OECD Multi-level Governance Studies

Multi-level Governance Reforms

OVERVIEW OF OECD COUNTRY EXPERIENCES

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Edited by Isabelle Chatry et Claudia Hulbert

OECD

BETTER POLICIES FOR BETTER LIVES

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Foreword

This report provides an overview of past, recent and current multi-level governance reforms in OECD countries. Multi-level governance reforms often have diverse objectives which may vary over time depending on economic, social and budgetary contexts. They include three main dimensions: an institutional dimension (re-organisation of powers and responsibilities across levels of government), a territorial dimension (re-organisation of territorial structures) and a public management dimension (re-organisation of subnational governments' administrative and executive processes).

The report focuses on the institutional and territorial dimensions (the third dimension, public management will be only mentioned). It describes the rationale for different reforms, as well as their characteristics and outcomes. It also focuses on the obstacles faced by governments in reform design and implementation, and on solutions identified to overcome them. Past reforms' successes and failures can provide guidance to policy makers for future multi-level governance reforms, although, according to cross-country comparisons, there is no "one-size-fits all" formula.

While analysing reform processes in all OECD countries, this report focuses in particular on Finland, France, Italy, Japan and New Zealand, which have experienced over time several multi-level governance reforms, sometimes with mixed results. The selection criteria included: all are unitary countries representing three continents, Europe, Asia and Oceania; all are characterised by country-specific frameworks based upon demographic, cultural, geographic and economic differences, as well as various territorial settings and different levels of decentralisation, but confront common challenges in terms of territorial and institutional reforms; all have developed both specific and common approaches, tools and institutions to overcome these challenges. These country case studies, which include a detailed analysis of reforms based on a common template, can be found in Annex A.

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Executive summary

Multi-level governance reforms, involving several layers of government, represent a particularly complex type of public governance reforms. They need to take into consideration and co-ordinate a wide range of stakeholders with various, and sometimes opposite, interests and political views. Such reforms are generally conducted by central governments who need to adopt a systemic and integrative governance approach by considering all levels of government and their interactions. They are often controversial and resisted by government officials at all levels, and may also face resistance from citizens and local business communities.

Multi-level governance reforms often have diverse, even contradictory, objectives and drivers which may vary over time depending on economic, social and budgetary contexts. These reforms include institutional, territorial and public management dimensions. These three categories of reforms may be closely related and often go hand in hand. Territorial reforms can be partly driven by decentralisation reforms (and vice versa), as an increasing amount of functions delegated to subnational governments (SNGs) induces pressure for increasing their scale. Public management reforms (such as the promotion of inter-municipal co-operation arrangements) and institutional and/or territorial reforms may also be introduced simultaneously. The former provide the opportunity to review and modernise current management processes which may complement the later. In some cases, however, public management reforms are more an alternative to unsuccessful or incomplete institutional or territorial reforms and are implemented to compensate for potential negative effects or difficulties.

Multi-level governance reforms entail risks that should not be underestimated. Reform processes often stall, fail and may be cancelled, postponed or even reversed. They may not go according to plan, and may be only partly implemented, adjusted, or even circumvented during the implementation phase, without producing instant results or the expected outcomes. Therefore, reshaping the multi-level system of government takes a long time and may need adaptation. To generate expected benefits, additional and complementary reforms are often needed to correct for potential deviations and improve multi-level governance mechanisms. Moreover, this is a never ending process: the challenge of multi-level governance reforms is not merely to adapt to a new, stable and definitive situation but to enable public administration at all levels of government to adapt continually to a permanent evolving environment.

OECD trends in multi-level governance reforms

Until the 2008 financial crisis, good economic performance allowed many OECD countries to launch public administration reforms and devote financial resources to this process. Many governments promoted regionalisation, municipal reorganisation and decentralisation of powers. The crisis and subsequent austerity policies may have halted, or even reversed, ongoing and planned reforms in some OECD countries. However, in the majority of cases the crisis served as an impetus to implement important reforms. The need to consolidate public finance has become both a driver and a major objective of

multi-level governance reforms. This renewed interest in multi-level governance reforms was observed in a great number of OECD countries and such reforms have further accelerated. However, while the crisis may have strengthened incentives for reform, difficult fiscal situations may constrain governments' ability to implement such reforms due to less financial incentives and flexibility.

Chapter 1 focuses on institutional reforms, describing the diverse and complex institutional landscape in the OECD. It defines decentralisation and analyses its rationales, opportunities and risks. It then gives an overview of past and recent decentralisation trends and their main characteristics in federal and (especially) in unitary states. OECD countries present a wide range of models of decentralisation, ranging from very decentralised systems in federations or unitary countries to highly centralised ones, mostly in unitary countries, with a variety of countries in-between that may share some common features. It next looks at fiscal reforms, with an emphasis on reforms introduced after the 2008 financial crisis. Fiscal reforms (tax and grants reforms, equalisation mechanisms, fiscal rules, fiscal co-ordination, external funding) are a key component of decentralisation processes but tend to be difficult to design and implement and often become the "weak link" of multi-level governance reforms. Finally, it considers efforts to reinforce dialogue and co-ordination across levels of government, crucial for the success of multi-level governance reforms.

Chapter 2 deals with territorial reforms. SNGs' territorial structures are constantly evolving both at the municipal and upper levels, due to the creation of new self-governing territorial entities or the re-scaling of existing administrative boundaries. The chapter analyses the main characteristics of territorial reforms, their rationales and their complexity, showing the need to take interactions across and within levels of government into account as well as to consider impacts on satellite and subordinate functional bodies, and emphasising the strong linkages between territorial, institutional and public management reforms. It then focuses on reforms at the municipal level: amalgamations, inter-municipal co-operation and metropolitan governance reforms, either through consolidation or co-operation. Finally, it considers intermediary and regional levels.

The political economy of multi-level governance reforms

Chapter 3 provides some policy insights. It confirms the extent to which public administration reforms are particularly sensitive and difficult to conduct, and the many issues policy makers face when designing, implementing and sustaining them.

A broad range of solutions and tools have been developed by OECD countries to alleviate these issues, successfully or not. Obstacles and strategic policy levers to overcome them may include:

- Understanding and efficiently managing relationships and mutual dependences across levels of governance constitutes the main challenge of multi-level governance reform.
- An "open-system" perspective should be adopted when designing, implementing and assessing multi-level governance reforms and decentralisation processes.
- Reforms should be approached in a multi-dimensional and comprehensive way in order to avoid negative and counterproductive outcomes.
- Bundling territorial, institutional and financial reforms can facilitate reform processes.

- Reformers can benefit from having a clear electoral mandate for reform.
- Reforms often build on previous steps but also pilot programmes, experiments and place-based approaches.
- Opposition from local governments can be overcome through co-operation, consultations, incentives and good relationships with associations of SNGs.
- Mobilising and generating acceptance from central and local civil servants through incentives, compensations and training.
- Gaining support from the civil society through information, public debates and consultations.
- Gaining political adhesion across party boundaries through expert committees.
- The importance of guideline documents, expertise, technical support and prefiguring tools.
- Promoting municipal mergers and inter-municipal co-operation through diverse tools
- Preserving homogeneity after metropolitan reforms.
- The evaluation of reform outcomes should be further promoted.

Introduction

Multi-level governance reforms, involving several layers of government, represent a particularly complex type of public governance reform. They need to take into consideration and co-ordinate a wide range of stakeholders with various, and sometimes opposing interests and political views. Such reforms are generally conducted by central governments who need to adopt a systemic and integrative governance approach by considering all levels of government and their interactions. They are often controversial and resisted by government officials at all levels (including local politicians and civil servants), and may also face resistance from citizens and local business communities.

Multi-level governance reforms often have diverse (even contradictory) objectives and drivers which may vary over time depending on economic, social and budgetary contexts. They include three main dimensions:

- an **institutional dimension:** reforms aim at re-organising powers and responsibilities across levels of government i.e. decentralising or – less often – recentralising tasks, assets, human and fiscal means from the central government to subnational governments (SNGs). They may also redefine the relationships between the different tiers of government, with the objective of setting up efficient vertical and horizontal co-ordination mechanisms. Such reforms include in particular fiscal reforms focused on designing and implementing revamped fiscal frameworks and intergovernmental fiscal relations.

- **a territorial dimension:** reforms that aim at re-organising territorial structures, often by updating and "re-scaling" regional and local government administrative areas, hence modifying the geographic boundaries of regional and local governments. Their goal is to reach a better match between the size of subnational structures and their responsibilities and functions. In most of the cases, they take the form of a consolidation process (enlargement of areas) rather than deconsolidation (splitting of areas). These territorial reforms may concern both SNGs and the central government (the "territorial" state).

- **a public management dimension:** reforms that aim at re-organising SNGs' administrative and executive processes. Inspired in particular by the "new public management" (NPM) and post-NPM currents, they focus on enhancing effectiveness, efficiency, quality, openness and transparency, accountability, citizen participation and co-ordination. They encompass a large diversity of initiatives and programmes in the field of human resources management, financial management, organisational management, optimisation of administrative processes and e-government, quality management, open government and citizen participation à subnational level, etc. Because of strong interactions between subnational and central administrative processes, public management reforms often have an impact on both central and subnational governments (e.g. public staff reform, tax reform).

These three categories of reforms may be closely related and often go hand in hand. Territorial reforms can be partly driven by decentralisation reforms (and vice versa), as an increasing amount of functions delegated to SNGs induces pressure for increasing their scale. Public management reforms (such as the promotion of inter-municipal co-operation arrangements) and institutional and/or territorial reforms may also be introduced simultaneously. The former provide the opportunity to review and modernise current management processes which may complement the later. In some cases however, public management reforms are more an alternative to unsuccessful or incomplete institutional or territorial reforms, and are implemented to compensate for potential negative effects or difficulties.

Multi-level governance reforms entail risks that should not be underestimated. Reform processes often stall, fail and may be cancelled, postponed or even reversed. They may not go according to plan, and may be only partly implemented, adjusted, or even circumvented during the implementation phase, without producing instant results or the expected outcomes. Therefore, reshaping the multi-level system of government takes a long time and may need adaptation. To generate expected benefits, additional and complementary reforms are often needed to correct for potential deviations and improve multi-level governance mechanisms. Moreover, this is a never-ending process: the challenge of multi-level reforms is not merely to adapt to a new, stable and definitive situation but to enable public administration at all levels of government to adapt continually to a permanent evolving environment.

What are the trends in the OECD concerning multi-level governance reforms? Until the global crisis, good economic performance allowed many OECD countries to launch public administration reforms and devote financial resources to this process. Many governments promoted regionalisation, municipal reorganisation and decentralisation of powers. The 2008-2009 global crisis and following austerity policies may have halted or even reversed ongoing and planned reforms in some OECD countries. However, in most of the cases the crisis served as an impetus to implement important reforms. The need to consolidate public finance has become both a driver and a major objective of multi-level governance reforms. This renewed interest in multi-level governance reforms was observed in a great number of OECD countries, and such reforms have further accelerated. However, while the crisis may have strengthened incentives for reform, difficult fiscal situations may constrain governments’ ability to implement such reforms, because of less financial incentives and flexibility.

This paper provides an overview of past, recent and current multi-level governance reforms in OECD countries, focusing on the institutional and territorial dimensions (the third dimension, public management, will be only mentioned). It describes the rationale for different reforms, as well as their characteristics and outcomes. It also focuses on the obstacles faced by governments in reform design and implementation, and on solutions identified to overcome them. Past reforms' successes and failures can provide guidance to policy makers for future multi-level governance reforms (although, according to cross-country comparisons there is no “one-size-fits all” formulae).

While analysing reform processes in all OECD countries, this paper focuses in particular on Finland, France, Italy, Japan and New Zealand, which have experienced over time several multi-level governance reforms, sometimes with mixed results. The selection of these specific countries has been based on several criteria. They all are unitary countries representing three continents, Europe, Asia and Oceania. They are characterised by country-specific frameworks based upon demographic, cultural,

geographic and economic differences, as well as various territorial settings and different levels of decentralisation. However they are confronted by common challenges in terms of territorial and institutional reforms. They have developed both specific and common approaches, tools and institutions to overcome these challenges. These country case studies, which include a detailed analysis of reforms based on a common template, can be found in the Annex.

This paper draws from the valuable inputs of the Regional Development Policy Committee delegates' network, surveyed in 2015 (GOV/RDPC(2015)8/REV1). Country case studies have been prepared through desk work, on the basis of OECD reviews as well as governmental, academic and media reports and articles.

The first part of the paper focuses on institutional reforms. It starts by describing the diverse and complex institutional landscape in the OECD. Based on 9 (quasi) federations and 25 unitary states and almost 138 000 subnational governments, it has dramatically changed over the last 20 years (especially since the crisis) as a result of decentralisation or recentralisation processes. The first section defines what decentralisation is, and analyses its rationales, opportunities and risks. The second section gives an overview of past and recent decentralisation trends and their main characteristics in federal and (especially) in unitary states. OECD countries present a wide range of models of decentralisation. They range from very decentralised systems in federations or unitary countries to highly centralised ones, mostly in unitary countries, with a variety of countries in-between that may share some common features. The third section focusses on fiscal reforms, with an emphasis on reforms introduced after the 2008 financial crisis which accelerated reform processes and shifted their priorities in many OECD countries. Fiscal reforms (tax and grants reforms, equalisation mechanisms, fiscal rules, fiscal co-ordination, external funding) are a key component of decentralisation processes, but tend to be difficult to design and implement and often become the "weak link" of multi-level governance reforms. Finally, the fourth section is dedicated reforms aimed at reinforcing dialogue and co-ordination across levels of government, a crucial component for the success of multi-level governance reforms.

The second part of the report deals with territorial reforms. Subnational governments' territorial structure is constantly evolving both at the municipal and upper levels, due to the creation of new self-governing territorial entities or the re-scaling of existing administrative boundaries. Re-scaling can take two main forms: territorial restructuring either through mergers ("up-scaling") or through the co-operation and pooling of public services ("trans-scaling"). The first section analyses the main characteristics of territorial reforms, their rationales (often, reconciling administrative and real functional areas) and their complexity, showing the need to take interactions across and within levels of government into account as well as to consider impacts on satellite and subordinate functional bodies. An emphasis is placed on the strong linkages between territorial, institutional and public management reforms. The second section focuses on reforms at the municipal level (amalgamations, inter-municipal co-operation and metropolitan governance reforms, either through consolidation or co-operation), while the third section focusses on the intermediary and regional levels. Both sections analyse the reforms' rationales objectives, obstacles/solutions and policy incentives, with an emphasis on the five countries afore-mentioned.

The third part concludes on the political economy of multi-level governance reforms, providing some insights for policy. It confirms the extent to which these public administration reforms are particularly sensitive and difficult to conduct, and policy

makers face many issues when designing, implementing and sustaining them. A broad range of solutions and tools have been developed by OECD countries to alleviate these issues, successfully or not. A non-exhaustive list of obstacles and strategic policy levers to overcome them include:

- Understanding and managing efficiently relationships and mutual dependences across levels of governance constitutes the main challenge of multi-level governance reform.
- An “open-system” perspective should be adopted when designing, implementing and assessing multi-level governance reforms and decentralisation processes
- Reforms should be approached in a multi-dimensional and comprehensive way in order to avoid negative and counterproductive outcomes
- Bundling territorial, institutional and financial reforms can facilitate reform processes
- Reformers can benefit from having a clear electoral mandate for reform
- Reforms often build on previous steps but also pilot programmes, experiments and place-based approaches
- Opposition from local governments can be overcome through co-operation, consultations, incentives and good relationships with associations of SNGs
- Mobilising and generating acceptance from central and local civil servants through incentives, compensations and training
- Gaining support from the civil society through information, public debates and consultations.
- Gaining political adhesion across party boundaries through experts committees
- The importance of guideline documents, expertise, technical support and prefiguring tools
- Promoting municipal mergers and inter-municipal co-operation through diverse tools
- Preserving homogeneity after metropolitan reforms
- The evaluation of reform outcomes should be further promoted.

Chapter 1

Overview of institutional reforms

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Reviewing and restructuring multi-level governance systems to produce more functional and effective governments are put forward in many OECD countries as an integral part of public sector reform. In fact the difficulties encountered in implementing successful changes in particular for the provision of essential goods and services (like regulation reforms, post-shock policies) reveal the importance of institutional settings and functioning and the need to adapt them to increase effectiveness of public policy.

The OECD institutional landscape is diverse and complex: OECD countries include eight federal countries, one quasi-federal country (Spain) and 25 unitary states, including "hybrid systems" between federations and unitary states such as United Kingdom, Portugal or Italy. Countries' institutional structures are crucial when considering multi-level governance reforms, especially in the case of reforms affecting SNGs' organisation (Box 1). In federal countries, sovereignty is shared between the federal government and federated states1, and federated states govern local governments under their jurisdiction. Local government reforms are hence decided at the state level. In unitary countries, sovereignty is not shared and local governments' organisation and reforms are decided by the central government. In quasi-federation and "hybrid systems", autonomous regions, which have legislative powers, have some room for manoeuvre for defining and reforming local government functioning, but less than in federations.

Box 1. **The importance of institutional arrangements in the OECD to analyse multi-level governance reforms**

In federal countries, sovereignty is shared between the federal government and self-governing regional entities (the federated states) which have their own constitution (except Canada), parliament and government, and large responsibilities (while federal governments have in general exclusive and listed responsibilities such as foreign policy, defense, money, criminal justice system, etc.). In most federal countries, in particular older ones, local governments are "creations" of the federated states and fall directly under their jurisdiction. Their status, organisation, responsibilities and financing are defined by state constitutions and laws, and often differ from one state to another. As a result, local government reforms are decided by the federated states and not the federal power, which has no say on those matters (United States, Canada, and Australia). In Australia for example, municipalities are not even explicitly recognised by the Commonwealth Constitution, despite several failed or abandoned referendums attempts proposing constitutional recognition in 1974, 1988 and 2013. In some federations however, the guaranteed principle of local self-government is set out in the federal constitution (e.g. Germany, Austria, Belgium, Switzerland and Mexico). In addition, despite the fact that, in theory, local governments are subordinated to the federated states where they are located and are not supposed to have direct and independent relations with the federal government (or only little), the reality is different. There is a growing tendency in several countries, including Australia and the United States, for local governments (particularly cities) to become part of intergovernmental relations. This is especially the case when there are direct financial relations and policy interactions between local governments and the federal government, through the delivery and funding of federal public programmes. Therefore local governments, represented by their national associations, are more and more recognised as having a role in inter-governmental co-ordination mechanisms in federal countries. In Australia for example, the President of the Australian Local Government Association (ALGA) is a member of the COAG, the main intergovernmental forum established in May 1992 jointly by the Commonwealth and State and Territory governments. Other members of COAG include the Prime Minister and State and Territory Premiers and Chief Ministers.

Box 1. **The importance of institutional arrangements in the OECD to analyse multi-level governance reforms** *(cont.)*

In quasi-federations or "hybrid systems", autonomous regions have less room for manoeuvre than in federations for defining and reforming local government functioning. Basic elements of local government functions and financing are often captured in national constitutions. Even if a great autonomy is given to autonomous regions in relation to lower tiers through primary and/or secondary legislative powers, it is often a competence which is shared with the central power. Spain for example is constitutionally a unitary state but in reality a quasi-federation with regions having a large autonomy. Organising the municipalities and provinces and changing municipal boundaries within the regional territory are exclusive responsibilities of the autonomous communities, but their functions and finances are decided in the framework of the national law (article 148 of the Constitution).

In the United Kingdom, since the devolution in 1998-1999 of certain powers and responsibilities to regional elected bodies, local governments' organisation and functions are defined and reformed by the UK government (and Parliament) for England, and by devolved nations for Wales, Scotland and Northern Ireland. In Portugal, there is also an asymmetric organisation with two autonomous regions having legislative responsibilities in overseas territory, while there is no self-governing region in mainland. The autonomous regions of Madeira and Azores are responsible for the financing and general supervision of local authorities within their territory, and also have the legislative power to create, dissolve and alter local government boundaries in accordance with the national laws. In Italy, defined as a "regionalised country", the five special status regions of Aosta Valley, Friuli-Venezia Giulia, Sardinia, Sicily and Trentino-Alto Adige/Südtirol are responsible for organising provinces and municipalities on their territory.

In theory, **the unitary states are "one and indivisible" entities**, and sovereignty is not shared. This means that citizens are subject to the same unique power on the national territory. This does not preclude the existence of local authorities, also elected directly by the population and with some political and administrative autonomy. Unitary states are thus more or less decentralised, depending on the extent of their powers, responsibilities and resources, and the degree of autonomy they have over these different elements. Some unitary countries even recognise autonomous regions and cities, which have more powers than other local governments. Unitary states can also be "deconcentrated", by having State representatives at the territorial level. This is the case in France (regional and departmental prefects), Poland (regional prefects), or Sweden with the County Governors at the head of the County Administrative Boards. In unitary countries, reforms of local governments are designed and implemented by the central power. In that process, local governments are more or less associated and consulted, in particular through their representative associations. This depends on the degree of decentralisation and the strengths of local governments, on the existence of structured and effective multi-level governance mechanisms, and on the quality of the dialogue between the central and subnational governments (in general but also at a given time, depending on the interplay of political forces). The quality of dialogue has also a cultural dimension, some countries being more open and favourable to ex-ante discussions and negotiations across levels of governments than others, where reforms are imposed in a more centralist/top down manner.

Source: Authors' own elaboration.

There are around 138 000 general-purpose subnational governments in OECD countries, which are distributed in one, two or three government layers (Table 1). In total, there were around 132 888 municipalities, 4 108 intermediate governments and 520 regions or state governments in the OECD in 2015-16.

Table 1. **Institutional organisation in the OECD and number of subnational government layers**

	8 countries with only one subnational level *Municipalities*	18 countries with two subnational levels *Federated states/regions* *Municipalities*	8 countries with three subnational levels *Federated states/regions* *Intermediary governments* *Municipalities*
9 federations and quasi-federations		Australia[1] Austria Canada Mexico Switzerland	Germany Belgium Spain[2] United States
25 unitary countries	Estonia Finland[3] Ireland Island Israel Luxembourg Portugal[3] Slovenia	Chili Korea Denmark Greece Hungary Japan Norway New Zealand Netherlands Czech Republic Slovak Republic Sweden Turkey	France Italy Poland United Kingdom[4]

Note: 1. Australia has three levels of government (Federal, state and territory, local) but that local governments are not recognised in the Constitution. 2. Spain is a quasi-federal country. 3. Finland and Portugal have autonomous regions on part of the country. 4. There is an intermediary level only on part of England.

Source: Authors' own elaboration.

1. What is decentralisation and why decentralise?

1.1. Political, administrative and fiscal decentralisation

Decentralisation is a key component of public sector reform, as it consists in transferring a range of powers, responsibilities and resources from central government to elected SNGs. The term “decentralisation” generally regroups three interconnected, political, administrative and fiscal aspects:

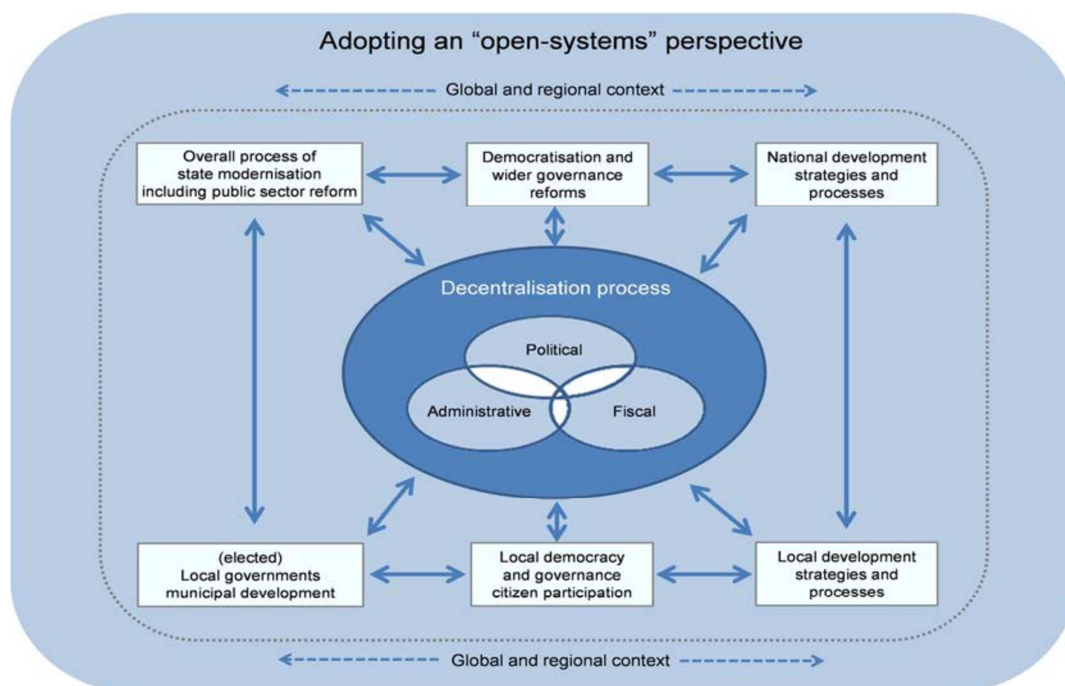
Political decentralisation involves a new distribution of powers according to the subsidiarity principle, with the objective of strengthening democratic legitimacy.

Administrative decentralisation involves a reorganisation and clear assignment of tasks and functions between territorial levels in order to improve the effectiveness, efficiency and transparency of national territorial administration.

Fiscal decentralisation involves delegating taxing and spending responsibilities to subnational tiers of government. In this case, the degree of decentralisation depends on both the amount of resources delegated and the autonomy in managing such resources. For instance, autonomy is greater if local governments can decide on tax bases, tax rates and the allocation of spending.

An “open-system” perspective should be adopted when designing, implementing and assessing multi-level governance reforms and decentralisation processes (Figure 1). Linkages between the three afore-mentioned dimensions (political, administrative and fiscal) should be considered to ensure effective decentralisation. These dimensions tend to be complementary and interdependent, and decentralisation reforms' outcomes depend on how the different elements of the reform are connected and interact. Finding the right balance between these three dimensions, and finding the right sequencing (i.e. deciding when to deal with each one over a long-term decentralisation process) may represent the two major challenges of a decentralisation reform.

Figure 1. **Decentralisation reforms: Adopting an open-systems perspective**



Source: European Commission, EuropeAid (2007), "Supporting decentralisation, and local governance in third countries", Tools and Methods Series.

Decentralisation also leads to a greater administrative (explicit or implicit sharing of policy-making authority), financial (co-financing, fiscal relations between levels of government) or socio-economic (issues and/or outcomes of public policy at one level have impact on other regions and the national level) inter-dependency between the central and subnational governments. In this context, multi-level governance reforms aim at reshaping and improving these interactions between public authorities[2] i.e. between central and SNGs and also within SNGs.

1.2. Rationale behind decentralisation and risks

Decentralisation is **first and foremost a political issue**. It often has both fervent supporters and detractors. An in-depth analysis of its rationale and effects is needed, and a pragmatic approach should be considered. Decentralisation is not a panacea for any type of problem or country and it can also face implementation challenges due to its complex and systemic nature.

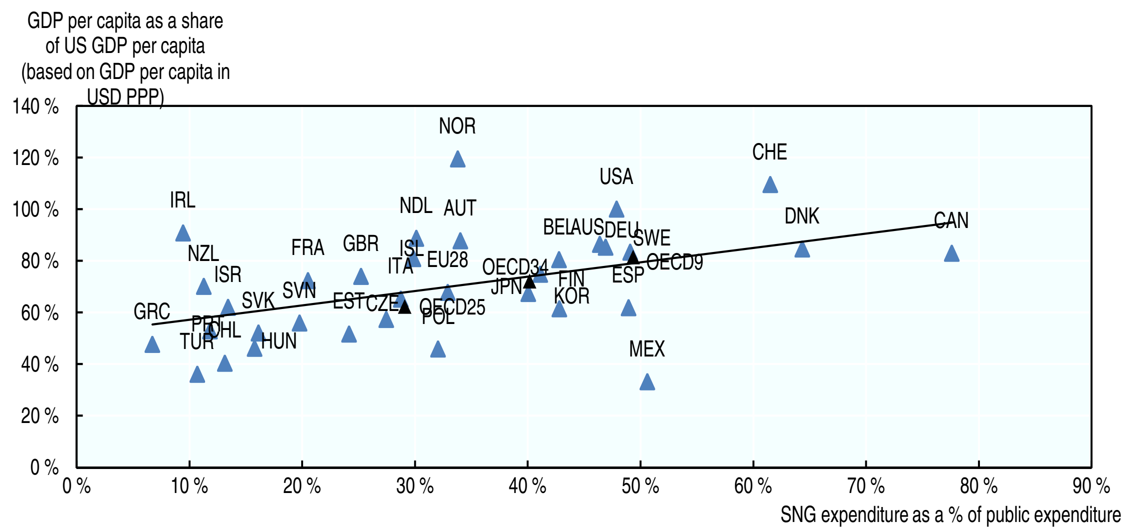
Decentralisation may **offer opportunities but it also entails risks** in terms of efficiency (public policies and services delivery), representation (political governance) and national unity (Table 2). It may produce perverse effects, and fail to keep its promises of better expected efficiency and political gains. In fact, opportunities and risks tend to be two sides of the same coin as they mirror each other.

On the positive side, decentralisation reforms address generally different incentives, which vary over time and space. Broadly speaking, the **three most common arguments** motivating decentralisation reforms are to enhance **stability, democracy, and economic development**. Reforms are shaped by the political, social and economic situations of

different countries at a given time. Understanding these initial conditions is an essential starting point for assessing the rationale for reform, its likely shape and pace, and the durability of resulting policies.

Decentralisation is often presented as a way of increasing efficiency in public service provision, reaching a better use of public resources and spending effectiveness, increasing equity in access and service, tailoring policies to local contexts and population needs, improving local democracy and citizen participation, and reaching greater accountability and transparency. There seems to be a positive correlation between gaps in GDP per capita and the level of subnational spending decentralisation (Figure 2).

