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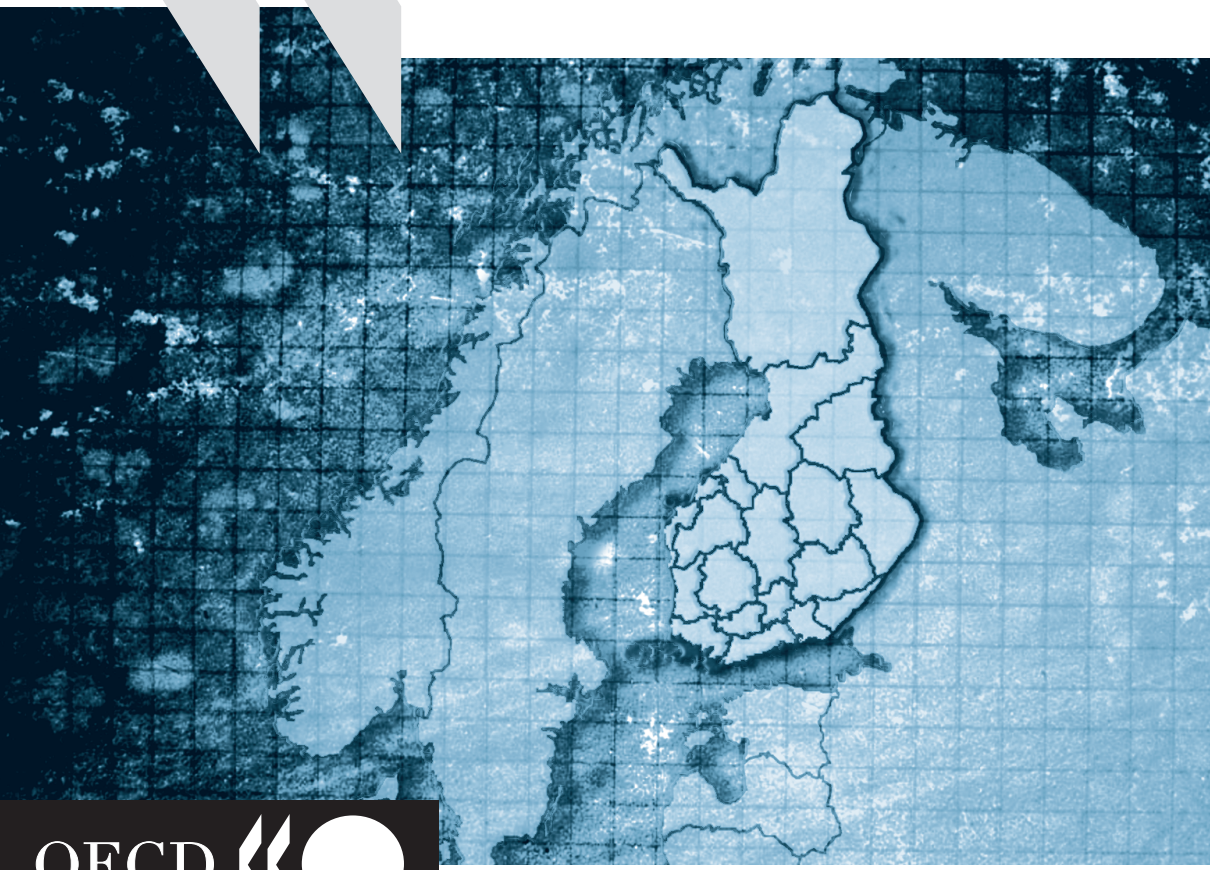

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The Review was directed by Mr. Mario Pezzini and co-ordinated and drafted by Mr. Philip Wade, with the contribution of Mrs. Claire Charbit, Ms. Lamia Kamal-Chaoui and Mr. Vincenzo Spiezia of the OECD Secretariat.

Table of contents

List of boxes

List of tables

List of figures

Assessment and Recommendations

Economic trends reflect overall good performances but Finland faces new challenges with relevant regional implications

The "Finnish way" for economic growth has proved successful over the past decade and has also promoted relatively balanced development across the country. In order to maintain capacity for economic competitiveness and development, Finland is dealing with challenges that may affect future outcomes and, amongst others, highlight regional development issues. How to maintain and enhance the competitiveness of the nation's "motor" regions given intense competition – in both the Information and Communication Technologies (ICT) markets and in more traditional products – and rapid ageing of the population? How to promote innovation and entrepreneurship in those intermediate cities where the economic fabric is particularly exposed to low cost competition and therefore has to permanently up-grade the quality of regional products and services? How to facilitate growth in those regions that have potential for development, but so far have been less successful in exploiting their comparative advantages? Together with a renewed interest in the contribution of regional development to national growth, these questions imply increased attention to multi-level governance issues.

To face these challenges, regional policy has evolved...

Are present regional policies capable of dealing with these new challenges? Finnish regional policy underwent a significant re-orientation over the last decade, reflecting changing economic circumstances and needs and progressively shifting objectives from equalisation of regional income to enhancing the competitiveness of regions. This shift was influenced firstly (in 1994) by the recession and the inception of EU policy and secondly (in 2003) by the aim to strengthen national policy for economic development. In the early nineties, Finland experienced one of the severest recessions in OECD countries since the Second World War, with unemployment reaching 17% of the active population. Drastic measures by the government, including devaluation of the

currency and large-scale enterprise restructuring, led to a remarkable and rapid recovery. In this context, the 1994 Regional Development Act concentrated on knowledge and programme based policy including knowledge infrastructure and specific subsidies to jump-start the economies of all regions, and not only the hardest hit areas.

… towards a growing focus on regional competitiveness and governance

Growth in labour productivity during the second part of the 1990s was among the highest in the OECD. EU accession (1995) – which promoted a shift in foreign trade towards the EU after the denunciation of the preferential trade agreements by the former USSR – in parallel with Finnish leadership in high growth mobile telephony markets, contributed to this turnaround. During the second part of the nineties, job creation in the private sector became prominent, strongly contributing to economic growth. Strategies aiming to further develop private sector competitiveness came to the fore. Improvements in the economic climate, lessons learned from implementation of the 1994 Act, and the recent perception of new challenges, in particular those requesting better capacity to diffuse innovation across regions and firms, led to a progressive evolution in regional policy thinking, incorporated into the Regional Development Act of 2003. Keeping a view to balanced development, this Act aims in particular at strengthening the competitiveness of regions while safeguarding the service structures throughout the country. In turn, emphasis on competitiveness enhancing policies has highlighted the need for a more coherent governance structure, in particular in two directions: increased horizontal cooperation at the central, regional and local levels, with the aim of strengthening regions, and further and enhanced coordination between regional and sector policies. The underlying recognition is that regional development strategies complement and strengthen the effects of sound macroeconomic policies.

Policy instruments reflect these changes… but could be further improved

In achieving these objectives, regional policy instruments have evolved significantly.

1. The role of innovation (both technological and organisational) and services to firms in regional development has become more central, through cluster-type approaches, although the instruments to translate this into practice remain scattered. At the same time a new strong instrument, the Centres of Expertise (CoE) programme, was launched.

2. Urban development policy has been reviewed, with the aim of creating a network of dynamic small and medium-sized cities recently integrated into concerns relating to support of Finland's major city functional areas, considered as key players in regional development.
3. Adequate provision of public services to all regions in a cost-efficient way is a key pillar of the equity balance dimension of regional policy.

Innovation in all regions and types of firms could benefit from a broader scope and improved coordination across levels of government…

To what extent can innovation policy promote further regional development and contribute to national competitiveness strategies? The "triple helix" interaction model of government, industry and universities, on which the Finnish innovation system is based, is sponsored principally by the Ministry of Trade and Industry and the Ministry of Education, acting through a dense network of specialised public agencies (Tekes, Finnvera, Sitra and VTT in particular). Although successful, this approach remains technology oriented and less attentive to management methods in small firms or traditional sectors having a strong role in most regional economies. It is mostly focused on large firms leading networks, and less aware of the role that entrepreneurship and proximity relations between firms can have in disseminating innovation. Thus, innovative capacity is concentrated in a few regions while potential and needs for innovative technologies and management methods are more widely spread. Taking R&D expenditures as a proxy for innovation, four regions account for over 80% of the total (4.9% of GDP in 2000, one of the highest levels in the OECD), while peripheral regions have per capita R&D expenditures of only 15% of those of the capital city region. Although a place-based tool like the CoE has contributed to improving the innovation capacity of firms in peripheral regions, the National Innovation System (NIS) could better integrate the concerns of non-core regions.

… requiring close association of all actors

It is recommended for these purposes to:

- Give more attention to a broader innovation concept so that small firms and traditional sectors are fully recognised as innovation and ICT policy targets within the organisation of the NIS.
- Give adequate articulation to this policy focus by establishing a standing inter-ministerial committee, bringing together the Ministries of Trade and Industry, Education, Labour, Transport and Communications, Health and

Social Affairs, Agriculture and Forestry, and the Interior. This Committee would be accountable to the Science and Technology Policy Council.

- Associate Regional Councils more closely to the definition of strategic innovation guidelines and programmes as they are in a position to help federate local efforts and ensure coherence between different initiatives and funding sources.

Urban development programmes need to be integrated into a unified strategy

Urban competitiveness issues are already a priority for the government but urban development policy needs to be better clarified. The Regional Centre Programme (RCP) targets urban network development for small and medium-sized cities while the CoE applies to all urban areas. In the recent past, urban development policies focused strongly on the RCP with the CoE programme being implemented in some of these small and medium-sized cities. In fact, these cities do play an important role in the development of the country as they concentrate an important share of the national productive activity. More recently Finland has diversified its urban policy and will launch a special policy to support the participation of major cities to the global economy. The "Policy Package for Major Urban Areas" offers the opportunity to clarify the role that the largest cities play in contributing to further development instead of simply seeing them as the actor of a "zero sum game" within the country. However, existing urban development policy programmes focused on small and medium-sized cities and new initiatives for larger cities have not yet been securely grounded in a unified strategy developing synergies within the country's urban structure.

In particular, it could be suggested to:

- Better clarify the management of the RCP in respect to that of the Major Urban Areas Policy Package.
- Recognise the leading role of major urban areas and introduce specific vertical and horizontal coordination mechanisms to promote the leading role of such cities in regional development, improve networking and co-operation among the targeted cities.

Public service delivery costs are increasing in the face of ageing

Proportionately small increases in resources *versus* rising costs of public service delivery puts pressure on municipal budgets. A large proportion of public service delivery in Finland, whether primary and secondary education,

child care, health care, care for the elderly and culture (public libraries), is the responsibility of municipalities. These expenditures represent 18.6% of GDP in 2001 and are rising in particular because of ageing. Municipalities employ more than 76% of civil servants to ensure delivery of quality services based on stringent national standards in all parts of the country. These services (74% of municipal expenses), are financed through local taxes, block grants and equalisation schemes compensating for additional costs stemming from a reduced tax base or low density. Municipalities are free to allocate resources across sectors as long as they can provide basic services: the more is spent on public services, the less is available for economic development. Although services are often delivered by several municipalities acting together ("joint municipal boards") and that cooperation is encouraged (Seutu and RCP programmes), rising costs are more pronounced in areas of population decline, generally corresponding to areas situated in the periphery such as Lapland, Kainuu and Etelä Savo. The phenomenon is however not limited to these low density areas, as 11 out of Finland's 20 regions have been experiencing population decline since 1995.

Safeguarding the service structures in areas of declining population requires cost-efficient approaches

In areas with declining population, new approaches would permit to safeguard the service structure in a cost-efficient way. There is not one single solution to tackle such problems and measures are being taken at the national and local levels to respond to the challenge. A national programme applying to all government levels designed to improve productivity in public administration has specifically identified increased use of ICTs and outsourcing, whenever possible, as tools to be more systematically used by public authorities. Within this policy framework a "Basic Services Programme" is now a part of the annual decision on government spending limits (also including grants to municipalities) and includes a section on efficiency and measures to improve it. More recently, directly addressing the issue of municipal spending on the one hand and both quality delivery and access to services on the other, a project to restructure municipalities and services has been launched to ensure that services have a firm structural and economic basis. Broad initiatives of this type are necessary and should be carefully implemented and monitored. Their success is largely based on the actions taken by individual municipalities, so adequate incentive mechanisms are required. It is thus suggested to:

Economies of scale and democratic accountability are to be sought in parallel to adequate use of ICTs

- Encourage deeper inter-municipal cooperation by devising awards on the basis of economies achieved by a joint municipal board.
- Pursue experimental approaches at the regional and sub-regional levels (RCP and Seutu programmes).
- Continue pursuing voluntary amalgamation based on incentives wherever possible, as it presents, besides scale effects, the advantage of authorising true democratic accountability.
- Ensure that new service obligations for municipalities do not translate into unfunded mandates.
- Allocate adequate funding to permit the training of all municipal personnel in new management techniques, efficient use of ICTs to foster new service processes and possibly introducing result oriented management.

The Finnish consensus seeking model faces new challenges in the area of regional development…

Regional development mechanisms and governance could be usefully reviewed. Regional development governance in Finland involves a constellation of actors of different weights and at all levels of government. It is characterised by intensive and regular processes of consultation and co-ordination largely orchestrated and/or overseen by the Ministry of the Interior. Its own financial weight in regional development is not significantly higher than that of other ministries but, with control of around one third of EU funding, it can exert a strong influence on strategic choices. This specific Finnish regional development model based on consensus seeking seems to have functioned rather efficiently up to now but its increasing complexity has prompted questions about sustainability. For example, can it adequately foster regional competitiveness at a time when EU enlargement will mean the reduction of certain funding sources that constitute strong incentives for regional cooperation? To help face these challenges it is proposed to:

… So, regional development needs to be more strongly linked to other major policy areas such as innovation

- Continue efforts to improve the budgetary transparency of regional development policy. At the national level the "budgetary readability" of overall

regional development funding will be improved with the 2005 budget, which includes, for the first time, precise allocations by ministry rather than just a listing of funding relating to regional development. Effective monitoring and evaluation mechanisms should be built into the new system.

- Build stronger formal links between the Ministry of the Interior and the three key ministries having a strong impact on regional development and innovation: the Ministries of Trade and Industry and Education (National Innovation System) and Transport and Communications (Infrastructure and in particular broadband deployment).

Regional Councils must deal with other regional level bodies

The purpose, status and powers of Regional Councils are central to efforts to strengthen governance at the regional level. Enhancing regional performance by leveraging local assets requires adequate visibility at the level of the region but this is difficult to achieve as sector ministries, through State Provincial Offices and Employment and Economic Development Centres (TE-Centres) are both "partners and controllers" of regional councils. It is thus recommended to:

Greater emphasis on the role of Regional Councils in regional development strategies could facilitate partnerships

- Strengthen the autonomy and resources of the Regional Councils, in particular by examining the possibility of creating bigger regions. This would facilitate the creation of a truly open and dynamic forum where all actors of regional development could meet and conciliate views.
- Strengthen connections between regional and special programmes.
- Carefully monitor the Kainuu experiment in regional self-government so as to reinforce the regional level in general.
- Explore how contractual and partnership approaches between the State and the regions can be facilitated through the Regional Councils, with a clear delimitation of mutual responsibilities in defining and implementing regional development strategies.
- Continue the series of programmes to boost social capital, such as the Civic Participation Programme (under the authority of the Ministry of Justice) and the Entrepreneurship Programme (piloted by the Ministry of Trade and Industry) and link these to concerns of regional development and local initiative.

EU funds have given organisational and financial impetus to regional development programmes

The consequences of EU enlargement over the next funding period require some organisational but also financial adjustments. It is expected that enlargement will translate for the next programming period (2007-2013) into reduced funding for a certain number of countries of the previous EU15, including Finland. Structural funds have brought a strong impetus to co-operation and programming of regional development, and this impetus could be reduced when these programmes are scaled down. National efforts to maintain momentum for co-operation will be needed. At present, there is great dispersion of management responsibility of EU funds at the regional level. For instance, LEADER funding is coordinated on the field by TE Centres and Objective 1 by regional councils. It is thus recommended to:

Innovative programmes and management methods need to be maintained and developed in the future

- Decentralise the operational management of these funds once budgetary allocations are decided at the national level after discussion with the regions.
- Introduce incentives to maintain the organisational and procedural innovations that the EU and national programmes have introduced (partnership working, cross-jurisdictional co-operation).
- Possibly consolidate the role of the Ministry of the Interior in this area by allocating additional funding to reinforce strategic actions and policy co-ordination in priority fields such as innovation.

Lastly, regional development policy could be more efficiently delivered if better explained

In Finland, a culture of consensus is a deeply rooted feature of society. To attain this consensus efficiently, improving the understanding of the aims and achievements of regional development policies from the perspective of citizens and firms is essential, given the complexity of the "Finnish model". Possible simplification of structures and more systematic communication of objectives and outcomes should be considered for this purpose.

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Figure 0.1. **Finland and neighbouring countries**

Source: Ministry of the Interior.

Box 0.1. **Finland basic facts and figures**

The land and the people

Population: 5 236 611 (2004).

Population density: 15 inhabitants per km^2.

Languages: Finnish and Swedish (6% of the population, mostly on the southwest coastline, are Swedish speaking).[1]

Area:[*] 338 000 km^2 (7th largest country in Europe), with close to 70% of forest (most densely forested country in Europe), 10% of lakes (187 888 in total) and 8% devoted to agriculture.

Climate: maximum average temperature of 17.2 °C in Helsinki and 14.8 °C in Sodankylä (Lapland), lowest average minimum of –4.9 °C in Helsinki and –14.1 °C in Sodankylä.

Daylight: In winter six hours in Helsinki, polar night (sun permanently below horizon) of 51 days in northernmost Finland, in summer 19 hours in Helsinki, polar day (sun above horizon for 24 consecutive hours) lasting 73 days in North.

Highest point: Mount Halti (Lapland): 1 328 metres above sea level.

Borders: 1 340 km with Russia (longest EU external border), 736 km with Norway, 614 km with Sweden.

Baltic States: Tallinn (capital of Estonia): 84 km from Helsinki, one hour and a half by hydrofoil ferry.

Governance

Independence: 16 December 1917, after having been for more than one century an Autonomous Grand Duchy of Tsarist Russia and before that, a part of Sweden for over 600 years.

Parliamentary democracy: 200 members of Parliament. Directly elected President with six-year mandate.

EU member: since 1 January 1995; currency: euro.

NUTS 5:[**] **432 municipalities** in 2005: average population = 11 700, more than half with less than 6 000 inhabitants and 14 with more than 50 000. Only self governing local government level.

NUTS 4: 77 sub-regions ("Seutukunta") in 2005: framework for inter-municipal co-operation.

NUTS 3: 20 regions ("Maakunta"), including the Åland Islands with specific status.[2]

NUTS 2: five regions ("Suuralueet"), South, West, East, North and Åland, the latter having both NUTS 3 and 2 status.

National administration regional offices: six Provincial State Offices, 15 TE-Centres, 13 Environmental Centres.

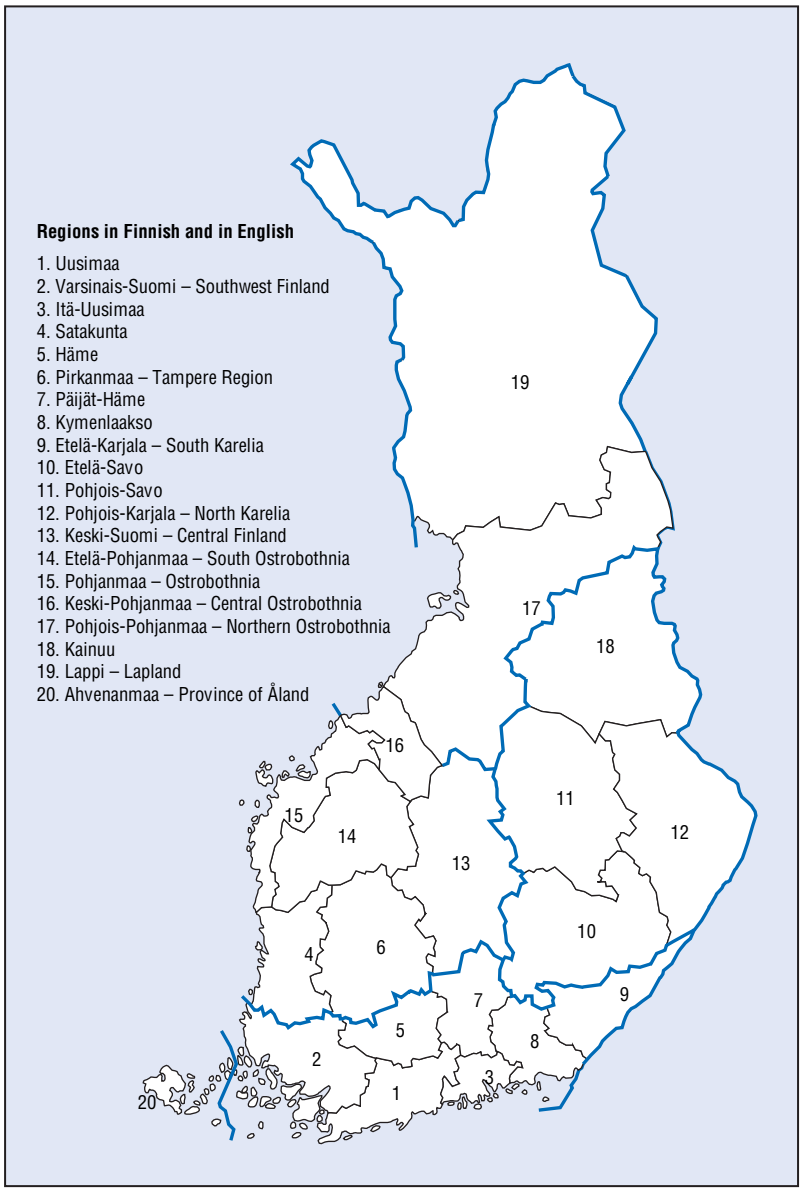
Box 0.1. **Finland basic facts and figures** *(cont.)*

* Area is total area (including water areas).

** NUTS: "Nomenclature des unités territoriales statistiques" (NUTS) provides a single uniform breakdown of territorial units for the production of regional statistics for the European Union. NUTS is a three-level hierarchical classification; it subdivides each Member State into a whole number of NUTS 1 regions, each of which is in turn subdivided into a whole number of NUTS 2 regions and so on. At a more detailed level, districts and municipalities became known as NUTS 4 and NUTS 5 units.

1. Both Finnish and Swedish are officially recognised in the 1919 constitution, meaning that schooling in Swedish is ensured in certain parts of the country and that higher education curricula is offered in Swedish in certain universities such as Helsinki, Turku and Vaasa.
2. Besides the 19 regions, on the basis of an international treaty signed in 1921, the Swedish speaking Åland Islands enjoys a wide status of autonomy and is the only Finnish region with self elected government.

Figure 0.2. **Finnish regions – NUTS 3 level**



Source: Ministry of the Interior.

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Chapter 1

Regional Performances and Underused Potentials

Introduction

At the turning of the 20th century Finland was a predominantly rural country, both in terms of the economy, strongly relying on the primary sector, with most industry based on wood and textiles. Outside of Helsinki, Turku (the former capital) and Tampere there were no other urban settlements of significant importance.[1] These characteristics remained typical of Finland for the major part of the last century, with industrialisation really developing only at the end of the 1960s and beginning of the 1970s. At that time, 36% of the active population was still working in the primary sector, mostly in forestry (versus less than 8% today). The country experienced a major economic boom in the 1980s, facilitated in particular by preferential trade agreements with the Soviet Union. At the beginning of the 1990s, trade with the Eastern block dropped dramatically, sparking a strong recession. During this last decade, Finland became a member of the EU[2] while enjoying a spectacular recovery thanks to the strong development of ICTs and private sector services.

Although Finland is becoming an increasingly urbanised country, with 61.1% of the population now living in cities and towns, the share of urban population remains well below EU and Scandinavian averages (Table 1.1). The fast growing Functional Urban Region of Helsinki comprises 1.24 million inhabitants,[3] around one-fourth of the total population of the country while only five other Functional Urban Regions – those of Tampere, Turku and Lahti in Southern Finland, Jyväskylä in Central Finland and Oulu in Northern Finland – comprise more than 150 000 inhabitants.[4] In spite of urban development, many areas are characterised by very low population densities (2.6 inhabitants per km^2 in Northern Finland and 9.9 in Eastern Finland).

Although the rural population is significant, the contribution of the primary sector to the economy has been regularly reduced and stands at only

Table 1.1. **Urban population in Europe and Scandinavia**

As percentage of total population	1980	2000
Europe	68.6	72.7
Denmark	83.8	85.1
Finland	59.8	61.1
Norway	70.5	75.8
Sweden	83.1	83.3

Source: Department of Economic and Social Affairs, UN, World Population Prospects.

5.1% in 2003, instead of 8.9% in 1993. The secondary sector, represented in particular by the wood, metal, mechanical, electronic and chemical industries, has seen its share remain relatively stable at 26.6% in 2003 against 26.3% ten years earlier, in particular because of the remarkable growth of ICTs, specifically mobile telephony. The service sector now predominates at 68.5%, instead of 64.5% in 1993. Public sector services are strongly developed in Finland as in other Scandinavian countries where the Welfare State model prevails. Municipalities are major employers and suppliers of health, social and education services, meaning that public spending has, as elsewhere, a strong direct effect not only on the national economy but on local economies as well. This first chapter presents major economic trends in Finland since the 1980s and than proceeds to analyse the factors influencing regional performances before identifying underused potentials.

1.1. Major macroeconomic trends

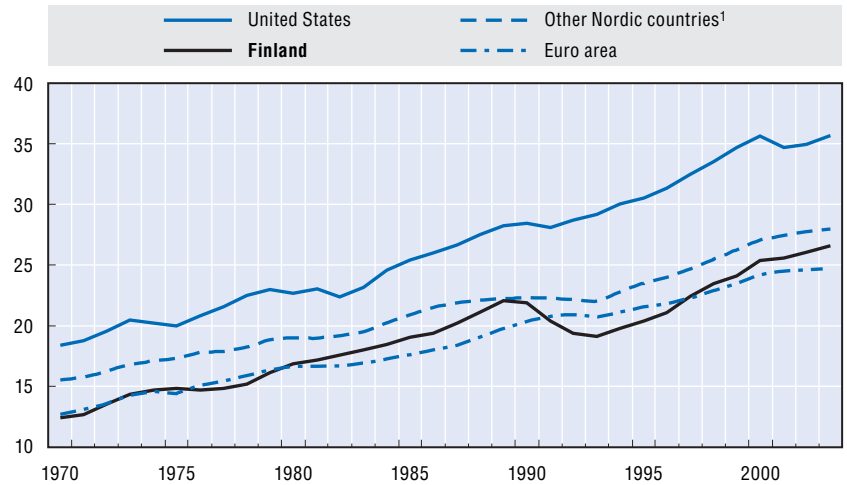
From the boom of the 1980s to the depression of the 1990s

At the end of World War II, Finland, having lost territory and required to make compensatory payments to the USSR, had to develop its industry to face its obligations (payments in kind, mainly in the form of steel products). The new industrial base developed considerably during the 1970s and 1980s, facilitated by monetary reform and development of the capital market. However, at the end of the period, high interest rates led to a substantive appreciation of the Finnish Mark. Added to the economic recession of its major trading partners, this difficult situation was abruptly aggravated by the termination of the preferential trade agreement with the Soviet Union, notified at the end of 1990. The loss of a market that represented 25% of Finland's foreign trade, combined with the other factors indicated above, contributed to a strong increase in unemployment that attained 17% of the active population during the first half of the 1990s. Devaluation of the Finnish Mark (12.3%) at the end of 1991, followed by floating currency rates a year later gave a boost to exports. Conversion of trade patterns over the last ten years translated into a shift towards EU member countries, becoming Finland's main commercial partners and accounting for more than half of Finnish exports.[5] In 2004 the major trading partners of Finland were Germany (14.7% of imports and 10.7% of exports), Russia (13.2% and 8.9%) and Sweden (10.9% and 11.0%).[6]

A rapid recovery

The deep recession of the early 1990s, one of the most severe experienced by any OECD country in the post-war period, was followed by a most remarkable recovery. The recession of the early 1990s led to widespread restructuring, considerable scrapping of the capital stock and a continuous decline in the capital-output ratio over the period. It also led to large-scale use

Figure 1.1. **GDP per capita growth**
Thousand USD, 2000 PPPs



1. Weighted average of Denmark, Iceland, mainland Norway and Sweden.

of early retirement schemes. Over the second half of the decade that saw the emergence of the ICT economy, growth in labour productivity and GDP per capita was among the highest in the OECD as shown by Figure 1.1 (OECD, 2004d).

The "ICT economy" outlook

One of the factors underlying the rapid recovery of the Finnish economy, spurred by EU membership in 1995, is the success story of Nokia, the firm that has become the leader in mobile telephony, employing more than 50 000 people around the world, around 22 000 of them in Finland,[7] around 2% of the total in the business sector (OECD, 2003a). This represents nonetheless a major share of employment in the Finnish ICT cluster: 32% in the year 2000, amounting to 54% if limited to ICT manufacturing (Steinbock, D. (2004). Originally making rubber boots, Nokia entered the mobile market as a pioneer with the Scandinavian NMT analog standard at the end of the 1980s before becoming one of the major proponents of the European digital GSM standard, with Finland being in 1992, the first country to offer commercial Global System for Mobile Communications (GSM) service. A deliberate export oriented strategy, a high level of investment in R&D and strong marketing capabilities explain the rapid growth of the firm that represents more than one-third of world mobile phone production.[8] Contribution of the firm to the performance of the economy is strong, accounting for one-third of national R&D spending. Heavy reliance of the economy on a single firm and sector in the context of globalisation is not without risk.[9]

Future challenges

Several factors affect the future prospects of the Finnish economy: increased competition in ICTs, access to global markets by all firms, development of Small and Medium Size Enterprise's (SMEs) but also leveraging of social capital and flexible responses to the ageing of the population. On the first point, Finland's flagship mobile manufacturer resisted better than others the economic downturn resulting from the explosion of the Internet bubble but its market share is exposed to new competition, particularly from Asia. To maintain its cutting edge, the firm must delocalise certain activities and produce in other markets. Recent investments have been made for this purpose in the United States, China and India.[10] Such a trend could reduce the contribution of this sector to overall employment in the country. Smaller productivity gains in the same sector as well as the continuation of falling ICT prices could also adversely affect the overall contribution to the economy (OECD, 2004d). Concerning SMEs, in Finland, the number of firms relative to the population is lower than in most OECD countries, with entrepreneurship culture unevenly developed across the country (see Chapter 3, Section 4). Support to entrepreneurship but also integration of ICTs into traditional sector firms are two related challenges. Using social capital by exploiting the networking and consensus seeking tradition of the country to enhance economic performance is another. These challenges bring up issues of regional development, as entrepreneurship and ICT penetration are lower in lesser performing regions. National competitiveness rests on the competitiveness of each region by leveraging of its unique assets (OECD, 2004d).

Finland's population is expected to peak in the early 2020s at about 5.3 million people but the labour force will start to decline in 2004 by 5% per year. The old age dependency ratio (those over 65 as a percentage of the working age population) will rise from 23% presently to around 37% in 2020, the fastest rise among OECD countries (OECD 2003a). Ageing will thus have a heavy impact on economic growth, with negative contribution to the average growth rate of GDP per capita expected as early as 2005-2010. Adding the decline in productivity indicated above and falling employment rates, within a decade Finland could well lose its top performer status and face the risk of stagnation (OECD, 2003a), as estimates in Table 1.2 clearly show. To offset this purely indicative scenario based on present data and conditions, OECD suggests in particular enhancing growth by boosting competition and labour market flexibility, to curtail early retirement schemes and control public spending by better fiscal co-ordination with municipalities. Pursuing balanced territorial development can help support these objectives as innovation, improvement of small and medium-sized cities' competitiveness and increased efficiency in service delivery can help to offset negative demographic trends by offering new jobs to qualified people while contributing to ensure a better performing allocation of municipal expenditure.

Table 1.2. **Contribution to annual average growth rate of GDP/capita in Finland**

	Contribution to annual average growth rate of GDP/capita			
	1995-2000	2000-2005	2005-2010	2010-2020
Productivity growth	2.5	1.7	1.8	1.8
Demographics	0.0	0.0	–0.2	–0.9
Employment rate	1.8	0.3	–0.3	0.1
GDP per capita	**4.4**	**2.1**	**1.3**	**1.0**

Source: OECD Territorial Database, 2004.

Comparative data concerning long-term migration trends across the country show strong resilience *versus* economic downturns during recent years. After the major internal migration movement that hit Finland in the mid-1990s, as a delayed answer to recession shocks and in recognition of the increasing opportunities in large urban regions in particular, migratory movements tend to have trickled down and were not seriously modified by the slow-down in economic growth generated by the explosion of the Internet bubble. In Oulu, a "high tech city" in North Ostrobothnia (see Chapter 2, Section 2), recent slower growth in the mobile sector translated into a cut in the number of jobs in the city area by the leading national manufacturer but, rather than moving out, most people are searching for jobs in the region where many small firms are developing. In a way, recent measures taken by the Finnish government to support areas subject to what is called "sudden structural change" constitute recognition that the workforce is less prepared for mobility and that mobility is not the only answer. This measure, directed towards the creation of new activities and retraining, applies in traditional sectors such as steel (Raahe sub-region) but also in newer ones like ICT. This is in particular the case of Kemijärvi (Lapland) where the delocalisation of Salcomp (mobile phone charger manufacturer) to China has led to many qualified workers being laid off.

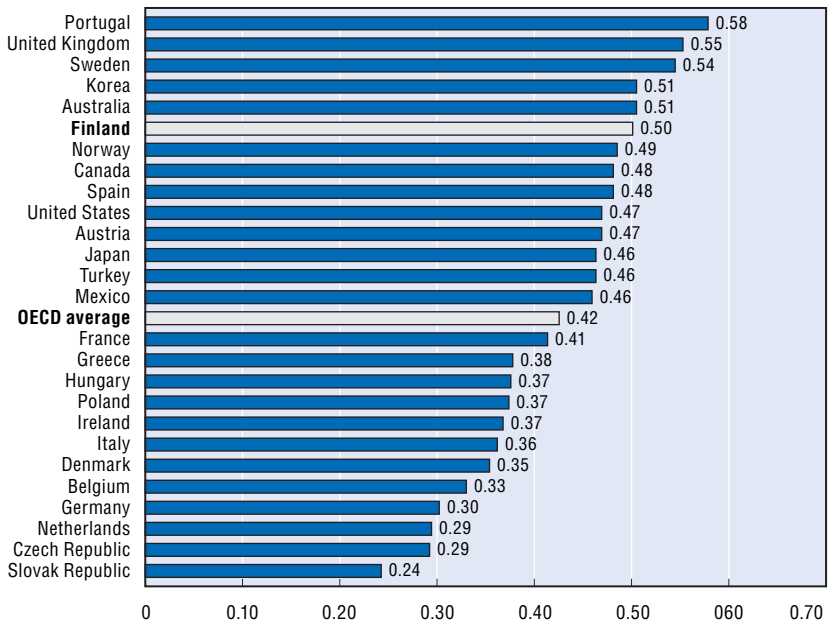
1.2. Regional trends

GDP per capita

The main feature of the Finnish economy is the high geographic concentration of economic activities. In 2001, four NUTS 3 regions accounted for over 60% of the national GDP, with the capital region alone representing 35% of the total. Compared to other OECD countries, Finland registers a relatively high degree of geographic concentration of GDP (Figure 1.2), ranking it in the sixth position behind Portugal, the United Kingdom, Sweden, Australia and Korea and just before Norway, with Denmark being the Scandinavian country exhibiting the lowest degree of geographic concentration of GDP.

High concentration is not only the result of the localisation of population but it is also due to differences in GDP per capita (Figure 1.3) (OECD, 2004d).

Figure 1.2. **Index of geographic concentration of GDP in OECD member countries, 2001**



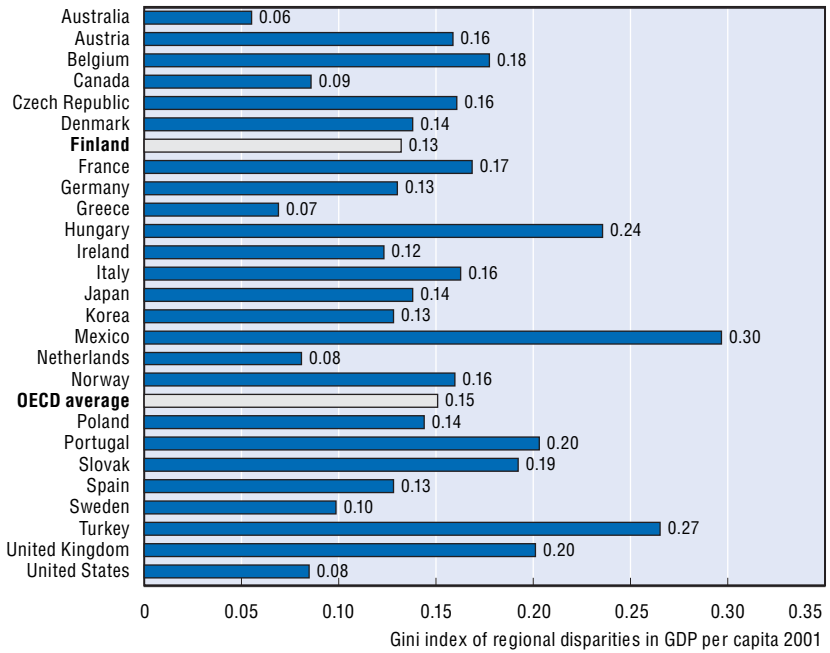
Note: The index compares the economic weight and the geographic weight over all regions in a given country and is constructed to account for both within- and between-country differences in the size of regions. The index lies between 0 (no concentration) and 1 (maximum concentration) in all countries and is suitable for international comparisons of geographic concentration.

Source: OECD Territorial Database.

Finland, like other countries in the region, appears to be characterised by the polarisation between densely populated regions and sparsely populated ones. In particular, GDP appears to be more concentrated than population, meaning that densely populated regions tend to have higher GDP per capita than scarcely populated ones. Thus, in Finland about 38% of GDP in 2001 was produced in predominantly urban regions, although these represented only 22% of the total population. This value is below the GDP-population ratio of Norway (where urban regions account for 23% of national GDP and 11% of the total population) but it is largely above the ratio observed in urban regions in Sweden (28% of national GDP and 21% of the total population) and Denmark (39% of GDP for 29% of the population).

Polarisation has increased over recent years. In 1997, GDP per capita was above the national average in five regions; by 2001, this group included only three regions: Uusimaa (Helsinki region), Southwest Finland (Turku) and Åland, with that of South Karelia and Kymenlaakso falling below the national average

Figure 1.3. **Regional disparities in GDP per capita amongst OECD member countries, 2001**



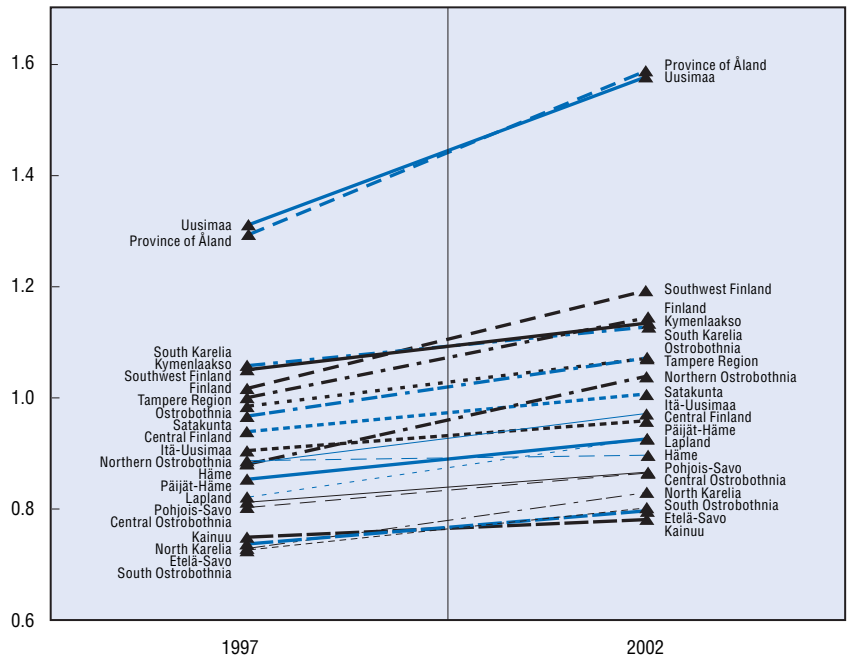
Note: Unweighted Gini Index, *i.e.*, each region is weighted by 1, independently of the size of its population.
Source: OECD Territorial Database, 2004.

(Figure 1.4). Inward migration patterns (see further), mostly from regions with lowest per capita income and highest unemployment rates towards more dynamic areas and cities, seem to have contributed to these developments rather than reducing disparities. Most skilled workers, upon leaving these areas contributed to an internal "brain drain" bringing their talent and capacities to the regions with the highest GDP per capita while becoming "lost assets" for the future renewal of their region of origin. Policies to better exploit the competitive advantages of regions with low level of per capita income are high on the agenda as they should help to counter such polarisation trends in the future (see Chapter 2).

Unemployment

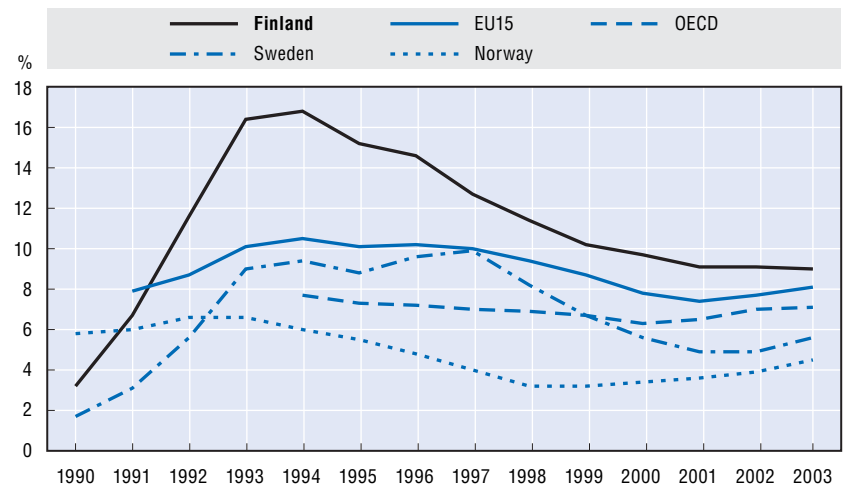
After a dramatic increase in the first half of the 1990s (up to about 17%), the unemployment rate in Finland has significantly decreased and has remained fairly stable since 2001, at around 9%. This rate is somewhat above the Euro area average and well above the average of OECD countries (OECD, 2004d) (Figure 1.5). The pattern of increasing regional disparities is even

Figure 1.4. **Trends in regional GDP per capita in Finland, 1997-2002 (Finland 1997 = 1)**



Source: OECD Territorial Database, 2004.

Figure 1.5. **Trends in national unemployment rates, 1990-2003: Finland, selected OECD countries**

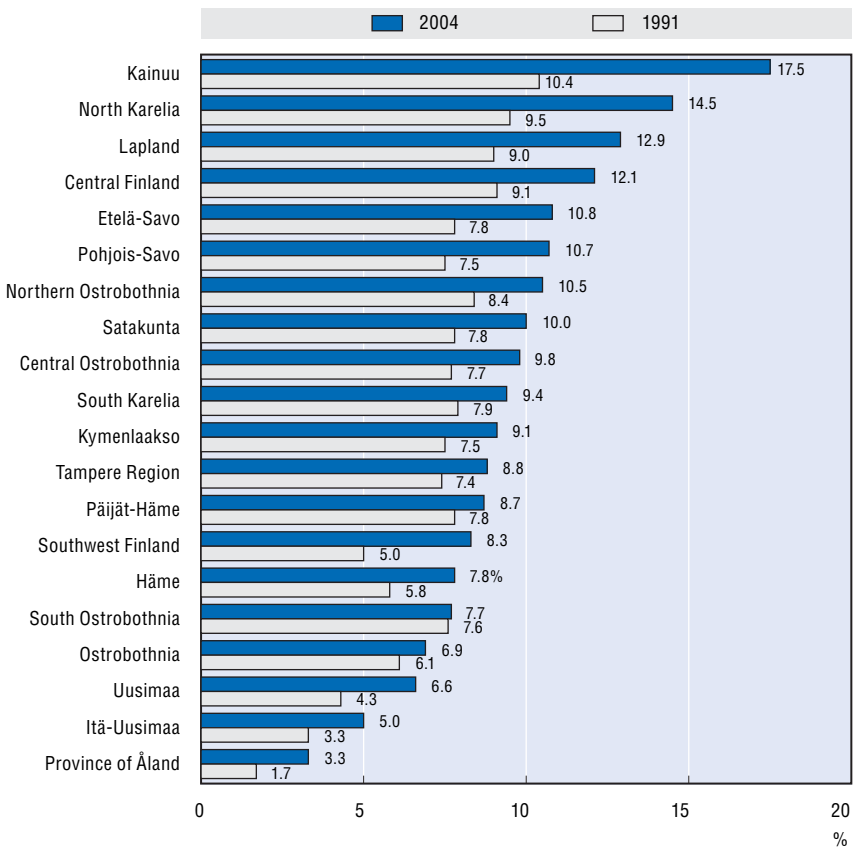


Source: *OECD Economic Survey of Finland*, 2004.

more pronounced in terms of unemployment than for GDP. In 2003, the regional differences in unemployment rates were as large as 18 percentage points, ranging from about 2% in Åland to 20% in Kainuu. Between 1991 and 2003, unemployment decreased mostly in those regions with an initial unemployment rate below the national average (Figure 1.6). Central Ostrobothnia, South Ostrobothnia and Tampere Region were the only high-unemployment regions that achieved a reduction in unemployment rates. As a result of this trend, unemployment disparities increased significantly, as measured by the rise in the Gini index from 0.12 in 1991 to 0.15 in 2003.

This trend seems confirmed when looking at employment rates, *i.e.*, the ratio between employment and population aged 15-64 (Figure 1.7). The largest increase in employment rates between 1993 and 2002 was registered in

Figure 1.6. **Trends in regional unemployment rates in Finland, 1991-2004**
Sorted by 2004



Source: Statistics Finland.

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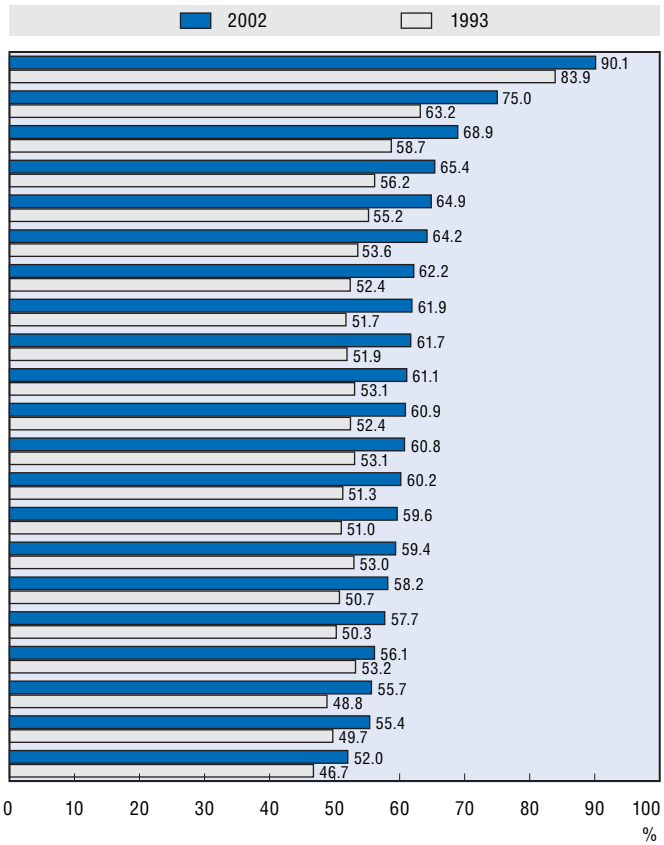
Figure 1.7. **Trends in regional employment rates in Finland, 1993-2002**
Sorted by 2002



Source: Statistics Finland.

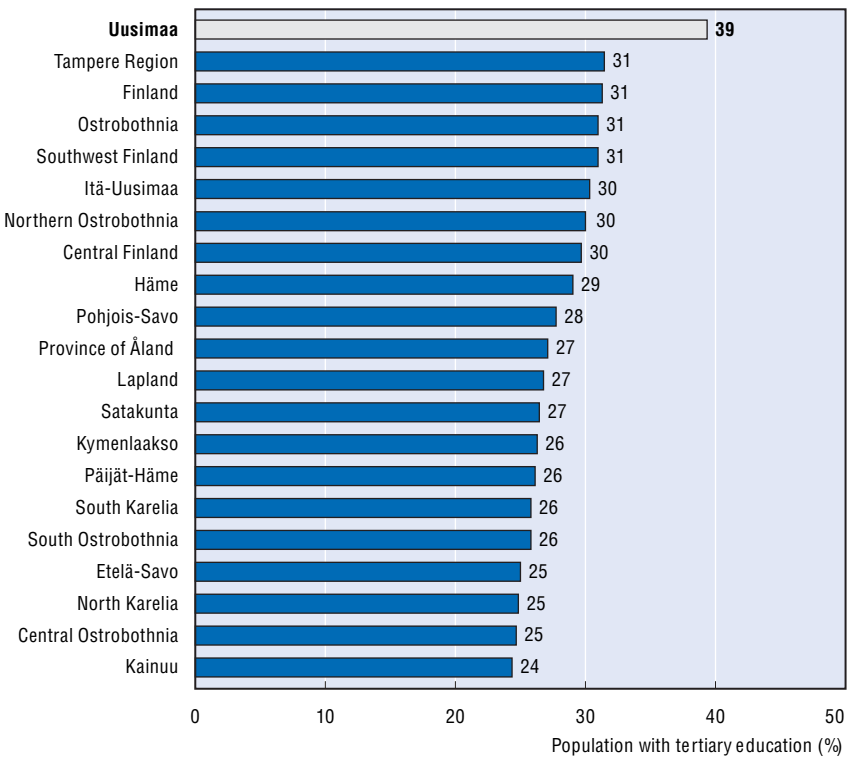
Uusimaa (from 63% to 75%) whereas Central Ostrobothnia, South Ostrobothnia and Tampere Region were the only low-employment regions that managed to achieve an increase in employment rates.

Skills and R&D

The quality of the Finnish educational system in terms of outcomes is generally excellent and Finland ranks high within OECD member countries concerning the proportion of 25- to 64-year-olds having completed tertiary level education (OECD, 2004e). At 14.7%, the share of 15-year-olds in Finland who achieve the highest level of proficiency on the PISA reading scale is second only among OECD member countries. As regards the mathematics/space and shape

scale, 7.9% of Finnish 15-year-olds achieve the highest level of proficiency. This compares with an average among OECD member countries of 5.8% of students (OECD, 2004b). It is worthwhile linking the preceding data to the Finnish public library system which is quite unique and can contribute to explain a high level of reading, development of human capital (see Chapter 3, Section 3.4) and life-long learning skills. There is a public library in each municipality, most being complemented with branch libraries and bookmobiles. Both municipal and research libraries are open to all citizens. Since 1928, use and lending of all library collections have been without fee and this now applies to videos, CDs and DVDs. Municipal libraries are run by local authorities, receiving statutory state aid for running costs. There are nonetheless significant regional differences in skills. The proportion of the population aged 25-54 years having a university degree or above varies from 39% in Uusimaa to 24% in Kainuu (Figure 1.8). Southwest Finland, Tampere Region, Central

Figure 1.8. **Disparities in educational attainments in Finland, 2000**



Note: Tertiary education corresponds to levels 5 and 6 of the International Standard Classification of Education (ISCED 97).

Source: OECD Territorial Database.

