU governance. It eventually grew into the Committee of the Regions, as established in the Treaty on European Union.⁵⁴ However, despite the progress made in the Treaty of Amsterdam⁵⁵ and in the Treaty of Nice,⁵⁶ the Committee of the Regions remains a mere consultative body.

Nevertheless, the Commission has been a strong proponent of the decentralization of European governance structure. With its issuance of the *White Paper on European Governance*,⁵⁷ the Commission committed itself to: (a) establishing “a stronger interaction with regional and local governments and civil society [through] a more systematic dialogue with representatives of regional and local governments through national and

51. Comm'n Decision 88/487/EEC, Setting Up a Consultative Council of Regional and Local Authorities, dt pml., 1988 O.J. (L 247) 23.

52. *Id.* art. 1.

53. *Id.* art. 7.

54. Treaty on European Union, Feb. 7, 1992, 1992 O.J. (C 191) 1 [hereinafter Treaty on European Union].

55. Treaty of Amsterdam Amending the Treaty on European Union, the Treaties Establishing the European Communities and Certain Related Acts, 1997 O.J. (C 340) 1 [hereinafter Treaty of Amsterdam]. The Treaty of Amsterdam granted to the Committee of the Regions the ability to adopt its Rules of Procedure, an increase in the number of areas in which consultation is mandatory, the right to issue opinions on its own initiative, and the right of the European Parliament to seek its opinion. *See* E.C. Treaty, *infra* note 73, arts. 71, 128, 137, 175, 264, 275.

56. The Nice Treaty introduced two main amendments: members of the Committee must have a regional or local electoral mandate, and members cannot exceed 350. *See* E.C. Treaty, *infra* note 73, art. 263.

57. *Commission White Paper on European Governance*, COM (2001) 428 final (July 25, 2001).

European associations at an early stage in shaping policy;⁵⁸ and (b) bringing “more flexibility in the means provided for implementing legislation and programmes with a strong territorial impact” through target-based contracts between member states, territorial authorities, and the Commission.⁵⁹

In order to realize these commitments, the Commission adopted the *Report Dialogue with Associations of Regional and Local Authorities on the Formulation of European Union Policy*, which strengthened “the framework, goals and modalities governing this dialogue with associations of regional and local authorities,”⁶⁰ and *A Framework for Target-Based Tripartite Contracts and Agreements Between the Community, the States and Regional and Local Authorities*.⁶¹ According to this latter report, contracts are to be awarded to sub-national authorities within the Member States in order to realize particular objectives defined in “primary” legislation.⁶² Such contracts should include arrangements for monitoring.⁶³ In addition, the Commission recently introduced a new governance mechanism that tends to foster the connection between the EU and the national and local governments. This new approach is called the “open method of coordination” (OMC) and it serves as a general model in several policy areas.⁶⁴

Finally, decentralization was a primary focus of the proposed EU Constitution.⁶⁵ This document included a number of important features relating to regional and local governments. In summary, these features included:

58. *Id.* at 4.

59. *Id.* at 13.

60. Eur. Comm’n, *Dialogue with Associations of Regional and Local Authorities on the Formulation of European Union Policy*, COM (2003) 811 final (Dec. 19, 2003), available at http://www.cor.europa.eu/document/activities/com2003_0811en01.pdf.

61. Eur. Comm’n, *A Framework for Target-Based Tripartite Contracts and Agreements Between the Community, the States and Regional and Local Authorities*, COM (2002) 709 final (Dec. 11, 2002), available at http://ec.europa.eu/governance/docs/comm_contrat_en.pdf.

62. *Id.* at 2.

63. *Id.* at 3–4.

64. See, e.g., Eur. Comm’n, *Modernising Social Protection for the Development of High-Quality, Accessible and Sustainable Health Care and Long-Term Care: Support for the National Strategies Using the “Open Method of Coordination”*, COM (2004) 304 final (Apr. 20, 2004). See generally Susana Borrás & Kerstin Jacobsson, *The Open Method of Coordination and New Governance Patterns in the EU*, 11 J. EUR. PUB. POL’Y 185 (2004); Sabrina Regent, *The Open Method of Coordination: A New Supranational Form of Governance?*, 9 EUR. L.J. 190 (2003).

65. Treaty Establishing a Constitution for Europe, Dec. 16, 2004, 2004 OJ (C 310) 1.

- the explicit recognition of local and regional self-government;⁶⁶
- the extension of the subsidiarity principle to include local and regional government;⁶⁷
- the extension of the concept of cohesion to include *territorial* cohesion;⁶⁸
- safeguarding the prerogatives of the Committee of the Regions;⁶⁹
- monitoring of the subsidiarity/proportionality system;⁷⁰
- increased consultation with regional and local governments, and more awareness of the financial impact of EU policies on local and regional governments;⁷¹ and
- the right of the Committee of the Regions to refer subsidiarity issues to the E.C.J.⁷²

If implemented, these aspects of the proposed EU Constitution would strengthen the principle of multi-level governance and make it easier for citizens to engage in European policies, thus ensuring that EU priorities better reflect citizens' everyday concerns.

C. The Law on Standing of Sub-State Bodies to Bring an Action Before the E.C.J.

The legal status of sub-state bodies within the EU may have interesting implications for the determination of whether local governments have standing before the E.C.J. Such a right would increase the recognition of local governments within the EU framework. However, currently, the legal status of sub-national bodies in annulment proceedings before the E.C.J. remains in doubt.

According to some scholars, in the absence of an express definition of "State" in the EU treaties—especially for the purpose of Article 230 of the Treaty Establishing the European Community (E.C. Treaty)⁷³—"State"

66. *Id.* art. I-5.

67. *Id.* art. I-11.

68. *Id.* art. I-3.

69. *Id.* art. III-365.

70. *Id.* at Protocol on the Application of the Principles of Subsidiarity and Proportionality.

71. *Id.*

72. *Id.*

73. Consolidated Version of the Treaty Establishing the European Community, Dec. 24, 2002, 2002 O.J. (C 325), available at http://www.europa.eu/en/treaties/dat/12002E/pdf/12002E_EN.pdf

should be interpreted as referring to entities with the capacity to sign and ratify agreements between States that have some sort of independent power on a territorial basis.⁷⁴ By contrast, others infer from E.C.J. case law that the term “State” embodies a collection of authorities and tasks.⁷⁵ This scholarly debate adds little to the interpretation of the second paragraph of Article 230.

Unfortunately, the E.C.J. has provided little guidance on this issue.⁷⁶ In two of its orders, the E.C.J. declared the actions for annulment brought by the Région Wallonne⁷⁷ and the Regione Toscana⁷⁸ as manifestly inadmissible. The wording of both orders is almost identical:

it is clear from the general scheme of the Treaties that the term “Member State,” for the purposes of the institutional provisions and, in particular, those relating to proceedings before the courts, refers only to government authorities of the Member States of the European Communities and cannot include the governments of regions or of autonomous communities, irrespective of the powers they may have.⁷⁹

Without citing to the E.C. Treaty itself, the E.C.J. confirmed that the second and third paragraphs of Article 230 cannot be applied by analogy to the regions.⁸⁰

However, in matters other than direct actions, the E.C.J. has often widened the scope of the term “State” to include any body, whatever its legal form, responsible for providing a public service and, for that purpose, has special powers beyond those given by the rules applicable in

[hereinafter E.C. Treaty].

74. Manuel Pérez González, *La subjetividad internacional*, in INSTITUCIONES DE DERECHO INTERNACIONAL PÚBLICO 219 (Manuel Díez de Velasco Vallejo ed., Tecnos 2001).

75. Maryvonne Hecquard-Theron, *La notion d’État en droit communautaire*, 26 REV. TRIMESTRIELLE DE DROIT EUR. 693 (1990).

76. It is argued that there is still no formal judgment to support that case law. However, such procedural rigor seems unconvincing given that pleas of inadmissibility, and in particular manifest inadmissibility, are usually disposed of by way of an order, in accordance with Article 92(1) of the Rules of Procedure of the Court of Justice. Rules of Procedure of the Court of Justice, art. 92(1), 1991 O.J. (L 176). The same is true of questions referred for a preliminary ruling, “where the answer admits of no reasonable doubt.” *Id.* art. 104(3).

77. Case C-95/97, *Région Wallonne v. Comm’n*, 1997 E.C.R. I-1787 [hereinafter *Région Wallonne*].

78. Case C-180/97, *Regione Toscana v. Comm’n*, 1997 E.C.R. I-5245 [hereinafter *Regione Toscana*].

79. See *Région Wallonne*, *supra* note 77, at I-1787–88; *Regione Toscana*, *supra* note 78, at I-5245–46.

80. See also Case C-452/98, *Nederlandse Antillen v. Council of the Eur. Union*, 2001 E.C.R. I-8973 [hereinafter *Nederlandse*].

relations between individuals.⁸¹ The elasticity of the term “State” in the E.C.J.’s case law is also manifested by the use of that term in cases involving the failure of member states to fulfill their obligations under EU law. For example, Spain was found in breach of its obligations when local and regional bodies were actually to blame for the breach.⁸² Thus, if a regional or local authority fails to fulfill its obligations under EU law, the Member State in which that authority is located has been held liable.