Figure 2. **Devolution of spending responsibilities is a feature of development (in terms GDP pc income gaps)**



Note: Luxembourg is not shown on the graph.

Source: Calculations using OECD (2016d) Subnational Governments in OECD countries: Key data. Subnational government structure and finance: http://dx.doi.org/10.1787/05fb4b56-en, based on OECD national accounts.

Table 2. **Decentralisation: Opportunities and risks**

Opportunities	Risks
Public policies and services delivery	
More capacities for place-based policies and better service delivery: – Better match between local needs and preference. – More flexibility and reactivity. – Stimulation of competition which in turn favours innovation, search for performance. – Room for experimentation. – Lower costs. – Mobilisation of the comparative advantages of local enterprises and the local non-profit sector. – Mobilisation of local resources (in the case of tax decentralisation and local user charges and fees).	**Deterioration of service delivery and increasing costs:** – Diseconomies of scale (especially if local governments are small), which may also affect service quality. – Inefficient scale of production for some services with high fixed costs (such as network services) which need a scale of production large enough to be economically efficient. – Duplication and overlapping of responsibilities and services generating administrative overheads. – Lack of human and technical capacities and of financial resources of SNGs (own and transferred) to take on mandates, resulting in bad service delivery. – External effects: citizens and businesses may shop around to neighbouring jurisdictions to get better services at no costs to them. – Inequity in accessing services and local differences in levels of services (scope and quality), requiring equalisation mechanisms. – Increased competition between SNGs, in particular tax competition, having negative effects (potential race to the bottom).
Representation: political governance	
Democratic governance: – Integrating the needs and interests of citizens, civil society organisations and local enterprises. – Opportunities for more participation, involvement and debate with the people and local actors as well as negotiation capacity and conflict settlement. – Granting a certain autonomy and political integration to minorities. – Accountability and transparency.	**Local politics and “bad local governance”:** – Elite and local interest groups capturing the process. – Insufficient transparency and accountability mechanisms. – Insufficient participation and involvement of citizens and local actors' (through elections or other schemes). – Corruption. - More complex governance structure imposing more co-ordination (vertically and horizontally and across policies) and higher transactions costs.
National unity	
National cohesion: – Can reach a more equal distribution of national resources. – Dispersion of political power in a vertical way. – Common decision or planning, or common execution of tasks. – National diversity despite national unity.	**Local tensions - moves for separation:** – Increased disparities between jurisdictions and less solidarity between regions and communities. – Lack of support and effective cross-level co-ordination mechanisms, in particular with the central government. – Contradictory effects of subnational and national policies. – Risk of joint decision traps (Scharpf, 1998) due to the increased number of veto players that renders co-ordination and reaching decisions acceptable to all the actors involved difficult. **More difficulty in meeting national macroeconomic goals and coherence:** - Incoherence between national and subnational policies; - Public finance governance and fiscal discipline (public investment, control of public debt, etc.) - Complexity of equalisation systems.

Source: OECD (2014b) Territorial Review of Netherlands – Adapted from Steinich, M. (2000), “Monitoring and Evaluating Support to Decentralisation: Challenges and Dilemmas”, ECDPM Discussion Paper, No. 19, Maastricht; European Commission, EuropeAid (2007), “Supporting decentralisation, and local governance in third countries”, Tools and Methods Series, Charbit and Michalun, 2009.

A key argument for decentralisation is the idea that local governments have better information regarding local spending needs and preferences, and hence may better satisfy certain needs of the population, at a lower cost, than the central administration. Local governments also tend to be “closer to citizens”, who can more easily participate in public meetings, hearings, elections, and establish direct contacts with officials (Faguet, 2004, 2011). Because of this closeness, governments may be more "transparent" and likely to be held accountable for their successes and failures.

Some more precise objectives can be pursued depending on the national context, for example:

- Promoting social and political stability in conflict environments. Decentralisation can reduce conflict by opening up new avenues for political participation and by giving people more opportunities to influence government (USAID 2009).
- Fighting against poverty and huge territorial disparities. This is a major goal of decentralisation reforms in Chile or Mexico for example.
- Preserving historical, linguistic, and cultural specificities. This has been a major consideration in the federalisation process in Belgium, and a major objective of the devolution process in the United Kingdom. It also explains some forms of asymmetric decentralisation in Italy, Spain, France, Portugal or Finland.
- Reducing the central budget by decentralising spending responsibilities, in the context of public finance crises and against the backdrop of tight budget constraints. This has been one of key goals of past decentralisation reforms in Japan, Korea and Finland and more recently (since the global crisis and consolidation measures) in the Netherlands or United Kingdom for example.

Such **developments may have been imposed by external pressures**, in particular from international organisations. In Korea for example, the 1997 financial crisis and resulting IMF bailout programme put pressure on the Korean government to conduct a public sector reform. This reform was introduced in 1999 and included a comprehensive decentralisation programme. This was also the case in several European countries heavily affected by the 2008 financial and economic crisis, rescued by the IMF and the European Commission. Several Memoranda of Understanding signed between the “Troïka” (IMF, European Central bank and the Commission) and these countries involved institutional reforms, including territorial and decentralisation reforms. In particular, local government reforms were adopted in 2011 by both Greece and Portugal, aiming at streamlining territorial organisation and optimising public spending through reinforced decentralisation.

Arguments against decentralisation often include the following: financially, SNGs may not show fiscal prudence or sufficient ability to manage their financial affairs; politically, corruption might be reinforced; administratively, SNGs may lack the capacity to properly meet their responsibilities. These risks often arise from difficulties associated with managing interrelated, mutually dependent levels of government, and can be addressed via sound multi-level governance mechanisms (Charbit and Michalun, 2009).

There is no clear-cut rationale on whether or not decentralisation should be pursued. Opportunities and risks can differ from one country to another. Similar decentralisation reforms may – and sometimes can have very different impacts in different countries. The outcomes of decentralisation reform depend to a large extent on national historical, cultural and political contexts, as well as on the ways in which the

reform is designed, planned, implemented, evaluated and adjusted. Decentralisation is a learning process and is not set in stone; permanent adjustments are necessary to correct for potential deviations.

OECD experiences show that there is **no universal consensus on the optimal structure of multi-level governance and decentralisation.** Decentralisation outcomes typically depend on how the complex relationships between levels of government are managed. Therefore, the key is **to understand and manage the relationships and the mutual dependence across levels of governance efficiently,** by identifying and properly addressing **the different multi-level governance challenges and gaps** (Box 2).

Box 2. **The OECD approach to multi-level governance challenges**

In a decentralised context, a complete separation of policy responsibilities and outcomes across levels of government is impossible to reach. The relationships among levels of government are characterised by mutual dependence. These relationships are simultaneously vertical (across different levels of government), horizontal (among the same level of government), and networked. Governments must therefore bridge a series of vertical and horizontal "gaps".

These gaps include, in particular, the fiscal capacity of governments to meet obligations and information asymmetries between levels of government. Other major challenges include gaps in administrative responsibility (when administrative borders don't correspond to functional economic and social areas), gaps in policy design (when line ministries take purely vertical approaches to cross-sectoral regulation that can require co-design of implementation at the local level) and finally a lack of human, or infrastructure resources to deliver services and to design strategies. Countries may experience these gaps to a greater or lesser degree but given the mutual dependence that arises from decentralisation, and the network-like dynamics of multi-level governance, countries are likely to face them simultaneously.

OECD member and non-member countries are increasingly developing and using a wide variety of mechanisms to help bridge these gaps and improve the coherence of multi-level policy making. These mechanisms may be either "binding" (such as legal mechanisms) or "soft" (such as platforms for discussion), and must be sufficiently flexible to allow for territorially-specific policies. Involvement of SNGs in policy-making takes time but medium- to long-term benefits should outweigh the costs of co-ordination.

Source: Charbit, C. and M. Michalun (2009), "Mind the gaps: Managing mutual dependence in relations among levels of government", OECD Working Papers on Public Governance, No. 14, OECD Publishing, Paris, http://dx.doi.org/10.1787/221253707200.

Table 3. **Mutual dependence across levels of government: Multi-level governance challenges/gaps in OECD member countries**

Types of challenges/gaps	Co-ordination challenges/gaps
Funding	Unstable or insufficient revenues undermining effective implementation of responsibilities at the subnational level or for shared responsibilities **=> Need for shared financing mechanisms**.
Administrative	Occurs when the administrative scale for investment does not correspond with functional relevance, as in the case of municipal fragmentation **=> Need for instruments for reaching "effective size" (co-ordination tools among subnational units; mergers).**
Policy	Results when line ministries take purely vertical approaches to cross-sectoral policies to be territorially implemented **=> Need for mechanisms to create multi-dimensional/systemic approaches and to exercise political leadership and commitment.**
Information	Asymmetries of information (quantity, quality, type) between different stakeholders, either voluntary or not **=> Need for instruments for revealing and sharing information.**

Table 3. **Mutual dependence across levels of government: multi-level governance challenges/gaps in OECD member countries** *(continued)*

Capacity	Arises when there is a lack of human, knowledge or infrastructural resources available to carry out tasks and to design relevant strategies for local development **=> Need for instruments to build local capacity**.
Objective	Exists when different rationales among national and subnational policy makers create obstacles for adopting convergent targets. Can lead to policy coherence problems and contradictory objectives across investment strategies **=> Need for instruments to align objectives**.
Accountability	Reflects difficulties in ensuring the transparency of practices across different constituencies and levels of government. Also concerns possible integrity challenges for policy makers involved in the management of investment **=> Need for institutional quality instruments => Need for instruments to strengthen the integrity framework at the local level (focus on public procurement) => Need for instruments to enhance citizens' involvement.**

Source: Charbit, C. (2011), "Governance of public policies in decentralised contexts: The multi-level approach", OECD Regional Development Working Papers, No. 2011/04, OECD Publishing, Paris, http://dx.doi.org/10.1787/5kg883pkxkhc-en.

Overcoming resistance to decentralisation, resulting from vested interests, can be difficult. L**ocal governments** often support, and even often demand, such reforms. However, they tend to fight unbalanced decentralisation processes, consisting of decentralising expenditures without devolving corresponding financial and human resources. This was the case in some countries during the recent financial crisis, when some social tasks were decentralised without real fiscal compensation, hence forcing local governments to play a "social buffer" role ("decentralisation of the crisis"). It may also be the case when combining (a) decentralisation reform with territorial reform (mergers, creation of a new level of government), although the decentralisation process may also facilitate the acceptance of the territorial reform. Fiscal reforms may also be opposed by local governments, as they may reduce their autonomy (see below). Finally, local governments are not always willing to take on new responsibilities, especially when they lack necessary capacities. However, in most cases the fiercest opponent to decentralisation efforts is **the central government** itself (organisations, civil servants), which may slow down or modify the reform process (Box 3). Decentralisation implies sharing power with SNGs, and tends to reduce civil servants' control over local governments. It may also directly affect their jobs, especially when the central government has a strong territorial level administration. Decentralisation efforts may also involve a transfer of personnel from the centre to subnational entities, which may result in a loss in terms of status and benefits (pensions, wages, non-pecuniary prerogatives). In addition, central government officials may also argue, sometimes rightly so, that SNGs lack the capacity to perform difficult tasks efficiently and that decentralisation could increase corruption.

Box 3. **Resistance to decentralisation reforms at central government level: The case of France and Japan**

Japan: significant friction between the Decentralisation Promotion Committee and the central government regarding the contents of the reforms was a major challenge. During the first Decentralisation Promotion Reform, various interest groups tried to shape the outcome of the recommendations whilst pressure came from central authorities. The reform was implemented simultaneously with a separate reform of the central government which reduced the number of ministries from 22 to 12; in this context, the Decentralisation Promotion Reform was perceived by some as another diminution of central power. The second Decentralisation Promotion Reform also encountered some resistance from central government bodies. In particular, the abolition of certain ministries' regional branch offices and the removal of restrictions on specific grants, perceived as important resources to

Box 3. Resistance to decentralisation reforms at central government level: The case of France and Japan *(continued)*

effect policy implementation at the local level, was opposed by central ministries. The bill reorganising the local branches of the central ministries was finally abandoned in 2012.

France: despite decentralisation laws, the French government is still very active on the local scene, playing a leading role in many areas. The central government has maintained, at both regional and departmental levels, a strong and powerful prefectural administration led by a *préfet*, as well as local directorates of various ministries placed under his authority, so-called "deconcentrated services". As in other OECD countries, (Poland, Sweden, Italy, Finland, Turkey, Hungary, Greece, Estonia, etc.) having such State representatives at the territorial level, means that these representatives continue to play a key role – in varying degrees depending on countries – in implementing national policies at local level. They ensure that these policies are in line with SNG policies and sometimes supervise local government actions. Having a thorough knowledge of local realities, the state territorial administration plays a co-ordination role between the different stakeholders. It acts as a "pivot" of the administrative system, facilitates multi-level government dialogue on the ground, and sometimes acts as an advisor and "mediator" able to reconcile different perspectives. In France, according to the Constitution, the prefect represents the government at a local level and is responsible for national interests, administrative supervision and compliance with laws. The prefect also remains in charge of public order. He is the direct representative of the Prime Minister and every minister at the departmental level, implementing government policies' and their planning. Prefectural administration is also responsible for supervising local government activities ("a posteriori" legality control). The 1982 decentralisation reform and successive reforms have substantially transformed the role of the prefect and deconcentrated administrations. However, they still have significant power and authority. Competence is often shared between levels of government, but the roles of the central government and subnational governments tend to overlap, hence affecting accountability. The central government has often retained an arguably unnecessary degree of prerogatives (ECO 2007c, OECD 2012c). This situation has also generated duplications of services and staff between the central and subnational levels, and therefore substantial additional costs. In particular, the 2010 reform of the state (REATE) aimed at streamlining the territorial administration and at improving the old and complex relationships between deconcentration and decentralisation, by building newly drawn and relevant areas and intervention methods for the state at local level (Kada, 2012). The 2015 reform related to the delimitation of the regions was an opportunity to thoroughly modernise the functioning of government services in regions and redefine their role and missions. To this end, "foreshadowed prefects" were appointed to develop organisational proposals.

Source: authors' own elaboration.

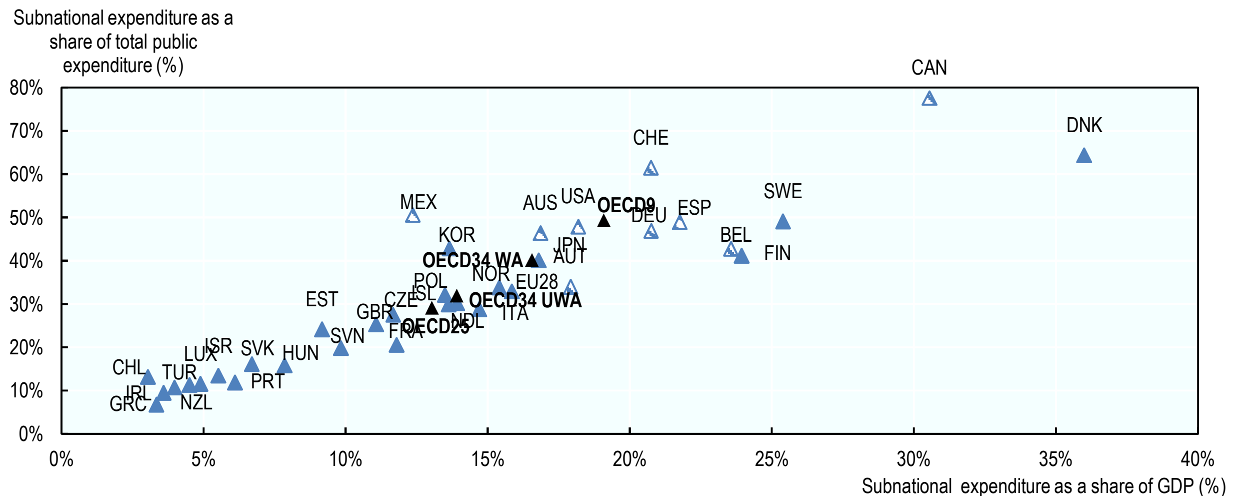
2. Past and recent trends regarding decentralisation/recentralisation reforms

OECD countries include **a wide range of decentralisation models**, ranging from federal (Canada, Switzerland, Germany and United States) or unitary (Denmark, Sweden and Finland) highly decentralised systems to highly centralised unitary systems as in Greece, Ireland, Portugal or Turkey. Between these two polarities, a variety of intermediary models can also be found.

The level of decentralisation is partly[3] reflected by the level of subnational expenditure (Figure 3). It is generally high when SNGs are in charge of many and large spending responsibilities in sectors such as education, social services and health. While SNG expenditure represented 40 % of public expenditure and 17% of GDP on average in the OECD in 2014, these numbers reached 49% and 19% respectively in federal countries (where subnational expenditures combine those of the federated state and local governments). By contrast, local government expenditure represented on average 29% of public expenditure and 13% of GDP in unitary countries. However there are wide differences between unitary countries where local governments have limited

responsibilities? (Greece, Turkey, Ireland, New Zealand or Chile) and more decentralised unitary countries where local governments' involvement in the economy is significant (Japan, Denmark, Sweden and Finland). Denmark, in particular, stands out from other countries in terms of SNG expenditure because SNGs administer a number of social security transfers.

Figure 3. **Subnational government expenditure as a percentage of GDP and total public expenditure (2014)**

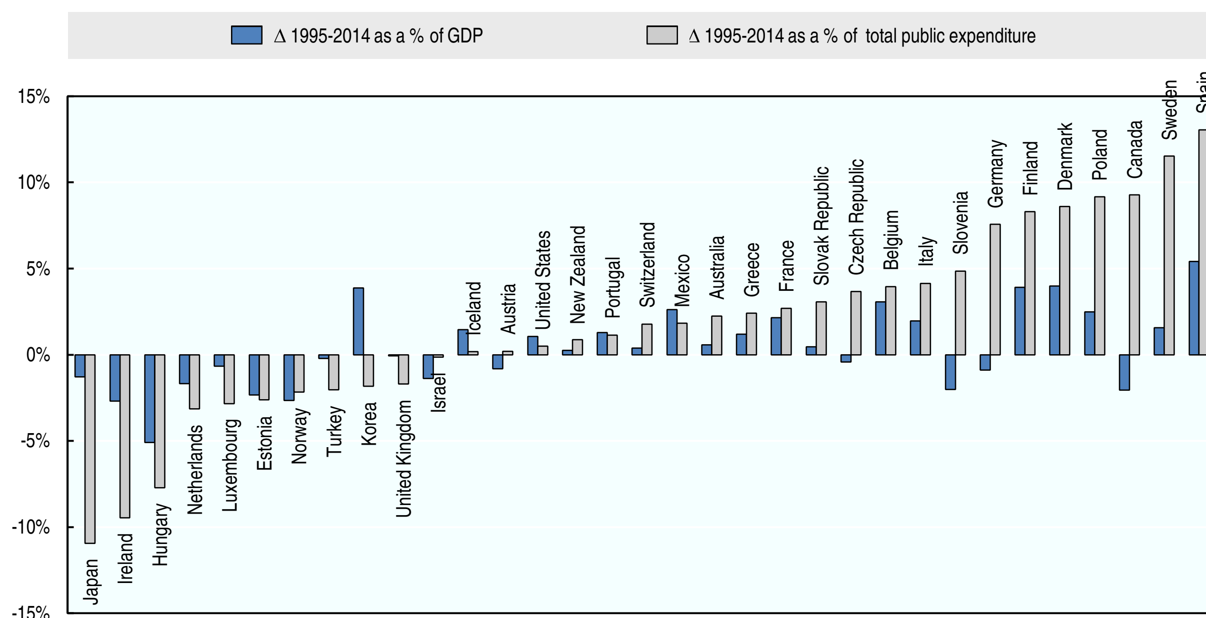


Notes: 2013: Chile, Mexico and New Zealand; 2012: Australia; 2011: Turkey. Information on data for Israel: http://dx.doi.org/10.1787/888932315602.

Source: OECD (2016d) Subnational Governments in OECD countries: Key data. Subnational government structure and finance: http://dx.doi.org/10.1787/05fb4b56-en, based on OECD national accounts.

The situation in 2014 is in some measure[4] the result of decentralisation processes which took place over the last few decades in many OECD countries. These reforms **transferred spending responsibilities from the central government to SNGs** and therefore resulted in an increase of the share of SNG expenditure in total expenditure and GDP (Figure 4).

Figure 4. **Changes in subnational expenditure between 1995 and 2014, as a share of total public expenditure and of GDP (percentage points)**



Notes: 1995-2012 Australia; 2003-2013 Mexico; 1995-2013 New Zealand; 1998-2014 Iceland; 1996-2014 Netherlands; 2005-2014 Ireland. No data for Chile and Turkey due to lack of time-series. Information on data for Israel: http://dx.doi.org/10.1787/888932315602.

Source: OECD (2016), OECD Regions at a Glance 2016, OECD Publishing, Paris, http://dx.doi.org/10.1787/reg_glance-2016-en.

This decentralisation trend has intensified continuously over the last few decades. Most OECD countries embarked on decentralisation or federalisation policies, which were sometimes very ambitious and required constitutional revisions. The recent crisis, and austerity policies that followed, created significant reform opportunities.

In federal countries, institutional reforms include improving the distribution of responsibilities between federal and federated states; improving intergovernmental fiscal relations (grants and tax sharing systems); strengthening internal stability pacts; changing the equalisation mechanisms (horizontal and vertical) and the co-ordination mechanisms between federal and state governments (Box 4). Reforms also include improving relations between state governments themselves to avoid fragmentation and to promote co-operation at state level (in Switzerland for example).

In OECD unitary countries, a wide variety of decentralisation/recentralisation processes have been engaged, in particular over recent years (Portugal, Greece with the Kallikratis programme, Chile with the regional reform and the modernisation of the municipal system currently under discussion in the parliament). These reforms aim to strengthen decentralisation and/or improve multi-level governance systems (Netherlands, Sweden, Finland, Denmark, Norway, France, Italy, England, Japan, etc.), reform local public management (New Zealand, Ireland), but also sometimes recentralise some functions (Hungary).

Box 4. **Institutional reforms in federal countries**

In Belgium, the federalisation process, which began in 1970, went through several successive stages (1980, 1988-1989, 1993 and the 2001 Lambermont Agreements). They have progressively transformed the Kingdom into a Federal country, and finally led to a new in-depth institutional reform: the institutional agreement on the Sixth State reform, entitled 'A more efficient federal State and more autonomous entities'. Adopted in December 2011, it provides for a substantial state reform that will take place over several stages. It devolves additional responsibilities to Belgian regions and communities (as of mid-2014) in four main areas: employment; healthcare; social assistance for the elderly and disabled; family support and justice. These additional expenditures are large, estimated at 4.5 % of the 2011 GDP. This reform also has a major fiscal component as it reinforces greatly the financial autonomy of federated entities (starting in 2014, with a transition mechanism for a period of ten years).

Germany also conducted two important reforms of its federal system in 2006 (*Föderalismusreform* I). The reform limited the Bunderat's right of veto but, in compensation, it transferred several new responsibilities from the federal government to the Länder (staff management, economic activities and trade, justice) and clarified the distribution of responsibilities across levels of government (sole and comprehensive responsibilities for universities and environment). In 2009, a second step was accomplished with the *Föderalismusreform* II, which modified financial arrangements.

In Switzerland, the federal reform adopted in 2004 and in force since 2008 reassigned several policy areas to either the federal or cantonal level and modified the equalisation system. It also introduced new rules for the further development of inter-cantonal collaboration to avoid fragmentation and "competitive federalism", especially in the area of cantonal tax and fiscal policy competition but also in some policy fields. For example, the Confederation may declare inter-cantonal agreements to be generally binding or require cantons to participate in such agreements in nine specific fields, including school education, cantonal institutions of higher education, cultural institutions, waste management, waste water treatment, urban transport, etc.

In Austria, the 2003 Austrian Constitutional Convention was supposed to carry out a wide reform of the federation, including reducing vertical fiscal imbalances, redistributing subnational responsibilities and simplifying the federal system. However, the Convention closed in 2005 without any significant agreement being reached. Since then, no new attempt of reforming the constitution was made. Instead, Austria launched a wide administrative reform in 2013 concerning all levels of government, which is intended to identify margins of efficiency and appropriate measures to reach savings on spending for administration and public subsidies. An important role has been given to a dedicated Commission on Tasks and Deregulation (*Aufgaben- und Deregulierungskommission*) which groups all layers of government. Co-ordination of monitoring of the effective implementation of the administrative reform will be carried out by an independent unit which will submit its reports to the parliament and the government.

Source: Author's own elaboration.

2.1. Central and Eastern European countries are still adjusting their institutions at the subnational level

Significant decentralisation developments took place in Central and Eastern European countries (CEECs) at the end of the 1990s, when local autonomy was re-established after several decades of a centralised socialist system. Targets set by the EU regarding the modernisation of public sector management had a strong impact in this process, as most of these countries were interested in joining the EU (despite the fact that the public administration system was not an explicit part of the *Acquis Communautaire)*. Therefore, decentralisation reforms have been strongly influenced by EU standards. Even if the EU did not promote a particular model of decentralised governance, the prospect of entering the EU led to some convergence in the decentralisation reform processes, based on

common principles: re-instating democratic institutions at the municipal level; setting up self-governing or administrative regional entities for acceding to EU funds; putting in place effective and efficient local governance and financing systems; complying with EU requirements for public services; building EU statistical standards for administrative units (NUTS), etc.

Some CEECs implemented decentralisation reforms **very quickly**. Sometimes, **they replicated** practices of old EU member states or international standards, without being sufficiently prepared for the implementation of such profound reforms. They also **faced resistance** from existing local and central administrations and other opponents to decentralisation. In this respect, among CEECs, Poland is considered to be a successful example of decentralisation, especially regarding reform implementation. Preparatory studies for potential reform in local governance began in 1980 and were developed semi-legally throughout that decade. When the political change arrived, the new model of local government was ready and was implemented within the first few months of non-socialist rule (IBRD/The World Bank, 2015).

Some important adjustments to multi-level government systems have therefore been necessary in several CEECs and are still needed. These countries are constantly improving and adjusting their decentralisation systems, sometimes by minor and incremental changes. In Poland, new responsibilities have been transferred or are considered for reassignment while new fiscal rules and territorial contracts are implemented. Between 1995 and 2014, the share of SNG expenditure in total public expenditure increased by more than 9 percentage points, going from 23% to 32% (Figure 4). In Estonia, the Local Government Reform under preparation since 2014 provides for a possible reorganisation of functions and tasks of different levels of governance (e.g. in the secondary education sector), together with a fiscal decentralisation reform and a municipal restructuring reform (promotion of mergers and inter-municipal co-operation). In the Czech Republic, some municipal responsibilities are currently being transferred from small municipalities to larger ones and to the central government within the framework of the Social Reform. In Hungary, reform is much more fundamental as the new Constitution and 2011 Local Government Act brought important changes to territorial organisation. Municipal and regional responsibilities have been recentralised to a large degree (primary and secondary education, healthcare, notably hospitals and some social services). The share of SNG expenditure in public expenditure and GDP decreased by 5 and almost 8 percentage points respectively over the last 20 years, particularly since 2011.

2.2. Decentralisation and self-government in Nordic countries is progressing

While already having a solid, long-established tradition of local self-government, Nordic countries have continued to carry out decentralisation reforms over past years by transferring new responsibilities to SNGs (see the impact on SNG expenditure on Figure 4) but also by improving the multi-level governance system towards more quality and efficiency. This was done initially in response to a crisis in the centralist Nordic model of governance. The rising costs of the welfare state led policy makers to seek ways of devolving greater responsibility for policy-making and service provision to the local level, with the aim of securing more responsive and cost-effective local services. "Free-communes" trials were introduced in Norway, Finland, Sweden and Denmark which permit experimentation with the devolution of various functions to local governments

while increasing local discretion to influence policies (DCLG, 2006), before enacting legislation to reinforce and modernise SNGs.

Today, the trend is towards further devolution of responsibilities to SNGs but most often in relation to joint territorial reforms at the municipal and/or regional levels. In 2007, Denmark implemented a comprehensive reform of its multi-level government system, comprising both a territorial component (municipal and regional mergers) and an institutional component: municipalities gained responsibilities for social welfare and education, making them responsible for most citizen-related tasks. The five new regions were granted responsibilities for healthcare services, including hospital services, regional development, and environment. Sweden represents an example of a bottom-up decentralisation process combined with territorial reform. Unlike many countries, the Swedish government did not impose a single decentralisation model, leaving each region free to experiment. The process took place in different waves and led to an asymmetric decentralisation. Some "pilot regions" tested the efficacy of a different institutional structure and the exercise of some new responsibilities (serving as both an example and a benchmark for other regions) (Box 5).

Box 5. **The experimentation of asymmetric and gradual regionalisation in Sweden**

Until the late 1990s, the County Administrative Boards (central government agencies) were responsible for regional development in each county. Since 1997/1998, Sweden has launched a rather singular regional reform process. The national government has not imposed a single model on the counties but instead different regionalisation options (OECD 2010c). It has promoted an asymmetric and bottom-up regionalisation as a gradual and experimental process (a laboratory of regionalisation). The underlying idea is that decentralised policy making leads to more innovation in governance. Therefore, from 1997 onwards, Sweden developed various regionalisation options in terms of political representation and responsibilities in different regions and in different phases: directly elected regional councils in the two "pilot regions" of Skåne and Västra Götaland, resulting from the mergers of respectively two and three countries; an indirectly elected regional council for Kalmar; and a municipality with regional functions for Gotland. The second wave (2002-07) started with the Parliamentary Act of 2002. This Act made it possible for counties, if all local municipalities agreed, to form regional co-ordination bodies (indirectly elected bodies i.e. in line with the Kalmar model) to co-ordinate regional development work. The third phase of experimentation, since 2007, corresponds to a renewed bottom-up demand for regionalisation. It started with the publication of the recommendation for the future of the regional level, published by the Committee on Public Sector Responsibilities in February 2007. The Committee argued for the extension of the "pilot region" model, which was assessed positively, the merger of current counties and the creation of six to nine enlarged regions in order address long-term challenges such as ageing. The reform was not applied as such until now but this bottom-up demand for regionalisation persisted, and since 1 January 2015 10 county councils out of 21 counties are responsible for regional development.