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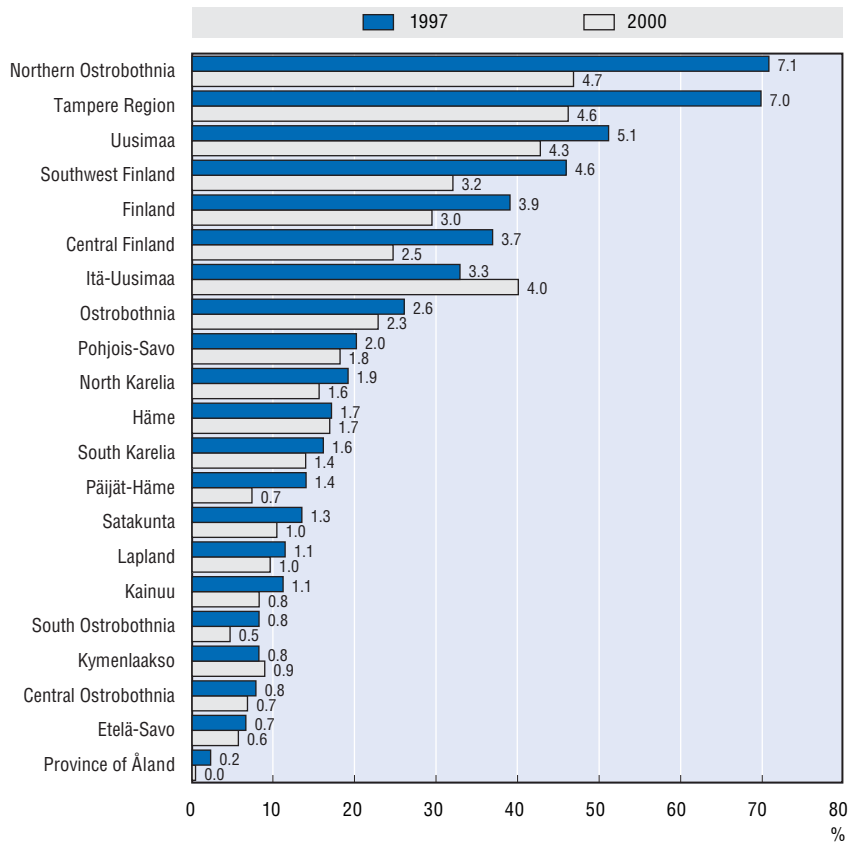
Finland and Northern Ostrobothnia are other regions with a high percentage of highly educated people (about 30%) while in all the remaining regions the proportion of skilled population is significantly lower (about 25%).

A similar pattern is detectable for the regional distribution of R&D. Over the period 1997-2000, R&D expenses as a percentage of GDP significantly increased in Finland, rising from 3% to 3.9%, which was one of the highest rates within OECD countries. This overall increase in R&D, however, was mainly driven by those regions that already had a high level of R&D, particularly Tampere Region and Northern Ostrobothnia (Figure 1.9). As a result of this trend, regional disparities in R&D have increased. In 2000, the share of GDP invested in R&D was the highest in Northern Ostrobothnia (7.1%),[11] Tampere Region (7%), Uusimaa (5.1%), and Southwest Finland (4.6%). In most other

Figure 1.9. **Regional trends in R&D in Finland, 1997-2000**
As a percentage of GDP, sorted by 2000



Source: Statistics Finland.

regions, the ratio of R&D to GDP was close to 2% while it was significantly lower in Kymenlaakso and South Ostrobothnia (0.8%), Etelä-Savo (0.7%) and Åland (0.2%).

Entrepreneurship can be considered as a strategic aspect of mastering of skills. In Finland, the relative amount of firms in comparison to population is lower than in other European countries (Eurostat New Cronos). One of the explanations put forward is that the important role of the Welfare State and public intervention did not favour a more entrepreneurial culture. Nonetheless, entrepreneurship and business culture are more developed in Western Finland than in Eastern Finland. Firm density is highest in the Åland and Uusimaa regions while the lowest density can be found in Kainuu and in Northern Ostrobothnia (Table 1.3).[12]

Table 1.3. **Places of business of enterprises by region in 2003**

Region	Number of places of business	Population of region	Places of business of enterprises/inhabitant (%)
The autonomous Åland Islands	1 815	26 347	6.9
South Ostrobothnia	10 556	193 954	5.4
Uusimaa	72 096	1 338 180	5.4
Ostrobothnia	9 312	173 111	5.4
Itä-Uusimaa	4 881	91 689	5.3
Southwest Finland	23 884	452 444	5.3
Satakunta	11 710	234 777	5.0
Central Ostrobothnia	3 517	70 584	5.0
Päijät-Häme	9 825	198 434	5.0
Tampere Region	22 223	457 317	4.9
Lapland	9 051	186 917	4.8
Etelä-Savo	7 680	162 296	4.7
Kanta-Häme	7 701	166 648	4.6
Central Finland	11 734	266 082	4.4
South Karelia	5 870	136 301	4.3
Kymenlaakso	7 917	185 662	4.3
Pohjois-Savo	10 628	251 356	4.2
North Karelia	7 052	169 129	4.2
Northern Ostrobothnia	14 964	371 931	4.0
Kainuu	3 402	86 573	3.9
Finland average	**255 818**	**5 219 732**	**4.9**

Source: Statistics Finland.

Territorial performances at the NUTS 3 level

When looking at the differences in performance between regions, one distorting factor, that of commuting, needs to be taken into account to avoid misinterpretations. Living in one region and working in another means that

earned income is accounted in one but spent income benefits another. As GDP per capita is measured with the former, commuting needs to be considered as proxy for the effects of geographic location. This having been stated, several factors contribute to explain the differences observed in regional performances. Some of these factors are related to the "natural" endowments of a region – geography, population trends, historical heritage, amenities – some others to a more efficient utilisation of regional assets – productivity, industrial specialisation, labour market efficiency, education, innovation. The factors of competitiveness specific to a region can be assessed by benchmarking regional performances against those of the whole country. Taking GDP per capita as a measure of performances, the difference between the level of GDP per capita in a region and the national average can be entirely explained as the results of seven factors:

- Labour productivity: a proxy for the productivity of the regional production system.
- Specialisation: sectoral mix has an impact on capability to compete in high value added activities.
- Employment rate: indicator of the efficient functioning of the local labour market.
- Skills: educational attainments measure the stock of human capital.
- Ageing: an indicator of the impact of population dynamics.
- Activity rate: measures the labour force supply.
- Commuting: proxy for the effects of geographic location.

The last of these factors – commuting – seems to account for a significant proportion of regional differences in GDP per capita in Finland. As individuals may live in a region and work in a different one, GDP per capita would be undersized in the region where they live and oversized in the regions where they work. When GDP per capita is corrected to take commuting into account, regional differences tend to be reduced (Table 1.4). In particular, the number of regions with a level of GDP per capita above the national average rises from three (Uusimaa, Southwest Finland and Åland) to five (Kymenlaakso and Itä-Uusimaa) while GDP per capita in South Karelia becomes close to the national average.

Figure 1.10 shows the factors behind the observed differences in GDP per capita adjusted for commuting. In a majority of regions, low labour productivity appears to be the main explanation for low GDP per capita. In Päijät-Häme and South Ostrobothnia, low productivity seems to account for a gap in GDP per capita of above 15 percentage points. In Kanta-Häme, Central Ostrobothnia, South Savo and North Savo, the GDP gap due to low productivity is no less than 10 percentage points. Productivity seems also a

Table 1.4. **Effect of commuting on regional GDP per capita in Finland (2001)**

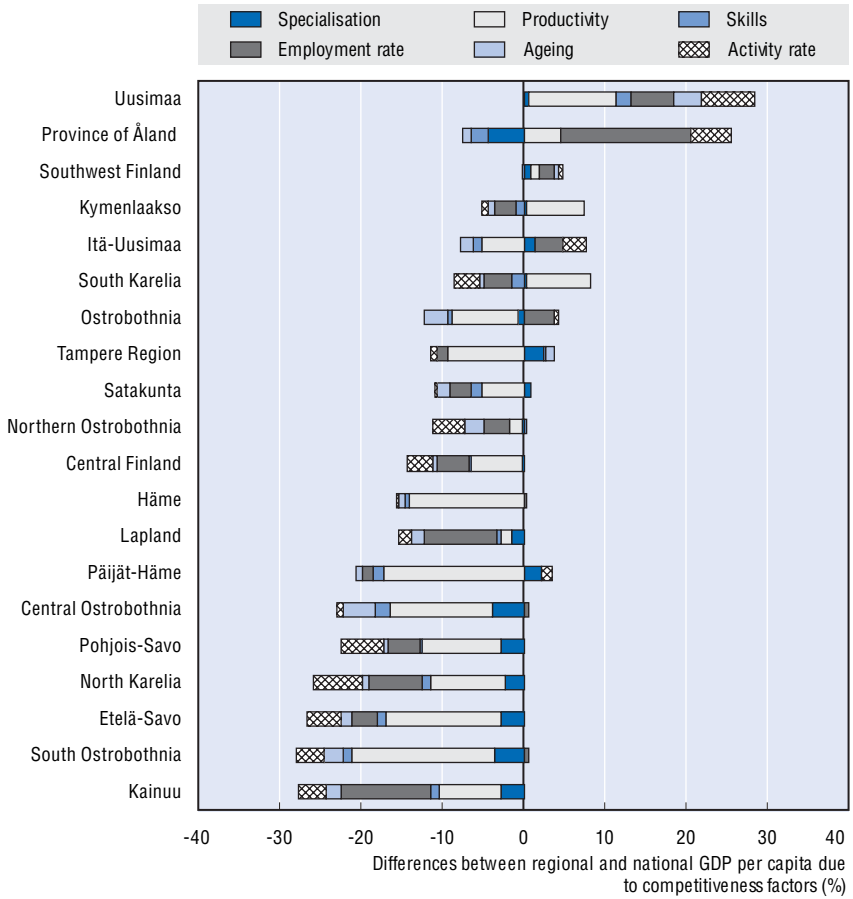
Region	GDP per capita	
	Observed	Adjusted for commuting
Uusimaa	30 420	28 318
The autonomous Åland Islands	30 632	26 069
Southwest Finland	23 006	23 083
Kymenlaakso	21 877	22 101
Itä-Uusimaa	18 492	22 597
South Karelia	21 745	21 961
Ostrobothnia	20 669	20 357
Tampere Region	20 659	20 333
Satakunta	19 423	19 898
Northern Ostrobothnia	20 036	19 675
Central Finland	18 744	18 903
Kanta-Häme	17 297	18 677
Lapland	17 882	18 646
Päijät-Häme	17 863	18 285
Central Ostrobothnia	16 678	17 113
Pohjois-Savo	16 712	17 103
North Karelia	16 003	16 384
Etelä-Savo	15 373	16 166
South Ostrobothnia	15 472	16 039
Kainuu	15 066	15 957
Finland average	**22 059**	**22 059**

Source: OECD Territorial Database.

key factor of regional success. In four out of the five regions with a GDP per capita above the national average, productivity was significantly higher. In South Karelia, high productivity compensates for the poor performance of the labour market so that GDP per capita stays close to the national average. Itä-Uusimaa is the only region where high GDP per capita does not seem to be explained by high productivity but by the combination of low unemployment, high labour market participation and specialisation in services.

High labour productivity, in turn, can be the result of four main factors: the stock of physical and human capital, the level of technology, the quality of infrastructures, and the economies of agglomeration due to the concentration of these factors in the same region. Their organisation and interaction by a cluster type approach could in itself be a fifth factor but, admittedly, it cannot be objectively measured. On the other hand, the results of a regression analysis[13] suggest that regional differences in productivity in Finland are mainly associated with settlement patterns: about 37% of the differences in productivity are explained by whether regions are urban, intermediate or

Figure 1.10. **Determinants of regional performances in Finland**



Source: OECD Territorial Database.

rural. Higher productivity in densely populated regions points out the crucial role of agglomeration economies but it is also due to the fact that investment in technology (as proxied by R&D), human capital (as proxied by educational attainments of the population) and infrastructure tend to be concentrated in urban and intermediate regions.[14]

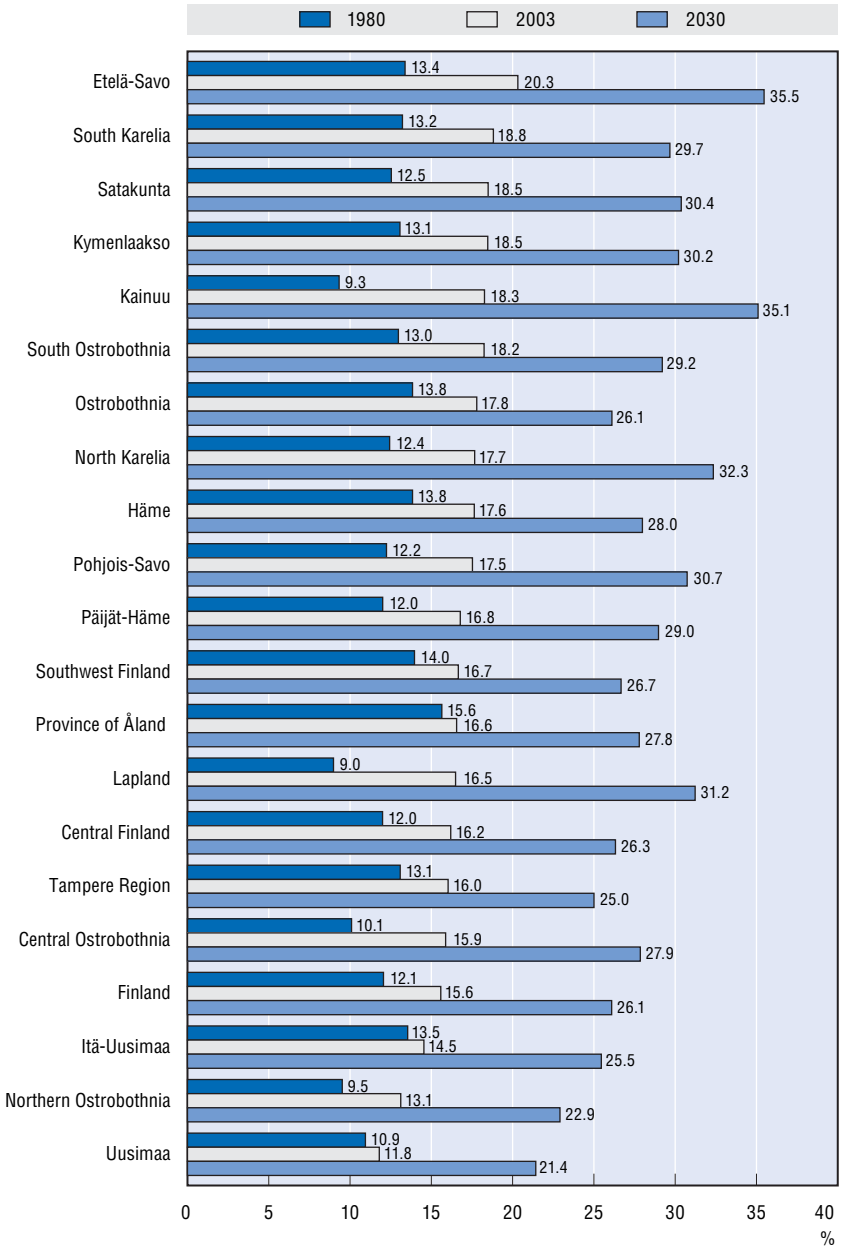
Poor performances of the labour market are a second factor of low regional competitiveness. Low employment rates in the Kainuu, Lapland and North Karelia regions seem to account for a gap in GDP per capita equal to 11.9% and 7%, respectively. In most other regions, low employment rates explain no less than 3% of the GDP gap. Participation in the labour market

appears to be a third important factor of regional performances. Due to higher activity rates, GDP per capita in Uusimaa and Åland exceeds the national level by 6% and 5%, respectively. On the contrary, in North Karelia, Pohjois-Savo, Etelä-Savo, and Central Ostrobothnia, low activity rates explain no less than 4% of the gap in GDP per capita, meaning that adequate job creation is required.

Sectoral mix mostly appears as a cause for low performances, although its effect tends to be smaller than productivity and employment. In general, GDP per worker in agriculture tends to be lower than in manufacturing and services so that the higher the share of agriculture employment, the lower the regional productivity. The gap in GDP per capita due to specialisation in low value added industries is the highest in Central Ostrobothnia and Åland (–4%) and in Etelä-Savo, Pohjois-Savo and Kainuu (–3%). Specialisation of Finnish regions appears mainly driven by two factors: the investment in technology (as proxied by R&D) and the geographic localisation of regions (as proxied by the travelling distance from Helsinki). Thus, regions with high investment in technology and a central geographic position are specialised in manufacturing whereas regions far away from Helsinki and with low investment in technology are more specialised in agriculture. This finding suggests that, to some extent, poor development in border regions is a result of the low accessibility of these areas.[15] Specialisation in services does not seem to correlate to either R&D and distance as these include both high value added activities, (likely to represent a larger share of total services in regions with high R&D) and low value added activities like retail, commerce and personal services (likely to be the largest share of services in regions specialised in agriculture).

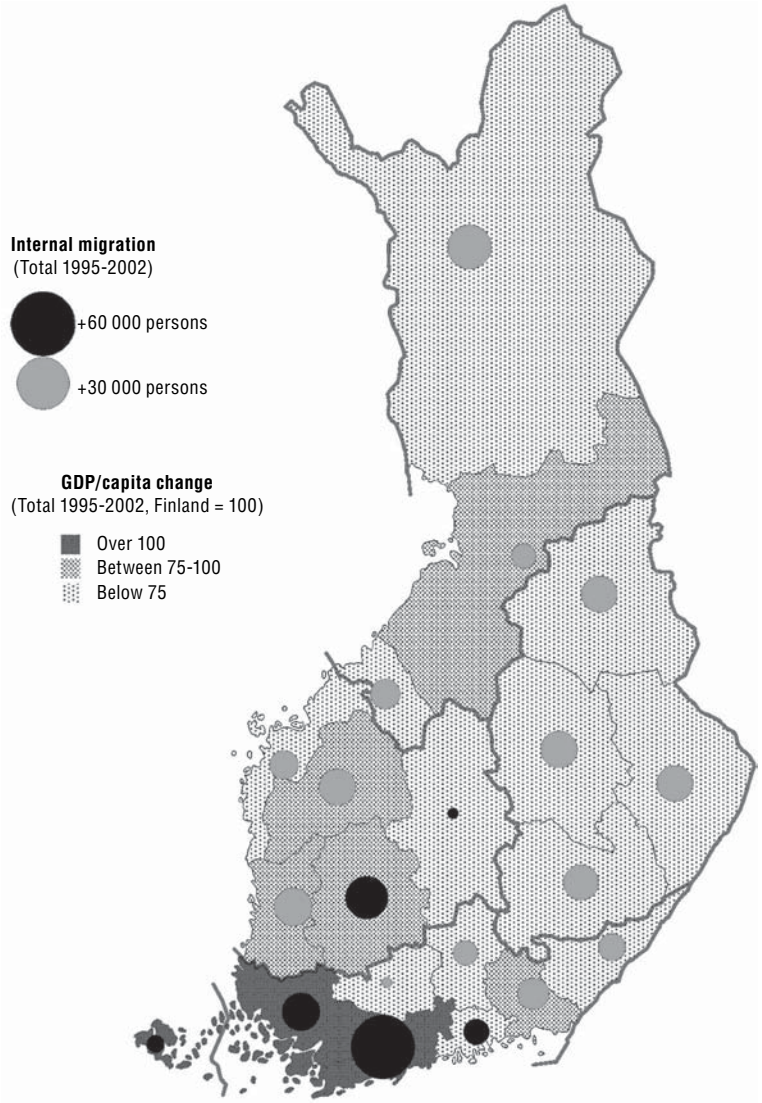
Finally, the age profile of the population tends to have a negative effect on the performances of all regions except Uusimaa, where the working age population (25-54 years old) is mostly concentrated. The GDP gap due to ageing (see Figure 1.11) is about 1% for most regions and particularly pronounced in Central Ostrobothnia and Ostrobothnia, where it accounts for no less than 3 percentage points. Ageing can also be correlated up to a certain extent with migratory patterns (see map Figure 1.12). Helsinki and its neighbouring regions (Southwest Finland and Tampere Region) benefited from significant migration inflows whereas the areas of strong out-migration are usually those where GDP per capita is among the lowest and the average age of the population is higher (Lapland, Etelä-Savo, Kainuu and North Karelia).

Figure 1.11. **Regional population aged 65 years and over (%), 1980-2030**
Sorted by 2003



Source: OECD Territorial Database.

Figure 1.12. **Internal migration in Finland, 1995-2002**



Source: Statistics Finland.

1.3. Underused potentials

Harnessing external resources

By most standards, Finland is a very successful country. As seen before, it registered the highest GDP per capita growth and increase in labour productivity amongst OECD countries between 1995 and 2002. It boasts, at

around 3.5%, among the highest rates for R&D spending in terms of percentage of GDP. It enjoys a leading position in mobile telephony. Its educational attainment levels and Internet penetration rates compare favourably with the most successful countries, laying the basis for a knowledge intensive economy and society. These high marks are recognised by the World Economic Forum,[16] which puts Finland in the number one position in the six following areas: Information Society, innovation and R&D, liberalisation, network industries, enterprise environment and sustainable development. Overall, Finland comes out at the top of a list of 14 EU member states on the basis of eight criteria (see Table 1.5).

In spite of these remarkable achievements, the "openness" of the Finnish economy remains limited in three specific areas that can contribute to regional development: Foreign Direct Investment (FDI), share of foreigners residing in the country and tourism flows. This can be explained in part by the peripheral location of the country and its unique but difficult language,[17] although, due to the excellence of the educational system many Finns speak at least one foreign language. Firstly, concerning FDI levels, Finland comes out amongst the lowest of OECD member countries. Secondly, despite the high level of education and the fact that some highly skilled job positions are not always easily filled, Finland has few foreign students and few foreigners work and live there, as compared to other European countries. Thirdly, in spite of a

Table 1.5. **Ranking of EU countries by the World Economic Forum (WEF)**

	Information society	Innovation, research, and development	Liberalisation	Network industries	Financial services	Enterprise environment	Social inclusion	Sustainable development	Average rank
Finland	1	1	1	1	2	1	3	1	1.4
Sweden	2	3	6	3	5	6	7	4	4.5
Denmark	4	9	5	4	3	5	4	3	4.6
United Kingdom	3	4	2	9	1	2	10	6	4.6
Netherlands	7	8	3	6	4	4	1	8	5.1
Germany	6	2	9	2	8	11	9	2	6.1
Austria	5	7	4	8	9	8	5	5	6.4
Belgium	9	5	7	5	7	10	2	7	6.5
France	10	6	11	7	10	12	6	9	8.9
Ireland	11	10	8	13	6	3	12	13	9.5
Portugal	8	12	10	10	11	7	13	10	10.1
Spain	12	11	12	11	12	9	8	12	10.9
Italy	13	13	13	12	13	13	11	11	12.4
Greece	14	14	14	14	14	14	14	14	14.0

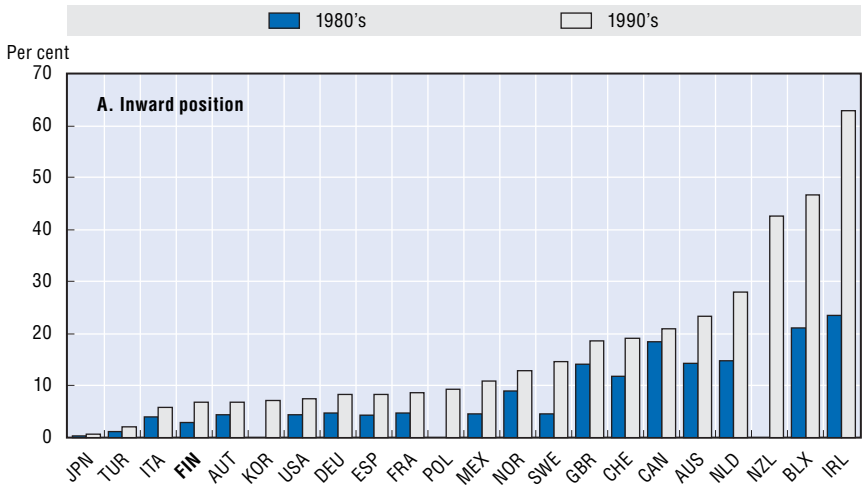
Source: World Economic Forum, 2004.

very well preserved natural environment and a worthwhile cultural heritage, the number of foreign tourists remains low in comparison to its Scandinavian neighbours. Tourism can be an important source of foreign revenue and an "image builder" but Finland remains a relatively confidential destination. All three factors – FDI, foreign population and tourism – constitute "components" of globalisation, with Finland striving, like other countries, to adapt to a changing international environment. As all three are concentrated in the Helsinki region,[18] the low level of these indicators constitutes a particular handicap for lagging areas, which cannot, under present conditions, truly benefit from the combined positive impact of these factors on the regional economy.

Limited level of FDI

Inward FDI in Finland is particularly low, with only three other OECD member countries trailing behind, when looking at the average over the 1980s and 1990s measured in terms of GDP percentage (see Figure 1.13). In absolute figures, average inward flows over the period 1999-2002 represent just about double the flows of Finnish direct investment abroad, respectively EUR 6 604 000 000 and EUR 12 467 000 000.[19] Surprisingly, the electronics industry receives a minor share as compared to more traditional manufacturing and to services, including telecommunications. These limited levels of FDI benefit very largely the Helsinki region; in 2001, the capital region registered 84 new

Figure 1.13. **FDI positions in OECD countries**
As a percentage of GDP



Note: Average values over the two periods. For countries where the FDI position data are not available, values of bilateral stocks reported by their OECD partners were summed to obtain an approximate measure of multilateral FDI stocks.

Source: OECD, *International Direct Investment Statistics Yearbook*: 1980/2000, 2001 ed.

foreign companies, with only 15 going to other regions. The figures for 2002 were respectively 82 and 24 and for 2003, 63 and 12.[20] This regional imbalance, which is a relatively frequent phenomenon in most countries, with the capital city region usually receiving the major share of FDI, signifies in the case of Finland, because of the overall low level of FDI, that regions receive but a trickle of foreign investment. Under the present conditions FDI cannot be considered as a possible factor to leverage regional development.

Using FDI to support regional development aims would suppose a substantial increase in the overall level of Foreign Direct Investment, so that the amounts going to regions could become more significant. Although the major share would be retained by the Helsinki region, specific measures could increase the percentage going to others. Such goals would not seem excessively difficult to pursue. There are no formal limitations to FDI in Finland and the overall degree of restriction is now similar to the OECD average. The OECD considers that removing remaining barriers as well as implementing further regulatory reform could boost the inward FDI position by up to one-third (OECD, 2004d). This could be coupled with more efforts to promote FDI. "Invest in Finland", established in 1992 as a bureau and a full-fledged public agency since 1996 under the responsibility of the Ministry of Trade and Industry, remains a small organisation, employing only eight people[21] and without any offices abroad. Many countries, including small ones such as the Czech Republic,[22] maintain a network of foreign offices to promote FDI. If Finland were to establish such a presence, specific campaigns highlighting the assets of certain regions in terms of know-how and specialisation could be developed.

Few foreigners in Finland

In spite of its insertion in the global economy, particularly with its strong position in ICT, Finland is among the European countries featuring a low percentage of foreign population. The total number of foreigners in Finland was 108 000 (around 2%) in 2004, having increased from only slightly more than 26 000 in 1990. The current level is still much lower than that of other Scandinavian countries (Sweden, 5.3%; Denmark, 4.9%; Norway, 4.3%) and is lower that that of the Czech Republic (2.3%) but higher than that of Hungary (1.1%).[23] The largest group is now constituted by Russians (25 000), followed by Estonians (14 000) and Swedes (8 000). Relatively high structural unemployment in certain regions, offering few low-skilled job opportunities, can explain the fact that few foreign labourers have settled in Finland. On the other hand, Finland provides an ideal environment for the highly skilled or those seeking to acquire or improve these. In the latter category, the high level of educational attainment and the excellence of its university system place Finland in an ideal position to attract promising students from abroad, yet the number of foreign students remains low. Developing the foreign student population

could, as a long term strategy, help Finnish exports and support outward investment linked to globalisation, particularly in the ICT sector.

Although Finland offers many high-level and well-paid jobs, with certain hard-to-fill vacancies, particularly outside of Helsinki, few foreigners fill these positions. This can, in part, be linked to the low level of FDI, as foreign investment usually entails presence of expatriate management. Even in the ICT equipment sector, which is totally open to globalisation, few foreign managers and researchers seem to hold positions in Finland and are mostly employed abroad in foreign affiliates. As in the case of FDI, opportunities existing in Finland seem to be under-publicised, even within the EU area. Inability to attract the highly skilled, as is done in the United States and in certain other European countries through specific amendments to otherwise restrictive immigration policies, might hinder Finland's future efforts to maintain and develop its competitive edge.

Demographic indicators clearly underline stronger trends in ageing in Finland than in many other countries, so immigration seems key to future demographic renewal and labour market fluidity, particularly after 2010 when ageing issues will become more acute. EU enlargement can offer an opportunity; it is estimated that in the first year of accession, 335 000 people will be moving from the new to the existing member countries, but that only 1.5% of them will go to Finland under the present conditions. That would mean annual immigration of only 4 000 to 5 000 people from the new member countries, mainly from Estonia, in the early phase of enlargement.[24] Another possibility would be to attract skilled Russians.

A small number of foreign visitors

Amongst the Nordic countries, Finland has the lowest number of foreign visitors. In 2002, Denmark and Sweden accounted for roughly one-third each of foreign tourists to Scandinavia, Norway represented slightly over 20% and Finland; less than 15%.[25] When looking at the number of incoming visitors related to the number of inhabitants in 2002, Finland is below the European average (0.55 versus 0.62) while Sweden and Norway are situated above (0.83 and 0.69 respectively). The total number of foreign visitors staying overnight in 2003 was 4 500 000, most visitors came from Russia (1 589 000), Sweden (779 000), Germany (344 000), Great Britain (262 000), Estonia (228 000), Norway (175 000) and the United States (119 000).[26] Increasing these numbers should not be too difficult as Nordic countries have comparable amenities to offer, whether in terms of an unspoilt environment well adapted to both summer and winter leisure activities and sports, unique experiences (midnight sun, aurora borealis) or cultural and architectural heritage.[27] Contrary to many tourism destinations, tourism in Scandinavian countries is not necessarily restricted to certain times of the year, as all seasons are attractive. Tourism infrastructures,

in particular lodging facilities, are well developed in all Scandinavian countries. Due to these comparable conditions, Finland could well increase its share of the international tourism market with a view towards supporting regional development.[28]

Many of the tourism sites and attractions in Finland are located in regions (Lapland, Eastern Finland) where GDP per capita is lowest and unemployment higher than average, so tourism can in itself benefit the local economy. This is the case in Lapland, where, aside from many Finns, the area draws a rising number of foreign tourists. There were 12 500 international charter passengers in Lapland in 1990, 100 000 in 2001 and 180 266 in 2003. This last year direct tourism income represented EUR 377 million and employment of 3 472.[29] There is certainly an underdeveloped potential to exploit in most Finnish regions including the latter, as well as room for attracting more tourists from other parts of Europe, with the majority of present visitors coming from other Scandinavian countries and northern Europe. Developing overall tourism flows could also have beneficial side effects concerning longer term prospects for settlement of foreigners in Finland by contributing towards building the image of a hospitable country offering many amenities and a good quality of life.

1.4. Major issues

Territorial disparities and competitiveness

As indicated in the preceding sections, territorial development disparities are the result of a combination of factors concerning regional endowments (level of skills, accessibility, and infrastructure) and weaknesses (higher than average unemployment, ageing, out-migration). Regional policy seeks to either enhance the former and/or compensate the latter depending on the specific characteristics of each region, by targeted use of certain measures. Bearing this in mind, the profile of Finland in its settlement patterns, from highly urban to deep rural, with a wide spectrum of intermediate situations, raises important questions in terms of regional competitiveness, innovation capacities and challenges to deliver quality public services across the whole country. Adequate analysis of these issues requires, as a preliminary, a presentation of urban settlement patterns, a summary of the geography of R&D and lastly the identification of the areas where demographic decline and low density conjugate in rendering public service delivery more costly and difficult.

In each case, policy requirements can be formulated in simple terms. Looking at competitive urban environments, the question is: can Finland benefit from a prospering capital city region and other large urban regions, which are essential growth engines for the economy, and support simultaneously a thriving network of small and medium size cities? This first issue appears from the presentation of the Finnish urban profile and related typologies. Can Finland both

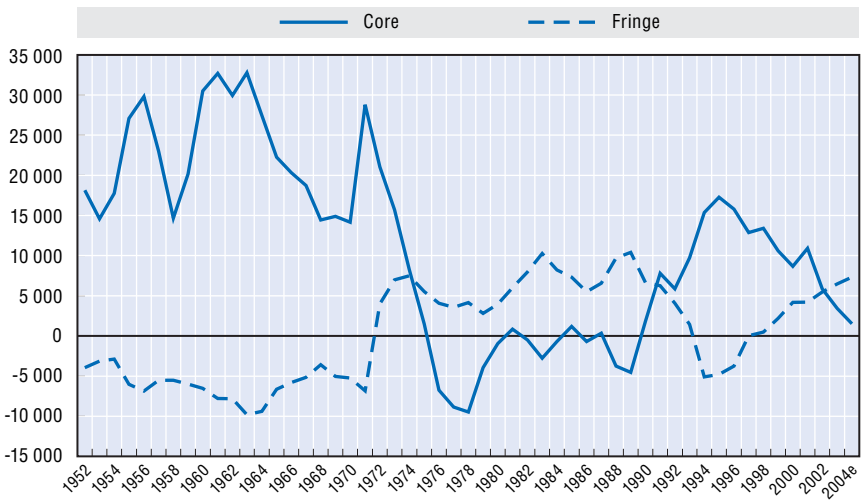
support high level technologically oriented R&D and also encourage innovation in regions where skills and cluster effects are not developed at the same scale? This second issue stems from the clear-cut geography of R&D concentrated in a few regions. Finally, can Finland maintain the essential characteristics of the Welfare State in all areas, including sparsely populated territories experiencing out-migration, without an excessive burden on public finances? This third issue relates to certain well identified regions or sub-regions, the characteristics of which need to be presented.

Urbanisation in Finland

The evolution of urban settlements in Finland over the past 100 years strongly reflects structural changes in the economy, with a relative stability until the 1960s and then accelerated change since the 1970s followed by the turning point of the recession in the 1990s (Antikainen and Vartiainen, 2005a and 2005b). From the late 19th century to the 1960s, urban growth in many parts of the country was often linked to the availability of natural resources, particularly in the forest sector. On the other hand, Southern Finland remained the most urbanised area, on the basis of maritime trade and accessibility, as well as political factors. The transfer of the capital from Turku to Helsinki in 1812 (only 4 000 inhabitants at that time) triggered its development and led to pre-eminence *versus* other cities.

Changes in the Finnish industrial and settlement structure were extremely quick and profound in the 1960s and early 1970s (Figure 1.14).

Figure 1.14. **Regionalisation of Finnish urban network**



Source: Statistics Finland and Ministry of the Interior.

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Strong restructuring and resulting urbanisation ("Great Move") led to a certain distinction between a developed Southern Finland and lesser-developed regions in Northern and Eastern Finland. This, in turn, led to the formulation of the first explicit regional policy initiatives, with the urbanisation process still rapid within peripheral areas in the 1970s and 1980s. Regional development thus remained relatively balanced and reflected the values and mechanisms of a strong Welfare State. Welfare institutions supported the growth of regional and local centres in less favoured regions. Smaller centres were strengthened by reforms in education and health care, affording equal access to a well distributed system of public service delivery. Rural centres grew as migration from sparsely populated areas accelerated, particularly during the 1960s. On the other hand, medium-sized regional centres were bolstered by new universities, the creation of regional state administrations and regional services. In parallel, industrial policy favoured investment in lagging regions.

The Finnish urban system that emerged since the mid-1970s was characterised mainly by the growth of cities of different sizes and "suburbanisation" of urban regions. At that time, this change in urbanisation patterns often began to be equated in Finland with regionalisation. The process was already prevalent in the 1970s and 1980s. The 1990s were actually a period of "urban centralisation", but starting in 2002 fringe municipalities began to attract again more people than core cities in Finnish urban regions. In the latter half of the 1990s – at the same pace as the recovery of the economy – domestic migration flows climbed up to the level of the early-1970s, when records in annual migration numbers were reached. The fear of another "Great Move" became more explicit and was considered to be fatal for Finnish rural and less-favoured regions. During the regional transition of the latter half of the 1990s, differences between Southern Finland and Northern and Eastern Finland were increasing again because the development of peripheral urban regions was lagging behind that of growth regions located mainly in the South.

From 2002 onwards, the regional development trend has evened out, and can be characterised as a period of decentralisation. The growth of the largest centres, including the capital region has slowed down and there are now more regional centres that have a positive migration balance. Also small and medium-sized urban regions as well as rural areas with good accessibility to the large urban areas in Southern and Western Finland have gained population. Present day policies to foster regional urban centres inherit these features, with limits between urban and regional policy being somewhat blurred, as developed further. There was no clear-cut location factor: growth was experienced in some eastern and northern fringe centres while population decline occurred in certain industrial urban regions in the South (see Figure 1.15). The Helsinki-Tampere-Turku triangle and "island-like" regional centres such as

Figure 1.15. **Migration patterns in the Finnish urban network**

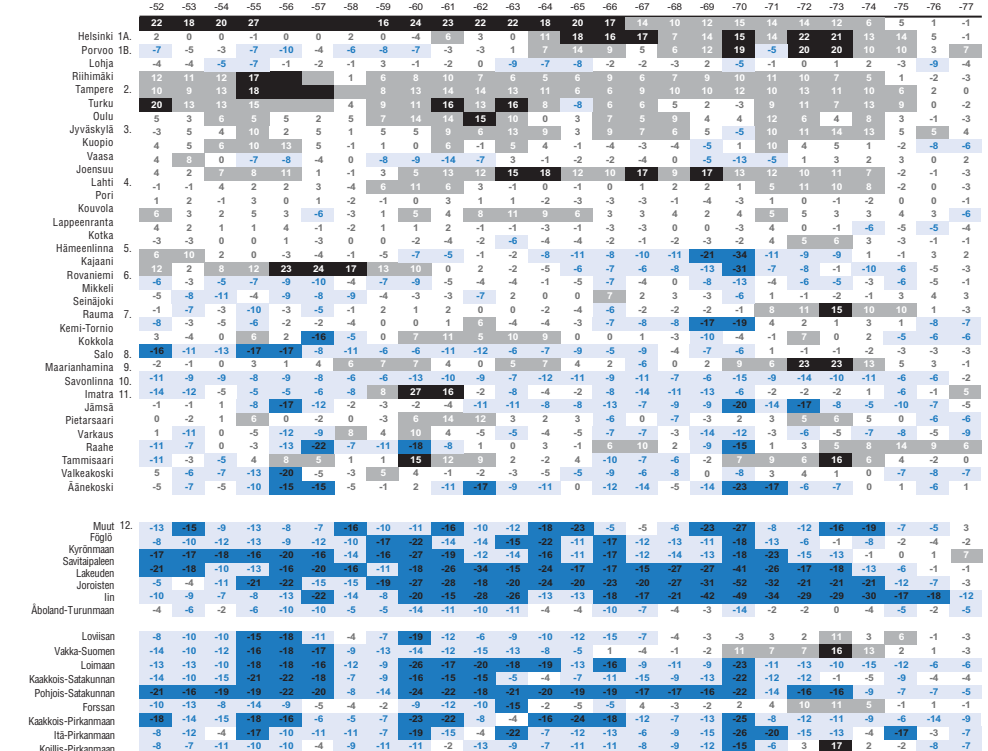

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Figure 1.15. **Migration patterns in the Finnish urban network** *(cont.)*

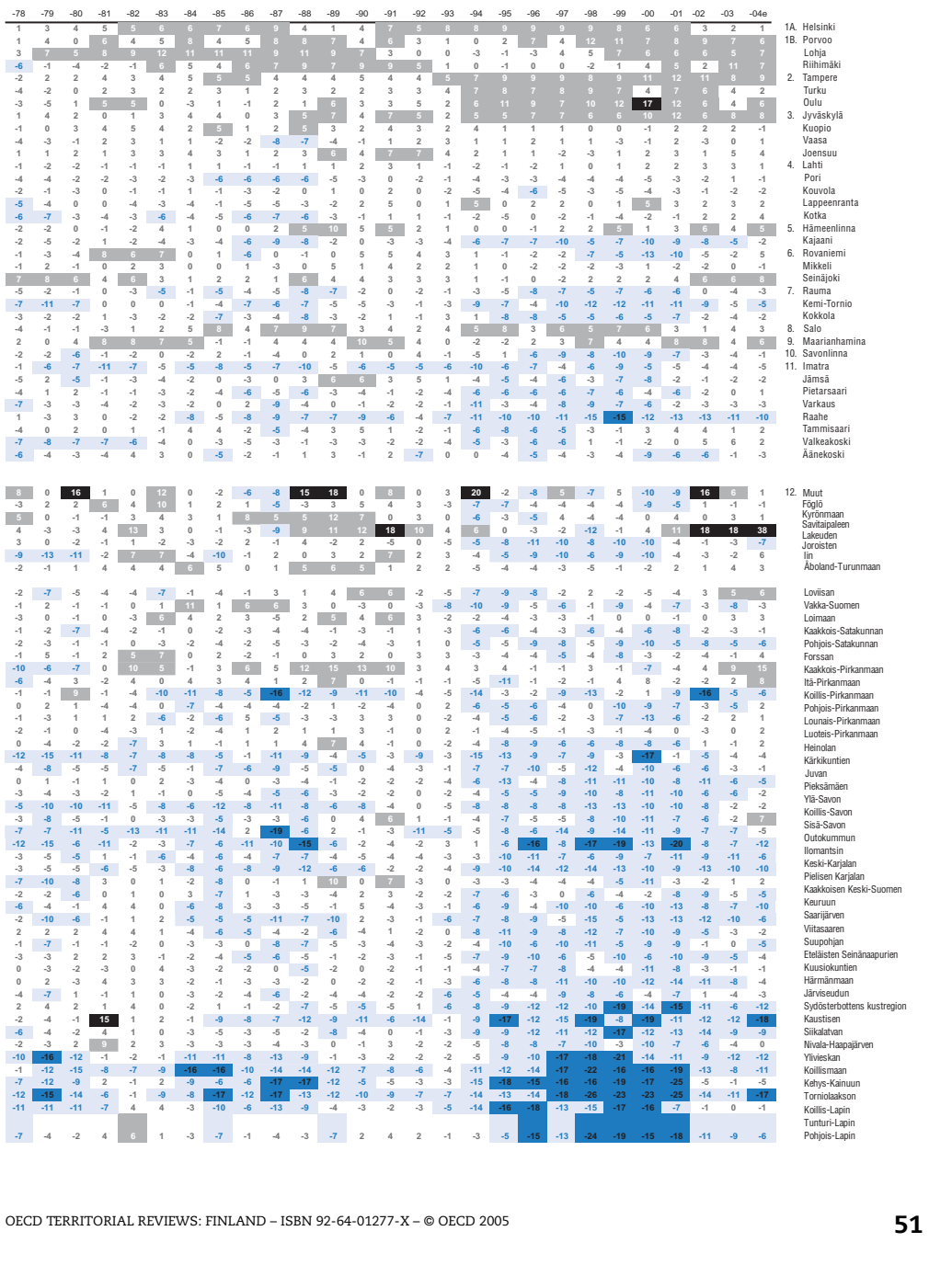


Figure 1.15. **Migration patterns in the Finnish urban network** *(cont.)*

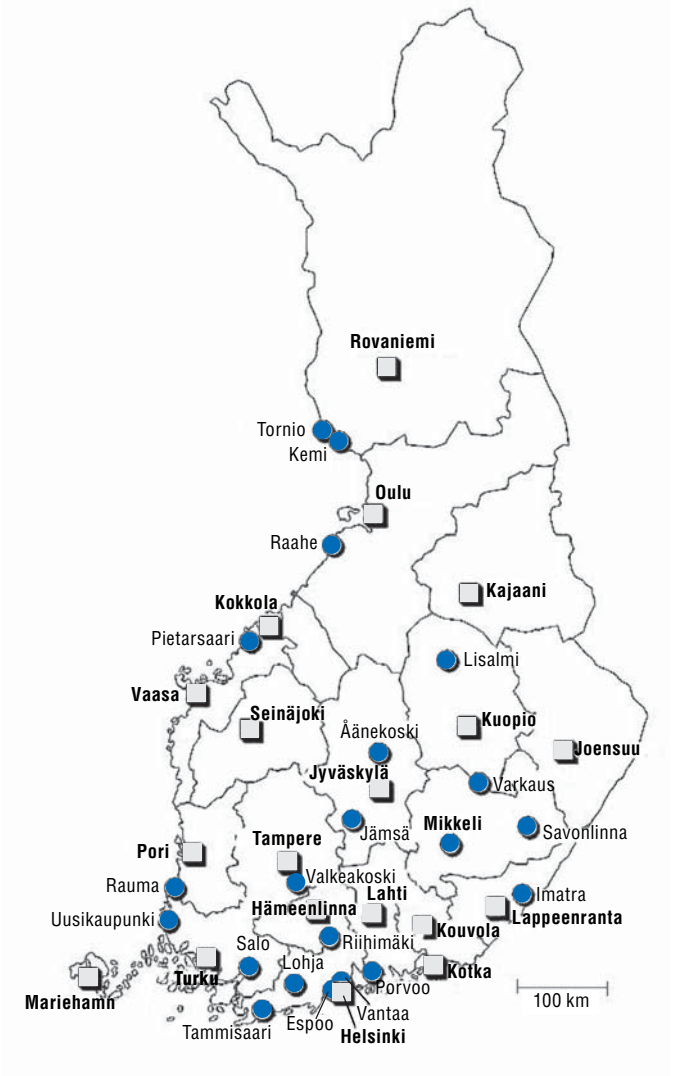
Migration patterns in Finland 1952-2004e.
Horizontal axis: years 1952-2001, vertical axis: sub-regions.
Rows 1-35 are urban regions, which are arranged according to the typology presented in the Urban Network Study, 1998 (Vartiainen and Antikainen, 1998, similar to typology presented in Table 1.7) Classification runs from A (Helsinki) to D (one-sided small urban regions).
Rows from 36 onwards are other than urban regions. First seven (7) rows are sub-regions, which because of administrative boundaries are classified as non-urban regions but are, in fact, influenced by near-by urban regions. Other sub-regions from row 43 onwards are arranged according to their sub-region number (approximately from South to North).
The numbers in cell refer to the net migration balance in sub-regions, *i.e.*, in-migration minus out-migration divided by the number of inhabitants in the sub-region. Number includes both domestic migration and emigration/immigration. Number is presented in per mil ([permil]).
Source: Statistics Finland and Ministry of the Interior (Janne Antikainen).

Oulu (Northern Ostrobothnia), Jyväskylä (Central Finland), Vaasa (Ostrobothnia), Kuopio (Pohjois-Savo) and Joensuu (North Karelia) illustrate this polycentric evolution (see Figure 1.16).

The strong recession of the 1990s, followed by a very rapid recovery after 1994, opened a period of regional differentiation. A few "winners" emerged thereafter: Salo (Nokia plants, company headquarters in Espoo), Helsinki, Oulu, Tampere but also Turku and Jyväskylä, although to a lesser degree (see Table 1.6). All of these early winners share common features: they are either large university regions and/or centres of ICT and electronics industries. Conversely industrial cities such as Lahti and Pori and one-sided and usually small-sized industrialised urban regions on the one hand and regional centres based on public sector services suffering strong budget cuts on the other were left behind. Looking at the more than 30 small urban regions (around 30 000 inhabitants), the situation is contrasted, with university-city regions usually faring better. Medium-sized cities in Northern Finland (Rovaniemi, capital of Lapland) and Eastern Finland (Kajaani, capital of Kainuu), that are mostly public sector oriented, face massive unemployment and out-migration.

The urban network in Finland comprises one European level centre with the Greater Helsinki Metropolitan Area, a few strong national centres, all located in Southern Finland, with the exception of Oulu and some 30 or more medium or small-sized regional centres. Although urbanisation has significantly increased since the Second World War, Finland remains one of the least urbanised OECD member countries. According to the OECD typology, only 25.5% of the population resided in a predominantly urban region in 2002, versus 62.2% in predominantly rural regions and 12.3% in intermediate regions.[30] According to Statistics Finland, the country had in 2002 eight urban regions with more than 100 000 inhabitants, totalizing a little more than 2 500 000 people (around half of the population). The Helsinki Region, consisting

Figure 1.16. **Map of Finland's cities**



Source: Ministry of the Interior.

of 12 municipalities, comprises 1 200 000 inhabitants, meaning that the seven other urban regions represent together only slightly more than 50% of the urban population. Looking at the size of municipalities, the three main cities within the Helsinki Metropolitan Area (HMA), Helsinki (559 000), Espoo (227 000) and Vantaa (185 000) are larger or equivalent in size to the next biggest city, Tampere (203 000). The Helsinki region concentrates 20% of the population, 25% of employment and one-third of the national GDP.

Table 1.6. **Growth of city regions of over 100 000 inhabitants between 1980 and 2004**

	1980		1990		2000		2004	
	Core	Region	Core	Region	Core	Region	Core	Region
Helsinki	483	938	492	1 044	555	1 201	560	1 240
Tampere	166	248	173	269	195	300	203	316
Turku	164	245	159	259	173	283	175	290
Oulu	94	141	101	159	121	189	127	203
Lahti	95	147	93	151	97	155	98	157
Jyväskylä	67	130	70	142	79	156	81	163
Kuopio	75	100	80	109	87	116	88	118
Pori	80	119	76	118	76	116	76	116
Whole country		4 788		4 998		5 181		5 236

Source: Statistics Finland and Ministry of the Interior.

Efforts to better understand new urban trends and their links with regional development led to the elaboration of typologies aiming at providing the analysis necessary for the design of better targeted policies. The typology generated in the Urban Network Studies (1998 and 2001) was applied in a 2004 publication of the Ministry of the Interior entitled "The Growth of Urban Regions" and recognises five types of urban districts,[31] four of which are divided into sub-categories (see Table 1.7).

Most recent trends (Antikainen and Vartiainen, 2005a and 2005b) show that the strong concentration that was taking place in the latter part of the 1990s has evened out. A certain number of medium-sized urban regions are also now amongst the "winners". On the basis of performances during the 2000-2002 period Finnish urban regions can be currently grouped into three different categories. Strongly developing and mainly large university centres and adjoining regions include Helsinki and adjacent areas, with Tampere, Jyväskylä, Turku and Oulu in this top group. Relatively balanced developing regional centres comprise other diversified university regions such as Kuopio and Joensuu and also medium-sized urban regions. Declining peripheral and small industrial centres usually saw their situation aggravated during the same period as indicated below.

The first two categories benefited from positive immigration flows. In particular, this is the case of the Helsinki region and adjacent areas, attracting in particular the younger population holding a higher education degree. Outward sprawl extended to Porvoo to the East and Lohja to the West and even as far as Tammisaari to the Southwest and Lahti to the Northeast. In parallel, the 200 kilometre-long Helsinki-Tampere urban corridor pursued its expansion.

Table 1.7. **Typology of urban regions**

Typology	Classification	Urban regions
A. Helsinki region and near-by regions	Aa. Helsinki region	Helsinki
	Ab. Near-by regions	Lohja Riihimäki Porvoo
B. Diversified university regions	Ba. Technology regions	Tampere Turku Oulu Jyväskylä
	Bb. smaller diversified regions	Kuopio Vaasa Joensuu
C. Regional centres	Ca. Industrial	Lahti Pori Kouvola
	Cb. Diversified	Kotka Lappeenranta Hämeenlinna Mikkeli Seinäjoki
	Cc. Public sector based regions	Rovaniemi Kajaani
	Cd. Small growth regions	Maarianhamina Salo
D. Small and specialised regions	Da. Industrial centres	Rauma Kemi-Tornio Kokkola Imatra Jämsä Pietarsaari Varkaus Raahe Valkeakoski Äänekoski Uusikaupunki Tammisaari
	Db. Peripheral centres	Savonlinna Lisalmi
E. Other regions	Other than functionally significant urban regions	48 regions

Source: Ministry of the Interior (Kaupunkiseutujen kasvun aika, 2004).

On the contrary, peripheral cities strongly relying on the presence of public sector services continued to suffer from increasing out-migration.

The number of jobs increased in all groups during the last ten years, with acceleration towards the end of the last decade. In addition, urban regions with the highest positive migration balance are also those where job creation

is the highest. However, because of the development of commuting, adjacent urban regions of Helsinki are enjoying a much higher immigration gain than job creation totals would suggest, as many of these are created in the core area. These trends have not however led to significant improvements in terms of reducing unemployment, even in the growth regions. This is due to the fact that employment growth is predominantly based on that of the new knowledge-based industries that do not provide opportunities for an often elderly and lesser qualified labour force. Contrary to the preceding period, job loss was also registered in most of the peripheral and declining industrial centres.