Further broadening the definition of “State,” the E.C.J. has incorporated that term into the meaning of “public authority” when applying Article 39(4) of the E.C. Treaty.⁸³ The E.C.J. held that employment in the public service includes all offices “which involve direct or indirect participation in the exercise of powers conferred by public law and in the discharge of functions whose purpose is to safeguard the general interests of the State or of other public authorities.”⁸⁴ The concept of “public authorities” encompasses “State” as well as sub-state bodies. In making its determination, the E.C.J. followed a variable approach which adapted the concept of “State” in order to guarantee the effectiveness of EU law and maximize the integration process.

However, the E.C.J. has not extended a similar interpretation to provisions relating to the distribution of powers within the EU, as held in *Regione Toscana*:

If the contrary were true [if sub-state bodies had standing to bring an action of their own right], it would undermine the institutional balance provided for by the Treaties, which determine, inter alia, the conditions under which the Member States, that is to say the States party to the Treaties establishing the Communities and the Accession Treaties, participate in the functioning of the Community institutions. It is not possible for the European Communities to

81. See Case C-188/89, *A. Foster and Others v. British Gas*, 1990 E.C.R. I-3313. The European Court of Justice (E.C.J.) pointed out that it previously held that provisions of a directive could be used against tax authorities (Case C-8/81, *Ursula Becker v. Finanzamt Münster-Innanstadt*, 1982 E.C.R. I-53); local authorities (Case C-103/88, *Fratelli Costanzo SpA v. Comune di Milano*, 1989 E.C.R. I-1839); constitutionally independent authorities responsible for the maintenance of public order and safety (Case C-222/84, *Marguerite Johnston v. Chief, Constable of the Royal Ulster Constabulary*, 1986 E.C.R. I-1651); and public authorities providing public health services (Case C-152/84, *M. Marshall v. Southampton and South-West Hampshire Area Health Authority*, 1986 E.C.R. I-723).

82. See Case C-355/90, *Comm’n v. Spain*, 1993 E.C.R. I-4221, I-4271; Case C-417/99, *Comm’n v. Spain*, 2001 E.C.R. I-6015, I-6025; Case C-499/99, *Comm’n v. Spain*, 2002 E.C.R. I-6031, I-6056.

83. E.C. Treaty, *supra* note 73, art. 39(4).

84. Case C-66/85, *Deborah Lawrie Blum v. Land Baden-Württemberg*, 1986 E.C.R. 2121, 2147 (emphasis added).

comprise a greater number of Member States than the number of States between which they were established.⁸⁵

There has not been sufficient development of the legal status of local authorities to justify shifting the institutional balance discussed in *Région Wallonne* and *Regione Toscana*. For this reason, the E.C.J. recently confirmed this prior case law in its *Regione Siciliana* decision.⁸⁶

D. The EU Framework for Local Public Entrepreneurship

Local governments have always been indirectly involved in the implementation of EU structural policies and directly involved in enforcing EU sectoral policies. In this latter framework, the Commission recently adopted a report entitled *Cohesion Policy and Cities: The Urban Contribution to Growth and Jobs in the Regions*,⁸⁷ which promotes local public entrepreneurship and encourages participation in global competition.

The Commission first acknowledged that “European cities attract investment and jobs.”⁸⁸ The proposals of the Commission regarding cohesion policy suggested that cities should use the “many tools at their disposal to strengthen their attractiveness.”⁸⁹ According to the Commission, local governments should intervene in four key sectors: “transport, accessibility and mobility;⁹⁰ access to services and amenities;⁹¹

85. *Regione Toscana*, *supra* note 78, at I-5246. Almost identical wording is found in *Wallonne*, *supra* note 77, at I-1788.

86. Case C-417/04, *Regione Siciliana v. Comm’n*, 2006 E.C.R. I-3881. The E.C.J. ruled that an action by a local or regional entity cannot be treated in the same way as an action by a Member State, the term Member State within the meaning of the second paragraph of Article 230 EC referring only to government authorities of the Member States. That term cannot include the governments of regions or other local authorities within Member States without undermining the institutional balance provided for by the Treaty.

87. Eur. Comm’n, *Cohesion Policy and Cities: The Urban Contribution to Growth and Jobs in the Regions*, COM (2006) 385 final (July 13, 2006), available at http://ec.europa.eu/regional_policy/consultation/urban/com_2006_0385_en.pdf [hereinafter *Communication on Cohesion Policy and Cities*].

88. *Id.* at 4.

89. *Id.*

90. *Id.* at 5. “Sustainable urban mobility means making the best use of all the transport infrastructure, co-ordination between the various transport modes and the promotion of the least polluting modes.” *Id.*

91. *Id.* “A competitive city needs to invest in modern, efficient and affordable services with easy online access. Key services include healthcare, social services, training and public administration. These services must develop and adapt to current and future demographic changes, especially the aging population.” *Id.*

the natural and physical environment;⁹² [and] the cultural sector.”⁹³

In the Commission’s view, cities should support local economies by providing “a stimulating environment for innovation and businesses to flourish.”⁹⁴ City-level actions have an added value because cities “have more information on the specificities of the business environment and are able to carry out smaller scale complex actions tackling multiple interlinked problems.”⁹⁵ The Commission suggested two methods for promoting local economic growth: (a) actions taken for the establishment of new enterprises;⁹⁶ and (b) actions relating to innovation and the knowledge economy.⁹⁷ These proposals may induce local governments to step into the economic arena and even enter into partnerships with private actors or other public entities.

In terms of governance, the Commission encouraged “flexible co-operation between the different territorial levels.”⁹⁸ According to the report, “[c]ities must find forms of governance which respect the institutional organisation of each Member State and which are able to manage all aspects of urban development.”⁹⁹ The Commission set forth several guidelines. First, partnerships should be developed “between cities,

92. *Id.* “Rehabilitation of derelict brownfield sites and renovation of public spaces . . . improves local services and the local area, as well as avoiding the use of greenfield sites.” *Id.* at 6.

93. *Id.* at 5. “An active cultural policy is a valuable tool for building bridges between communities and fostering the integration of immigrants and other newcomers to the city.” *Id.* at 7.

94. *Id.* at 7.

95. *Id.*

96. *Id.* To promote business initiatives at the local level, local governments are required to improve their economic infrastructure. This requires “[p]roviding advice and support services to business, including social enterprises” as well as providing “assistance in the adoption and efficient use of new technologies, science parks, ICT [Information and Communication Technologies] communication centers and incubators. It also includes support and coaching in the areas of management, marketing, technical support, recruitment, and other professional and commercial services.” Also, local governments should work to build networks of “cooperation between local partners—including business, trade unions, universities, NGOs [non-governmental organizations], training institutes and the local community.” These support networks would assist in creating “[n]ew mechanisms for sharing knowledge and experience.” The financial aspects are, of course, particularly relevant.

[P]artnerships between local authorities, funders, service providers and SMEs [small and medium sized enterprises] facilitate the bringing together of financial and non-financial instruments, to meet local needs. Packages may consist of grants; micro credit schemes; guarantee funds for sharing high risks; mezzanine funds, advice and training.

Id.

97. *Id.* “Cities should attract and retain knowledge workers and, more generally, an important share of tertiary educated residents. A key input to choice is the attractiveness of a city in terms of transport, services, environment and culture.” *Id.* Furthermore, cities can “stimulate and co-ordinate partnerships and clusters of excellence with universities and other institutions of higher education, creating business incubators, joint ventures and science parks.” *Id.* at 7–8.

98. *Id.* at 11.

99. *Id.*

regions and the state, within the framework of an integrated and coherent approach to urban development.”¹⁰⁰ Also, cities should address the challenge of global competition by creating “strategies co-ordinated at the level of agglomerations or urban networks in order to achieve critical mass.”¹⁰¹ Particularly, the Commission hoped to promote “co-ordination between urban authorities (both central and suburban) on the one hand and rural and regional authorities on the other.”¹⁰²

In addressing urban economic growth, the Commission emphasized that “urban development is a complex and long term process.”¹⁰³ Therefore, cities should maximize all the key factors for this development by adopting a long term, integrated perspective.¹⁰⁴ Towards this goal, cities should enact economic measures that are “sustainable in social and environmental terms. Monitoring and evaluation systems should be in place to verify results on the ground.”¹⁰⁵ Finally, localities should include all key partners—“the private sector, the community and NGOs [non-governmental organizations], as well as local, regional and national government”—in planning, implementing and evaluating urban development.¹⁰⁶

Regarding financing, beyond EU Structural Funds urban development may be supported through private resources.

Private financing is useful and often necessary to complement public resources. A clear legal framework must underpin the setting up of public-private partnerships. The private sector brings not just money but complementary skills and competences. An effective public-private partnership requires both a strategic and long term vision and technical and management competences on the part of local authorities.¹⁰⁷

100. *Id.*

101. *Id.*

102. *Id.* Such co-ordination is important because

urban areas provide a service to the wider region in terms of employment, public services, public spaces, social centres, sport and cultural facilities; and because in a similar way, rural areas provide services to wider society through the provision of rural amenities, recreational opportunities and environmental goods as reservoirs of natural resources and highly valued landscapes.