Source: Authors' own elaboration.

A new decentralisation phase is starting in Nordic countries, as most of them are undertaking new local government reforms: Sweden (regional reform by 2019), Norway (regional and municipal reform under preparation, to be implemented in 2017 and 2020) and Iceland (several new transfers of responsibilities to municipalities in the social sector are currently discussed). In Finland, the new institutional reform launched in 2015 followed several failed – or partly failed – territorial reforms, in a context of population aging which generates pressure on the sustainability and quality of service provision (Box 6). It was decided to consider the problem from another angle: instead of upscaling municipalities, the new approach is to upscale the functions that they perform

instead. In order to do so, a new autonomous elected regional level will be created, based on the existing 18 joint municipal authorities (different scenarios have been discussed including the creation of only five regions). These new bodies will be in charge of the organisation of healthcare and social services, among others functions (not totally decided at this point). The approved regionalisation project includes the creation of 18 new autonomous regions, with 15 regions being responsible for their own social and healthcare services (the last three would organise services in co-operation with other regions). A legislative package will be presented in spring 2016, to be followed by a consultation round to discuss draft acts on the organisation of healthcare and social welfare services; on autonomous regions; and on their financing. The central government also reformed its regional-level state administration in 2010 (ALKU reform). These state entities will also have to evolve with the creation of self-governing regions.

Box 6. **Finland: From the "free-communes" trial to the Paras reform and the 2015 new institutional reform**

The Finnish decentralisation process was motivated by the economic crisis of the 1980s and the need to make savings in the public sector. The Free Commune Act was passed in 1988. The experiment was originally intended to run until 1992 but was extended for a further four-year period. Some measures involved all Finnish municipalities, while others were reserved to the 56 selected "free municipalities" (DCLG 2006). This experimentation served as a basis for permanent changes in legislation: in 1995, a new enabling Local Government Act gave local governments more freedom to organise their affairs, thereby permitting greater diversity.

Enacted in 2005 and 2007, the PARAS reform was a multi-dimensional reform promoting municipal mergers, inter-municipal co-operation and changes in managerial practices to improve productivity. It was implemented in different phases from 2007 to 2012. It produced mixed results: few mergers were actually formed; and the impact of co-management areas, created to perform healthcare and education responsibilities at the right scale, created complex and distanced decision-making structures, according to the ARTTU evaluation report. There was very little progress of governance reform in urban areas; the reform did not have very conclusive economic results in terms of greater productivity or in curbing growths in spending. It was also criticised for the method used (reform of local boundaries first instead of reforming local functions). There are, however, several positive results such as the modernisation of municipal management, including budget, and a greater harmonisation of local service provision at the national level, at least for social welfare and healthcare. The PARAS reform was rapidly followed by other reforms to re-structure municipalities. The Municipal Structure Act, which took effect in July 2013, strongly encouraged municipal mergers. The government envisaged to force amalgamations in certain cases. This reform gave rise to strong resistance and was finally abandoned to be replaced by a major new reform based on regionalisation. This reform is a component of the programme of the new government which took office in May 2015.

Source: Authors' own elaboration.

2.3. Devolution, federalisation and regionalisation in the United-Kingdom, Spain, France and Italy

In the United Kingdom, Spain, France and Italy, decentralisation has been closely associated to regionalisation. The United Kingdom chose a complex way towards decentralisation through devolution in 1998, which created the three devolved nations of Northern Ireland, Wales and Scotland, with a directly-elected "national assembly"/parliament and their own government. Major governing power and responsibilities were transferred to them, creating an asymmetric decentralisation between devolved nations (with different powers) and England (no regional

governments). Since 1998, the autonomy of the devolved nations has continued to increase: restoration of devolution in Northern Ireland in 2007; extension of the powers of the Welsh Assembly after the 2010 referendum; new powers transferred to the Scottish Parliament by the Scotland Act 2012.[5] In England, decentralisation under the form of "localism" has gradually emerged since the 2000s. A process based on several white papers and reviews on local government led to the adoption of the Localism Act 2011, aimed at pushing decentralisation forward by, among others, giving local authorities a general power of competence and transferring new responsibilities to local authorities. In parallel, following its 2011 paper, *Unlocking growth in cities,* the government has negotiated "City Deals" with large cities. City deals are an agreement between the government and the city that give local areas specific powers and freedom to help the region support economic growth, create jobs or invest in local projects, provided that they improve their governance.

However, the road to reverse years of relative centralisation is a long one, and until now the Localism Act does not seem to have delivered what was initially planned, in particular in terms of devolution of powers and fiscal decentralisation. A new Act was adopted at the end of January 2016. The "Cities and Local Government Devolution Act 2016" is considered an important step towards decentralisation. It makes various amendments to the 2009 Act to allow greater devolution of powers to combined authorities (housing, transport, planning and policing powers), and to introduce directly-elected mayors, thanks to "Devolution Deals" (11 deals signed as of April 2016).

In Italy and Spain, often referred to as "regionalised countries", a process of decentralisation based on strong regions was launched in the 1970s. Spain, in particular, has undergone a deep process of decentralisation, shifting from a highly centralised system before the 1978 constitution to a highly decentralised one. This process is reflected in the change in the share of SNG expenditure in GDP, which increased by 5.4 percentage points between 1995 and 2014, while the weight in total public expenditure increased by 13 points (Figure 4). This sizable shift even led to the establishment of a quasi-federal country, grounded on strong autonomous communities, although with varying powers, as well as provinces and municipalities. Since the crisis, a profound reform is on-going, affecting both the regions (following the work of the Commission for the Reform of Public Administration set up in 2012) and the local sector (Law 27/2013 for Rationalisation and Sustainability of Local Administration).

In Italy, the decentralisation process has been gradual (Box 7), starting in the 1970s to continue through important steps in the 1990s, until the Constitutional reform of 2001. However, the reform became what could be termed an "unfinished agenda", leading to the adoption in 2009 of a new framework law on fiscal federalism. The deepening of the crisis led the government, in 2011, to go further by reforming Italian territorial organisation, in particular, to abolish the provinces. After several legislative attempts, related to the constitutional nature of the province, the law 56/2014 was adopted. It introduced several changes, in particular the transformation of the provinces into inter-municipal co-operation bodies (which were to become "metropolitan cities" in each of the ten metropolitan areas designated by the law). This implies a new distribution of responsibilities and resources across levels of government, in particular, transfers from the provinces to the regions and the municipalities. A proposal for a new constitutional

reform has been also prepared by the Renzi government and will be submitted to a referendum, to be held in December 2016. If adopted, it will again profoundly change the Italian multi-level governance system. In addition to abolishing the provinces as self-governing entities definitively, the bill provides for significant changes in the allocation of responsibilities between the central government and ordinary regions. In order to avoid duplications, it intends to put an end to shared responsibilities/expenditures and build a system of exclusive responsibilities for the regions and the central government. Regions should also gain more autonomy from the central government – on the condition that their budget remains balanced and that they respect a "supremacy clause", which is to be introduced.

Box 7. **Decentralisation reforms in Italy: A gradual process**

After the expansion of regional functions in the 1970s (especially healthcare in 1978) and the 1980s, decentralisation really started with Law No. 142 of 1990 ("Regulation of local autonomies"), which granted new powers to local authorities. Several other major reforms took place in the following years and significantly changed local governments' fiscal, administrative and political frameworks. In particular, the 1997 Bassanini reform already included the principle of subsidiarity, which would be the cornerstone of the later constitutional reform. Sometimes referred to as "administrative federalism", the very complex Bassanini reform comprised several laws, including law 59/1997. This particular law transferred all functions to the regions and local authorities except those listed in Law No. 59, which remained with the state (Panara and Varney, 2013). The criterion used for the distribution of powers between the different governmental levels was to reach "the optimal level for the exercise of a given function".

The Constitutional reform of 2001 was a major move towards decentralisation, setting up a multi-layered governance system: regions, provinces and municipalities were enshrined in the Constitution as autonomous governments and placed on the same level as the central government. It "upgraded" the system created by the Bassanini reform to constitutional level by explicitly setting up a multi-layered governance system and identifying a role for each subnational layer. The clause listing the responsibilities of the central government was introduced in the Constitution, while the regions received all residual responsibilities. However, the meaning of the reform was far from clear as there was no specific provision determining the fundamental functions of the local authorities. As a result, the allocation of responsibilities between the different layers of government remained imprecise. Finally, the constitutional reform was supposed to be implemented by subsequent legislative decrees but several attempts to implement this reform failed (Panara and Varney, 2013). In the meantime, the funding system had become opaque, inequitable with respect to public service levels, and fiscal relations had become ever more inefficient and prone to spending excesses and deficit bias (Blöchliger and Vammalle, 2012).

A new constitutional reform was proposed in 2006. It aimed, among others institutional changes, at further strengthening the regions, transforming Italy into a quasi-federal country like Spain. However it was rejected in a national referendum by 61% of the voters. Finally, the economic crisis of 2008 exacerbated the risk of an unsustainable fiscal federalism and a new framework law was adopted in 2009. It aimed at reshaping subnational government functions and relations between levels of governments. It also aimed at increasing subnational fiscal autonomy, as it modified substantially article 119 of the Constitution on financial provisions. This fiscal federalism law No. 42 of 2009 set a milestone for Italy in its gradual move towards decentralisation and federal institutions. While focusing on fiscal matters (see below), it included several other components (transfer of state property to municipalities, legal status for Roma Capital, definition of services standard costs). The objective of

Box 7. **Decentralisation reforms in Italy: A gradual process** *(continued)*

the reform was to increase both the efficiency and accountability of SNGs and to ensure adequate levels of subnational services across the country. However, as in the other previous cases, Law 42 set down the principles for reform but left their implementation to a set of 8 legislative decrees (and around 70 concrete measures) which were expected to be adopted before 2016. This implementation process has been slowed by the economic and public finance crisis but all decrees were adopted in 2010 and 2011.

The deepening of the crisis and the need to cut costs and consolidate public finances led the government to suggest reforming the Italian territorial organisation in 2011, in particular, abolishing the provinces. This process led to the final adoption of Law 56/2014 in April 2014 and the Bill on Constitutional Reform (see main text).

Source: Authors' own elaboration.

In France, the decentralisation process has taken place in several waves over the past three decades (Box 8). France moved from one of the most centralised systems of public administration in Europe to embrace a substantial level of decentralisation (CoR, 2001). However, France remains less decentralised than Italy and Spain and is among the "middle-decentralised" of the OECD (Figure 2). A new multi-level governance system was announced in 2013, the so-called, Acte III de la decentralisation. The government (elected in 2012) initially planned to carry out one large reform with different sub-chapters. However, following intense debates in Parliament, a more gradual approach was adopted through several proposals, covering both territorial and institutional issues. The reform package consists of three parallel reforms phases, with successive laws passed in 2014 and 2015. The first one is dedicated to metropolitan governance (MAPTAM law on the Modernisation of Public Territorial Action and Metropolises, enacted in January 2014). The second one is a reform of regional boundaries, introducing forced amalgamations of several French regions (law relative to the Delimitation of Regions and Regional and Departmental Elections), and came into force in January 2015. The third law was dedicated to subnational responsibilities and inter-municipal co-operation (law NOTRe on the New Territorial Organisation of the Republic), and came into force in August 2015. This law clarifies the responsibilities allocated to each level of subnational government through the removal of the general clause of competence for the regions and the departments, deemed to generate overlapping of responsibilities and duplication of spending (this clause had been restored by the MAPTAM law).

The law NOTRe also modifies the distribution of responsibilities between subnational governments, strengthening those assigned to the regions. In particular, regions gained greater responsibilities and powers regarding regional economic development (aid schemes to SMEs, innovation, internationalisation), territorial planning, and environment protection planning. Their planning power, based on regional planning schemes, now has a mandatory and prescriptive character vis-à-vis the decisions of other authorities. Metropolitan cities may be exempted from it as far as the “regional plan for economic development, innovation and internationalisation” is concerned, which may cause some tensions in the future between regions and metropolises. Regions have also a new regulatory power, allowing them to adapt national legislation to the local context. Departments' responsibilities (and even their existence at some point) were questioned in the early stages of the reform but they ended up keeping most of their responsibilities (e.g. secondary schools, roads, social affairs). Departments will focus more on social

solidarity and territorial cohesion, in particular, the support rural municipalities. Finally, the law NOTRe restructured the inter-municipal landscape (increase of the minimum population threshold, which will reduce the number of groupings) and made it mandatory for municipalities to transfer new functions to inter-municipal bodies (see Part II). Therefore, inter-municipal co-operation bodies should become the main players at local level, thereby reshaping the municipal landscape.

Box 8. **Successive waves of decentralisation in France: From Act I to Act III**

The "first Act" (later called "Acte I de la décentralisation") was launched in 1982-83 with the Deferre laws, named after the minister of the interior of the time. These decentralisation laws cancelled the *a priori* oversight of the central government on local governments, replacing it with the principle of "free administration". This oversight was previously carried out by the prefects, representatives of the central government at the local level. They organised the transfer of responsibilities (education, social affairs, etc.) and resources (staff, finances), in particular to the *départements* and the regions, created as self-governing bodies by the above-mentioned laws. New contractual arrangements across levels of government were implemented in 1982: the State-Region Planning Contracts or *Contrat de plan État-région* – CPER, to serve as a planning, governance and co-ordination mechanism in regional development policy. CPER has become a major co-ordination tool for co-deciding and co-financing interventions between the central government and SNGs, and is still in use with the new 2015-2020 generation of CPER (OECD 2015h).

The "second Act" (*Acte II de la décentralisation*) started with a revision of the Constitution, and was implemented from 2003 onwards through several organic laws. New responsibilities were transferred to SNGs, mainly to departments and regions (social sector; spatial planning and regional development; local and regional transport and national roads; vocational training, etc.). Subnational financial autonomy and the ability of local governments to carry out experiments in several areas (e.g. management of structural funds or of ports under state responsibility) were strengthened.

In the late 2000s, the government sought to further deepen decentralisation and improve its functioning. The Committee Balladur was established in 2009 for this purpose. The central government, through the different ministries and the prefectural administration, still had important powers in local matters. Although it retained full responsibility in relatively few areas, it still shared many responsibilities with SNGs, thereby often holding on to a major role. It became essential to reorganise the system to avoid overlapping responsibilities (inducing a high cost for taxpayers) and to improve transparency and accountability (OECD 2006, OECD 2007c, OECD 2012c).

In December 2010, a multi-faceted local government reform was launched, based on several pieces of legislation. It included multiple components, among which a clarification of responsibilities (abolition of the general clause of competence for the *départements* and the regions); the setting up of common "territorial councillors" for regions and *départements* (councillors who would sit both on general councils and on regional councils from 2014 onwards); a reform of the local taxation system; reform of equalisation mechanisms and co-financing frameworks; streamlining of inter-municipal co-operation; the creation of a new status of *métropole*, etc. This package of laws has been widely contested, seen by some as a new step towards decentralisation, and by others as a movement towards recentralisation. In particular, the 2010 tax reform reduced substantially the fiscal autonomy of regions and *départements*. The powers of the French regions, recently created as self-governing authorities, were further reduced in 2010.

As promised in the programme of the subsequent government elected in 2012, important parts of the 2010 legislative package were revoked (in particular the "territorial councillor"). A new territorial and decentralisation reform was announced in 2013, referred to as the "Act III of decentralisation", which resulted in the adoption of three new laws in 2014 and 2015 (see main text).

Source: Authors' own elaboration.

2.4. The long path towards decentralisation in Asia

In Asia, as a corollary of democratisation engendered by economic development, decentralisation and local autonomy have become vital reform agendas (Kamo, 2000). However, decentralisation initiatives have been hesitant in the two OECD Asian countries (Yagi 2004, Ahmad E., Brosio G. and Tanzi V. 2008).

In Korea*,* the decentralisation process is relatively recent. Starting in 1987 with the "Declaration for Democratisation", it gained momentum the following year when the Local Autonomy Act and the Local Finance Act were thoroughly reformed. The first local elections (held in 1991 for local councillors and in 1995 for the chief executives of local governments) marked the real birth of the decentralisation process. This process continued in the 1990s and 2000s, in particular through a vast public sector reform, implemented in 1999, as well as the 2004 the Special Act on the Promotion of Decentralisation. However, the recent global crisis illustrated how policy making and implementation are still centralised in Korea. The decentralisation of governmental functions has slowed down and fiscal decentralisation still remains limited (OECD/KIPF, 2012c).

In Japan, the push for decentralisation started during the post-World War period, and was viewed as a means of achieving more democratic political outcomes. The promotion of a democratic system of local government was part of the national agenda. However, the model of central-local relations put in place remained quite centralised in practice, based on the agency-assigned function system. In the 1990s, an ambitious decentralisation programme was launched, encompassing changes to local governments' functions; an increase in local authorities' autonomy; a revision of local governments' financing; and a territorial reform based on municipal amalgamations. This process was carried out through several steps over a long period (Box 9). However, the share of SNG expenditure in public expenditure and GDP over the last 20 years (Figure 4), already very high in 1995 (SNG expenditure represented around 50% of public expenditure), was not impacted and even decreased instead of increasing. Most SNG expenditure was, in the main, delegated spending from the central government, with little or no decision-making power. The regular decreases in the share of SNG spending since 1995 are also partly due to a significant reduction in the number of local employees (from 3.28 million in 1994 to 2.76 million in 2012, i.e. a decrease of 16%) and wages, as well as fiscal consolidation measures.

The Japanese decentralisation process has been supported by a Decentralisation Promotion Committee, set up in July 1995 and composed of members from the private sector, local government, academia, etc. It was charged with drafting recommendations for the reform, to be submitted to the Prime Minister. This Committee, under different names and configurations, remained throughout the process. Many tensions arose with the central government (still largely in control of local matters), and recommendations from the different committees have been regularly modified and watered-down. A revision of the Local Autonomy Law came into force in 2014, and in 2015, a local finance plan considered enhancing decentralisation and local fiscal autonomy. The current decentralisation process takes place within the broader framework of the "Regional Revitalisation Strategy" and the National Spatial Strategy, adopted in August 2015 (OECD 2016a).

Box 9. **A decentralisation process carried out step by step in Japan**

New moves towards decentralisation started in 1995 in a context of serious economic downturn and criticism on excessive centralisation. The process has been carried out step by step over a long period, with the support of a Decentralisation Promotion Committee set up in July 1995. The Committee was empowered with the ability to conduct investigations and deliberations, and could request information from both local and national authorities.

The first "Decentralisation Promotion Reform", launched in May 1995, led to the adoption of the Omnibus Decentralisation law in 2000 - the cornerstone of the new wave of decentralisation in Japan. This broad decentralisation reform centered on three main axes: an increased local government effectiveness and efficiency; greater local autonomy; and better accountability. One of the major outcomes of this reform was to successfully abolish the much- criticised system of agency-assigned functions, which required local governments to implement public policies decided at the central level. This system, often described as the core of Japanese centralism, was criticised for its lack of transparency regarding the origin of decisions, and because it treated subnational governments as mere local de-concentrated state services (CLAIR, 2010). Other objectives were assigned to the reform, such as correcting the excessive population concentration in Tokyo, or addressing ageing issues. The Omnibus Decentralisation law (also called the "comprehensive Decentralisation Law") was extensive, introducing revisions to more than 475 anterior laws and involving major changes in the Japanese multi-level governance system. It included, in addition to the abolition of the Agency Delegated Function system, the transfer and clarification of responsibilities; the reduction of central government control; the creation of a new system of cities; the promotion of municipal mergers, etc. This law was followed by the Trinity Reform in 2004-06, which laid out the financial component of the decentralisation reform.

The Second Decentralisation Promotion Reform started in 2006 and came into force the following year. It complemented the first reform and aimed at reaching similar objectives: granting further authority to local governments and rationalising their functions; rationalising the power of central government on local authorities; and consolidating local administrative systems through municipal mergers. It also considered reforming the central government regional administration at the territorial level. New sets of recommendations led to the adoption of a new set of bills, in 2011 and 2012. In parallel, reform of the prefectural level and the creation of a "Doshusei" Regional System were considered but have not been implemented since. Further decentralisation reforms are still on the agenda as SNGs still have limited autonomy, in particular, in relation to spending and revenue.

Source: Authors' own elaboration.

2.5. *The decentralisation approach in New Zealand*

New Zealand presents singular forms of multi-level governance systems, reflecting its British origins, with local government arrangements still close in nature to those in the United Kingdom or Ireland. In these countries, the central government plays a key role in driving local government reforms. These reforms often aim in particular at increasing governance flexibility, improving local efficiency, as well as access to and quality of local public services, rather than decentralising new functions (Box 10).

Box 10. **Local government reforms in New Zealand: The influence of the New Public Management movement**

New Zealand is among the most centralised countries in the OECD with regard to spending responsibilities. SNG expenditure represented only 4.5% of GDP and 11.3% of public expenditure in 2013 (Figure 2). However, SNGs enjoy a certain level of autonomy in terms of spending as well as in terms of revenues. More than 52% of their revenues come from own-source taxes (property tax).

Influenced by the NPM movement, many parallel measures were introduced in the late 1980s / early 1990s to reform local governments in New Zealand. These measures included a restructuring of local authorities through a drastic reduction in their number (1989 consolidation reform); a separation between local policy-making and policy implementation; a move towards more corporatisation of local public services; and greater local government accountability. A large reform of local governments' functions came into force in 2002 with the aim to enhance local governments' efficiency (in particular for service provision) and increase their accountability. The Local Government Act 2002 (LGA 2002) broadened and redefined local government's powers, roles and responsibilities, by separating policy making from policy implementation. It strongly increased their autonomy regarding the activities they undertake, by providing them with a general power of competence. Previously they could only undertake activities permitted by law. With the purpose of creating democratic and effective local authorities, it introduced collaborative, citizen-centred processes ("special consultative process" with many requirements in terms of information provision and public consultation), within a framework oriented to securing community well-being and sustainable development (Reid M, 2010). Another major component of this set of reforms was a move towards greater corporatisation of government-owned commercial activities, either through privatisation or the creation of public (or semi-public) corporations. This Act was amended in 2010 and again in 2014, in line with the Better Local Government New Zealand reform, in order to clarify and increase transparency for development contributions; increase flexibility for local boards; encourage inter-municipal co-operation and shared services (in particular with the private sector); clarify responsibilities between regional councils and territorial authorities; promote long-term planning, etc. Finally, the Local Government (Financial Reporting and Prudence) Regulations 2014 introduced new benchmarks and indicators for financial management.

Source: Authors' own elaboration.

3. Fiscal reforms: A sometimes overlooked but key component of decentralisation

3.1. Specificities and difficulties of multi-level fiscal reforms

3.1.1 The specificities of multi-level fiscal reforms

As a general rule, decentralisation of spending responsibilities should be accompanied, according to the "connection" or "matching principle", by an equivalent transfer of additional funds to ensure that SNGs will be able to perform their new tasks in a proper manner. In the course of decentralisation, it is recommended avoiding a mismatch between subnational revenues and expenditure (Prud'homme, 1995; Ter-Minassian, 1997; de Mello, 2000,). These additional funds come mostly from central government transfers (general or earmarked) but also from shared taxes as well as from additional own-source revenues (local taxes, user fees and charges, revenues from assets). The assignment of revenue sources among governments is a key dimension when designing or reorganising the subnational funding system. The composition of revenues may vary greatly from one country to another, from one SNG level to another, and even from one local government to another (e.g. between urban and rural authorities). In this process, another important step is to define the degree of fiscal autonomy with which SNGs can exercise their authority: the extent of discretion in intergovernmental transfers (from earmarked and conditional transfers to general-purpose grants based on a formula) and tax autonomy. Greater tax autonomy for SNGs has pros and cons however (Ter-Minassian, 2015). On the positive side, SNGs benefit from more own-source revenues,

with certain benefits: improving the quality and efficiency of spending to respond to community preferences, increasing democratic accountability to citizens, ensuring a better mobilisation of local resources, improving budget management efficiency, promoting fiscal responsibility, and ensuring better access to credit. More tax autonomy can also provide incentives for growth-oriented economic and fiscal policies. However inappropriate fiscal instruments and little discretion to use them may harm decentralisation processes which would be "doomed" (Yilmaz, Beris and Serrano-Berthet, 2008, Reid 2015). There are however some counter-arguments which would justify limiting to a certain extent tax decentralisation which are linked to economic, distributional, administrative and political economy obstacles: Enhancing tax autonomy may have some drawbacks, leading to a higher mobility of tax bases within the national territory, hence increasing the scope for tax evasion, and leading to a detrimental form of tax competition among SNGs (race to the bottom). Other possible negative impacts include an unequal distribution of tax bases, increasing revenue disparities and undermining SNG ability to provide common standards for basic public services; a drop in the cost-effectiveness of subnational tax administrations (diseconomies of scale, lack of capacities); and a risk of greater fiscal instability for both SNGs and the central government. In this context, a key challenge of multi-level fiscal reforms is to set up the vertical distribution of tax revenues across levels of government. The issue of which taxes to assign to SNGs, and under what criteria and degree of discretionary power over tax bases and rates, is particularly difficult.

New fiscal arrangements should include an equalisation system of revenues and costs. Decentralisation processes may lead to disparities across SNGs and territories in terms of revenues and increase the heterogeneity of service provision. Equalisation can be based on horizontal and vertical mechanisms, and also aims at developing national norms and standards to ensure equal access to local services and a minimum level of service quality (Allers, 2011).

Fiscal decentralisation reforms also need to provide for the definition and implementation of sound budgetary, accounting and reporting frameworks. These frameworks should be based on common standards for all levels of government, in order to facilitate the monitoring, control and transparency of financial operations. This requires an efficient budget administration system at the subnational level, which can be a key issue if SNGs lack capacities. Hence, reforms should establish an appropriate division of labour between national and SNGs (for tax collection, cadastre management or maintenance of companies' registry, for example). Strong co-ordination mechanisms and institutional and technical support for assisting low-capacity SNGs should also been introduced. Subnational governments could also gradually enhance their administrative capacities.

Strengthened fiscal decentralisation also requires rethinking the role of the state in the exercise of budgetary and financial controls on SNGs. These typically take the form of a posteriori controls rather than a priori ones. The regulatory framework should be revised to include clear and sound fiscal rules, and provide for internal (e.g. internal audit committees) and external audit procedures (e.g. ministries, independent public audit offices, accounting professionals, etc.).

3.1.2 The difficulties of multi-level fiscal reforms

As described above, multi-level fiscal reforms should go together with a decentralisation of spending responsibilities, ensuring a sound overall design of

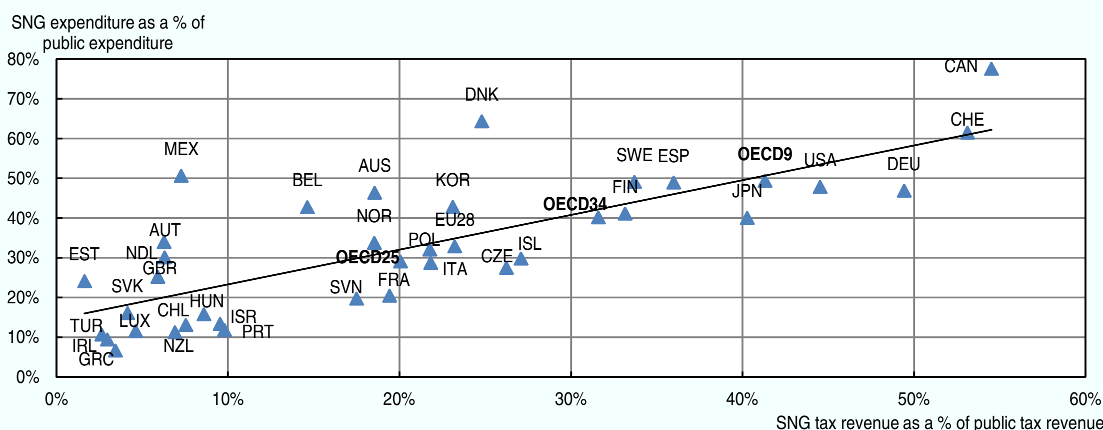
intergovernmental fiscal arrangements. However this is not always the case and fiscal reforms are sometimes the "weak link" of decentralisation reforms. In a number of OECD countries, the process of decentralisation has been quite unbalanced. In some cases, responsibilities and expenditure duties have been shifted to SNGs without transferring proper fiscal resources, leading to unfunded mandates and to a high risk of deterioration of public service provision at local level. In other cases, functions have been delegated to the subnational tiers and with the accompanying financial means but without delegating sufficient autonomy over these resources, in particular in terms of tax autonomy. The "fiscal gap", i.e. the difference between SNG expenditures and own-source revenues can be large in some countries, and is widening in some cases. In several OECD countries, SNGs' dependence on central government grants may be particularly significant (Box 11).

Box 11. **Subnational government revenues and fiscal imbalances in 2014**

In 2014, SNG revenue represented 16% of GDP and 42% of public revenue in the OECD. Shared and own-source taxes were the main source of SNG revenues on average (44% of total revenues). Grants and subsidies represented 38% of subnational revenue while local public service charges (tariffs and fees) and property revenues (sale and operation of physical and financial assets), represented 15% and 2% of SNG revenue respectively. The share of each category of revenue in total SNG revenue varies a lot from one country to another, reflecting each national inter-governmental fiscal framework and the level of fiscal decentralisation. Tax revenues (shared and own-source) are significant in most federal countries (Germany, Switzerland, United States, Canada), as well as in several unitary countries (more than 48% of local revenue in Iceland, Sweden, New Zealand and France in 2014). By contrast, SNGs depend largely on central/federal government transfers in federal countries such as Mexico and Austria, and in numerous unitary countries (e.g. Netherlands, Slovak republic, Turkey, the United Kingdom, Estonia or Ireland).