The geography of R&D

Finland exhibits a highly geographically concentrated pattern of R&D. Peripheral regions like Lapland, Pohjois-Savo and Etelä-Savo have R&D expenditures per capita around eight times less than the capital city region. Table 1.8 shows that the top four regions account for more than four-fifths of

Table 1.8. **R&D expenditure by region and sector 2003**

Region	Business	Public agencies	Universities	Total	
	EUR millions	EUR millions	EUR millions	EUR millions	%
Uusimaa	1 437.8	334.2	371.8	2 143.8	42.7
Itä-Uusimaa	43.2	–	0.1	43.3	0.9
Southwest Finland	389.0	13.5	134.3	536.8	10.7
Satakunta	55.3	2.5	8.6	66.5	1.3
Kanta-Häme	34.4	31.0	4.7	70.2	1.4
Tampere Region	601.7	40.3	126.7	768.7	15.3
Päijät-Häme	39.7	1.3	2.5	43.5	0.9
Kymenlaakso	36.8	0.3	2.2	39.3	0.8
South Karelia	40.9	1.6	24.0	66.5	1.3
Etelä-Savo	8.4	3.4	8.4	20.1	0.4
Pohjois-Savo	42.5	13.4	56.7	112.6	2.2
North Karelia	15.8	10.6	30.4	56.9	1.1
Central Finland	111.6	16.7	65.3	193.6	3.9
South Ostrobothnia	13.4	1.2	3.4	18.0	0.4
Ostrobothnia	83.2	1.0	10.8	95.0	1.9
Central Ostrobothnia	10.5	2.3	2.4	15.2	0.3
Northern Ostrobothnia	535.8	28.7	104.7	669.3	13.3
Kainuu	11.9	1.5	3.0	16.4	0.3
Lapland	15.3	10.9	16.4	42.6	0.8
Åland	*0.8*	*0.8*	–	*1.6*	*0.0*
Total	**3 527.9**	**515.4**	**976.3**	**5 019.7**	**100.0**

Source: Statistics Finland.

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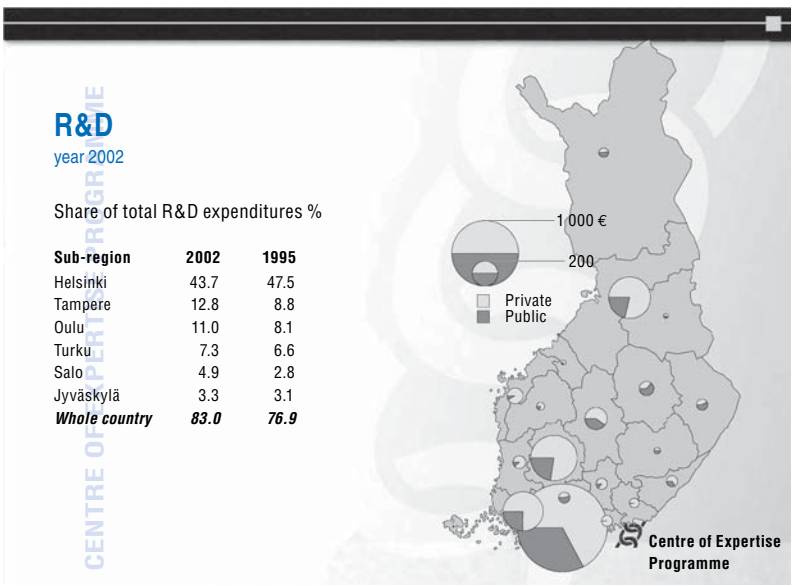
corporate, public, Tekes company and Tekes HEI funding, (capital city: over 40%). It reveals that in leading regions private investment outstrips public investment but in peripheral regions (North Karelia, Lapland) public investment including universities is not matched by the private sector. The geographical distribution of knowledge intensive sectors partly explains this, since electronics and ICT, highly concentrated in Helsinki and other major cities, account for around 60% of private R&D.

These regional figures conceal the fact that R&D expenditure is concentrated in a limited number of major cities (Figure 1.17). In terms of R&D intensity per capita the top ranking cities are Salo, Oulu, Helsinki, Turku, Jyväskylä and Tampere, representing together 83% of R&D expenditure in 2002, increasing since 1995 (76.9%) With the exception of Salo, the original base for Nokia, all of these are university cities. The remaining university cities are Vaasa in Western Finland, Kuopio, Lappeenranta, Joensuu in Eastern Finland, and Rovaniemi in Lapland ranking 8th, 7th 11th, 12th and 20th respectively in terms of R&D investment per capita. Kuopio, Joensuu and Lappeenranta together with Rovaniemi were locations for the creation of new universities during the 1960s.

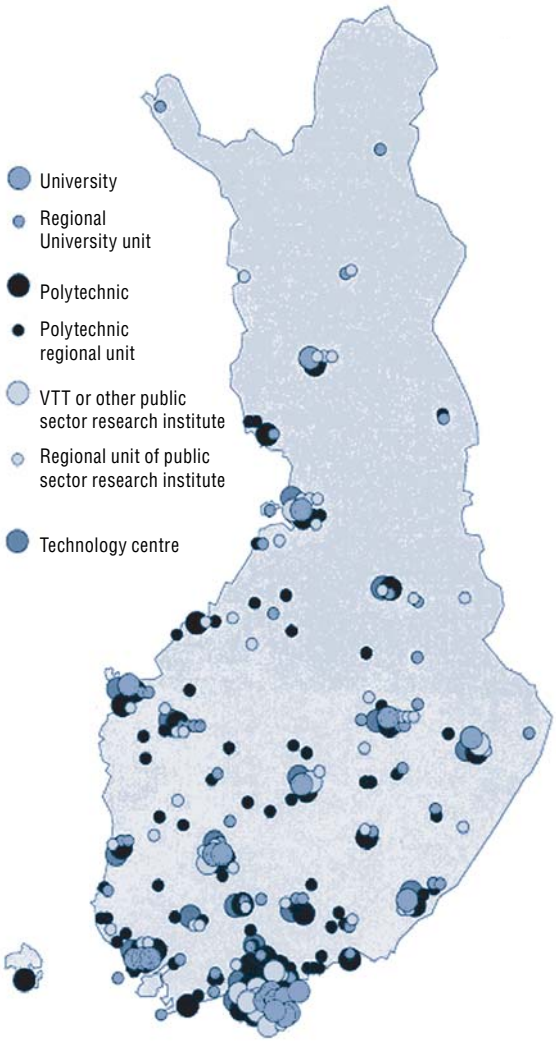
There is no comprehensive map of the location of the components of the national innovation system (see Chapter 2, Section 2.3). Figure 1.18, compiled by Tekes, suggests a much more geographically dispersed structure of units

Figure 1.17. **Share of total R&D expenditure**



Source: Ministry of the Interior.

Figure 1.18. **Network of universities, polytechnics, public institutes and technology centres**



Source: Tekes, *Innovations Generate Regional Vitality*, 2004.

than is identified by investment in R&D itself. While many of the units are very small, such as the outstations of universities and polytechnics, the map confirms clustering of intermediaries in major cities outside of Helsinki notably Turku, Tampere, Oulu, Jyväskylä, Lahti and Kuopio. This "dispersed concentration" is particularly important for the support of non-intensive R&D sectors (forestry, metal and food processing) located outside the core regions. Nevertheless, the extent to which other smaller centres can achieve

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a critical mass of infrastructure (communication links, specialised business services), and high level skills plus the social and cultural facilities to attract and retain creative people constitutes a major issue for regional innovation policy.

How do these innovation inputs link to outputs in terms of company and regional performance? Little data are available to directly answer this question. An analysis by Tekes of average R&D spending per capita by region over the period 1997-1999 and added value per capita in 2001 reveals a clear correlation between R&D inputs in the earlier period and value added performance at the later date. Data on patent registrations exhibit a less geographically concentrated pattern than R&D but nonetheless around 40% originate from the capital city region, 15% from the Tampere region, 8.5% from Southwest Finland, 7.5% from North Ostrobothnia (Oulu) and more than 5% from Central Finland in 2003.[32] "Inventive capacity" is useful to establish but it does not indicate which patents have been successfully developed into new businesses. This is linked to concerns of access to credit for development of business ideas and also entrepreneurial attitudes needing to be developed (see Chapter 3, Section 3.4).

Tables 1.9, 1.10 and 1.11, forming a set, draw together data on R&D expenditure for the main growth regions of Helsinki, Tampere, Oulu and Turku, comparing them with three regions in Eastern Finland where universities play a major role and Jyväskylä as an "in-between" case. The Helsinki region accounts for around 40% of inputs into and outputs from the innovation system (although as Figure 1.17 shows, its share of R&D expenditure has declined slightly

Table 1.9. **R&D expenditure indicators by region in 2003 (four key regions *versus* others)**

Region/ City-region	Total		Business enterprises		Public sector (research. Institutes)		University sector	
	EUR millions	%	EUR millions	%	EUR millions	%	EUR millions	%
Finland total	**5 019.7**	**100.0**	**3 527.9**	**100.0**	**515.4**	**100.0**	**976.3**	**100.0**
Uusimaa/Helsinki	2 143.8	42.7	1 437.8	40.8	334.2	64.8	371.8	38.1
T-Region/Tampere	768.7	15.3	601.7	17.1	40.3	7.8	126.7	13.0
N-Ostrobotnia/Oulu	669.3	13.3	535.8	15.2	28.7	5.6	104.7	10.7
SW-Finland/Turku	536.8	10.7	389.0	11.0	13.5	2.6	134.3	13.8
Other regions	901.1	18.0	563.6	16.0	98.7	19.1	238.9	24.5
C-Finland/Jyväskylä	193.6	3.9	111.6	3.2	16.7	3.2	65.3	6.7
P-Savo/Kuopio	112.6	2.2	42.5	1.2	13.4	2.6	56.7	5.8
N-Karelia/Joensuu	56.9	1.1	15.8	0.4	10.6	2.1	30.4	3.1
S-Karelia/Lappeenranta	66.5	1.3	40.9	1.2	1.6	0.3	24.0	2.5

Source: Statistics Finland, Tekes, Ministry of Education (KOTA database).

Table 1.10. **R&D funding, patents and publications by region (four *versus* others)**

Region/ City-region	Tekes R&D funding (2003)				Domestic patent applications by companies in Finland (1999-2003)		Academy of Finland funding to universities (2002)		Scientific publications by universities in the region (2003)	
	Firms		University							
	EUR millions	%	EUR millions	%	Number	%	EUR millions	%	Number	%
Finland total	**230.0**	**100.0**	**162.0**	**100.0**	**8 371**	**100.0**	**127.0**	**100.0**	**22 213**	**100.0**
Uusimaa/Helsinki	96.1	41.8	74.2	45.8	3 354	40.1	59.4	46.8	8 716	39.2
T-Region/Tampere	29.6	12.9	23.1	14.2	1 355	16.2	13.5	10.6	2 974	13.4
N-Ostrobotnia/Oulu	19.3	8.4	15.3	9.4	666	8.0	11.7	9.2	2 111	9.5
SW-Finland/Turku	27.3	11.9	11.4	7.0	692	8.3	20.8	16.4	4 116	18.5

Source: Statistics Finland, Tekes.

Table 1.11. **EU-funding for R&D and Objectives 1&2 (structural funds): four regions *versus* others**

Region/City-region	EU-funding for R&D and innovation (total 2000-2005)		EU objective 1 and 2 funding (2000-2004): EU + national parts	
	EUR millions	%	EUR millions	%
Finland total	**240.6**	**100.0**	**2 166.0**	**100.0**
Uusimaa/Helsinki	0.2	0.1	2.8	0.1
T-Region/Tampere	11.8	4.9	68.3	3.2
N-Ostrobotnia/Oulu	16.9	7.0	207.5	9.6
SW-Finland/Turku	6.6	2.7	59.2	2.7
Other regions	205.1	85.3	1 828.2	84.4
C-Finland/Jyväskylä	23.7	9.9	174.0	8.0
P-Savo/Kuopio	29.8	14.2	302.8	14.0
N-Karelia/Joensuu	18.4	7.6	201.8	9.3
S-Karelia/Lappeenranta	15.4	6.4	65.3	3.1

Source: Ministry of the Interior (FIMOS database).

since 1995). The only exception concerns public research institutes where the Helsinki region accounts for 65% of expenditure (versus 38% within the university sector). Significantly, competitive funding to universities from Tekes and the Academy of Finland is more concentrated than total university R&D but the outputs that could be linked to these inputs in terms of patents and academic papers respectively is more dispersed, suggesting that research "productivity" may be greater in less central areas (Table 1.10). However, the absence of matching R&D capacity in the business sector and growing global competition in academic research create added difficulties for smaller cities and universities to sustain the research base and translate it into commercial benefit.

A significant redistribution of funding, currently absorbed by public research institutes in the Helsinki region, could contribute to sustaining the research capacity of regions and yield greater value for money in terms of research output. Activity that helps to translate research into business benefits is supported by EU structural funds for R&D and innovation. These funds have been of great importance in Eastern Finland and to a lesser degree in Oulu and Jyväskylä (Table 1.11). The evidence of patenting activity in the smaller regions could reflect the influence of the EU measures and the presence of creative people living in these areas, including those working in Knowledge Intensive Business Services (KIBS). However the impending rundown of EU funding does suggest that some national redistribution of public resources will be necessary if achievements are not to regress.

Profile of areas with declining population

The problems of areas with population decline are profound, as these areas have not yet succeeded in replacing an occupational structure of agriculture and traditional manufacturing industries with profitable "new economy" enterprises and job creation (excepting a growing tourism sector). On-going out-migration of young people to regional and national centres and low birth rates aggravate the problem of keeping population numbers stable. The financing of service provision is directly linked to the local economy, because tax on personal income is the main source of municipal finance, on average it makes up 52% of municipal revenue.[33]

Service delivery within social welfare, health care, education and culture make up an average total of 74% of municipal expenses (current expenditure and expenses). The challenges of service delivery are underlined by changing needs, on one side a declining number of children to be served by day-care and educational services, and on the other side an ageing population, generating an increased demand for services within health, home-based care and institutions for the elderly.[34] The municipality of Ranua (population 4 800) in Lapland,[35] gives a striking example of these changes: 55% of the current expenditure goes to social welfare and health services, and 34% to educational services. In the 1970s, the expenditure proportions were exactly opposite, meaning that this municipality, like many others facing ageing and out-migration, has gone through a redirecting of budgetary priorities due to changes in demand stemming from demographic processes.

On the national level, expenditures in long-term care are expected to grow from 1.6% to 2.7% of GDP in the 2000-2030 period (OECD 2003a, Table 10). At the municipal level, where today an average of 48% of the expenditure goes to social welfare and health care, an expenditure rise as envisaged in the GDP projection will make it very difficult to also keep up educational, cultural and infrastructural standards. As the latter strongly contribute to the attractiveness of

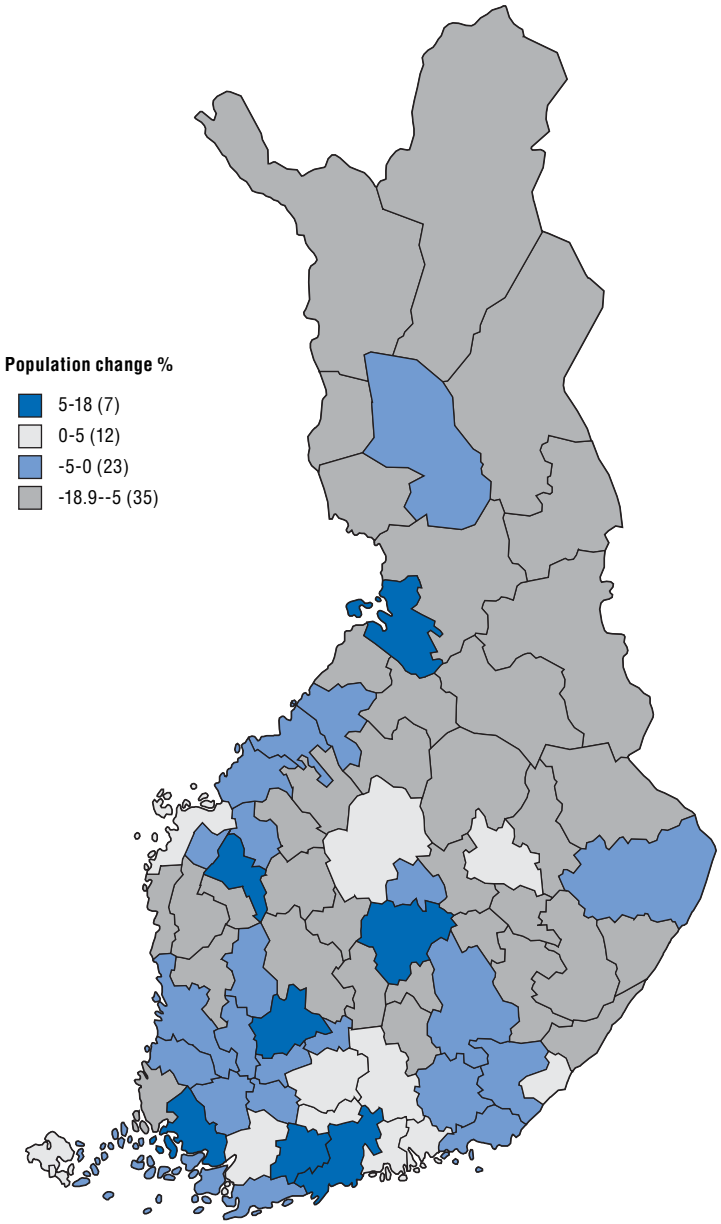
small areas and towns to retain young inhabitants and attract newcomers and entrepreneurs, this could become a major issue in the future, with declining population areas at risk of progressively losing their vitality and becoming mostly "retirement settlements". These trends however are not only a problem for areas of declining population, as ageing processes will affect the whole Finnish society in the coming decades, but their impact will be more difficult to deal with in these smaller declining areas.

Areas with population decline are to be found mostly in low density territories, rural parts of Northern Finland, in Eastern but also in Western Finland. These areas are estimated to comprise around one million inhabitants, 20% of the total Finnish population. As the map shows, the proportionally largest losses in population are in the regions of Lapland, Kainuu, and Etelä-Savo. It is predicted that these three regions will also suffer the greatest losses in the years to come; by 2030, the population decline in these three regions could be of one-third.[36] In the 1995-2004 period, 11 out of Finland's 20 regions have already experienced population decline (Nordregio Report 2002:2, Figure 1.7), so the phenomenon is not only a peripheral one that would be limited to certain areas, particularly those with the lowest population densities.

Some smaller cities have experienced population decline, but in general population loss is mostly a problem of the rural areas of Finland's eastern and northern periphery, and particularly in rural areas without reasonable commuting possibilities to a regional centre (distance and accessibility). It is essential here to underline that not all rural areas are areas of declining population as Figure 1.19 demonstrates. Rural areas located within commuting distance to the larger cities of Finland are experiencing population growth, and are at present assessed as the most favourable environments for habitation in Finland (Rintala and Heikkilä 2004, p. 171). Such a finding underlines the usefulness of comforting positive trends of this type by supporting adequate rural-urban linkages and fostering co-operation in small functional areas, as is pursued by the Regional Centre Programme presented in Section 2.1, but also by the SEUTU project (see Chapter 3), relating to small sub-regions defined around commuting zones.

Although the Finnish periphery municipalities have small population numbers,[37] they cover large territories, and the level of, and the access to, services for people living in the outlying villages is of special interest, both to costs and to challenges of finding adequate models of organising basic services. Delivering public services to all citizens is indeed a challenge in certain regions: average population densities in Lapland are only of two inhabitants per km^2 against a national average of 15 (2003), and outside of the few urban centres, the population is particularly dispersed (see Box 1.1). The features of the municipality of Ranua, typical of Lapland, illustrate well the

Figure 1.19. **Population change by sub-region, 1995-2004**



Source: Ministry of the Interior.

Box 1.1. **Population trends in Lapland**

The region of Lapland (population 186 000) has two urban areas. The municipality of Rovaniemi and its surrounding municipality (population total 56 000) constitutes the first one. The sister municipalities of Tornio and Kemi (population total 45 000) is the second. The remaining population of about 80 000 people live in 18 rural municipalities with an average population of 5 000 inhabitants.

1. From 2002 to 2003, only four of the municipalities in Lapland had population growth, while 18, including Kemi and Rovaniemi, experienced a population decline.[1]
2. At best, population trends over the last 20 years show slow decrease or stagnation as in the case of the six municipalities of the Torne valley.

The main municipality is located on the coast (Tornio, population 22 000) and up the Torne valley there are five smaller municipalities. In the five rural municipalities, there is a slow downward trend but the situation stabilised after 2000. In the city municipality of Tornio there was stable growth in the 1980-1995 period, but since then there has been population decrease and again a stable situation during the last few years. This shows the resilience of people inhabiting sparsely populated places with cold climate and long distances. In the early 1990s a massive out-migration was expected, in the face of an extremely difficult labour market, and a corresponding public finance setback. The demographic development trend however was largely unaffected in the short term by the economic crisis.

- The population forecasts from Statistics Finland indicate that almost all the municipalities in Lapland will have positive birth/death ratios in the years to come, but a projection of migration trends is likely to produce population decrease in all municipalities, except for the "new", enlarged Rovaniemi municipality.[2]

1. Lapland by figures 2004, Regional Council of Lapland.
2. The municipalities of Rovaniemi and Rovaniemi Rural have decided to merge by 2006.

Source: Statistics Finland, Aho *et al.*, 2004.

difficulties of delivering public services in villages and remote settlements. The municipality comprises 4 800 inhabitants (7 000 in 1967) in 23 settlements over a territory of 3 500 km^2.

Notes

1. Lahti, fifth city in Finland (around 100 000 inhabitants) was only created in 1905 as an industrial centre.
2. Finland is the only Scandinavian country in the euro zone.

3. The Functional Urban Region comprises the Helsinki Metropolitan Area (965 000 inhabitants) including the cities of Helsinki (560 000 inhabitants), Espoo (205 000), Vantaa (175 000) and Kauniainen, plus eight other municipalities.
4. Functional Urban Region figures in 2004: Tampere: 316 000; Turku: 290 500; Oulu: 203 000; Jyväskylä 163 500 and Lahti: 157 000. Source: Statistics Finland. Definition of urban regions is based on "Kaupunkiseutujen kasvun aika", Ministry of the Interior, Helsinki 2004.
5. OECD European countries accounted for 60% of total goods exports in 2001, while Russia and the Baltic States represented close to 10% (*OECD Economic Survey of Finland*, 2003).
6. National Board of Customs.
7. Major locations in Helsinki, Espoo, Salo, Oulu, Tampere and Jyväskylä.
8. Twenty-five per cent of market share in 1999, 35% in 2001. Mobile phones account for about three-quarters of its net sales and networks for most of the rest. Nokia represents around one-quarter of total Finnish exports (49% of turnover for European sales, 25% for the Americas and 26% for Asia, with increase of the latter two). From *OECD Economic Survey of Finland*, 2003.
9. Market share for the first quarter of 2004 has fallen from 35 to 30% (OECD, 2004d).
10. Finnish firms employ 20 000 people in China, with Nokia accounting for the majority, Nykänen, 2004 in *OECD Economic Survey of Finland*.
11. Oulu is home to a major ICT cluster in Finland.
12. The regional capital, Oulu, is nonetheless a dynamic hi-tech city (see Chapter 2, Section 3) and efforts are being made to spread its success through regional co-operation.
13. The regression analysis is a statistical technique to test how much of the observed difference in the dependent variable (*i.e.*, productivity) is due to the effect of a set of explanatory variables (*i.e.*, R&D, skills and OECD Regional Typology, see Appendix).
14. For an in-depth analysis, see "Constructing an Index for Regional Competitiveness", Huovari, Kangasharju and Alanen, Pellervo Research institute Working Papers, Helsinki, June 2001.
15. As underlined in a recent report concerning Nordic peripherality: Nordic Peripherality in Europe, Klaus Spiekermann and Hallgeir Aalbu, Nordregio, 2004.
16. *The Lisbon Review*, 2002-2003. An assessment of policies and reforms in Europe.
17. Finnish belongs, like Hungarian, to the Finno-Ougrian family of languages.
18. Although winter tourism is developing in Lapland and Oulu (North Ostrobothnia) is an attractive location for Foreign Direct Investment.
19. UNCTAD WID Country Profile.
20. Invest in Finland 2004. No figures indicating regional distribution in terms of investment amounts were made available.
21. The budget for 2004 is EUR 1.6 million. Recent reports have suggested that an increase of at least EUR 1 million would be necessary.
22. Czechinvest maintains foreign offices in eight countries in three continents and has an EU bureau in Brussels. One of the US offices is located in the Silicon Valley.

23. OECD in figures, Statistics on the member Countries, OECD Observer 2004/ Supplement 1.
24. Ministry of Labour, 2002 and OECD, 2003a.
25. Nordic Statistics and Swedish Tourist Authority, in "Tourism in Sweden in 2004".
26. Border Interview Survey, Statistics Finland/Finnish Tourist Board.
27. UNESCO World Heritage sites number 13 in Sweden, five in Norway, five in Finland and four in Denmark.
28. The 465 659 cottages (secondary housing) in Finland in 2003, visited regularly by 1.7 million Finns and irregularly by another 1 million are a strong base for regular domestic tourism flows benefiting mostly rural areas in Eastern and Central Finland (Lake Area).
29. Regional Council of Lapland and Statistics Finland.
30. A community is defined as rural if its population density is below 150 inhabitants per km^2. A predominantly rural region is one where more than 50% of the population lives in rural communities; a predominantly urban region is one where less than 15% lives in rural communities; an intermediate region is one where the percentage of the population living in rural communities is between 15% and 50%.
31. Districts (*seutukunta*) are a sub-regional unit introduced in 1994 between the municipality and county levels. These units were determined according to travel to work patterns and volumes and also by analysis of cooperation between municipalities.
32. Statistics Finland.
33. See Figure 3.7, in Chapter 3.
34. The proportion of over 65 year-olds is expected to reach a level of 40% in some municipalities by 2030, Rintala and Heikkilä, 2004, p. 167.
35. The municipality of Ranua, visited by the OECD team provides useful insights into issues facing small rural municipalities experiencing ageing and losing population, as developed in Chapter 2, Section 2.4.
36. According to a study by Nivalainen and Volk (2002), cited in Rintala and Heikkilä, the population in these three provinces will be reduced by one-third by 2030.
37. See map, Figure 3.6, which show the territorial spread of municipalities, by four size categories, and Figure 3.5 with ten size categories, showing that there are about 200 municipalities with less than 4 000 inhabitants.

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Chapter 2

Strategies and Policies

Introduction

The evolution of Finnish regional policy is directly related to major macroeconomic changes and EU accession that has cast a new light on leveraging regional assets. Before the 1990s, the investment rate was high in Finland, with the public sector, in particular, contributing to growth. The Regional Development Act that came into force in 1994 was a response to the severe recession that Finland experienced at the beginning of the 1990s, with basic goals seeking to support countrywide restructuring and reform to redress the economy. This Act outlined the development of living conditions and availability of basic services; the expansion of infrastructure for regional development; the renewal of regional production structures with improvement of companies' operating conditions and new job creation; and finally the strengthening of regional economies and skills. Channelling of investment was a tool of regional policy but a progressive change of focus from investment-driven growth to innovation-driven development created the basis for a paradigm policy shift. Investment in expertise and human capital, including adaptation to rapid technological change and emphasis on logistics was preferred to hard investment. Public sector role in the economy tended to decrease while that of the private sector increased (Ministry of the Interior, 2003b).

Efforts to promote balanced territorial development by leveraging the assets of these areas and encouraging local initiative rather than pursuing the subsidy-type approach of the past, dispensed in a top-down fashion, are now being made. Also, introduction of greater coherence by policy linkages is pursued but a "crystal-clear" reading of complex regional development mechanisms and aims remains to be achieved. Many measures are focused on the "hub logic", recognising the validity of enhancing the role of small and medium-sized urban centres playing a key role in the development of local areas and, in the case of bigger urban centres, of a whole region. The "logic of expertise and specialisation" concentrated in these centres, again for the benefit of a wider area, represents a second strong feature of these policies. As will be developed further, Finnish "urban" policy departs from traditional notions of improvement of the living environment or infrastructure development to focus on factors of competitiveness. Innovation policy in the broader sense does not have direct territorial aims but the issue of how significant parts of the territory and population of Finland can benefit from

innovative environments and processes is a question. So is the challenge of delivering public services in many sparsely populated areas, experiencing population decline, due to rising costs, particularly in the light of the ageing phenomenon.

In a sense, the policy challenges facing Finland today and tomorrow evolve around innovation in all policy areas: not only technological but process change, not only innovation in the private sector but also in the public sector and in administration, not only in bigger firms but also in smaller ones, not only in cutting edge hi-tech areas but also in traditional sectors, and lastly, not only in the sphere of the economy but also in that of the social realm. As Finland has proven in the past how to successfully mobilise its energies to develop innovative approaches in many fields, the country undeniably possesses assets from this point of view. Thus, the main challenge is how to leverage and sustain innovative approaches and environments for the benefit of regional development. Policy innovation is itself at the fore. The three themes analysed in this second chapter all have an "innovation lens", either through the policies devised as is the case for urban hubs and networks seen through the angle of competitiveness (Section 3.1), or through mobilisation of intangible assets such as knowledge, precisely in innovation-led policies (Section 3.2) and lastly in the public sector, to pick-up the challenges of areas with declining population (Section 3.3). These policy areas are cornerstones of the Finnish regional development framework presented below.

2.1. Finnish regional policy today

Less than ten years after the recession shock, a remarkable recovery and EU membership created a new setting for Finnish regional policy. The Regional Development Act of 2002, in force since January 2003, focuses on the three following main targets:

- To strengthen the competitiveness of the regions.
- To safeguard service structures throughout the country.
- To develop a balanced regional structure.

Although more focused, the present Act raises a major issue: how can competitiveness be improved by sustaining growth poles, while attending to the needs of less-favoured areas experiencing out-migration and loss of vitality? Tighter budgets and the phenomenon of ageing, which is particularly marked in Finland as compared to other OECD member countries (see Chapter 1) require well-identified priorities, particularly in view of the foreseeable reduction in EU funds resulting from enlargement. The broad assumption is that regional development will support the growth of the national economy and in turn that this is reflected throughout the country. The strengthening of regional expertise, entrepreneurship and employment is expected to boost

growth and create the potential for maintaining the basic features of the welfare society. This brings up a second issue: how to control basic infrastructure and welfare costs and still offer a good level of services while allocating sufficient resources to economic development goals? Support to regional government and sub-regional co-operation is explicitly stated as a way to help achieve the aims of regional development and to help in limiting expenses in the delivery of public services.

The programme for regional policy is very innovative but it remains a complex tool to manage because of its multi-faceted aspects and the wide sharing of responsibilities between different actors. The Ministry of the Interior, in co-operation with other ministries and the regional councils (see Chapter 3), is responsible for the formulation of national targets for regional development. In addition, the Ministry of the Interior is responsible for co-ordinating, monitoring and evaluating the preparation and implementation of regional strategic programmes and other programmes in accordance with the Regional Development Act. The Government decides on regional development targets (see Box 2.1) for a fixed term (current period 2004-2007). State authorities are required to take account of regional development targets set by the Government in their operations, and promote their achievement (detail about the actors involved and co-ordination is provided in Chapter 3).

The Regional Development Act (602/2002) adopted by Parliament requires Government to draw up a Decision guiding and harmonising regional strategic programmes and development targets and measures across the administration and levels of governance (SEUTU and Kainuu projects). The Government can also decide on fixed-term special programmes drawn up in order to complement the Regional Programme. These different programmes are presented in Figure 2.1. Recent Government Decisions mostly concern the continuation of existing programmes such as the Centre of Expertise Programme, the Regional Centre Programme (to sustain small and medium-sized cities and foster inter-municipal co-operation), the Rural Policy Programme, and the Island Development Programme. More recently a Programme on "sub-regionalisation of business services" was launched under the responsibility of the Ministry of Trade and Industry to establish a network of at least 50 regional business service points.

As an integral part of regional policy, ten key ministries[1] must now define their regional development plans, as Figure 2.1 also shows. The Ministry of Education was the first to compete its own plan at the beginning of 2004. This strategy defines and strengthens the role of Higher Education Institutions (Universities and Polytechnics) in regional programmes. The Ministry of Agriculture and Forestry emphasises urban-rural linkages and rural hubs qualified as "competence centres", in line with the Regional Centre Programme (see Section 3.1) deployed by the Ministry of the Interior. The Ministry of the

Box 2.1. **Regional Development Targets**

The nine Regional Development Targets adopted by the Government in January 2004 are:

Improving of competitiveness of regions in the global market by strengthening specialisation and promoting the Information Society. This relates to regional innovation policy and, more specifically, to the Centre of Expertise Programme.

Promoting of industrial development and entrepreneurship, with specific reference to the operating environment of companies.

Enhancing employment and reducing regional unemployment disparities in particular by improving the functioning of regional labour markets.

Providing better accessibility through adequate transport connections and fast, affordable ICT infrastructure and services.

Maintaining and improving the living environment and natural surroundings.

Safeguarding the availability and quality of basic services throughout the country, in particular by sustainable funding of services, implying support to supra-municipal and regional co-operation as well as to reforms in service structures and production methods.

Developing a polycentric regional structure based on a competitive Helsinki Metropolitan Area and a network of regional centres.

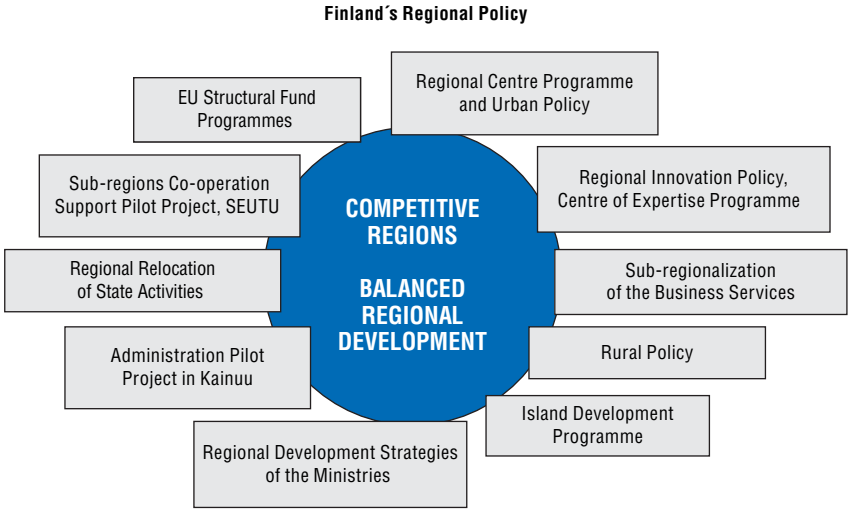
Mobilising sufficient financial resources for regional development programmes, with regional council's role to be strengthened in co-ordination of regional actions and allocation of resources.

Regionalising in the long run certain central government functions, with location of units and jobs (in particular vacated through retirement) outside of the Helsinki Metropolitan Area, primarily in regional centres.

Source: Based on information provided by the Ministry of the Interior.

Environment focuses on communities' attractiveness. The Ministry of Labour's strategy is focused on the TE Centres servicing individuals and businesses (Chapter 3). The Ministry of Trade and Industry is attentive to regional competitiveness: in particular, competences and enterprise financing. The Ministry of Transport and Communications will focus on the ICT infrastructure framework with implementation largely the responsibility of local government (regions, joint municipal boards and public-private partnerships) and on Information Society policy, aside from traditional missions (roads, increasingly a regional prerogative).

Figure 2.1. **Regional Development Programmes**



Source: Ministry of the Interior, 2004.

At the sub-national level, regional development policies are managed by the regional councils under the Regional Development Act. Each regional council draws up a "Regional Plan" (long-term strategic vision) referring to the regional development targets decided at the national level. "Regional Strategic Programmes", debated with the main public and private regional actors and also discussed with the national level to ensure overall coherence, are decided by the different regional councils. The "Annual Implementation Plans" detail financing from committed sources (EU, national, municipalities, and private sector), taking into account the regional development programmes defined at the national level.[2] Each actor, at different levels of government can thus express views, with the regional council actively co-ordinating the preparation and elaboration of the strategic documents that it is to adopt, thus defining its regional development goals, measures and means of implementation. This responsibility extends to land use as the regional land-use plan,[3] up-dated every fourth year, follows guidelines defined in the regional plan. The Lapland Regional Development Programme for 2004-2006 (Box 2.2) highlights the regional council's role in use of EU structural funds emphasising in this case, with Interreg, the northern dimension.

The Ministry of the Interior permanently assumes a role of monitoring trends and bringing forward strategic issues that can impact the outcome of

Box 2.2. **Lapland Regional Programme, 2004-2006**

The Lapland Regional Programme refers to the Regional Plan Lapland 2020 defining a vision for the development of the region: in particular, development of sustainable tourism, adequate management and utilisation of northern conditions and natural resources and basic modern industries. The regional programme is financed through national regional programmes such as the Centres of Expertise (Experience Tourism) and the Regional Centre Programme as well as funding from the regional allocations of sector ministries. EU funding is from the Objective 1 and Interreg IIIA programmes. Objective 1 comprises three priorities:

- Promotion of growth and development of existing companies and creation of new firms.
- Continuation of basic production in rural areas, diversifying the rural livelihood base.
- Support to expertise and employment: training and support in management in particular.

EU funding represents EUR 165.8 million between 2000 and 2006 (32.3%), out of a total of EUR 513 million, with the State contributing EUR 140.2 million (27.3%), the private sector EUR 181.4 million (35.4%) and municipalities EUR 25.6 million (5.0%). Interreg A North aims to increase cross-border co-operation with Sweden, Norway and Russia. It comprises three sub-programmes (total budget between 2000 and 2006 is over EUR 129 million):

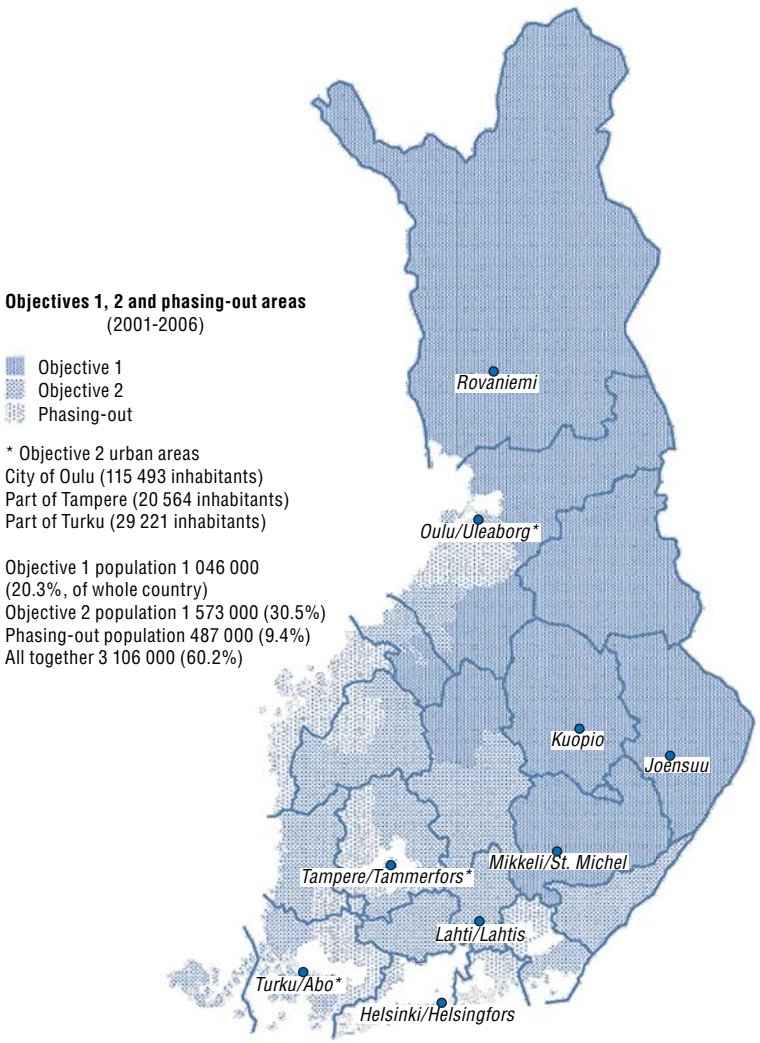
- North Calotte supporting joint projects in the area between the Scandinavian countries concerned.
- Kolarctic promotes co-operation between North-West Russia and the North Calotte.
- The Sapmi project supports the unity of the Sami people in the programme region.

Source: Based on information provided by the Regional Council of Lapland.

regional development policies. This on-going process of strategic thinking seeks adjustment to the evolving challenges of globalisation and innovation, EU enlargement and phasing out of structural funds or ageing. The Report of the Regional Development Strategy Working Group, "Finland's Regional Development Strategy 2013", released by the Ministry of the Interior in 2003 reflects these concerns in tackling questions that will require in the future specific attention. Many of these matters, dealt with in the present Territorial Review of Finland, are overarching in terms of national policy but have a strong bearing on regional policy. Such is the case of what the report calls a

"business gap" in Finland: the low number of start-up companies and micro-enterprises. Another case in point is how technological expertise can be applied to other sectors than new growth industries. It states in particular that "more research on technology and the introduction and application of innovations in traditional sectors (including social and organisational innovations) is needed in Finland". These analyses apply directly to the Objective 1 areas of Finland (see map, Figure 2.2) that concern only about 20% of the population but

Figure 2.2. **EU Structural Funds**



Source: Ministry of the Interior.

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around two-thirds of the territory of the country. These regions, mostly in Northern and Eastern Finland present common features in terms of low density, ageing, and out-migration.

2.2. Policies for urban competitiveness

Towards a national policy for urban areas

Until recently, Finland did not have an explicit urban policy. In the context of strong municipal autonomy, the central government's role was confined to traditional regional development policy in favour of less developed and populated areas. When cities received support, they were small and medium-sized, located mainly in rural areas. Even if Finland remains one of the OECD's most rural countries, conditions have changed however. The urbanisation process is accelerating, with people moving mainly from small urban communities to larger ones, thus raising new employment, social and infrastructure issues. The deep economic recession of the beginning of the 1990s has particularly stressed these problems. Moreover, with the acceleration of globalisation and Finland's integration into the European Union, enhancing cities competitiveness has been recognised as a national objective in a report by the national *ad hoc* Committee on Urban Policy, appropriately titled "Cities as Generators of Growth" (Ministry of the Interior, 1996).

It is in this context that the central government readapted its regional development policy approach and launched an explicit urban development policy. It should be noted that urban policy in Finland differs from the urban policies followed in most OECD countries, where focus is usually on support to distressed urban areas resulting either from de-industrialisation or suburban block-housing where the percentage of foreign immigrants and unemployed tend to be much higher than the national average. Urban policy thus often equates with concerns of social cohesion, neighbourhood renewal and improved infrastructure. In Finland, the polycentric urban pattern, the low percentage of foreign immigrants and an effective consensus based on the principles of the Welfare State and equal access for all to basic health and education services have prevented the development of urban distress or decay that is witnessed in many other countries. This does not mean that this phenomenon is non-existent in Finland. Many former industrial cities have experienced the difficulties of restructuring and in certain parts of the Helsinki Metropolitan Area there is a higher concentration of foreign immigrants. Nonetheless, these situations are dealt with in the context of either industrial policy (support to innovation) or social policy (effective access to public services, new housing). Policies relating to urban areas in Finland are thus fully geared towards enhancing cities competitiveness and maintaining a balanced urban network

of cities of different sizes, but recent trends might require specific attention to service production and social issues.

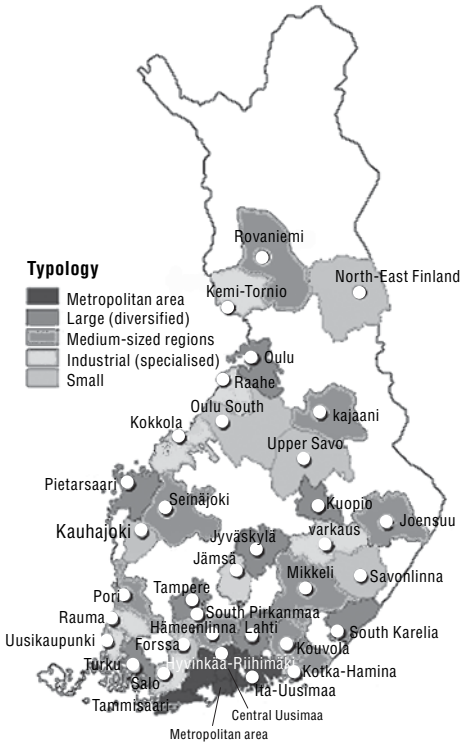
The premise of the national urban policy started with the creation of the *Centres of Expertise* (CoE) Programme in 1994, first applied in the eight largest urban regions. The CoE aims to encourage innovation and specialisation within the broader goal of enhanced competitiveness. It was then followed by an *Urban Programme* policy during the period 1997-2000 that sought mainly to promoting co-operation for economic development within urban regions. The assessment of the first *Urban Program* was mitigated but it acted as a catalyst for further actions.[4] Since 2000, national urban policy has gained a new momentum. On the one hand, following the recommendation of the Second Permanent National Committee on Urban Policy, the Finnish government launched the *Regional Centres Programmes* (RCP), a more comprehensive urban policy aimed at developing cities of different sizes into strong regional and local centres, whilst maintaining the existing CoE programme. On the other hand, a metropolitan-level development policy was set up for large cities with a specific approach for the Helsinki metropolitan region that was excluded from the RCP.

Several features characterise this new urban approach. First, it establishes a typology of cities so as to assign different policy objectives. The national urban network of Finland was analysed in the *Urban Network Study 1998* initiated by a first permanent national Committee for Urban Policy, later updated in the *Urban Network Study 2001*. This document was used in the conception of the RCP, differentiating urban policy according to five different types (see Figure 2.3) of urban regions: *i)* metropolitan area; *ii)* large diversified regions; *iii)* medium-sized urban regions; *iv)* industrial (one-sided) urban regions; *v)* small (primary production oriented) urban regions. In parallel, a special policy package for major urban regions was set up to adapt the existing CoE and RCP programmes to the special needs and potential of large urban regions.[5] Second, urban policy is considered an integral part of regional policy as the RCP aims to create a network of attractive medium-sized cities (polycentric urban structure) supporting the development of surrounding rural areas. Third, the principle objective in Finland is to foster economic competitiveness by supporting specialisation of urban regions and fully integrating them in the national innovation system.

Developing urban hubs by promoting innovation

Three main rationales have driven Finnish urban policy: *i)* cities as nodal points for the creation of new jobs and the spread of economic growth; *ii)* promotion of innovation to enhance cities competitiveness; and *iii)* sustaining a large network of cities, including small and medium-sized, to ensure balanced territorial development. The main instruments to reach these

Figure 2.3. **Regional Centre Programme Typology**



Source: Ministry of the Interior.

objectives are the *Centres of Expertise* (CoE) programme launched in 1994 and *the Regional Centre Programme* (RCP) introduced in 2001.

The CoE programme represents one of the main tools of Finnish regional innovation policy. The objective is to increase co-operation between universities and enterprises, develop top-level expertise, attract investments and talents to the region and improve regions' ability to raise R&D funding. The programme is implemented by local development companies based on the *Triple Helix model*, *i.e.*, partnership between *i)* universities and related institutions (research institutes); *ii)* the local business community (companies and science parks); and *iii)* public authorities (municipalities, regional councils, national government). The responsibility for the management of the Centres of Expertise is often assumed by the local science and technology park company.

The CoE programme administered by the Ministry of the Interior functions efficiently as a programme crossing administrative boundaries. It is based on competition so that only the best local programmes have been awarded the

centre of expertise status. These also have to compete for basic state funds annually. In 2003, the ministry's basic funds for the programme amounted to EUR 8 million and EUR 9.5 million in 2004. These funds are matching grants, as local actors, mainly cities, are also required to invest in the programme an equal amount of funding (so called 50/50 principle). In 2003, the total funding of the CoE projects was of EUR 40 million including various sources such as the EU (European Social Fund), private companies and national innovation organisations.

The CoE, aiming to develop and consolidate international top-level knowledge within firms in particular by fostering connections with academia and research (see following section), is widely considered as a success story (Ministry of the Interior, 2003). A 2003 mid-term evaluation of the programme reported that modest public funding has successfully mobilised private resources in most cities involved. In 1998 and 2002, the national government decided to extend it to new regions so that by the end of 2006, there should be around 22 Centres of Expertise operating in 45 branches. The programme, that initially targeted large urban areas, is thus progressively being extended to medium-sized city regions in coherence with the national objective to ensure a polycentric urban structure.

The principal objective of the *Regional Centre Programme* (2000-2006) is to ensure balanced territorial development by establishing cities of different sizes as strong regional or local centres, with the aim of boosting the competitiveness of the regions concerned. The programme also specifically stresses the development of *sub-regional co-operation* by bringing together in a joint network, municipalities, universities, research units and enterprises. On the basis of an agreement between municipalities, responsibility for the programme lies with the urban centres or the joint regional organisation of the municipalities, such as regional business development companies. The assumption is that urban regions are considered as functional entities for the development of which the core city and the surrounding municipalities must cooperate closely.

The 34 cities[6] that qualified for the RCP belong to the different categories identified in the typology of the *Urban Network Study* with the exception of urban regions in Uusimaa, which originally were excluded from the programme. They represent a total of 264 municipalities, *i.e.,* 3/5 of total Finnish municipalities and 63% of total population. Ministry of the Interior funding for the programme amounted to EUR 10 million per year in 2001-2003, whilst the total expense amounts to EUR 20 million per year (2004-2006). In terms of policy actions, the main emphasis of the RCP is on competence and development driven by technology innovation within the functional regional centre area as shown in the example presented in Box 2.3. Quality of the environment and culture are also focused as competitiveness factors.

Box 2.3. **Joensuu Regional Centre Programme**

Joensuu (population 53 000) is the main city of the region of North Karelia bordering with Russia. The Joensuu Region is a sub-region within North Karelia, comprising eight municipalities with a total population of 106 000 inhabitants.

The RCP programme for Joensuu Region is operated by JOSEK Ltd., incorporated in 2001 as a public company formed by the municipalities with operative responsibility for determining the economic policy of the small region, providing corporate counselling to its members, company development services and marketing the area for investors. Two additional municipalities from a neighbouring sub-region are affiliated members of the company (Ilomantsi and Tuupovara, respectively close to 7 000 and 2 200 inhabitants) but the RCP it manages extends also to two other sub regions (Keski-Karjala, Pielisen-Karjala Regions).

The RCP promotes use of the knowledge stemming from the North Karelia Centre of Expertise specialised on the one hand in wood technology and forestry and in plastics and tooling on the other. In doing so it works closely with the Joensuu Science Park focusing on these areas of competence but also on ICTs, welfare technologies and services, particularly for "independent living" (elderly people). Know-how in this last area is based in the "Development Centre for Devices for Independent Living".

RCP objectives for 2004-2006 are to continue to strengthen the expertise in these areas, to support development of businesses targeting the Russian market and the Baltic countries, in particular by establishing a business centre office in Saint Petersburg. Tourism is another priority area (North Karelia is the pristine major setting and place of origin of the Kalevala epic legend that helped to forge Finnish identity and culture in the 19th century). The strategy puts emphasis on quality control of tourism services. Development of regional (public) services is the last axis.

Total RCP expenditure for 2004 is EUR 1 108 000 fairly divided between the sectors and activities mentioned above. Funding is provided by the Ministry of the Interior for 46% and the remaining 54% mainly by the Joensuu Region and also associated regions (Keski-Karjala, Pielisen-Karjala Region, except one municipality and Ilomantsi-Tuupovaara Region).

Source: Based on information provided by the Region of North Karelia.

Like the CoE programme, the RCP is co-ordinated by the Ministry of the Interior in co-operation with other ministries, the programme areas, the Regional Councils and State regional authorities. A main difference with the CoE is that its implementation, also based on the Triple Helix Model, rests

more outside the business sector. Nonetheless, the RCP has a role in regional innovation systems, particularly in those not featuring a Centre of Expertise. In 2004, a mid-term evaluation of the RCP, published by *NetEffect Ltd*, pointed out that the programme has been successful in encouraging partners within urban regions to co-operate to improve the competitiveness of the region (Ministry of the Interior, 2004). Meanwhile, the evaluators reported significant problems concerning involvement of the ministries in programme implementation. They also expressed concerns as to what extent the programme has benefited to small surrounding municipalities and noted that links to enterprises could be stronger.