Id.

103. *Id.*

104. *Id.*

105. *Id.* at 12.

106. *Id.*

107. *Id.* at 13.

Local public entrepreneurship is also recognized in the Commission's soft law regarding services of general economic interest. The Commission seems to leave wide discretion to local governments regarding what services are offered to constituents and how those services are provided. "However, providers of services of general economic interest, including in-house service providers, are undertakings and therefore subject to the competition rules of the E.C. Treaty."¹⁰⁸ Nevertheless, Member States have increasingly used "public-private schemes, including design-build-finance-operate contracts, concessions and the creation of mixed-economy companies to ensure the delivery of infrastructure projects or services of general interest."¹⁰⁹

In addition, with its *Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions*, the Commission sought to "launch a debate on the application of Community law on public contracts and concessions to the PPP [public-private partnership] phenomenon."¹¹⁰ The Commission clarified that it was not attempting "to make a value judgement regarding the decision to externalize the management of public services or not." Such a decision should remain "squarely within the competence of public authorities. Indeed, Community law on public contracts and concessions is neutral as regards the choice exercised by Member States to provide a public service themselves or to entrust it to a third party."¹¹¹ Quite similarly, Directive 2006/123 of the European Council states that its provisions should not be read to "oblige Member States either to liberalise services of general economic interest or to privatise public entities which provide such services or to abolish existing monopolies for other activities or certain distribution services."¹¹² Thus, the Directive "does not deal with the liberalisation of services of

108. Eur. Comm'n, *White Paper on Services of General Interest*, COM (2004) 374 final (May 12, 2004), at 15, available at http://eur-6x.europa.eu/LexUriServ/site/en/com/2004/com2004_0374eng01.pdf.

109. In particular, according to the White Paper Member States have a wide margin to decide how to organize services of general interest. In the absence of Community harmonization, the relevant public authorities in the Member States are in principle free to decide whether to provide a service of general interest themselves or whether to entrust its provision to another (public or private) entity. *Id.* at 15.

110. Eur. Comm'n, *Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions* 7, COM (2004) 327 final (Apr. 30, 2004), available at http://eur-lex.europa.eu/LexUriServ/site/en/com/2004/com2004_0327en01.pdf.

111. *Id.*

112. Council Directive 2006/123/EC, ¶ 8, 2006 O.J. (L 376).

general economic interest, reserved to public or private entities, nor with the privatisation of public entities providing services.”¹¹³

The position of the Commission primarily relies on principles of EU primary law. For example, Article 295 of the E.C. Treaty establishes a position of neutrality regarding public versus private ownership.¹¹⁴ In addition, Article 86 states that undertakings

entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly [are] subject to the rules contained in this Treaty, in particular to the rules on competition, [but only] in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them.¹¹⁵

VI. THE U.S. LEGAL FRAMEWORK AND DOCTRINE

When defining the right to local self-government within the U.S. legal framework, one cannot start without integrating this discussion into the broader framework of American federalism. At the outset, I briefly summarize the characteristics of U.S. federalist institutional design. In doing so, I adhere to Roderick Hills’s characterization of American federalism. According to Hills, “‘federalism’ is the body of legal rules protecting the power of ‘regional’, sub-national governments.”¹¹⁶ Hills asserts that regional governments have three defining characteristics: (1) they possess a “general power to collect taxes and expend revenue;” (2) they have “general regulatory power to govern territory containing several local governments;” and (3) they “define those local governmental powers through the regional laws.”¹¹⁷ Hills draws a parallel between the individual

113. *Id.* art. 1, ¶ 2.

114. “This Treaty law shall in no way prejudice the rules in Member States governing the system of property ownership.” E.C. Treaty, *supra* note 73, art. 295.

115. *Id.* art. 86. Article 16 of the E.C. Treaty is also relevant:

Without prejudice to Articles 73, 86 and 87, and given the place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social and territorial cohesion, the Community and the Member States, each within their respective powers and within the scope of application of this Treaty, shall take care that such services operate on the basis of principles and conditions which enable them to fulfill their missions.

Id. art. 16.

116. Hills, *supra* note 28, at 196.

117. *Id.* “‘Local governments’ are the atom of the system, for their laws do not define or control the powers of any ‘general purpose’ governments smaller than themselves, although their territory may encompass other, smaller local governments, as counties’ territory (for instance) encompasses

and collective right to self-government, concluding that: “[d]ecentralization is the backbone of self-government, both individual and collective. . . . Thus, collective self-government is simply the natural extension of the concept of individual rights.”¹¹⁸

However, aside from Hills’s suggestive and agreeable parallelism construing the right to local self government as an “‘inherent’ right of group association,”¹¹⁹ American legal scholarship seems profoundly divided on the actual legal status of local governments within the U.S. institutional framework. For some scholars, the city is a powerless creature of the state.¹²⁰ Others object that this view ignores empirical evidence depicting the city as “a complex local polity, entitled to self-governance and capable of supporting a local political system” and ultimately “a state in microcosm.”¹²¹

According to Richard Briffault, the difference between these two theses can be understood in light of the coexistence of Dillon’s Rule¹²² and home

municipalities.” *Id.* As to the foundations of the right of local self-government, Hills recalls Abraham Lincoln’s speech on the Kansas-Nebraska Act:

I trust I understand, and truly estimate the right of self-government. My faith in the proposition that each man should do precisely as he pleases with all which is exclusively his own, lies at the foundation of the sense of justice there is in me. I extend the principles to communities of men, as well as to individuals. I so extend it, because it is politically wise, as well as naturally just: politically wise, in saving us from broils about matters which do not concern us.

Id. at 189–90.

118. Hills, *supra* note 28, at 190–91 (“In short, there is no difference in principle between the considerations that justify collective individual self-government [. . .] [d]ecentralization serves the goal of self-government, whether the ‘self’ doing the governing is an individual, the members of a private organization, or the population of a local jurisdiction.”).

119. Roderick M. Hills, Jr., *Romancing the Town: Why We (Still) Need a Democratic Defense of City Power*, 113 HARV. L. REV. 2009, 2017 (2000).

120. See, e.g., Gerald E. Frug, *The City as a Legal Concept*, 93 HARV. L. REV. 1057, 1059 (1980); Gerald E. Frug, *Property and Power: Hartog on the Legal History of New York City*, 1984 AM. B. FOUND. RES. J. 673, 687–90 (1985).

121. Briffault, *supra* note 5, at 391–92.

122. A reader who is not familiar with U.S. local government law may appreciate a definition of these two concepts. In his *Treatise on the Law of Municipal Corporations*, John Forrest Dillon explained that while the powers of states exist except for express restrictions under the state or federal constitution, municipalities have only the powers that are expressly granted to them. JOHN F. DILLON, TREATISE ON THE LAW OF MUNICIPAL CORPORATIONS 101–02 (James Cockcroft & Company 1872). Thus “Dillon’s Rule” states that municipal governments only have the powers that are expressly granted to them by the state legislature, those that are necessarily implied from that grant of power, and those that are essential to the municipality’s existence and functioning. *Id.* at 102. Any ambiguities in the legislative grant of power should be resolved against the municipality so that its powers are narrowly construed. *Id.* However, when the state has not specifically directed the method by which the municipality may implement its granted power, the municipality has the discretion to choose the method so long as its choice is reasonable. *Id.*

rule,¹²³ which reflect the tension between differing perceptions of local governments. According to the former, the city is “a complex local polity, entitled to self-governance and capable of supporting a local political system.” But according to the latter, the city is an “administrative arm of the state, and as such both a potential threat to individual liberty and a hierarchically subordinate institution subject to state control.”¹²⁴

There is still debate about the proper scope of local autonomy. The legal discourse divides into two factions.

The two arguments emphasize different fundamental values: participation in public life in the one and efficiency in the provision of public sector goods and services in the other. Similarly, the theories rely on contrasting metaphors for the central mechanism of local public life: “voice” in the one case and “exit” in the other.¹²⁵ Yet the two tales told by political and economic theorists share a common commitment to localism.¹²⁶

These two separate traditions, although reliant on distinctive premises, converge on the general contention that local autonomy is the superior value in need of protection. Notably, a common denominator ties together the political and economic schools of thought: local public entrepreneurship.

Frug, the most prominent among participation theorists, suggests that local governments’ power should be enhanced so that they have the ability to, for example, operate banks, insurance companies, and other financial institutions, provide housing, create food cooperatives, and run for-profit

123. The “home rule” concept has been described as so:

Under governing principles of law, political subdivisions of a state cannot engage in any activity unless they have received explicit authority from the state legislature. The only exception to this rule exists where a locality has received “home rule” power either in the state constitution or from the state legislature. A locality that possesses “home rule” may initiate legislative programs without prior approval from the legislature. It seems relatively clear that the decision to contract with private firms for the provision of a particular good or service would be subject to this rule of plenary state power. Thus, a locality that desired to privatize one or more of its functions would presumably have to receive explicit authority to do so or would have to possess “home rule” power. The scope of “home rule” is itself somewhat ambiguous, though courts are likely to include within that category any activity that has minimal effects outside the jurisdiction.