Similarly, there are great imbalances across countries between the level of SNG expenditure as a share of public expenditure and the level of SNG tax revenue in public tax revenue. These imbalances reflect the level of fiscal decentralisation in OECD countries – however, imperfectly, as tax revenue also include shared taxes, on which SNG have little or no taxing leeway.

SNG expenditure as a % of public expenditure and SNG tax revenue as a % of public tax revenue (2014)



Note: 2013 Mexico, Chile and New Zealand; 2012 Australia; 2011 Turkey

Source: OECD (2016d) Subnational governments in OECD countries: key data (brochure). Subnational government structure and finance database: http://dx.doi.org/10.1787/05fb4b56-en.

In addition, **some issues may be overlooked or underestimated by governments**, such as increased fiscal disparities, fiscal indiscipline or a lack of financial sustainability.

Reforming fiscal relations across levels of government to make them **more efficient, more equitable and more stable is therefore a continuous process.**

However, such processes are particularly difficult to carry out. They may encounter **political, technical or economical obstacles, as well as lack of capacities at the subnational level** (Blöchliger and Vammale, 2012). The costs and benefits of fiscal reforms tend to be unevenly distributed, creating winners and losers at all levels of governments. When local taxes are concerned, citizens may be affected as well (e.g. the poll tax riots in the United Kingdom). The central government should accept to lose part of its fiscal powers and control (moving from earmarked grants to general grants, sharing national taxes, increasing local tax autonomy, etc.). In contrast, SNGs may collectively complain about a reform limiting their financial autonomy (cutting grants, moving from earmarked grants to general grants, reducing taxing power, shrinking local leeway over tax rates or bases, imposing spending constraints and fiscal rules, such as borrowing limits, budget balance targets, etc. There may be also diverging interests within the subnational sector itself: between regions or municipalities or across the same tiers, between rural and urban municipalities, between richer and poorer local governments, between wealthy and less wealthy local governments. For instance, the introduction of horizontal equalisation mechanisms can be perceived as a limitation of local autonomy, especially by "giving" authorities as opposed to "receiving" ones. In Italy, for example, while all subnational tiers of government favour the fiscal decentralisation process introduced by Law 42/2009 on Fiscal Federalism, there were strong tensions over the actual implementation. In particular, the definitions of equalisation funds and standard costs generated a lot of tension between rich and poor SNGs.

As a result, **reforms can be expensive** as they need to compensate losers with temporary transition funds or mechanisms. They can also **increase uncertainty levels**, and may thus not be acceptable in crisis periods (Tompson, 2010).

Many efforts to reform fiscal relations have encountered difficulties, and have stalled, or have been introduced only partially after several unsuccessful attempts. In the short run, **fiscal federalism reforms tend to be a zero-sum game where one government level will lose what the other government will win**, leading to the temptation of status quo (Blöchliger and Vammale, 2012).

3.2. Overview of fiscal reforms in the OECD

In all countries, decentralisation reforms have been accompanied by local finance reforms, redefining the system of inter-governmental grants (general and earmarked); of subnational shared and own-source taxation (Box 12); and equalisation mechanisms and budgeting frameworks, including fiscal rules (budget balance and debt). Establishing an appropriate framework is challenging, as it needs time to design and implement and requires consistent objectives (see 3.1).

In federations, major fiscal reforms have been implemented recently with the aim of improving inter-governmental fiscal mechanisms. In Canada, an important equalisation reform was conducted in 2007, followed by a second reform in 2009. In Austria, the 2008 reform of the Financial Equalisation Law transformed 40% of federal transfers to the federated states into tax revenues (not earmarked) in order to reduce strong vertical fiscal imbalance. In Germany, the 2009 *Föderalismusreform II* modified financial arrangements (phasing out of the *Solidarpakt II* transfers and of the existing horizontal equalisation system planned for 2019, creation of the Stability Council, and the introduction of a "debt brake" to reduce future public debts). In Belgium, the 2001 Fifth State reform

(Lambermont Agreement) reinforced the federalisation of the country, and re-assigned several taxes to the regions. Ten years after, in 2011, the Sixth Reform of the State modified the Special Finance Act to further reinforce regional tax autonomy. Starting in 2014, with a transition mechanism for a period of ten years, regions are able to raise additional percentages on the individual income tax ("regionalisation" of the PIT) and gain additional powers on tax bases and exonerations. New transfers are being introduced to fund the new responsibilities. The reform also introduces a revision of the equalisation mechanism, called "national solidarity". In Switzerland, the Federal Reform adopted in 2004 and in force since 2008 modified the equalisation system. It also introduced new rules for inter-cantonal collaboration to avoid fragmentation and "competitive federalism", especially in the area of cantonal tax and fiscal policy competition. In Spain, after several years of intense negotiations, Law 22/2009 on the financing of the autonomous communities was adopted. In effect since 2011, it has introduced major changes, increasing significantly the financial autonomy of regions. The share of autonomous communities in shared taxes was raised (from 33% to 50% for PIT and from 40% to 58% for special taxes) and autonomous communities gained a greater leeway with these taxes. Solidarity was reinforced with the reform of the equalisation system: 75% of tax proceeds are now subject to redistribution, mainly determined by demographic patterns (through the Guarantee of Basic Public Services Fund). Two new convergence funds, funded by the state, were introduced to offset regional imbalances. In Mexico, the 2007 Fiscal reform increased the federated states' taxing powers and simplified the formulas for the distribution of federal transfers. In Australia, the Intergovernmental Agreement on Federal Financial Relations (IGAFFR) established through the COAG (Council of Australian Governments) was reviewed in 2008, with the objective to simplify and increase the flexibility of intergovernmental grants.

In most central and eastern European countries, new Acts on Local Government Revenue were adopted or revised in the 1990s (during the transition) and 2000s (at the time of EU accession). These reforms were often linked to the decentralisation of expenditure duties. In Poland, for example, the 2004 Act on Local Government Revenue profoundly modified the financing of subnational governments. SNGs gained more financial autonomy, with a decrease in the share of central transfers (and of earmarked grants), and increased shared tax revenues (higher proceeds from PIT and corporate tax). In Slovakia, the 2005 Act on Local Financing deeply modified the subnational financial system, by raising both shared and own-source taxes, and reducing central government transfers to SNGs. In Slovenia, a new law on municipal financing came into effect on January 1, 2007 (replacing the 1998 law). The system of vertical tax equalisation was consolidated with a transitional period. The financial autonomy of municipalities was reinforced through the introduction of new resources - in particular a poll tax aimed at covering the average costs necessary to perform urgent municipal tasks. In these two countries, the reforms led to a significant increase in the share of tax revenues in GDP and public tax revenues (Box 12).

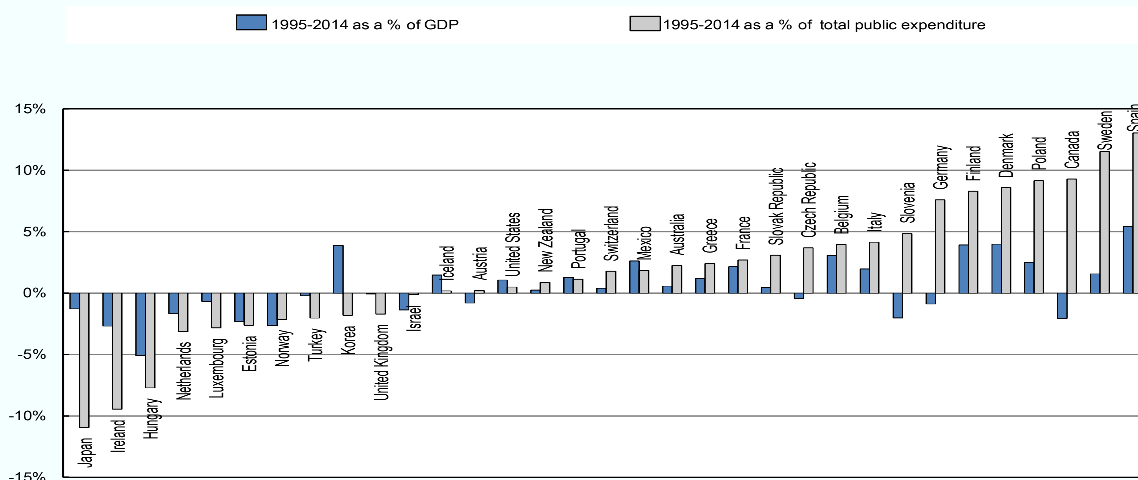
Box 12. **Fiscal decentralisation and tax revenues in OECD countries between 1995 and 2014**

Between 1995 and 2014, subnational tax revenues (shared and own-source taxes) increased – or decreased – significantly in several countries as a % total public tax revenue and GDP. These changes typically reflect economic performances (taxes such as PIT, corporate tax, VAT, property transaction, consumption, construction activity, etc., are sensitive to economic fluctuations). They may also be impacted by fiscal reforms affecting SNGs. Several fiscal reforms aimed at increasing the importance of taxes in subnational funding by allocating larger shares of national taxes to SNGs and/or more taxing powers (ability to create local taxes, to determine rates and bases and to grant tax allowances or reliefs). These fiscal reforms have resulted in significant increases in SNG tax revenues in Spain (in 2002, 2009 and 2012), Poland (2004), Slovenia (2009), Czech Republic (2005), Belgium (2002), or Japan where the increase was more progressive. In Italy, tax revenue increased vastly after the 1998 Bassanini reform from 25% in 1997 to 41% of subnational revenue and after the 2009 reform).

In contrast, the share of subnational tax revenue contracted in Norway (abolition of the national corporate income tax as a local tax in 1999), Denmark (especially since the 2007 local government reform and the abolition of counties) and some federal countries (Australia and Switzerland).

However these figures do not provide a fair view of fiscal decentralisation, in particular in relation to tax autonomy. Tax revenue figures do not make the distinction between shared taxes and own-source taxes, for which SNGs have a certain leeway over rates and bases. In France for example, the 2010 local finance reform did not affect the share of tax revenue in local revenue or GDP, but diminished significantly the share of own-source taxes, inducing a reduction in tax autonomy. In other countries, the reverse is also true: a stability in terms of tax revenue may have been be observed over the years although there was an increase in tax autonomy resulting from the introduction of new own-source local taxes or the broadening of the local decision-making power for setting rates or bases on existing local taxes (e.g. property tax). Italy recently went through such situation.

Subnational tax revenue as a % of total public tax revenue and as a % of GDP in 1995 and 2014 (changes expressed in percentage points)



Note: 2013 for Australia, 2003-2013 for Mexico; 1997-2013 for New Zealand, 2013 for Japan, 1998 for Iceland; Information on data for Israel: http://dx.doi.org/10.1787/888932315602.

Source: Authors' own elaboration.

Important fiscal reforms were also implemented in other unitary countries such as Portugal (2007 Local finance Reform), Denmark (2007 local government reform, introducing new financing and equalisation systems), Korea (2005 and 2009 fiscal reforms creating general-purpose grants), Norway (2007 reform of the property tax),

Turkey (2008 Law on Allocations from Tax Revenues under the General Budget to Special Provincial Administrations and Municipalities), Sweden (2005 reform of equalisation), Italy, France and Japan (Box 13). In Denmark and France, these reforms led to a decrease in subnational revenue autonomy, while in Turkey, Korea, Finland, Portugal, Italy and Japan local revenue autonomy increased.

Box 13. **Local government fiscal reforms in Italy, France and Japan**

Italy: the difficulty to properly implement the 2001 constitutional amendment agenda on the financial side rendered the funding system opaque, inequitable with respect to public service levels. Fiscal relations had become ever more inefficient and prone to spending excesses and deficit bias. The 2008 economic crisis exacerbated the risk that fiscal federalism would become unsustainable. In a context of successive failed attempts, the reform was ripe and it was urgent to adopt it. This was done through the fiscal federalism law No. 42 of 2009 (implementing article 119 of the Constitution) which made a significant move towards decentralisation. It focused on fiscal matters but also included several other components (transfer of state property to municipalities, legal status for Roma Capital, definition of services standard costs). The objective of the reform was to increase SNG fiscal autonomy, efficiency and accountability, and to guarantee an adequate level of subnational services across the country. It included several elements: i) an increase of own-taxes and shares in national taxes with the aim of covering spending obligations, which also induce the replacement of a portion of central government grants by tax revenues; ii) a clarification of spending obligations, in particular by making a distinction between compulsory services and all other services (for these compulsory services, minimum standards are defined by the central government whereas for the others, SNGs are free to set their own standards and spending levels; iii) a review of the equalisation system, with the introduction of a new system based on covering the costs of essential public services and equalising tax-raising capacities; and iv) a process for harmonising accounting principles across regional and local governments (Blöchliger and Vammalle, 2012). New fiscal reforms are underway concerning SNG revenues, budgetary frameworks (including the harmonisation of SNG accounting standards), borrowing rules and multi-level financial governance.

France: an important tax reform took place in 2010 after years of discussion. Its primary objective was to abolish the local business tax (*taxe professionnelle*), paid by companies and based on the rental value of fixed assets. This tax had always been criticised for its negative impact on companies, employment and investment, and for the significant inequalities it created both among SNGs and businesses. The business tax reform led to a broader reshuffle of the local tax system, decreasing the share of own-source tax in favour of shared taxation. The local business tax was partially replaced by a new “territorial economic contribution” (CET), composed of two taxes: a business tax on real estate (CFE – own-source), and a business value-added tax (CVAE). Other shared taxes were created in parallel. The reform led to a tax “specialisation” between subnational government tiers (all SNGs used to benefit from the same four local taxes before the reform). Departments and regions lost many of the taxing powers. They are now particularly limited for the regions. New horizontal equalisation mechanisms were introduced: the Equalisation fund for inter-municipal and municipal resources (FPIC, redistributing 2% of total tax revenues in 2016), the departmental fund based on the property transaction tax (droits de mutation), and the Equalisation funds based on the business value added tax (CVAE, for departments and regions). These new mechanisms supplement existing vertical equalisation instruments based on central government grants, allocated according to different criteria (expenditures, resources or specific constraints). Several other reforms have been prepared since 2010 but were postponed to 2017. In particular, reforms of the main general-purpose grant and of the equalisation system were considered. Regional financial resources should be reformed to match new regional responsibilities. The future of the regional taxation system remains unclear (at the time of writing this paper). In 2015, the government announced a major increase (from 25% to 50%) of the regional share in CVAE revenues

Box 13. **Local government fiscal reforms in Italy, France and Japan** *(continued)*

(*cotisation sur la valeur ajoutée des entreprises*). According to the 2016 Finance Law, the costs corresponding to new transfers of responsibilities resulting from the reform will be, prior to their transfer, assessed by local commissions.

In Japan, the 2004 Trinity Reform included three major components: i) the transfer of tax revenues from the central government to local governments (creation of a tax-sharing system); ii) a reform of the equalisation tax; iii) the abolishment of several national earmarked grants. The reform aimed at increasing the share of own-revenues in local governments' budgets while decreasing their reliance on inter-governmental transfers. A Committee for the Decentralisation Reform was created and the six major regional government associations proposed plans for reforming the national transfer system. However, these recommendations were not taken into account, which was strongly criticised. Local governments argued that they didn't gain enough financial autonomy and independence. Critics also objected that the primary aim of the reform may have been fiscal consolidation rather than decentralisation. Transfers of tax revenue sources were insufficient to compensate for the cuts in grants, which led to financial deterioration at local level and increased the gap between rich and poor local authorities. New reforms implemented since the Trinity reform included one of special funds (the conversion of earmarked grants into general-purpose grants in 2011 and 2012) and a reform that increased the local rate of national sales tax in 2014. New reforms are also under preparation.

Source: Authors' own elaboration.

3.3. Impact of the crisis on subnational fiscal reforms

Over the last few years, the crisis had a strong impact on planned or ongoing fiscal reforms. In the short-run, the crisis has had diverging effects on reforms across countries (Allain-Dupré, 2011). Many countries today are, however, moving back to their reform agenda.

In the early stages of the crisis, many countries planning to introduce local finance reforms decided to freeze the process. The focus on urgency hindered institutional reforms, which often require long negotiations before being adopted. For instance, in Finland, the planned reform of the grant system was scaled down. In the United Kingdom, the Localism Act was adopted, but not the planned financial reforms, such as the Local Finance Government Bill 2012-13. In Italy, the adoption of the eight legislative decrees implementing Law No. 42 of 2009 was slowed by the crisis.

In other countries however, **the crisis contributed to accelerating some reforms.** This was especially the case in countries facing strong recessions. In the Czech Republic, amendments to the 2000 Local Finance Act increasing the shares of municipalities and regions in national taxes passed in 2013 and 2015; in Estonia, the local share in PIT revenues was modified in 2013. **Many countries also sought to optimise revenues from property taxes**. Changes in property tax systems were often resisted over the last two decades, as they tend to be particularly unpopular (Blöchliger, 2015, Slack and Bird, 2014). Several OECD countries used the crisis as an opportunity to enact reforms in this sector. New property taxes were introduced both in Ireland (Local Property Tax) and in the UK (Business Rates retention and localisation of the Council tax) in 2013. Italy re-introduced a property tax in 2012 (IMU). Some countries changed their rates or bases, or increased the autonomy of SNGs over them (Netherlands, Spain). Reforms also modified land registries, valuation and revaluation methods on tax bases, etc. In Portugal, a major initiative involving the revaluation of 4.9 million properties was undertaken in 2013 to underpin the new property tax regime (EC, 2013). In France, an important reform of

rental values was launched in 2015. It will take several years, as data have not been updated since 1970 and are thus obsolete, and/or complex, inequitable and illegible for taxpayers. The reform has begun with an experiment in five *départements*, which have tested a new method of assessing the rental values of residential premises. A report detailing the impact of this revision on taxpayers, local government and the central government was presented to the Parliament.

Today, many countries facing deteriorating fiscal situations are moving back to their reform agenda. Indeed, the fiscal consolidation context is likely to trigger reforms increasing SNG efficiency, tightening fiscal discipline, and modifying central grants and equalisation mechanisms. In addition, many reforms are also being taken to alleviate the issues of ageing and health cost pressures on subnational finances (OECD 2015f), and to improve access to external funding.

Central governments' transfers to SNGs have been recently reformed in several countries. These reforms often modified horizontal or vertical **equalisation mechanisms** in a context of increasing territorial inequalities (Box 14).

Box 14. **Some recent reforms of grants and equalisation systems**

Belgium (Flanders): Flemish municipalities will gain financial autonomy as earmarked subsidies will be integrated into the general Municipal Fund, which will serve as a basis for the equalisation system.

Finland: since the major 1993-95 reform of the transfer system converting matching grants into formula-based grants, grant formulae have been modified several times. The latest reform was introduced in 2014, with the aim of simplifying formulae and making the system more transparent (Moisio, 2015). An important renewal of the grant system is under preparation. A new Act on regional financing is also being developed to plan for the creation of self-governing regions in 2019, and this is also closely linked to the reform of health and social protection financing. The central government should have primary responsibility for financing the regions.

France: the main general purpose grant (Dotation Globale de Fonctionnement - DGF) for municipalities and inter-municipal co-operation bodies is being reformed. Although initially planned for 2016, it has been postponed as many local governments asked to make some adjustments. This reform takes place in a context of strong pressures on local finance resulting from large cuts in central transfers to SNGs (11 EUR billion over 2015-2017). It aims at reaching a greater level of simplicity, transparency and equity, and adapting the DGF to the current territorial reform. The DGF is complex, comprising a great number of components. Distribution criteria are often considered as particularly opaque. This reform may improve the redistribution of funds between SNGs. Its redistributive function could also be improved given sizeable “unjustified" disparities between municipalities in per capita DGF. Finally, the reform aims at encouraging the pooling of services. Other equalisation mechanisms may also be revisited to enhance the coherence of the system and increase horizontal equalisation. In 2015, vertical equalisation tools represented almost 80% of the funds devoted to equalisation.

Hungary: a stricter grant system was introduced in 2013. It involves a shift from an income-based system towards a task-based system (earmarked funds); tightened distribution rules; and the introduction of new equalisation criteria based on tax capacity.

Netherlands: a new fund for social affairs was created to accompany the decentralisation of social responsibilities to municipalities. The transfer indexation system will be re-evaluated to take into account these new tasks.

Poland: The equalisation framework, dubbed the “Robin Hood tax” system, redistributing tax revenues among local governments to support lower-income governments, should be reformed.

Portugal: the 2014 local government finance law changed the methodology for the calculation of central government’s transfers to local authorities.

Sweden: in 2008, a new audit of the equalisation system was entrusted to a parliamentary committee. Its aim was

Box 14. **Some recent reforms of grants and equalisation systems** *(continued)*

to identify growth-deterring factors linked to the equalisation system. This audit led to the adoption of several measures in 2012 and 2014 but ultimately benefited high-revenue SNGs. Since 2015, new measures are on-going to correct this situation.

Estonia: the local government reform initiated in 2014 includes a revision of the local financing system. Based on an evaluation of the funding and implementation of spending responsibilities as well as on a measurement exercise of the local governments' real costs of providing public services. (OECD 2015l), the reform would foresee more leeway for municipalities in designing their own tax revenues and a reform of the equalisation system.

United Kingdom (England): recent measures have granted local authorities greater freedom and flexibility and more control over budgets. The number of earmarked grants decreased from more than 90 to less than 10. A new single general-purpose formula-based grant ("Local Services Support Grant"), regrouping all previous earmarked grants, was introduced in 2013. Only school funding and the new public health grant remain earmarked.

Source: Authors' own elaboration.

Many OECD member countries recently **tightened their fiscal rules at all levels of government.** Fiscal rules include **budget balance rules** (deficit thresholds, balance or surplus targets on an annual/ multi-annual basis), **spending constraints** (expenditure ceilings, growth standards for current expenses and/or investment), and **borrowing constraints** (golden rule, limits on outstanding debt or servicing, need of prior approval). Borrowing constraints can also include new prudential rules prohibiting or restricting the use of certain financial instruments and speculative transactions (derivatives, debt refinancing) – this is the case in, for instance, France, Italy, Spain, the Netherlands or Austria (OECD, 2015f). In the Netherlands, local governments also have, since 2013, the obligation to transfer excess liquidity to the Dutch State Treasury Agency. The goal of this measure, apart from reducing funding needs, is a further reduction of market risks and counterparty exposure for local government (OECD 2014b). Fiscal rules can also include mandatory **multi-year fiscal strategies** and the implementation or tightening of **sanction systems** when rules are broken. Finally, in this process of developing SNG responsibility and accountability, several countries also recently established new **"transparency portals",** designed to provide citizens and businesses with comprehensive information on public accounts, financial management practices, and a range of benefits offered by national and subnational governments (e.g. Austria, Estonia, Poland and Portugal).

Several EU federations or quasi-federations reinforced their internal stability pacts and strengthened fiscal rules both for the central government and SNGs: Spain (Organic Law 2/2012 on Budgetary Stability and Financial Sustainability), Austria (Internal Stability Pact, renewed in 2014 until 2019) and Belgium (Internal Stability Pact 2015-18). In Mexico, such reforms are also ongoing, in particular the 2013 fiscal reform, part of the "*Pacto Por Mexico*" package of structural reforms. It aims to strengthen the fiscal responsibility framework and overhaul rules for state and municipal debts.

The recent crisis has also triggered **reforms tightening subnational fiscal rules in a number of unitary countries. These countries** have adopted white papers, regulations and new laws on the sustainability of public finance, thereby implementing or reinforcing fiscal rules: the Netherlands in 2013 (Sustainable Public Finances Bill), Norway (2012

White Paper*)*, Hungary (debt brake rule anchored in the 2012 Constitution for all levels of government), Poland (2013 amendment of the 2009 Act on Public finance), Slovakia (2012 Fiscal Responsibility Law), Slovenia (2013 constitutional amendment), Portugal (2013 Regional Finance Law and Local Finance Law), Denmark (introduction by the 2012 Budget Law of legally multi-annual binding expenditure ceilings at all levels of government), Estonia (2012 Financial Management of Local Authorities Act and 2014 State Budget Act), Czech Republic (draft "Financial Constitution" regulating local government indebtedness), Iceland (draft Organic Budget law establishing a system of fiscal rules), Hungary (authorisation framework for borrowing, strengthening of the financial supervision of SNGs). Fiscal rules reforms also took place in the 5 countries analysed in the case studies (Box 15).

Box 15. **Recent reforms in Italy, France, Japan, New Zealand and Japan concerning SNG fiscal rules**

Italy: A reform enshrining the budget stability rule in the Italian constitution passed in May 2012, reforming the 1998 Stability Pact. This "golden rule" aimed at guaranteeing Italy's compliance with fiscal equilibrium at all levels of governments. Deficits can no longer be financed through debt. This reform reinforced the role of the State in the co-ordination of public finances, subjecting regional and local government budgets to central control. New reforms are on-going concerning a new local budgetary framework (including harmonisation of the accounting standards of SNGs), borrowing rules and multi-level financial governance.

France: after several years of discussion, SNGs are now involved in the definition of an objective target to control annual public spending in the context of the new governance rules. The public finances planning law 2014-2019 (PSSA) included SNGs in annual public spending objectives. In particular, it introduced an annual spending growth standard for local governments (ODEDEL, expressed in annual percentages) and improved budgetary decision-making.

Finland: the 2015 amendment of the Municipal Act reinforced the macro-steering of the local finance system, ensuring in particular the matching between revenue and expenses. An objective was set for local governments' deficits and a spending limit was imposed on central government measures affecting local finances. This reform should be supplemented by an amendment to the Local Government Finance Act tightening fiscal rules for individual municipalities and joint municipal authorities. Local governments will need to offset any deficit within a period of four years, with no leeway to postpone this offsetting.

New Zealand: new financial prudence requirements were introduced by the Local Government (Financial Reporting and Prudence) Regulations 2011 and 2014. These regulations aim at promoting prudent financial management by local governments.

Japan: the 2010 Fiscal Management Strategy introduced a number of medium and long-term fiscal targets for the central and local governments. It also established a number of basic principles for fiscal management, such as a pay-as-you-go rule (requiring the government to secure permanent revenue sources for new spending programmes, including ageing-related outlays), tax reductions, and better co-operation between central and local governments. Besides fiscal consolidation, this reform aims at avoiding a shift of financial burdens to local governments (OECD 2013f, OECD 2015f).

Source: Authors' own elaboration.

Some reforms also aimed at improving **the access to external financing, in particular to financial markets.** Pooling mechanisms have emerged recently under the aegis of associations of local governments (France, England and New Zealand) inspired by successful municipal agencies models in Sweden, Finland, Denmark and Norway. Several initiatives have been authorised through regulation. In New Zealand, the Local Government Funding Agency (LGFA) was created in December 2011 under the initiative of local and central governments. It is a debt vehicle regrouping 47 member councils,

raising bonds on financial markets in order to lend to local governments at competitive interest rates. One of the aims of this agency was to ensure continuity in the funding of infrastructure projects. More generally, the agency's objectives were to increase the certainty of funding for local governments, to reach more favourable funding conditions, and to secure longer term funding. In France, *Agence France Locale*, the French LGFA, was created in December 2013. *Agence France Locale* is 100% owned by French local authorities. Its mandate is to raise cost-efficient resources in capital markets by pooling together the funding needs of all member local authorities. It aims to provide French local authorities with alternative funding sources (its target market share is 25%).

4. Reforms reinforcing multi-level dialogue and co-ordination

Most OECD countries have developed both **formal and informal co-operation and co-ordination mechanisms between central/federal and subnational governments.** These instruments include dedicated structures to promote dialogue and co-ordination across levels of government, and are often part of multi-level governance reforms. Such structures allow countries to share experiences; understand the needs and problems at different levels of government; submit proposals and comments; negotiate with the central level; and obtain help in the design, implementation and monitoring of reforms. OECD experiences show that countries with well-developed co-ordination arrangements, such as inter-governmental committees and regular formal meetings, have a comparative advantage for the introduction and implementation of future reforms (OECD2013a).

This type of co-operation mechanism is well-developed in federal countries and in some regionalised states, where vertical co-ordination often takes place in the Senate, but also in dedicated permanent policy exchanges forums or “conferences”: Conference of Minister-Presidents in Germany, Conferences of Cantonal Directors and governments or the Tripartite Agglomeration Conference in Switzerland, Council of Australian Governments (COAG) in Australia. The latter includes the Prime Minister and the Heads of state governments, as well as the President of the Australian Local Government Association. It is a forum aimed at facilitating decision making and prioritisation of investments. In Spain, vertical co-ordination between the central government and regions takes place via the Conference of Presidents created in 2004. This conference is chaired by the Prime Minister and regroups the presidents of the 17 regional governments and 2 autonomous cities. Sectoral conferences are also held and the National Commission for Local Administration is another platform for dialogue. In Italy, there are three levels of “conferences” between the central and subnational governments, serving as fora for intergovernmental co-ordination: the Conference of State-regions (created in 1988), the Conference of State-Municipalities and other Local Authorities (since 1996) and the Unified Conference of State-Regions-Municipalities and Local Authorities (since 1997 and includes all the members of the two other conferences). This type of co-ordination mechanism is also **widespread in Nordic countries** where co-ordination is ensured through regular formal meetings held between representatives from central and local government, in particular in associations of local governments (Norway, Finland, Sweden, etc.). SNG associations are consulted on any legislative changes impacting subnational government and participate in the dialogue and negotiations with the central government.

Besides these permanent foras or conferences, **ad hoc commissions can be established for a given period,** accompanying the design and the implementation of a national strategy or of a specific reform (decentralisation, municipal mergers, regional

reform, etc.). These temporary commissions can be more or less independent, depending on their composition, administrative dependence and operational means (staff, budget, communication). They may have more legitimacy and impact if they are directly connected to a high level of government (presidency, Prime Minister, parliament). These foras may involve experts and different stakeholders from the civil society and public and private sectors. It is a well-developed method in Nordic countries, as well as in Japan and New Zealand (Box 16).