A specific approach for large cities and the Helsinki metropolitan region

Whilst the Finnish approach to urban policy is clearly based on ensuring a polycentric urban structure, the role of large cities in the national economy has also been duly recognised. As indicated above, about half of Finland's population lives in eight major city regions. A particular emphasis has been put on the Helsinki metropolitan region. The background report ordered by the Working Group on Urban Policy (Pikkarainen, 1996) states that "the role of Helsinki, as Finland's only international knowledge-intensive major city area needs to be promoted for the simple reason that it competes more with major cities in other countries than with urban regions in Finland". It remains however difficult to assess the extent of national government involvement. Uusimaa was excluded from the RCP since the beginning and funds allocated to the Urban Policy Programmes for the Helsinki Region from 2002 and to Central Uusimaa, Lohja and Tammisaari urban regions since 2004 have been rather modest. On the other hand, since most of the leading high-tech and knowledge-based industries and talents are concentrated in the Helsinki metropolitan region, much of the innovation policy funds end up there.

The role of the City of Helsinki as a pole of growth contributing to the development of other areas in Finland[7] is well recognised but recent evolutions in overall financial flows could somewhat modify this perception, so a clarification is necessary. In 2003 and 2004, net state grants (earmarked, minus equalisation) in favour of Helsinki show a positive instead of a negative value, which was the case during the three previous years.[8] Helsinki is now a net grant receiver instead of a net contributor to the rest of the country. Nonetheless, referring only to the equalisation component of these financial flows, the City of Helsinki effectively remains a net contributor to other parts of the country, for a total amount of EUR 308 million in 2004. The overall shift is probably due to changes in the allocation of corporate tax revenues which is now more favourable than in the recent past to municipalities with numerous firms. It remains to be seen if this change will be confirmed in the future, meaning that the city of Helsinki is now suffering from some negative

agglomeration effects in terms of public service costs. On the basis of the Helsinki Metropolitan Area (four municipalities) the overall fiscal contribution to the rest of the country is however in line with past trends, even if there is only one single net contributor,[9] namely Espoo. These last changes plead in favour of reinforcing co-operation at this level rather than dealing with these City of Helsinki issues in the wider national perspective, as is the case for municipalities that are net receivers.

For the past two years the national government has been concentrating on improving the governance framework of the Helsinki metropolitan region. As pointed out in the *OECD Territorial Review of Helsinki* (2003), lack of co-operation between municipalities where interdependence of problems – from immigration to economic development and housing – is on the rise, threatens the competitiveness of the whole metropolitan region (Box 2.4). A major challenge is to intensify inter-municipal co-operation in an operating area that reaches beyond the Helsinki Metropolitan Area Council area consisting of Helsinki, Espoo, Vantaa and Kauniainen.[10] Several fields for co-operation within the Helsinki region have been identified including planning and land use, housing, transport, and to a lesser extent, economic development, education and culture. A specific problem to be addressed is the housing shortage in the Helsinki region due to in-migration but also to the fact there could be a disincentive for municipalities to develop new construction, as additional population would entail pressure on budget allocations for basic public service delivery.

In 2003, an *Advisory Commission on the Helsinki Region* chaired by the Minister in charge of regional development was established including representatives of several ministries, the mayors of the four core municipalities and regional council members of Uusimaa and Itä-Uusimaa. A proposal for legislation has been prepared[11] and is still publicly debated at the beginning of 2005 bringing new dynamics to collaboration within the Helsinki Region. The positive dialogue based on this proposal concerns municipalities of the Helsinki Metropolitan Area (Advisory Committee of Helsinki Metropolitan Area), Central Uusimaa as well as a few other fringe municipalities. The core contents of a proposed agreement for cooperation prepared by 14 municipalities would cover housing, land-use and transportation. Co-operation would be voluntary, progressive and based on partnership principles. As a concrete first step, municipalities would prepare a common land-use strategy. A wide consensus has been reached between municipalities, meaning that if this model brings results, no legislation might actually be enacted.

The "Helsinki Club" has also been particularly active regarding elaboration of common strategies and devices to implement appropriate mechanisms answering metropolitan governance challenges. This informal think tank groups high-level representatives from business, science, media, cultural life,

church and public administration discussing future challenges of the Helsinki region and defining strategic priorities and key projects. The proposals provide impetus for political decision makers.[12] The Club provided recommendations for the Innovation Strategy of the Helsinki Region, handled by Culminatum Ltd., the Helsinki Centre of Expertise.

From a policy perspective, financial involvement from the central government has been rather limited. As a large metropolitan region, Helsinki benefited to some extent from traditional urban policy aimed at responding to new challenges raised by rapid population growth and declining neighbourhoods, (housing shortage, unemployment, social exclusion and immigration). The main financing source has been the EU Urban initiative, implemented in the cities of Helsinki and Vantaa.[13] Urban II concerns 45 000 people with a total public financing of EUR 20 million for the 2000-2006 period. According to a mid-term evaluation of the Urban II Programme (Helsinki Urban Facts, 2004), some targets (such as employment, gender equality or multiculturalism) have not been emphasised strongly enough in implementation. Meanwhile, the relevance of the programme can be seen in increasing participation and clear aims for promoting the attractiveness of the area. Cities in the Helsinki region also benefited from other similar programmes such as the *Suburban Programme* (1995-1999) and the Suburban renewal 2000 Programme (2000-2004), cross sectoral ministries programmes managed by the State Housing Fund.

Besides this traditional urban policy, which remains quite sector oriented, a new explicit and more comprehensive urban policy targeted at the Helsinki region has been established, entitled the *Urban Policy Programme*. Following the decision to exclude Helsinki from the RCP, the mayors of the four central municipalities decided to draw up an initiative for a common urban policy along with the participation of the business community, universities and civic organisations which identified international competitiveness and social cohesion as main priorities. This initiative was concretised in 2002 under the title "A competent and cohesive city – urban policy programme for Helsinki metropolitan area 2002-2004". The programme includes 18 pilot projects to be implemented through a partnership involving cities, government authorities and the third sector. Ministry of the Interior funding amounted to EUR 1 million for 2002-2004 which, although it acts as a catalyst for local funding, remains a pretty modest contribution.

In January 2005, the central government launched the preparation of a "Policy Package for Major Urban Areas" concerning the nine major cities in Finland (Helsinki, Tampere, Turku, Oulu, Jyväskylä, Kuopio, Lahti, Lappeenranta-Imatra and Vaasa).[14] This initiative fully recognises the crucial contribution of large cities to the Finnish economy. The main objectives are to increase major cities' international visibility and competitiveness and improve their

Box 2.4. **The need to rethink metropolitan governance in Helsinki**

Greater Helsinki is well known for having developed a competitive cluster in ICT. The specialisation of the Finnish ICT cluster has been favourable for growth, contributing to significant agglomeration economies and territorial capital, while enabling the key locations to become more competitive and thereby attracting more firms. However, this specialisation has introduced considerable vulnerability, as it is dependent on a single sector rather than several sectors. Although size is far from being an obvious factor of economic success, Helsinki with its 560 000 inhabitants is commonly perceived as an intermediate urban centre in European or international comparison. It fears marginalisation on the North East corner of the EU and wants to address competition from the region of Öresund, or Stockholm. A well-managed and better co-ordinated GHR of more than 1.5 million could be a response to the question of size within the so-called competition between urban regions. Despite the perceived advantages of scale to marketing the GHR, municipalities continue to compete among themselves to attract FDI. This reflects the relative weakness of co-ordinated regional marketing in contrast to the vigorous competition between municipalities, classically between Espoo (which was very successful) and Helsinki, but with Vantaa increasingly involved in the game.

In order to organise and sustain growth, the Helsinki region needs financial support to make major investments in terms of infrastructure and housing. Also, uncontrolled, dispersed urban sprawl requires co-operation between planning authorities (regional councils and municipalities) within the GHR in a context of long established autonomy of municipalities that may prevent it.

The success that the region has enjoyed and the absence of any imminent crises provides little incentive for prospective thinking on the ability of the current system to sustain advantages indefinitely. Projected social outcomes based on the emerging socio-economic differences are not desirable, as the city of Helsinki would end up with a disproportionately large share of the region's poor and needy households. Although the trends are not yet dramatic, they are clear enough to cause concern given the large role that local governments play in providing social services. Immigrants dependent on social support and other allowances would tend to be concentrated, with attendant social problems in the city, Espoo and Kauniainen and some other parts of the region would become progressively wealthier and more entrenched enclaves for the affluent.

Source: OECD Territorial Review, Helsinki, 2003.

individual specialisation for a better division of labour throughout the country. The link with the Regional Centre Programme concerning small and medium-sized cities is that further development in main urban areas will benefit the whole region, including its other urban centres. In that sense, this approach integrates both aspects of urban and regional policies. This package also constitutes an attempt to ensure better co-ordination of existing programmes and policies, with the objective of integrating the multi-faceted aspects of urban development (economic and innovation policies, social, housing and integration policies, infrastructure and environment policies). This is an ambitious objective which remains to be translated into an appropriate framework. As the Ministry of the Interior's policy memorandum rightly puts it "these measures still require collaboration between different ministries".

Preliminary assessment of the first urban policy

Whilst Finnish urban policy is still in its early stages, some initial results can be identified. First, by introducing a clear differentiation among city types, the Finnish approach towards urban areas strives to take into account local factors, avoiding a "one-size fits all" model. Second, it relies on mechanisms of conditional grants through transfer programs such as the RCP to promote inter-municipal collaboration. Programmes such as the RCP, the CoE and the Urban Policy Programmes in Uusimaa have also helped to increase co-operation between different levels of government, universities and the private sector. The active and leading participation of non governmental partners such as universities, research centres and the business community might even be quoted as a best practice amongst OECD countries. Third, sustaining regional competitiveness is the main objective of an urban policy based on innovation and drawing in particular on the research and knowledge potential of universities. Finally, while pursuing the objective of a balanced urban network, efforts are made to sustain and improve the competitiveness of the metropolitan region of Helsinki, growth engine for the national economy. However, a certain number of issues should be raised.

Most programmes, including the most important one, the RCP, target cities of different sizes, including in rural regions. The CoE, which was first targeted at large urban regions, is also now being extended to smaller cities. This can be explained by the Finnish urban structure which features many small and medium-sized urban centres. In this respect, current urban policy appears more as a broad regional development policy. Moreover, despite interest for the Helsinki region and other large cities, urban policy remains largely favourable to small and medium-sized cities. It is maybe too early to assess whether the recently introduced "Policy Package for Major Urban Areas" will provide more funding for the nine cities concerned. Mayors of large cities also complain about the fiscal system which seems to have been

unfavourable to them in the recent period (see Chapter 3). The issue here is, based on the assertion that large urban regions are essential to national economic growth, to what extent sustaining less competitive small urban areas will be detrimental to larger more performing areas. By involving a large number of municipalities around a core city, the RCP assumes that development of localities is not a zero-sum game.

Despite efforts vying a holistic approach, the different policy actions remain, up to a certain extent, sector-oriented. What is still missing is integrating multiple actions and programmes in a better defined policy framework, to avoid duplications and favour a more integrated approach. A case in point is housing. Housing shortages, integration of immigrants and other social issues may become major future challenges, especially in the biggest cities. For the moment, policies in these areas seem to be treated separately from the competitiveness-based urban policy. Metro-wide economic growth depends not only on economic interdependencies but also on social cohesion and the physical environment. Urban policy initiatives in many OECD countries have emphasised the need to bring together economic, social and environmental issues in a single strategy combining central and regional sources of funding and expertise.

Efforts have been made to improve horizontal co-operation at the central government level. As a cross-sectoral issue, urban development requires an appropriate framework for inter-ministerial co-operation. The Ministry of the Interior is responsible for the co-ordination of urban policy, with the Minister of Regional and Municipal Affairs[15] playing an important role. The latter has set up an *Inter-ministerial Monitoring Group on Regional Development Measures* to follow up the implementation of national regional development targets, including urban issues. An *Advisory Committee for Major Urban Regions* has been established by the Ministry of the Interior whilst the Minister of Regional and Municipal Affairs is heading an *Advisory Committee for the Helsinki Sub-Region*.

Urban policy targets different objectives that might be difficult to reach at the same time. Based on the limited amounts of funding for regional and urban policy, it will be difficult to ensure balanced territorial development by seeking to sustain the competitiveness of a large number of small and medium-sized cities, including those which experience high levels of unemployment or migratory outflows. The question for the RCP is whether the selection process has not been too large.[16] Also, the financial commitment from the national government dedicated to the programmes included in urban policy remains quite modest. In the context of strong local autonomy, this is coherent with the objective of the national government to remain essentially a catalyst promoting certain policy objectives and encouraging different forms of co-operation. It is thus important to limit national actions to

a number of coherent and realistic objectives, while ensuring the complementarities and synergies between programmes.

A main objective of the RCP is to promote co-operation between core cities and peripheral municipalities. However, projects may tend to benefit a limited number of municipalities, most often the core centres. The assumption is that economic development will finally spread and benefit the surrounding communities of urban regions. The question is to what extent this will effectively happen. It can be objected that the interest of the core city and the rest of the region could diverge. This issue is raised in certain countries like the United Kingdom, now assessing the validity of the city-region concept. It would be useful to provide evidence concerning such positive territorial spill-overs so as to enlist support for this policy. Finally, it should be noted that the large size of RCP areas, more extended than strictly functional ones might create extra friction between localities (Laakso, *et al.* (2004)).

2.3. Innovation-led policies

The National Innovation System

The international success of Finland is widely attributed to the sophistication of its "triple helix" interaction model of government, industry and universities. The Finnish "National System of Innovation", sponsored principally by the Ministry of Trade and Industry and the Ministry of Education, is overseen by the Science and Technology Policy Council chaired by the Prime Minister. In a formal sense, the Centre of Expertise and the Regional Centre programmes, analysed in the preceding section, sponsored by the Ministry of the Interior, and the network of science parks, usually owned and initiated by municipalities, do not seem to be presented on an equal footing with other measures and appear to lie at the periphery of this "innovation matrix". Although they can be mentioned in certain organisational maps (see Figure 2.4), full integration into overall innovation policies and strategies has yet to be achieved. How the "top down" national system interacts with "bottom-up" initiatives having the specific objective of promoting local and regional innovation environments is a key question. Can a regional dimension to the triple helix be defined that contributes simultaneously to national performance and aspirations for regional development?

Finland leads the way amongst OECD countries in transforming its policy to support science and technology delivered through universities, government research establishments and support for private sector R&D into what is defined as a "national innovation system". It was the first OECD country to embrace academic ideas about the optimal pattern of investment in R&D to maximise economic benefits in terms of innovative performance by strong networking of key actors and agencies (the link between inputs and outputs)

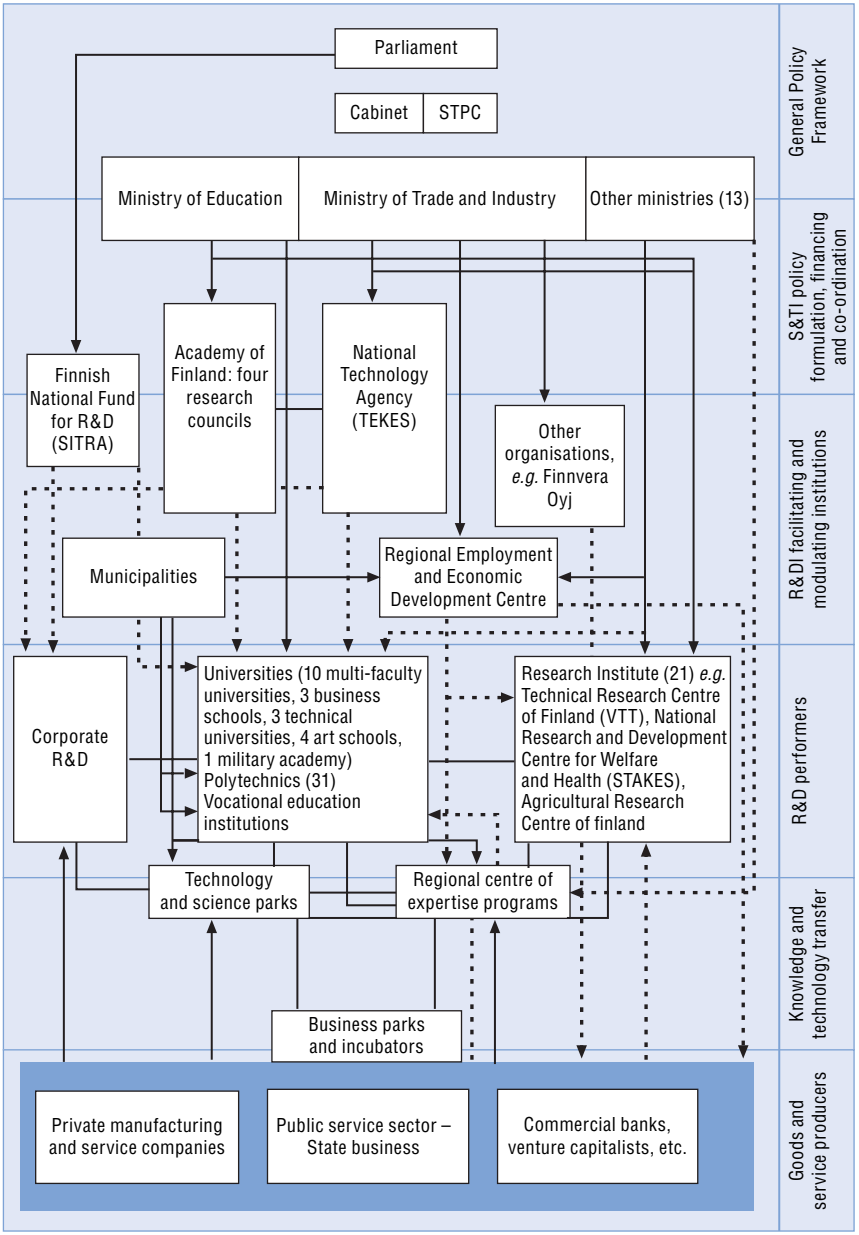
(Georghiou L. *et al*. (2003)). Prior to the 1980s Finland had a traditional approach of separate support for universities, companies and government R&D. In 1983 a new approach was the establishment of the antecedents of the current National Technology Agency (Tekes), followed by the transformation of the Science Policy Council into the Science and Technology Policy Council in 1986. It drove foreword a multifaceted networked innovation system embracing a wide range of domains including regional policy (Nieminen, M. and Kaukonen, E. (2001)).

The current structure of the innovation system is described in Figure 2.4. The diagram highlights the direct lines of policy steerage and indirect influences on and by key stakeholders. Within regions there are autonomous actors in the form of municipalities with their support for technology centres and science parks (generally housing the Centre of Expertise) and also Regional Employment and Economic Development Centres (TE Centres) sponsored by central government, embracing in particular the regional arms of Tekes and the Ministry of Labour. In addition, universities and polytechnics, with strong links to municipalities, are also major stakeholders in cities across Finland.

In face of the recession of the early 1990s, Finland dramatically increased its share of GDP devoted to R&D. While government expenditure on R&D as a percentage of GDP declined or remained steady in most OECD countries, Finland increased public investment through the 1990s. Nevertheless the publicly financed percentage of business expenditure on R&D remained below other OECD countries, reflecting strength of private investment by a few companies, mostly Nokia. The scale of resources deployed under each policy domain and share of private investment are indicated in Figure 2.5. Overlapping spheres reflect the complexity of the system moving away from a classical linear innovation model. Significantly, the diagram, produced by the Ministry of Trade and Industry, does not embrace the EUR 20 million of the Centre of Expertise programme.

Although Figures 2.4 and 2.5 depict a unified innovation system, in practice it is possible to consider two distinctive pillars, one based around universities and the other around a wide range of public/private intermediaries supporting near market activities. In response to the crisis of the early 1990s public funding of university research gradually shifted from block allocations to a competitive mode of funding for basic and applied research. Funding for the former is now awarded by the Academy of Finland on competitive bidding and peer review. Likewise, applied research, chiefly funded via Tekes, is competitive, strongly steered and based upon networking between universities and industry. Thus, during the 1990s, core funding of universities increased by only 18% but there was a 105% increase in external funding (Nieminen, M. and Kaukonen, E. (2001)). Significantly, most of this funding is based on marginal cost, with core funding linked to teaching via

Figure 2.4. **A policy-central organisational map of the Finnish system of innovation**



Source: M. Nieminen and E. Kaukonen, "Universities and R&D Networking in a Knowledge-Based Economy", SITRA, Reports Series, 11, 2001.

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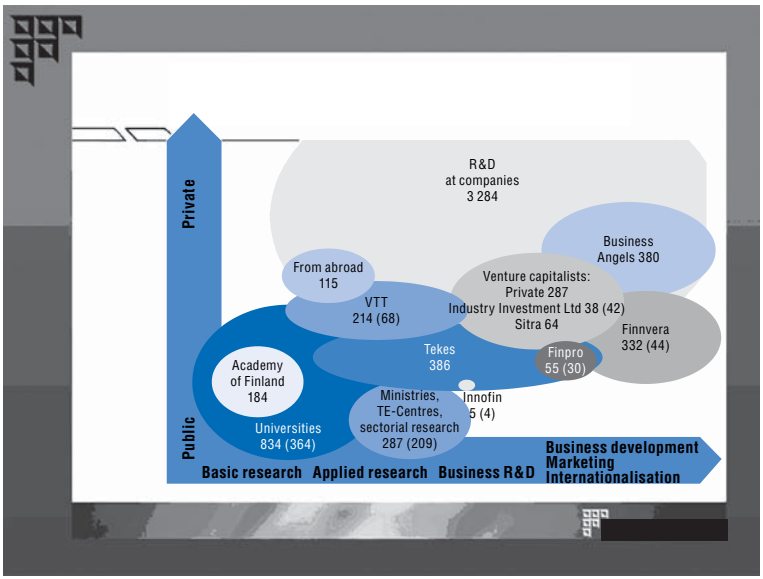
Figure 2.5. **Innovation system resources and funding, 2001**



Note: Numbers indicating total resources of the organisation and funding of the organisation from the state budget (in brackets).

Source: Ministry of Trade and Industry.

graduate output numbers, leaving universities little headroom to invest in translational research facilities and knowledge transfer supporting engagement with the regional and national innovation systems.

In many instances this gap has been partially filled by municipalities, through their investment in science parks and technology centres, supplemented in EU Objective 1 and 2 areas by European Regional Development Funds delivered via Regional Councils. Municipalities have often taken the initiative in this area because universities in Finland do not own their own estates and rent their premises from a state holding company. This company is expected by the Ministry of Finance to charge notional market rents and as a consequence a significant proportion of the national higher education budget is allocated to Helsinki to meet the higher notional rents there, an adverse consequence in regional policy terms of a national financial policy (Goddard, J. *et al.* (2003)).

Further components of the research intensive end of the national innovation system are the national research institute (VTT) and the national fund for R&D (SITRA). VTT carries out commercial R&D for companies (40% of its budget); joint projects with companies and public bodies (30%) and

self-financed R&D projects (30%). Its priorities embrace electronics, IT, industrial systems, process industries, biotechnology and building/transport. Seventy per cent of staff is employed in Espoo.[17] Only Oulu, Tampere and Jyväskylä have more than 100 VTT employees. SITRA's role is that of a research fund and policy research organisation, financing and facilitating innovation and industrial development.

The key player in the second pillar of the national innovation system is Tekes. As Figure 2.5 shows, its activities bridge key stages in the innovation process. Tekes focuses on technology based development with emphases on four programme areas: ICT; Bio and Chemical Technology; Product and Product Technology; and Energy Environment and Construction. The main instruments of Tekes are R&D grants and loans to firms for technical research with public organisations. The regional dimension represents a relatively new feature in the work of the agency: it now has technology units located in the 14 regional Employment and Economic Development Centres.

The agency closest to the final stage of the innovation process is Finnvera, a public financing company providing risk finance (mainly loans and grants) and other financial products (such as export guarantees) particularly to SMEs. It is required to promote the development of enterprises, regions and export. Its 400 staff is spread in 15 regional offices where it works closely through the TE Centres with the regional offices of Tekes and the Ministry of Labour in supporting all aspects of the innovation process in regional businesses.

The TE Centres are an important initiative in terms of seeking to achieve the joining up of national policy at the regional level. These regional offices of central government have access to a wide range of national funding programmes which can be tailored to the needs of businesses in their area. An example is the new Ministry of Labour programme (TYKES) which embraces support for work-place development projects designed to improve both the effectiveness of organisations (*e.g.*, leadership, work processes, customer services) and the quality of working life (*e.g.*, collaboration and trust in the workplace). This EUR 87 million programme over the period 2004-2009 emphasising social innovation, is part of an emerging "soft" innovation policy distinct from the "hard" technology-driven approach. The regional innovation environment outside the workplace can be critically important and this again raises the question of how these top down programmes interact with regional initiatives.

The most explicit regional element in national innovation policy is the Centres of Expertise sponsored by the Ministry of the Interior. These focus on key industries in many different sectors including culture,[18] media and digital content (see Figure 2.6), where there is a certain degree of regional specialisation in the private sector and research competence in universities and polytechnics.

Figure 2.6. **Centres of Expertise, 2005**

I CENTRES AND FIELDS OF EXPERTISE:

1. Hyvinkää Region Centre of Expertise
- Lifting, Moving and Logistics Industries

2. Häme Centre of Expertise
- Professional Expertise and Learning

3. Jyväskylä Region Centre of Expertise
- Information Technology
- Paper Manufacture Management
- Energy and Environmental Technology

4. South-East Finland Centre of Expertise
- High Technology Metal Constructions
- Processes and Systems for the Forest Industry
- Logistics
- Russian Business Development

5. Kainuu Centre of Expertise
- Chamber Music
- Measuring Technology

6. Kokkola Region Centre of Expertise
- Chemistry

7. Kuopio Region Centre of Expertise
- Pharmaceutical Development
- Healthcare Technology
- Agrobiotechnology

8. Lapland Centre of Expertise
- Experience Industry

9. Western Finland Centre of Expertise
- Energy Technology

10. Mikkeli Region Centre of Expertise
- Composites and Coatings

11. Oulu Region Centre of Expertise
- Information Industry
- Well-being Industry

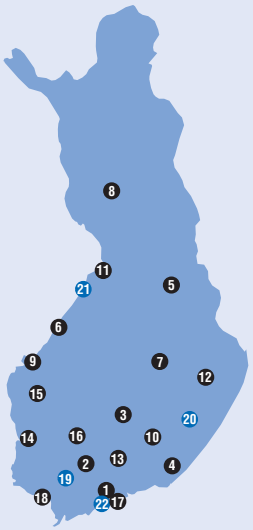
12. North Karelia Centre of Expertise
- Wood Technology and Forestry
- Plastics and Tooling

13. Lahti Region Centre of Expertise
- Design, Quality and Ecological Technology

14. Satakunta Centre of Expertise
- Material Technology
- Distance Technology

15. Seinäjoki Region Centre of Expertise
- Food Processing Industry
- Intelligence Technology

16. Tampere Region Centre of Expertise
- Mechanical Engineering and Automation
- Information and Communications Technology
- Media Services
- Health Technology



17. Helsinki Region Centre of Expertise
- Adaptive Materials and Microsystems
- Gene Technology and Molecular Biology
- Software Product Business
- Medical and Welfare Technologies
- Digital Media, Content Production and Learning Services
- Logistics

18. South-West Finland Centre of Expertise
- Biomaterials, Diagnostics and Pharmaceutical Development
- Materials Surface Technology
- Cultural Production and Digital Content Production
- Information and Communications Technology

NETWORKED CENTRES OF EXPERTISE:

19. Centre of Expertise for the Food Processing Industry – ELO
- Food Processing Industry (co-ordination: Jokioinen)

20. Centre of Expertise for Tourism – MOSKE
- Tourism (co-ordination: Savonlinna)

21. Centre of Expertise for the Metal Industry of the Bothnian Arc – ProMetal
- Metal Products and Industrial Maintenance Services (co-ordination: Raahe)

22. Centre of Expertise for Wood Products – PuuOske
- Wood Products (co-ordination: Helsinki)

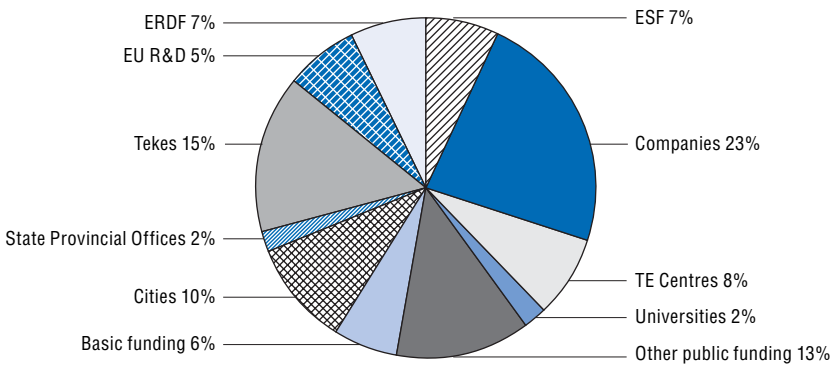
www.oske.net

Source: Ministry of the Interior.

Successive rounds of centres have been designated following national competitions. There are now 18 different regional centres across the country. The centres are expected to network nationally as well as regionally so as to develop their core competence in a networked fashion, thus creating a mutually supportive framework across the country. Besides these "regional clusters of competence", four centres have been specifically created with a national vocation and comprise networked sub-centres. Three of these centres[19] are relevant to the industrial development of more rural or peripheral regions (food, wood products, and tourism). While investments in the centres has been small relative to other strands of innovation support, the Ministry of the Interior considers that this EUR 20 million has levered in EUR 330 million of total project funding (Figure 2.7).

Following a major policy review the Ministry of Education published its own *Regional Strategy for Education and Research up to 2013* (Ministry of Education (2004)). The overarching vision is that "Finland's welfare and international competitiveness rests on the vitality and innovativeness of the regions, which is promoted by a regionally comprehensive provision of education and research". The specific vision and strategic policy guidance for research and development are set out in Box 2.5. The translation of these policies into action has been the subject of an on-going process of review. The recommendations of a report completed in 2003 are summarised in Box 2.6. At the top of the recommendation is "strengthening the role of Higher Education Institutions (HEIs) in regional innovation systems". Most significantly, the review recommended revision to the basic laws defining the role of HEIs to embrace a "third task". The 2004 University Act embodies this task as follows: "Universities should, as part of their operation, interact with surrounding

Figure 2.7. **Total funding *via* Centres of Expertise, 1999-2000**
Finished projects



Source: Ministry of the Interior.

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Box 2.5. **Ministry of Education Regional Strategy for Higher Education and R&D**

Vision: "*Research and development is of a high quality in the different regions and its results are utilised in a versatile and effective way to strengthen the vitality and welfare of the regions. The regional innovation environments are based on university research and polytechnic R&D, which is geared to working life and regional development.*"

Strategic policy lines: R&D in higher education institutions will be based on the development of their own strengths and on varied local, national and international networking. The Academy of Finland will support high-standard research with long-term funding based on quality. Research infrastructures and support services will be developed to make quality R&D results available in different parts of the country. The utilisation of research findings will be developed to make the knowledge of universities and polytechnics easily and flexibly accessible in different regions.

Measures will be taken to strengthen regional research cooperation between universities and polytechnics, the latter's co-operation with other players in the region and universities' and polytechnics' contribution to the Centre of Expertise and Regional Centre Programmes and to science parks and technology centres. The operations of large, versatile research environments will be enhanced and their knowledge will also be utilised outside their own regions.

Source: Ministry of Education.

society and promote the positive impacts of research activities". In parallel, the Ministry of Education requires polytechnics[20] to co-operate with universities in this area, thus engaging these other higher education institutions in regional development. Both universities and polytechnics are to update their "third task", *i.e.*, regional development, strategies by September 2005.

Alongside these national actors and agencies an ongoing review by the Science and Technology Policy Council of the role of intermediate organisations in the Finnish innovation system identified 100 to 160 regional development companies, around 40 technology and innovation centres or incubators in about 60 locations. Another on-going study refers to 22 technology centres employing 506 staff with net sales of EUR 90 million. These bottom-up initiatives meet with top down programmes in a complex geography of R&D investment.

Box 2.6. **Recommendations of the Working Group for Regional Developments of Higher Education**

1. **Strengthening the role of higher education (HE) in the regional innovation system** by including a third role in the university and polytechnic law, creating a Ministry of Education regional strategy for HE, promoting an active dialogue of the Ministry of Education with other ministries in the regions and defining regional targets and incentives for universities and polytechnics.
2. **Increasing co-operation/networking between universities, polytechnics, other partners** by common strategies, common councils, co-operation and networking between Swedish language HE units, regional co-ordination between different actors and special programs for less developed regions.
3. **Structural development of universities and polytechnics** by increased co-operation between universities and polytechnics, profiling of the universities, structural development of polytechnics via fusion and merging.
4. **Research on regional impacts of HE** by research and evaluation, development of statistical data and of a "know-how-register".
5. **Special issues concerning the Helsinki metropolitan area**

6-8. **Classification by a regional barometer**

Innovative growth regions/"Neutral" regions/Less developed regions

9. **Measures to develop education and research in engineering**
10. **Development of business knowledge**
11. **Better utilisation of EU programmes**
12. **New HE supply (*e.g.*, Pori and Mikkeli)**
13. **New funding**

Source: Science and Technology Policy Council, 2003.

The regional dimension to the innovation system

There have been numerous evaluations of the various strands within the Finnish innovation system and in 2003 the Ministry of Trade and Industry published an international evaluation of the Finnish Innovation and Support System (Georghiou *et al*. (2003)). However, there have been few publicly sponsored evaluations of the territorial dimension of the system, specifically how the top down and bottom-up initiatives come together to create a supportive environment for innovation within a particular city and its surrounding region. The MTI sponsored evaluation does however contain a number of important insights relevant to the regional dimension.

Drawing on the extensive literature the review sees innovation as a process:

- Integrating market opportunities with the design, development, financial and engineering capabilities of firms, in ways that are both uncertain and complex.
- With continuous feedback between activities, rather than linear transitions.
- Characterised by complex interactions between firms and their external environments, and in which innovation takes on a collective character.
- Which is continuous rather than intermittent and in which capabilities and performance develop cumulatively over time.

This perspective, emphasising innovation as a collaborative or even collective process, involving firms, supporting services/agencies, shaped by the interaction between actors, is particularly relevant at the regional scale because of face to face interactions. This is not to imply that all interactions are regional, but rather that at this scale better co-ordination between key actors and agencies and between different levels in the national system can be achieved. This may be particularly important for traditional industries such as forestry where activities complimentary to R&D like logistics, production, and branding are important to competitiveness and may come in the form of "disembodied" knowledge transmitted through a relatively decentralised industrial support infrastructure.

This perspective has resonances with an industrial cluster approach to economic development. The Centre of Expertise programme, although focused on specific sectors, through its emphasis on networking, adopts methodologies associated with cluster development. However, at a national level, the only explicit cluster programme based on innovation relates to IT production, concentrated in Nokia and a limited number of cities. This factor and the globalisation of Nokia's research and innovation depicted in Figure 2.8 prompted the Ministry of the Interior to commission a review entitled "*What Next? Finnish ICT Production and Globalisation*" (Steinbock, D. [2003]). In its introduction to the review the Ministry sets out its perspective on the future development of innovation policy, clearly much wider than supporting IT production locations (Box 2.7). It embraces education and skills including "operating environments" that attract and retain creative people, highlighting ICT use. The future performance of the Finnish economy will depend on the ability of small firms in traditional sectors to benefit from the trickle-down effect of innovative cluster-type environments by efficiently adopting new technologies and organisational methods.

The regional perspective may also be important in addressing two generally recognised weaknesses of the Finnish Innovation System, namely the low rate of new enterprise formation and the low take up of ICTs, both

Figure 2.8. **Nokia's R&D production locations**

***a)* Worldwide (2003)**

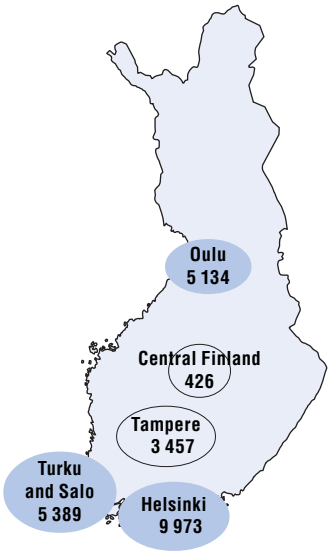
Nokia's R&D locations
- Australia
- Canada
- China
- Denmark
- Finland
- Germany
- Great Britain
- Hungary
- India
- Japan
- South Korea
- Spain
- Sweden
- USA

Nokia mobile phones
- Brazil
- China
- Finland
- Germany
- Great Britain
- Hungary
- Mexico

Nokia networks
- China
- Finland

Nokia ventures organisation
- China

***b)* In Finland (2000)**



14 R&D Centers	Espoo, Helsinki, Oulu, Salo, Tampere, Turku, Jyväskylä
5 manufacturing sites	Espoo, Haukipudas, Oulu, Salo, Vantaa

Source: Nokia.

linked to the fact that the Finnish business sector is characterised by relatively large industrial companies, responsible for a major export share. In terms of new enterprise formation, the shortcomings of the Finnish venture capital market have been noted in an evaluation undertaken for the Ministry of Trade and Industry (Maula, M and Murray, G (2003)). The underdeveloped nature of

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Box 2.7. **The Finnish ICT Cluster: a view from the Ministry of Interior**

The key question of future regional development is whether Finland will be successful as a user of the new information technology and not only a producer. To produce information services and contents can have a much wider basis than what is currently the case. All regions cannot be successful ICT producers, but each of them can increase their competitiveness through skilful ICT use.

The comprehensive educational network of Finland enables development based on expertise: universities, polytechnics and second grade vocational training support city regions on every level. In order to develop, every field of production needs top expertise. Universities, polytechnics and science parks are thus central actors in the new growth. Basic factors for growth in the city regions are technology-oriented research and development operations and productive applications, inputs on expertise and human capital, social innovations, functional infrastructure as well as good accessibility that requires functional logistics.

The competitiveness of the regions consists of quality factors that make certain regions attractive operating environments for businesses and skilful labour. Increasingly, the competitive ability of companies consists of local resources and quality factors. National policy without local commitment and division of labour is not sufficiently effective.

Narrow technology policy will no longer be sufficient. We need an extensive innovation policy and development of innovative environments. As a small country, Finland needs a special policy that is suitable for a small country in which different actors of innovation policy co-operate intensively and systematically.

We need specialisation of the regions, deepening division of labour within the country, between city areas and networking, co-operation and creation of clusters. Region's competitiveness ought to be strengthened so they become internationally attractive operating environments in their fields of expertise as well as pleasant living environments for skilful labour. It is necessary to decentralise national innovation policy.

Source: D. Steinbock, 2003, "What Next? Finnish ICT Clusters and Globalisation", Ministry of the Interior.

these markets outside of Helsinki is exemplified by the fact that 61% of venture capital investments are made in the more prosperous parts of the country (*i.e.*, Southern and Western Finland) (Steinbock, D. (2003)). Regional initiatives increasing the supply of good projects, including those from

universities, could contribute to developing these markets in other parts of the country.

Concerning ICTs, OECD notes that take up and use of the Internet for electronic trading by SMEs falls far short of the image of Finland as a leading "Information Society" country (OECD, 2005b), (Castells, M and Himanen (2001)). Promotion of ICTs within business has not been a strong strand in national innovation policy. However, the Ministry of Finance is an active promoter of the strategic development of the Information Society through a specific national programme under its responsibility and the Ministry of Transport and Communications oversees the implementation of an ambitious Government Broadband Strategy formulated in 2003, targeting coverage of most of the country by the end of 2005.[21] A recent report of the latter ministry recognises ICTs as a source of productivity and economic growth.[22] The lack of connection between these policy domains and to the regional agenda is surprising, as particular characteristics of the regional environment can have a major influence on entrepreneurial activities while new technology diffusion amongst small businesses obeys to a "neighbourhood" effect. Local broadband networks, actively implemented by regions and municipalities, could make a significant contribution to improving national innovative performance, given adequate attention to training and financial needs of SMES in this strategic area.

In meeting these challenges regionally based science parks and technology centres are essential components of the national innovation system. Individual science parks are part of a national network (TEKEL) with 22 members located in 19 cities. The science park companies employ around 500 professional and support staff with estate and economic development functions increasingly divided into separate organisations, often referred to as "technology centres". The main concentrations are in Tampere, Turku and Oulu.[23] A number of parks have been established in smaller towns over the past ten years, many in places without a university. The Science Park Association claims to house 1 600 enterprises and bring together 32 000 experts working in different fields (see Table 2.1). All but one of the parks/technology centres supports the development and application of ICTs. All science parks aim to play a role in the national innovation system, including enhancing links to the university science base. In reality, because these are essentially bottom-up initiatives, variations in focus (technology and sector), ownership (universities, municipalities, private sector), governance (who is accountable to who) and geographical reach (city, region, national) are inevitable.

Table 2.1. **Profiles of Finnish Science Parks**

	Agropolis Ltd, Jokioinen	Carelian Science Park, Joensuu	Culminatum, Espoo	Finn-Medi Research, Tampere	Foodwest, Seinäjoki	Helsinki Business and Science Park	Hyvinkää Techvilla	Jyväskylä Science Park	Kajaani Technolgy Centre	KETEK Technology Centre, Kokkola	Lahti Science and Business Park	Media Tampere	Prizztech, Pori	Seinäjoki Technology Centre	Technology Centre Hermia, Tampere	Technology Centre Innopark, Hämeenlinna	Technology Centre Kareltek, Lappeenranta	Technology Centre Merinova, Vaasa	Technology Centre Teknia, Kuopio	Technopolis, Oulu and Vantaa	Technopolis Ventures, Espoo	Turku Science Park
Automation, lifting and moving technology							■								■			■				
Biotechnology, pharmaceutical development	■		■	■		■			■										■	■		■
Chemical and plastic technology	■	■								■												
Digital media, content production			■									■	■			■				■		■
Electronics, optoelectronics			■				■	■	■				■		■		■	■		■	■	■
Energy technology								■					■					■		■		
Environmental technology	■					■		■			■		■		■	■	■	■	■	■		
Food technology	■				■	■													■			■
Forestry and wood technology		■															■					
Healthcare and medical technology			■	■		■		■			■		■			■			■	■	■	■
Information and communication technology	■	■	■	■		■	■	■	■		■	■	■	■	■	■	■	■	■	■	■	■
Laser technology, optics		■							■	■												
Logistics			■				■										■			■		
Materials research and technology			■							■			■								■	■
Measurement technology									■													
Metal, machine and tool technology		■									■				■	■	■					
Nanotechnology			■					■												■	■	
Paper manufacturing technology								■														

Source: Finnish Association of Science Parks (Tekel).

Innovation in Finnish regions

Northern Finland: building a new industrial base in a peripheral region

Oulu, capital of North Ostrobothnia, a major centre for Nokia's R&D and production (4 300 employees today), is a significant growth centre in Northern Finland which has experienced continuous expansion of employment opportunities since the end of the Finnish recession in the early 1990s. It hosts a number of ICT businesses which exploit mobile technology. Oulu promotes itself as a technology "hot spot" and is one of the few cities in Finland to have a well developed international marketing ("Invest in Oulu"). All elements of the national innovation system and its regional counterparts have developed and evolved in Oulu, including a strong technological university, a polytechnic, a science park ("Technopolis") and the only significant part of VTT outside of the Helsinki region. Stimulated by the funding available from the ERDF Objective 2 programme, considerable effort has been made to integrate separate initiatives within the framework of the "Oulu Growth Agreement" (see Box 2.8) supporting different industry clusters.

Networking between the various actors and agencies in Oulu has been facilitated by the creation of new physical environments, most notable the Science Park called Technopolis. Technopolis Limited provides premises, business and professional services, developmental services and programmes. It has recently acquired a major site in Espoo in the Helsinki region, underlining its aspirations to become an international and well as a national player. A supra-regional vision in a globalising economy is another approach adopted to anchor new strategies. The Multipolis network launched by Technopolis reflects an entrepreneurial ambition to extend the reach of firms and organisations evolving around the Oulu science park to 15 smaller centres in Northern Finland on the one hand, with extension to neighbouring countries on the other. Plans are well advanced to strengthen links to centres in Northern Norway, Northern Sweden and to extend co-operation to Russia (see Box 2.9).

A significant feature of the Oulu innovation system is constituted by projects to provide services from the city to the wider region, which is the underlying logic of the Regional Centre Programme. Following difficulties with launching local innovation support programmes in small municipalities, a "1 + 3" regional council agreement was drawn up to include these sub-regions under the umbrella of an Oulu led initiative. Whether differences in industrial structure (*e.g.*, wood/pulp, metal processing and tourism) and travel distances (about three hours to the most distant city in the coalition, in a region spreading from the Gulf of Bothnia to the border of Russia) inhibits the spread of the agglomeration effects of the Oulu network remains to be seen. On the

Box 2.8. **The Oulu Growth Agreement and cluster development**

The Oulu Growth Agreement, orchestrated by Oulu Innovation Ltd. (Centre of Expertise) focuses on five clusters: IT; content and media; wellness; biotechnology and environment. These five fields employ about 14 700 in 780 enterprises with a total turnover of EUR 3.7 billion. These clusters are supported by programmes in corporate development and logistics.

Central to the cluster development programmes are industry forums which bring together 150 companies. The "Mobile Forum" supports R&D and business development for future mobile services and products and the use of Octopus, an open innovation and testing environment for mobile technologies, special purpose vehicle to optimise time, money and effort needed for successful US product launches. The well-being cluster embraces medical, information, bio and environmental technologies and its forum brings together companies, education and research and public services; bound together by the flow of resources, pilot projects and experts. Eighty companies have joined these forums and 63% of these have claimed a product innovation as a result of participation.

These developments, while benefiting smaller firms, all indirectly support the strategy of the key player in Oulu, Nokia, to diversify into new application areas for its technologies. They also demonstrate that the presence of Nokia itself in Oulu, added to the presence of other knowledge-intensive institutions such as the university and park constitute a favourable environment for cluster development in mobile technology and ICTs in the area.

Source: Based on information provided by the City of Oulu.

other hand, Oulu is the only significant city in the region in a position to assume this leadership for the benefit of the region. Also, representation of municipalities in regional councils (see Chapter 3) is conducive to the necessary networking.

Rovaniemi, capital of Lapland, has an economic base focusing on tourism and industries related to the northern environment (cold climate testing environment for automobiles, snow mobiles but also rescue and mobile technologies under severe climate conditions). It has its own university which is strong in social sciences, a polytechnic, a science park ("Aurora Borealis") and a Centre of Expertise seeking to develop tourism as an "experience industry". The development programme for the Rovaniemi region is overseen by the business development company EERO constituted as a joint municipal board between the municipalities of Rovaniemi and Ranua (see Box 2.10). EERO seeks to draw together a range of organisations and programmes

Box 2.9. **Multipolis: a network of local centres of knowledge in the northern periphery**

Multipolis, launched in 2000, is a network of centres of knowledge from northern Finland, now associated to other centres in northern Sweden and northern Norway, focusing on different sectors of high technology. The Multipolis network's key objectives are 1) to improve the competitiveness and strengthen the expertise of technology enterprises in northern Finland, and the northernmost part of Europe; 2) to create new jobs in the hi-tech sector; 3) to extend the fields of expertise in the Oulu Region to the other centres of northern Finland; and 4) to stimulate national and international co-operation amongst these centres.

The Multipolis network areas of specialisation are in particular telecommunications, wellness technology and cold climate expertise. Close co-operation combines the know-how of locally operating centres of expertise, R&D, technology companies and public authorities. The network acts also as a catalyst and promoter of development programmes between the centres and facilitates collaboration between companies. The network is an essential tool for innovation policy in northern Finland.

Source: Based on information provided by the Council of Oulu Region.

including those emanating from the university, the polytechnic, the Centre of Expertise, Regional Centre Programme, the Science Park and TE Centre. It maintains operational links with the Ministry of Interior, as it supports the Lapland Centre of Expertise for the Experience Industry, relating to the development of new tourism products and approaches. The science park is also a member of the Multipolis network hubbed on Oulu.

The co-development of the Oulu innovation system and that focused on the City of Rovaniemi (Lapland) will be interesting to observe, in particular to answer the challenges of extending the agglomeration effects of large urban centres across a thinly populated region. Can synergies be effectively developed in the supra-regional logic indicated above, between two neighbouring regions having similar environmental and demographic conditions? ERDF funding encourages this type of approach. An example would be linkages between the Aurora Borealis testing centre for wireless, navigation, experience and tourism services and the mobile technology expertise in Oulu. Another possible application could relate to co-operation between the latter and the police research laboratory recently relocated in Rovaniemi from Helsinki.

Box 2.10. **A public development company in Lapland: EERO**

Given the weight of the service sector in Rovaniemi, EERO focuses on programmes of education, training and enterprise. A particularly innovative concept is the ANNA service which seeks to attract entrepreneurs to Rovaniemi and than support them. This service is a necessary recognition that in such a northerly location creating an environment that attracts and retains creative people has to be a key focus of policy.

The environment is turned to advantage in the field of cold and winter technology defined as "all products, services and systems which are used or produced in cold or wintry conditions as well as activities supporting the research, development, teaching and marketing and application of these". This perspective clearly illustrates a broadly based approach to innovation capitalizing on local conditions.

Likewise, the Lapland Centre of Expertise in the Experience Industry draws on "the behavioural", as distinct from the hard sciences and engineering, indicating the flexibility of the underlying concept of linking industry (in this case a service industry) to the knowledge base in higher education. However, the capacity of local tourist businesses to absorb this knowledge remains a challenge, as major successful initiatives are the result of direct municipal investment.*

* This is the case of the famous Santa Claus Village that draws visitors from around the world, rendering Rovaniemi the second busiest airport in Finland after Helsinki.

Source: Based on information provided by EERO and the Lapland Centre of Expertise.

Tampere City Region: restructuring an older industrial base

Tampere City and its surrounding region is one of the "motors" of the Finnish economy outside of the capital city. The municipality (central city) has a population of 201 000. Including the immediate hinterland, the population of the functional region is 312 000. The whole Tampere Region (the Regional Council area) embraces a population of 457 000 (8.7% of the Finnish total). Tampere is a centre of established Finnish industries which have successfully modernised; it has also developed a buoyant ICT sector.[24] Despite these favourable developments, there are persistent problems, such as high unemployment. The unemployment rate has remained quite high since the recession at the beginning of the 1990s and is currently around 12-13%. The hard core of unemployment is structural in nature: innovation policy can contribute to alleviate the situation but cannot be the unique remedy.

On the other hand, one of the major problems of Tampere Region, especially in comparison with the capital region, is precisely the low number of new start-up companies with very ambitious growth and internationalisation objectives.

This is presumably due to the cultural heritage of large-scale industrial employers and the strong orientation towards wage work instead of a more entrepreneurial attitude. This problem has been tackled by many economic development and innovation policy measures, but progress has been slow. "eTampere" Programme, a five-year local Information Society development project with a budget of EUR 130 million, has a sub-programme called eAccelerator that aims to facilitate the development and innovation of growth companies. The identification of clusters has been facilitated by the four Centres of Expertise relating to mechanical engineering and automation, ICTs, media services and health technology.

The success of Tampere is clearly linked to the strength of local initiatives. Local actors have been able to work together to take advantage of national schemes like the Centre of Expertise Programme[25] and national resources available to the TE Centre. They have also been capable of taking advantage of more general economic development and technological trends by focused initiatives. Tampere is one of the areas that has benefited from the expansion of the Finnish ICT industry and the growth of Nokia, now the biggest private employer in the region (approximately 3 700 employees almost entirely in R&D).[26] Equally important, public authorities have not sought to control the development process but rather to facilitate it through arms length intermediary organisations which have a private sector ethos even if the majority shareholding is in the public sector, a so-called "enabling model" for economic development (Sotarauta *et al*. 2003). Of significance from a regional perspective is the fact that the City of Tampere has assumed a key leadership responsibility for the wider region.

Eastern Finland: the role of universities in a border region

Eastern Finland has a traditional industrial base in forestry, wood products and the heavier end of mechanical engineering and three medium-sized universities each with a distinctive academic profile located in three different cities: Kuopio (North Savo Region), Joensuu (North Karelia Region) and Lappeenranta (South Karelia Region). These universities were established during the 1960s as a conscious act of regional policy, with their regional role having been the subject of two rounds of evaluation conducted under the auspices of the Finnish Higher Education Council (FINHEEC) a body accountable to the Ministry of Education (Goddard, *J. et al*. (2003)). Rather than a single large comprehensive university in one of the cities, the decision was made to found three independent universities, each catering for different facets of the development of a border region, with ill-defined expectations that the universities would act together to achieve a common goal.