Clayton P. Gillette & Paul B. Stephan III, *Constitutional Limitations on Privatization*, 46 AM. J. COMP. L. 481, 501 (1998). See also Gillette, *supra* note 22.

124. Briffault, *supra* note 5, at 391.

125. Here, Briffault is expressly referring to ALBERT O. HIRSCHMAN, *EXIT, VOICE, AND LOYALTY* (Harvard Univ. Press 1970).

126. Briffault, *supra* note 5, at 393.

businesses.¹²⁷ In Frug's view, municipal economic activism would transform local political life by empowering workers, the poor, and consumers.¹²⁸ Indeed, he contends that a municipal bank or insurance company "might make different judgments about the relative value it places on the profit margin, the kinds of loans that it deems socially useful, and the kinds of consumer protection it seeks to provide" than would private lenders.¹²⁹ Municipal ownership of housing "could prevent gentrification of these units, and encourage democratic control over the operation of multiple-family housing."¹³⁰ In other words, city-owned enterprises could provide socially-oriented and beneficial programs.¹³¹

In contrast, Ellickson, a prominent economic perspective legal scholar, argues that local governments already have relatively broad powers to participate in business activities.¹³² He contends that "during the twentieth century, state grants of power to cities have become more and more generous."¹³³ This is in part due to the fact that "state courts have considerably altered their interpretation of the constitutional and statutory texts that they once invoked to limit city business activities."¹³⁴ According to Ellickson, "Frug's 'powerless' local governments currently develop housing complexes, retail stores, office buildings, sports stadiums, and redevelopment projects. They rent tools; own and operate distant vacation resorts; sell at retail products such as gasoline, liquor, light bulbs, and sportswear; and lend money to home-buyers and business enterprises."¹³⁵ For example, in "Arizona, a state more rugged in its individualism than

127. See Frug, *The City as a Legal Concept*, *supra* note 120, at 1150; Frug, *Property and Power*, *supra* note 120, at 687–91.

128. See Frug, *The City as a Legal Concept*, *supra* note 120, at 1145–46.

129. See *id.* at 1150.

130. Frug, *Property and Power*, *supra* note 120, at 688.

131. *Id.* at 688–89.

132. Robert C. Ellickson, *Cities and Homeowners Associations*, 130 U. PA. L. REV. 1519, 1568–72 (1982).

133. *Id.* at 1569. Ellickson continues:

Current mainstream economic theory, which would limit the role of government to instances of market failure, seems today to have little more constitutional relevance in most states than Herbert Spencer's social statics.

... [T]he Supreme Court repeatedly held that the due process clause did not prevent states and cities from entering into businesses commonly carried out by private enterprise. Perhaps the broadest holding came in 1920, when the Court in *Green v. Frazier* [253 U.S. 233 (1920)] unanimously sustained the constitutionality of a North Dakota statute that authorized the establishment of state banks, state mills and grain elevators, state homebuilding agencies, and other state enterprises.

Id. at 1571–72.

134. *Id.*

135. *Id.* at 1570–71.

most, a constitutional provision explicitly authorizes all cities ‘to engage in industrial pursuits.’”¹³⁶

Local public entrepreneurship in the United States includes a variety of public policies, as well as legal and financing techniques, available to local governments to encourage economic development. Notably, local governments’ business-oriented activism encompasses the exercise of eminent domain for land acquisitions, public-private partnerships for urban renewal projects, issuance of debt and securities (e.g., industrial development bonds), and municipalization of (as well as re-municipalization of previously privatized) local services.¹³⁷ On a more corporate level, local public entrepreneurship entails establishing public authorities¹³⁸ and business improvement districts¹³⁹ to finance urban renewal projects or local public services, and to carry out development projects.¹⁴⁰

VII. GLOBALIZATION’S INFLUENCE ON LOCAL PUBLIC ENTREPRENEURSHIP

Economic globalization requires local governments to compete globally. The key features of the globalization of the world economy are mobility of capital, large scale division of labor, advances in communications technology, large-scale migrations of citizens and reductions in travel time.¹⁴¹ Those features thrust cities into a primary role in global governance.¹⁴² Globalization encourages local government to create horizontal networks that foster interlocal cooperation and forces

136. *Id.* at 1571.

137. See Shelley Ross Saxer, *Eminent Domain, Municipalization, and the Dormant Commerce Clause*, 38 U.C. DAVIS L. REV. 1505, 1515 (2005); see also Shelley Ross Saxer, *Government Power Unleashed: Using Eminent Domain to Acquire a Public Utility or Other Ongoing Enterprise*, 38 IND. L. REV. 55 (2005).

138. See Jonathan Rosenbloom, *Can a Private Corporate Analysis of Public Authority Administration Lead to Democracy?*, 50 N.Y.L. SCH. L. REV. 851 (2005–2006). “Public authorities are quasi-public independent entities generally created to provide one public service or undertake one public project such as transportation, school construction, housing, redevelopment, or financing.” *Id.* at 851 n.1.

139. Richard Briffault, *A Government for Our Time? Business Improvement Districts and Urban Governance*, 99 COLUM. L. REV. 365, 414–17 (1999).

140. *Id.* at 420–25.

141. John Friedmann, *The World Cities Hypothesis*, in *WORLD CITIES IN A WORLD SYSTEM* 317–18 (Paul Knox & Peter Taylor eds., 1995).

142. For the first academic accounts of this relatively new phenomenon, see generally Yishai Blank, *Localism in the New Global Legal Order*, 47 HARV. INT’L L.J. 263 (2006); Yishai Blank, *The City and the World*, 44 COLUM. J. TRANSNAT’L L. 875 (2006); Gerald E. Frug & David J. Barron, *International Local Government Law*, 38 URB. LAW. 1 (2006).

them to implement the programs of international organizations.¹⁴³ The result is a diminution in national institutional and legislative influence over cities.¹⁴⁴ In their new global standing, cities have become the object of international organization policies that promote new forms of urban governance¹⁴⁵ and development strategies,¹⁴⁶ and they are now subject to international trade and investment agreements¹⁴⁷ and arbitral decisions.¹⁴⁸

The United Nations Human Settlements Programme (UN-HABITAT) and other international organizations comprised of city governments are attempting to codify the right to self-government in international law.¹⁴⁹

143. Examples of such networks are United Cities and Local Governments, a group that advocates democratic local self-government, and the Cities Alliance, launched in 1999 by the World Bank and the United Nations Human Settlements Programme (UN-HABITAT). On the emergence of sub-national networks, see generally ANNE-MARIE SLAUGHTER, *A NEW WORLD ORDER* (2004).

144. See John Friedmann, *The World City Hypothesis*, in *WORLD CITIES IN A WORLD-SYSTEM* 317 (Paul L. Knox & Peter S. Taylor eds., 1995).

145. See UN-HABITAT, *THE GLOBAL CAMPAIGN ON URBAN GOVERNANCE CONCEPT PAPER* (2d ed. 2002), available at <http://www.unhabitat.org/governance> (follow "Reports" hyperlink); UN-HABITAT, *INTERNATIONAL LEGAL INSTRUMENTS ADDRESSING GOOD GOVERNANCE 5* (2002), available at <http://www.unhabitat.org/governance> (follow "Reports" hyperlink; document under "Legislative Reform"). Also, see generally UN-HABITAT's Global Campaign on Urban Governance, and in particular, information on Legislative Reform and the Campaign Overview, available at <http://www.unhabitat.org/categories.asp?catid=25> (follow "Legislative Reform" and "Campaigns" hyperlinks). For discussion of new forms of urban governance, see generally NEIL BRENNER, *NEW STATE SPACES: URBAN GOVERNANCE AND THE RESCALING OF STATEHOOD* (2004); CITY MATTERS: COMPETITIVENESS, COHESION AND URBAN GOVERNANCE 349-403 (Martin Boddy & Michael Parkinson eds., 2004); CITIES TRANSFORMED: DEMOGRAPHIC CHANGE AND ITS IMPLICATIONS IN THE DEVELOPING WORLD (Mark Montgomery et al eds., 2003).

146. THE WORLD BANK, *CITIES IN TRANSITION 20* (2000), available at <http://go.worldbank.org/V8UGUNCWKO> (last visited Nov. 8, 2007). See generally the World Bank's Comprehensive Development Framework, available at <http://go.worldbank.org/GS7LSYDFHO> (last visited Nov. 8, 2007); UNITED NATIONS, *MONTERREY CONSENSUS ON FINANCING FOR DEVELOPMENT 5* (2002), available at <http://www.un.org/esa/ffd> (last visited Nov. 8, 2007). For more general information on the World Bank's urban development projects and policies, see the World Bank's website section on "Urban Development," <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTURBANDEVELOPMENT/0,,menuPK:337184~pagePK:149018~piPK:149093~theSitePK:337178,00.html> (last visited Mar. 9, 2008).