Box 16. **Ad hoc commissions and committees facilitating the dialogue with stakeholders**

Denmark: the Commission on Administrative Structure, appointed by the Government in 2002 to perform a critical review of the Danish governance system, played a major role in reform processes. The Commission was established to provide a technical analysis of decision making regarding changes in public sector tasks. Its tasks were to assess the "advantages and disadvantages of alternative models for the organisation of the public sector”. The Commission accomplished its work in 2003 and released recommendations in January 2004, proposing six different administrative models (OECD 2009).

Norway: a committee of experts was recently appointed to analyse the new regional map (around 10 new regions will be created) and a possible reshuffle of tasks across the different levels of government.

Sweden: in the context of the new local and regional government reform, a commission is due to be appointed to propose mergers at the county level and investigate a possible harmonisation of local responsibilities. The commission should present its final results by August 2017. This reform intends to create around 7/8 regions. Sweden also set up a Forum for Sustainable Regional Growth and Attractiveness 2015–2020 to ensure well-developed dialogue and collaboration between the national and regional levels for the implementation of its National Strategy for Sustainable Regional Growth and Attractiveness.

Finland: working groups in charge of drafting the recent reform measures included members from the two coalition government parties and opposition parties as well as members from the Finnish Association of Local and Regional Governments. This led to a large political support base in favour of the reform despite a change in government during the reform process itself.

New Zealand: the independent commission in charge of the reform (Local Government Commission) was built with the aim of reaching across party boundaries (the chair of the Commission, Sir Brian Elwood, was a previous National party candidate, while the minister in charge was from the Labour Party). Established by legislation, the Local Government Commission still exists. It has three members (appointed by the Minister of Local Government) and a small team of support staff. Its main role is to make decisions on the structure of local authorities and their electoral representation. The commission is a permanent Commission of Inquiry for local government reform.

Japan: committees have been in charge of drafting the successive decentralisation reforms. Although these committees were not independent from central government (in contrast to New Zealand), committee members were typically from the private sector, local government, academia, etc., and not politicians which helped to build legitimacy. A bill creating a dialogue forum between the central government and local associations was also adopted in 2011.

Source: Authors' own elaboration.

Since the crisis, many countries have created **similar committees.** In Portugal, for example, the government established a new permanent Council for Territorial Dialogue in March 2015, chaired by the Prime Minister. The Council aims at favouring and institutionalising a continuous dialogue between the central government and subnational governments. This permanent platform regroups various central government entities and

territorial levels and should serve as a tool to promote better co-ordination of public policies and a deepening of territorial cohesion.

Co-ordination efforts were particularly intensified in the fiscal sector, **to improve the governance of public investment** and of **public finances.** On average, in the OECD, almost 60% of public investment is carried out by subnational governments. In nearly all OECD countries public investment is a shared policy competence, making its governance particularly complex, especially in a context of deteriorating public finances. Managing the relations between different levels of government is hence crucial to strengthen the efficiency and effectiveness of public investment (Allain-Dupré, 2011). Effective co-ordination among levels of government helps to identify investment opportunities and bottlenecks, to manage joint policy competencies, to minimize the potential for investments to work at cross-purposes, to ensure adequate resources and sufficient capacity to undertake investment, to resolve conflict, and to create trust. OECD member countries have acknowledged the importance of better governance for public investment by adopting the Recommendation of Effective Public Investment Across Levels of Government in March 2014 (OECD 2014a). The Recommendation regroups 12 Principles into three pillars, including one dedicated to co-ordination across government and policy areas (OECD 2015h). The implementation toolkit provides basic guidance to help policy-makers at all levels of government implement this principle in practice, providing concrete examples and good practices from countries, such as **contractual arrangements** between the central government and SNGs – for example State-Region Planning Contracts in France (*Contrats de Plan Etat-Region* or CPER), that serve as a key planning, governance and co-ordination instrument in regional development policy.

Particular efforts have been made since the crisis to reinforce inter-governmental fiscal co-ordination in macro-economic management. Multi-level fiscal frameworks were introduced through co-operation agreements, internal stability pacts and “fiscal councils”, to promote sustainable public finances and intensify fiscal discipline across levels of government through co-operation agreements, internal stability pacts and “fiscal councils”. Fiscal councils may have a monitoring, assessment or advisory role. Many have been reinforced or established recently in federal countries (OECD 2015f): the High Council of Finance in Belgium (and its now official intergovernmental “Consultative Committee”), the Fiscal Advisory Council in Austria (created in 2013), the Fiscal and Financial Policy Council in Spain*,* the German Stability Council in Germany (and its new Independent Advisory Board created in 2013). Several unitary countries also reinforced or introduced new councils to co-ordinate fiscal policies, in line with the OECD Recommendation of the Council on Budgetary Governance (OECD 2015i): the Public Finance Council in Portugal (established in 2011) and the Parliamentary Budget Office in Italy (set up in 2012) are two examples.

However, **setting up a multi-level dialogue platform on a permanent basis is not an easy task and may face some resistance**. In France for example, many attempts have failed. SNGs are currently represented by a multiplicity of associations, each defending the particular – and sometimes diverging - interests of their members (rural municipalities, small cities, mid-sized cities, large cities, urban communities, mountainous municipalities, departments, regions, inter-municipal communities, etc.). This may be an obstacle in reaching a consensus and developing reform processes. The creation of a dedicated co-ordination body has been discussed for many years. In its initial version, the Bill to Modernise Public Territorial Action and the Affirmation of the Metropolis provided for the establishment of a High Council of the Territories (*Haut conseil des territoires*) chaired by the Prime Minister. The council would have been

consulted on any draft law concerning subnational governance. It would have grouped together several existing and dispersed bodies, such as the Local Finance Committee and the National Council on Norm Assessment. It would have established an Observatory of local public management, responsible for collecting and disseminating data and good practices; sharing its expertise; and implementing audits. This body was finally removed from the draft law in December 2013 by the Senate, which was hostile to its creation as providing this type of dialogue platform is one of its own functions.

NOTES

1. The term of “federated states” is used here as a generic term to refer to the constituent regions of a federation. They have specific names depending on the federation: states and territories in Australia, states or provinces in Austria (Bundesländer), regions and communities in Belgium (régions and communautés), provinces and territories in Canada, states in Germany (Länder), cantons in Switzerland, states in Mexico (estado), autonomous communities in Spain (Comunidades Autónomas) and states in the United states.
2. “Multi-level governance” approaches can be also more comprehensive and includes also interaction between public entities and private stakeholders (profit or non-profit ones), in particular citizens and businesses. See Ostrom et al. (2010).
3. However, the importance of subnational government expenditures is sometimes overestimated, in particular in countries where SNGs have numerous spending obligations on behalf of the central government. In some cases, SNG expenditures are delegated from the central government, and SNGs act simply as a “paying agent” with little or no decision-making power and room for manoeuvre. SNGs can also be constrained by regulations, norms and standards, or budget balance targets.

4. It is important to note however that an increase – or a decrease – in SNG expenditure does not always reflect only decentralisation – or recentralisation – of new responsibilities. There are many other factors which can increase SNG spending, such as greater social needs (particularly since the crisis began), an ageing population, increasing quality standards and costs of related services. Conversely, a decrease in SNG spending can be explained more by the effects of fiscal consolidation measures (spending cuts, saving programmes) or public management reforms aimed at seeking effectiveness and cost-efficiency (pooling of services and shared services agreements, performance assessments, public staff reforms, assets management, etc.) than a recentralisation process per se.

5 A referendum on Scottish independence took place in Scotland on 18 September 2014. It ended with a rejection (the "No" side won, with 55.3%; turnout 84.6%).

Chapter 2

Overview of territorial reforms

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

The structure of subnational governments (SNGs) is constantly evolving due to territorial reforms modifying administrative boundaries. These reforms can consist of:

- **Creating new territorial entities**, either from scratch or based on pre-existing non-autonomous administrative structures (administrative regions or statistical regions). In this case, territorial reforms are associated with institutional reforms, as newly created regions or intermediate governments receive responsibilities and resources.

- **Rescaling of existing administrative boundaries to reduce territorial fragmentation**, whether at the municipal or regional level. Rescaling can take two main forms: **territorial restructuring through mergers (up-scaling)** but also de-mergers[1] (down-scaling); **co-operation between municipalities or regions**, i.e. pooling public services into larger inter-municipal entities **(so called "trans-scaling")**.[2] Up-scaling and trans-scaling are not mutually exclusive. Some countries can promote both options simultaneously (e.g. Finland, France). In addition, trans-scaling can be a first step towards up-scaling. In some cases, rescaling can be associated with institutional reforms.

All levels of SNGs are concerned: municipal (including metropolitan functional areas), regional, and intermediary levels for those countries that have three layers of SNGs.

1. General considerations on territorial reforms

1.1. Why does territorial reform happen?

There are **various rationales** behind consolidation reforms. **Four major drivers can be identified.** They are not mutually exclusive and territorial reforms generally combine several of these factors:

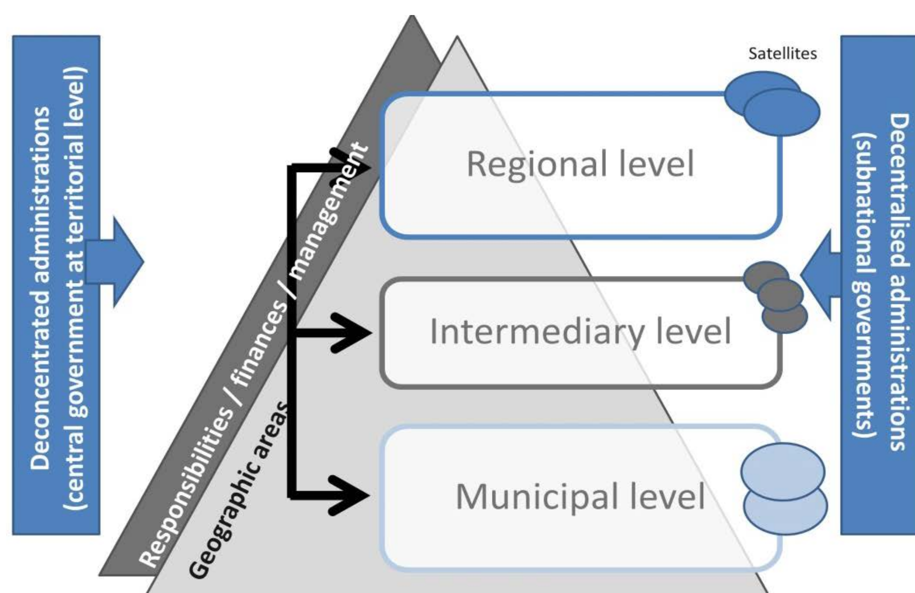
- **Political change:** changes in the multi-level governance system (decentralisation or recentralisation processes) which have a direct or indirect impact on territorial boundaries.
- **Demographic change:** migration, rural exodus and population growth in urban areas, as well as population ageing.
- **Socio-economic change**, especially regarding growth in services, transport and ICT uses. Economic and social development scales have changed. Basic modern territorial structures rely on functional areas that are largely determined by commuting and socio-economic flows. Regional, intermediary or municipal historic administrative boundaries are often obsolete. The mismatch between real functional areas and these traditional administrative boundaries may hamper growth by fragmenting the scale of local public policies – unless efficient co-ordination mechanisms are in place. This is particularly true in metropolitan areas (OECD 2015j). It is thus necessary to adapt public services to these new features as well as to citizens' needs.
- **Local management and finance:** the need for fiscal consolidation often translates into territorial consolidation especially since the crisis. The decrease in SNG revenues requires SNGs to reduce and rationalise their spending and/or pool resources and equipment. Up-scaling or trans-scaling intend to reduce duplications/overlapping, sterile and disruptive competition and incentives. They may allow economies of scale and of scope by lowering unit production costs of public services, increasing negotiating

capacities with providers, and suppressing redundant functions. They can also improve the quality of local management and public services, by providing a wider range of services and public goods in a more professional manner, with upgraded subnational human and technical capacities. They can develop the financial strength and sustainability of local governments, allowing them to manage and invest more efficiently. Finally, larger communities can also facilitate partnerships with other public and private actors and increase visibility and attractiveness, in particular for regions increasingly engaged in international and European competition to attract investors.

1.2. The complexity of territorial reforms

Territorial reforms do not simply consist of a change in geographic areas and boundaries. **They should be approached in a multi-dimensional and comprehensive way** in order to avoid negative and counterproductive outcomes (figure 5). Firstly, territorial reforms often concern not only subnational government levels but also **central government entities** operating at the territorial level (when such deconcentrated administrations exist). Reforms therefore need to optimise the presence and missions of the central government within territories. When the central government has no territorial bodies, a major challenge is to enhance the vertical co-ordination between SNGs and the central government and to ensure consistency. It is thus necessary to develop parallel and co-ordinated efforts to reform both central and subnational governments. In France, for example, the 2015 regional reform is a one of both self-governing regions and regional state prefectures (see below). Secondly, a territorial reform targeted at one specific subnational level (e.g. municipal) often has **an indirect impact on other levels (e.g. regional or intermediary)**, hence the importance of taking a systemic approach to territorial reforms. Thirdly, any territorial reform also has an **impact on satellite and subordinate functional bodies** that are attached to SNGs, such as inter-municipal or inter-regional co-operation structures, local associations, local public companies, regional agencies, sub-municipal entities (parishes, local boards, etc.), etc. Finally, **territorial reforms are often accompanied by institutional and public management reforms,** i.e. a reorganisation of responsibilities and human, technical and financial resources across the different levels of government (decentralisation or recentralisation). Local governments recently involved in territorial reforms have often needed to re-organise once the reform has been implemented. While this is obvious in the case of the creation of new sub-national entities, changes to existing SNGs may have great impact on their structures. For example, in the case of mergers or inter-municipal co-operation, reorganisation is needed to avoid a duplication of services and staff, which may then result in workforce reductions.

Figure 5. **A systemic approach to territorial reforms is essential**



Source: Authors' own elaboration.

2. Municipal reforms

The main rationale for territorial reform at the municipal level is the problem of **local fragmentation**, which sometimes makes provision of local services inefficient and raises issues of equity in access to services, including varying quality. Some OECD countries are characterised by a particularly high municipal fragmentation. This means that not only municipal average and median sizes are quite low but also that such countries may have a high proportion of very small municipalities, either in terms of population, geographic area, or both (Table 4). The most fragmented countries are Austria, the Czech Republic, France, Hungary, Iceland, the Slovak Republic and Switzerland. In contrast, some countries have very large municipalities, such as Ireland, Korea, Japan, New Zealand or the United Kingdom. It is important to note that most of these countries with large municipalities also have a structured sub-municipal level which allows them to maintain a certain level of proximity and local democracy despite large municipal governments.

Table 4. **Number and size of municipalities in the OECD, 2015-16**

2015-16	Number of municipal level entities	Average municipal size (number of inhabitants)	Median municipal size (number of inhabitants)	Average municipal area (km²)	% of municipalities with less than 2 000 inhabitants
Federal countries					
Mexico	2 457	45 740	12 730	797	13%
Australia	571	41 005	12 605	12 369	19%
Belgium	589	19 030	12 045	51	1%
United States	35 879	8 990	n.a.	249	69%
Canada	3 805	8 205	950	695	68%

Table 4. **Number and size of municipalities in the OECD, 2015-16** *(continued)*

2015-16	Number of municipal level entities	Average municipal size (number of inhabitants)	Median municipal size (number of inhabitants)	Average municipal area (km2)	% of municipalities with less than 2 000 inhabitants
Germany	11 092	7 320	1 710	32	54%
Spain	8 119	5 605	565	62	72%
Austria	2 100	4 090	1 790	39	55%
Switzerland	2 294	3 590	1 370	17	61%
Unitary countries					
Korea	228	224 440	146 520	436	0%
United Kingdom	389	166 060	132 240	623	0%
Ireland	31	149 530	122 900	2 206	0%
Japan	1 741	72 715	31 300	215	4%
New Zealand	67	68 590	32 400	3 954	1%
Denmark	98	58 155	42 850	438	1%
Turkey	1 397	53 940	8 595	550	7%
Chile	345	51 650	18 205	2 146	5%
Netherlands	390	43 540	26 515	86	1%
Sweden	290	33 890	15 435	1 405	0%
Greece	325	33 410	n.a.	403	n.a.
Portugal	308	33 400	14 380	299	2%
Israel	255	33 190	n.a.	85	3%
Finland	313	17 530	6 060	971	14%
Poland	2 478	15 530	7 540	126	1%
Norway	428	12 185	4 715	711	22%
Unitary countries					
Slovenia	212	9 730	4 730	95	12%
Italy	8 047	7 545	2 430	37	44%
Estonia	213	6 165	1 710	204	54%
Luxembourg	105	5 360	2 520	25	37%
Iceland	74	4 445	880	1 355	72%
Hungary	3 178	3 125	815	29	76%
France	35 885	1 855	435	16	86%
Slovak Republic	2 927	1 850	655	17	85%
Czech Republic	6 258	1 640	420	12	89%
OECD 34	**132 888**	**9 570**	**n.a.**	**251**	**31%**

Notes: Countries are sorted by column 2. Australia: the municipal level comprises "local government areas" which include a wide diversity of entities depending on each of the six states and two territories. Unincorporated areas are not included. - Austria: the municipal level comprises statutory cities, towns, markets and villages. - Canada: the municipal level corresponds to census subdivisions. Indian reserves, Indian settlements and unorganised territories (1 233 entities in 2015) as well as special purpose entities such as schools boards are excluded - United States: the municipal level comprises only general purpose entities (i.e. municipalities, towns and townships) as of 2012 census. Special purpose entities (i.e. special districts and schools districts) are excluded from the counts reported in the table (there were 51 146 such entities in 2012). Calculations do not comprise Native American reservation areas. - Czech Republic: the municipal level includes municipalities, towns and statutory cities. - Estonia: the municipal level includes rural municipalities and cities, all with the same legal status. - France: the total number of municipalities includes Corsica and overseas regions (Martinique, Guadeloupe, Guyane, La Réunion and Mayotte). However, Guyane is not included in the average and median calculations. - Greece: since the 2010-2011 Kallikratis reform, municipalities

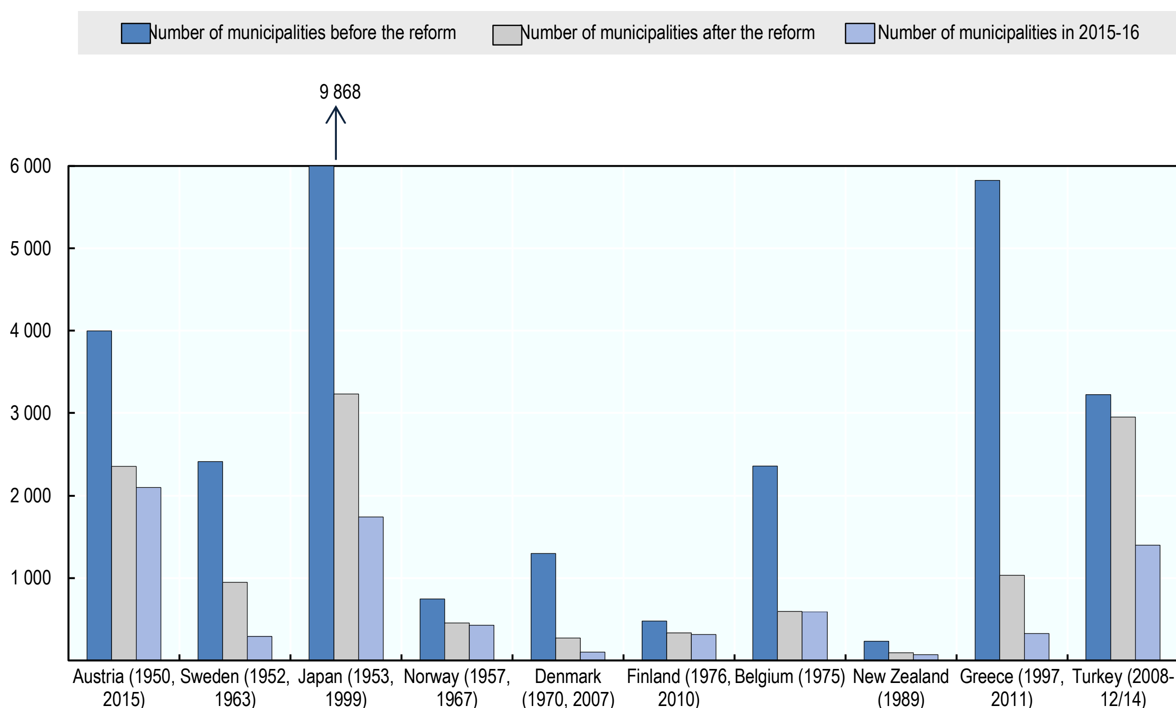
are divided into sub-municipal localities (local and municipal communities). - Hungary: “settlements” include the capital city of Budapest and its 23 districts, towns of county rank, towns and villages. The number of counties excludes Budapest. - Ireland: the new municipal level set up with the 2014 Local Government Act includes 31 county and city councils. The 2014 reform also created a nationally representative system of sub-county governance, the Municipal Districts. - Israel: the municipal level comprises municipalities, local councils and regional councils. The latter are responsible for governing a number of settlements spread across rural areas (mainly *kibbutzim* and *moshavim*). - Japan: the municipal level comprises Cabinet-Order Designated Cities, cities, towns, villages and special wards. - Korea: the municipal level comprises cities, counties (mostly rural) and autonomous districts. It is further subdivided in around 3 500 sub-municipal localities. - New Zealand: the municipal level includes city councils, district councils and Auckland Council, all referred to as “territorial authorities”. There is also a structured sub-municipal level (community boards). - Portugal: municipalities are subdivided into sub-municipal localities (*freguesias*). - Slovak Republic: the municipal level includes cities, rural municipalities, city districts in Bratislava and Košice as well as three military districts. - Slovenia: among the municipalities, there are 11 urban municipalities which have a special status. There is also a structured sub-municipal level (around 6 000 settlements). - Turkey: the municipal level comprises metropolitan municipalities, provincial capital, district municipalities and town municipalities. Turkey also contains 18 362 villages (*köy*) as of December 2014 in some areas (not dependent on a municipality). Average and median municipal sizes exclude metropolitan municipalities in order to avoid double-counting. - United Kingdom: the municipal level consists of 324 local authorities in England, 22 in Wales, 32 in Scotland and, since 1 April 2015, 11 local councils in Northern Ireland (formerly 26).

Source: OECD (2016d) *Subnational governments in the OECD countries: key data* (Brochure) and Subnational government structure and finance database: http://dx.doi.org/10.1787/05fb4b56-en.

2.1. Municipal mergers

Municipal mergers have been planned, launched or completed in most OECD countries over the last 15 years (Figure 6). In some countries, there have been successive waves of reform. In others, there has been an ongoing process over a long period, such as in the Netherlands or Switzerland. **The recent global crisis acted as a catalyst to reactivate or introduce municipal amalgamation policies,** such as in Estonia (2015-18), Ireland (2014), Luxembourg (2015-17), Norway (2014-17), Turkey (2012-2014), France (2015 Law on “new municipalities”), and Italy (Law 56/2014). Some federal countries also introduced mergers under the leadership of federated states (e.g. New South Wales and South Australia in Australia, Styria in Austria, Flanders in Belgium, Manitoba or New Brunswick in Canada.

Figure 6. **Municipal merger reforms reduce the number of local governments: Country examples in the OECD**



Notes: Japan; 9 868 municipalities in 1953.

Source: Authors' own elaboration from Dexia-CEMR (2012), OECD research work.

2.1.1 Rationale behind municipal amalgamations

Reasons for mergers are numerous, including:

- **to adapt to demographic change** (ageing, migration, shrinking or expanding), which can lead to specific problems. In regions with demographic decline, it is difficult to sustain the provision of public services, in a context of increasing charges (spiralling cost provisions), while revenues become more constrained (less tax payers). In dense urban regions, administrative fragmentation increases transaction costs and policy spillovers;
- **to reduce the mismatch between obsolete municipal administrative boundaries and socio-economic functional areas** (labour and economic markets, new mobility patterns, etc.). This allows for a more co-ordinated and effective municipal infrastructure and delivery of services. The development of ICT and e-government applications at the municipal level is a further argument supporting the need to change and adapt to new scales;
- **to implement economies of scale and scope**, generate **cost savings and internalise spillovers** in the provision of local public services. Up-scaling increases the size of facilities, helps to reduce the costs and to share costs more equitably. Up-scaling can also reduce administrative overheads and risks of duplication of expenses;

- **to increase municipal administrative capacities**, in particular financial and human resources, and therefore increase the ability of municipalities to provide public services in a sustainable way. This can address the issue of financial weaknesses in some smaller municipalities, in particular during times of crisis. It also allows provision of services in a more equitable manner (not all municipalities are able to provide the same level of municipal services due to their limited capacities; in addition, larger municipalities can result in less income disparities). Improving financial sustainably has become a major motivation for amalgamating municipalities in many countries;
- to improve **the quality and quantity of municipal infrastructure and services;**
- and more generally, **to improve the governance, professionalism and efficiency of municipal management.**

Several of these arguments in favour of upscaling, however, raise many questions (Box 17).

Box 17. **Asserting the benefits of mergers: A difficult question**

One of the main lessons from international experience is that **the expected benefits of mergers do not always materialise or are overshadowed by shortcomings.** Studies exploring the effects of municipal mergers on **economies of scale and savings** are rather inconclusive and do not show clear-cut positive results. Many factors have an impact on the efficiency gains of scaling up:

- whether the reform takes place in **rural vs. urban areas**, or whether it concerns the merger of very homogenous vs. **heterogeneous municipalities** (in terms of services, wages, financial strengths, level of debt, large and small municipalities, etc.). Research on economies of scale in Finnish municipalities shows that large municipalities tend to show lower cost efficiency than smaller ones in service delivery (such as basic welfare or education). The optimal size of municipalities in terms of cost efficiency was found to be between 20 000 and 40 000 inhabitants (Moisio, Loikkanen, and Oulasvirta 2010). According to McKinley (1998), the 1989 reform in New Zealand successfully enhanced the capacity and operational efficiency of large local governments but negatively affected smaller councils (with less than 20 000 residents).
- whether it concerns **capital-intensive** services requiring infrastructural investment and maintenance (such as water management or public transport) **vs labour-intensive services** (such as policing, social services, education or healthcare). A study by TBD Advisory (2013) tried to identify economies of scale in local councils in New Zealand by considering 70 local authorities and 16 distinct functions over 5 years. In line with international studies, the authors failed to identify a clear relationship between efficiency and the size of local governments. However, they found evidence for economies of scale for 5 specific functions out of 16 (mostly large-scale capital investments) and, by contrast, diseconomies of scale for labour-intensive functions.

Moreover, such policies often aim at **improving the quality of services** (without trying to generate savings). In the case of joint institutional reforms (decentralisation), there may also be a **transfer of additional responsibilities** requiring more spending (not less) after the merger.

In addition, reaching savings may require **several years after the actual reform**. Such reforms may induce **transition costs** and may prevent costs from rising only in the long run. A rise in expenditure, at least in the medium term, was observed in several countries due to the high costs of integrating operations in areas such as information systems or infrastructure development. In Japan, for example, there is some anecdotal evidence for some of the mergers, of great increases in costs (in particular relative to wages) compared to pre-merger situations (C. Schmidt, 2009). This is in line with Suganuma (2006), who finds that these amalgamations have resulted in oversized assemblies and wage inflation. In Denmark and Finland, free-riding behaviour by municipalities prior to municipal mergers has also been observed, the merger process creating a temporary

Box 17. **Asserting the benefits of mergers: A difficult question** *(continued)*

common pool problem which arises because of a delay between the initial merger decision and the actual merger (Blom-Hansen, J. 2010).

Finally, amalgamations can also result in **diseconomies of scale**. Some empirical studies have revealed the existence of diseconomies of scale for small municipalities and congestion costs for the largest ones with high population density. Municipalities with less than 20 000 to 25 000 and with more than 250 000 inhabitants appear less efficient than those within that range (McKinlay Douglas Limited, 2006; Holzer et al., 2009). In the case of Japan, Hayashi (2002) found that the unit costs of local public services follow a U-shaped curve: they are high for the smallest municipalities, tend to decrease until around 120 000 inhabitants, and increase as municipalities grow beyond this threshold. Similar results were obtained by Yoshida (2003), who shows that per capita expenditure is the lowest for municipalities with around 125 000 inhabitants (OECD 2005c). In Finland, the OECD found that costs appear to be lowest in the 20 000 to 40 000 inhabitants range (OECD 2014d). A review of the literature by Byrnes and Dollery in 2002 reveals mixed results: only 8% of the reported studies found economies of scale while 24% indicate diseconomies of scale, and 29% found evidence of both economies and diseconomies of scale.

In addition, besides these economic efficiency considerations, another concern is that **municipal mergers are not always democratically effective and** may hinder **accountability and democracy.** People's voices, through public meetings, hearings, elections, and direct contacts with officials, may be less heard at the local level (OECD 2014b). Another recurrent problem is that mergers are often seen as a threat to **local identity and historical legacies**, which is a great concern in Japan or in France.

Source: Authors' own elaboration.

2.1.2. Top-down or bottom-up approaches for mergers

Merger reforms may involve top-down decisions or bottom-up choices, either all at once or progressively. Mandatory approaches have been chosen in Japan (during the "Great Shōwa", 1953-1999), New Zealand (1989), Denmark (2007), Greece (2011) and Turkey (2008 and 2012). Forced amalgamations have been carried out either through strict pre-determined plans and targets or with more flexible objectives. Targets have been used - and reached - in Japan and New Zealand (Box 18). In contrast, the compulsory approach in Denmark was characterised by some level of flexibility. Local authorities were free to choose the neighbouring municipalities with which to merge. The central government gave the municipalities six months to prepare their merger plans, with the implicit threat of intervening and imposing mergers from above in cases of non-compliance. Described as a "controlled voluntary process", which was ultimately a surprisingly smooth process, the plans were prepared and accepted by the central government in a cross-party political agreement in parliament, in March 2005. There were only a couple of cases of opposition to mergers which were nonetheless resolved within a few months, and the amalgamation plan was finally agreed upon in the summer of 2005. The reform was deemed a success and by January 2007 the new system was implemented with no disruption to public services for citizens (OECD, 2014b).