Kuopio University specialises in health and life sciences (with links to a university hospital) and environmental sciences. Joensuu University was

founded with specialisation in teacher training, forestry and other renewable resources and has developed specific competencies in basic sciences, arts, humanities and social sciences. Lappeenranta is a University of Technology specialising in mechanical and electrical engineering and IT, and also business administration. Each has sought to develop distinctive national and international profiles. In terms of contribution to regional development the FINHEEC review identified here three different models of regional development. In Kuopio, "science push" created a new industrial base from scratch chiefly through spin-outs and the attraction of mobile investment, showing that over a span of years a University can be a nucleus leading to creation of thriving firms in sectors that were either absent or modestly represented in the local economy . In Joensuu, the "learning region" model seems to have emerged, capitalising in particular on the traditional know-how in the forestry sector.[27] Finally, in Lappeenranta, the university successfully contributed to the restructuring of older industries in this border city, now also helping efforts of other cities in the region to gain access to foreign markets, particularly in Russia.

Regional Universities maintain presence in different parts of their region, effectively extending their influence to other cities. The University of Joensuu, for example, has an affiliate institution in Savonlinna with more than 1 000 students (one-sixth of total enrolment). Also, it should be noted that in Mikkeli (Region of Etelä-Savo), the only significant city in Eastern Finland without a university, the Ministry of Education has more recently supported the establishment of branches of the University of Helsinki and of the Helsinki School of Economics and the development of a new concept of a University Centre and campus housing these branches jointly with Mikkeli Polytechnic. The concept of university centres[28] rests on the recognition that each region cannot possess a full-fledged university because of issues of critical mass, knowledge base, international competition and financing. University centres, strongly linked to major universities offer the proper alternative. In these regions, Polytechnics naturally play a crucial role, insofar as collaboration with firms is anchored in the tradition of such Higher Education Institutions.

The universities with their own research institutes and national centres of excellence designated by the Academy of Finland, the Centres of Expertise based on four science parks and national R&D facilities in the region are all regional components of the national innovation system. The relevance of this infrastructure to the industrial development of Eastern Finland has been questioned in 2001 by a review of the EU sponsored Regional Innovation and Technology Transfer Strategy (RITTS) (Lautenen, T (2001)) suggesting that focus on technology "push" is not particularly relevant to the 85% of businesses in Eastern Finland employing less than five persons. In the case of SMEs, it underlined that the diversity of manufacturing skills and technologies and

shortcomings in terms of general business capability, entrepreneurship and demand for inter-company co-operation were not taken into account. The weak industrial base of Eastern Finland raises challenges for a technology driven approach to innovation-led regional development and the role of universities in such a strategy. Many of the opportunities in knowledge intensive business services, including tourism and culture and in expanding markets in nearby Russia do not depend on technology for their successful exploitation.

It is useful to draw a parallel with the UK experience where similar efforts are made to develop the third task, with specific focus on the University of Newcastle and Northeast England where innovative approaches have been taken. Newcastle is a research intensive multi-faculty university with a medical school located in a peripheral and less prosperous region. It has roots in the local economy and has successfully become a national and global institution. Restructuring, designed to raise its competitive position globally has a strong local component. The revised mission statement mentions "A world class research led educational institution playing a leading role in the economic, social and cultural development of the North East of England". Significant restructuring of the university faculties and departments has taken place, to introduce greater clarity in the academic management hierarchy and ensure ability to respond corporately to the needs of business and the community. The strategy aims to enhance business development in three new faculties, to commercialise intellectual property through specialist advice, to develop consultancy, commercial services and training while building collaborative links in technology transfer with other universities in the region.[29] The "Newcastle model" is internationally recognised (see Box 2.11) (Hansson, F., *et al.*) and can be a useful reference, provided it is adapted to different national contexts. In the case of Finland, this would mean emphasising high quality research and education, well in line with Finnish achievements.

The initiative to establish a "regional higher education system" in Eastern Finland coincided with a period of redistributive regional policy in the 1960s. There have been difficulties in adjusting to new policy paradigms having the creation of regional innovation systems based on cities at its heart. The experience of Eastern Finland universities prompts a number of questions about higher education provision and regional development in Finland:

- Can relatively small HEIs achieve sufficient critical mass to compete internationally and engage regionally?
- Is a broadly defined peripheral region such as Eastern Finland a meaningful entity for guiding and developing the interface between national higher education, science and technology, and regional policy?

Box 2.11. **University/business interaction (A Newcastle/Copenhagen comparison)**

The danger is, in brief, that by building intermediary institutions such as Symbion (Science Park in Copenhagen), we may in fact institutionalise and cement a low interaction between higher education institutions and industry. By creating these intermediary institutions we produce the illusion of bridging the gap between science and economy, while in fact such intermediaries contribute significantly to keeping the institutions of science and economy apart. This brings us to the key strength of the Newcastle model. Here the vision is not to transfer certain research results with particular commercial potential from the university to the regional economy, rather it is to make the university itself an active player in the regional economy, in other words to place the university "at the heart of the regional economy". A fundamental difference between this and the traditional model is that the latter is tailored to help commercialise research, whereas the Newcastle model seeks to build an institution that is capable of producing commercialisable research. The traditional model is tailored to help new entrepreneurs commercialise research-based technologies, while the Newcastle model seeks to make entrepreneurs of students and commercialisable technologies of research.

Source: Based on information provided by the Copenhagen Business School, 2004.

- How can inter-institutional divisions of functions to meet regional needs be managed under a funding regime which operates on a national subject by subject basis (*e.g.*, business studies, law, engineering) as distinct from a functional basis (*e.g.*, technology transfer, continuing professional development)?
- How can the triple helix model of university, industry and government operate at a regional scale when the demand side from industry is relatively weak?

The emerging challenge of globalisation and localisation

In a significant triennial review entitled Knowledge, Innovation and Internationalisation published in 2003, the Science and Technology Policy Council of Finland links national innovation policy to regional development.[30] It notes (p. 2/3) "the past success of Finland in combining extensive production and economic utilisation of knowledge with other aims such as the promotion of welfare and balanced regional development". However "apart from technological innovation this requires systematic inputs into producing social innovations geared to prevent societal and social development from diverging from

economic and technological developments … a systematic aspiration to create innovations cannot be limited to the national setting and traditional co-operation. Internationalisation must proceed at the level of the innovation system as a whole". These challenges are linked to the theme of placing knowledge exploitation at the heart of regional development. The review argues that regions face "the same international challenges which influence the national level. In order to be able to give a successful response to these, regions need to enhance their own factors for development. HEIs and local units of research institutes have a particular task in contributing to regional knowledge capital and to put it at the disposal of users. Relating to this, the anticipation of labour and educational needs must be urgently developed".

The focus on a broader definition of innovation adopted here is consistent with an emerging consensus amongst experts working in the field of science, technology and innovation policy. Gibbons in a discussion of globalisation, makes a powerful if oblique case for a regional dimension to a new form of national innovation policy (Gibbons, M. (2004)) (Box 2.12).

Box 2.12. **Globalisation and innovation**

''(Globalisation) can be viewed as the outcome of the processes of imitation and adaptation of innovations as they are taken up (diffused) by one country, firm or institution after another. Here, innovations are "solutions" to problems of many different kinds – whether they are scientific discoveries, new technologies, organisational forms, or modes of working. As innovations, these "solutions" offer different ways of doing things and as such they compose of threat to established routines. The diffusion of innovation to and from one institution to another or from one country to another provokes a competitive response in so far as it induces others to protect themselves from a possible threat to their position. As we are constantly reminded, under globalisation this threat can now arise from anywhere in the world. Thus, globalisation enhances competition and stimulates innovation, but the particulars of any innovation – the ways in which it can be imitated or adapted – depend crucially upon local circumstances. A crucial point to keep in mind is that not only institutions and organisations but also countries (and regions) differ in their ability to imitate and adapt solutions produced elsewhere. Globalisation then turns on the differences in the process of imitation, adaptation and diffusion between one locality and another. As a consequence, globalisation processes do not operate to produce the homogenisation of institutions, corporations and products, as is so often asserted. In fact the overall effect of the diffusion of innovation is to increase diversity."

Source: Gibbons, M. 2004.

A more recent report from the "Finland in the Global Economy" project published in December 2004 by the Prime Minister's office, entitled "Finland's Competence, Openness and Renewability" highlights the need for a shift from science and technology policy to innovation policy (Prime Minister's Office (2004a)). It notes that in comparison with Finland's strong technological competencies there are "obvious shortcomings in competence in early stage production and commercialisation ... insufficient capital for start up enterprises ... and ... much disparity amongst innovation organisations". In support of a more open environment the report highlights the importance of attracting foreign investment and employment based immigration. Although the report does not highlight the regional dimension it is clear that many of these challenges must be addressed both nationally and regionally. A key underlying theme of both Finnish reports is the capacity of agencies at the regional level to address the challenges of globalisation. The Science and Technology Policy Council is most explicit about this with regard to the role of universities (Box 2.13).

Regional initiatives supported by the Ministries of the Interior and Trade and Industry are equally relevant to the issue of capacity. The limited

Box 2.13. **Globalisation, innovation and universities**

One major question is how the university as an institution will be able to manage the pressures and growing expectations directed at it with regard to social, cultural and economic development ... whether the university has the internal capacity for renewal needed to lighten its work load in the face of constant new challenges. The traditional mission of the university is to promote free research and scientific education and to provide higher education based on research. The burning question in today's debate is how to include the duty to promote the utilisation of new knowledge in the Universities Act as the university's third mission. This question arises from both the growing expectations directed at universities by the users and from the legislative issues involved in efforts to reconcile the university's administrative culture, business and research ethics. The need to address these questions is tangible, because the change taking place in universities' mission and funding structure is systemic, shaking up the institution to its core.

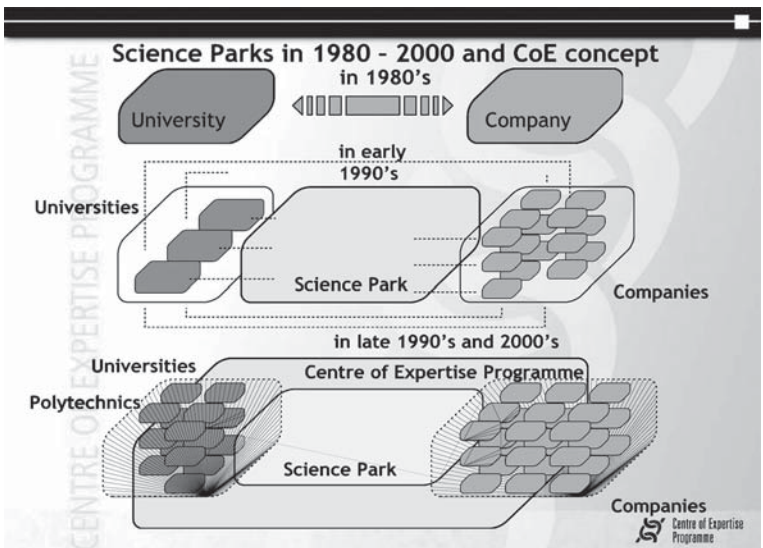
A new challenge for universities and the whole research system is to be able to combine in-depth specialised knowledge with versatile expertise for the benefit of users and in contract research and in joint projects with them. A question partly relating to this is the future of higher education on the whole: how its different parts will take shape jointly and separately.

Source: Science and Technology Policy Council, 2003.

resources of the Centre of Expertise Programme and more especially the Regional Centres Programme have already been noted. The large number of intermediary organisations increases the co-ordination challenge and enhances transaction costs to support innovation in the private sector. Those responsible for the Centre of Expertise Programme based on science parks see these as key institutions drawing together universities and businesses (Figures 2.9 and 2.10). However this raises fundamental questions regarding the financial relationship between centres, parks universities and polytechnics and the contribution of the public *versus* private sectors, with efforts being made to provide Universities with additional resources.[31] If in the future Higher Education Institutions assume a more active external role under legislation designed to address the challenges noted by the Science and Technology Council, they are likely to become more significant players in regional innovation systems. This brings forward questions regarding their relationship with other intermediary organisations (technology centres, science parks, TE Centres and regional VTT offices). If universities, working with polytechnics, were formally assigned a lead regional role this would result in a better participation of higher education into an integrated national innovation system and clarification of roles for the elaboration and implementation of regional programmes.[32]

A particular advantage of developing this integration would be in terms of a more transparent linkage between innovation and higher level skills that are

Figure 2.9. **Science Parks and the Centre of Expertise Programme**



Source: Ministry of the Interior.

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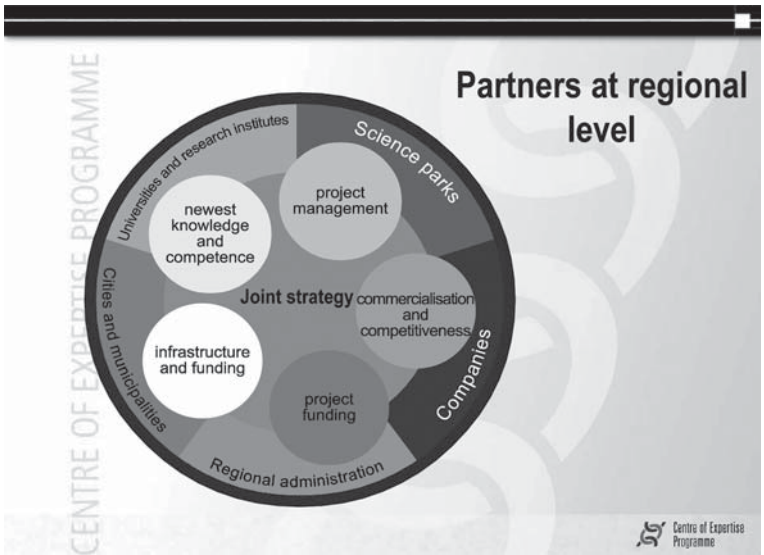
Figure 2.10. **Partners at a regional level**



Source: Ministry of the Interior.

provided through the education system. An interim evaluation of the Centre of Expertise Programme concluded that in the future a "technology based programme should require special grounds for extending into new 'soft' fields or new innovation instruments better suited to soft fields of expertise". This is clearly a matter for higher education including non technological fields of study such as management, social sciences and the arts and humanities. These fields are vital in relation to the new emphasis given to social innovation (new ways of working) highlighted by the Science and Technology Policy Council and to knowledge intensive business services, including cultural industries (emphasised in the report from the Prime Minister's office). The issue here is actually how to properly support and disseminate a "culture of innovation" whereby individuals and firms but also public institutions would internalise creative processes and thinking when preparing strategic decisions of an organisational nature or bearing on methods of work. Finland has here the potential for a "leading edge", insofar as social innovation is now on the agenda (see Chapter 3, Section 4), building on a long-standing tradition of civic participation.

There are a number of reasons why it would be appropriate for HEIs to be assigned a lead role in the orchestration of regional innovation support

systems and regional development.[33] Drawing on the learning region model of development, regional engagement by the university can be seen as:

- Knowledge creation by research and exploitation by technology transfer (spin-off, IPR…).
- Knowledge transfer via teaching involving work based learning, graduate recruitment, professional development and continuing education.
- Students establishing the social relations on which knowledge exchange is built.
- Cultural and community development creating milieu and social cohesion for innovation.
- In summary, the university can play a key role in local civil society, joining up separate strands of national policy (learning and skills, research and innovation, culture and social inclusion).

Enhanced regional engagement as proposed above would not be incompatible with ambitions for Finnish Universities to compete on a global stage. The FINHEEC evaluation of Kuopio, Joensuu and Lappeenranta in Eastern Finland and Turku in South West Finland highlight external engagement as driving the creation of better managed and more competitive institutions. The resources of the local environment, notably science parks and technology centres when integrated with core resources of the universities, are potentially major assets that could support global competitiveness, particularly if their own estates also came under their control (measures will be taken by the Ministry of Finance and Education to improve the basis on which rents for facilities are calculated). Such a transfer would be totally consistent with a policy of giving more autonomy than currently to universities. However such autonomy would need to be "earned" through an obligation for each university to serve its "region". This perspective would be fully coherent with the aims of the third task by directly contributing to its implementation, bringing forward, nonetheless, important questions concerning the financial resources that could be optimally allocated for this purpose.

A major challenge in relation to territorial development in Finland is that of sparsely populated regions outside the immediate sphere of influence of ten or so major cities. However a key characteristic of the Finnish Higher Education System is the strong national coverage of provision. In addition, to mainstream undergraduate and postgraduate programmes there is an extensive professional development activity undertaken by Centres of Continuing Education. The development of e-learning should also ensure that those living outside the large centres can be supported. Recently established University Centres provide a mechanism for knowledge transfer from first tier to second and third tier cities. Finally, given a shift in policy from technology

driven innovation to an approach focussing on the spread of tacit knowledge, this learning infrastructure can be a key asset for regional development and national competitiveness.

Key to the transformation of universities to more regionally engaged entrepreneurial institutions must be a reform of the current funding model of marginal costing for externally sponsored research. The introduction of full economic costing and pricing would ensure that universities have the resources at their disposal to invest in the infrastructure necessary to render their research and teaching suitable for private and public utilisation. Such a transformation of universities could drive a rationalisation of the complex and sometime diffuse structure of regional intermediary bodies, many poorly resourced. Engagement of universities in the top level of the national innovation system would ensure that the best intermediary organisations, for example amongst the Centres of Expertise and the businesses they serve, were at the heart of the system.

A wider recognition of the role of HEIs can play in the development of regions should flow from a thorough review of regional innovation addressing the following questions:

- Who are the key agencies (*e.g.*, Tekes, TE Centre, technology centres, Centre of Expertise, Municipalities, Development companies, universities, polytechnics)?
- What levers of influence do they have – advisors, grants, loans, premises (*i.e.*, inputs)?
- What are the outputs in terms of innovation performance?
- What are the spheres of influence of each of the agencies – city, region, national, international?
- How do the agencies relate to one another and business in their sphere influence?
- Evidence of joint working (*e.g.*, forums).
- Evidence of competition and/or overlap of responsibilities.
- The role of skills and training, including the work of university and polytechnic Centres for Continuing Education.
- Issues of governance – who is accountable to whom?

Conclusions and recommendations

The evidence reviewed here on the concentration of input to and outputs from the innovation process confirms that Finland's success in the production of new technology has been associated with a highly polarised pattern of territorial development nationally (Helsinki *versus* the rest of Finland) and

regionally (the major cities *vis-à-vis* less densely populated areas). While these patterns could be attributed to market forces and the decisions of the private sector, the strong role of the state in national innovation policy has contributed to this concentration. While public sector R&D is slightly more dispersed than that in the private sector, the lion's share of public support goes to research institutes and universities in the Helsinki area. Nevertheless an important feature of the Finnish success story has been the role played by major urban centres outside of Helsinki supporting the exploitation of science.

Whilst there has not been an explicit territorial dimension to the national innovation system, Finland has made significant progress in this direction. In large measure this can be attributed to the role of the Ministry of the Interior in facilitating local initiatives. The willingness of municipalities in the large and urban centres to invest in science parks and technology centres housing Centres of Expertise and to adopt an enabling rather than controlling role in relation to economic development has contributed to the emergence of entrepreneurial intermediary agencies supporting innovation in the private sector. Significantly some of the most dynamic of these bodies, like Technopolis Ltd. in Oulu, are extending their reach to smaller centres (via the Multipolis initiative), thereby contributing to less polarised territorial development whilst entering the top level of the urban hierarchy. Initiatives like Multipolis can strongly contribute towards the strengthening of existing innovation networks, with smaller centres benefiting from the experience and resources of more important ones, the latter developing a supra-regional role. Their consolidation could be actively pursued with financial incentives from the centre, in particular to encourage and support research and economic development programmes with quantifiable aims.

This entrepreneurial behaviour is less apparent in the core parts of the national innovation system. Here the emphasis has been on the implementation of national programmes in regions, distinct from supporting initiatives where the emphasis is along the development of the regions themselves. The importance of skills and know-how in facilitating innovative ways of working including the adoption of ICTs, especially by SMEs, does not figure prominently in the action supported by the Ministry of Labour through the TE Centres. Here the emphasis is on the delivery of national measures directly related to the needs of the unemployed. Although its approach is changing, Tekes regional offices have hitherto focused on the administration of national technology driven programmes. Where joining up of national programmes in relation to regional needs and opportunities does occur, it appears to be achieved through networking facilitated by the Centres of Expertise. However, their work is focused on key clusters, raising the question of support for innovation in businesses outside these areas. The extent to which there is a

strong commitment to the formation of innovative new businesses as distinct from supporting existing enterprises is also open to question.

The Centres of Expertise have also played a key role in drawing universities into their cities and regions, but again focusing on competency in specific technologies. Nevertheless, there would appear to be a long way to go in ensuring that universities become active players in all aspects of promoting innovative regional environments. The shortcomings of the basic funding model, particularly the general failure to adopt full economic costing for contract research and the lack of financial control over the university estate, are inhibiting the emergence of truly entrepreneurial universities locally engaged and also acting on the global stage. The capacity of a university to contribute to the softer aspects of regional innovative environments for all sectors through teaching, including skills enhancement, fostering creativity and leadership and attracting international students is an under-utilised asset. This is particularly important to fostering innovation in the regional service sector, particularly public services. In short, the strength of the Finnish Higher Education system in contributing to a stock of high quality manpower seems to be taken for granted and is not explicitly recognised as an active component of regional innovation.

Notwithstanding the strategic position of the Science and Technology Council, which has been a strong advocate of a regional dimension to national science and technology policy, it is apparent that there is some resistance to a greater joining up of policy at the national level. Centres of Expertise have been a great success but are the responsibility of a Ministry with principle links to local and regional government and not to business. It has been suggested that responsibility for the Centres should be transferred to the Ministry of Industry and Trade which has far greater resources to support innovation through agencies like Tekes. However, the latter has no tradition of engagement with the infrastructure and environment for innovation in particular places (*i.e.*, what goes on outside the workplace) and in synergistic contexts (the Learning Region concept). Similarly strictures could apply to the way in which the Ministry of Education supports the development of the regional role of the universities. While there may be a case for giving greater responsibility and autonomy to universities to support the development of innovative regional environments, such an approach contrasts with a tradition of steering of universities in terms of funded numbers of graduates. Enhanced regional engagement should not be incompatible with building academically strong institutions, provided local resources are mobilised to this end with universities becoming more embedded in the national innovation system through regional support mechanisms.

The preceding general discussion points to a number of specific recommendations for consideration.

- In relation to the concentration of public support for R&D in Helsinki, a review of location and resources provided to VTT with a view to strengthening the translational research capacity of universities and technology centres outside the capital. The review should embrace the what, where and how aspects of VTT work and not be simply an assessment of relocation possibilities.
- In order to build on the success of the Centres for Expertise Programme, science parks and technology centres, their links to HEIs needs to be reviewed. The review should consider land and property related issues and engagement with university technology transfer services and Centres for Continuing Education. It should be linked to ongoing discussions about the full economic costing for research and consulting services and the overall funding model.
- A key issue in terms of regional policy is the geographical reach of urban based innovation networks and initiatives. The Regional Centres programme of the Ministry of Interior, the University Centres and the Oulu Multipolis network are all attempts to spread the benefits of agglomeration, incorporating in certain cases smaller centres. The appropriateness of this model for knowledge transfer needs further empirical testing.
- To address the low rate of new training in the regions and the shortage of good projects that attract the attention of the Helsinki dominated venture capital market, consideration should be given to the establishment of a locally controlled "proof of concept fund" which could *inter alia* help bring university research ideas to market locally.
- Currently most public funding provided directly to business to support innovation is determined centrally and administrated regionally through TE Centres. The linkage between such direct measures and those relating to the work of many local actors and agencies dealing with the environment for innovation is far from clear and needs to be evaluated on a region by region basis to identify areas of complimentary and/or overlapping and possible rationalisation of agencies and funding streams.
- In most of the less developed regions of Finland the public sector is not only the principle employer, but also a potential source for innovations in products and service delivery, for example in such fields as health and well being. How public employers can more formally be incorporated into regional innovation systems needs to be systematically reviewed, for example in relation to technology transfer and exploitation of ICTs. Such a review could lead to a regional economic development dimension to national e-society initiatives.

- The promotion of regional development through measures to foster and support innovation involves drawing together separate national policy domains. Regional development is the primary responsibility of the Ministry of the Interior, while the Ministries of Industry and Trade and Education are the principle custodians of the national innovation system. To have an impact on policy and practice the reviews noted above need to be owned by all three Ministries. Consideration should thus be given to establishing a standing inter-ministerial committee on regional aspects of innovation policy, accountable to the Science and Technology Policy Council, whose role it is planned to strengthen, thus giving greater impact to the yearly report to Parliament on innovation.

2.4. Service delivery in areas with population decline

Issues

As befits the tradition of the Welfare State, areas of population decline, most of which are rural and/or peripheral and sparsely populated, are fully integrated into Finland's constant policy of equal access for all to public services across the country. Factors related mostly to very low population densities, long distances and severe climate, entailing consequences for economic and demographic developments, demand special attention in terms of organisation, cost and efficiency. This is particularly the case today, with the phenomenon of ageing (see Chapter 1, Section 1.1, "future challenges") being pronounced in many remote areas,[34] creating increased demand for certain types of services, the delivery of which is often very costly. New forms of organisation, co-operation and competitive tendering for the provision of services but also the opportunities offered by ICT are some of the issues that this section explores. In many small regions, private services, such as those offered by the local grocery store are often just as important for social and economic sustainability of small settlements, so these will also be included in the analysis.

Policies relevant to service delivery involve action taken at the national level by several ministries, in particular the interior, social affairs and health, education, agriculture and forestry but also transport and communications. Municipalities and their joint municipal boards (see Chapter 3) are, by far, the main providers of these services delivered on the basis of national standards, defined by law. These relate more to numerical and quality criteria (number of pupils per class, personnel ratios in general) than to the organisation of the delivery itself, which is largely left to the initiative of municipalities acting by reference to available financial resources and their efficient use. The Finnish grant system, as well as fiscal equalisation measures, allow compensating for structural demographic problems but can also stimulate innovations in

service delivery. However, the requirement to control, from the national perspective, the rising cost of public services, particularly in areas of declining population, but also factors such as the availability of skilled personnel, cast a new light on this important policy area.

The hypothetical picture of a problem-ridden public service sector is in stark contrast with Finland's strong bid for a leading role in the Information Society, precisely because adequate use and development of ICT could help to solve or at least alleviate some of the problems related to long distances and to serving small numbers of people even for basic services. The out-reaching potentials of ICT are certainly there, especially with the spread of broadband connections, as analysed by OECD in a publication concerning ICT and rural areas (OECD, 2001a). On the other hand, certain authors are supportive of the view that the Information Society could encourage a trend of population concentration in major metropolitan nodes (Castells and Himanen, 2001, p. 64). Admitting that this would be the case, rural areas cannot afford to stay behind in terms of ICT development, thus comforting this trend, with Finland running the risk of being increasingly divided into successful and struggling regions (Rintala and Heikkilä, 2004, p. 165). Successful projects in public service delivery (e-government, e-health, e-learning) in sparsely populated areas in countries such as Canada, presenting similar traits to Finland, underline the adaptability of these technologies and services to such environments (OECD, 2001a).

The main points that are addressed in this section are presented as follows:

- A focus on state-municipality relations, highlighting equalisation measures within the municipal sector, and the role of pre-defined standards within service sectors.
- A focus on the performance of municipalities in service delivery, addressing the question of how more efficient service delivery could be developed.
- Central level and municipal level policies, primarily rural development policy, aiming to develop the local economy and civil society with expected positive effects upon service delivery, by indirect (tax base) and also direct effects.
- Programs impacting access to services in regional centres, by means of urban-rural co-operation in sub-regions and (broadband) ICT connections and services.
- Finally, an assessment of the present strategies for improving efficiency in service delivery, with special attention to the pros and cons related to municipal amalgamations and the potential of deepened inter-municipal co-operation.

Central level policy response

The Finnish policy response to the problems of areas with population decline is twofold: in the regional policy field as well as in the field of Welfare State responsibilities. One general impression of the policy response is that central level decision makers have a profound concern over growing regional disparities in economic development and in municipal finances that may in its turn lead to a widening of regional differences in welfare standards. Regional development policy objectives thus merge with concerns relating to public service delivery with tools such as the above-mentioned RCP and SEUTU programmes, precisely aiming to encourage inter-municipal co-operation at the level of a territory with a coherent local economic and social dimension. Efforts to promote through incentives the amalgamations of municipalities[35], as in the case of Rovaniemi developed further, can also be considered to obey to the same logic. Just like inter-municipal co-operation, amalgamation permits to achieve economies of scale that are useful from this point of view.

There is a firm commitment to the principle of equal welfare provisions and living standards irrespective of geographical location in Finland. Policy responses of stimulating migration from disaffected areas, or an acceptance of lower service standards in these areas, due to the costs of delivery when economies of scale cannot operate, has no political support in a country where the Welfare State ethic is engrained and rural "spirit and origin" are well alive, even amongst city dwellers. In spite of projected demographic changes, all parts of the country are expected to remain populated in the foreseeable future.[36] Although there is population growth in the largest urban centres, particularly in the capital city area, a clear majority of people in Finland consider rural areas better places to live.[37]

Even if people in the areas of population decline are eligible to public services of the same quality as those living in growth areas, the welfare outcome, measured by objective as well as by subjective indicators, may be regionally skewed. Studies based on objective indicators like the level of education, income, habitation, unemployment, and morbidity reveal regional differences, with people in the rural periphery (but definitely not those in rural areas living within commuting distance of urban hubs) as the losers.[38] On the other hand, social capital-resources are more readily available in sparsely populated areas than in cities, with reports of more neighbour contacts and participation in collective and organisational activities (Rintala and Heikkilä, 2004, p. 172). Welfare services and levels also have a subjective component. A study shows that people in the rural periphery have less trust in local and national leaders than people living in cities and in rural areas near cities. In particular, rural periphery inhabitants express distrust of politicians

at the national level.[39] This feeling of being left out of Finland's economic development may in its turn impact the quality of services (*e.g.*, time and resources spent on conflicts and handling of complaints) and the entrepreneurial spirits needed to renew the local economic base. This attitude reveals a "communication gap" with rural citizens that do not have the impression that "rural really matters" although very innovative approaches have been devised to this end.

Population decline, and an increasing proportion of elderly people, is characteristic of large parts of Finland's territory today. The municipalities, responsible for service delivery are experiencing an eroding tax base and will need more transfers from the centre to finance (mandatory) services at the quality level required. The following challenge arises: if more money from the state can be transferred, it is likely that it will contribute to the continual running of very cost-demanding service operations. Two mechanisms will tend to produce this result; first, the national standards to be fulfilled in service deliveries, and second, the readiness of professionals in the service field (doctors, nurses and teachers) to verify that the standards are strictly observed. At the same time, the overall pressure on public finances (pension schemes, pressure for lowering of taxes) makes it very unlikely that a munificent transfer system, favouring people in the periphery, can be politically legitimised and thus maintained. There is not one solution to this problem, but a series of critical points in the complex chain of inputs to the service system that should be examined.

The Welfare State development in Finland has to a great extent been implemented through the fine-grained system of municipalities,[40] as an alternative to giving the task to regional councils, or having the central level running decentralised offices.[41] The choice of municipalities in the Welfare State implementation process has in its turn strengthened the societal role of the municipalities in Finland, as in the other Nordic countries in the post WWII period. Particularly in the periphery, the role of the municipality in the local economy and the municipality acting as an employer, has become very significant and in many cases, dominant.

The mechanism enabling municipalities to develop and deliver mandatory services was until the 1990s based on earmarked grants and a sharing of expenses between state and municipality. For the municipalities in the periphery, this system had some obvious advantages, as extra cost caused by distances, and problems of scale in the delivery of service provisions, to a certain extent would be compensated by transfers from the state. But as to efficiency this system had some obvious weaknesses: first, because of its strictly sectoral character, it resulted in a binding of transfer money to specific purposes, irrespective of local needs and cross-sectoral considerations.

Second, because by the way it operated it produced disincentives to reorganise services so as to improve economies of scale.

The specific-grants system was abolished in the 1993 reform and was replaced by a system of (in principle) one single grant from the state (see Chapter 3), computed on the basis of parameters that the municipality cannot influence to its advantage by political decisions. The following example could illustrate this change: prior to 1993 a municipality could have been rewarded economically by the state for operating village schools with a munificent teacher/pupil ratio. After 1993 the municipality in question would have been on the contrary economically "punished", as payments were from than on computed on the basis of numbers of pupils alone.

The present system has two elements, one related to income equalisation, the other related to a (partial) compensation for expenses in the mandatory service sectors (see Chapter 3, municipal revenue). It is both a policy and political question whether parameters related to distances and geographical location should be included in the construction of state transfers, and what weight should be given to each parameter. This would represent in a way a subsidy covering additional costs due to specific constraints of the environment. In municipalities that cover large geographical areas, expenses will be larger in operating home-based services, and this is an argument in favour of having compensatory measures built into transfer computation. One argument against this would be that a system with a "road length" parameter may be a disincentive to organising a village-based delivery of services, *e.g.*, to the elderly, by training village people in home-based nursing, rather than to have them served from a far-off municipal or regional centre.

When the municipality receives the grant, it is free to use the money for whatever purpose, together with the local income tax, as long as services in education, health, social welfare, etc., are provided at the minimum level set by central authorities. The advantage is that this facilitates reallocation processes between sectors and the municipality's ability to respond to a changing demand structure. Areas of declining population experience decrease in birth rates, and increasing demand for services to the elderly; thus the present system of revenue allocation should be ideal. Another advantage is that in a situation with minimum standards met and revenues exceeding the expenses needed, the municipality is free to choose between spending unused revenue to increase the quality in service sectors, or to venture into new types of policies, *e.g.*, business development strategies. In a situation where municipalities try to attract young families, it could be rational to use such resources to increase quality in day-care or primary education.

One disadvantage of the present system lies in the setting of national welfare priorities. When central authorities wish to prioritise a certain field

and if this field lies within the competences of the municipalities, the state cannot use financial incentives to achieve its objectives within the present system of transfers, but will have to use legislative measures. This means that the centrally determined minimum standards are in fact the only effective way of securing equity in welfare levels in a situation where municipalities or their joint municipal boards are left with discretion over spending transfer money. Even today's system might create very slight differences in welfare standards, but in principle only from the minimum required level and upwards. If standards were lowered or left to each municipality to decide, a widening gap between rich and poor municipalities would most certainly occur, to the disadvantage of areas experiencing population decline. Norway is a case in point, as explained in Box 2.14.

The present system places heavy responsibility on each municipality in allocating resources between activities, only restricted by minimum standards. It is rational for the municipalities operating within this system to seek new solutions when costs per unit are running high, either in the form of lowering down to a minimum (but not below the level set by central authorities), or by innovative action, involving increased use of ICT and/or cross-sectoral arrangements like co-localisations, competitive tendering for some services like cleaning and food provisions, and the involvement of

Box 2.14. **Block grant transfer system in Norway**

The block grants system was introduced in a municipal finance reform in Norway in 1985, with, in particular, the former ear-marked grants to be phased out. In 2003, the block grant transfer amounted to 23.8% of gross municipal income while income from ear-marked grants still represented 12.7% of revenues. The block grants transfer system has not been fully implemented so far as financial incentives from the state level make up about one-third of the transfer volume.

The intended phasing-out of ear-marked transfers halted, due to central level initiatives in specific areas, especially within child care, refugee accommodation and services to the elderly. For reasons of securing accountability, the Parliament is unwilling to add sums to the block grant system when reforms involving the municipalities are to be implemented. The effects however are not dramatic, but the percentage of municipal free revenue dropped from 80% to 70% during the 1990s.*

* Aarsæther and Vabo, 2002: "Unchained and well-managed? Municipal Norway. Samlaget, Oslo (in Norwegian).

Source: Based on information provided by the Ministry of Local Government and Regional Development.

voluntary sector actors in service provisions. In spite of its rational financing structure, the service delivery system is under pressure in the areas in question. There may be several reasons to this.

First, there is a financial problem relating to a diminishing tax base that also needs to be adjusted to per unit costs for services, to obtain when possible economies of scale in sparsely populated areas. The shrinking tax base is an issue facing municipalities experiencing ageing and out-migration (the two phenomena are usually linked), that national authorities seek to compensate for by fiscal equalisation schemes (see further). Concerning allocation of resources to different types of public services, one salient example is that of schools with a decreasing number of pupils. By the way the grants system operates, a reduced number of children will lead to a reduction in transfers. But as children are mainly served by collective means like classes, schools and day-care centres, a per-pupil reduction in transfers from the state will in many cases not be met by municipal savings, as there are fixed expenses per class or per school which may have to be maintained at least for some time. The way school services are provided thus lead to more budgetary pressure in the municipal economy.

In 1990, only 22 schools were closed in Finland, but this number rose to a maximum of 163 in 1993, the year that the block grants from the state replaced the earmarked transfers. The number of school closures remained high throughout the 1990s, but after the turn of the century this trend has weakened (a total of 1 121 closures between 1990 and 2003).[42] This development can be interpreted as a natural effect of adapting to the fiscal freedom produced by the new grants system, enabling the municipalities to redirect resources to more pressing needs, *e.g.*, in serving the elderly. But it can also be interpreted as a sheer cut-back response to a worsening financial situation. The Theme Group on Remote Rural Areas of the Finnish Rural Policy Committee reports that municipal finance in general tightened during the last decade, due to a weakened municipal tax base, and the cuts made to the amount of state grants at the end of the 1990s. According to the theme group, the state's share of financing of expenditures of social and health services decreased from 40% to 20%. The regions of Etelä-Savo, Central Finland and Lapland have the weakest situation in terms of municipal finance.[43]

The second weak point in the system is the vulnerability of the total grant appropriation in the state budgeting process. A block grant sum is politically easier to cut than specified items, in dire financial circumstances. And municipalities in areas of declining population with a weak tax base and thus a heavy dependency on the level of transfers in the state budget will be more negatively affected than "rich" municipalities when central level cuts are made. And even though much goodwill is expressed by central level authorities towards the municipalities with population decline, this attitude

can hardly be expected to be shared by the representatives of the larger urban municipalities striving to make their ends meet. Thus there will be political pressure and a real conflict of interests over the scope of the tax equalisation mechanism. At present, a "rich" municipality's contribution to the equalisation scheme cannot exceed 15% of its total tax revenues (see Chapter 3, intergovernmental and grants). If this is to be respected also in years to come, more responsibility will be placed on the state to make the level of the total transfer correspond to the needs for financing of municipal services.

The third problem with the system resides in personnel skills. To function optimally, the system presupposes an equal availability of qualified personnel at the local level to forecast, plan, and allocate resources in an efficient manner. In particular, highly sophisticated human resources management skills will be required of staff in charge of preparing recruitments, so as to identify new needs and translate these into precise job descriptions. At the level of service personnel, it presupposes flexibility when local level decisions on reallocations of inputs are to be implemented. In the smaller and peripheral municipalities with population decline this certainly represents a challenge. This challenge will also be more and more difficult to meet in the future, with high percentages of retirements for municipal personnel expected within ten years (in the case of Ranua, 40% of employees). This is an important issue that may require, in particular, increased inter-municipal co-operation and more frequent use of competitive bidding for provision of services by the private sector (see further).

Summing up, the state-municipal transfers based on block grants and predefined service standards represent no hindrance in obtaining satisfactory welfare service levels in areas of population decline. A more targeted or ear-marked approach would certainly have some advantages, but the present system's placing of responsibility for the allocation at the local level should be preferred. To improve its functioning, there should be a close monitoring of the parameters and weighting arrangements making up the block grant at the central level, and of the skills and competences at the level of the municipality, including the operating of inter-municipal boards.

Public services: a focus on the municipality

As to the provision of public services, the municipality provides a wide range, from children's day-care, education and health services to care for the elderly. A full overview is presented in Box 3.1, Chapter 3. The range of services adheres to the Nordic type Welfare State model, and compared to Norway a country of approximately the same population as Finland (respectively 4 564 000 and 5 200 000 inhabitants in 2003), which has a very similar local

governance pattern (430 municipalities and 19 regions), the challenges of service deliveries in areas of population decline are pretty much the same.[44]

The municipal income tax is the most important element in the financing of municipalities, on average about 60% of the municipal income is generated by this tax. In rural municipalities, however, only 40% of the income is from this tax.[45] The setting of the tax rate involves local level assessments of the employment situation, of the income level among those employed or earning their income from own businesses, and the levels of the neighbouring areas. Areas with population decline generally suffer low employment rates, and income levels well below the average. But the municipalities in question can hardly respond to this situation by substantially increasing the tax rate to get sufficient municipal funding, because this will only aggravate the problem of out-migration. The tax equalisation mechanism is so calibrated that there is an incentive to stimulate employment and income levels (see Chapter 3, municipal revenue sources).

Organisational challenges

For municipalities in the peripheral regions, a sharp rise in unemployment in the early 1990s led to increased social welfare expenses, and at the same time a drop in income tax revenues. In this situation, the municipalities managed to cope, but by welfare cuts, rather than by developing local welfare policies of their own (Rintala and Heikkilä, 2004, p. 173). Today, the organisational challenge for the municipality is to venture into a more systematic use of modern technologies in administration and in the service sectors, and to stimulate and experiment innovative and locally well-adapted solutions in the production of cost-efficient services. To what extent municipalities with population decline can expect increased transfers in the future remains a question open to debate, with the expectation that taxes are likely to be reduced or at least to correspond to a smaller amount of GDP (OECD 2003a, Table 10).

The system of state-municipal relations places a heavy responsibility on the decision-making structures at the local level. As open democratic processes determine the orientations and competencies of elected representatives, the critical factor in decision making, innovations and implementation capacities rests with administrative leadership and service personnel. The municipalities in question are not expected to attract the most competent and skilled personnel resources, as they cannot offer the professional environment found in larger administrative and service providing staffs. The challenges of administering services in a peripheral municipality are also different from those of larger municipal units. First, cross-sectoral co-operation will be more in focus, and this demands skills in inter-personal relations. Second, the smaller environments demand skills in co-operating

closely, both with the elected politicians, and with local level associations and user groups. On the other hand, there is in Finland a well-established tradition of citizen participation that the government is seeking to sustain (see Chapter 3, Section 3.3), so, in smaller municipalities, such processes are probably less conflictual than would usually be the case.

The availability of personnel competent to manage and run the services depends on several factors. The output of the higher educational system should secure a favourable situation for smaller municipalities, as there will be a shortage of jobs for qualified personnel. However, the attraction of urban centres to well educated young people, and massive retirement as a consequence of ageing within less than ten years, can only aggravate the situation in the future. Thus it will be necessary to render administrative and service positions more attractive than today. National level wage negotiations and a weak municipal economy make it unlikely to use strong economic incentives to attract personnel. In Norway however, substantial success has been obtained by offering an economic premium to newly educated people seeking employment in the Northern Zone (Finnmark region plus municipalities in the northern part of Troms region). In Australia, tax abatements are also consented to attract rare skills to certain areas, in particular qualified medical personnel. These initiatives are beginning to impact on recruitment and retention of doctors in Australia's rural areas, and improving the viability of smaller, rural, remote residential aged care homes.[46]

The quality of in-service training and further education schemes will be decisive to secure improvement of competence levels and to limit turnover in key administrative positions. In the training of administrative officers and service personnel, more focus should be directed towards flexible, innovative and locally adapted solutions, rather than on the implementation of service delivery models developed to function in urbanised and large scale contexts. Also a bottom-up-approach to the utilisation of ICTs, combined with mobile technology in service deliveries should be encouraged as part of the in-service training schemes. To provide this type of training will be a challenge requiring co-operation with the universities and polytechnics in the regions, developing new applications corresponding to the specific needs of inhabitants in areas of low population.

Service points, mobile libraries: innovative responses

The establishment of public service points is another innovation in service delivery that deserves attention: one point can handle information from many different administrations and agencies at different levels and facilitate the accomplishment of basic formalities. Central government, regional, and municipal services can thus be physically integrated, at least at the level of being served with information by people used to handle all types

of requests. The on-line equivalent of the service point is an Internet portal opening access to many different services. In both cases the principle is "one-stop shopping", making things much easier for the user. The service points however can hardly be the places where the "heavy" servicing of people is carried out, in the form of educational and health services, but the idea of people having one single place to seek information on public services has a solid basis, particularly in rural areas where delivery can be costly. In Finland, service points emphasise the municipality as a cross-sectoral institution acting for the welfare of all its citizens. A specific programme has been designed to facilitate their establishment (Box 2.15). However, an evaluation of Service points by the University of Lapland (1999) reports rather small cost-savings.

When discussing the merits of service points, one should have in mind however that information in the form of visual contact, of support in filling out forms, etc. increasingly will be possible to give by ICT and directly home to the person. For many users, a well-working, updated and interactive homepage on the Internet will be far more important than a physical service point, in dealing with municipal and other public authorities. The issue here is also one of availability of skills as such a service requires competent personnel, usually younger and motivated people with the necessary savvy and capable of being able to collect all relevant information at the local level, regularly up-date it and present it in an attractive and user-friendly way. Also, ICT based services should be conceived in a comprehensive way instead of just adding an ICT component to the traditional service. For obvious reasons, such Web sites

Box 2.15. **Citizen Service Points**

To facilitate citizen contact with public offices, a Citizen Service Point project was launched in Finland in 1993, comprising 15 units. Today 210 Service Points are operated, both in the cities and in the periphery municipalities. They are co-financed by project funding, and by contributions from the participating municipality, regional, and central level agencies. Citizen Service Points are under the responsibility of the Ministry of the Interior for co-ordination, monitoring and reporting purposes. At the regional level, these service points are co-ordinated and supported by the State provincial Offices. Service points are located so as to maximize physical access to the citizens of a municipality, and are typically organised in municipalities between 2 000 and 7 000 inhabitants. In addition to services offered by the municipality, the Service Points offer services, in particular, from the tax office and the KELA social insurance agency.

Source: Based on information provided by the Ministry of the Interior.

serve their purpose when they are wider area portals, implying that they be under the umbrella of joint municipal boards or at least be the result of specific co-operation between certain municipalities. Such a vision, determined by user needs, also corresponds to greater financial capacity towards recruiting and motivating skilled personnel working for a larger area.

To summarise, in the delivery of services in areas of population decline, an organisation based on integration of functions will be needed, with a combination of physical presence of certain services in centres, mobile services and virtual ones. Multi-functional rural walk-in health centres on a municipal basis or by inter-municipal co-operation are a good example of how to organise welfare services and are well developed in Finland. While service points mean that people travel into the centre, other services may be organised on a mobility principle, with personnel travelling to serve users and clients. Home-based nursing operates on this principle and resort to mobile Internet solutions such as consulting at distance a medical file. In addition some municipalities have organized mobile libraries to serve users at the village level. The rise in the number of such arrangements during the last decade reflects a reduction in the number of localised library departments, due to both population decline in the villages and the need for cutting expenses.

Services to the young: education and day-care centres

The educational sector and the care for old people represent the main challenges for the municipalities, both in terms of finance, manpower, and societal importance. As late as the beginning of the 1990s, more than 60% of Finland's lower-stage schools were 1-3 teacher schools.[47] Since that time, there has been a trend of closing village schools. In Lapland, a total of 123 schools have been closed since 1990, and the corresponding numbers in the regions of Kainuu and Etelä-Savo are 86 and 91. It is interesting to note that school closures in the two richest regions in Finland, Itä-Usimaa and Åland, have hardly occurred in the same period (eight and two closures, respectively), probably because the population has remained stable or even increased.

Parents always strongly defend the local school, and local officials usually try to keep a structure of easily accessible school services, especially for the youngest pupils. The loss of a local school may render the local environment much less attractive to families with children, and the basis for shops and other services will be undermined. For the children, long transportation distances are definitely negative, while attending a larger educational environment may be a positive factor. In all cases, contemplated closure of a school, as that of any other public service in rural areas, can have long-term damaging effects with unforeseen consequences on local society and economy. It is advisable for this purpose to provide for ample debate before

taking such a decision. In Australia, recent policy measures by the Government of South Australia to introduce "Regional Impact Assessment Statements" render the debate compulsory, with adequate publicity being given to the effects, direct and indirect, over a long time frame. The purpose of the assessment process is to provide an opportunity for inter-agency co-ordination, and community consultation to inform decision making. These factors taken into account, municipalities can consider, for the outlying villages where a school closure would have a clear negative impact, the following options:

- To allow private schools to be run by a village association, on the basis of experimental or alternative pedagogic models (Montessori or Steiner models), which is possible in Finland on the basis of a Ministry of Education authorisation. In Norway, the state will cover 85% of running costs of schools operating in this mode. This means additional inputs in the form of voluntary labour or payments from parents to comply with national standards. For the municipality this may alleviate the budget, while the ministry will have expenses marginally increased. In total, contributions in kind make up a favourable balance for the public sector at large.
- To fully exploit the potentials of co-locating children's day-care centres and schools and of merging schools located close to municipal borders with the nearest school in the neighbouring municipality. Rural development policy seeks to encourage such co-operation, after thorough investigation of the issue in one of the multi-sector theme groups.

Services to the elderly

Elderly people are a "black box" challenge to municipal service provisions, because even at the level of the municipality there are many actors involved, and a whole range of models and practical solutions are in operation; informal, voluntary sector, public, and commercial. The field itself may not appear volatile at the level of the municipality but it can display striking variations within an area of declining population as to health conditions, life time expectancies, social integration, migration of elderly people (in and out) and preferences for types of care. Also, in social and economic terms, difficult decisions are at hand concerning the type of services best adapted to specific situations, with subjectivity eluding here more strict administrative, financial or statistical criteria.

Everyone will agree that making elderly people manage on their own, whenever possible, is the best solution. But prolonged good health and longevity may backfire in the cost-demanding forms of care needed if people manage well on their own until 90, but from then on need constant care over the last decade(s) of their life. Planning, standardisation of policies, and

forecasting is extremely difficult, but the demographic trends are univocal, and especially so for municipalities with population decline. The challenge will in practice boil down to how to serve the widowed woman in her 80s, living alone in her own house far away from the municipal centre, and becoming increasingly dependent on help and care. In this respect, documentation from Norway shows a dramatic variation between rural municipalities in the use of cost-demanding institutionalised care: among inhabitants over 80 years the proportion living in homes for the elderly vary between 2% and 67%.[48] Obviously, local cultural traditions and the availability of informal and family support vary, and at the level of the municipality, flexibility and co-ordination of the services for the elderly will be of great importance.

From a cost-efficiency perspective, the municipalities have much to gain by investing in self-help schemes at the level of the individual (health promotion for the elderly and assisting people in adapting their homes), at the self-organisational level, by facilitating the construction of private, co-operative homes in the municipal centres, and further, by having home-based and institutionalised care integrated so as to be able to obtain maximum flexibility. Like in the school sector, some of the municipalities in question may face an economic problem by running several, small homes for the elderly, due to the settlement pattern. Like in the school sector, the municipality may venture into partnership arrangements with village level associations, if people at that level are strongly opposing the closing down of a local institution that cannot be run cost-efficiently. The ultimate solution in this respect would be the cost-free transferring of a home, to be run on either private or co-operative basis, thus alleviating the municipality from some economic burdens. On the other hand, many of these villages may be inhabited mainly by elderly people with low pensions, so the organisational and economical resources for self-help in elderly care may be lacking, thus placing a continual responsibility on the municipality.

Faced with increased expenses related to expanding demand also for institutionalised care, municipalities have to look for ways of coping economically. Due to the dominant role of the municipal organisation in the local community and the small scale of settlements, it is hard to imagine that a market for delivering care services on a commercial basis will emerge, even if the municipality goes for competitive tendering in running of homes for the elderly or for home-based care. Experience from competitive tendering in elderly care in the Nordic countries has so far shown that the gains in economic terms are small, if contract and monitoring costs on the municipality's part are included. This is hardly surprising, given that wages are nationally negotiated, that the service is heavily in-person based, and that retrenchment in the overall public sector have led to cutting costs wherever possible, during the 1990s. Further, the well-being of the elderly is not affected by private or

public running of an institution. Rather, the most salient finding from comparing public and private running of institutions lies within staff satisfaction. Perhaps contrary to expectations, the nurses and other personnel report more satisfaction with overall work conditions when a private company is responsible for running an institution.[49] In itself this result is highly interesting, and experiments with private and partnership organisations should be encouraged, even in municipalities where there is a firm commitment and a preference for public services arrangements.

Services to the elderly represent labour-intensive work, and a substantial part of the task demands semi-skilled and unskilled labour. In municipalities, growth of the elderly care sector translate into much needed employment opportunities for women, from unskilled cleaning tasks to semi-skilled and skilled nursing practices, including medication. Municipalities with good reputation for elderly services should be encouraged to build on this competence to stimulate local economic development in the commercial parts of the elderly services sector, offering a close to nature and safe environment to in-migrating pensioners. Recent policy trends build up on this recognition, with the Target and Action Plan of Social and Health Care for 2004-2007 aiming at the over 75-year-old segment,[50] planning a substantial increase in home services (see Table 2.2). The corresponding total budget expenditure for these measures is approximately EUR 11.6 billion, with state grant amount representing close to 33% managed by the Ministry of Social Affairs and Health. In the "Finnish model", measures for the elderly are also taken in consultation with those concerned: the 300 or so "Elderly Committees" across the country bring together senior people, the municipality and associations in preparing projects concerning that age segment.