147. On this subject, see generally ELLEN GOULD, *INTERNATIONAL TRADE AGREEMENTS: RECENT DEVELOPMENTS OF INTEREST TO LOCAL GOVERNMENTS* (2004), available at <http://www.civicnet.bc.ca> (follow "Publications" hyperlink; "Guide to Info Services" hyperlink); H.V. SAVITCH & PAUL KANTOR, *CITIES IN THE INTERNATIONAL MARKETPLACE* (2002); Ward Ferdinandusse, *Out of the Black-Box? The International Obligation of State Organs*, 29 *BROOK. J. INT'L L.* 45, 66-71 (2003); Saskia Sassen, *Introduction*, in *GLOBAL NETWORKS: LINKED CITIES* (Saskia Sassen ed., 2002).

148. Vicki Been & Joel C. Beauvais, *The Global Fifth Amendment? NAFTA's Investment Protections and the Misguided Quest for an International "Regulatory Takings" Doctrine*, 78 *N.Y.U. L. REV.* 30, 59-86 (2003).

149. See UN-HABITAT & World Associations of Cities and Local Authorities Coordination, *Towards a World Charter of Local Self Government: Initial Draft Text of a World Charter of Local Self Government*, <http://www.gdrc.org/u-gov/charter.html> (last visited Nov. 8, 2007) [hereinafter *Initial Draft Text of a World Charter*].

They have drafted a World Charter of Local Self-Government (World Charter) that has yet to be presented to the UN General Assembly. It reveals the current state of international legal scholarship regarding local government.¹⁵⁰ Many aspects of the World Charter resonate with the European Charter, which has been in force since 1988.¹⁵¹

However, at the global level there has been a greater emphasis on the role of cities as international economic actors.¹⁵² The “world cities” concept acknowledges the importance of local public entrepreneurship and partially resembles that of Martinotti’s third-generation cities—cities with the goal of attracting worldwide investment.¹⁵³ At the same time, this concept stresses the importance of democratic participation and poverty reduction policies.

The World Bank maintains that “[u]rbanization, when well managed, facilitates sustained economic growth and thereby promotes broad social welfare gains,”¹⁵⁴ while emphasizing the need for cities to become livable, competitive, and bankable.¹⁵⁵ This requires that cities eliminate burdensome regulation and transaction costs, facilitate public-private partnerships, and promote best practices. The World Bank’s stated goal is to improve the lives of the poor in the world’s cities.¹⁵⁶

150. The draft recognizes and requires protection in domestic legislation of local self-governance. *Id.* art. 2. As to the meaning of local self-government, the draft includes therein “the right and the ability of local authorities, within the limits of the law, to regulate and manage a substantial share of public affairs under their own responsibility and in the interests of the local population” *Id.* art. 3. On the level of financial autonomy, local authorities shall hold “adequate financial resources of their own, of which they may dispose freely within the framework of their powers.” *Id.* art. 9 § 1.

151. See Charter of Local Self-Government, *supra* note 37.

152. SASKIA SASSEN, *THE GLOBAL CITY: NEW YORK, LONDON, TOKYO* 3–4 (1991). Today, cities function in four new ways: first, as concentrated command points in the organization of the world economy; second, as key locations for finance and specialized service firms, which have replaced manufacturing as the leading economic sectors; third, as sites of production, including the production of innovations in these leading industries; and fourth, as markets for the products and innovations produced.

Id.

153. Guido Martinotti, *A City for Whom? Transients and Public Life in the Second-Generation Metropolis*, in *THE URBAN MOMENT: COSMOPOLITAN ESSAYS ON THE LATE-20TH-CENTURY CITY* 165 (Robert A. Beauregard & Sophie Body-Gendrot eds., 1999). Martinotti elaborates three stages of cities. “First generation” cities serve their own residents and focus on providing them municipal services. *Id.* at 160–62. “Second generation” cities emphasize their relationship with nonresident users, such as tourists and commuters, and focus on attracting these outsiders by building convention centers, sports stadiums, theme parks, and the like. *Id.* at 162–65. “Third generation” cities’ main goal is to attract worldwide business and focus on making the city attractive to business executives. *Id.* at 165.

154. THE WORLD BANK, *CITIES IN TRANSITION*, *supra* note 146, at 2.

155. *Id.* at 8–14.

156. *Id.* at 1.

The Cities Alliance¹⁵⁷ follows the World Bank's Cities in Transition approach, proposing that "[c]ities and towns are essentially markets,"¹⁵⁸ and that it is essential to unleash their potential by modernizing economies with city-supported infrastructure and private investments.¹⁵⁹ "The most fundamental requirements for a productive urban economy include available and affordable land for firms and for housing and transport networks that promote the mobility of both goods and workers."¹⁶⁰ UN-HABITAT adopts a similar strategic vision. It seeks to "promote pro-poor urban governance"¹⁶¹ and views "the city as an organizing agent for national development."¹⁶² In its Global Campaign on Urban Governance, UN-HABITAT emphasizes governance rather than government and the strategic value of public-private partnerships and democratic participation, making "stakeholder" consensus a key feature of local decision making.¹⁶³

VIII. TWO CASE LAW STUDIES

This section presents case studies from two opinions, one each arising out of the E.C.J. and the U.S. Supreme Court. In both cases, the courts scrutinized local government economic entrepreneurship. This entrepreneurship played a major role in fostering local government innovation and enhancing community well-being in both cases. However, as I discuss, E.C.J. jurisprudence currently discourages local governments from engaging in such activities, thereby undermining the right to local self-governance. Conversely, the U.S. legal system actively encourages local public entrepreneurship in order to facilitate urban services and infrastructure.

157. The Cities Alliance is an organization focused on poverty reduction and on creating "cities without slums."

158. Cities Alliance, *2004 Annual Report* 4, available at <http://www.citiesalliance.org>.

159. *Id.* at 3.

160. *Id.* at 7.

161. Governing Council of UN-HABITAT, *Update of the UN-HABITAT Strategic Vision* § 36, U.N. Doc. HSP/GC/19/INF/10 (Apr. 25, 2003), available at http://www.unhabitat.org/downloads/docs/1785_31621_K0361420.pdf.

162. *Id.* § 3.

163. *See generally* UN-HABITAT, THE GLOBAL CAMPAIGN ON URBAN GOVERNANCE CONCEPT PAPER, *supra* note 145. In addition, the Founding Declaration of United Cities and Local Governments blends the defense of local democracy with the enhancement of cities' "strategic role in economic development." United Cities and Local Governments, *Founding Congress Final Declaration* § 21 (2004), available at <http://www.dsf-fsn.org/en/documents/Declaration-UCLG-en.pdf>.

A. *The EU Debate on In-House Operations*

In recent years, the E.C.J. has developed substantial jurisprudence on “in-house operations.” Under the “in-house” umbrella, public authorities award public contracts to entities that have a distinct legal personality but are partially or wholly owned by the contracting authority itself.¹⁶⁴ The E.C.J.’s findings, together with the analysis provided by the Advocates General, represent dissatisfaction with this concept of local public entrepreneurship.

1. *The Teckal Criteria and the Substantive Scope of the In-House Exemption*

The first opportunity for the E.C.J. to consider in-house operations came in *Gemeente Arnhem v. BFI Holdings BV*.¹⁶⁵ At issue was whether the award of a public service contract to a public limited liability company jointly incorporated by two Dutch municipalities was subject to E.C. public procurement rules. Advocate General La Pergola contended that the company’s formation was a measure of administrative reorganization and the award of public responsibilities to the company was to be construed as an “inter-department delegation,” thereby escaping the scope of the (old) Public Service Contracts Directive.¹⁶⁶ However, the E.C.J. did not address this issue.¹⁶⁷

164. Advocate General Kokott explains in *Parking Brixen*,

In-house operations *stricto sensu* are transactions in which a body governed by public law awards a contract to one of its departments which does not have its own legal personality. *Largo sensu*, however, in-house operations may also include certain situations in which contracting authorities conclude contracts with companies controlled by them which do have their own legal personality. Whereas in-house operations *stricto sensu* are by definition irrelevant for the purposes of procurement law, since they involve transactions wholly internal to the administration, in-house operations *largo sensu* (sometimes called ‘quasi-in-house operations’) frequently raise the difficult question whether or not there is a requirement to put them out to tender.

Case C-458/03, *Parking Brixen GmbH v. Gemeinde Brixen*, 2005 ECR I-8585, http://eur-lex.europa.eu/RECH_jurisprudence.doc (follow “Advocate General’s Opinion,” “Search”) (last visited Nov. 9, 2007). There are three in-house or quasi-in-house scenarios: an award to a company wholly owned by a contracting authority or entity equated with that authority; an award to a joint public company, the shares of which are held by a number of contracting authorities; and, a award to a semi-public company, in which genuinely private parties hold a majority or minority stake. *Id.*

165. Case C-360/96, *Gemeente Arnhem v. BFI Holding BV*, 1998 E.C.R. I-6821 [hereinafter *Gemeente Arnhem*]. See also Rhodri Williams, *The “Arnhem” Case: Definition of “Body Governed by Public Law,”* 8 PUB. PROCUREMENT L. REV. 5 (1999); Evangelia Papangelis, *The Application of the EU’S Works, Supplies and Services Directives to Commercial Entities*, 9 PUB. PROCUREMENT L. REV. 201 (2000).