Box 18. **Mandatory mergers in Japan (Great Showa) and New Zealand**

Japan: several waves of mergers have drastically reduced the number of municipalities, from 9 868 in 1953 to 1 719 today. The first wave, the "Great Shōwa", lasted from 1953 to 1999 and was compulsory. The objective was to reduce the number of municipalities to one third of the original number and to attain a minimum target size of 8 000 inhabitants per municipality. This wave reduced the number of municipalities from 9 868 to 3 232.

New Zealand: Before the consolidation process, the local government sector was characterised by high fragmentation and enormous disparities in size and activities, both at regional and local levels. At local level, there were around 800 long-established structures, including around 200 local authorities with different statuses (counties, municipalities, independent town districts, district communities) and numerous elected "special purpose bodies" (harbour boards, catchment boards and drainage boards, etc.). They were reduced by the 1989 reform to 74 "territorial authorities" (and subsequently to 67), including 12 city councils, 54 district councils and the Auckland Council. The reform also created a sub-municipal level of community boards. The authority over the reform process was delegated to an independent commission, the Local Government Commission. The municipal reform was also a regional reform (creation of 12 "regional councils" – subsequently 11) and a public management reform, focused on improving community governance and efficiency.

Source: Authors' own elaboration.

Municipal amalgamations in Norway, Iceland, Luxembourg, Netherlands, Finland ("PARAS" reform) and Japan ("Great Heisi" consolidation ongoing since 2006) followed a **relatively bottom-up approach**, with voluntary mergers often relying on various incentives. Negotiations of merger plans and consultation by referendum with the local population may lead to merger failure (Box 19).

Box 19. **Referendums may cause the merger process to fail**

Citizen consultation mechanisms such as referendums (binding or not) are often used in the case of territorial reforms, carried out locally (municipal mergers, metropolitan reforms) or regionally, and even nationally. But as they might result in a reform being rejected, referendums are a two-edged tool, often with a definitive effect, from which, in any case, it is very difficult to back away.

At municipal level, several mergers partly failed after a referendum, such as in Norway (2003), Iceland or Luxembourg. In Finland*,* where each municipality was free to have (or not) a referendum, referendums were used as consultation tools only in a small number of municipalities (18). While a majority of referendums were in favour of mergers (10 out of 18), they could generate specific obstacles. In particular, referendum results cannot be ignored. In five municipalities, the voters were against a merger but local authorities decided to merge anyway. In France, referendums have historically been required before municipal amalgamations and their results have often led to the rejection of merger projects. Defiance of politicians towards referendums in this context is so common that this requirement was abolished in the 2015 reform.

Source: Authors' own elaboration.

Mergers based on voluntary approaches may not always achieve their objectives, as in Japan and Finland (Box 20). As a result, the Japanese government decided to continue and reinforce previous measures through the "Basic Policy for Promoting Municipal Mergers". In 2013, the Finnish government decided to adopt a more direct approach, or even coercive in some cases (for municipalities facing financial difficulties). This policy was finally abandoned by the new government, which took office in May 2015, because of strong resistance and the risk of it being unconstitutional. Despite its difficulties, the voluntary approach seems to be a non-negotiable condition for several countries such as France or Norway. In Norway, for example, the parliament is concerned about forcing

municipal changes within the new municipal reform (cf. Proposal on Municipal Economy 2015).

Box 20. **The process of municipal mergers in Japan and Finland**

Japan: the second wave of mergers (this time voluntary) started in 1999. Called the "Great Heisei Consolidation", it was part of the broader Decentralisation Promotion Reform. The main arguments for these mergers were cost-efficiency, the weak fiscal situation of many small towns and villages, and the fact that many rural municipalities were considered below the critical size to provide public goods efficiently. The government used different financial incentives (grants and tax advantages) available until 2006. Moreover, "special amalgamation bonds" were introduced to fund projects related to amalgamations. Residents could also take the initiative to propose mergers. Measures to mitigate the resistance to mergers were also taken, such as the guarantee to maintain the seats of local assembly members, a local tax "freeze" and the use of new organisational structures to enhance local representation (OECD, 2006). By January 2006, the number of municipalities had declined from 3 232 to 1 820, while the initial target was to reduce the overall number of municipalities to 1 000. This is why consolidation continued after the Great Heisei Consolidation, based on the "Basic Policy for Promoting Municipal Mergers", reinforcing previous measures. Prefectures had to present their respective initiatives concerning municipal mergers and organise merger conferences by the end of 2010. Population thresholds were eased. Special provisions were undertaken concerning local taxes and assembly members (number of seats, terms of office) and since 2011, additional measures focusing on the facilitation of voluntary municipal mergers have been taken. The number of municipalities decreased to 1 719 in 2014. The objective is still to reach approximately 1 000 municipalities - no timetable has been established.

Finland: Enacted in 2005 and 2007, the PARAS reform was a multidimensional reform including municipal mergers, inter-municipal co-operation (in particular in the areas of healthcare and education), and better governance in urban regions. The objectives of the reform were to strengthen municipal and service structures, improve productivity, slow down the growth of local government spending and create a sound basis for local service provision. The 2007 Act introduced quantitative population thresholds to be reached for a number of activities (e.g. 20 000 for primary health care, 50 000 for vocational basic education). Municipalities were free to choose whether to merge or not (but had then to enhance inter-municipal co-operation to provide healthcare and education services) and to select their merging partners. Financial incentives were implemented to promote mergers, in particular, grants were offered to merging municipalities. Other incentives were proposed (organisation and consultations tools, including local referendums). As decisions were voluntary, each municipality/urban region implemented (or not) its plans at its own pace. In a majority of cases, mergers were not implemented: 144 mergers plans were initially drawn; of those, 77 did not lead to a merger. Only 67 mergers took place between 2007 and 2013, most mergers involving two municipalities. The number of municipalities declined from 431 in 2006 to 320 in 2013. Beyond these quantitative outcomes, the reform was evaluated by ARTTU Research, showing mixed results. The PARAS reform was rapidly followed rapidly by other plans for municipal amalgamations. Another reform to restructure municipalities was introduced in 2011. A Municipal Structure Act entered into force in July 2013, aiming at encouraging, among other things, voluntary amalgamations over 2013-17 and considering, in some cases, forced amalgamations. It was part of a wider local government reform, following the PARAS reform. Several new criteria were taken into consideration: municipal financial situations; the mobility of workforce; the ability to provide basic services for municipalities of less than 20 000 inhabitants; the belonging to an urban area. Special subsidies were foreseen to help municipalities investigate possible mergers and then to support the merger process. This large-scale merger plan was abandoned in 2015 because of strong resistance and the risk of being unconstitutional. The government, which took office in May 2015, has prepared an alternative reform allowing both a preserving of local autonomy and an achieving of economies of scale. This reform consists of pooling municipal healthcare and social services at the regional level, making the municipal reform become a regional reform. It will result in the creation of self-governing regions (see below), and imply in turn a reduction of municipal duties and obligations in the field of healthcare and social services (the government will still continue, however, to support voluntary mergers).

Source: Authors' own elaboration.

Finally, some countries prefer **a two-step approach to** facilitating the reforms: voluntary mergers as a first step (with incentives), followed by forced amalgamations

(without incentives) for reluctant municipalities. This approach was considered by Finland in the context of the 2013 reform (but was abandoned in 2015) and is currently under consideration in Estonia within the framework of the 2015-18 local government reform.

2.1.3. Is there an ideal municipal size?

Some countries define **a threshold** under which municipalities must or should merge. There are no common or international standards in the OECD concerning an ideal municipal size or minimum threshold in terms of population or geographic area.

Identifying the optimal size of the unit is a particularly difficult task. Without even considering the optimum size from a democratic point of view, the optimum size from an economic point of view depends on **numerous factors**. In fact, several factors may lead to differences in the costs of services: geography (topography, remoteness and accessibility, etc.); demographic characteristics (density, socio-economic structure of population, ageing population); general environment (urban or rural); and economy (economic sectors, municipal financial resources, etc.). **The nature of the responsibilities** carried out by the municipalities may be important as well: both the optimal size and functional areas differ from service to service (e.g. water supply versus education). In light of the above, large municipalities in a given context can appear very small in another. In Luxembourg, the critical mass of a municipality was set to 3 000 inhabitants (and a minimum surface area of 100 km^2). In Estonia, the government recently defined the minimum size of a municipality as 5 000 inhabitants, following the recommendations made in November 2015 by an administrative reform expert committee set up by the Minister of Public Governance. According to the experts, only a local municipality with 5 000 – 6 000 residents would have sufficient capacity and expertise, based on better paid and skilled local specialists, to implement long-term investments (including European support funds). In contrast, in Japan, the optimum size would be around 100 000 inhabitants, a threshold that the Netherlands had also envisaged in the first stage of its coalition agreement in 2012 (but abandoned). In Norway, the ad-hoc expert committee appointed by the government recommended that, given the tasks municipalities have today, the minimum size of a Norwegian municipality should be between 10 000 and 20 000 inhabitants. In Finland, within the framework of the PARAS reform, a municipality (or a group of municipalities) responsible for primary healthcare or associated services, had to regroup at least 20 000 inhabitants. The threshold was established at 50 000 inhabitants for vocational education services. However, the establishment of such quantitative thresholds in Finland was subsequently widely criticised. In urban regions, these thresholds would encourage wealthy “inner-ring” municipalities to co-operate with the central municipalities while maintaining their own services. This criterion may also induce “geographical blindness”. As a result, many argued that a greater importance should be given to structural factors such as distances, accessibility, regionalisation, dispersion trends, etc. This explains why the legislation changed in 2011 - more diverse criteria had to be taken into account (Box 20).

Within any given country, **flexibility regarding thresholds** can be adopted for specific geographical conditions (islands, remote locations, mountainous areas, rural vs metropolitan areas, etc.) or for linguistic and/or cultural particularities (examples of this in Finland, Iceland, Estonia, Greece, etc.). Some additional criteria can also be taken into consideration, such as geomorphological characteristics, links by road or rail, and existing co-operation between municipalities (e.g. Luxembourg).

A major discrepancy factor is whether municipalities supposed to merge are located in an urban region or not. The principle guiding municipal amalgamation should not be based on the average municipal size; it should be weighted according to the rural/urban characteristics of each region. Analysis confirms that urban regions tend to benefit from a reduction in municipal fragmentation, whereas rural regions are not affected or may even benefit from fragmentation. In rural areas, decreasing municipal fragmentation means that local governments manage an even vaster area, increasing the difficulty of reaching citizens and matching their preferences. As a result, reforms of national administrative structures should take into account regional territorial features, advocating for a place-based approach to institutional reform. The reduction of municipal fragmentation may lead to better economic performance only in regions where most of the population lives in urban areas, e.g. regions that contain metropolitan areas (Bartolini, 2015).

2.1.4. What incentives for municipal mergers?

Several countries have used **incentives** to encourage municipal mergers. These may consist of offering special **financial subsidies**. In Norway, such incentives took the form of a 5-year financial support to help municipalities reorganise services and administration, as well as a special aid for smaller municipalities. In Switzerland, funds for consulting, guidance and technical assistance were introduced to prepare the ground for mergers. In France, merging municipalities benefited from reduced cuts in grants than other municipalities.

Incentives for mergers can also consist of a **mix of different types of incentives**. In the Netherlands, a new "Policy Framework for Municipal Redivision" was adopted to give more guidance to municipalities which decided to merge. A greater role was given to provinces to assist municipalities in their merging process. The merger grant was also adjusted and expanded, aiming at compensating newly merging municipalities for the additional costs incurred (known as "friction costs"). In Estonia, in addition to a merger grant, the government plans to fund consultancy and expertise costs to help municipalities to prepare the merger process. The merger grant should double for voluntary mergers until January 2017, and included a bonus if the size of the merged municipality exceeded 11 000 inhabitants. In Italy, Law 56/2014 encourages municipal mergers through state and regional financial incentives. The Stability Law 2015 also introduced additional incentives for municipal amalgamations by excluding merged municipalities from limitations set for hiring personnel. In Japan, during the second wave of voluntary mergers, amalgamations were encouraged through financial incentives as well as organisational measures to enhance local representation. Several countries also facilitated the process by proposing free assistance and financial estimations, and by preparing instructional tools (e.g. sample documents, guidelines for mergers, etc.). In Finland, the PARAS reform encompassed multiple incentives, including financial support, organisational support and consultation tools. An important factor was the guarantee that there would be no lay-offs in merged municipalities during the five years following the merger.

Another strategy employed in order to promote municipal mergers is the introduction of **special status for larger cities.** For instance, in Japan, a third tier of special status cities (core cities) was introduced by the central government. This status aimed to encourage municipal mergers by pushing municipalities to amalgamate in order to gain the new responsibilities associated to it. This status concerned cities of more than 300 000

inhabitants, meeting a few other requirements. There is some evidence that this strategy may have been successful in Japan.

Another incentive encouraging mergers is **to keep the former municipal administration as a sub-municipal structure,** i.e. as local de-concentrated units. This additional institutional layer is often a necessary counterpart to an increase in municipal size, in order to overcome identity and proximity problems and to ensure citizen and local elected representatives' acceptance. These sub-municipal entities have, the majority of the time, a legal status with a deliberative assembly, a delegated executive body (mayor, council) - elected by the population -, an independent budget etc., even if they depend on the municipalities. This type of sub-municipal organisation maintains local accountability despite a comparatively large average municipal size in terms of population. This increases the representativeness of local stakeholders; better addresses local needs and maintains local identity; and protects historical legacies, traditions and democracy. There are several examples of such entities in OECD countries: parish and community councils in the United Kingdom; *Eup* and *Myeon* in Korea; *freguesias* in Portugal; settlements in Slovenia, etc. In New Zealand, the 110 community boards created by the 1989 local government reform still operate in both urban and rural areas to carry out functions and exercise powers delegated to them by their councils. Such approaches have been followed by more recent amalgamations reforms, in particular in Greece, Ireland and France (second "New Municipality" reform – "*commune nouvelle*"). Combined with significant financial incentive, these reforms allowed to reduce the negative effects of consolidation and thereby facilitated the acceptance of municipal mergers (Box 21).

There are also other means of compensating for the loss of proximity. Some specific tools bringing more accountability, transparency, and stronger citizen participation can be introduced. They include, for instance, consultative committees, e-government, municipal citizen services, one-stop shops, municipal Ombudsman, etc.

Box 21. **Transforming municipalities into localities in a merger process: A way of keeping proximity and safeguarding local democracy**

Greece: the *Kallikratis* municipal amalgamation reform maintained historic communities as deconcentrated entities, providing "some intra-municipal decentralisation" (Council of Europe, 2015).

Ireland: the 2014 local government reform created a system of sub-county government, the "municipal districts".

France: the formula of *commune nouvelle* is part of this trend. An amendment passed in March 2015 (reactivating a former 1971 arrangement, also revised in 2010) promoted the status of "associated municipalities". This status allows the municipalities abolished in a merger to remain and retain a delegate mayor, a town hall (annex), an advisory council, etc. The success of this formula results from the relaxing of rules for the creation of these new municipalities. The greater flexibility introduced for the composition of municipal councils reduced opposition from local representatives. This success is also due to a large extent to financial incentives, allocated to small municipalities deciding to merge before January 2016. Moreover, for merging municipalities under 10 000 inhabitants, the law provides for an exemption of cuts to general grants (*Dotation Globale de Fonctionnement,* DGF) over a three- year period. There is a bonus of 5% of the DGF if the new municipality groups more than 1 000 inhabitants (while still remaining under 10 000 inhabitants in order to avoid larger municipalities engaging in a subsidy race). This reform seems to be quite effective even if it has not fundamentally changed the municipal landscape: 308 new municipalities were created before January 2016, resulting in the elimination of 1 019 municipalities. In light of this success, the financial scheme was renewed in 2016. It is interesting to note that this legislative amendment was strongly supported by local representatives themselves (*Association des Maires de France*) in a context in which municipal amalgamations remain a very sensitive issue.

Source: Authors' own elaboration.

2.1.5. "Bundling" municipal amalgamations with other territorial and institutional reforms

Reform processes may be facilitated by closely connecting **municipal reforms with territorial changes at other subnational levels.** For example, in Norway, the municipal reshuffle is intimately related to the reform of the counties, and the regional reform process is planned to catch up with the municipal merger process. Municipality and county structures should be mutually calibrated (NordRegio, Nordic Center for Spatial Development). In Finland, the new strategy of the government for reorganising the municipal sector is based on the creation of a new self-governing level. The municipalities would transfer some responsibilities to these new regions (healthcare and social care) but would also receive new responsibilities from the central government.

Connecting municipal reforms with institutional changes may also make the process smoother. Opposition to a given reform may be reduced by packaging it with another, more popular, reform. In many cases, stakeholders who stood to lose from one of these reforms can gain from other elements (OECD, 2010a). An important example of this approach relies on the combination of **a territorial reform with a decentralisation reform,** i.e. the transfer of new responsibilities and financial resources to merged municipalities. The two components are then closely related and appear to be two sides of the same coin, the territorial reform being partly driven by the decentralisation reform (whether intended or not). This was the case in the Danish 2007 local government reform where the abolition of counties and the reallocation of part of their responsibilities to the municipalities provided incentives for municipal mergers. In the Netherlands, the decentralisation programme, starting in 2007 and continuing in the framework of the 2012 new Coalition Agreement "Building the bridges", has encouraged municipalities to co-operate and to merge. In January 2015, large responsibilities were transferred to municipalities in the areas of social care, with the requirement that they consolidate (or collaborate) to perform their new mandatory social functions adequately. The first decentralisation process in 2007 showed that small municipalities did not have the managerial, administrative and financial capacities to deal with these new responsibilities, and several small municipalities needed to reorganise themselves on a more suitable scale. In Ireland, local authorities have been given an expanded role in economic development under the 2014 local government reform. In Norway, in the context of the 2014-17 municipal reform, transfers of additional responsibilities from the counties (e.g. secondary education and public transport) and the central government to municipalities will occur only if they merge into larger units. These units should be based on functional areas with sufficient capacity and competence to manage these new tasks. In Japan, the *Great Heisei Consolidation* was conducted in parallel to the *Trinity Reform* (fiscal component) which aimed at granting further authority to local governments, rationalising their functions and increasing their financial autonomy. Finally, the case of the 1989 Local Government Reform in New Zealand is particularly interesting because of its wide scope: local amalgamations were introduced in parallel to a wider restructuring of local governments in order to improve "community governance", and were combined with efficiency reforms within public sector organisations (Reid M., 2010).

2.2. Inter-municipal co-operation arrangements

Besides amalgamations, there are different options to counteract the negative effects of municipal fragmentation. One possibility is to reallocate some municipal tasks from small municipalities towards other entities (larger municipalities, e.g. in the Czech

Republic; other levels of SNGs, e.g. regions in the ongoing reform in Finland; or the central government, e.g. the recentralisation policy in Hungary). Another option for rescaling is "**trans-scaling", i.e. inter-municipal co-operation (IMC) arrangements** to jointly provide specific public services and infrastructure. **Legal frameworks and policies supporting IMC have been significantly enhanced over the last few years,** and **IMC is widespread** today and firmly rooted in European and OECD municipal management practices (Hulst and van Montfort, 2007).

IMC allows to **internalise externalities** in the management of the services and to benefit from economies of scale for utility services (water, waste, energy, etc.), transport infrastructure and telecommunication. Services may be shared as well: back office and administrative functions (e.g. payroll, finance, compliance and control activities, etc.), telecommunications and information technology, environmental services and parks maintenance, joint procurement, frontline services such as customer services, etc. At the same time, IMC allows municipalities **to retain their identity and those functions** that either do not require a larger scale of production or do not affect neighbouring municipalities.

IMC arrangements are **well developed in the OECD and also extremely diverse**, varying in the degree of co-operation, from the softest (single or multi-purpose co-operative agreements) to the strongest form of integration (**supra-municipal authorities** with delegated functions and even taxing powers). For instance in France, public establishments for inter-communal co-operation (*EPCI à fiscalité propre*) have their own sources of tax revenue. Other **shared services arrangements** are common in countries such as the United Kingdom, Australia, New Zealand or Ireland (shared services programmes). In addition, it is frequent that one municipality adheres to several inter-municipal groupings, and the size of these groupings may vary from two to dozens of municipalities, covering regional scales.

2.2.1 Drivers, benefits and constraints of inter-municipal co-operation

In theory, inter-municipal co-operation (IMC) allows for **efficiency gains and costs savings** which typically motivate reforms. In Spain, for example, clear benefits were observed concerning the joint management of waste collection (cost savings were particularly high in small municipalities, estimated to 20% in towns with less than 20 000 inhabitants, and to 22% in towns with less than 10 000 inhabitants – Bel, 2011). In England, recent figures from the Local Government Association show that the current 416 shared service arrangements between councils resulted in GBP 462 million of efficiency savings (as of September 2015).

IMC may also lead to **better local services**; improved processing times; **innovative/high-tech** and/or very specialised services (e.g. through the application of shared technologies); increased **staff performance;** and access to **expertise,** especially in remote locations that experience skill shortages (Local Government New Zealand, 2011).

One important driver for IMC or shared services arrangements is also to provide **an alternative or a counter strategy to municipal mergers,** in cases of strong amalgamation pressure from the central government or the state (e.g. Finland, Slovak Republic, Czech Republic, France, Iceland today, Victoria and New South Wales in Australia, New Zealand, etc.). In Iceland, for example, there are still many small municipalities but an evaluation of merger policies conducted in 2010 promoted inter-municipal co-operation instead of mergers. The 2011 Local Government Act clearly opted for co-operation rather than amalgamation by promoting municipal collaboration through regional boards, regional federations, or economic development agencies co-owned by the municipalities. Most of the time, however, **IMC is promoted in parallel to municipal mergers** (Norway, France, Estonia, the Netherlands). In Finland, the PARAS reform allowed municipalities to choose between co-operation and mergers. "Co-management areas", based on population thresholds, were established for healthcare and education services (Box 22). IMC can also correspond to a **transitional phase before mergers**. In Sweden, for instance, between 1962 and 1964, all municipalities were grouped into 282 "municipal blocks" based on urban-rural complementarity, which ultimately led to mergers within the block.

Box 22. **Inter-municipal co-operation in the PARAS reform: The local co-management areas**

One of the three objectives of the PARAS reform was to form larger catchment areas for municipal services with insufficient population bases, in particular, through increased inter-municipal co-operation. The reform provided for the establishment of "local government co-management areas" for social welfare and health services and for upper secondary vocational education. The same thresholds as for municipal mergers were defined for the creation of local co-management areas: a population of about 20000 inhabitants for primary health care (or closely associated social services), and a population of at least 50000 for vocational education and training. The local authorities involved in a co-management area could agree that these functions would be conducted jointly or by one municipality on behalf of one or more other municipalities.

After the PARAS framework act came into force, municipalities actively started to establish co-management areas for health care and associated social welfare services. By late 2012, there were 54 co-management areas of this type in Finland. All the plans for creating such areas were not implemented (at some point, 66 areas were considered). Moreover, some areas were also disbanded, as some municipalities decided to merge or to put an end to co-operation because of dissatisfactions. Among the 54 co-management areas, 21 were managed by joint municipal authorities, while a majority (33) was managed by a host municipality. Co-management areas were very diverse in size and by the number of participating municipalities (from 2 to 8). In the vocational education sector, co-operation between municipalities was driven both by the PARAS reform and the 2006 project of the Ministry of Education and Culture. This project aimed at ensuring a sufficient structural and economic basis for vocational education and training. At the end of the reform period, a very large majority of co-management areas (and municipalities) reached the population thresholds set for vocational education.

The creation of co-management areas led to significant organisational changes. According to the ARTTU report, decision-making structures have become more complex and municipal and co-management areas' decision-making has become more separated. However, the PARAS reform has positively impacted the integration of municipalities' social welfare and healthcare services. The establishment of co-management areas also led to modernising the management system in a large majority of municipalities.

Source: Authors' own elaboration.

Finally, another strong motivation for IMC may be **to fulfil new compulsory requirements**, for example, obligations to provide new services following the decentralisation of responsibilities. In Iceland, following the decentralisation of social services for disabled people, IMC became compulsory for small municipalities. In the Netherlands, inter-municipal co-operation (developed in parallel to municipal amalgamations) has gained impetus recently with the decentralisation of a number of tasks to local governments, in particular, for employment and social welfare services. To comply with these new complex responsibilities and to improve financial management, many municipalities decided to create new co-operation structures, for example, inter-municipal social services (ISD).

However, the **positive effects of IMC in terms of efficiency gains are not always clear** in practice. IMC can lead to significant **constraints:** in Finland (Box 22) and in France, a country where inter-municipal co-operation is one of the most developed and formalised within the OECD, IMC outcomes are quite ambiguous. Although efficiency gains exist in some areas, financial incentives, combined with other factors, have generated an ineffective proliferation of IMC structures and have not led to streamlining costs as initially planned (Box 23). Another important drawback of IMC is its **lack of transparency**. IMC may cause confusion among taxpayers, as responsibility is subdivided among all municipalities participating in the agreement, thereby reducing accountability (Slack and Bird, 2013). The introduction of IMC and shared services may also cause **political, organisational and operational difficulties.** Strong leadership and staff motivation may be needed to overcome potential resistance, which can require considerable time and effort. In fact, there can be asymmetries of power between the participating authorities. Bigger units may have more weight in the bargaining processes and can thus ensure that their interests prevail over those of smaller ones. Such asymmetries are typical, for example, for co-operative arrangements involving a large city and surrounding smaller municipalities (OECD, 2014b). Technical challenges are also related to discrepancies across municipalities in terms of resources, equipment, systems or processes. Finally, **co-operative processes can be costly** (high transaction costs and externalities) and complex, at least in the first stages when expected savings are rarely made (Local Government New Zealand, 2011). Overall, the efficiency of IMC depends on a range of factors, including the number of participating municipalities, the extent of transaction costs, and the characteristics of the public good in question (Bartolini and Fiorillo, 2011). To overcome these difficulties and make inter-municipal co-operation work, **some strategies must be developed during both the design and implementation phases**. In that respect, **central or state government policies can play a fundamental role in encouraging and facilitating the development of IMC.**

Box 23. **Unclear outcomes of inter-municipal co-operation in France**

The French government strongly encouraged municipalities to form co-operative structures by providing grants to those who introduced a common business tax with neighbouring municipalities. As a result, nearly all French municipalities are currently part of an "integrated" inter-municipal co-operation structure.

There are four main types of co-operation structures in existence since 2014 (the 2014 MAPTAM law created the "metropolis"): "communities of municipalities" bringing together small rural municipalities (less than 50 000 inhabitants), "town communities" (between 50 000 and 250 000 inhabitants), "urban communities" for urban areas (between 250 000 and 400 000 inhabitants) and "metropolis" above 400 000 inhabitants. Governed by delegates of municipal councils, these structures are considered as particularly "integrated" because they levy taxes to finance the carrying out of duties transferred to them: mandatory responsibilities (imposed by law) and

Box 23. **Unclear outcomes of inter-municipal co-operation in France** *(continued)*

optional tasks (depending on the decisions of member municipalities).

However, an evaluation of the current system reached the conclusion that, although efficiency gains exist in some areas such as public infrastructure, financial incentives (combined with other factors) have caused a superfluous number of inter-municipal structures. This has in turn created a scattered and complex system of governance which is confusing for citizens (Kitchen, 1993), caricatured with the name "*mille-feuille"* (many-layers).

IMC has not led to a streamlining of costs as initially planned. Instead, it has led to an overlapping of responsibilities and duplications in terms of services and staff, as a proper re-allocation of resources (in particular human resources) from municipalities to inter-municipal groupings did not occur. This induces additional costs for member municipalities, due to the operating costs of inter-communal structures, overlapping functions, and the increasing wages of personnel transferred from municipalities (OECD, 2006). In addition, while inter-municipal co-operation structures can raise taxes, they are lacking democratic legitimacy and have reduced political accountability (Bird, 1995; OECD 2013b).

Source: Authors' own elaboration.

2.2.2 On-going reforms concerning inter-municipal co-operation

Most OECD countries have now passed laws promoting inter-municipal co-operation. Specific and appropriate legal frameworks for IMC are now in place. Many of these frameworks have been reformed since the crisis to reinforce IMC or encourage/force municipalities to participate in co-operation agreements. In Austria, a federal constitutional amendment, adopted in 2011, further reinforced IMC. Other examples include New Zealand (2013 amendment to the Local Government Act 2002), Chile (law 20.257 in 2011), and the Slovak Republic (2012-2013 ESO Programme).

In a few countries, co-operation is **compulsory**, at least for small municipalities and/or for specific local public services: Greece (for waste management); Iceland (for municipalities of less than 8 000 inhabitants). In Hungary, the Cardinal Act of December 2011 forces municipalities under 2 000 inhabitants to regroup their administrative services within local government offices. In Estonia, the upcoming law could lead to compulsory inter-municipal co-operation in some areas. The law will also widen the responsibilities of inter-municipal groupings. In Italy, the new law 56/2014 on municipal unions significantly reinforced IMC (widespread since 1990) in around 500 municipal unions and mountain communities. A minimum population threshold was established: municipalities of less than 5 000 inhabitants now have the obligation to adhere to a Union of municipalities. The responsibilities of municipal unions were also extended to include all basic municipal functions. In Portugal, the 75/2013 law created 23 compulsory inter-municipal communities, as sub-regional bodies responsible for "Nuts III" territorial strategies (they regroup previous urban communities, inter-municipal communities for general purpose, and some previous metropolitan areas). In France, since the *NOTRe* law, all municipalities must include an inter-municipal structure with own-source taxes (public establishments for inter-communal co-operation or "EPCI"). Despite a very good coverage of the French territory by inter-municipal structures, there were some remaining "grey areas" with "isolated" municipalities. Many isolated municipalities remained in the *Ile-de-France* region in particular which then had to become part of the *Grand Paris* metropolis.