Innovations in the elderly services sector are needed. There is already much R&D work in the "well-being" sector in Finland.[51] ICT-based monitoring, communication and alarm systems are now implemented in many municipalities. Elderly people of tomorrow will to a much greater extent

Table 2.2. **Target and action plan of social and health care 2004-2007 (75+)**

Service	The number of people benefiting from the service	Percentage of 75-year-olds or older	Targeted percentage of 75-year-olds or older
Home services	68 986 (households)	18.7	25
Support for relatives	12 938	3.5	8
Service housing	20 270	5.5	3-5
Houses for aged people	16 735	4.5	5-7
Institutional health care in health centres	8 709	2.4	

Source: Association of Finnish Local and Regional Authorities.

become used to handling PCs and mobile phones, thus facilitating contact and combating problems of isolation. The Nordregio innovations study (2004) investigated the innovation potentials in six Lapland municipalities, with a total of 29 public sector innovations registered in the survey part of the study.[52] A closer study of the most promising innovations in the six municipalities revealed systematic utilisation of scientific research results, combined with entrepreneurial spirit and networking involving partners and contacts at all levels (Aho, *et al*. 2004). The targeted areas of innovations and specific solutions worked out varied however to a great extent, depending on the strength of the private sector in each municipality, and in each village.

The complexities of the elderly sector, together with its large share of the expenses of the municipalities require constant and competent monitoring, flexible responses to changes in demand and an awareness of the technological and organisational possibilities for improvement, for additional financing, and for cutting expenses. The inter-sectoral working principle of the municipality is assessed as a clear advantage to finding adequate solutions, assisted by experimenting and bench-marking practices. Budgetary pressure, both on the national and local level will necessarily stimulate the search for innovative organisational and technological solutions within individual municipalities and joint municipal boards intervening in service delivery. Ageing is considered both a challenge and an opportunity for which Finland is certainly better prepared than other countries in a recent report issued by the Ministry of Social Affairs and Health.[53] As seen above, there is certainly a wealth of useful experiences across the country and systematic publicising of these would be very useful.

Policies for rural Finland: relevance to service delivery

Much attention is directed towards attempts at improving the economic base of Finland's periphery, and in particular, in areas of declining population, including through programmes presented in other parts of this chapter and having a wider focus, such as innovation policies or those of the Regional Centre and Centre of Expertise programmes. The expectation is that a long-time downward spiral effect can be replaced by local economic growth and thus improve the base for public services, by the mechanism of local income taxation. According to the 1995 Law of municipalities, these have a broad responsibility for the well-being of their citizens, and it is for the municipalities themselves to decide how to promote local well-being, as long as they fulfil their mandatory obligations in the fields of social welfare, education, etc.

The rural policy doctrine is defined within the Regional Development Act of 2002, acknowledging that even well functioning growth centre development is not sufficient, because there are logistical problems of reaching out to all

rural areas, and because some peripheries have experienced the opposite of a trickling-down effect by urban growth processes. The complementary "rural" doctrine, aiming to stimulate growth in rural areas, has been implemented as The Rural Policy Programme, a "special programme" within the Regional Development Act. The 4th Rural Policy Programme has been approved by the Finnish Government, for the period 2005-2006.[54]

Particularly in terms of service delivery, new co-operative forms between partners in public, civil, and commercial sectors are seen as solutions to the problems faced by an "overloaded" municipal economy (Mustakangas and Vihinen, 2003, p. 177). This means that the Rural Policy programme's contribution to solving problems of service deliveries may be threefold:

- First, by improving the financial base for services, to the extent that new commercial initiatives lead to increased employment which can be taxed.
- Second, by the nature of the solutions worked out in the area of service deliveries, where combined efforts by different actors can alleviate the financial and organisational burdens of the municipality.
- Thirdly, a latent contribution will be that of creating overall social capital at the level of the municipality as a result of local level experience and learning from co-operative projects.

Within the first three national programmes, a series of objectives were specified, and a high percentage of these have been successfully implemented (Rural Policy Committee, 2004, p. 18). Rural policy interventions thus may have had a substantial positive impact on service delivery in areas of population decline, but only to the extent that the doctrinal formulations address the key issues, and to the extent that the practical measures undertaken produce the expected results. Rural programmes have been in operation since 1991, but an overall effect in the form of stabilised demographic development in most rural areas[55] has yet to occur. Also regional disparities in welfare standards have grown in the period (Rintala and Heikkilä, 2004, p. 176). Of course, structural trends in economy and culture, and financial problems for the municipalities, may have outweighed the positive contributions to rural development made by the three rounds of Rural Policy Programmes, but there are also certain aspects of the implementation of the policies for the development of rural Finland that deserve a closer scrutiny.

Services at the village level

The question of whether Rural Policy Programmes address key issues pertaining to service delivery commands a positive answer. Tasks prioritised in the sections "Maintenance and construction of basic services" and "Raising the level of know-how" in the 4th Programme (Rural Policy Committee, 2004, p. 36-37) are exemplary. Such is the case of the following measures: a support

system for small schools, development of multi-care services and the support system for village shops developed into a system for multifunctional services (Rural Policy Committee, 2004, p. 36-37). The potentials of the single village shop should be better utilised in areas of population decline. Even though most today are chain stores, there is room for experimenting with shops as municipal, net-based information centres and postal services. A move from subsidising village shops to offering training of shop-owners in multifunctional operations has been made within Norwegian regional policies, and should be considered.

Today's village development strategies include initiatives in the service sectors. Increasingly, municipal actions move from regulation to flexible in-person services while the people organised in village associations and farm households are initiating service enterprises that may complement the municipality's service policies. This is the approach taken both by the Village Action Association of Finland and the LEADER Local Action Groups. The former is a very active voluntary organisation receiving public funding support (see Box 2.16). As for LAGs, there are 59 different ones in Finland covering all rural areas. The positive role of LAGs in terms of citizen involvement and definition of small innovative village projects with economic and social impact is generally recognised across Europe. One salient example would be a former private farm being converted to care and educational institutions for young people.

Box 2.16. **The Village Action Association of Finland**

The first village groups started to form in the 1960s, as a response to rural depopulation processes and the national organisation was founded in 1981. By 1990, over 3 000 village committees were in operation. After Finland joined the EU, the Association was reorganised as SYTY in 1997. It has since been co-operating closely with several new programmes for rural development (LEADER, LAG, POMO, ALMA). By 2003, 2 200 "village committees" (out of a total of 3 900) are registered as associations. The purpose of the village committee is to provide co-ordination and to focus on development of the village as a whole. The SYTY functions as an umbrella organisation, with all the 59 LEADER Local Action Groups among its members (Halhead, Vanessa (2004).

The association brings together 40 000 volunteers in 2003. Public project funding represented EUR 31 million and independent funding 3.2 million. Altogether, activities of the association cover areas where more than 2.5 million Finns live, more than half of the country's population.

Source: Based on information provided by the Village Action Association of Finland.

In order to help securing new services in rural areas, a new model of "Rural Agreements", contracted by local action groups and village associations, has been introduced. The main purpose of the model is to pool and canalise resources. Another example of "creativity" in rural policy is the Women's resource centre "Karelli" in Northern Karelia: Finland Karelli is a limited company, the main targets of which are to act as a development and information centre for women's entrepreneurship, plan and implement projects which enhance women's entrepreneurship and employment opportunities, build women's local, regional, national and international networks and act as a tool for regional development. The Karelli centre was rewarded a prize for innovative action in 2002.

Delivering certain types of services is not necessarily only a challenge but can represent an economic development opportunity under certain conditions. Thus, senior citizens can be considered as a target group in helping to foster economic development. Ristijärvi, a peripheral municipality in Kainuu, has created a specialised and adapted living environment for senior people with economic development strategies specifically focusing on the production of services for the elderly. Activities in this "senior pole" include feasibility studies for operational requirements in senior areas of residence, sketching development processes for activities responding to senior needs and creating business opportunities built on the characteristics and requirements of this age group.

Policies of access and service delivery: ICTs

Policies of access are crucial to most areas with population decline. Studies show that people living in rural areas within commuting distance to regional centres are the ones to reap the growth and welfare dividends in today's Finland (Rintala and Heikkilää, 2004, p. 171). Policies of stimulating a more fine-grained centre structure, technology programmes and universities/ polytechnics' third task, are meant to benefit also people living in the disaffected areas. One issue highly relevant to the access aspect of service delivery is the implementation of adequate ICT network infrastructure, namely broadband. Concerning broadband, the Rural Policy Programme has as one of its aims that every village should be connected by 2007 (Rural Policy Committee, 2004, p. 30). Contrary to many other countries, Finland has chosen to develop broadband infrastructure in a highly decentralised fashion, leaving it to the responsibility of regions, joint municipal boards and municipalities to envisage and adopt the most appropriate strategies and financing modes in conjunction with the operators, on the basis of estimated needs of firms, public services and households. Due to cost of infrastructure, the region is the territory of reference and each regional council is obliged to adopt its strategy.[56] One of the positive effects is that rural connectivity projects have

strengthened collaboration between municipalities and fostered partnerships between public and private actors (OECD, 2003b).

In Lapland, the regional council has developed an Information Society Programme catering to the needs of the different types of users, both public and private, indicated above. It comprises specific actions to anchor the ICT and innovation capacities of firms in Lapland while supporting increased use of ICT for service delivery. Sensitisation and training are part of this programme. The infrastructure component aims to connect the 22 municipalities in Lapland by 2005-2006, covering 95% of the population, which is quite remarkable, due to the very low population density. It is contemplated that the network will be rented from the operators. In certain municipalities, such as Ranua, a gradual reach out-strategy of broadband connections has anticipated this by direct connection to the already existing main backbone that serves Rovaniemi. Fifteen villages in the municipality out of 23 already have access to the network.

The gains within general informational services and communication with the municipality will depend on the training and skills provided, especially involving elderly people living in rural areas, so that the potentials are fully exploited. In this respect, as elderly people will be increasingly comfortable with utilising ICT, this can reduce physical transportation and save time and expenses for the municipality. Within primary education, ICT could be essential to have a municipal village school operating on a partnership basis with a village association, instead of being closed down. This may be organised on the basis of e-education two days a week, with volunteers from the village association assisting the children at work with their PCs. The saving as to teacher inputs may be substantial, while time municipal responsibility is maintained and the school profits from close ties to civil society.

Software adapted to the needs in the service sectors, including education, and further integration of mobile communication tools will make living in the rural areas less burdensome, and enhance the competitiveness of these areas for people on the move. The change from yesterday's situation will be the escape of being "switched off from the rest of Finland". Even if adequate ICT infrastructure coupled with "Internet literacy" cannot be a panacea to stop the depopulation of a peripheral area, nevertheless Finnish projects, as those undertaken in other countries (OECD, 2001a) to bring ICT solutions to people living in rural areas have shown some remarkable results, especially in Upper Karelia where systematic training of village people has been provided together with the deployment of technical facilities.[57] Also for private service delivery, e-shopping may be facilitated by closer co-operation between local shop-owners, the postal service, and Internet retailers. ICT can function as an important mediating link not only to municipal and regional centre activities,

Box 2.17. **Sami language education by ICT**

Enontekiö (population 2 000), is located in the Fell Lapland sub-region. The municipality is home to Sami people, with teaching Sami language in school involving only a small number of children and few skilled teachers readily available. Other pupils and students also learn the Sami language in Helsinki. Bringing these groups together by video and Internet-based co-operation has made the delivery of this service more viable, while offering adequate availability of quality teaching resources. This co-operation has been mediated by the University of Helsinki, which operates a biological research station in Enontekiö, well equipped with ICT facilities. This programme, which has been going on since 1994, has since been used by at least one other municipality (Aho *et al.*, 2004, p. 208).

Source: Aho *et al.*, 2004.

but it also facilitates access to resources and services located elsewhere, with a direct bearing on the well-being or development of remote communities, as the Box 2.17 example demonstrates.

Evolution of local government and public services

The co-ordination complexities in the services field between municipal policies, rural empowerment strategies, and infrastructural policies and programs managed at different regional levels have already been pointed out. This complexity makes it hard to assess the merits of any specific policy instrument affecting service delivery, as there is permanent interaction between these. In the future, the areas in question will have their services organised in a variety of ways, involving public, civil, and private sector actors. For the municipalities there is just one alternative. Some municipalities will merge into larger units, while others will continue in their role as small local government units. Both small and larger municipal units however will have to pursue and strengthen inter-municipal co-operation. It is worth noting that Sweden, with much larger municipal units than Finland, is at present already urging its municipalities to increase mutual co-operation.

Amalgamation pros and cons

As other Nordic countries, Finland has adopted a top-down incentive policy to stimulate municipalities to amalgamate, to achieve economies of scale in service provision and save expenses by rationalising administrative functions. Basic services like day-care, schools and elderly homes are not likely to be affected, by making larger municipal units. Respecting the value of local autonomy within the framework of a nation-state, Finnish as well as

Norwegian central authorities (but contrary to recent developments in Denmark) have been reluctant to impose legislation changing municipal structure by parliamentary decisions. The Finnish incentive is in form of a bonus programme of EUR 35 million per year (2005-2008) to benefit municipalities that voluntarily choose to amalgamate. This scheme has been in vigour for more than 15 years, but very few municipalities in the areas of population decline have responded positively (OECD (2003a), p. 73). One obvious reason is that municipal leadership itself has interest in keeping jobs and political positions. Another is that job opportunities offered by administrative tasks are among the few competence-demanding jobs in the area covered by a municipality, so there is strong popular support to keep these job opportunities as one of the few mechanisms attracting well-educated people.

Amalgamations in these areas will certainly produce some economies of scale, and more attractive work environments for professional staff, but at the same time the structure of service delivery will have to take the settlement pattern as given, at least for a long time period, and in this way an amalgamation may produce savings but also increased costs related to transportation. Besides, some of today's well-functioning but small municipal centres will drop below a viability threshold if the administrative functions are transferred to a larger centre, and there is a risk of closing down shops and other private services so that people may experience the amalgamation as a net welfare loss.

The costs of changing a system that local people politically defend are worth taking into account. Identity factors may seem irrational from a strictly economic point of view, but at least for a time period amalgamations may lead to less efficiency in cases where the identity factor has in fact lubricated the service, administrative and political machinery in the smaller municipal units. The present financial incentive to amalgamations however prevents a lock-in situation in cases where people at the local level find the services provided to be of a too low quality. Finally, there is the risk of a worked out amalgamation scheme to be destroyed by one unit opting out in a late stage in the process. This risk operates as a disincentive to embark on lengthy processes of preparing voluntary mergers, particularly if the local political situation presents contrasts rather than homogeneity.

On the other side, the gains from municipal amalgamations are obvious, because the merging of municipal administrations into one will produce increased administrative efficiency and less overhead costs. Few positions however will be superfluous, so that direct gains in manpower saving are not very likely to occur, at least not in the short run. But the "new" municipal centre will be strengthened by an amalgamation and can perhaps hope to attract more advanced services in the private sector. Some services, like technical infrastructure, planning and specialised health and social services

will also profit from operating in a larger municipal environment. This is the prevailing logic in two cases in Lapland. The coming merging of Rovaniemi with the Rovaniemi Rural Municipality[58] into a more coherent centred region may enhance service quality. A similar process in the urbanised part of the Kemi-Tornio region may also produce some improvements in the quality and financing of service deliveries. In the Rovaniemi case, it should be noted that a sub-municipal council located in a village of the former rural municipality with responsibilities for educational and social services will be established as a consequence of the merger.

Strengthening inter-municipal co-operation

With a large number of small municipalities expected to offer a wide range of welfare services, inter-municipal co-operation is an obvious alternative. Finland's municipalities engage in inter-municipal co-operation in a series of sectors (see Figure 3.11, horizontal co-ordination). Among the 240 joint municipal boards there are only a few in business promotion, while the important service sectors (health, social and education) are the most common. The tendency of joint boards to take on new member municipalities is interesting, because it illustrates the flexibility of this form of governance.

Inter-municipal co-operation may be organised on a more structured basis, in sub-regions (Box 2.18), or it may be tailored to specific needs and possibilities according to the service. There are gains to be obtained by both strategies. The argument in favour of a structured co-operation within the framework of a sub-region is that it may be the first step in a process of amalgamation. Also, there will be gains in the form of a possible co-localisation of administrative staff and functions for several co-operative efforts. The argument in favour of co-operating with different partners for different purposes is increased flexibility in the pursuit of the most cost-effective co-operation set-up. With the utilisation of ICT, co-operation between municipalities will not necessarily be restricted to the immediate geographical area. Seeking out partners irrespective of geographical location could stimulate more innovative behaviour than the systematic directing of co-operation to one's geographical neighbours.

The organisation of inter-municipal boards with responsibility for running the services seems to be a viable way of finding solutions to economic problems and the utilisation of investments and manpower. The boards are made up by representatives from the participating municipalities, and this type of political representation has some advantages, especially as this helps to maintain a constant awareness in the wider political environment on questions of sharing costs and benefits on a fair basis. This organisational mode may certainly have its disadvantage in the form of offering little leeway

Box 2.18. **Sub-regional co-operation in Ylä-Savo**

Ylä-Savo (main town: Lisalmi) is one of the sub-regions in North Savo, a region of Eastern Finland. The sub-region has a population of 61 000 inhabitants in eight municipalities in an area of more than 8 000 km^2. The sub-region is participating in the Regional Centre Programme. In this sparsely populated rural area (Agriculture and forestry represent 18% of the workforce, industry 25% and services 57%) with declining population, co-operation for the provision of public services is indispensable. At the sub-regional level several consortia have been formed to deliver different services. The first one was launched in the 1960s in the area of vocational education, now including agricultural education. The Ylä-Savo Regional Consortium for Public Health started operation in 2004. It was founded by four of the eight municipalities with others purchasing the services. The drivers were both cost saving and quality improvement. Waste management and water supply are also areas in which sub-regional public companies have been formed. The Ylä-Savo sub-regional broadband network, to be completed in 2005, is another venture in public infrastructure lay-out, partnering with operators.

The scope of sub-regional co-operation is no obstacle to specific co-operation between certain municipalities that consider that mutual interest justifies co-operation in other areas than those covered at the sub-regional level. For example, the adjoining municipalities of Keitele and Pielavesi decided in 2004 to co-operate to offset the effects of a negative migration balance that narrows the financial margin of each. An advisory committee comprising public and private representatives from the municipality but also from the TE Centre of North Savo is to devise a common marketing strategy for which EU financing will be applied for, so as to create new jobs to prevent migration and hence the shrinking of the tax base. Co-operation also concerns in particular education and culture (one single organisation), the environment (common board) and social and health care (mostly care for the elderly).

Source: Based on information provided by the Sub-region of Ylä-Savo.

for strategic leadership, but it is in line with the Finnish tradition of co-operation and consensus seeking.

Dynamic municipalities

Maintaining dynamic municipalities is of crucial importance, because at the local level this institution is created with the specific purpose of handling complexities, and to have a legitimising function underpinning the solutions chosen or developed by the electoral mechanism. The complexity of the policy

environment surrounding local actions and initiatives can hardly be expected to be reduced in the future, and thus the power to "make sense" out of this multitude of policy measures will rest with the democratically elected local government leaders and their administrative counterparts.

It may be hard, but not impossible[59] for the smaller municipalities, often covering vast geographical areas, to fill the role of local developer and provider of at least the basic services demanded.[60] In contrast to the working style of a small-scale municipality, the doctrine of the Welfare State has been one of providing well-defined services, organised on the basis of specialisation and sectorisation. From the start of the Welfare State expansion, there has been a conflict between a rural type responding to needs and problems on the one hand, and the idea of delivering professional services by specialised departments on the other (Pyy and Rannikko, 1995, p. 144). The "multifunctionality" principle of rural working life is reflected in small municipal institutions, with close contacts between politicians and staff, and between different types of specialists. The financing system lends itself easily to this way of responding to local needs, and some of the problems in the service sectors may stem from an insufficient economy, with difficulties in recruiting competent personnel also having stronger impact in the future.

The requirement to take into account evolving public service delivery needs in a cost-efficient manner leaves little room for manoeuvre: the best answer is in productivity increases. In the Basic Services Programme (BSP) established in 2004 and covering the 2005-2008 period, a document evaluating the balance between municipal welfare services and public funding is now part of the annual decision on central government spending limits which include grants to municipalities. This document includes a chapter on efficiency and measures to raise it. The BSP is part of a far-reaching government programme to increase productivity in the public sector (see Chapter 3, Section 3.2). On the other hand, the Basic Service Programme contemplates rewarding increased efficiency by a "significant rise in state aids … related to extra investments in social and health as well as in education services". The same programme takes into account that the numbers of pupils in Finnish schools will drop by a number of 34 000, thereby creating a surplus of EUR 90 million from 2005 to 2008. Pursuing goals of increased efficiency in public service delivery, the Government launched in May 2005 a project on municipalities and service structure. The aim is to ensure that services provided have a firm structural and economic basis, taking into account quality and accessibility of services as well as, effectiveness and technological possibilities in service production. It is contemplated that a legislative proposal will be discussed in 2006 for implementation in 2007.

Increasing the efficiency of service deliveries by competitive tendering

Increasing the efficiency of service delivery by competitive tendering and by a voucher system enhancing freedom of choice may be an option to municipalities as well as in inter-municipal co-operation. A study of the orientations of a total of 39 municipal office holders and elected leaders in four South Ostrobothnian municipalities (area of population decline) reports that leaders are willing to consider alternative suppliers of services and to study their ability to cope with the tasks.[61] However, in areas with few clients and high transportation costs, markets for services are unlikely to function. To secure an efficient provision of services, the competition for funding by the cross-sectoral budgeting model should in principle be sufficient, but in practice this is often not so. Proceeding to cuts and budgetary reallocations is not the same as innovating within and across service areas. Innovative approaches to service delivery need to be continuously stimulated and best practices highlighted and disseminated.

Summing up

The task of assessing results of municipal, regional and central level initiatives to improve access to, and the quality of, services for people living in areas of declining population is problematic, because of local level variations, and that the usual criterion for assessing success is demographic development. Thus it would be valuable to have updated research carried out analysing the factors underlying transition from population decline to population stability in the areas where this has occurred. Research on rural development in the post-industrial era in Nordic contexts show that local engagement in activating social capital by local democracy and outreaching networking, as well as entrepreneurial spirit, are pivotal. This is particularly the case when the economic base is not sufficiently modernised or employment is supported by the localisation of public institutions (Bærenholdt, J.O, 2004).

Moving from specific areas of interest to the overall assessment of Finland's performance as to securing geographical equity in service delivery, the question is whether or not the present public service delivery model is sustainable in economic terms in areas of population decline. At present, the high level of standards, equalisation grants, and the expectation of special state interventions if a financial crisis occurs at the local level, are likely to lead to higher expenditure if the present population trends are not reversed. To counter these trends, the following options could be considered:

- Make room for people moving in. Policy measures are needed to stimulate young families moving in to take up key position in municipal services and administration.

- As long as there are no signs of a crisis looming over the overall Finnish economy, the existing model of state transfers to municipalities, with pre-defined standards as a control mechanism, with minor improvements, appears well proven.
- The improvement potentials lie primarily within the area of increased inter-municipal co-operation, and in some of the areas to push for amalgamations.
- Develop in co-operation with universities and the Association of Local and Regional Authorities, training programmes for elected officials, administrators and service personnel to address the multifunctional and innovative aspects of service delivery.
- Accept complexity. Providing services of high quality in a cost-effective manner cannot be based on one organising principle. If the present model is taken as a point of departure (since results are satisfactory, there are good reasons to do so), some of today's problems could be met by strengthening ICT use[62] and benchmarking practices in some key areas while allowing, within mandatory services, for more experimenting in alternative ways of providing basic services.

Notes

1. In May 2005, eight out of ten ministries had finalised their regional strategy.
2. Regional Management Committees manage these implementation plans (see Chapter 3).
3. The regional land-use plan has a steering effect on municipal master planning.
4. Evaluation by Tampere University: Kaupunkiohjelmat kaupunkipolitiikan toteuttajina. Kaupunkiohjelmamenettelyn arviointi 1999. (Urban programmes as tools of urban policy. Evaluation on urban programme procedure.) Editor: Ilari Karppi. Publisher: Ministry of the Interior 2000 (Urban Policy Committee).
5. Urban regions of Helsinki, Tampere, Turku, Oulu, Jyväskylä, Kuopio, Lahti, Lappeenranta-Imatra and Vaasa.
6. Kauhajoki (2003 population: 14 591) in South Ostrobothnia was not retained as a formal member of this network as it does not constitute a coherent functional labour market area. A network pilot, with RCP support was however set up because of project quality in a rural area context: in particular, creation of business opportunities, strengthening of entrepreneurship, improvement of knowledge capital.
7. "The cleavage between Helsinki interests and the rest of the country is becoming a major issue to manage for the central government", A. Haila and P. Le Galès, 2002.
8. State grants, received for health, education and social purposes, were in 2003 superior to the equalisation grant based on tax revenues which is traditionally negative for Helsinki. Moreover the evolution between 2002 and 2003 consists in a radical shift: from EUR 118 899 217 paid by Helsinki to the State in 2002 to EUR 7 706 662 received by Helsinki from the State in 2003.

9. State grant statistics for Helsinki Metropolitan Area

	2001	2001	2002	2002	2003	2003
	1 000 EUR	EUR/capita	1 000 EUR	EUR/capita	1 000 EUR	EUR/capita
Helsinki	–51 951	–93	–118 588	–212	7 756	14
Espoo	–46 807	–216	–78 940	–356	–65 523	–292
Vantaa	23 626	131	25 153	138	40 719	221
Kauniainen	706	83	–3 218	–375	182	21

Source: Ministry of the Interior.

10. Operating areas formed by adjacent municipalities within the sphere of influence of the Helsinki Metropolitan Area (the Central Uusimaa and Lohja regions) will be supported to reinforce the development of the greater Helsinki area.

11. Based on Rapporteur ad int. Jussi-Pekka Alanen's proposals.

12. According to the vision of Helsinki Club II, the "Helsinki Region is a continuously progressing business and innovation centre at world-class level, based on science, arts, creativity and learning capacity, the success of which benefits all the region and all Finland". Helsinki Club proposes four strategic priorities and 14 key projects under these. The priorities are 1) strengthening competence and innovation capacity, 2) improving the quality and quantity of housing, 3) making welfare services more efficient and 4) increasing the position of Helsinki as an internationally well-known place as well as increasing the international interaction.

13. The objective of the Urban Community Initiative is the economic and social regeneration of urban neighbourhoods in crisis as well as the promotion of sustainable development. Finland's only Urban Programme is being implemented in Finland by the cities of Helsinki and Vantaa. The targets of the Urban Programme are: 1) promoting the attractiveness of the target area, 2) enabling participation, 3) the promotion of networking by enterprises, 4) improving employment, 5) improving the living environment, 6) promoting multiculturalism, 7) bolstering co-operation between homes and school, and 8) making information technology accessible to residents.

14. See memorandum SM043:00/2004, Ministry of the Interior, Finland, "Structure and emphases of the Policy Package for Major Urban Areas".

15. In Finland, the Minister in charge of Regional and Municipal Affairs exercises his responsibilities within the Ministry of the Interior, with responsibility for other matters, including police and security, belonging directly to the Minister of the Interior.

16. The RCP programme covers 63% of the Finnish population. Knowing that the Helsinki region, to which this programme does not apply, includes 22% of the population, this means that only 15% of Finns are left out of the wide sphere of urban policies.

17. Espoo is located in the capital city region.

18. One hundred thousand people are estimated to work in the cultural sector in Finland, an important element in regional development in terms of employment but also in terms of local identity and tourism potential.

19. The fourth centre, located in Raahe, North Ostrobothnia, is devoted to the development of highly sophisticated metal products.

20. The OECD (2003) publication on Polytechnic Education in Finland (Reviews of National Policy for Education, OECD, Paris) states that the creation of a national network of polytechnics from previously municipally-funded further education colleges was a key step in developing a regionally based national system of higher education.
21. The strategy includes special measures in regions where demand is not sufficient (low density areas).
22. Tieto- ja viestintäteknologia tuottavuuden ja talouskasvun lähteenä 2005. [Tieto- ja viestintäteknologia tuottavuuden ja talouskasvun lähteenä. 2005. Liikenne- ja viestintäministeriön Liikenne- ja viestintäministeriön julkaisuja 11/2005. Helsinki.]
23. The figures for Oulu are distorted by the acquisition by Technopolis Ltd of a major site in Helsinki.
24. See *e.g.*, Kaukonen *et al.*, 2002 and Kostiainen and Sotarauta, 2003.
25. The Tampere Region Centre of Expertise has succeeded as a key policy tool and it has been seen as successful programme also in external evaluations (see Huippuosaamisesta alueille kilpailukykyä, 2003).
26. The major employment sector is however mechanical engineering and automation (25 500 jobs in 2002), followed by health technology (12 000) and ICT (10 000) (Ministry of the Interior, Centres of Expertise, in Finland, 2003).
27. The CoE for Wood Technology cooperates with Finnish and European organisations in devising new wood products and composites.
28. University Centres were introduced in 2001. There are six University Centres in the country. The five others are: Lahti, Kajaani, Kokkola, Pori and Seinäjoki.
29. The University participates, with two other universities in the North of England in an ambitious supra-regional scheme called the "Northern Way", actively promoted by the three regional development agencies.
30. Science and Technology Policy Council of Finland (2003) Knowledge Innovation and Internalisation, Helsinki.
31. Basic funding for Universities has been increased by EUR 60 million for 2005-2007. Competitive external funding will be developed and new measures should give universities the capacity to purchase stocks and establish their own company. In parallel, universities will also be able to participate directly in the operation of Science Parks through joint funding models.
32. It is planned that HEIs will be brought together in larger units and management capacities will be developed.
33. See for example OECD (1999), The Response of HEIs to Regional Needs, IMHE, OECD, Pau and P. Chatterton and J. Goddard. (2003), "The response of HEIs to regional needs" in Rutten, R. *et al.,* "Economic Geography of Higher Education: Knowledge information and learning regions" Routledge, London.
34. Ageing is one of the factors affecting regional economic performance (see Subsection in 1.2 concerning territorial performances at NUTS III level.
35. For a detailed presentation of amalgamation mechanisms and issues, see Chapter 3.
36. Nivalainen and Volk (2002), cited in Rintala and Heikkilä, 2004, p. 167.
37. EVA (1997), cited in Rintala and Heikkilä, 2004, p. 170.

38. Siirilä *et al.*, 1999, Kainulainen *et al.*, 2001, Viljanen, 2001, cited in Rintala and Heikkilä, 2004, p. 171.
39. Seventy-two per cent of people in the rural periphery give a negative assessment of national level politicians, compared to 38% in cities and 42% in rural areas near cities, ibid, Rintala and Heikkilä, 2004, p. 173.
40. Including inter-municipal co-operation, mandatory as for hospital services, voluntary for other purposes.
41. Unemployment payments however are an exception to this.
42. Statistics Finland, National Board of Education. In Norway, with a population and municipal structure fairly similar to Finland, the number of school closures was only 193 for the same period.
43. Rural Policy Committee: The future of welfare services in rural areas, March 2003.
44. One significant difference is that specialist health services, down to local hospitals in Norway, are run as state-owned enterprises by a recent reform. In Finland, access to hospitals, based on 20 districts covering all regions obeys to a more central model than other health services. It is considered as satisfactory. Also dental services are not a municipal responsibility in Norway.
45. Rural Policy Committee/Theme group for welfare services, 2003: "The Future of the Welfare Services in the Countryside" (in Finnish).
46. Commonwealth of Australia 2001: Stronger Regions, a Stronger Australia, 8.
47. Paakkinen, 1993, cited in Pyy and Rannikko, 1995, p. 136.
48. Statistics Norway/KOSTRA.
49. Aarsæther and Vabo, 2002, 151-153 (Norwegian text).
50. In the mid-1990s the National Elderly Policy Committee set a target by which 90% of those aged 75 or more should be able to live at home.
51. The Centres of Expertise of Kuopio, Oulu and Tampere work on these issues.
52. Aarsæther (ed.) 2004: Table 1.3, p. 31.
53. "The changing age structure of the population and preparing for its effects in the different sectors of administration." Helsinki 2004, 78 pages.
54. Rural Policy Committee 2004: Viable countryside – our joint responsibility. Rural policy programme 2005-2008. Summary.
55. As seen before, only certain rural areas within commuting distance of a city centre have stable or increasing population.
56. Limit date: September 2004.
57. *Ibid.*: 108, 97-81.
58. The total population of the new municipality will be 58 000 inhabitants (present City of Rovaniemi is 36 000). The municipality will be one of the largest in Europe in terms of area: 30 000 km^2.
59. Aho *et al.*, 2004 found that even in municipalities down to a size of 2 000 inhabitants, innovative projects were developed within public services, drawing heavily on expert guidance from research institutions.

60. Actually, research shows that the accessibility of social services (day care, services for the elderly, and social work) is rated highest in sparsely populated rural areas (Rintala and Heikkilää, 2004, p. 175-176).

61. Lemponen and Kahila, 2002, p. 17.

62. The above-mentioned OECD e-Government study indicates that e-government services provided to business are more advanced than those provided to citizens. On the other hand, the national "Citizen Portal" with access to official information and a series of formalities that can be accomplished on-line (taxes, licenses, etc.) is already very popular, so improvements in this area could be highly beneficial.

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Chapter 3

Governance Issues

Introduction

Finland has been particularly capable to link economic development with social policy, quality of life issues, and collective action to solve problems (Haila and Le Gales, 2002). The remarkable recovery after the recession of the early 1990s, regulatory reform, successful EU membership and a leading position in ICT development are ample proof. In the uncertain period that has been ushered in by the burst of the Internet bubble and accelerated globalisation and delocalisation, Finland is confronted with adapting its multi-level governance to keep its competitive edge. Following the Regional Development Act adopted in 2003, various programmes and experiments are currently or will be implemented to this end.

This chapter first stresses general governance challenges relating to regional development than presents the institutional framework, assessing recent changes in multi-level governance. An analytical distinction between vertical and horizontal co-ordination devices is made, even if it appears often blurred in administrative practices. Finally, the chapter concludes by addressing the enlargement of the "networking culture" to non public actors, following two dimensions: capacity to involve users, firms and citizens, in strategic decisions targeting local and regional development and capacity to build social capital.

3.1. Regional policy challenges

Most countries manage simultaneously two strategies for regional development. On the one hand, in the short term, they equalise the financial resources of local/regional governments in order to allow them to fulfil their mandates for delivery of public services. On the other hand, central governments support long term development projects of local/regional authorities to generate growth and, at a later stage, produce greater fiscal autonomy and reduced needs for equalisation. However, a 2002 Nordregio report (Hanell, *et al.* (2002)) shows that *regional cohesion policy* is increasingly differentiating itself from *regional development policy*, as the former concentrates on welfare and redistribution in favour of the weaker regions, and the latter on economic growth across all parts of the country. Less emphasis is placed on "regional balance" and lagging regions and more is put on "economic development" across all regions. Central government intervenes to sustain both the position of leading regions, engines of national growth, and to break the negative cycles characterising lesser performing regions.[1] Based on the policy goal of a territorially balanced service

structure, public service delivery in areas of declining population (developed in Chapter 2), could be considered as a sub-set of cohesion policy.

Efforts to enhance competitiveness are at the heart of regional development policies and are related with governance schemes. Entrepreneurs' quest for achieving stable competitive advantages is dependent on the quality of the local environment for business and of locally provided services and public goods. In particular, small and medium-sized firms (SMEs), given their size, are dependant on "local collective competition goods" such as availability of relevant skills, access to research and technical centres and information about new markets and new technologies. The supply of these services involves the participation of various actors: public authorities at local, regional and central levels (sometimes at the supranational level), private firms and non-profit organisations. In order to fulfil this mission, governance is increasingly oriented towards schemes promoting co-operation among actors. This is true with respect to both vertical linkages (between lower and higher levels of government) and horizontal linkages (between ministries at central level or between regions or municipalities).

A renewed regional policy, based on efficient governance mechanisms, could be an answer to the financial and fiscal difficulties which will be soon faced by local authorities because of their limited sizes that do not provide critical mass to efficiently support economic development and a growing demand for more and better welfare services. While municipalities in Finland have important powers for rising autonomous resources via the income tax, they face rising costs for public service delivery. It seems that the needed complementary grants are rising as is borrowing. In fact municipal capacity to make decisions seems to be reduced, even if it remains much greater than that of the regional councils, which have only indirect democratic legitimacy (through the municipalities themselves) and possess no power of taxation. Even if the latter have important mandates regarding the definition of regional development strategies, this is a shared responsibility with the State and the municipalities. The regions depend on State regional development grants and mainly on the contributions of their member municipalities.

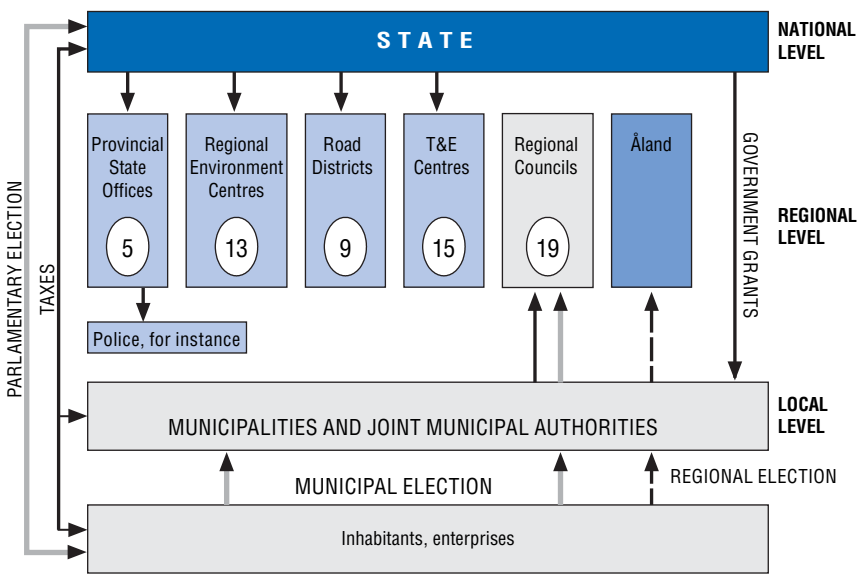
Finnish authorities are aware of these problems and have engaged a process of "re-organisation of decentralisation" targeting two key objectives: the progressive emergence of a regional level to co-ordinate competitiveness policy and the reinforcement of networking between different actors. This process is open to debate in Finland. On one side competencies, decision making and funds allocated to the regional level seem to remain modest in comparison with the proclaimed goals of an innovative regional policy. On the other side, Finnish historical and cultural traits, linked both to consensus for collective decisions and to recognised tradition of municipal autonomy, entail inertia in implementing new operational modes between different levels of government.

In order to enlist support for the new objectives and programmes, central authorities seem, not surprisingly, to have opted in favour of fully respecting these traits. Association between municipalities is only voluntary, even if incentives exist. Various institutional experiments have been launched featuring learning processes instead of top down decision making, and above all, co-operation has been chosen as a superior principle for decision and implementation. Even if no other relevant option appears to be possible, the risks cannot be ignored. Moreover, the absence of a "broad picture" for regional policy and the multiplication of programmes, projects and experiments associated to the deployment of regional policy introduce a certain degree of complexity for Finnish citizens to recognise efforts made by their country at a time of delicate choices and change to preserve success. Such a complexity also creates difficulties in implementing strong changes in administrative bodies for more effective horizontal and vertical co-ordinations, insofar as policy responsibility seems dispersed.

3.2. The institutional framework

Regional development governance in Finland obeys to a complex matrix, as institutional actors involved in regional development matters belong to different categories (see Figure 3.1). First, State ministries and their various agencies intervene in this policy area, with the Ministry of the Interior having

Figure 3.1. **Administration on three levels in Finland**



Source: Association of Finnish Local and Regional Authorities.

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specific own tasks and also major responsibilities in terms of co-ordination with other ministries and bodies at the sub-national level. Second, the 15 TE Centres (Employment and Economic Development Centres) and the six State Provincial Offices represent the central government at the provincial and regional levels. Thirdly, regional councils are the expression of a partnership for regional development of municipalities within a given region.

Last but not least, 432 municipalities and indirectly around 230 joint municipal authorities are the main providers of public services and important regional development actors insofar as they indirectly contribute to shaping regional development strategies by way of designation of the regional councils. The weight of municipalities can be appreciated in terms of municipal expenditure, representing 30% of total public expenditure on average and their overwhelming share of employment in public administration. There were 544 000 civil servants in Finland in 2004 of which 128 000 work for the State administration and the rest, 76.5%, for Local Government. This percentage corresponds to 333 000 direct municipal employees and 93 000 in joint municipal boards. The municipality of Helsinki permanently employs 39 000 people. Ranua (Lapland), with 4 800 inhabitants employs 300 on a full time basis plus 200 part-time. In comparison, regional council offices are much more lightly staffed: between 13 and 76 employees.

The central level of government

The top level of government in Finland consists of 13 fairly small entities, including the Prime Minister's Office (with 200-300 people in each), nine of which intervene in the area of regional development. Among them, the Ministry of the Interior, with specific responsibilities in regional development policy, is in fact a twofold Ministry:

- The Minister of the Interior is responsible for the affairs of the police Department, Department for rescue services, immigration Department and frontier guard Department.
- The Minister of Regional and Municipal Affairs is responsible for the affairs of the Department for development of regions and public administration and the Department of municipal affairs.
- Under this level, the national regional administration is based on the State Provincial Offices (6) which bring together seven different ministries: social affairs and health; education and cultural affairs; police; rescue services; transport; consumer affairs; competition; food-stuffs control; veterinary services and protection of animals; and the judicial administration. Besides the State Provincial Offices, more specialised bodies represent the central level government at sub national levels: The regional environment centres (13), the road districts (9) and the Employment and Economic Development Centres

(15 TE centres), integrating the activity of three ministries at the regional level: Labour, Trade and Industry, and Agriculture and Forestry. Since December 1996, the services of the Police, local Register Offices, districts bailiffs and prosecutors have been organised at the local level. There are 90 Local Districts in Finland.

From the perspective of regional development budgetary allocations, Table 3.3 gives certain indications concerning the weight of different funding sources and sectors. However, this can only produce an approximate view for the following reasons. Budget sections are mentioned as regional development sections. Still, only part of the money in each section is allocated to regional development. Approximate share of each section varies between 10-70% depending on the budget section (excluding sections of the Ministry of the Interior, totally devoted to regional development). This figure shows that the Ministry of the Interior needs to co-ordinate allocation of funds from many different sources for regional development, with its own contribution representing a small share of this. On the other hand, the ministry has a strong position in channelling EU funding (Table 3.1) that contributes significantly towards shaping regional strategies and programmes, as it controls close to one-third of these totalamounts.

It is also difficult to compare regional policy across countries, and especially the regional policy budget per inhabitant because of the variety of elements included and the lack of clear mandates for many different administrations and agencies. Despite these difficulties Table 3.2 gives some

Table 3.1. **EU Objective 1 and 2 programme funding by programme and by ministry**

Including bound public funding between 1/2000 – 9/2004

Programme	Ministry								
	MTI	MTC	MAF	MEd	MI	MSH	ML	MEnv	In total
Objective 1 in total	358 428 020	27 481 531	271 261 484	237 730 232	95 082 116	6 695 371	209 043 907	55 967 540	1 261 690 200
Objective 2 in total	250 746 669	33 261 471	0	177 630 890	160 943 478	1 374 019	173 264 658	92 000 953	889 222 138
In total	609 174 689	60 743 002	271 261 484	415 361 122	256 025 594	8 069 389	382 308 565	147 968 493	2 150 912 338

Source: Ministry of the Interior (FIMOS-database).

Table 3.2. **The narrow regional policy budgets of the Nordic countries, 2002**

= extra costs for less developed areas

	Denmark	Finland	Iceland	Norway	Sweden
Population in national support areas	942 000	2 125 000	108 000	1 137 000	1 409 000
Budget of regional policy 2002					
Total budget (mill. euro)	78.60	710.92	15.08	187.76	364.51
Budget per inhabitant (euro)	83	335	140	165	259
EU contribution in % of total budget	48%	49%	–	–	30%

Source: Nordregio (2002).

Table 3.3. **Budget 2004: sections mentioned as regional development sections**

Admin. field	Budget section (sub-item)	Allocation, EUR millions
MI	Regional Development Grant (Regional Councils)	*35.6
	ERDF contribution to structural fund programmes	*128.7
	State's (MI) co-financing of EU structural funds	*29.0
MF	State's co-financing (MF) of EU structural funds	*0.2
MEd	State's co-financing (MEd) of EU structural funds	*71.1
MAF	European Agricultural Guidance and Guarantee Fund's contribution to rural development	*47.9
	State's co-financing to rural development co-funded by EU	*66.6
	Promotion of nature forestry	*5.6
	Marketing and structural policy promotion in fishery (part)	15.3
MTC	Maintenance of basic road network	589.2
	State aid for construction and maintenance of some aviation fields	*1.2
	Purchasing and development of public transportation services	82.4
	Purchasing and development of transportation in archipelago	8.0
	State's co-financing (MTC) of EU structural funds	*7.8
MTI	Interest subsidies of Finnvera Plc. (part)	141.7
	Compensations of losses of Finnvera Plc. (part)	26.0
	Regional transportation subsidy	4.4
	Investment subsidies for enterprises (part)	21.4
	State subsidies for development service activity of enterprises (part)	3.6
	State's co-financing (MTI) of EU structural funds (part)	83.4
MSH	State's co-financing (MSH) of EU structural funds (part)	4.6
	State aid to municipalities' projects in social affairs and health	52.3
ML	ESF's contribution to EU structural fund programmes	*131.7
	State's co-financing (ML) of EU structural funds	*82.9
	Employment based transfers to investments	*39.5
MEnv	Promotion of environmental protection (part)	1.7
	Environmental work	*10.0
	Subsidies to municipal planning and land-use steering	0.9
	State's co-financing (MEnv) of EU structural funds	*9.8
	Some subsidies (part)	1.6
	Total	1 546.3

Notes: The above budget sections are mentioned as regional development sections (according to the Regional Development Act). Still, only a part of the money in each section is allocated to regional development related actions. Approximated share of each section varies between 10%-70% depending on budget section (excluding budget **sections marked in** *, which are totally for regional development).
MI: Ministry of the Interior
MF: Ministry of Finance
MEd: Ministry of Education
MAF: Ministry of Agriculture and Forestry
MTC: Ministry of Transport and Communications
MTI: Ministry of Trade and Industry
MSH: Ministry of Social Affairs and Health
ML: Ministry of Labour
MEnv: Ministry on Environment

Source: Ministry of the Interior.

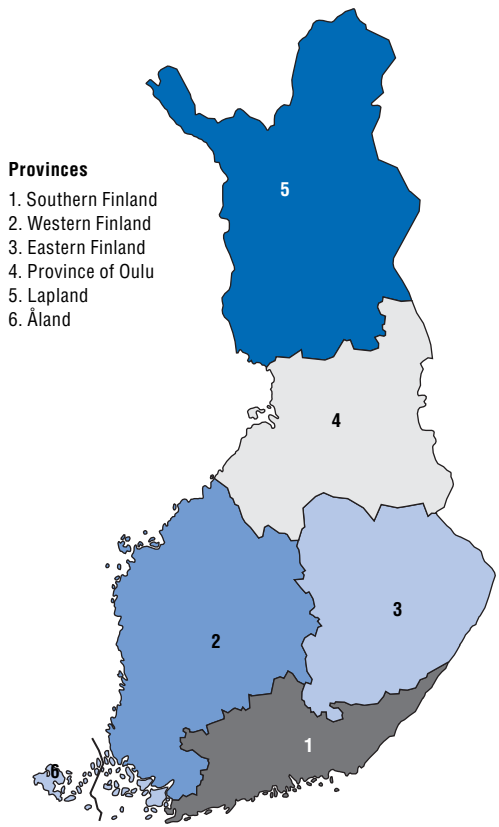
interesting results of comparisons and underlines the specific position of Finland *versus* other Scandinavian countries. It shows in particular that the per capita amounts devoted to regional development in the lesser developed areas of these countries are by far higher in Finland than elsewhere.

Intermediate institutional actors

Provincial State Offices

The six Provincial State Offices (see Figure 3.2) monitor and evaluate the implementation of key services by municipalities for the seven ministries. They represent the central state at the sub-national level and implement national decisions at the regional level in certain policy fields. In particular they monitor security and equality and, with regards to regional development, they implement structural fund programmes in the field of education. The

Figure 3.2. **State Provincial Offices**



Source: Ministry of the Interior.

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Ministry of Education thus retains important prerogatives in terms of educational competencies at the regional level.

In addition to their main locations, the six State Provincial Offices maintain sub-provincial agencies. The division of labour among the departments at the Provincial offices varies from one province to the next. Over 1 000 people are employed by the State Provincial Offices. As far as regional development is concerned two main missions are carried out by State Provincial Offices: secondary education and welfare services. As these involve relations with other institutional actors (both vertically and horizontally) they are included in the next section.

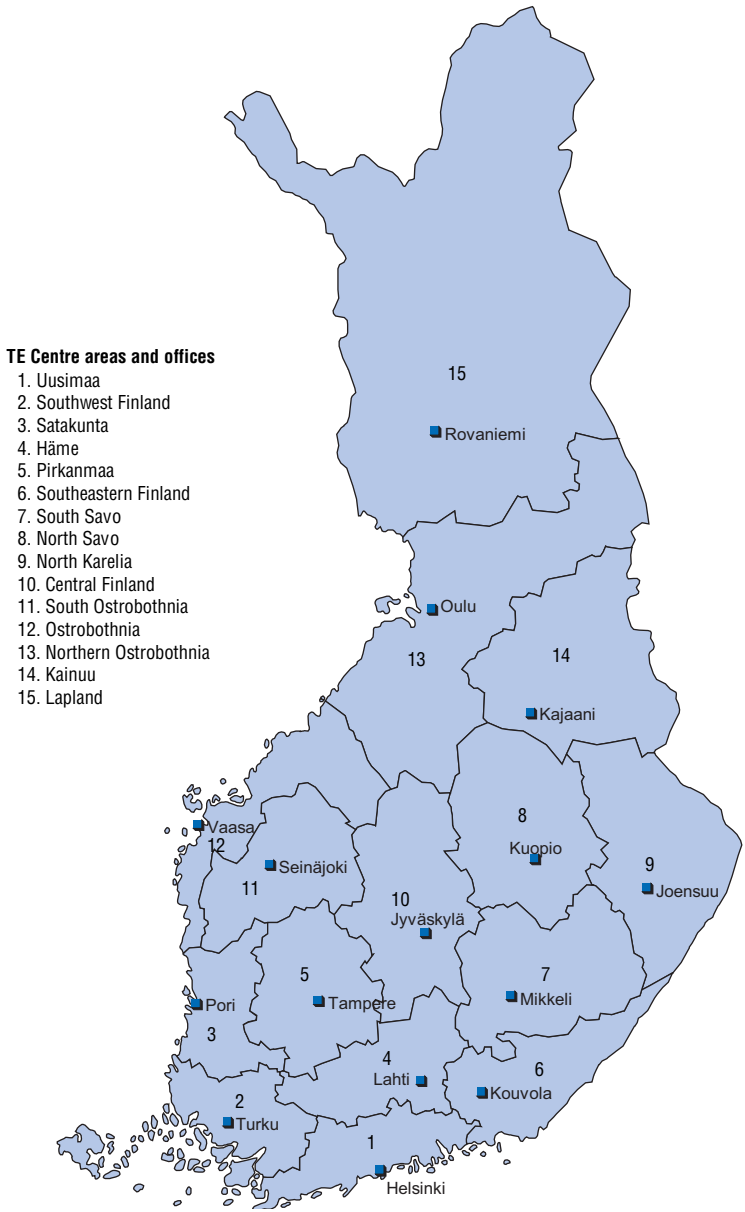
As regards EU funding in Finland, many provincial, regional and local actors share responsibility, which entails problems of co-ordination, with possible overlapping. An example could be EU structural funds (Objective 3) supporting development of skills for people seeking to enter or return to the labour market. Overall, knowledge has a significant impact on competitiveness and on the innovation potential of regions, explaining why projects in this area imply involvement of State Provincial Offices, and TE Centres but also regional councils. The Ministry of the Interior has the task of co-ordinating this funding at the national level and also monitoring implementation on the field by ensuring that all bodies, both regional agencies of national bodies and regional councils effectively follow the guidelines set within national and regional programmes. An example of co-ordination difficulties could be that of LEADER *versus* Objective 1 funding: the first is co-ordinated by TE Centres and the second by regional councils.