166. *Gemeente Arnhem*, *supra* note 165, at I-6840. See also Rhodri Williams, *The Scope of the EC*

R.I.SAN Srl v. Comune di Ischia concerned a public service contract awarded to an Italian company, the capital of which was held as to 51% of the contracting authority itself and as to 49% of a central government undertaking.¹⁶⁸ Advocate General Siegert Alber maintained that whether one contracting authority exercises a “decisive influence” over another entity is determinative of whether an “in-house” relationship exists.¹⁶⁹

In its landmark *Teckal* decision,¹⁷⁰ the E.C.J. forged a hermeneutic method that has subsequently been adopted to evaluate in-house operations in all cases. *Teckal* concerned the direct award to an interlocal consortium (forty-five municipalities) of a contract to operate the heating systems of several municipal buildings, including the contracting authority.¹⁷¹ The key issue in the case was whether granting a public service to an entity of which the contracting authority is a member is subject to the detailed E.C. rules on public procurement. The E.C.J. carved out the basic elements of an in-house operation and extended it to relations between a contracting authority and entities having a distinct legal personality, provided that certain conditions are met. Most notably, an in-house relation exists if “the local authority exercises over the person concerned a control which is similar to that which it exercises over its own departments and, at the same time, that person carries out the essential part of its activities with the controlling local authority or authorities.”¹⁷²

Thus, substantive subordination to the contracting authority of a publicly-controlled legal entity in regards to decision-making and operating functions does not trigger the applicability of E.C. rules on public procurement. As to the scope of the in-house derogation, *Teckal* generalized the principle explicitly foreseen only in Article 6 of the Public Service Contracts Directive and extended the application of the in-house rule to public contracts outside public services.¹⁷³

Public Procurement Directives: An Analysis of the Arnhem Decision, 8 PUB. PROCUREMENT L. REV. 43, 49 (1999).

167. *Gemeente Arnhem*, *supra* note 165, at I-6851–52. The E.C.J. canvassed instead the corporate structure of the company to establish whether it constituted a “body governed by public law” (i.e., having legal personality, subject to public control and established for meeting needs in the general interest, not having an industrial or commercial character), falling therefore within the scope of the “in-house” explicit exemption set forth in Article Six of the old Public Service Contracts Directive. *Id.*

168. Case C-108/98, *R.I.SAN. Srl v. Comune di Ischia*, 1999 E.C.R. I-5219, I-1542.

169. *Id.* at I-5234. On the basis of functional considerations, he concluded that even without knowing all the organizational details of the entity in question, it formed a part of the Italian State by the mere fact that the state owned 100% of its shares. *Id.* at I-5234–35.

170. Case C-107/98, *Teckal Srl v. Comune di Viano*, 1999 E.C.R. I-8121 [hereinafter *Teckal*].

171. *Teckal*, *supra* note 170, at I-8147–249.

172. *Id.* at I-8154.

173. The contract at issue concerned both the provision of services and the supply of goods.

Since *Teckal*, the E.C.J. has broadened the scope of “in-house” services to include public supply and infrastructure works contracts,¹⁷⁴ as well as concession agreements¹⁷⁵ granted by a public authority,¹⁷⁶ whereby the local government, acting as a contracting authority, exercises oversight over the awardee company substantially equivalent to that exercised on its own internal services, and the awardee dedicates the majority of its activities to the authority that controls it.¹⁷⁷

However, as the value of the latter was greater than the value of former, the E.C.J. ruled on the basis of the old Public Supplies Contracts Directive. *Id.* at I-8152–53.

174. Case C-26/03, *Stadt Halle v. Arbeitsgemeinschaft Thermische Restabfall-und Energieverwertungsanlage TREA Leuna*, 2005 E.C.R. I-1; Case C-29/04, *Comm’n v. Rep. of Austria*, 2005 E.C.R. I-9705; Case C-340/04, *Carbotermo SpA v. Comune di Busto Arsizio*, 2006 E.C.R. I-4137 [hereinafter *Carbotermo*].

175. See Council Directive 04/18, art. 1 § 4, 2004 O.J. (L 134) 114. A “‘service concession’ is a contract of the same type as a public service contract except for the fact that the consideration for the provision of services consists either solely in the right to exploit the service or in this right together with payment.” *Id.* at 127. A similar definition is drawn for public works concessions. *Id.*

176. See Case C-231/03, *Consorzio Aziende Metano v. Comune di Cingia de’ Botti*, 2005 E.C.R. I-7287; Case C-458/03, *Parking Brixen GmbH v. Gemeinde Brixen*, 2005 E.C.R. I-8612 [hereinafter *Parking Brixen*]; Case C-410/04, *Associazione Nazionale Autotrasporto Viaggiatori (ANAV) v. Comune di Bari*, 2006 E.C.R. I-3303 [hereinafter *ANAV*]. “Notwithstanding the fact that, as Community law stands at present, [public services or works concession contracts] are excluded from the scope of Directive 93/38, the contracting entities concluding them are, none the less, bound to comply with the fundamental rules of the [E.C.] Treaty, in general, and the principle of non-discrimination on the ground of nationality, in particular.” Case C-324/98, *Telaustria Verlags GmbH v. Telekom Austria AG*, 2000 E.C.R. I-10745, I-10746 [hereinafter *Telaustria*]. The E.C. Treaty prohibits discrimination on grounds of nationality. E.C. Treaty, *supra* note 73, art. 12. Regarding provisions on public service concessions, Article 43 states, “restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited.” *Id.* Also, “restrictions on freedom to provide services within the Community shall be prohibited in respect of nationals of Member States who are established in a State of the Community other than that of the person for whom the services are intended.” *Id.* art. 49. The E.C.J. interprets Articles 43 and 49 as specific expressions mandating equal treatment. See Case C-3/88, *Comm’n v. Italy*, 1989 E.C.R. 4035, 4059. It interprets the prohibition on discrimination on grounds of nationality similarly. See Case 810/79, *Überschär v. Bundesversicherungsanstalt*, 1980 E.C.R. 2747, 2764–65. In its case law relating to Community directives on public procurement, the E.C.J. affords equal opportunity to all tenderers when formulating their tenders, regardless of their nationality. See Case C-87/94, *Comm’n v. Belgium*, 1996 E.C.R. I-2043, I-2076, I-2097. As a result, the principle of equal treatment of tenderers must be applied to public service concessions, even absent nationality discrimination. In addition, the principles of equal treatment and non-discrimination imply a duty of transparency, which enables the concession-granting public authority to ensure that they are complied with. It “consists [of] ensuring, for the benefit of any potential tenderer, a degree of advertising sufficient to enable the service market to be opened up to competition and the impartiality of procurement procedures to be reviewed.” *Telaustria, supra*, at I-10746.

177. In *Stadt Halle*, the E.C.J. held that:

A public authority which is a contracting authority has the possibility of performing the tasks conferred on it in the public interest by using its own administrative, technical and other resources, without being obliged to call on outside entities not forming part of its own departments. In such a case, there can be no question of a contract for pecuniary interest concluded with an entity legally distinct from the contracting authority. There is therefore no need to apply the Community rules in the field of public procurement.

Moreover, the E.C.J. has asked for the fulfillment of the *Teckal* test in cases where the purpose of the procurement laws is to ensure a transparent and non-discriminatory selection of private contractors could have no foundation. In *Commission v. Spain*,¹⁷⁸ the E.C.J. upheld the application of *Teckal* to inter-administrative cooperation agreements formed between two or more public legal entities. This determines whether the contract in question falls under the scope of the Public Procurement Directives or under the “in-house” exemption. In *Commission v. France*¹⁷⁹ and more recently in *Auroux v. Commune de Roanne*,¹⁸⁰ the E.C.J. utilized the *Teckal* test for urban renewal projects. *Auroux* concerned a redevelopment agreement for a brownfield area and the construction of a leisure center in Roanne, France.¹⁸¹ The Municipal Council authorized the mayor to sign a contract with a semi-public company owned by the Region of Loire.¹⁸² The Court stated that the agreement showed that the construction of the leisure center was intended to house commercial and service activities designed to regenerate an area of Roanne, thus fulfilling an “economic

Stadt Halle, *supra* note 174, ¶ 48.

178. Case C-84/03, *Comm’n v. Spain*, 2005 E.C.R. I-139; Martin Dischendorfer, *Issues under the EC Procurement Directives: A Note on Case C-84/03, Commission v Spain*, 14 PUB. PROC. L. REV. 78 (2005).

179. Case C-264/03, *Comm’n v. France*, 2005 ECR I-8831.

180. Case C-220/05, *Auroux v. Commune de Roanne*, 2007 E.C.R. I-389.

181. *Id.* ¶¶ 13–14.