Most of the time, IMC is promoted **on a voluntary basis.** Incentives are created to enhance inter-municipal dialogue and networking, information sharing, and possibly to help in the creation of IMC entities. These incentives can be financial (e.g. special grants for inter-municipal co-operation and a special tax regime in France; additional funds for joint public investment proposals in Estonia and Norway; bonus in grants in Spain for municipalities making savings through co-operation, since the new law 27/2013). Incentives can also have a more practical nature (consulting and technical assistance, production of guidelines, measures promoting information sharing such as in Canada, United States, and Norway, etc.). Some governments also implemented new types of contracts and partnership agreements to encourage inter-municipal co-operation: Poland (with the introduction of territorial contracts) and Portugal (with multi-level contracts introduced in the 75/2013 law). Even Japan, where inter-municipal co-operation was not particularly encouraged (amalgamations being the privileged option to consolidate municipalities and increase their efficiency), is now developing a new type of contract (Partnership Agreements, introduced in the 2014 Local Autonomy Act).

Besides promoting IMC, some governments are restructuring the inter-municipal landscape. This is the case of Finland and France. In Finland, the 184 special-purpose joint authorities in charge of joint municipal services (mostly in health care and education) will be reorganised by the upcoming reform. New self-governing regions will take over health care and social responsibilities, carried out today by municipalities and joint authorities. In France, the objective of the new 2015 reform is now to redefine and streamline the inter-municipal landscape (Box 24).

Box 24. **Reforming the inter-municipal landscape in France**

In France, inter-municipal co-operation structures are well-established. The inter-municipal level has become a quasi-fourth level of subnational government with a complex and costly system of governance. There are around 2 145 groupings of municipalities with their own sources of tax revenue (not counting the 13 000 single and multi-purpose inter-municipal syndicates).

The recent *NOTRe* law, enacted in August 2015, aims at streamlining and reducing the number of IMC structures. The objective is that groupings should correspond to socio-economic functional areas. After numerous debates, the minimum threshold for groupings passed from 5 000 to 15 000 inhabitants (20 000 in a previous version), with exemptions to take into consideration sparsely populated areas, mountainous areas, recently merged groupings and islands. This objective should be attained before January 2017. All municipalities will have the obligation to integrate an inter-municipal co-operation body. The number of inter-municipal syndicates (single or multi-purpose, without taxing power) will have to be reduced.

The government also seeks to clarify the distribution of responsibilities between inter-municipal structures and their member municipalities. Departmental schemes for co-operation (SDCI) will include an inventory of the distribution of responsibilities of existing groups. Municipalities will have the obligation to transfer some additional duties to their “communities of municipalities” and “town communities” (water and sewerage, waste, tourism, reception of travellers, commercial activities (but no longer economic development); other optional responsibilities have been added by law (e.g. creation of public services centres). In addition, provisions for the pooling of services and personnel have been improved by law to avoid duplication. Finally, one initial proposal was overturned by the Senate and was abandoned. It concerned the introduction (before January 2017) of direct elections for representatives of inter-municipal co-operation structures with taxing power, aimed at reducing the “democratic deficit”. These elections would have had a major impact on the municipal landscape.

Source: Authors' own elaboration.

2.3. Metropolitan governance reforms

Metropolitan governance reforms address the issue of fragmentation at the scale of functional urban areas. Administrative borders in metropolitan areas, based on historical settlement patterns, no longer reflect current human activities or economic and social functional relations (OECD, 2015j). Efficient metropolitan governance has become a hot topic in many countries. Enhancing the co-operation and co-ordination of public policies on a metropolitan-wide basis, in particular with regard to the provision of public infrastructures and services, aims at improving the quality of life and international competitiveness of large cities.

However, most metropolitan governance reforms have triggered or still cause **intense political debates and controversies** as they hinge on specific national and municipal history, and also cultural and socio-institutional frameworks. Various factors explain strong resistance to metropolitan governance reforms: strong local identities and antagonisms; vested interests of politicians and residents; opposition from higher levels of SNG (regions) which tend to be in competition with metropolitan bodies; and local financing system and high costs of reforms. These factors often provide disincentives for metropolitan-wide engagement (OECD 2013b, OECD 2015j). For this reason, national reforms are often used to facilitate the process and provide incentives or even impose such reforms.

As a result, the number of metropolitan governance authorities of all types (soft inter-municipal co-operation, more structured and integrated forms, mergers) has increased considerably. There has been a **renewed momentum in the number of metropolitan governance bodies** created or reformed since the 1990s, against the backdrop of the early 1990s recession and the 2008 financial crisis. Among the 275 OECD metropolitan areas (500 000 or more inhabitants), at least 49 entities were created in the 2000s, and at least 15 in the first three years of this decade. Currently, around two-thirds of these metropolitan areas have a metropolitan governance body (Ahrend et al. 2014).

2.3.1 Metropolitan governance reforms in federal countries

In federal countries, metropolitan reforms (like other territorial reforms) are designed, supported and implemented by individual federated states and not by the federal government - with more or less voice for local governments in the process. However, in some countries **the federal government tends to intervene,** setting general guidelines for metropolitan reforms, and letting state governments carry out the implementation within their territory (OECD, 2015j). In a globalised world where cities are increasingly seen as critical areas for competitiveness and national growth, several federal governments consider that they cannot ignore these strategic issues and that they have a role to play on behalf of the “national interest” (Box 25).

Box 25. **Federal governments tend to intervene increasingly in metropolitan reforms**

Australia: the federal government presented a "Cities Agenda" in 2015 focusing on improved access to quality local jobs and affordable housing; the sustainability and amenity of cities; preparation of national policy papers and guidelines; and financing of large metropolitan infrastructure projects.

United States: the Federal government, very early on (from 1960), sought to encourage co-operation between local authorities in major cities to deal with problems that seemed relevant at the metropolitan level, primarily concerning transport. It supported the creation of two major co-operation arrangements in several US cities: the Councils of Governments (COG, also called "metropolitan councils" or "regional councils") and the Metropolitan Planning Organizations (MPO). Gradually, the COG and the 405 MPOs in the United States gained skills and resources, and are now nationally the only organisations taking the metropolitan level into account.

Switzerland: an amendment to the Constitution (in 2001) opened the way for urban policies at federal level, stating that "the government shall take into account the particular situation of cities and agglomerations". It was followed by the implementation of a federal "agglomeration programme" in 2001, aimed at improving amenities and the competitiveness of urban centres and agglomerations through incentives (special funds for traffic infrastructure), networking between players and the pooling of knowledge.

Source: Authors' own elaboration.

Federated states can be very active in promoting metropolitan governance reforms. In Canada, amalgamations of urban municipalities into metropolitan municipalities took place in the mid- to late 1990s to overcome fragmentation and increase the efficiency of municipal services at metropolitan level. These mergers include the metropolitan areas of Halifax (1996), Toronto (1998) and Montreal (2002, de-merged in 2004). In Germany, several *Länder* have designed and implemented metropolitan reforms: *Hesse* with the *Regionalverband* of Frankfurt, founded by a state law, consisting of the compulsory association of 75 municipalities; Baden-Württemberg with the Verband Region Stuttgart (voluntary association); Lower Saxony with the foundation of the "Region Hannover" in 2001; etc. In Australia, a profound reform of metropolitan governance has been underway since 2011 in all Australian states. This reform followed an audit of the organisation of municipalities and metropolitan areas in Australia, initiated by the Council of Australian Governments' Reform Council (OECD 2013b). Launched in 2009, the national audit helped to develop a COAG "Agreement on Cities". This agreement recognised the importance of cities and metropolitan areas, and the need for effective planning: various Australian states then launched their metropolitan reforms. For example, in June 2011, the state of Western Australia commissioned a group of experts (the Metropolitan Local Government Review Panel) with the task of conducting an evaluation of metropolitan governance in Perth. Some Mexican states are also involved in the promotion of metropolitan governance arrangements, e.g. the states of Jalisco (metropolitan area of Guadalajara) and Nuevo León (metropolitan area of Monterrey) (OECD 2015c, OECD 2015e).

2.3.2 Metropolitan governance reforms in unitary countries

In unitary countries, **central governments tend to increasingly take the leadership of metropolitan governance reforms.** There is a growing awareness of the contribution of strong large metropolitan areas to countries' overall growth and well-being. A wide diversity of approaches exists (OECD, 2015j): supporting or facilitating bottom-up initiatives, offering effective incentives, enacting regulations, and sometimes imposing new metropolitan governance arrangements (mergers or inter-municipal co-operation bodies). C**entral governments play two other key roles. i) They provide**

adequate funding to metropolitan bodies in order to match their responsibilities and to respond to their financial needs in terms of infrastructure and services - “adequate” meaning sufficient, tailored, diversified, sustainable and favouring equity. Specific schemes, taking into account the particular financial needs or constraints of metropolitan structures, may be introduced. This is often the case regarding equalisation, as metropolitan areas are typically affected by wide internal disparities in terms of revenue-raising potential, expenditure needs and investment capacity (OECD 2015j). **ii)** Central governments also play an **arbitrating and mediating role** between metropolitan bodies and other levels of government (municipalities, intermediate levels such as regions or provinces). Intermediate levels of government, in particular, may perceive metropolitan bodies as an alternate centre of power, especially if they have sizeable responsibilities and resources. For example, the complex relationships between city-regions and provinces were a sensitive issue in the Netherlands (OECD 2014b). This has also long been the case in Italy and in France.

Many regulations and initiatives have been taken over the last five years to promote metropolitan governance reforms: New Zealand (2010), Turkey and Japan (2012), France and Italy (2014), Poland (2015). In England, the "Cities and Local Government Devolution Act 2016" allows for greater devolution of powers to combined authorities and introduces directly-elected mayors. In Poland, the reform was preceded by several years of discussions on the status and future of Polish metropolitan areas. The law on metropolitan communities entered into force in January 2016. The first metropolitan communities were created under the initiative of the central government; from January 2017 onwards, they will be created at the request of municipalities. New Zealand, Japan, France and Italy illustrate the diversity of governance arrangements as well as the difficulties to design, implement and sustain effective metropolitan governance reforms (Box 26).

Box 26. **Metropolitan reforms in New Zealand, Japan, France and Italy**

New Zealand: the major territorial reform since the end of the 1989 reform is the creation of the Auckland Council. Seven territorial authorities and the Auckland Regional Council were merged into a single council in 2010. The process started in 2007, when the central government concluded that the large number of councils, their difficulty to work together, and the weakness of the regional government were hindering Auckland's progress. The government set up a Royal Commission on Auckland Governance to analyse potential restructuring. Two main options were considered: creating a stronger regional government or amalgamating all councils under one local authority. The Commission asked for several background research papers, conducted several visits around the world and organised numerous public consultations. In 2009, the Royal Commission submitted its report, and the newly elected government subsequently announced that a "super city" would be created, including the full metropolitan area under a single Auckland Council. A number of Acts of Parliament were passed, and an Auckland Transition Agency was created by the central government. Despite several controversies (some recommendations from the Royal Commission were not taken into account by the government), the selected area (the region), choice of governance model (merger), organisational structure, and outsourcing of major functions to external independent agencies (council-controlled organisations or CCOs) were respected. The Auckland Council became operational in November 2010, combining the functions of the Auckland regional council and seven other territorial authorities. Although the Auckland Council was only created quite recently, hence making ex-post evaluation difficult, there is anecdotal evidence of both positive and negative outputs (cf. Case Study 5 in the Annex). The reform is considered as “still a work in progress” but some stumbling blocks seem to be on their way to being resolved (e.g. introduction of local boards in the governance model). However, observers consider that an independent evaluation of the impact of the reform would be useful to ascertain the level of its effectiveness.

Box 26. **Metropolitan reforms in New Zealand, Japan, France and Italy** *(continued)*

Japan: a legislative measure allowing Japanese metropolitan areas to form new urban governments was passed by Japan's parliament in 2015. The law enables large cities to reorganise themselves into new special entities modelled on Tokyo's system of metropolitan governance (with a system of special wards), considered as best practices. Osaka and nine other major Japanese cities with populations of over two million (Sapporo, Saitama, Chiba, Yokohama, Kawasaki, Nagoya, Kyoto, Sakai and Kobe) can introduce new metropolitan structures, following approval by city referendum. Despite strong support of local representatives and business communities, Osaka's citizens rejected a proposal for a new metropolitan government. This proposal would have merged the existing 24 administrative subdivisions into five new elected municipal bodies with enlarged responsibilities.

France: efforts were made by the central government during the 2000s to encourage co-operation at an urban level (spatial planning directive, DATAR calls for metropolitan projects). However, apart from the creation of urban communities in 1966, they had little success. The 2010 "Law on the Creation of Metropolitan Areas" has led to the creation of only one metropolis (Nice Côte d'Azur), confirming once again that regulation is not sufficient to induce reform. A new step was achieved in 2013 with the first discussions on the new law on metropolitan areas. Government adopted a new approach, based on governance solutions tailored to territorial specificities and local needs. The 2014 "MAPTAM" law, on the modernisation of public territorial action and metropolises, introduced a degree of diversification across French territories. 14 metropolises (more than 400 000 inhabitants) will be granted greater responsibilities than "standard" municipalities or inter-municipalities, justified by their larger size and urban nature. Among them, the three largest metropolitan areas (Paris, Lyon and Aix-Marseille-Provence which already have a specific status since the 1982 PLM law) received *ad hoc* different governance structures - i.e. different organisation, responsibilities and resources. The *Métropole du Grand Lyon*, operational since January 2015, has (unlike Paris and Aix-Marseille-Provence) a particular metropolitan status: it merged the responsibilities of the existing inter-municipal co-operation entity *Grand Lyon* and those of the *département du Rhône*, covering about 1.3 million people - the only one of its kind in France. Political representatives for the metropolis will be elected through direct suffrage from 2020 onwards. This innovative "asymmetrical" approach based on "recognising the diversity of territories within the unity of the Republic" is relatively new in France (OECD 2013g), where past policies were uniform across territories (except for overseas territories). It aims at adapting organisational structures and policies to the distinctive characteristics of territories at an appropriate scale. Another innovation is the setting up of two transitory inter-ministerial "prefiguration" task forces for Grand Paris and Aix-Marseille-Provence. These task forces, headed by the prefect and composed of national and local civil servants and experts, prepared the reforms and then help in the transition process. They also work to gain support from citizens, local authorities, the private sector, and civil society (OECD, 2013b). Finally, the French metropolitan reform is a good illustration (at least in the cases of *Grand Paris* and Aix-Marseille) of resistance from local mayors, and possibly from the regional level The implementation process is as crucial as the nature of the reform itself: the adoption of a law is not sufficient as it may not, or partly, be implemented in practice.

Italy: Italy went through more than two decades of deadlock in the "metropolisation" process, before a recent turn in 2014 (OECD 2015j, OECD 2013b). The initial legal framework was introduced in 1990: Law n. 142/1990 offered the possibility for ten major cities to establish "metropolitan cities" (*città metropolitane*), endowed with a range of key responsibilities (spatial planning, economic development, etc.). These new institutions would be created by regional law, in the absence of which the central government could intervene. However, neither the regions nor the central government took any strong institutional or financial action. A few local attempts remained unsuccessful. However, a new draft law introduced in 2013 removed the ability of regions to oppose the creation of *città metropolitane*. The national operational programme for metropolitan cities (PON Metro) should also support the creation of new ones. This programme, included within EU Structural Funds (2014-2020), aims at supporting investments at a metropolitan scale; it should benefit the ten cities, and four additional cities from special status regions (Palermo, Messina and Catania in Sicily, Cagliari in Sardinia).

After a long and difficult legislative process, Law N 56/2014 (adopted by the Parliament in April 2014) established a new roadmap for *città metropolitane*. In an effort to avoid the delicate question of metropolitan boundaries – which had proven a major obstacle to the emergence of metropolitan structures in the past – the

Box 26. **Metropolitan reforms in New Zealand, Japan, France and Italy** *(continued)*

government decided to fix these boundaries to those of the corresponding provinces. However, it left to each territory the freedom and responsibility to decide the depth and breadth of inter-municipal co-ordination. The law includes the possibility to change provincial boundaries but this process is complicated and could be discouraging in practice. As for France, there will be some differentiation within Italian metropolises in terms of status, organisation, responsibilities and financing (which will be adapted to local needs).

Source: Authors' own elaboration.

Metropolitan governance reforms are still under discussion in Chile (bill proposing the creation of metropolitan areas for administrative purposes), in Portugal (possible improvements in the metropolitan governance and administrative areas of Porto and Lisbon and adapting their administrative area to the functional urban areas) and Finland (Box 27). In Greece, the metropolitan areas of Attica and Thessaloniki, included in the Kallikratis reform, still need to be implemented. An interesting singular case is also the Netherlands where the eight city-regions were created by the state through the WGR+ regulation in 1995, on a compulsory basis. These regions were amended in 2005, and abolished in January 2015 in order to simplify the country's complex multi-level governance structure, among other reasons. However, the law provided for the creation of specific new metropolitan governance arrangements for the two largest urban areas: Amsterdam and Rotterdam-The Hague (OECD 2016b). Other city-regions may use existing voluntary co-operation mechanisms to remain active. This reform illustrates the government's recent willingness to tailor its urban policy to the specific needs of different urban areas, as opposed to imposing a uniform setting across the entire country.

Box 27. **Resistance to governance reforms in urban areas in Finland**

Metropolitan governance reforms for Helsinki and ten other urban areas have been planned for many years but remain on paper only. The PARAS reform provided for specific arrangements for urban areas, including the Helsinki Metropolitan Area. It involved some specific incentives (financial but also organisational, such as structural models serving as tools guiding land use). Urban authorities had to design plans in order to alleviate problems linked to dispersion and insufficient co-operation for services, and for the organisation of transport and housing. But in urban areas, despite some positive improvements in terms of regional planning and economic collaboration, inter-municipal co-operation and mergers have progressed only slowly. This slow progress results from a lack of political commitment; lack of trust between municipalities, which have "historically competed over residents, enterprises and jobs" and, in addition, home builders; and a lack of support from the resident population (ARTTU). The next law, adopted in 2013, put metropolitan reform back on the agenda with an aim to strongly encourage mergers in urban areas. However the proposal was turned down.

Source: Authors' own elaboration.

3. Reforms of intermediate and regional levels have a more diverse set of rationales

At regional and intermediate levels, "pure" territorial reforms, i.e. a restructuring of boundaries, are very rare. Most often, they are carried out jointly with institutional reforms aimed at redefining or attributing new assignments and resources to the "new" regions. The reverse is less true: many institutional reforms at regional and intermediate levels do not have a territorial component (see Part I).

Territorial reforms at regional and intermediate levels **aim at reaching a greater critical size** and thus consolidating and reducing the number of entities. Many OECD

regional or intermediary governments are still based on historical settlement patterns (Table 5) which have not been modified for many decades. But beyond that, **the rationales behind regional and intermediary government reforms are diverse**, and differ depending on whether regions or intermediary governments are concerned.

3.1. The specificity of the intermediary level and the design of territorial reforms

In OECD countries with three subnational tiers, **intermediary governments have relatively heterogeneous characteristics**, in particular, in terms of area or population. They do, however, have something in common: while the intermediary level was typically **historically strong**, with solid roots and attachment to the local population, **it tends to be weaker today**, excluding France (Dexia, 2008). Over the last decades, it has lost many of its powers and responsibilities in favour of regions, which gained more importance. In a majority of countries, intermediary governments are now mainly responsible for administrative tasks. They have small budgets and in general no, or only limited, taxing powers (Spain, Italy, counties in Poland and rural districts), with the exception of provinces in Belgium.

The administrative boundaries of these entities, based on historical settlement patterns, are now **often outdated** and do not reflect socio-economic relations and functional areas: Polish counties, Italian, Spanish and Belgium provinces and French *départements* (Box 28) all provide illustrations of this fact. In addition, the intermediary level, above municipalities and below the regional level (defined as the **"meso-government" level** (Sharp 1993)) is, most of the time, **squeezed between the upper and lower levels of government.** Its development depends to a large extent on those of municipalities and regions. In many OECD countries, the intermediate level is under pressure from municipal restructuring (up-scaling), inter-municipal co-operation (trans-scaling) and metropolisation. In addition, it simultaneously faces competition from regions that become stronger.

Box 28. **Intermediary governments' administrative boundaries are often based on a reality different from today's: The case of France and Italy**

In France and Italy, intermediary governments have deep historical roots but their boundaries are now outdated. They do not reflect socio-economic relations and functional areas:

- The French *départements* were created by the French Revolution in 1791. While many have been added to the list of the first 83 *départements* over time (101 today) and several changes made, the general principle for defining boundaries was that an individual could reach the central administrative city (*chef-lieu*) by horseback and return within the same day from every corner of the territory. The cantons were also created during this period as an electoral subdivision of the *département*. A canton is a territory of around 16 to 20 square kilometres whose boundaries were determined along the same lines as those of the *département*, i.e. within a single day's journey from the central city, but this time on foot. The names of the *départements* were derived from rivers and mountains situated on the territory, in a radical departure from the names of the provinces of the *Ancien Régime*.
- Italian provinces were established by Napoleon Bonaparte on the model of French *départements*. When Italy was unified into a single kingdom in 1861, the provinces remained, their status formalised under the Rattazzi Law in 1865, for a total of 59 provinces. Since then, most provinces have remained the

Box 28. **Intermediary governments' administrative boundaries are often based on a reality different from today's: the case of France and Italy** *(continued)*

same although their number grew regularly after further annexations (Veneto, Friuli, Mantova, Rome, etc.). In 1927, a royal charter created 19 new provinces. Since 2000, seven new provinces have been established, including four in Sardinia, giving a total of 110 provinces today. Most Italian municipalities also have a similarly long history.

Source: OECD (2014c), *OECD Regional Outlook 2014: Regions and Cities: Where* Policies *and People Meet*, OECD Publishing, Paris, http://dx.doi.org/10.1787/9789264201415-en.

In this context, in almost all OECD countries concerned, **debates were conducted for many years on the role and relevance of intermediary-level authorities**, in particular in urban areas. However they rarely led to consolidation reforms, this due to strong resistance. In Germany, for example, some *länder* carried out several amalgamations of rural districts, e.g. Saxony-Anhalt and Saxony in 2008 (having the number of *landkreis* in both cases) and Mecklenburg-West Pomerania in 2011. In England, the two-level system still in place in some rural areas is disappearing and counties are gradually replaced by "unitary authorities".

More recently several governments put the abolition of the intermediate level back on the agenda, especially in the aftermath of **the crisis and the resulting pressures on public finances** (COE, 2013). However, these attempts were met (once again) with strong opposition. To avoid protests, many governments considered **transforming the intermediary level instead of merely abolishing it -** at least as a first step. In Belgium, for example, while the elimination of provinces was envisaged in both Wallonia and Flanders, the regions decided respectively to instead involve provinces in the development of "supra-municipalities" (in Wallonia) and to downsize provinces by reducing their responsibilities and temporarily restricting their taxing power (in Flanders). In Spain, despite the fact that provinces have been contested for a long time and suffer from a lack of democratic legitimacy (Bertrana et al., 2011), the 27/2013 law on the "Rationalisation and Sustainability of Local Administration" has strengthened their role by recentralising some small municipalities' responsibilities (under 20 000 inhabitants) at the provincial level. In Italy and France, the abolition of the intermediate level was also announced but provoked an outcry. In Italy, the government found an alternative solution which could lead to abolition in the longer term while, in France, discussions on the future of *départements* was postponed until 2020 (Box 29).

Box 29. **Reforming the intermediary levels in Italy and France: A difficult path**

Italy: the abolition of Italian provinces had been envisaged since 2009 but only gained some momentum in 2011 following budget consolidation measures introduced in the context of the public finance crisis. The first decree-law planning for the abolition of provinces was passed within Mario Monti's *Salva Italia* decree. Another decree, passed in November 2012, stated that the number of provinces – located in ordinary regions – should decline from 86 to 51 in 2014. However, the Constitutional Court rejected this reform in July 2013 on the grounds of constitutional illegitimacy (the provinces are enshrined in the Constitution). The subsequent governments (E. Letta and M. Renzi) were also in favour of a territorial reform so the momentum for reform remained; the reform process was entrusted to Graziano Del Rio and benefited from the strong support and leadership of Matteo Renzi. A new proposal of law was approved by the Assembly in December 2013 and finally passed in April 2014. Instead of abolishing provinces, this law transformed them from self-governing entities into inter-municipal bodies (and into metropolitan cities in the ten metropolitan areas). According to the law, regional administrations are in charge of determining which responsibilities and functions should be transferred from the provinces to regional or municipal governments within their jurisdiction. This should lead to a great variety of local government regional systems across the country (such as in federal countries). Although slow progress was initially made by the regions in this direction, almost all regions had adopted such agreements in late 2015. The reassignment of provincial human resources (around 8 000 employees) and provincial assets and liabilities was considered a complex question, with potentially costly changes needing implementation in a period of budgetary restriction. Finally, a Constitutional reform approved by the Senate in October 2015 would abolish the provinces from the Constitution (subject to a referendum in December 2016).

France: in contrast to other countries, French *départements* are still powerful despite the rise of the regional level since the 1982 decentralisation laws. In 2014, they represented 32% of local government expenditure (compared to 12% for the regions), with the municipal sector representing the bulk (56%) of local spending. They manage a wide range of responsibilities from social welfare (60% of their current expenditure: youth protection, minimum insertion income, social protection for the elderly and disabled) to secondary education, departmental road network, rural development, etc. The Act II of decentralisation (2004-08) aimed at strengthening regional government but, in the end, the *départements* benefited most from these transfers of power, with a further increase in their roles within the subnational public sector (COE, 2013).

Following the Committee Balladur's recommendations (report entitled "Urgent Decisions Need to be Made"), the government announced its desire to abolish *départements* in the framework of the 2010 territorial reform. However this decision faced strong resistance and the 2010 territorial reform had to find a substitute. It set up a new type of locally elected representative instead, so-called "territorial councillors" sitting both on general councils (*département* level) and on regional councils. The introduction of these councillors was seen as a way of maintaining the *département* while reducing the number of local politicians, putting an end to duplications and enabling the pooling of resources. This measure was a sort of prelude to the redefinition of the role of *départements* and potential mergers between the two levels.

The 2010 law was, however, revoked by the next government elected in 2012, as promised in its programme. The government launched a new territorial and decentralisation reform in 2013. After some hesitation and many public statements, the abolition of *départements* by 2020 was finally announced by the Prime Minister in April 2014. However, as it would require a revision of the constitution, other scenarios were prepared: including maintaining *départements* in rural areas but merging them with the new metropolitan cities in urban areas; merging *départements* and intermunicipal groupings (a scenario inspired by the Italian reform as well as by the example of the *Métropole du Grand Lyon*). Finally, following intense parliamentary debates, the *départements* have been maintained. Moreover, although the general clause of competence has been eliminated for the *département*, most departmental responsibilities have been preserved by the law NOTRe enacted in August 2015 (secondary schools, roads, social affairs). The *départements* will focus more on social solidarity as well as on supporting rural municipalities. Discussions on the future of the départements have been postponed to 2020, and *départements* in the meantime, the different hypotheses about their future transformations remain valid.

Source: Authors' own elaboration.

3.2. *Territorial reforms at regional level*

Strong regionalisation processes took place in the OECD in the 1980s and 1990s, resulting in the creation (or strengthening) of an autonomous regional level, for example in Spain, Italy, France, the United Kingdom, or in several central and eastern European countries, such as Poland, Slovak Republic and Czech Republic. In more recent years, regional reforms are still considered in the OECD, although fewer countries envisage introducing a new self-governing regional level. Finland is one of them. More often, regional reforms have evolved towards the up-scaling of existing regions and/or their institutional reinforcement. In some countries, this issue is still being debated, sometimes for many years and in an intermittent fashion,, but with no concrete results so far (e.g. Japan). Finally, in some countries, regionalisation projects have been abandoned, postponed or rejected by the population via referendum (Slovenia in 2008, Portugal in 1998, England in 2004).

Table 5. **Intermediary and regional governments in the OECD**

2015-2016	Intermediary and regional levels	Year of creation	Recent reforms - Notes
Federal countries			
Australia	6 states and 2 territories	1901	
Austria	9 Bundesländer	Middle-Ages - 16th	
Belgium	10 provinces	1830	Provinces' role being transformed by their respective region.
	3 regions and 3 language communities	1970	Six State Reforms from 1970 to 2011 transforming Belgium into a federal county.
Canada	10 provinces and 3 territories	1867 - 1999	
Germany	Intermediary: 402 districts (295 rural districts and 107 district-free cities)	Since 16th century	
	Regional: 16 länder	1949 and 1990	2006 and 2009 Federal Reforms
Mexico	31 states and the federal district (Mexico City)	1824	Fiscal and regulatory decentralisation since late 1980s.
Spain	Intermediary: 50 provinces	1833	Since 2013, some municipal responsibilities (under 20 000 inhabitants) transferred to provinces.
	Regional: 17 autonomous communities	1978	Each region has its own autonomous status. Specific "foral" status for Basque Country and Navarra.
Switzerland	26 cantons	Middle-Ages	
United States	Intermediary: 3 031 counties	Since 1630's	
	Regional: 50 states	1776/1781 (original 13)	
Unitary countries			
Chile	15 regions	2009	Regional councils directly elected since 2013; regional executives to be elected directly in 2017.
Czech Republic	14 regions (including City of Prague)	2000	
Denmark	5 regions	2007	2007 regional reform merged 13 counties to form 5 regions without taxing powers
Finland	1 autonomous region (island region of Åland)		A reform is under way to set-up 18 self-governing regions.
France	Intermediary: 101 *départements*	1791	Discussions on the future of the departments postponed to 2020.
	Regional: 18 regions	1982	13 regions instead of 22 in mainland France since the 2015 reform. They received additional responsibilities.
Greece	13 regions	2011	Created by the Kallikratis reform as self-governing regions from previous 54 prefectures.
Hungary	19 counties	Restored in 1990	Counties lost several responsibilities since the 2012 Constitutional reform and 2011 Law on Local Governments.