TE Centres

TE centres, established in 1997, combine three State authorities: Trade and Industry, Labour and Agriculture and Forestry, with the former responsible for the general steering of each territorial unit, within which the prerogatives of each sector ministry have been maintained (see below). TE centres replaced former district authorities which were not identically spread over the country. This explains why there are only 15 TE centres for the 19 +1 regions (see Figure 3.3). Some TE centres are thus responsible for more than one region.[2] Besides, 150 employment services offices are placed under the responsibility of the TE centres. Both employers and employees are served at these offices.

The purpose of the TE centres is to support enterprises, by providing business consultancy, promoting their technological development and helping them with exports. They are significant EU funding management organisations in the region. TE centres include technology units, which act as providers for services from TEKES (national technology agency, see Chapter 2 on innovation policies). They also implement and organise regional labour policy. TE centres are

Figure 3.3. **Map of TE-Centres**



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responsible for collecting labour market information and publishing regular reviews of employment trends and business development. Labour policy is implemented through employment service instruments such as training, and supported employment. Resources support specific projects such as employment-based investment funding, one of the key tools for regional development in the labour administration. Finally TE centres promote farming and fisheries and develop the vitality of rural areas and agriculture.

TE centres institutionalise co-operation among the three ministries at the regional level. However, their financing and internal organisation remain attached to the separation among these three fields. Each ministry is responsible for the use of its own budget sections. Operational funding[3] is allocated to the TE centres in result negotiations in which the three steering ministries and TEKES jointly participate. The three steering sector ministries and TEKES set common targets for all of the TE Centres. These "strategic impact targets" are set for a four-year government period. In addition, each ministry sets yearly result targets for every TE centre. These general result targets are negotiated every year, centre by centre, with more precise specific targets providing necessary detail for monitoring and evaluation purposes. Result management is based on the use of the Balanced Scorecard system.

The dynamism of labour policy in Finland must be underlined. It is built in such a way that the central level has developed a network of active institutions very present on the field. This proximity to regional issues and perspectives is a source of relevant knowledge for elaborating programmes. However, can TE Centres, as representatives of the central level, be able to be really involved in regional co-operation rather than acting only as intermediaries of central demand? Without such effective horizontal co-operation with other institutional and private key actors at the regional level, there is little room for developing true bottom up policies, which can lead to providing relevant "local competition collective services" to companies and employees. This co-operation can be favoured by the relative decisional autonomy of the TE Centres *versus* the Ministry of Labour. This issue appears all the more relevant that unemployment levels in certain lagging areas of Finland remain well-above the national and EU averages.

Regional Councils

Regional councils were created by the Regional Development Act of 1994. One specific characteristic of the Finnish system is that regions are constituted by aggregation of their municipalities, through their representation in the regional council. This means that in Finland, the classical scheme of decentralisation entailing devolution of certain powers to the regional level is not applicable. The new regions are less the result of a delegation of powers from the central level than that of a sharing of powers between the

municipalities themselves. Practically, co-operation between municipalities takes place through regional councils offering the critical size required for economic development strategies and joint municipal boards fostering collaboration in a smaller area. The major difference between the two resides in the fact that the former have the power to decide the use of State funds which is not the case for the latter.

Regional perimeters have been defined by National Law. However, changing them requires regions and concerned municipalities to be consulted. There are 19 regions in Finland plus the Åland Islands which historically enjoys a special status, since a 1919 Treaty with Sweden. This 20th region, with about 25 000 Swedish-speaking inhabitants, exercises wide-ranging legislative and administrative competencies, and has its own assembly ("Lagting"), directly elected, which adopts an annual budget. Since 1954 it has its own flag and since 1984, its own stamps.

The purpose of regional councils is to ensure that regional planning and development are steered and co-ordinated adequately across the country as a whole. Their main tasks are the following:

- Drawing up regional development programmes.
- Managing regional land-use planning.
- Presenting objectives for regional infrastructure planning.
- Leading regional and international co-operation.
- Co-ordinating EU regional development programmes.
- Developing a framework for business activities.
- Looking after regional interests.

Besides their main tasks Regional Councils can also carry out voluntary functions depending on special regional features and conditions. These may be the promotion of tourism, preservation and enhancement of cultural heritage, regional marketing, improving public services or information society issues. International activities, one of the main tasks of councils, are organised in a pragmatic fashion, depending on the regional context. For example, the Regional Council of North Ostrobothnia and the Kemi-Tornio Development Centre (Lapland) opened a Brussels office in 2002 ("European North Lapland-Oulu Office") that also represents the interests of the Lapland Regional Council.

Each region has an assembly, elected by the municipal councils. Members of this assembly have to be members of the municipal councils and each municipal council elects its own representatives. Representation of municipalities in the assembly is proportional to their population. The Assembly elects a Board and appoints a Chairman of the Board. The head of the regional council, a civil servant appointed by the Assembly, is also managing director of the regional staff office assisting the regional council in its administrative tasks.

Regional Councils have no power of taxation. They are joint authorities formed and principally funded by their member municipalities, each contributing in proportion to its population. The aggregate annual membership fees represent about EUR 32.9 million (in 2000). The Councils directly receive an annual "regional development grant", the total amount of which represents EUR 12.75 million (2004), used in particular for regional support to entrepreneurship and business creation, (see Table 3.4). Corresponding development projects are implemented not only by municipalities but also by public development companies, other organisations and associations.

For Centres of Expertise (CoE) and Regional Centre Programme (RCP) funding (respectively EUR 9 020 and EUR 9 200 million in 2004), the regional council only transfers the grants received to local projects, without selecting priorities or influencing their design. However, regional councils are more actively involved when the RCP or CoE programme is originally drawn up in collaboration between different regional actors. Sub-regions, via a sub-regional economic

Table 3.4. **Regional development grants allocated by the Ministry of the Interior, 2004**

		General grant (not bound)	Centre of Expertise	Regional Centre Programme	In total	General grant (not bound) (%)	Centre of Expertise (%)	Regional Centre Programme (%)	In total (%)
Uusimaa	1	1 700 000	1 555 000	865 000	4 120 000	13.3	17.2	9.4	13.3
Northern Ostrobothnia	17	750 000	1 175 000	995 000	2 920 000	5.9	13.0	10.8	9.4
Southwest Finland	2	930 000	790 000	700 000	2 420 000	7.3	8.8	7.6	7.8
Kainuu*	18	1 150 000	420 000	360 000	1 930 000	9.0	4.7	3.9	6.2
Pohjois-Savo	11	600 000	500 000	665 000	1 765 000	4.7	5.5	7.2	5.7
Tampere Region	6	500 000	770 000	480 000	1 750 000	3.9	8.5	5.2	5.7
North Karelia	12	650 000	430 000	510 000	1 590 000	5.1	4.8	5.5	5.1
South Ostrobothnia	14	650 000	360 000	550 000	1 560 000	5.1	4.0	6.0	5.0
Satakunta	4	660 000	340 000	430 000	1 430 000	5.2	3.8	4.7	4.6
Central Finland	13	550 000	500 000	350 000	1 400 000	4.3	5.5	3.8	4.5
Kymenlaakso	8	650 000	0	700 000	1 350 000	5.1	0.0	7.6	4.4
Kanta-Häme	5	450 000	560 000	300 000	1 310 000	3.5	6.2	3.3	4.2
Päijät-Häme	7	600 000	250 000	380 000	1 230 000	4.7	2.8	4.1	4.0
Lapland	19	740 000	60 000	425 000	1 225 000	5.8	0.7	4.6	4.0
South Karelia	9	300 000	440 000	480 000	1 220 000	2.4	4.9	5.2	3.9
Etelä-Savo	10	420 000	400 000	340 000	1 160 000	3.3	4.4	3.7	3.7
Ostrobothnia	15	600 000	220 000	260 000	1 080 000	4.7	2.4	2.8	3.5
Central Ostrobothnia	16	400 000	250 000	210 000	860 000	3.1	2.8	2.3	2.8
Itä-Uusimaa	3	450 000	0	200 000	650 000	3.5	0.0	2.2	2.1
		12 750 000	9 020 000	9 200 000	30 970 000	100.0	100.0	100.0	100.0

* The amount for Kainuu included allocation for the Kainuu administration pilot (EUR 350 000).

Source: Ministry of the Interior, 2004.

development centre, are the key actors in the definition of projects and their yearly funding, in accordance with the national programme targets.

The aim of the 2002 Regional Development Act is to steer regional development at the national and regional level in such a way that development work forms an interface between regional and central government. The willingness to consider regions as a strong authority of intermediation lays on two complementary aims and competencies: to activate the right level for identifying local sources of competitiveness in a bottom-up perspective on the one hand, and to warrant national coherence in implementing central level decisions on the other. The exercise of these competencies depends on the way this level is regarded by other actors of local development and mainly by the municipalities.

An EU Committee of the Regions publication (2001) recalled that "the decision to establish a directly elected regional level of government in 1994 in Finland was a new departure". The transfer of regional development tasks from the state (provinces) to regional councils (indirectly, the responsibility of municipal government) constituted a decentralised approach, the democratic character of which has been confirmed by the Council of Europe. This evolution can be compared to the Swedish process of trials at regional autonomy (see above-mentioned Nordregio report, 2002). In Sweden the issue of establishing responsibility for regional policy at the regional level led to a "pilot" scheme based on elected County Councils in two regions (the Danish/Norwegian approach), but the Swedish government however opted for a model where municipalities take responsibility for co-ordinating regional policies at the county level, although they have no control over policy implementation (the Finnish approach). A departure from the existing model has been taken in Finland with the Kainuu experiment in regional autonomy started in 2005 (see below) that is meant to test the implementation and functioning of regional self-government.

However, due to the strong culture of consensus and of municipal autonomy in Finland, it does not appear easy to follow another path than that of the incremental method for operating institutional change. Nonetheless, the existing regional council framework, defined as an inter-municipal body more than a supra-municipal one, could achieve results in two other fields. The first relates to the reinforcement of inter-municipal co-ordination for programming of development projects. The second possibility concerns the definition and implementation of significant regional programmes within a coherent national vision of balanced territorial development, based on the recognition that at least three types of regions with very distinct features exist in Finland. The North and East on one side, the Southwest on the other and finally the metropolitan/urban areas of Helsinki, Tampere and Oulu are sufficiently differentiated so as to be treated with specific tools and not a "one size fits all" approach. The perception of

a community of interests among regions belonging to such broad perimeters could be considered as a relevant objective.

Transferring regional development tasks to the regional councils has boosted development policy in which regions defined their own aspirations and targets. Horizontal collaboration between different regional actors strengthened, and regional opinion and regional visions were given more room than before (Riepula, 2004). Regarding this first overview, it could be said that regional councils have played a very important role in providing local actors with "local collective competitive goods", sources of interaction among them and of innovation at the level of the territories. Given these achievements, it will be interesting to see if self-government at the regional level as planned on an experimental basis in the Kainuu Region, will significantly contribute towards strengthening these trends as has occurred in other countries.

Municipalities

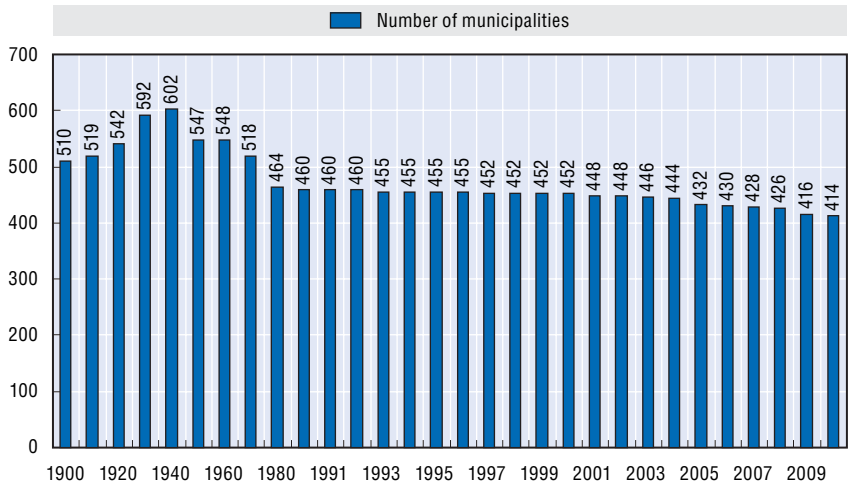
Finland has a strong, long-established tradition of local self-government. The independent status of municipalities is confirmed in the Local Government Act of 1995 stating that "a municipality shall endeavour to promote the welfare of its inhabitants and sustainable development in its area". Looking at municipalities from a public finance perspective provides a clear picture of their important role. Finnish municipalities have numerous fiscal tools at their disposal, but their relative importance is changing. Volatile tax revenues and tax sharing schemes are beginning to be replaced more frequently with general purpose grant revenue systems. Also, municipalities will continue to face fiscal limits with rising public service costs. To attain critical mass for efficient public spending, municipalities set up joint municipal boards for delivery of public services but also for purposes of local economic development.

Finnish municipalities enjoy a high level of local autonomy that has been further strengthened by the 1993 fiscal reforms. Similar to other Nordic countries, Finland is highly decentralised as demonstrated by their share of tax revenue in total local government revenue. In terms of expenditure, local government share accounts for over 30% of total public spending. This is due to the heavy reliance on municipalities to deliver public services, including public health care, social welfare, education and culture and environmental and technical infrastructure. Finland's strong commitment to uniform delivery of those services is partly ensured by the imposition of high standards in the form of recommendations from the centre. But because of these centrally imposed norms, some observers mitigate the strong local autonomy pattern by qualifying the Finnish system as one in which the municipalities serve as agents of the state rather than as one of autonomous local governments making their own decisions about service quality (OECD, 2003c, p. 103)).

Municipal organisation

Municipalities are, on average, relatively small in size and vary from an island village of 132 inhabitants to the capital Helsinki of more than half a million people. There is also wide discrepancy in land area and population density. Figure 3.4 shows the evolution and projected trends of the number of municipalities. The gradual decrease in numbers results from amalgamation policy. A comparison between 1999 and 2004 concerning the number of municipalities according to their size, (see Figure 3.5), shows that policy impact is limited since it affects municipalities of different sizes but not the smallest (often located in remote areas with geographic features that inhibit mergers). Figure 3.6 presents the 444 municipalities according to size, which demonstrates the contrast seen throughout Finnish territory.

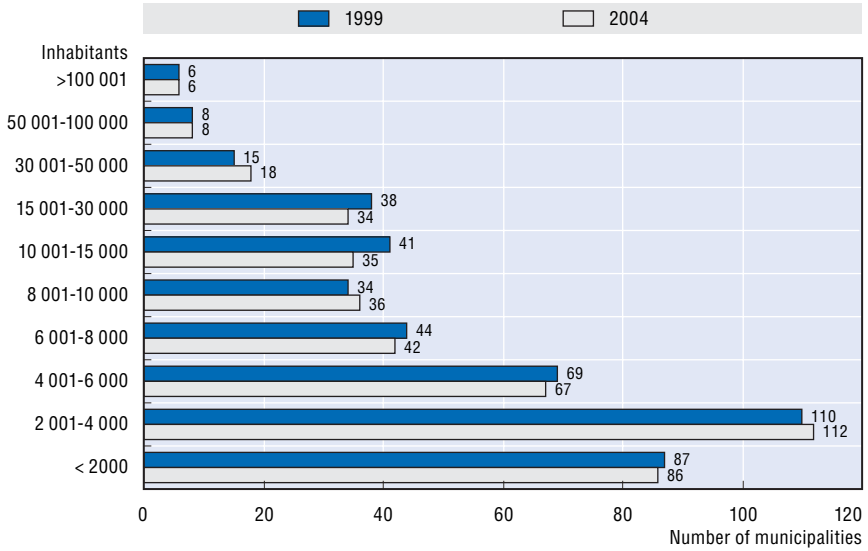
Figure 3.4. **Evolution in the number of municipalities 1900-2010 (2006-2010 estimate)**



Source: Ministry of the Interior.

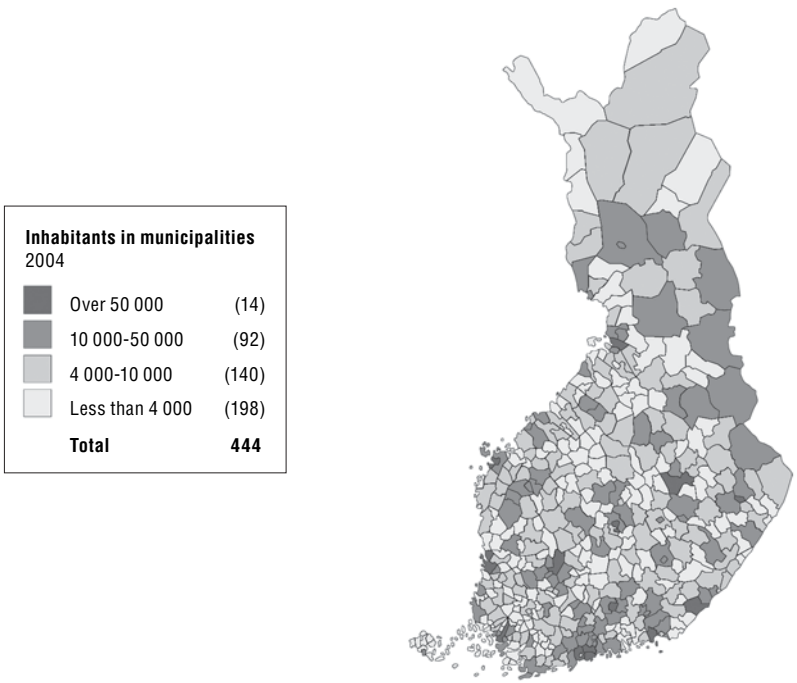
Municipal organisation is based on the municipal council, with members directly elected every four years. The councils are the highest decision-making body and the selected chairman is the political and administrative leader of the municipality. Municipal council members choose a municipal board, a smaller body that aids in implementing the council's decisions. The Council also selects a "municipal manager" (called the mayor in cities and towns).[4] The council and board members are dispatched in different committees, each responsible for a specific municipal activity and they are free to set as many committees as deemed necessary to fulfil municipal missions.

Figure 3.5. **Comparing municipalities by population size, 1999 and 2004**



Source: Ministry of the Interior.

Figure 3.6. **Municipal map of Finland**



Source: Ministry of the Interior.

Municipal public service provision and expenditures

Finland is committed to high quality and extensive public services, many of which are provided equally to rich and poor, stemming from a strong egalitarian ethic that it shares with other Nordic countries (OECD 2003a). Compared to other countries, Finland relies to a large extent on municipalities to deliver and finance these public services. Finnish local governments have very large spending responsibilities, including the provision of primary and secondary education (facilities and remuneration of staff), social welfare, public health services (management of day-care centres and hospitals, free dental care for persons under 17), and technical infrastructure (see Box 3.1). Many of these tasks are required by national law, with standards or recommendations concerning service levels determined by the State. Such standards or benchmarks are typically in the form of input requirements, (number of adult-care givers per child in day-care, number of teachers per student in primary school and minimum amount of space per child).

Besides standards determined by quantitative ratios, others are qualitative such as measurements of average waiting time for access to health services (delay in obtaining appointments). When agreement is easily reached, recommendations rather than standards are delivered by the national level (care for the elderly). In primary education, a municipality has leeway on how to achieve the standards (on its own or in co-operation with adjoining municipalities), including the compulsory division of teaching hours by subjects. In high schools and vocational education and in polytechnics, the organisational flexibility is similar. For polytechnics, yearly negotiations with the Ministry of Education determine targets and levels of expenses as per the number of students. The system generally seems to have permitted to maintain an equal quality of services across the country so limited availability or quality differentials in public services is not an issue in terms of regional development, contrary to many other countries.

The setting of clear expectations for service quality by the central government ensures fairness in public service provision and minimises the potential problem of the "race to the bottom": the tendency for municipalities to scrimp on the provision of services to maintain their competitive positions. On the other hand, these responsibilities and high standards can have a big impact on local government finances. In the EU, local public service responsibilities are particularly extensive in Denmark (30.2% of GDP), followed by Sweden (25.3%), Finland (18.6%) and the Netherlands (17.1%).[5] Local public expenditure/GDP is highest in countries in which local governments are responsible for costly expenditure items like the remuneration of teaching staff and/or hospital management, and in the case of Finland the municipalities cover both costs. In 2002 for example, social welfare and health care services

Box 3.1. **Basic public services provided by the Finnish municipalities**

In terms of education, municipalities provide:

- The National comprehensive school.
- Upper secondary school.
- Vocational education and training.
- Libraries.
- Art classes.
- Adult education/ Liberal education.
- Cultural and recreational services.

In terms of social services and health care, municipal responsibilities are:

- Children's day care.
- Welfare for the aged.
- Welfare for the disabled.
- Preventive and basic health care services.
- Specialist medical care.
- Dental care.
- Promoting a healthy living environment.

Municipalities are also responsible for the maintenance of the technical infrastructure:

- Supervision of land use and construction.
- Water and energy supply.
- Waste management.
- Street and road maintenance.
- Environmental protection.
- Fire and rescue services.

Many services are jointly supplied with other municipalities through Joint Municipal Boards, particularly in the case of hospitals and various educational institutions. Municipalities also seek to promote economic development and employment while regional development and planning are the responsibility of the regional councils.

Source: Based on information provided by the Ministry of the Interior.

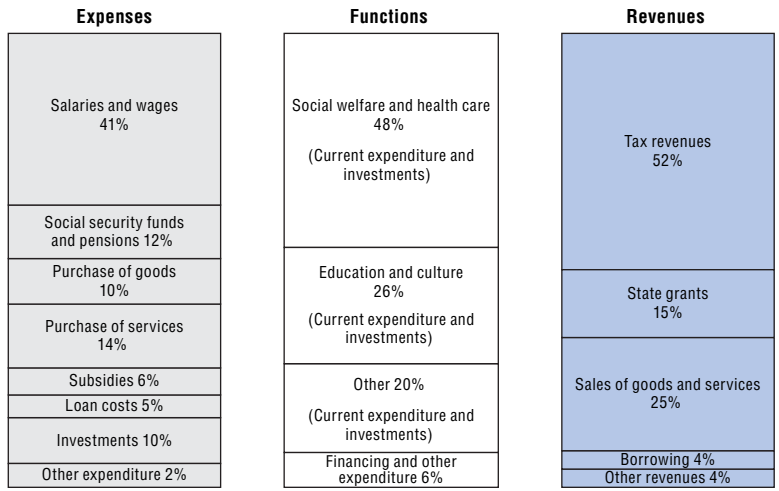
represented 48% of the total operating costs of all Finnish municipalities, while education and culture accounted for another 26%.

Municipal revenue sources

Finnish local governments rely primarily on tax revenue and inter-governmental grants to cover their public service provision costs. Municipalities have a certain amount of freedom in how revenue is spent and, in principle, reasonable influence on the size of revenue, through their right to set the flat rate for local income taxes. The current funding system was put in place as part of major reforms in 1993, prior to which the central government had a more direct influence on spending via earmarked grants (OECD 2003a). In 2002, local tax revenues represented 52% of the EUR 27 billion total local revenues followed by 25% for sales of goods and services (operating non-tax income), 15% for transfers from the national government, 4% for borrowing and another 4% for other revenues (see Figure 3.7). Overall, Finland's fiscal gap is narrow by OECD standards, thanks in part to the significant local tax revenue.

Municipal taxes. The municipal sector relies heavily on tax revenues to fund public spending, with the most weight given to income taxes.[6] This differs from other OECD countries where the property tax is the more prominent fiscal tool. In Europe, only six other countries implement a local personal

Figure 3.7. **Breakdown of municipal expenditures and revenues in 2002**



Source: Finnish Association of Local and Regional Authorities.

income tax: Belgium, Denmark, Finland, Italy, Spain and Sweden. On average, Finnish local income tax represents 81.9% of total tax revenues, followed by 13.4% for corporate income taxes and 4.7% for real estate taxes.[7] The labour income tax base is the earned income of local residents that includes fringe benefits, the estimated labour share of non-incorporated business income, social security benefits and exercised stock options, and is identical to that used by the central government. Municipal labour income tax rates are flat and municipalities have the power to set the rates, most municipalities charging from 17% to 19%.

Municipalities also receive a share of the revenues from the corporate income tax paid by companies operating within their jurisdiction and according to the number of persons employed. Prior to 1993, corporations paid some taxes directly to the municipalities, but since 1993, they pay all of them to the State at a rate and the State returns a share to the municipalities. Revenue from corporate income tax is volatile though and has declined from a peak of 22% of total municipal tax revenue in 2000 to 7% in 2003, partly due to the reduction in the municipal share of total corporate tax revenues from 36.5 to 19.75% over that time period. While the corporate tax rate is being lowered from 29 to 26% as of 2005, the government proposed to keep municipal revenue unchanged by raising their share from 19.75% to around 22% (OECD, 2004d)). Therefore, municipalities are still exposed not only to the fluctuations in corporate profitability but also to the specific fortune of firms located within their boundaries via this arrangement. For example, in Helsinki and Espoo where much of Nokia's activities are located, corporate tax revenues reached peaks of respectively 26% and 28% of municipal operating expenditure in 2000, with a subsequent decline to 7% and 9% in 2003. These revenue fluctuations and tax rate changes help to explain the shifts of fiscal flows into and out of municipalities in the Greater Helsinki Metropolitan Area, as discussed in Chapter 2.

The structure of local tax revenue rests on rather volatile tax revenue that fluctuates due to changes in the tax base over the business cycle, as discussed above, which makes it difficult to co-ordinate expenditure programmes. As stated in the 2003 *OECD Economic Survey of Finland*, the country has one of the most highly taxed economies in the OECD, with tax revenue equalling over 45% of GDP. During the second half of the 1990s, revenues from the corporate and labour income taxes, which are highly sensitive to economic cycles, grew substantially and the maturing of stock option programmes also gave a boost to municipalities' receipts from the labour income tax. This occurred despite the introduction of measures at the central government level, which resulted in lower tax revenues apportioned to municipalities. Recent increases in several tax allowances to the earned-income tax have narrowed the tax base while the municipalities' share of corporate tax revenues

has been cut. The central government has also offset the rise in municipalities' tax revenues by reducing state grants, after already severe cuts in the first half of the 1990s due to recession. Overall, financial resources of municipalities in volume terms have not changed significantly since the mid-1990s while their mix has shifted towards tax revenues OECD (2002a).

Intergovernmental transfers and grants. Since municipalities are responsible for many functions that involve redistribution (from the rich to the poor but also from the working-age population to the young and the old), some equalisation of resources is necessary. This is done through two different intergovernmental financial flows. The first consists of transfers by programme area to the municipalities from the central government. The second is equalisation payments from the municipalities with large taxable capacities to those with low capacities.

State transfers for particular services are in effect lump sum grants. Lump sum grants are independent of the level of spending selected by the municipality and generate only income effects on public spending. Added to (or subtracted from) these transfers are the equalisation payments, also in lump sum form. Assuming that the net flow is positive, municipalities have more resources and are likely to spend somewhat more on public services than otherwise would have been the case. Because funds are fungible, however, the additional funds need not be spent on the public services for which they were intended and could potentially be used to reduce local tax rates or to increase other public services. This danger is mitigated given demanding compulsory standards on quality of services.

The state grants or sector specific transfers come primarily through the Ministries of Social Affairs and Health, and Education. Prior to 1993, these transfers were based on actual expenditures by municipalities, but that approach was abandoned because policy makers recognised that such transfers could lead to excessive spending and low incentives for efficient provision of services. The current system provides block grants based on notional expenditure needs and is intended to compensate municipalities with heavy service demands for the additional costs that they face in providing public services. Thus, the Ministry of Social Affairs and Health contributes through an ear-marked grant based on a EUR/inhabitant criterion, while the Ministry of Education through an ear-marked grant based on a EUR/student criterion.

This approach recognises that factors outside the control of local officials make it more costly to provide public services in some places and thus there should be compensation to some extent by the central government. For example, a city with many young families and consequently many children would receive more assistance per resident for day-care services than one with a smaller proportion of young families. In general, factors such as

population age, economic structure, unemployment rate and illness rate of the inhabitants would affect the costs of providing social welfare and health services and hence are factored into the transfer formulas for those services. Some additional adjustments are made for particular needs, such as Swedish speaking families, and for the surface size of the municipality. Transfer payments are intended to make the costs borne by local governments the same per inhabitant regardless of actual costs.

In addition to the grants municipalities receive from other ministries, the Ministry of the Interior plays an important role in their financing. It both contributes to the municipality's budget through an equalisation of the municipal taxation (based on local resources) and a general state grant (based on needs and more specifically to a EUR/inhabitant criterion). There is also a discretionary grant for municipalities with exceptional and unexpected budgetary problems. In 2004, around 50% of the 244 municipalities applied for this additional grant and less than 100 of them received extra funds. One objective of the Ministry of the Interior is to improve incentives for more efficient local expenditures in the future by eventually limiting these extra grants to 50 or less.[8]

The second component of aid flows is designed to reduce fiscal disparities among revenue-raising capacity of the municipalities. The tax equalisation system is based on a comparison between every municipality's potential tax revenues per inhabitant and the country average (potential tax revenues are defined as those that the municipality would get if it adopted the average tax rate applied in the country). If the potential tax revenues of a municipality fall below 90% of the country's average, then the tax equalisation scheme raises this municipality's financial resources by redistributing tax revenues collected from wealthier municipalities (in 2000, three-fourths of municipalities were below the threshold). If it exceeds the 90% threshold, the municipality contributes to the redistribution scheme (40% of its tax revenues, starting from the 90% threshold). Up to 2001, revenue equalisation was capped. By law, a rich municipality's contribution to the tax equalisation scheme cannot exceed 15% of the municipality's tax revenue. Thus, when a municipality's tax revenues exceed 144% of the country average, its contribution to the scheme is brought down to 15% of its total tax revenues, which is low by Nordic standards. This capping limit was removed in 2002, yet Finland's scheme equalises local government revenues to a much lesser extent compared with the equivalent schemes operating in Denmark, Norway and Sweden (OECD 2002a, 2003a).

Every year, state transfers are adjusted to reflect price and public sector wage developments. In spite of these rules, state grants have been cut significantly since the early 1990s. As mentioned earlier, booming corporate income tax revenues in the late 1990s led to cuts in state grants, *de facto* preventing excessive spending. As a result, the share of grants in total local

revenues has declined substantially, from 30% in 1990 to below 15% in 2000. Due to budgetary pressure, municipalities responded by raising local income tax rates and have been able to manage because of the overall growth in the economy afterwards (OECD 2002a).

Similar to the situation with municipal tax revenue, there is no automatic mechanism via the block grant funding formula, or official discretionary policy to protect municipalities from cyclical variation in revenue. Furthermore, there is sometimes a degree of uncertainty about the level of equalisation payments or a delay in their payment, both of which can amplify the problem of unpredictable and fluctuating revenue. A need to increase the predictability of public funding was acknowledged in a 2002 Ministry of Finance report and authorities also recognised the need to reduce municipalities' exposure to corporate income tax revenue to lessen cyclical variations in municipal revenue (OECD, 2003a).

Issues related to the institutional framework

A certain number of specific issues arise from the characteristics of Finnish governance and recent trends in regional development policy. These relate first to central government organisation and budgetary allocation in terms of regional development matters. The role of municipalities and the appreciation of their degree of autonomy concerning resource allocation is the second issue. Thirdly, the role and powers of regional councils are, by definition, at the centre of debate. The evolution of the role of Provincial State Offices and TE Centres is a fourth area of investigation. Overall, fiscal co-ordination with municipalities and efficient service provision cannot be separated from regional policy.

At the ministerial level, regional development issues, although placed under the responsibility of the Ministry of the Interior, are on the agenda of a large set of ministries. Finnish authorities have made the choice of improving the co-ordination of the different ministries actions in terms of regional policy. However other choices are possible. For instance in three out of the five Nordic countries (Iceland, Norway and Sweden), responsibility for industrial and regional policy belongs to the same ministry. This thematic proximity favours links between regional issues and economic development, underlining the evolution of the meaning of regional policy (regional development rather than regional cohesion).

In the national context, the final decision on how sector budgets are to be utilised is taken by each sector authority itself while the Ministry of the Interior makes an ex-officio assessment of the sector budgets having an impact on regional development (Nordregio report, Regional Development in the Nordic Countries, 2002). This consideration leads to two different issues: is

the Development Act of 2002 able to improve co-ordination of the different ministries at the regional level, in particular through the regional development strategies that ministries have had to adopt? The Ministry of the Interior appears more as a co-ordinator of other department's policies at the regional level than as a significant contributor. How do both co-ordinators at the central level (Ministry of the Interior) and at the regional level (the regional council) co-ordinate with each other? Do these partners appear sufficiently strong *versus* other actors (other central ministries, big municipalities) in terms of resources and decision-making power?

Even if Finnish municipalities are presented as very autonomous in their decisions, it seems that this relates rather to implementation of mandates than to more strategic projects. The standards reduce the freedom of the municipalities and could be called into question, but municipal governments appear to treat them as if they were laws. On one side the benefit is high because municipalities have appropriate incentives to provide those services in a relatively cost-efficient-way (the more funds they can free up from their tax revenues, the less they will have to set the rate and the more funds they can free up for other purposes). On the other side, after spending funds to meet the standards for basic public services, most municipalities have little budgetary flexibility to provide additional services (and among them contribution to regional development projects). The evolution of the costs of these public services even risks confronting the municipalities, and especially the smaller ones, with unfunded mandate problems.

At this stage it is necessary to mention the role played by the Association of Finnish Local and Regional Authorities, a powerful organisation comprising all Finnish municipalities,[9] defending their interests and that of other bodies (joint municipal boards and regional councils)[10] in which they play a key role. It is staffed by 330 people and an additional 560 employees in various service companies (accounting, consulting, training, engineering, architecture) working for local government. It provides local authorities with guidance and information and also engages in research, studies and publishing. Specific expertise residing in areas of municipal finance and legal matters includes traditional areas (public services, infrastructure…) and newer ones (Regional and economic development, Environment, Information Society). The association promotes dialogue with central government, thus weighing indirectly on key policy decisions and new legislation. Its functioning is based on consensus, the weight of different political parties in its bodies corresponding to the results of the most recent municipal elections. The key issue here is how such a well-structured and smooth functioning organisation can evolve so that its members accept relinquishing in the future certain economic development competencies in favour of the regional level.[11]

Mandates given to the regional councils bring to the fore an essential question. How can such decision-making powers be assigned to bodies whose functioning is linked to the will of the State and the municipalities? If responsibility for regional development continues to be controlled by the State on one side and the municipalities on the other, can regional councils develop a long-term clear cut strategy and have the means to implement it? Knowing if different regions can follow different kinds of development paths in the future remains an open question. From this point of view, the 2002 Regional Development Act could be considered as a step in a progressive process of change and empowerment of regions, notwithstanding the possible impact of the Kainuu experiment in elected self-government (see further).

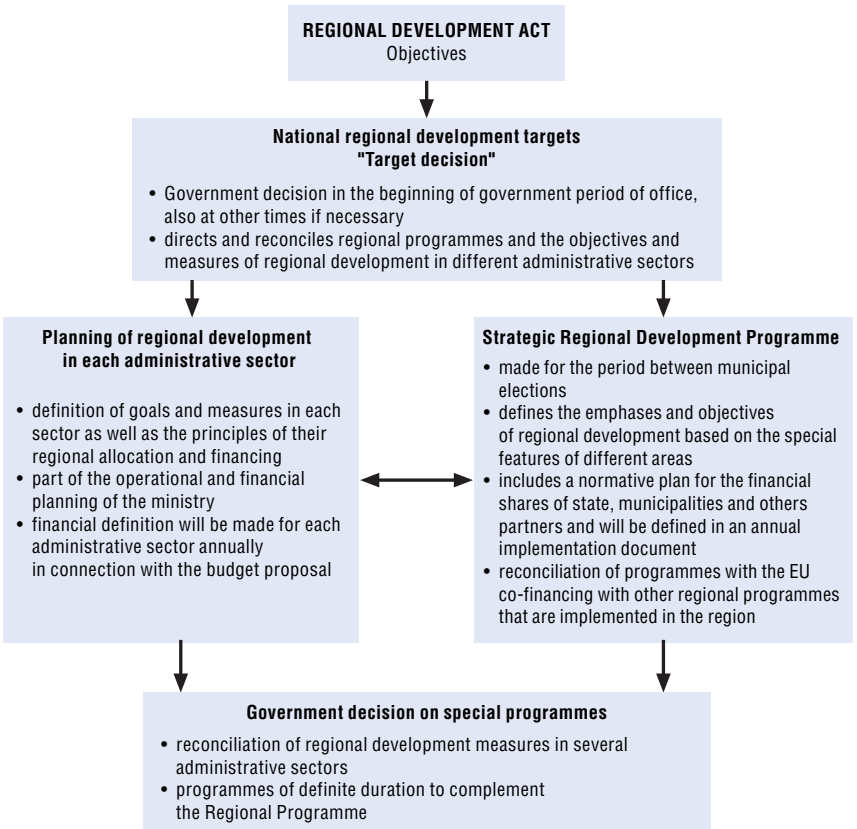
Certain questions concerning the organisation of TE centres and the role of State Provincial Offices need to be further investigated. In the case of the former, internal coordination among the three different ministries as well as the relationship with local and regional actors having development mandates needs to be examined. Is there reduced efficiency and complexity for firms because of redundant sources of funding and advice? Concerning State Provincial Offices, playing in particular, an important role in the sphere of Education, their importance has diminished with the new powers devolved to regional councils. Nonetheless "control authority" remains while a partnership approach is developed with regions. On the longer term, is this sustainable? The answer could reside in assuming a more active role in regions to promote horizontal co-ordination between the regional sector strategies and regional council strategies.

Most of the previous remarks bear on the challenges now facing Finland in terms of increasing costs of public service delivery and the long-term impact of regional development. Looking at these two issues it is worthwhile to highlight one of the statements of the 2004 *OECD Economic Survey of Finland*. "Further pension reform is needed in order to improve government finances in the face of the ageing shock. The reform to be introduced in 2005 will help, but risks being insufficient. As a minimum requirement, central government and municipalities should avoid fiscal deficits, while the pension funds continue to accumulate assets. Maintaining these balances, while reducing the high taxation of labour, will require more efficient service provision, better fiscal co-ordination with municipalities and meeting some of the future growth in service demand via private funding. At the same time, the demand for still more and better welfare services is growing and puts pressure on central government". On this basis, regional policy could well be considered also as the only option to accompany the necessary evolution of welfare policy, while enhancing future prospects for sustaining growth as an answer to increasing fiscal pressure.

3.3. Vertical and horizontal co-ordination

The Regional Development Act is built on a multi-dimensional matrix bringing together different tasks and actors (see Figure 3.8). First it includes different calendar sequences such as strategy elaboration and steps for implementation. Second, it encompasses vertically different levels of governance: central level targets condition regionally determined strategies. Third, it also stresses horizontal links, both at the local level since regional strategies are elaborated by local actors co-operating and at the ministerial level because regional development measures have to be planned and specifically identified in each administrative sector.[12] Moreover, the central government retains a fair amount of decision-making power concerning special programmes such as the Centres of Expertise and the Regional Centre programmes.

Figure 3.8. **Regional Development Act hierarchy**



Source: Ministry of the Interior.

Complexity is mirrored in each of the various programmes included in the Act, by blending of vertical and horizontal dimensions. For example, relations between the Ministry of the Interior and the regional councils are automatically connected to vertical links between these two levels of governance and horizontal partnerships between local municipalities, the latter constituting the core of the regional councils. This is also valid for the TE Centres. Their functioning is based on vertical links between each of the TE Centres and the three ministries in charge, and on horizontal links at the central government level for co-ordination of regional policies between the latter.

The Finnish system is clearly dominated by co-operative and consensus-seeking principles of organisation. These are the basis for building and/or reinforcing knowledge-based regional economies by bringing together a large set of local actors and their specific knowledge and competencies (thus recognising the specificity of each regional development process) as well as a way of harmonising local and central plans, in a fashion adapted to Finnish history and culture more than hierarchical type of relationships. The entailing complexity of such co-ordination mechanisms requires analysis of the specific modes of regulation between actors by distinguishing vertical and horizontal frameworks.

Vertical co-ordination

In the 1970s, coordination of public finances was introduced in Finland (Committee of the regions, EU, 2001). Central and local governments agreed to negotiate annually to ensure stable evolution of public finances. Participants (in particular the Ministry of the Interior and the Association of Local and Regional Authorities) thus developed a common culture of consensus building on joint recommendations, for example about local tax rates, development of services activities, operating and investment expenditure and the distribution of costs between central and local governments. However, municipalities are expected to follow the recommendations but are not obliged to do so. Overall, the local government side feels that this experience in dialogue has been positive, opening a channel for the exchange of relevant information and discussion of common interests between local and central government.

One positive outcome of this culture of co-operation with local actors, who have a very wide range of responsibilities regarding public expenditure and supplying of public services, is that the question of local capacity building is less pressing in Finland than in other countries where the decentralization process is less advanced or more limited.[13] Such an evolution means that past "command and control" postures must definitely be left behind and that these need to be replaced by incentives and dissemination of "best practices", as has begun to be the case. Trying to impose hierarchically any kind of "optimal

solution" would not be adapted and would prevent adequately using local knowledge and competencies to build competitive regions. Vertical relationships are of different types.

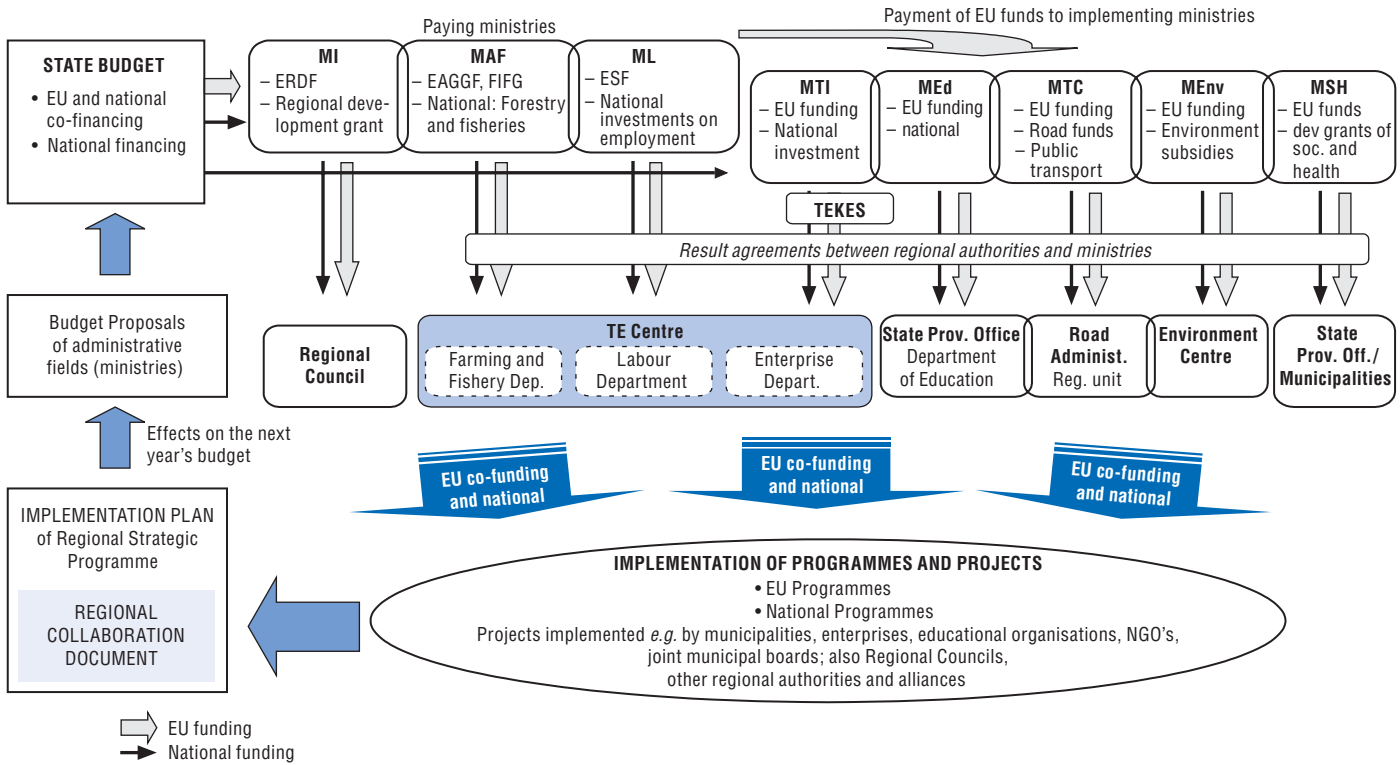
Types of vertical links

Figure 3.9 sums up the way different ministries are related to regional bodies (institutionally and financially). One important aspect of this structure is the assignment of roles in the decisional and operational steps of regional development programmes. This allocation of responsibilities reflects permanent interaction between upper and regional levels, between targets and proposals. Thus, the Ministry of the Interior is responsible for the formulation of national targets for regional development, in co-operation with other ministries and the regional councils (see detailed list of nine targets defined in 2004 in Chapter 2, Section 2.1). Both determination of targets and definition of strategies require the participation of all actors, in a process of negotiation to create a broad consensus. The general targets of regional development having been agreed in this fashion, implementation of strategies, programmes and projects, following a similar process, is based on a solid foundation.

Implementation of the three general targets (reinforcing regional competitiveness, safeguarding the service structure throughout the country, achieving a balanced regional structure) rests on a series of guidelines and shared responsibilities. The Government Decision on Development Targets specifically indicates that "Local and Central government and the regional councils acting as the regional development authority in the regions will be responsible for implementation of the national regional development targets. All administrative sectors are to contribute to their achievement, with major ministries (see introduction to Chapter 2) having to define their regional development targets and actions. In turn, regional councils take the national targets into account when drafting their regional strategic programmes (see below). These also include, in particular, EU regional structural fund programmes and special programmes such as the Regional Centre Programme, the Centre of Expertise Programme, the Rural Policy Programme and the Archipelago Programme. The regional strategic programme for Lapland includes a section dealing with Sami culture and industries drawn up by the Sami Parliament.

These regional strategic programmes must refer to the "regional plan", also drawn up by the regional council presenting the main long-term development aims of the region. To achieve these strategic aims, annual "programme implementation plans" are required. Coherence with land-use is ensured as the regional land-use plan, drawn up for a 15/25 year horizon and frequently up-dated, refers to guidelines contained in the regional plan (see

Figure 3.9. **Direction of regional development resources and bodies involved**



Source: Ministry of the Interior, 2004.

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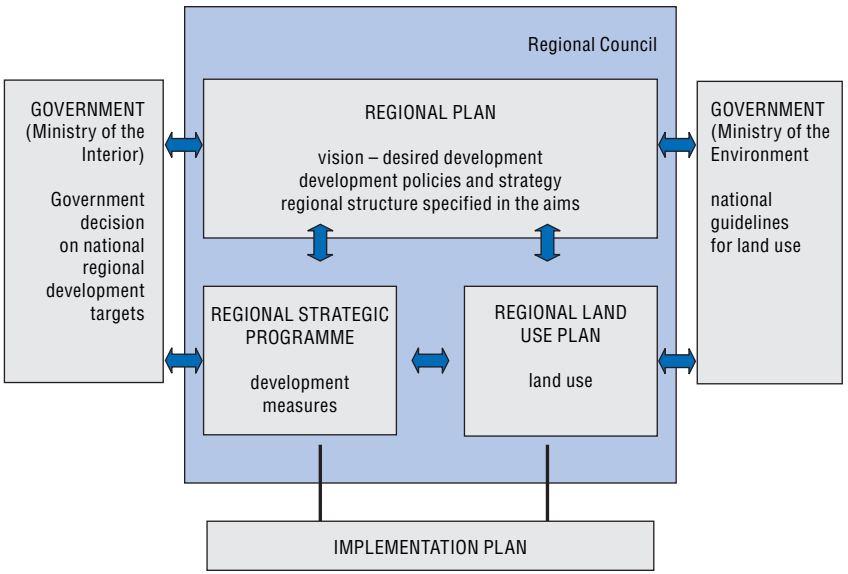
Chapter 2, Section 2.1). Thus, an important feature of the "Finnish approach" in regional development policy is that the breaking point of upper and regional responsibilities is not located at the boundary between strategy definition and implementation. Planning documents are produced jointly by State authorities, municipalities and other parties involved in financing (see Figure 3.10). This translates into a lengthy process (up to two years), but this is not infrequent in regional planning, as other country examples show. This is the case in France to achieve agreement amongst stakeholders on the "Contrats de Plan Etat Regions" (State Regions Planning Contracts) presented further (Box 3.3). In Italy, chances of success are recognised as being greater if the consultative process has been sufficiently long (OECD, 2005).

Figure 3.10. **Regional Planning System**



Source: Ministry of the Interior, 2004.

Vertical links remain divided into sectors

Processes have been recently engaged to strengthen regionalisation of important formerly direct central-level responsibilities, now delegated to Provincial Offices or, in the case of labour issues, to the TE Centres. Due to increasing specialisation in regional development, some decision-making power has been transferred. Regionalisation is monitored and strengthened by developing results management (top down from the Ministry of Labour) and

by reinforcing regional capacity to monitor local development trends. The Ministry of Labour recently launched a "Regional Strategies" project, which aims to strengthen two-way interaction (bottom-up and top-down) in order to better focus employment policy towards regional and local needs. Identifying the special features of each region is a precondition for focusing labour policy efficiently, as accomplished with success in Canada (see Box 3.2). Thus, TE Centres draw up their own regional employment and labour strategies, which follow the national employment policy strategy. In order to support employment policy pro-actively, advance local and regional information is also needed. The TE Centres even use a special Foresight method of Labour and Educational demand (TKTT) designed to monitor the regional features of the labour market and steer measures according to needs.

The regionalisation of central policy has also been launched in the Education and Welfare fields. These are placed under the responsibility of the ministries of Education and of Social Affairs and Health, represented by the State Provincial Offices (and their regional entities) at the regional level. Even if these last bodies are just territorial offices of their ministries, the rule for regulating interaction between the central and the regional level is based on responsibility and co-operation principles. In effect, The Ministry of Education drew up a three-year agreement (2003-2005) with the State Provincial Offices on promoting development of the regions, planning programmes and strategies, financing and evaluation. The agreements refer to the National Development Plan for Education and Research (KESU) drawn up by the Ministry of Education, constituting a central guideline connecting strategies at different levels. In addition, yearly negotiations on goals to achieve take place between the Ministry of Education and State Provincial Offices on the one hand and between the former and higher education institutions on the other.

Also, State Provincial Offices are controllers as well as providers, with the municipalities, of equal access to welfare services for every citizen, regardless of where they live. Their functions include steering and monitoring municipal social and health care services and prevention, and State subsidies for social and health investment and development projects. They are thus providers of earmarked actions and transfers encompassing redistributive missions, which are (in theory) better achieved through general purpose grants rather than specific purpose subsidies. On the other hand, their participation in a negotiation process involving three levels of government to harmonise strategies, as described above in the case of Education, can be considered a way of managing this escape from theory.

Under the Regional Development Act there are no changes regarding the relative powers of State authorities. The State's responsibility for development work is clarified when the ministries define aims, measures and financing of regional development in their respective sectors. The budgets of the nine

Box 3.2. **Federal Provincial Partnerships in active employment policy in Canada**

After a request from provinces to receive more control over labour market programming, the federal government offered in 1996 to turn over responsibility for active labour market programmes to the provinces. The offer encompassed the transfer of CAD 1.5 billion in 1997-1998 and 3 620 full-time equivalent staff from federal to provincial administrations. In the two years that followed, agreements were negotiated between the federal government and most of the provinces. As of June 2001, Labour Market Development Agreements (LMDAs) have been negotiated with all the provinces and territories except Ontario. The Agreements are of two types: the first provides for a "full transfer" of authority to the province/territory, the second type is designated co-management where there is no transfer of staff or funds. Under the "transfer" LMDAs, provinces and territories assume responsibility for delivery of active labour market assistance programmes similar to those described as Employment Benefits and Support Measures (EBSM) in the Employment Insurance Act. The "co-management" LMDAs involve an innovative partnership between federal and provincial agencies administering the EBSMs.

Preliminary findings from 11 completed formative evaluations indicate that LMDAs contribute to partnership and harmonisation of programmes and services and to local flexibility. Factors that have contributed to partnerships include a strong willingness to work together and maintain customer service during implementation. In some situations, co-operation has uncovered opportunities for efficiencies and economies. Evaluations in most jurisdictions indicated duplication had decreased or remained the same as prior to the LMDA. Moreover, over 75% of EBSM participants rated service as good or excellent. These results confirm that LMDAs are being used to assist eligible clients for employment benefits. Issues for further investigation include: the need to assess longer-term results, how to further improve co-ordination, and potential gaps in programming for non-Employment Insurance eligible clients.