182. *Id.* ¶ 2. In 2002, the French municipality of Roanne decided, as an urban development measure, to construct a leisure center in the area close to the railway station, including a multiplex cinema, commercial premises, a public car park, access roads and public spaces. *See id.* ¶ 13. The construction of other commercial premises and a hotel were envisaged subsequently. *Id.* In order to implement this project, the municipality of Roanne awarded a semi-public development company (the *Société d’équipement du département de la Loire*), to acquire land, obtain funding, carry out studies, organize an engineering competition, undertake construction works, coordinate the project and keep the municipality informed. *Id.* ¶ 15. The Administrative Tribunal of Lyon asked the E.C.J. to establish whether the award of the contract to the regional company constituted an award of a public works contract subject to a call for competition in accordance with E.C. directives concerning the coordination of procedures for the award of public works contracts. *Id.* ¶ 20(1). As to whether the development agreement constituted a public works contract, the E.C.J. first reasoned that the directive concerning the coordination of procedures for the award of public works contracts defines a public works contract as any written contract, concluded for pecuniary interest between a contractor and a contracting authority (State, local authority, body governed by public law) whose purpose is, in particular, the design and/or execution of works, or a work corresponding to the requirements specified by the contracting authority. *See id.* ¶ 6.

The E.C.J. noted that SEDL, a contractor within the meaning of the directive, *id.* ¶ 44, was engaged by the municipality on the basis of an agreement concluded in writing. *Id.* ¶ 43. It observed that, although the agreement to engage SEDL contained an element providing for the supply of services, its main purpose was the construction of a leisure center, which involved work within the meaning of the directive. *Id.* ¶¶ 46–47. The E.C.J. stated that it was irrelevant that SEDL did not execute the work itself but instead delegated that work to subcontractors. *Id.* ¶ 44.

function.”¹⁸³ As such, it must be regarded as an ordinary public works contract.¹⁸⁴

The application of *Teckal* to specific cases reveals that its two criteria are blurry. The E.C.J. interprets them very strictly because their fulfillment deactivates the E.C. public procurement legislation and principles. The burden of proof is on the person seeking such derogation.¹⁸⁵ This narrow interpretation means that it is often unlikely that the *Teckal* criteria will be met.¹⁸⁶ Unfortunately, unrestrained formalism in construing these criteria jeopardizes local entrepreneurship, innovation and new forms of interlocal cooperation.

2. *Teckal's Effect on Local Public Entrepreneurship*

Recently, the E.C.J. has tried to place the *Teckal* criteria in context. It is difficult to prove that a contracting authority controls its legally distinct contractor the way it controls its own departments. The “similar control” criterion should be adapted to the factual context and applied flexibly. Unfortunately, the E.C.J. has narrowed the scope of in-house operations, rendering them barely realistic.

In *Stadt Halle*, the E.C.J. held that the award of public responsibilities to public-private companies is not an “in-house” operation and is therefore subject to the E.C. public procurement rules.¹⁸⁷ This holding affects local public-private partnerships¹⁸⁸ such as major, long-term projects for services relating to transportation, public health, and waste management. After *Stadt Halle*, contracting authorities are obliged to apply Public Procurement Directives twice (once for the choice of the private shareholder and once for the choice of the contractor) and may be prevented from using this form of cooperation.¹⁸⁹ And, in *Parking Brixen*

183. *Id.* ¶ 41.

184. *Id.* ¶ 47.

185. *Stadt Halle*, *supra* note 174, ¶ 46; *Parking Brixen*, *supra* note 176, ¶ 63; *ANAV*, *supra* note 176, ¶ 26.

186. For instance, Advocate General Cosmas opined that the “control criterion” was unlikely to be met in a case where forty-five municipalities owned the entity in question and the contracting authority had only 0.9% share of the entity’s capital. *Teckal*, *supra* note 170, at I-8136.

187. *See Stadt Halle*, *supra* note 174.

188. Public-private partnerships are neither regulated nor defined at the European level. Before *Stadt Halle*, it was not clear whether the assignment of public tasks to such entities in the form of public contract or concession fell within the scope of the Public Procurement Directives. *See id.*

189. *See Commission Communication on Public-Private Partnerships and Community Law on Public Procurement and Concessions* 8, COM (2005) 569 final (Nov. 15, 2005). The European Commission plans to publish an interpretative Communication to clarify the limits of the public procurement rules’ application to joint undertakings between the public and the private sector. This

and *Commission v. Austria*, the E.C.J. made clear that the award of concessions or contracts even to wholly owned subsidiaries of contracting authorities may be subject to the public procurement regime.¹⁹⁰

In *Carbotermo*, the E.C.J. refined the second *Teckal* criterion.¹⁹¹ It interpreted the “essential part of activities” factor to require that the entity is “devoted principally” to the contracting authority and “any other activities are only of marginal significance.”¹⁹² As a result, national judges must carry out qualitative and quantitative analyses of the facts.¹⁹³ This assessment applies to any activities carried out under a contract awarded by the contracting authority, regardless of who the beneficiary is (the contracting authority or the user of the services) or who pays the contractor.¹⁹⁴

Such extensive interference in municipalities’ self-governance and organizational discretion is, even from the standpoint of the market, extremely disproportionate.¹⁹⁵ In *Parking Brixen*, Advocate General Kokott noted,

After all, the purpose of procurement law is to ensure that contractors are selected in a transparent and non-discriminatory manner in all cases where a public body has decided to use third parties to perform certain tasks. However, the spirit and purpose of procurement law is not also to bring about, “*through the back door*,” the privatisation of those public tasks which the public body would like to continue to perform by using its own resources. This would require specific liberalisation measures on the part of the legislature.¹⁹⁶

Through its use of the phrase “control *similar* to that which,” *Teckal* indicates that a local authority has different possibilities to influence its

initiative, although soft law, will guide the selection of private partners participating in public partnerships and contribute, to a better understanding of relevant E.C.J. case law. See Sue Arrowsmith, *Public-Private Partnerships and the European Procurement Rules: EU Policies in Conflict?* 37 COMMON MKT. L. REV. 709 (2000); L. Hausmann & J. Denecke, *Changes to German Public Procurement Legislation by the PPP Acceleration Act*, 14 PUB. PROC. L. REV. 195 (2005).

190. *Parking Brixen*, *supra* note 176, at I-8612; *Comm’n v. Austria*, *supra* note 174, at I-9705.

191. *Carbotermo*, *supra* note 174, at I-4137.

192. *Id.* ¶ 63.

193. *Id.* ¶ 65.

194. *Id.* ¶ 65–67.

195. See Charter of Local Self-Government, *supra* note 37. Article 6(1) provides that local authorities must “be able to determine their own internal administrative structures in order to adapt them to local needs and ensure effective management.” *Id.*

196. *Parking Brixen*, *supra* note 176, at I-8585.

own departments and public undertakings.¹⁹⁷ Whether a contractor is akin to an administrative department or other market operators is not based on whether, *from a formal point of view*, the public body has the same possibilities *in law* as it does in relation to its own departments (for example, the right to give instructions in a particular case). Rather, the issue is whether, *in practice*, the contracting authority attains its public-interest objectives fully at all times.

It is practically impossible for most public or private undertakings to fulfill this second *Teckal* criterion. Contracting authorities comply with procurement rules before concluding contracts with their subsidiaries, insofar as those subsidiaries are organized as public or private limited companies. Therefore, the choice of a public or private limited company as a form of organization is appreciably less attractive. Such extensive interference with the organizational sovereignty of the Member States and, in particular, with the self-government of many municipalities is not necessary for the market-opening purposes of public procurement law.

The E.C.J. case law on in-house operations deserves at least careful re-reading, if not complete re-thinking, due to these local self-governance implications. *Teckal* intended to preserve local governments' sphere of self-governance regarding organization and service provision. Subsequently, the E.C.J. expanded "in-house" to apply to all other types of public contracts.¹⁹⁸ The expansion of this category triggered the E.C.J.'s interpretive self-restraint. Sometimes this attitude led the E.C.J. to deeply weaken local governments' entrepreneurial discretion, as well as interlocal cooperation.

B. *The U.S. Debate on the "Public Use" Issue*

U.S. local public entrepreneurship is more developed than its European counterpart, and American local governments are more conscious of their intrinsic entrepreneurial nature than are those in the EU. U.S. local governments' business-oriented strategies involve a wide variety of public policies designed to nurture and trigger economic development.¹⁹⁹ This business-like activism encompasses the exercise of eminent domain. Eminent domain is used to assemble land for economic development. I use

197. *Teckal*, *supra* note 170, at I-8121.

198. The Community procurement regime does not provide an "in-house" provision similar to the one foreseen for in the E.C. Directive concerning the coordination of public service contracts awarding procedure.

199. Richard Briffault, *A Government for Our Time? Business Improvement Districts and Urban Governance*, *supra* note 139, at 423.

the example of eminent domain to illustrate the U.S. judiciary's attitude toward local government political economy. A recent U.S. Supreme Court ruling, *Kelo v. City of New London*,²⁰⁰ has endorsed a municipality's right to condemn private land for economic development purposes.