Source: OECD Territorial Review of Canada, 2002.

ministries (apart from the Ministry of the Interior) responsible for regional development merely include sections which are considered regional development-related. Precise budget allocations are thus difficult to establish. According to the Regional Development Act, these ministries will for the first time define precise regional development budgets (as well as targets) in the State budget for 2005. As a result, the role of the State and State financing in regional development should become more visible and transparent.

Transfers and incentives

Transfers related to regional development granted by the central level in favour of Regional Councils (in addition to the contributions of municipalities, defined according to their size)[14] are of different kinds. The annual non-earmarked grant is meant primarily for regional development projects while specific transfers support both the Centres of Expertise and Regional Centre programmes. Grants for these programmes are allocated first to the regional councils. Regional councils than channel the grant to municipalities or common sub-regional economic development organisations, technology centres or science parks (in the case of Centres of Expertise). In the general grant, the regional council has a certain degree of freedom to choose which projects to support. In the case of the CoE and RCP, regional councils are bound to the priorities of the local programmes. On the other hand, yearly RCP and CoE funding depends on evaluation of impact of use the previous year. Good practices and results are thus financially rewarded. In general, the level of granted funding in relation to the applied sum is about 80%.

Looking at efficiency and impact of public spending in the area of regional development, it appears that such tools based on systems of bonuses and sanctions have not yet been devised and that only an accounting perspective, checking that funds are used within the timeframe and for the purpose decided is followed. A qualitative perspective is certainly more difficult to achieve in this field than that of public service delivery where precise and calibered standards, the degree of fulfilment of which can be measured, are to be followed by municipalities. Strengthening efficiency through incentives could also be conceived through possible competition among regions for financing of certain types of projects. Nevertheless, the Finnish culture of cooperation and effective equivalence of public services in the different parts of the country does not really seem conducive to this. The generalisation of a "results management" tool,[15] on the basis of objective criteria, could be a possible approach in the future.

Committees and the assignment of competencies

At the interface of vertical and horizontal relationships, coordination requires intermediary committee-type bodies:[16]

- The *Government Committee for Regionalisation*: regionalisation policy, strongly linked to the development of the Regional Centre policy is led by the "Government's Coordination Committee for Regionalization". Its objectives for further decentralisation are formulated in the transfer of public agencies from Helsinki (4 000 to 8 000 State jobs will be reassigned to the regional levels before 2011) as well as the decentralisation of central government activities to regional centres.

- At the regional level, the regional councils and state regional authorities monitor implementation, which is itself reviewed regularly at the national level by the *Ministerial Group of Administration and Regional Development (HALKE)*. This ministerial group discusses regional development and prepares major policy decisions for government approval.[17] HALKE includes the two ministers (Internal Security; Regional and Municipal Affairs) of the Interior as well as the Vice-Minister of Finance. It is an unofficial sub-committee of Ministerial Committee of Finance.
- The Minister of Regional and Municipal Affairs recently set up an inter-ministerial *Monitoring Group on Regional Development Measures* to follow the implementation of national regional development targets. The functions of the group are 1) to promote, monitor and coordinate the implementation of the targets; 2) to review and evaluate the effects of the targets and the effects of other State's regional development measures; and 3) report and make suggestions on measures to the Ministerial Group for Administration and Regional Development.
- *Regional Management Committees* support cooperation between regional authorities. They are based on a tri-partite agreement equally encompassing the regional council (and its member municipalities), State authorities (TE centres, State Provincial Offices) and representative labour market, trade organisations and NGOs. The regional council board appoints the Regional Management Committee and its chairman, an elected official of a member municipality. Budgetary constraints and implementation of EU Structural Funds have stimulated negotiations and co-operation among regional authorities. The Regional Management Committee co-ordinates the allocation of Structural Fund resources and corresponding national co-financing with a document known as the "regional co-operation document". Regional Management Committees have also contributed towards increasing co-operation in the case of nationally funded projects.
- Specialised committees complete this list. The inter-ministerial *Rural Policy Committee* is the main co-ordinating body in the field of rural policy matters (appointed by the Ministry of Agriculture and Forestry). The inter-ministerial *Regional Centre and Urban Policy Committee* was in charge of regional centre policy until 2001. It has been replaced by the *Advisory Committee on Major Urban Regions* (9) which prepares and promotes policy for large urban regions (a combination of the existing Regional Centre and Centres of Expertise Programmes). The *Committee for the Centres of Expertise Programme* is an experts, practitioners and ministry representatives committee, (co-ordination, evaluation, drafting of proposals). The Committee for EU Affairs comprises sections, which are horizontal committees at the central government level, with section 4 responsible for regional and structural policy, led by the Ministry of the Interior.

Assessment

The features of this governance framework can be summarised by three main characteristics:

- The Finnish multi-level governance system is marked by permanent interactive processes between the central and regional levels to define targets and ensure implementation;
- In the absence of more authoritarian modes of coordination, there is a multiplication of committees for regulation of vertical co-operation;
- A contradictory trend to cooperation principles is manifest: the thematic division of vertical actions (between the different ministries and their regional representative authorities) rather than fully integrated funding for regionalisation.

The following issues deserve proper attention:

- The multiplication of programmes and plans and the ensuing lack of sufficient clarity can be a source of confusion, both for the administrative bodies having to prepare related documents as well as for the applicants having to submit projects to different entities for approval and funding. Confusion can also result from overlapping mandates of committees dealing with similar issues.
- At the infra-national level, education seems to be directly managed by state provincial offices in relation with municipalities or joint municipalities, thus by-passing regional councils. A recommendation could be, on the basis of the fact that education is already considered as a strategic theme for regional development, to reintroduce the regional councils in the decision-making process of sub national education issues. Moreover, this would be a logical and useful measure for regional councils which have already to forecast needs for vocational education.
- Vertical co-ordination at the infra-national level seems to be complex because of the institutional weight of municipalities in regional councils.

The results of Regional Development Act implementation are not yet available, (except for certain mid-term evaluations, see urban policy, Chapter 2). It is thus difficult to assess the relevance of the selected methods. It could be nevertheless underlined that an important feature of this policy is that it obliges regional actors to elaborate the criteria of evaluation of their programmes simultaneously to the elaboration of the programme itself. What has been assessed for the moment is that regional development itself has not increased inter-ministerial co-operation very much. On the other hand, Regional Management Committees have brought regional authorities closer together in terms of cooperation. A recent study of regional policy (Government

Programmes for 2003-07) completed by Rapporteur ad int. Dr. Esko Riepula (2004) states various proposals:[18]

- To bring together available resources for regional development in different ministries in the national budget.
- To strengthen co-operative decision-making concerning resource allocation both horizontally (at the national and regional levels) and vertically (between the central government and the regions). In order to achieve this objective, a "result alliance" would be established as a co-operation forum between national ministries as well as a "regional board" to define regional aims and to make resource allocation more synergetic.
- To leave place for more democratic steering of regional development resources, in particular by securing for national parliament a clearer picture of the resources allocated for regional development, and of the problems and challenges facing each region. At the regional level, the author prones a stronger engagement of elected officials in these matters rather than allowing major decisions to be taken mostly within various organisations and technical agencies.

These proposals bring forward a certain number of questions that are also debated in other countries such as France, which has long developed a specific tool for regional development, the "Contrats de Plan État-Région" (CPER), presented in Box 3.3. As in France, the current limits of co-ordination of regional policy and regional development measures in Finland appear clearly. The recommendations seem to have been better accepted by the regional councils than by the ministries and their agencies at the regional level. The first of these suggestions is relevant but remain only a transitory solution towards a greater clarification of national regional policy budgets. The suggestion to introduce new fora of decisions at the regional and national levels could be useful if it supports other committee's work rather than just adding a new body. This brings up the question of the interaction between two possibly redundant structures: the proposed new "regional board" and the existing "regional management committee". To avoid any confusion, these new boards, if decided, have to be clearly conceived as predominant (primus inter pares). Following wide debate in 2004, it appears likely that the following measures will be taken:

- In the national budget, all important regional level allocations related to regional development would be gathered by administrative field.
- In Strategic Regional Programme Implementation Plans, preparation of the budgetary allocations would be based on negotiations between ministries and regional councils.
- Each sectoral ministry would allocate monies for regions.

- These allocations would be placed under the responsibility of bodies' co-ordinating at the regional level (TE Centres, State Provincial Offices, and Regional Councils).

Horizontal co-ordination

Horizontal co-ordination deployed for regional development will be analysed along the following lines. Firstly, traditional forms of municipal cooperation will be examined. Secondly, the various programmes included in the Regional Development Act for fostering stronger and more effective relations among municipalities will be presented. The incentives supporting this policy will then be explained before concluding with an overall assessment.

Inter-municipal co-operation in Finland

Municipalities can enter into cooperation agreements or create a separate organisation (joint municipal board) to handle their combined affairs. There are 240 joint municipal boards in Finland, financed by member municipalities, representing about 20% of total municipal expenditure. On an international level, there is an old and well developed tradition for building such boards. Inter-municipal co-operation is a legal obligation for the exercise of certain responsibilities in Finland,[19] as in Austria, Ireland, the United Kingdom and for small municipalities in Hungary.[20] These responsibilities comprise at least secondary health care (hospitals, institutions for the handicapped, emergency services), and vocational schools/high schools.[21] The allocation of tasks provided by joint municipal boards reflects the hierarchy of spending shares in municipal budgets, allowing for great importance to health and to education services. A trend towards progressive reduction of the number of joint municipal boards has been identified. It can be explained by the fact that interested municipalities are now included in larger boards, with existing boards attracting new members rather than having new boards created, while less efficient boards are phased out. Amalgamations have comforted this trend. It is to be noted that the decision to establish new boards or abolish existing ones is taken only by the corresponding municipalities.

Joint municipal boards are compulsory in certain cases and in others obey to the recognition that achieving economies of scale through co-operation is desirable, which entails voluntary co-operation in certain fields such as tourism promotion for instance (see Figure 3.11). The Local Government Act of 1995 (§2 and §76) sets that municipalities are free of using cooperative structures for offering these services. Joint-municipal boards are thus an on-going process, not only in their operation but also in their creation or suppression as developed above. From this point of view they can be considered as rather flexible tools permitting both management of public services and launching of

Box 3.3. *Contrats de Plan État-Région* (CPER)

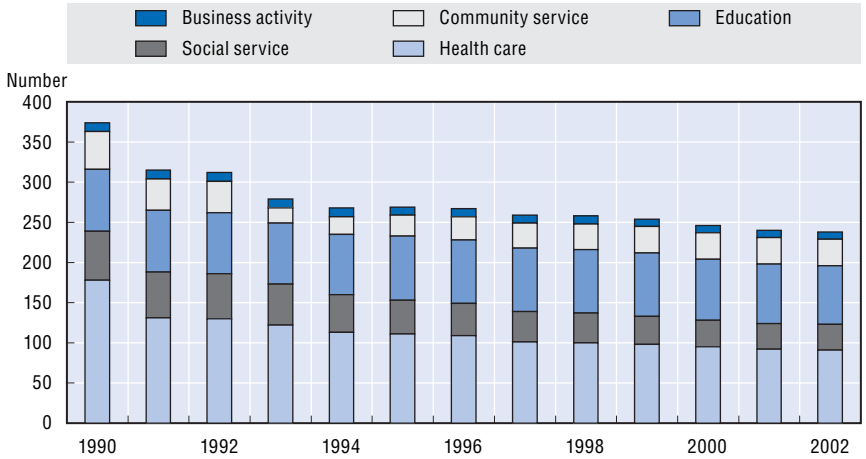
The "State-region plan contract" (Contrat de Plan État-région, CPER) is a key instrument of regional development policy. Contracts passed with all regions for the periods 1984-88, 1989-93, 1994-98/99 and 2000-06 have progressively enlarged their scope and expenditure amounts. The contract is a detailed document, setting out a series of policies and programmes to be carried out for a certain period. The central government and the region jointly finance the projects in the contract. Recent contracts include contributions of European structural funds and infra-regional governments. The contract includes a financial appendix stating the exact financial commitment of each party for the period covered. Contracts do not necessarily imply budgetary transfers between the central government and local governments; instead they usually stress the commitments of each, while providing a detailed description of the purpose of each measure.

Although the CPER have proven their usefulness and are a strategic part of the French regional development landscape insofar as they oblige sectoral ministries to allocate specific sums to regional programmes and projects, some shortcomings can be noted. Certain critics see such arrangements as being more an instrument of State devolution than as imparting any real impetus in partnership terms. The approach also tends to remain much too top-down due to the stronger negotiating power of the State with the consequences that priority actions do not differ significantly from one region to another. Another issue resides in implementation delays that may require extension beyond 2006. Underperformance is usually the consequence of delays in availability of funds, stemming from budgetary regulation, but reallocations, underestimation of costs or unfinished preliminary studies are also mentioned.

French authorities are aware of these problems. An evaluation of the CPER device, currently in process, has generated a number of recommendations. Among them, the proposal to re-centre the planning contracts around a limited number of structural policies is a crucial one but a lot of observers believe that reforming the device in this way will threaten local initiative. Another important recommendation is related to the insufficiency of the evaluating process that could be improved through a more transparent and independent council for evaluation. Other financial considerations have also led to recommend greater budget "flexibility". A last important recommendation is that in order to strategically reinforce the long term coherence of the various CPERs a "national scheme with a long term perspective" could be set up. The region would be in charge of a "strategic document of orientation" which would consolidate its role as the leading intermediary structure between the national and local levels.

Source: Based on information provided by DATAR.

Figure 3.11. **Joint municipal boards**



Source: Ministry of the Interior.

new types of co-operation between municipalities in different areas such as provision of network infrastructure, in case of default of the private sector.

Sub-regions obey to a different logic. They are only in Finland statistical units, although they can in a wider sense help to foster local identity. The sub-regional territorial division was established in 1994 as a tool to monitor regional development and development needs.[22] The borders of Finnish sub-regions are decided by the Ministry of the Interior (by negotiation with municipalities) and adjusted if necessary. There are 82 sub-regions in Finland, three of them in Åland, (NUTS 4 level). This division is used to define the EU structural fund objective areas. It is mainly based on labour market and commuting areas. The sub-region thus corresponds to certain economic and social realities, rendering it appropriate for local development strategies, including those based on small and medium-sized urban hubs with influence over a wider area, such as promoted by the RCP programme (see Chapter 2, Section 2.2).[23] This can perfectly be commensurate with an increasing role for development agencies at the NUTS 3 level, insofar as strategies complete each other and overlapping is avoided. In countries such as France or the Czech Republic, where economic co-operation between municipalities is well developed, regional development agencies fully perform their tasks, co-operating with micro-regional or inter-municipal entities.

New programmes for inter-municipal policy

The main objective of inter municipal co-operation is the improvement of efficiency in public spending. If this is to be achieved, is there an optimal

scale? This is a difficult question because theoretical models do not provide one solution. It is especially hard to define the optimal size of a municipality or municipal grouping. Some countries remain attached to the idea of reinforcing mergers by using one specific public service as the proxy for defining the size of the multi-services operators that the municipalities finally are. In Denmark, for example, the policy concerning mergers relates to criteria based on the efficient size for providing education services, considered to be 30 000 people. However, most countries rely on voluntary decisions from municipalities rather than on hierarchical decisions (see OECD, 2005, "Building Competitive Regions; Strategies and Governance"). This is the case for Finland, which also uses experimental approaches to identify the best adapted solutions.

The SEUTU project. SEUTU (sub-region in Finnish) is a project which aims to increase and develop co-operation between municipalities at the sub-regional level (see Box 3.4). The goal is to devise measures by which the equal accessibility and financing of public services can be safeguarded. This is carried out by developing co-operative production of services and developing new structures for decision making (*i.e.*, sub-regions' councils). The SEUTU project is based on the Act concerning experiments on sub-regional councils as well as the Act concerning experiments on sub-regional co-operation (2004). It was launched in 2000 by the Ministry of the Interior in collaboration with the Finnish Association of Local and Regional authorities. Municipalities are offered the possibility of electing a sub-regional council for a four-year period.

One of the selected sub-regions (Nivala-Haapajärvi) in the project had decided in principle to implement a sub-regional council as part of the experiment but it was never established. Only two municipalities accepted to join the sub-regional council in 2004 and one of the municipalities wanted to delay membership until 2008. The main reasons expressed were that co-operation was being built in the wrong order (structures before projects), with an improved financial situation in the municipalities coming to the rescue of municipal autonomy. Still, co-operation will be engaged in the fields of health care, education and basic infrastructure through joint municipal boards.

Evaluation of this project up to now seems to have been rather critical (Haveri, Nyholm, Airaksinen, April 2004). Two main brakes seem to explain the limited success of this experiment. The first is the apparent lack of willingness of the municipalities to really enter into such co-operative processes by further transfer of basic services, although sub-regional co-operation has proceeded quite well in the fields of economic development policy, physical planning and supporting services. The second concerns the institutional limits of the sub-region's decision-making power compared to those of rather

Box 3.4. **The SEUTU Project**

The SEUTU project launched in 2000 by the Ministry of the Interior with the Finnish Association for Local and Regional Authorities aims to support and promote voluntary sub-regional co-operation of municipalities, in order to safeguard the delivery of public services, to practice successful economic development policy and to implement efficiently land-use planning and environmental protection. Decentralisation of decision making is promoted for this purpose and municipal self-governance strengthened (*i.e.*, some local state activities transferred to sub-regions). The tasks of the SEUTU experiment are 1) support to draw up common sub-regional strategies and development programmes; 2) prepare a proposal for special legislation on co-operation; 3) inspect and prepare, when needed, general changes to legislation (promoting voluntary municipal groupings); 4) prepare government measures supporting sub-regional experiment; 5) monitor and evaluate the experiment; and 6) make proposals for further action.

SEUTU has eight pilot sub-regions, chosen from the 30 sub-regions expressing interest in joining the project.* The subregions of Hämeenlinna, Lahti, Loimaa, Nivala-Haapajärvi, Oulu, Pieksämäki, North Lapland and Turunmaa are those involved. Government financing of SEUTU is around EUR 650 000 in 2004. The municipalities co-finance projects for equivalent amounts. The Ministerial Group of Administration and Regional Development proposed at the end of 2004 to expand the SEUTU project to seven new regions (15 in total). These new regions would be Kaustinen, Kemi-Tornio, Kuopio, so called "Kuuma" sub-region (Central Uusimaa), Mikkeli, Savonlinna and Ylivieska. Legislation was enacted in January 2005 to permit this extension, including continuation of the whole project until 2012.

Selection criteria includes eight items: selected sub-regions should be many-sided and represent different kinds of regions in Finland, sub-regional co-operation has to be organised adequately, municipalities have to commit to supra-municipal work by decisions and financing, synergy with the Regional Centre Programme should be reached if possible, co-operation has to be innovative to some extent, cover many fields, be possible to implement easily. Sub-regions are expected to participate in preparation of necessary legislation in the future.

* The Regional Centre Programme also has a role in sub-regional co-operation. RCP's focus lies in supporting and speeding up collaborative methods and culture between municipalities in a sub-region. RCP, contrary to SEUTU does not include basic service delivery.

Source: Based on information provided by the Ministry of the Interior.

strong co-operation structures such as existing joint municipal boards. Management of co-operation does not seem to be working quite well in the eight pilot regions and participation of the member municipalities is not yet wide enough. In the future, sub-regional solutions could depend on effective leadership at the regional level recognising the importance of effective sub-regional partners, which seems in contradiction with the present weakness of the regional councils representing municipalities rather than themselves.

The Kainuu experiment. The main reason invoked to launch an experiment in the Eastern region of Kainuu (see Box 3.5) is to search for new ways to tackle

Box 3.5. **The Kainuu experiment in regionally-elected self government**

In Kainuu, the democratically elected regional administration will have decision-making power on certain services on regional development and regional planning. Regionally provided services will be social services, health care and education (including high-schools and vocational institutes but excluding elementary school). These will be organised by one joint municipal board, "Kainuu Region Joint Municipal Board", including social services, health and education. Staff from the municipalities and existing joint municipal boards will be supplied for this purpose to the regional board. Personnel from the Regional Council of Kainuu, the Joint municipal board for special health care, the basic social and health care services in the municipalities (excluding day-care) and that of high schools and vocational schools will be transferred to the new "Kainuu Region Joint Municipal Board". This new body will have altogether 3 400 employees. The old Regional Council and earlier Joint municipal board for special health care in Kainuu will be abolished.

The role of regional offices (TE Centre, State provincial office, Regional environment centre, Forest Centre and Regional Unit of the Finnish road administration) will remain unchanged concerning use of allocated funding, but they will give guidance and allocations to the new regional council. Ministry of the Interior financing for the Kainuu experiment is EUR 1 million for three years (2005-2007), with approximately the same amount contributed by municipalities. The "Experimental project on decreasing Social security Charges" in certain lagging regions such as Lapland and the archipelago regions will be expanded to include the Kainuu region. Since the beginning of 2003, employers in these areas do not have to pay any social charges, the aim of this experiment being to assess how the reduction of social charges has a positive impact on employment.

Source: Based on information provided by the Ministry of the Interior.

the problems of this devitalised area (decreasing population, high unemployment). The economic and financial situation of municipalities in Kainuu is difficult and is getting worse. The production of services will be even more challenging in the near future due to the limited resources of individual municipalities. The development trend would also concentrate services to the regional capital of Kajaani. The goals of the self-government experiment in Kainuu, starting in January 2005, rise also from the need to get regional and economic development actions more focused and synchronised. Larger-scale projects are now needed and thus resources have to be gathered at the regional level. This experiment raises challenging issues: can regional self-government in a distressed area better contribute to regeneration than the existing framework? Since the contemplated "Joint Regional Development Board" will have a mandate concerning the delivery of public services, will the economies of scale generated be reallocated to economic development or will specific programmes support these measures? Can the Kainuu experiment be considered as a first step in a process of amalgamation of the eight partner municipalities or will it prepare the ground for deeper regionalisation in Finland?

Incentives and amalgamation issues

The Finnish Act concerning the Experiment on sub-regional councils (2004) allows municipalities to agree on the financing of the sub-regional administration in two alternative ways: based on population or based on a certain share of revenue of the municipalities. This includes the possibility that municipalities can agree on how the corporate income tax revenues of each will be allocated in the sub-region as has successfully been done in France (see Box 3.6 below). Only one sub-region (Jyväskylä) has used this possibility up to now. The Jyväskylä Regional Development Company (Jykes, Ltd) has funding consisting of two elements. The first part (approximately 90% of revenue) comes normally from the municipalities' membership fees according to their population. The second part (approximately 10% of revenue) comes from the revenues of municipalities' corporate income tax so that 2% of this tax revenue in total will be directed to Jykes.

In Finland, municipalities can be granted a subsidy to amalgamate (see example of Rovaniemi in Lapland, Chapter 2, Section 2.3). This grant is an incentive through which the Government strives to merge municipalities into functionally and financially more efficient units. The amount of the subsidy, allocated in a decreasing way over a five-year period, depends on the size of the municipalities, with a maximum of EUR 6.7 million over a four-year period. A recent Finnish study (Moiso and Uusitalo, 2003) concluded that mergers are, at least at the beginning, more costly than keeping autonomous municipalities or, at best, permit only a slight saving in municipal expenditure (as assessed in Switzerland, Steiner, 2003). In order to by-pass this drawback, Finnish authorities

Box 3.6. **The single business tax system in France (Taxe Professionnelle Unique)**

In the absence of incentives, laws related to the reinforcement of inter-municipal co-operation seldom produce significant results. In the French system, a number of laws call upon fiscal incentives to encourage inter-municipal collaboration. Voluntary co-operation is promoted by offering municipalities an incentive grant, in addition to their existing general purpose grant entitlements. One of the conditions is that the municipalities adopt a single business tax system (Taxe Professionnelle Unique, TPU) within the area (the business tax is the main local tax in France). Under this system, a firm will pay the same rate no matter where it chooses to locate within the group of communes that have jointly adopted the tax. The TPU is compulsory for new urban communities and for communities of agglomerations and optional for communities of communes containing fewer than 500 000 inhabitants.

In the partner municipalities, the EPCI (Établissement Public de Coopération Intercommunale), *Public agency for inter-municipal co-operation*, fixes the tax rate by vote and receives the entire revenue from the tax (any revenue which has not been spent must be re-allocated to the member municipalities). However, under a 1999 law, member municipalities are given a ten-year delay to reach an agreement regarding the single business tax rate for the whole area. Compensation is attributed to each member municipality, according to the previous amount of collected tax.

Source: OECD Secretariat.

have devised a specific way for dealing with these expenditures for first steps: since 2002, there is an added investment and development subsidy[24] which can be granted separately for economic development, community structure, environmental protection, education or social welfare purposes. The maximum grant amount is EUR 1.7 million, and the tacit rule seems to protect current staff of the merged municipalities. So far, only a few municipal amalgamations have occurred each year. In 2005, a total of nine amalgamations will take place, reducing the number of municipalities by 12. Nevertheless, it is predicted at the central level that more amalgamations will occur in the near future than before, mainly because of the growing difficulties for municipalities to achieve health and social welfare standards in a context of ageing and reduction of local personnel.

Assessment

However relevant these different experiments and programmes may be, it seems that municipalities remain very free for opting in or out.[25] Even regarding economic development policy, collaboration is spreading, but

numerous municipalities still set their own economic policy agenda themselves. Thus even if best practices are identified or solutions to reach them are proposed, the difficulty will be to convince local authorities to adopt them. This is a frequent situation in countries where municipalities have important power of decision and are perceived as the basis of public action. In Finland, this underlines a contradiction that will have to be resolved in the future: how can the development of the regional level be encouraged while pursuing simultaneously goals to support inter-municipal co-operation, thus strengthening a level of government that still retains stronger powers than the regions themselves?

It appears appropriate to conclude this section with a major question concerning the continuous process of regionalisation following the incremental method used in Finland. The central government gives the decisive impulse through policy and regions consolidate their power on the basis of the voluntary co-operation of municipalities. Horizontal co-ordination of regional development policy is ensured at the national level by measures related to the Regional Development Act and by co-ordination through committees in particular. At the regional level, the number of actors involved, even only in one policy area, is much more important. Innovation issues would typically concern TE Centres, State Provincial Offices (for Education), universities, science parks, municipalities and their joint municipal boards, the private sector with the regional council (and its regional management committee) having to ensure permanent co-ordination and validation in reference to the regional plan. The co-ordination task now also covers the regional development strategies of ministries.

Is there a critical threshold in terms of feasibility of flexible and consensual co-ordination? In other terms, wouldn't it be more efficient to empower regional councils more strongly in terms of regional development competencies so that most tasks could be devoted to strategies and implementation rather than to securing prior agreement with a vast array of actors, which is particularly resource consuming and lengthy? Insofar as municipalities are proportionally represented in regional councils and that regional cities seem to assume a leading role in regional development issues,[26] strengthening of the regional level would not be at the expense of consensus building which could be achieved through processes of consultation and working groups created at the initiative of the regional council. Most European countries having followed the path of decentralisation and regional self-government at different times, whether Spain at the end of the seventies, France at the beginning of the 1980s or the Czech Republic at the beginning of the millenium, have all devolved direct and clear powers to the regional level serving the purpose of democracy and efficiency simultaneously.

3.4. Citizen participation

In an economy that places a very high value on knowledge, regional policy cannot afford to disregard the cognitive resources available. Among the variety of Public Private Partnerships (PPPs), some are devoted to support innovation provided by clusters (Section 3, Chapter 2), and some are mainly conceived as means of finding others sources of funding for the supply of local infrastructure or public services delivery (Section 4, Chapter 2). There is a third type of PPP which can be called "participatory PPP" for territorial projects (OECD, 2005), involving active participation of civil society.[27] Economic sociology, since the seminal publication of Granovetter in 1985, shows that economic innovative development rests on social-effective networks. The notion of "embeddedness" is easier to understand at the local rather than at the national level, where personal interests and individual links are more aggregated. On the other hand, comparative analysis of social capital is more difficult in a regional than a cross-country setting. Key concepts such as trust, norms and civil society are fundamentally collective notions, and it is extremely difficult statistically to measure their effects within a given territory, let alone proceed to objective comparisons. This section will address issues of inclusiveness, looking at electoral turn-out, citizens' participation in public local decisions, involvement in non profit organisations and labour unions and lastly policy responses aiming to further citizen participation or entrepreneurship in a country where consensus seeking and strong local level public intervention through municipalities can bear on individual initiative.

Participation in local decisions and civil society

According to Putnam (1995), social capital refers to features of social organisation, such as trust, norms and networks that can improve the efficiency of society by facilitating co-ordinated actions. Social capital can improve government performance in three ways:

- It can broaden government accountability, making governments responsive to citizens at large.
- It can facilitate agreement where political preferences are polarised.
- It is associated with greater innovation when policy makers face new challenges.

The main difficulties regarding such issues are measuring of social capital and government performance and of setting a causality link between both. Knack (2000), using for the US case an index of social capital built on criteria such as trust, volunteering and census response, shows that in states with more social capital, government performance is rated higher. Although this type of literature is now frequent, the elaboration of criteria is not completely satisfying. Various authors express their concerns about the

"catch-all" character of the concept of social capital which amalgamates various objects such as "beliefs, behavioural rules and such forms of capital assets as interpersonal links" which could be studied separately (Dasgupta, 2001; Ponthieux, 2004). Whatever the academic project linked to this notion, different criteria of citizen participation to public processes are worth noting since they constitute elements in favour of the dynamism and the institutional innovation of local society. Then, proxies for evaluating the social capital of different Finnish regions may help to better understand disparities related to the "networking capability of a territory". The first of these is the participation rate in elections.

Finnish electors,[28] like the majority of European citizens, pay more attention to national elections than to elections to the European Parliament: the participation rate for the latter was only 41.1% in 2004[29] while it was 60.3% in 1996. The most important participation rates are reached for the Presidential elections. The 2000 election that led to the election of Mrs. Tarja Halonen, shows a very high national second round rate of 80.2%, with only marginal differences across regions (except Åland with 61.6%). The results of the 2004 municipal elections, with voting turnout of 58.5%, show a significant increase in the share of women among the elected councillors: 36.3% (1.7% more than for the 2000 municipal elections). The regional variation of the voter turnout among the municipalities for these elections is not very important: from 55.3% in North Karelia to 65.6 % in the Vaasa area. However differences are greater between municipalities: the highest voting turnout of the country, 89.5% was attained in Iniö (Turku archipelago; population, 251 inhabitants) and the lowest in Vantaa (50.8%), one of the lesser affluent municipalities of the Helsinki Metropolitan area.

It is worthwhile mentioning that the Kainuu elections at the end of 2004, experimenting the direct election of the regional councillors, produced low voter turnout at 51.2%, clearly less than the lowest rate of municipal elections. This weak rate for participating in the experimented process cannot necessarily be seen as a failure, as lack of voter concern may come from difficulty in understanding the issues and possible changes because of the smooth functioning of the municipal system and Welfare State, rather than scepticism about the expected reforms. However it would be necessary to analyse why local citizens do not feel very concerned about this experiment, especially to assess this process before possible extension.

There is no formal system of direct citizen participation in Finland (Mäenpää, 2002). Residents are free to associate and can gather towards any aim but these conventions or assemblies have no direct responsibility in the control of local affairs. However there is a "right of initiative": if 2% of local electors submit a question belonging to municipal council competencies, it must insert the initiative in its agenda within six months. Above all, for long-

term decisions related to urban planning and the environment open public processes are compulsory. Some form of public consultation may also be organised for decisions related to public services such as education. The organisation of these public consultations are not institutionally ruled and rather left to the local authorities' decision. Transparency is a basic principle of municipal governance in Finland and documents related to municipal decisions are available on-line.

Associations are easy to create in Finland and this right is safeguarded in the Constitution. The fields of Finnish associations are various: sports, culture and arts, charity, but they can also concern local projects, such as those in which the Village Action Groups (see Chapter 2, Section 4) are involved.[30] According to the "Leisure Study" by Statistics Finland (2005), 52% of Finns in 2002 participated in activities provided by at least one association, compared to 58% in 1981. Most important losses have been in professional associations (drop from 21% to 8%) and in political associations (from 6% to 2%) whereas sport associations gained interest from 17% to 23% and other associations (culture or hobby associations) from 12% to 19%. Relatively to population, the highest numbers of associations is in Lapland and Kainuu, which are economically not as well off than other parts of the country. However the share of individuals belonging to at least one non-profit association is greater in regions like Etelä-Savo and Etelä-Pohjanmaa. It could be deduced that in economically less developed areas, the will to build an association is high (and there are many) but the inter-individual linkages are poorer (and there are less people in each association). A more pragmatic explanation could also be found in the difficulty to manage such inter-personal links in remote areas with very low population density. It should be recalled that NGOs and other associations are members of the Regional Management Committees (see "horizontal co-ordination" in this chapter).

Regarding participation in public life, Finland is characterised by the important role of labour unions. Labour associations are numerous and most of them belong to one of the three national federations. The union density rate (more than 70%) in Finland is one of the highest in the world: in 2000 Finland was the third OECD country behind Iceland and Sweden in terms of syndication rates (*OECD Employment Outlook*, 2004). In Finland, Iceland and Sweden, over three out of four salaried workers are unionised today, while the figure is only one in eight or less in France, Korea and the United States.[31] Finnish union membership includes not only wage-earners and the unemployed but also "special groups" such as students, pensioners or the self-employed. At the local and regional levels, there is a regional advisory committee with a three year mandate. This committee promotes employment and economic development issues. Under the leadership of TE centres, labour associations, regional development authorities and other partners participate to this body. Under

the responsibility of the labour administration, there is also a local labour committee which is led by the public employment office and in which local labour associations and the municipality participate. These committees underline the consensual approach applied in Finland, in this case relating to issues that, in many other countries, are more contentious.

In Finland, the importance of social capital was recognised as early as 1998 in the Report of the "Special Parliamentary Committee for the Future". This document contains a special section about social capital focusing on the importance of education, as well as productivity and equality, from the standpoint of the potential of individuals. Even if inter-regional comparisons are difficult to establish, the exercise of evaluating the impact of social capital indicators at the regional level has been attempted by A. Alanen and L. Pelkonen in 2000. The findings of their study suggest that during the whole period under review from 1970 to 1990, there is a detectable and consistent statistical association between social factors and regional growth. Electoral turnout was not found to have any statistical association with regional economic growth. By contrast participation in leisure organisations showed statistical correlation with economic growth during the 1980s, whereas participation in interests' organisations and religious movements did not.

Policy approach

The policy programme on civic participation

In 2004 the Ministry of Justice launched an inter-ministerial broad-scope programme aiming at: improving civic education, contributing towards building a framework for civil society, improving traditional and new modes of participation and reinforcing the structure of democracy at the municipal and the national levels. This programme is one of the Government's key priorities and one of its main characteristics is the development of an evaluation process of this programme, organised from its inception. The actions encompassed in the project to improve electoral participation and to provide opportunities for active civil participation between elections are linked to the role of schools in citizenship education, to the review of government communications by the Prime Minister's Office, of on-line forums related to public life and to youths participation in civil society organisations. The policy programme aims to support projects[32] by promoting research regarding Finns as citizens, the changing challenges of citizenship, social capital, indicators of citizen participation and the state of democracy.

Under-qualified adults

As Lundvall and Borras have shown, what is important in innovative processes (for the economic success of individuals, firms, regions or nations)

is not the stock of knowledge but rather the ability to learn and thus to build new knowledge (Lundvall and Borras, 1999). Although the Finnish educational system is highly rated, there are some under-qualified adults. A programme of training in favour of this population, launched in 2003 for four years, called "Noste" in Finnish, "uplift" in English addresses the 380 000 Finns between 25 and 59 years old with no post-compulsory qualifications.[33] However, the budget of this programme will allow the participation of just 40 000 volunteers (EUR 57.5 million spent during the first three years). The training periods, (up to three years), has attracted a growing number of volunteers: 3 400 in 2003 (5% are unemployed). Adults planning to pursue future studies often have a great deal of experiential knowledge. They do not need to start from scratch but can build their formal training on their prior knowledge and skills. The programme has a twofold objective. Firstly it is a social promotion and employment tool. Secondly, it is an instrument to counter the effects of ageing of the population by building the competencies that will be lost because of the important retirement flow. Unions and employers are partners in this programme and contribute to promote it. As with programmes to bolster employment, local actors are also stakeholders: local centres for vocational training, high schools, business centres, and associations are required to respond to needs. Noste is another illustration of the "Finnish consensus".

The "Entrepreneurship Programme"

Social capital addresses the positive effects of the embedding of people in a relatively stable community creating social relationships. However, these social capital values have to be counterbalanced by a "creative tension" (Sotarauta, 2000), needed for responding to the insecure and uncertain future of a turbulent world. "Actually, social capital and creative tension should not be seen as competing forces in regional innovation systems. Both are needed and should complement each other in order to keep sufficient social cohesion and creative drive in regional innovation networks" (Harmaakorpi and Pekkarinen, 2003, pp 4-5). In order to promote such a creative tension, Finnish authorities have set up an Entrepreneurship programme (see Box 3.7).

Finnish authorities are aware of the necessity to strengthen the entrepreneurship culture in order to support economic development in the near future. The Entrepreneurship Programme for the 2004-2008 period answers this concern. However it must be underlined that this programme is not only aiming at promoting the emergence of start-ups but also at ensuring a stable business environment for enterprises. As entrepreneurship in a country with a strong tradition of local public intervention within the concept of the Welfare State is not strongly embedded in the national consciousness, the programme seeks to foster a progressive change in attitudes.

Box 3.7. **The Entrepreneurship Programme**

The Entrepreneurship Policy Programme started in 2003 seeks to create a business environment that will enhance the start-up, growth and internationalisation of enterprises. Another aim is to provide enterprises with appropriate conditions for long-term investments and employment. A horizontal ministerial group is responsible for design and implementation of the programme which is co-ordinated by the Minister of Trade and industry, implying co-operation with: the Ministries of the Interior, Finance, Education, Agriculture and Forestry, and the Ministry of Labour. These Ministries will provide resources such as technology funding, general aid to business, the Regional Centre Programme, the Rural Policy Programme, the use of labour policy resources for promotion of entrepreneurship and the network of polytechnic and universities.

The Entrepreneurship Policy Programme consists of five sub-areas: entrepreneurship education and training and counselling; business start-ups, growth and globalisation of enterprises; taxes and payments affecting entrepreneurial activity; entrepreneurship in regions; legislation affecting enterprises and the functioning of markets.

Source: Based on information provided by the Ministry of Trade and Industry.

Even if the programme clearly recognised that planning and implementing business policy need to keep in mind that the circumstances and conditions of entrepreneurship vary greatly in different parts of the country, this specificity of treatment is not really attested. The fact is that the varying needs of the regions are taken into account when deciding the priorities of the actions and allocation of resources, but the criteria for such decisions are not clearly defined. Reaching the regional objectives of the programme is left to the improvement of collaboration between administrative sectors and among regional actors. Canada provides examples of such collaboration supported by agencies (see Box 3.8).

In Finland as already underlined, there is a highly shared culture of consensus in a sense that it can be considered to be an implicit reference in policy making and more so, implementation, supposing a continuous process of negotiation to reach agreement. With such a view, it could be considered that a programme for reinforcing citizen participation and/or civil society organisations might be superfluous. Indeed, collective answers by citizens usually appear preferred to individual ones (explaining the low level of entrepreneurship). However the renewed political will for reinforcing such a culture and adapting it to new challenges by involving more citizens and their

Box 3.8. **The Atlantic Canada Opportunities Agency**

The Atlantic Canada Opportunities Agency (ACOA) of the Government of Canada was created to promote an entrepreneurial culture across the Atlantic Canada region. The agency aims to make more people aware of opportunities for business creation and support, thereby helping to increase the rate of small business creation and the success rate for small businesses. It offers programmes and services for future entrepreneurs, business owners and managers, non-commercial organisations, communities and academic and research institutions throughout the region.

Education can be an important means of developing entrepreneurial skills and changing mindsets to encourage more positive attitudes towards business creation. ACOA has developed programmes aimed at both schools and universities, including the development of entrepreneurship skills among post-secondary students and curriculum materials on entrepreneurial values and concepts for use in kindergarten through 12th grade classes.

In Newfoundland and Labrador, ACOA has supported the creation of the Y-enterprise centre, which is aimed at supporting entrepreneurship among young people by providing counselling and small business information for young entrepreneurs. It also organises an "Enterprise Olympics" which showcases the best business plans developed in enterprise education courses. In addition the centre provides in-house training for teachers and administrators.

Source: OECD Territorial Review of Canada, 2002.

associations in democratic processes, in particular at the local level, seems to promote a new interpretation of the notion of public service. The idea is to disconnect the notion of public good from the one of state public supply in the traditional Welfare State context and to replace it by the concept of collective good, offered by combinations of public and private actors, in particular here the non-profit ones. This strategy could be one of the answers to the growing costs of keeping such a high level of services in a context of ageing population.

3.5. Future developments

In the area of governance, which is closely linked to regional development concerns and impacts on the capacity of national, regional and municipal authorities to contribute to territorial development and growth but also conditions the quality delivery of public services in a cost efficient fashion, overall assessment of Finnish strengths and weaknesses offers a

contrasted and unique picture of flexible and pragmatic adaptation. This is effectively the case for public service delivery facing increasing costs, for the evolution of regional council's roles and also building the agenda of regional development at the national level. This however leads to complexity in the overall policy picture that can constitute an obstacle to a clear understanding of often innovative policies.

Concerning public service delivery, adaptation to new budgetary constraints fully take into account Finnish culture and traditions relating to the role of the Welfare State and the governance sharing of responsibilities between the national level (steering) and the municipal level (applying but with latitude on best ways to integrate local needs and conditions without compromising on the egalitarian ethic nor on quality). Because of the rising cost of delivering these services, particularly in certain peripheral regions, where these also contribute to anchoring population and firms, how far can municipal co-operation go in providing an adequate answer in the face of the ageing phenomenon? Will more amalgamation be necessary and is a more pro-active approach from the national level required? Some of the analyses of this review provide basis for future investigation.

The empirical method indicated above is also the one used to progressively shape and extend regional development council's prerogatives while preserving the strong traditional role of municipalities in the area of economic development. The region is the territorial entity of reference for strategies and investment in a globalizing economy and this is one of the factors explaining the strengthening of this level of government in many countries. Can this regionalisation process be pursued in Finland without a clearer separation between the economic development roles of regions and that of municipalities? Can regional councils continue to be a “club of municipalities” with indirect democratic legitimacy rather than a self-governing body with the full capacity to initiate regional development strategies? The case of France, still a quite centralised State, is an interesting one to ponder since regions, in this context, have nonetheless seen their powers increase while the contractual approach with the National level has been strengthened. International and particularly European trends can be a reference for future debate in Finland.

Concerning the overall governance mechanisms of regional development policy as it is managed from the national level, with the strong creative role of the Ministry of the Interior, higher than proportional when referring to its budgetary allocations as compared to certain sectoral ministries, the question is: how will regional development be integrated into economic development policy in a context of globalisation? Following Finnish tradition, there is a strong “rural lens” and concern for peripheral and less favoured areas but up to what point will this translate into recognition that regional competitiveness is a key to national performance? This would contribute to reinforcing and

"mainstreaming" approaches like the Regional Centre and the Centre of Expertise Programmes, thus fully integrating these into a national innovation system still largely based on high technology and metropolitan/urban environments.

The "step by step" approach of Finnish policy, well in line with national cultural traits also explains the complexity of governance and co-ordination mechanisms for regional development, stemming from multiple initiatives, programmes and projects that blur the overall vision for citizens and businesses alike. There undoubtedly is a vision of regional development based on stronger local and regional initiative, partnerships and fora for democratic debate but the overall picture remains "fuzzy", what with new initiatives being launched without previous ones disappearing or being integrated into the latest programmes. Greater visibility by simplification of the overall "policy scenery" and better identification of responsibilities at all levels would certainly contribute to a clearer understanding of the goals pursued and the changes and efforts required to this end. In a way the "Finnish innovation model" should be applied to explaining and marketing of regional development policy itself.

Notes

1. The evolution of EU regional policy, putting emphasis on the promotion of the factors of competitiveness, seems to plead in favour of a strong and effective regional policy.
2. Regions which are gathered in the TE outline are the following: Uusimaa and Itä-Uusimaa; Häme and Päijät-Häme; Kymenlaakso and South Karelia; Ostrobothnia and Central Oostrobothnia; and Southwest Finland and Åland. Other regions have the same boundaries than the TE centres.
3. The funds for operational costs of TE Centres are located in the Ministry of Trade and Industry.
4. It should be noted that mayors in Finland, contrary to most countries, are not the elected official but a person chosen on basis of experience by the elected municipal council.
5. Figures represent 2001 local public expenditure as a percentage of GDP, from Dexia's *Local finance in the twenty five countries of the European Union*, Paris, 2004.
6. Finland actually has a Dual Income Tax (DIT) system, which was implemented in 1993. Under a DIT system, all household income is divided into two components: capital income which includes dividends, interest income, capital gains and rents; and the labour income. For more information, see *OECD Economic Surveys: Finland 2002*, Paris.
7. Calculations based on 1999-2004 municipal tax revenue figures from the Department for Municipal Affairs.
8. This position was presented by the Department for Municipal Affairs of the Ministry of the Interior.

9. Resources are based on membership fees in proportion of the population of each member municipality and by service fees and revenues, in particular from its affiliated companies. The governing body is the General Assembly in which all municipalities are represented, the smallest having at least one member. The assembly elects a council, the latter choosing a board meeting monthly, which is assisted by a series of advisory boards in different areas (education and culture, social services…).
10. In particular, the association maintains a Brussels office.
11. The view point of regions is expressed through the board (members from certain municipalities can also belong to regional councils) and the association regularly organises a meeting of chairmen of regional councils while the executive directors of the latter have their own "sub-association".
12. The Ministry of Finance (in charge of taxes while the Ministry of the Interior is responsible for grants) is not specifically included among the various Ministries in charge of regional development issues.
13. Training programmes for national and regional civil servants stress co-operation and partnership to facilitate appropriation of the complex operation of Finnish regional policy, for instance how to build and monitor a regional programme.
14. Regional council budgets, entirely devoted to regional development, are proportionally much smaller than municipal budgets.
15. Result management is now standard practice in TE centres.
16. Usually the proliferation of committees is an answer to institutional fragmentation (OECD, 2005).
17. In matters of regional and municipal affairs, the Minister of Regional and Municipal Affairs only consults HALKE in cases implying prior discussion and agreement in preparation of major government policy decisions.
18. Riepula, Esko (2004), Kootuin voimin vaikuttavampaan aluehallintoon. Selvityshenkilö Esko Riepulan ehdotukset aluehallinnon vahvistamiseksi. Sisäasiainministeriö. (With joint efforts towards more effective regional administration. Government inspector Esko Riepula's proposals to strengthen regional administration, Ministry of the Interior, 12/2004.)
19. This type of co-operation seems more developed in Finland than in the other Nordic countries (Nordregio, Regional Development in Nordic Countries, 2002).
20. Dexia, "Local Finance in Europe", 2002.
21. Moreover regional physical planning is a responsibility of specific inter-municipal institutions: the Regional Councils.
22. Sub-regions have also been chosen for new approaches in inter-municipal cooperation (see below).
23. Sub-regional contracts and letter of intent type agreements can be used for this purpose: 20 regional centre areas have made such arrangements.
24. This added subsidy, paid since 2002, seems to have increased municipalities' willingness to amalgamate.
25. In the case of the Kainuu experiment, the town of Vaala opted out of the regional project involving all other municipalities, because it wished to continue organising its special health care in conjunction with the area of Oulu (Northern Ostrobothnia).

26. Both in Oulu for North Ostrobothnia and in Rovaniemi for Lapland, the OECD team witnessed strong links between city development strategies across a wide functional area and regional development strategies. In other terms the regional city fully assumes its logical role of a growth engine, seeking to develop synergies within its natural territory of influence.
27. Some definitions of governance limit this concept to institutional settings where private actors and citizens are partners of the decision and implementation affecting the "bonum commune" (A. Héritier, ed., 2002).
28. Data of the Statistics Finland's election result service.
29. The participation rate in EU elections was 60.3 in 1996 but this higher level is due to combined municipal and EU elections.
30. Citizen participation is promoted in different strands of rural development policy (see Chapter 2, Section 2.4).
31. It must be said that in Finland (as in Sweden and others countries) unemployment benefit as a rule is administrated by union-affiliated institutions.
32. At the moment around 20 different projects and operational ensembles have been started.
33. In Noste training there are no course fees, neither for the student nor for the employer.

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APPENDIX A

OECD Regional Typology

The OECD Regional Typology is based on three criteria.

1. The **first criterion** identifies rural communities according to their population density. A community *(NUTS 5)* is defined as rural if its population density is below 150 inhabitants per km^2 (500 inhabitants for Japan to account for the fact that its national population density exceeds 300 inhabitants per km^2).
2. The **second criterion** classifies regions according to the percentage of population living in rural communities. Thus, a region is classified as:
   - **Predominantly rural (PR),** if more than 50% of its population lives in rural communities.
   - **Predominantly urban (PU),** if less than 15% of the population lives in rural communities.
   - **Intermediate (IN),** if the percentage of population living in rural communities is between 15 and 50%.
3. The **third criterion** is based on the size of the urban centres. Accordingly:
   - A region that would be classified as rural on the basis of the general rule is classified as Intermediate if it has a urban centre of more than 200 000 inhabitants (500 000 for Japan) representing no less than 25% of the regional population.
   - A region that would be classified as Intermediate on the basis of the general rule is classified as Predominantly Urban if it has a urban centre of more than 500 000 inhabitants (1 000 000 for Japan) representing no less than 25% of the regional population.

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Selection of Finnish Web sites

National

1. Ministry of the Interior
   www.intermin.fi
2. Finnish Regions and Regional Councils
   www.reg.fi
3. Finnish TE Centres
   www.te-keskus.fi
4. Further information on State provincial offices
   www.laaninhallitus.fi
5. Prime Minister's Office
   www.vnk.fi
6. Parliament of Finland
   www.eduskunta.fi
7. Finnish legislation
   www.finlex.fi
8. Public services in Finland
   www.suomi.fi
9. National board of education in Finland
   www.oph.fi
10. Ministry of Finance
    www.vm.fi
11. Ministry of Foreign Affairs
    www.formin.fi
12. Ministry of Education
    www.minedu.fi
13. Ministry of Trade and Industry
    www.ktm.fi
14. National Technology Agency of Finland
    www.tekes.fi

15. Ministry of Agriculture and Forestry
    www.mmm.fi
16. Ministry of Environment
    www.ymparisto.fi/default.asp?node=17&lan=fi
17. Environmental administration in Finland
    www.ymparisto.fi
18. Ministry of Labour
    www.mol.fi
19. Finnish Association for Local and Regional Authorities
    www.kunnat.net/k_kuntaliitto_etusivu.asp?path=1;184
20. Finnish municipalities
    www.kunnat.net
21. National statistics, Statistics Finland
    www.stat.fi
22. The Finnish national fund for research and development SITRA
    www.sitra.fi
23. Invest in Finlands
    www.investinfinland.fi

Other Web sites

(providing additional detail for examples in boxes)

- Box 2.2: Lapland Regional Programme
  www.lapinliitto.fi
- Box 2.6: Science and Technology Policy Council in Finland
  www.minedu.fi/tiede_ja_teknologianeuvosto/vttn.html
- Box 2.8: Oulu Growth Agreement
  www.oulu.ouka.fi/kasvusopimus
- Box 2.10: Public development company EERO
  www.rovaniemi.fi/?deptid=680
- Box 2.15: Citizen service points
  www.intermin.fi/intermin/hankkeet/yhteisp/home.nsf/pages/indexfin
- Box 2.16: The village action association in Finland
  www.maaseutuplus.net
- Box 3.7: The National entrepreneurship programme
  www.ktm.fi/index.phtml?menu_id=885&lang=1

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The "Finnish way" of economic growth has proven successful over the past decade and has promoted relatively balanced development across the country. In order to maintain its capacity for economic competitiveness and development, Finland is dealing with challenges that may affect future outcomes and highlight regional development issues. Given intense competition in both ICT and more traditional product markets, as well as rapid ageing of the population, how can Finland maintain and enhance the competitiveness of those regions that are the nation's economic drivers? How can the country promote innovation and entrepreneurship in intermediate cities particularly vulnerable to low cost competition and thus permanently upgrade the quality of regional products and services? How can Finland facilitate growth in those regions that have potential for development, but so far have been less successful in exploiting their comparative advantages? Together with a renewed interest in the contribution of regional development to national growth, these questions imply increased attention to multi-level governance issues.

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