Professor Gillette describes the power of eminent domain as "necessary to cure what is itself a political problem—the capacity of individual private property holders to frustrate majority will by refusing to sell privately held land for public purposes."²⁰¹ Gillette signals the risk of abuse because local officials may take private property even when public benefits would be lacking. The provision of the "public use" requirement as a prerequisite to condemn, and the imposition of just compensation, is meant to deter public officials from exercising taking powers when public costs exceed public benefits.²⁰² But Gillette underlines that in light of the erratic nature of twin safeguards, they shall work as safety valves in order to guarantee that "systemic abuse will create political backlash."²⁰³ The fear of electoral redress effectively constrains local officials.²⁰⁴

In many economic development programs in which local governments play a role, the power to acquire land through eminent domain is crucial. Practically every state has adopted legislation on land assembly through eminent domain.²⁰⁵ Such legislation authorizes the use of eminent domain mainly in urban renewal projects which have economic redevelopment as their primary objective.²⁰⁶ Some states have also enacted new legislation that, regardless of urban renewal aims, authorizes the use of eminent domain for economic development.²⁰⁷ The use of eminent domain for economic development has sometimes been used to convey the land the

200. 545 U.S. 469 (2005).

201. Gillette, *supra* note 12, at 14–15.

In theory, publicly interested officials will use the condemnation power only to solve what is called the "land assembly" problem and only to do so where the result is to confer net benefits on their constituents, that is, only to make residents as a whole better off, even though some of those residents will lose private property that they might have preferred to retain.

Id. at 15.

202. Steve P. Calandrillo, *Eminent Domain Economics: Should "Just Compensation" Be Abolished, and Would "Takings Insurance" Work Instead?*, 64 OHIO ST. L.J. 451, 490–91 (2003) (citing Frank I. Michelman, *Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law*, 80 HARV. L. REV. 1165, 1214 (1967)).

203. Gillette, *supra* note 12, at 16.

204. *Id.* at 16.

205. Daniel R. Mandelker, *Public Entrepreneurship: A Legal Primer*, C629 ALI-ABA 587 (1991).

206. David M. Lawrence, *Constitutional Limitations on Government Participation in Downtown Renewal Projects*, 35 VAND. L. REV. 277 (1982).

207. Mandelker, *supra* note 205, at 587.

governmental agent acquires to a private entity, which then carries out a development project.²⁰⁸

Thus, a question of constitutionality arises. All states share federal constitutional limitations on the use of their eminent domain power. However, U.S. courts have construed the notion of “public use” very broadly to also include “economic development.”²⁰⁹ This reflects a “deference to legislative judgments about the proper use of public expenditures and the proper interaction between government and business.”²¹⁰

In *Kelo*, the U.S. Supreme Court recited the conditions under which the judiciary must refrain from interfering with local political economic decision-making and rejected “any monolithic metric for economic development.”²¹¹ As Gillette underscores, the Court deferred to the political assessments of the locality and its “carefully considered” economic plan.²¹² The Court limited its analysis to “apparent political process failure that courts could detect and correct better than the political process itself.”²¹³ It noted that nothing in New London’s development plan was adopted “to benefit a particular class of identifiable individuals.”²¹⁴

Judicial intervention in local government and economic development activities must be restrained in some circumstances. *Kelo* “articulate[s] those conditions under which judicial intervention *is* warranted.”²¹⁵ In Gillette’s view, the *Kelo* Court explains its deference to the City of New London when holding that the case “turned on the question [of] whether the City’s development plan serves a ‘public purpose.’”²¹⁶ The Court held that “[t]he City has carefully formulated an economic development plan that it believes will provide appreciable benefits to the community.”²¹⁷

208. *Id.*

209. “Promoting economic development is a traditional and long accepted function of government.” *Kelo*, 545 U.S. at 484.

210. See Gillette, *supra* note 12, at 16–17.

211. *Id.* at 17. The Court did not restate the so-called blight requirement. *Id.* The original state statutes approved the use of eminent domain in urban renewal projects, provide that the land to be acquired through the exercise of eminent domain was located in an area that had been designated as “blighted.” The type of area that conventionally has been called “blighted” is an area that contains substandard housing or nonresidential buildings. *Id.* at 16–17. All state courts have upheld the acquisition of blighted areas under the eminent domain power as a sufficient basis to prove public use or public purpose of the redevelopment of the cleared land by a private entity. *Id.*

212. See *Kelo*, 545 U.S. at 478.

213. Gillette, *supra* note 12, at 17.

214. *Kelo*, 545 U.S. at 478.

215. Gillette, *supra* note 12, at 17.

216. *Id.* at 480.

217. *Id.* at 483.

Therefore, “given the comprehensive character of the plan, [and] the thorough deliberation that preceded its adoption,” the Court reviewed the plan as a whole to determine whether it satisfied the public purpose requirement.²¹⁸

Europeans judges can learn from *Kelo* and the foregoing American jurisprudence on the interaction between local economies and local governments. For one, “the flexibility in defining the proper relationship between local government and the local economy is what makes the inquiry uniquely *unsuitable* for judicial investigation.”²¹⁹

In addition, European legislatures should learn from U.S. state laws enacted post-*Kelo* that introduced “procedural safeguards, such as hearing requirements, to the condemnation process.”²²⁰ Gillette argues that “openness and opportunity for collective action will generate more publicly-interested decisions and reduce the risk of abuses.”²²¹ Gillette properly underscores that *Kelo* fits within the American jurisprudential “tradition of counteracting the need for flexibility in urban planning with political process protections.”²²² The same result would ensue in a case in which business and government interacted in a public policy field other than urban renewal.

IX. CONCLUDING REMARKS

Cities should be allowed to engage in business activities or make strategic decisions like business players. In particular, they should be able to step into the economic arena or back-up private projects to foster economic growth because cities compete with each other to gain new investors, citizens and lenders. The overall aim is to improve the competitiveness and well-being of their jurisdictions by providing new or better public services and infrastructure, and by increasing their tax-base or debt leverage.

218. *Id.* at 484.

219. Gillette, *supra* note 12, at 19. Gillette’s claim is that:

the capacity of the judiciary to make inquiries into the process, to reverse engineer the political decision to determine whether it was tainted or whether the same decision would have been reached on objective grounds, is minimal. Thus, perhaps the best that a court can do is to define the conditions under which the probability of abuse is minimal and defer to the political process when those criteria are satisfied.

Id. at 20.

220. *Id.* at 20.

221. *Id.*

222. *Id.* at 16.

Local governments are both political and economic entities. They represent a form of human organization which shares both a governmental and an associative nature. Consequently, they feature characteristics of both public and commercial entities. Therefore, local governments should be granted political liberty (the right to local self-government) and economic liberty (the right to provide public local goods and engage in economic activities for local development).²²³ For these reasons, legislatures should recognize and protect local public entrepreneurship. Correspondingly, judges should adopt a more deferential approach to such activities.

Briffault is right when he warns that the “widespread use of local government structures,” for the implementation of pro-business policies threatens abuse of “the coercive power of the state for private economic ends,” which circumvents direct democratic control.²²⁴ To avoid abuses, however, the legislature does not have to deny or frustrate local governments’ autonomy.

Therefore, democratic counterbalances are crucial. Intervention should not be left only to the judiciary. When the decision is of a purely political nature, citizens (directly or through their representatives) should have the last word. It is incumbent upon the legislature to design and implement democratic counterbalances that make local governments’ entrepreneurial initiatives (in the economic as well as social field) more participatory.²²⁵

Finally, globalization has completely changed the characteristics of competition among local governments. Today, competition takes place in the international marketplace. Rising to this global challenge requires full development of a city’s entrepreneurial spirit. Local public entrepreneurship must foster interlocal cooperation; otherwise, local

223. Adam Smith argued that economic “liberism” (i.e., laissez-faire capitalism) would not come without political “liberalism,” and vice versa, in order for individuals to fully develop their personalities. Economic liberty is a key tool for political liberty. See ADAM SMITH, *THEORY OF MORAL SENTIMENTS* (1759). See also JOHN RAWLS, *POLITICAL LIBERALISM* (1993); ROBERT A. DAHL, *A PREFACE TO ECONOMIC DEMOCRACY* (1985). See also MILTON FRIEDMAN & ROSE D. FRIEDMAN, *FREE TO CHOOSE* 2–3 (1980):

Economic freedom is an essential requisite for political freedom. By enabling people to cooperate with one another without coercion or central direction, it reduces the area over which political power is exercised. In addition, by dispersing power, the free market provides an offset to whatever concentration of political power may arise. The combination of economic and political power in the same hands is a sure recipe for tyranny.

For the purpose of this paper, the tyranny from which local governments need to be freed is that of national and regional governments that hinder their innovation and entrepreneurship.

224. Richard Briffault, *Who rules at home?: One Person/One Vote and Local Governments*, 60 U. CHI. L. REV. 339, 383 (1993).

225. See DAVID HELD, *MODELS OF DEMOCRACY* 259 (2006).

governments will not be able to face global competition. International codification and regulation of the right to local self government, with all its implications, including the right to economic entrepreneurship, is necessary.²²⁶

226. The Initial Draft Text of a World Charter, *supra* note 149, suggests this direction.