Table 5. Intermediary and regional governments in the OECD *(continued)*

Italy	Intermediary: 107 provinces and metropolitan cities	1802 – 1861	Provinces being transformed into inter-municipal bodies and creation of metropolitan cities (2014 Act). Constitutional reform underway to abolish the provinces.
	Regional: 20 regions + 2 autonomous provinces	1948 and 1970	5 regions with special status and 15 with ordinary status, 2 autonomous provinces. Constitutional reform is underway.
Japan	47 prefectures	1871	One metropolitan district (Tokyo), two urban prefectures (Kyoto and Osaka), one "district" or "circuit" (Hokkaidō), and rural prefectures. Regional reform discussed for many years (mergers - *doshusei*).
Korea	17 regional-level entities	1991	Nine provinces, six metropolitan cities, Sejong Self-governing City and Seoul capital city.
Netherlands	12 provinces	Before 1848.	Regional reform envisaged for many years (mergers). Last attempt in 2014 failed in the Parliament.
New Zealand	11 regional councils	1989	
Norway	18 counties	1660s	A regional reform is underway (mergers and new distribution of responsibilities).
Poland	Intermediary: 380 counties	Re-instated in 1999	Counties include 314 counties and 66 cities having the status of county.
	Regional: 16 regions	1999	A law passed in 2009 reinforced regional responsibilities.
Portugal	2 autonomous regions of Azores and Madeira	1976	Creation of 8 self-governing regions in continental Portugal rejected by a referendum held in 1998.
Slovak Republic	8 higher territorial units	2001	
Sweden	21 county councils	1634	County councils having different status and responsibilities. Regional mergers now investigated.
Turkey	81 entities	2005	Since 2012 reform, 51 self-governing special provincial administrations and 30 metropolitan municipalities.
United Kingdom	Intermediary : 27 county councils (England)	1889	
	Northern Ireland, Scotland and Wales	1998	Project of regionalisation in England suspended indefinitely following negative referendum of 2004.

Source: Authors' own elaboration.

3.2.1. Reasons behind regional reforms.

A **main objective is to reach greater critical mass.** In several countries, regions were established **many centuries or decades** ago when the fastest means of transport was by horse, without significant revision since then (Austria, Japan, the Netherlands, Norway, Sweden, Switzerland, etc.) (Box 30). In some cases, regions are very small in terms of population and/or geographic area, and may appear disconnected from today's realities. Socio-economic and demographic changes (migration, ageing, urban concentration) are pushed forward by reform supporters to justify a regional remodelling.

Box 30. **Some OECD regions with strong historical foundations have outdated boundaries**

Austria: Most Austrian *Länder* are centuries-old regions. Their origin can be traced back to the Middle Ages (Carinthia, Styria and Austria, which corresponds to the modern Lower and Upper Austria) or the sixteenth century (Tyrol, Salzburg, Vorarlberg). Only Vienna and Burgenland were created more recently, under the First Republic in 1920 (the constitution of the First Republic defined Austria as a federal state).

Japan: The current system of prefectures was created by the Meiji government in 1871 with the abolition of the *han* system (*haihan-chiken*). 72 prefectures were created at the end of 1871. Their number was reduced to 47 in 1888. The Local Autonomy Law of 1947 gave prefectures more political power, through the introduction of prefectural governors and assemblies. The number of prefectures has not changed since the end of 19th century.

Box 30. **Some OECD regions with strong historical foundations have outdated boundaries** *(continued)*

Netherlands: The provinces are one of the Netherlands' oldest institutions, pre-dating the 1848 Constitution. With the exception of Flevoland (created in 1986), their number and size has remained constant for centuries.

Norway: Counties (*Fylker*) and their predecessors (*Amts)* are the oldest administrative units in Norway. 12 *Amts* were established during the 1660s (replacing the earlier *Len* and *Sysler*). A further subdivision over 1671-1866 increased the number of *Amts* to 20. In 1919, their name was changed from *Amt* to county (*Fylke*). In 1972, the number of counties was reduced from 20 to 19, when the city-county of Bergen merged with the county of Hordaland. Throughout this period, some minor changes in county borders have taken place and a few municipalities have changed from one *Amt*/county to another.

Sweden: The number of counties is almost the same as it was in 1634, when they were established by the constitution, superseding the historical provinces of Sweden. Some changes occurred more recently. In 1997, the counties of Kristianstads and Malmöhus merged to create the new county of Skåne ("Skåne" being the historical name of the same territory in the Middle Ages). In 1998, three counties were amalgamated into one county called Västra Götaland.

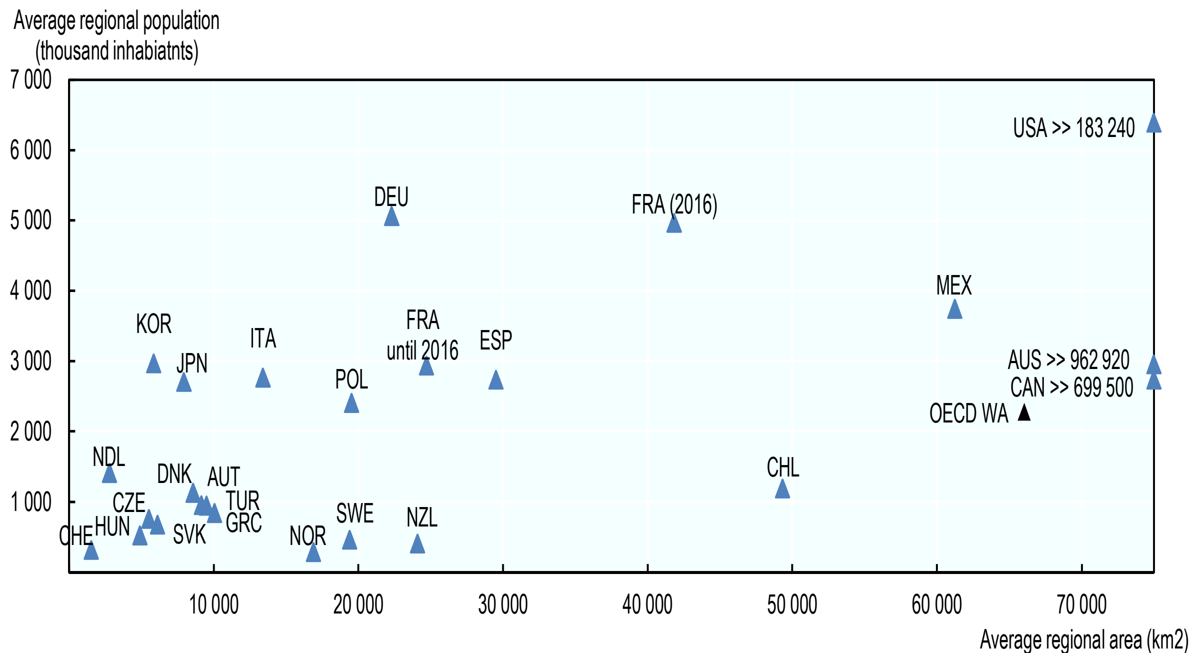
Switzerland: The majority of Switzerland's 26 cantons trace their roots back hundreds of years to the Middle Ages. The Swiss Confederation was built up in piecemeal fashion, with additional cantons joining the original three cantons of Uri, Schwyz and Unterwalden. With a few exceptions, the cantonal boundaries have remained unchanged over decades. Created in 1979 as a result of its secession from the Canton of Bern, the Canton of Jura is the most recent.

Source: Adapted and expanded from OECD Regional Outlook 2014. Various sources compiled by OECD research.

Other small regions have been established more recently and the rationale of their creation has not always been clear. In Central and Eastern European countries, for example, the creation of regions arose from the need for decentralisation and re-emergence of regional autonomy. The rationale behind regional boundaries differs from one country to another: some regional boundaries were largely based on historical regions (e.g. Poland, Hungary), others derived from previous state administrations (Slovak Republic) whilst still others were determined by EU regional policy requirements (Czech Republic). In Greece, the previous regional level (54 prefectures before the Kallikratis reform) was closer to an intermediary level than a real regional level due to the existence of a strong state territorial administration at the regional level (13 peripheries). In France, regional boundaries, established in the 1950s and reinforced by the 1982-1983 decentralisation laws, have been constantly debated. They were initially thought to be temporary and it was envisaged that the number of regions would decline to 15.

No norm or ideal size has been set for regional boundaries. There is a **great diversity of geographic or demographic regional sizes in the OECD** (Figure 7), even across federal countries: regions are large and populated in the United States; large but moderately populated in Australia and Canada; populated but small in Germany; and small both in terms of area and population in Austria and Switzerland. Among unitary countries, the largest regions in terms of population and area are found in France (since the 2015 regional reform). Regions in Korea, Japan, Italy, Poland (and France until the regional reform) have an average population of between 2.4 and 3 million inhabitants. Spain, a quasi-federation, is close to this group. Regions in Norway, Sweden and New Zealand have less than 500 000 inhabitants on average.

Figure 7. **Size of regional government in the OECD in 2014**



Note: France: without the 5 overseas regions. Belgium and the United Kingdom are not represented on the graph.

Source: Author's calculations from OECD (2016d) Subnational governments in OECD countries: Key data (brochure) – Subnational government structure and finance database: http://dx.doi.org/10.1787/05fb4b56-en.

Another motivation behind regional up-scaling can also be the **"reduction of complexity" (**simplifying inter-governmental relations by reducing the number of actors involved and simplifying public administration). This was an objective in the Netherlands, for instance (OECD, 2014b). Another goal may be **to reduce costs through economies of scale and scope**, the **pooling of resources or a reduction in bureaucracy**. Regional up-scaling is hence intended **to increase efficiency**. Increasing efficiency was a major objective in Finland and France (Box 31), as well as in Japan (where the introduction of a regional system abolishing prefectures had been debated for several years - Box 34).

Box 31. **Cost-savings and efficiency gains: A strong motivation behind French and Finnish regional reforms**

Finland: the objective of the current regional reform is to attain a greater efficiency for public services in order to bridge the EUR 3 billion sustainability gap, by up-sizing and reducing costs.

France: the regional consolidation reform took place in a context of deteriorating public finances linked to the Eurozone crisis and pressure from European authorities to introduce structural reforms. It was implemented at the same time as significant cuts in transfers from the central government to local authorities and regions, already facing budgetary challenges. Therefore, the introduction of the regional reform aims at consolidating public finance by generating savings and reaching efficiency gains. These gains should also come from an institutional reform (clarification in the allocations of responsibilities between the regions and the departments, and abolition

Box 31. **Cost-savings and efficiency gains: a strong motivation behind French and Finnish regional reforms** *(continued)*

of the general clause of competence). One report submitted to the government on June 2014 found that EUR 5.7 billion was wasted each year due to overlaps and cross-flow of funds between SNGs. Another report from April 2014 found that each region had, on average, 75 different bodies dedicated to economic development. Efficiency gains should also come from the simultaneous reform of the state regional administration. The French central government has started to adapt its own administration to the new regional map, in particular, to the creation of seven regions with entirely redefined areas (six regions remain unchanged).

Source: Authors' own elaboration.

Larger regions may also lead to **larger capacities in terms of budget, human resources and action**. According to Fitch Ratings (FitchRatings 2014), reducing the number of regions could increase the bargaining power of the larger regions and impact positively credit capacities over time. The agency considers that bigger regions with larger borrowing programmes may also be able to tap into a wider range of funding sources, for example, via bond markets and bank liquidity lines, and enjoy improved access to European development funds.

Another objective of regional reforms can be to **reduce inequalities in service provision across the country**. In Finland, this is a major goal of the current reform. The new regions will take over most health and social services from municipalities and the central government in order to improve the equity, quality and accessibility of health and social care across the territory. Therefore, a major aim of the reform is to provide people with services on a more egalitarian basis, thereby levelling out differences in health and well-being. This regional reform is part of a broader package including a reform of the health and social system.

Regional consolidation may also build stronger regions able to **compete at international and at European level,** with a more visible trademark image and the ability to build strong and balanced partnerships with other regions. Larger regions could also become stronger partners for trade and industry (in particular international businesses) and more robust administrative partners in relation to the central government and multi-level governance institutions. This was a major incentive in the Netherlands (2014 abandoned reform) and in France (where granting regions sufficient weight to engage in international and inter-regional European co-operation was a stated goal).

The need for territorial reform can also result from **institutional reforms affecting the regions** (Finland, France). As indicated above, regional reforms focusing solely on the territorial dimension are very rare. They often include an institutional aspect consisting of revamping regional responsibilities and resources, in order to build not only larger, but also stronger, regions. In France, the law establishing the new regional boundaries is closely linked to the law *NOTRe*, which clarifies and strengthens regional responsibilities.

Finally, regional reform can be motivated by reforms of **other levels of governments.** Municipal reorganisations are often the main drivers of transformation at the regional level. The increasing size of municipalities and enhanced inter-municipal co-operation affect the role of existing regions. For example, in the Netherlands, the rationale behind up-scaling was to maintain the balance between provinces and municipalities. It aimed in particular at giving provinces a clear added value in

comparison to municipalities, at reinforcing their political clout with regard to municipalities, and at consolidating the provincial inter-administrative co-ordination and supervisory role (OECD 2014b, Bos, 2010). In Finland, planned changes in the municipal landscape were met by strong opposition, and thereby created one of the major drivers of its regional reform. 18 self-governing regions will be created to replace the regional inter-municipal co-operation entities (called "regional councils"), taking over their responsibilities but also a substantial proportion of those carried out by the municipalities and the central government in the social and health sectors. In that context, the regional reform is a way of bypassing difficulties in implementing the municipal reform. It also aims at rationalising the subnational government sector and improving public service delivery, accessibility, quality and costs, while enhancing its accountability with new elected bodies. The state shall have primary responsibility for financing the counties. The existing multi-channelled financial resources will be simplified and citizens should have more freedom of choice regarding these services.

3.2.2 The issue of delimitating regions

The issue of defining new regional boundaries is highly sensitive and has sparked many debates in France since the 1950s and the same phenomenon can be observed in Finland and the Netherlands (proposals from the Geelhoed Commission, the Kok Commission or the Holland Eight).

The choice of new boundaries is restricted by several factors and it is often difficult to start from scratch. Regional geographical characteristics, social, political and cultural contexts (including linguistic specificities), and existing territorial disparities and complementarities, should be taken into consideration. **Existing administrative boundaries** (pre-existing regions, boundaries of other governmental entities at the central and local levels) must also be taken into account. In Greece, regional geographical boundaries were defined on the basis of the previous 13 regional state administrations (deconcentrated regions). In France, the law relative to the "Delimitation of Regions and Regional and Departmental Elections", which entered into force on 16 January 2015 and introduced forced amalgamations for regions, used different criteria to set the new regional boundaries. However, in order to avoid lengthy debates that could block the reform process, it was decided to merge regions "block by block" without splitting *départements*. Although this choice allowed for a greater simplicity and rapidity, it may have prevented the drawing of a truly consistent regional map. In Finland, different proposals were made and, following intense debates, the regional boundaries will correspond to those of the existing "regional councils" (Box 32).

Box 32. **New regional boundaries in France, Finland and New Zealand: Different approaches**

France: in January 2016, the number of regions in mainland France decreased from 22 to 13. A major objective of the French regional reform was to build more homogenous regions from a socio-economic point of view. Regional boundaries have been criticised since the creation of administrative regions in the 1950s. The main criterion for new regional boundaries was population size (new regions should have at least 2 million inhabitants). Regional surface areas were also taken into account, as well as the presence of a metropolitan city within regional territory, regional economic performances, and cultural cohesiveness. However, to avoid lengthy debates that could block the reform process, regions were merged "block by block" without splitting departments. There are now 13 regions in mainland France instead of 22. Six regions remained unchanged (Île de France, Centre, Pays de la Loire, Bretagne, Corse, Provence-Alpes-Côte d'Azur) and the seven new regions

Box 32. **New regional boundaries in France, Finland and New Zealand: different approaches** *(continued)*

resulted from mergers with entirely redefined areas. The new French regions are more consistent in terms of population and GDP, which also means that regional disparities tend to be lower.

Finland: several scenarios were considered, from 5 (a figure based on several economic and social criteria) to 19 regions. Finally, the approved project is based on 18 new autonomous regions, which will be based on the current map of statutory joint municipal boards (operating as regional development and planning authorities). The 18 self-governing regions whose councillors will be elected by direct universal suffrage, will be created in January 2019.

New Zealand: the Local Government Commission in charge of restructuring the organisation of local governments was not bound by the previous local structure. It could thus introduce drastic changes, as some former councils could be divided across several new entities. The Commission radically reformed the structure and functions of local governments. For this purpose, it relied on a set of "principles" enshrined in the Government Economic Statement (1987) and sent to local authorities for information and consultation. The existing 200 local authorities were replaced by 12 regional councils and 75 city and district councils (now 11 regions and 67 city and district councils). A large number of special-purpose bodies were abolished (there were 800 general and special-purpose authorities initially). Restructuring was very heterogeneous, with some local authorities remaining unchanged, while others were formed from the amalgamation of several small authorities, or by portions from larger authorities. Regional boundaries, in particular, were mainly based on the boundaries of drainage basins. However, the choice to disregard old communities may have been costly. Previous political structures often did not disappear but were transformed into boards or committees which generated animosities and impacted on the effectiveness of the reform. It has been argued that a more bottom-up approach would have generated greater public support, in particular from the historical political structures. Moreover, such a process would have helped to maintain greater identification with local communities.

Source: Authors' own elaboration.

While there is no standard in terms of size, the objective could be to **match up traditional administrative boundaries with the places where people actually live, work and socialise.** A coherent objective may be to define regions according to **social and economic functional areas, based on economic and social integration** (OECD 2013c). A functional region is a self-contained economic unit according to specific criteria (commuting patterns, water service, land use, economic development, school districts, urban and rural areas, etc.). Functional regions are well-suited to analysing how geography plays a part in production, productivity growth, the organisation of urban labour markets, and the interactions between urban and rural areas. This notion may help local governments to plan infrastructure, transportation, housing, schools, and spaces for culture and recreation. In summary, matching regional boundaries to functional areas may lead to better integration and adaption to local needs. In the Netherlands, for example, the merger of the provinces of Utrecht, Flevoland and Noord-Holland into a larger province ("North Wing Province", *Noordvleugel*) was considered in order to match the reality of the Amsterdam Functional Urban Area. This merger would have enhanced the effectiveness of spatial planning and economic development (OECD 2014b). Other mergers were also considered, taking into account the specific characteristics and policy challenges of each province. However, all of these merger projects were abandoned. In Sweden, a reduction in the number of regions to 7 or 8 has been under consideration since March 2015, so that changes in functional geographies can be taken into account. A commission was appointed, with the task of proposing mergers of counties based on

demographic developments, commuting flows and healthcare needs. The commission should present its final result by 31st August, 2017, and mergers should then start in 2019.

Regional boundaries should also correspond to regional functions and responsibilities. The consistency between regional size and responsibilities (e.g. transport, environment, health and social services, etc.) is crucial. However, responsibilities are not always taken into account when drawing new regional maps; for instance, in Finland and France, regional responsibilities were (or will be) reformed after the definition of regional boundaries. In some cases, regional boundaries and responsibilities are reformed in an iterative process – for instance in the Swedish and Norwegian current regionalisation projects. In Sweden, future regional boundaries will take into account healthcare needs, a major competence of the counties. In Norway, a white paper on regional functions should be published in 2016. This paper should introduce several proposals for consolidating counties and creating approximately 10 regions in 2020.

3.2.3. What regionalisation processes?

Different approaches have been adopted in the OECD to conduct regionalisation reforms. Even if they are often preceded by long debates and unsuccessful proposals, most regional reforms are **imposed and done in one go and rapidly to cover all of the national territory**. However, there are some examples of **uncommon processes, including bottom-up and progressive approaches.** For instance, Finland experimented with a regional government in the Kainuu region between 2005 and 2012. These atypical approaches have both advantages and limitations (Box 33).

Box 33. **Experimental approaches to regionalisation in Finland and Sweden**

Finland: considered as a test case for a possible generalisation of regionalisation to the whole country, the experiment consisted of giving extensive responsibilities to the Kainuu regional council, democratically elected for a four-year term. These responsibilities included part of those traditionally carried out by the central government and around 60% of those carried out by the 9 municipalities within its territory (as measured by costs). However, the experiment was stopped. One municipality refused to carry on, illustrating the political difficulties associated with municipal co-operation. The impact on costs savings, a main motivation behind the reform, was contested. However, the experiment may have brought other benefits, such as improvements in service availability and quality (André C. and Garcia C. 2014).

Sweden: the heterogeneous and experimental approach towards regionalisation chosen by Sweden (Box 5) has created scope for learning, fine-tuning the reform and fostering consensus (OECD 2014b). However, it has also shown some limitations. The regional governance system that emerged has become complex, relying on the co-ordination of several counterparts: county councils (with directly elected regional assemblies and dissimilar responsibilities), regional co-ordination bodies (alliances of municipalities) and county administrative boards (national government agencies at the regional level). In this context, the Swedish government decided to launch a new process for the entire territory, to merge counties and create larger regions. In March 2015, it announced the appointment of a commission in charge of investigating the creation of larger regions. The commission should publish a report before August 2017 and the first mergers should be implemented by 2019.

Source: Authors' own elaboration.

Methods to carry out regional reforms can be diverse. In some countries, the central government may choose to **control the entire process** (France). In others, it may manage the territorial reform process under the influence and monitoring of an

international body (e.g. the Troïka in Greece). It may also choose **to delegate its authority to an independent Commission**. New Zealand, in particular, chose this option to conduct its 1989 reform. The government appointed a Commission independent from central authorities (the Local Government Commission). The merger objectives were achieved by reaching across party boundaries to protect the reform process from political interference; all decisions were taken by the Commission and not by the government. The Commission consulted extensively with the civil society to build a stronger legitimacy. In particular, it worked in close co-operation with the association of local authorities (Local Government New Zealand) as well as with individual local authorities. The reform was implemented very quickly, especially regarding local government restructuring. The rapidity of the implementation and the delegation to an independent Commission were seen by many as positive for the success of the reform. It is also common in some countries to create **special committees:** "boundary committees" (England), high-level committees or ad hoc parliamentary committees, composed of multiple stakeholders and experts (e.g. Denmark, Sweden, Norway). These committees aim to consult, prepare and monitor (and, more rarely, evaluate) such reforms, in particular when they have a wide scope, encompassing institutional and managerial aspects.

Some countries decided **to simultaneously address** the territorial and institutional aspects of regional reforms (*Kallikratis* reform in Greece, current reforms in Norway and Sweden). Other countries may opt **for a time-staggered process**, the territorial reform preceding the institutional reform (or conversely). In France, the law on the delimitation of the regions (enacted in January 2015) preceded by a few months the law on the distribution of responsibilities (law *NOTRe*, enacted in August 2015). In Finland, the number of new regions was set prior to the allocation of their responsibilities and resources. However, disassociating these two aspects, especially if by a large degree, may be risky.

3.2.4. Resistance to regional reforms

Several regional reforms, consisting of either the creation of a new regional level or the up-scaling of existing regions, **have failed** over the last years - either **blocked by parliament** (Netherlands, Japan) **or the population** (Slovenia, Portugal and England). In the Netherlands, the consolidation of provinces into regions has been debated since the 1960s but never materialised. The last failed attempt took place in 2014. A two-step approach was considered: the provinces of Utrecht, Flevoland and Noord-Holland (North Wing Province) would have merged by January 2016, and a gradual bottom-up merger process would have been conducted for the nine other provinces, taking into account their specific characteristics and policy challenges. However this project was very controversial and faced resistance from provincial authorities. It threatened provincial identity, and inter-provincial co-operation to address the issue of territorial fragmentation was preferred to mergers. In Japan, regionalisation plans have been considered for decades. The prefectures are almost 150 years old, and plans for consolidating them have been discussed since 1920. The different waves of municipal mergers, which significantly increased the size of municipalities, gave a new impetus to regionalisation in the 2000s. Several discussions and studies are still ongoing but until now all projects have failed, and no reorganisation has yet been scheduled (Box 34).

Box 34. **Intense debates on a regional reform in Japan**

Under the term *doshusei,* several regionalisation projects were proposed in the 2000s but were all rejected by the parliament. A first plan in 2003 suggested creating ten regions with greater autonomy than the existing prefectures. Another proposal was made in 2006 following a recommendation of the Local Government System Research Council (LGSRC). This proposal included three models of regional organisation (9, 11 and 13 regions), with more autonomy in terms of powers and finance. The central government also set up an informal group (CLAIR) to analyse the creation of a regional level. Its first report was published in 2008. In 2014, the Prime Minister announced that the 31st LGSRC would carry out further investigations and deliberations on the future of the regional administrative system, in particular to address the issue of Japan's ageing and declining population. Several discussions and studies are still ongoing but until now all projects have failed and no reorganisation has been scheduled yet.

The abolition of provinces and their replacement with a new regional system is highly debated. Arguments in favour of regionalisation include the need to: correct interregional disparities; increase regional and local resources (prefectural functional areas are outdated); and boost opportunities for economies of scale in infrastructures and services. Regionalisation may streamline administration by reducing bureaucracy and administrative overlapping, and by consolidating sub-prefectural administrations. It may also build large regions capable of competing at an international level. Businesses and industrial organisations, critical of the prefectural administrative system, tend to be strong supporters of regionalisation reforms. On the other hand, there is also a strong opposition to regionalisation, resulting from divergences in the powers and finances allocated to the new regions. Opponents also argue that the new system would be detrimental to democracy and proximity, would further increase disparities between rich and poorer regions, would create a new layer of bureaucracy, and would undermine the sense of national unity.

Source: Authors' own elaboration.

Several regional reforms have also been abandoned after being **rejected by the population**. Citizen consultation mechanisms such as referendums (binding or not) have been used several times in the OECD, but (as for municipal mergers) they have sometimes led to unfavourable results (Slovenia, Portugal and England - Box 35). Creating a new regional government tier should be considered only when there is a clear economic and institutional rationale as well as strong citizen support (OECD, 2011). The issue of regionalisation comes up regularly in discussions and debates in Portugal and Estonia[3] but, so far, without any concrete follow-up.

Box 35. **Several regional reforms failed after unfavourable referendums**

In Slovenia and Portugal, the constitution provides for the creation of self-governing regions. However, concrete proposals were rejected by referendum. In Slovenia, low voter turnout at the referendum (10.9%) suggested limited interest in, or understanding of, the topic. The referendum proposal provided for the creation of 13 new regions (which was considered too many in comparison to the size of the country - later, another proposal considered the creation of 6 regions only). The number of new regions (13 in the project put to the public referendum which was considered as too much considering the country size, and six in another proposal), their responsibilities, and their financing were controversial. In Portugal, regionalisation failed to find legitimacy, handicapped by a lack of historical precedent and leadership. The regionalisation plan was progressively abandoned, even by its supporters, in the face of growing scepticism. Fear of regional bureaucracy and concerns about increased costs and lower democratic legitimacy were the main arguments against the reform. The number

Box 35. **Several regional reforms failed after unfavourable referendums** *(continued)*

of planned regions (eight in continental Portugal) was also considered excessive for a country the size of Portugal.

In England, a reform proposal intended to address anomalies linked to the UK's asymmetric decentralisation – Scotland, Wales and Northern Ireland have elected assemblies (albeit with varying powers), but England does not. This project would have created four elected regional assemblies in North East England, North West England, Yorkshire and the Humber. The Regional Assemblies (Preparations) Act 2003 also entrusted these new assemblies with some political powers. However, the proposal was suspended indefinitely. It was rejected during the first referendum (three other planned referendums were postponed and later dropped) held in the North-East of England in November 2004. The main reasons behind this no vote were contestation over the choice of "regional capital", the lack of convincing arguments in favour of the reform, and the fear of adding another layer of politicians, public servants and taxes.

Source: Authors' own elaboration.

Another **significant obstacle** to reform at regional and intermediate levels is strong **resistance from civil servants.** Restructuration of public services at the regional level can affect both central government officials working in the region and employees of the regional government. In Italy, the phasing out of the provinces (their functions are being transferred to the regions or municipalities) will reallocate, progressively, around 8 000 provincial staff, mainly to the regions. For instance, Tuscany (which already has 2 300 public employees) will have to absorb around 1 000 provincial personnel working in the fields of environment, agriculture, vocational training and roads. This issue has been very sensitive and may explain the slow progress made by Italian regional authorities in the implementation of the reform. However, agreements safeguarding employment have helped to facilitate the process. In France, the current regional mergers will lead to moderate changes for regional personnel. All employees will likely keep the same status, benefits and salaries but will work for the newly merged regions. Some staff receive, under certain conditions, a mobility allowance if large geographic distances are involved. Of the 27 000 civil servants employed in regional councils, between 2 000 and 3 000 will have to move. The redeployment of staff to the new regional offices will last for three years, from 2016 to 2018.

NOTES

1. In Eastern and European Countries, the democratic transition after the socialist era (which forced municipalities to merge as part of central government policy to rationalise, plan and control territorial structures) led to a deconsolidation process, i.e. a splintering of merged municipalities and in many case to the re-establishment of historical municipalities (e.g. Czech republic, Slovak Republic, Hungary). In Slovenia, in contrast to the pattern observed in many OECD countries, the number of municipalities has grown over the last 20 years going from 147 in 1993 to 2012 in 2014. Besides historical consideration, this deconsolidation is partly linked to the municipal funding formulae which tend to favour smaller and less dense municipalities. Deconsolidation is also occasionally happening in cases of amalgamations, for example, in Iceland, Norway, Sweden, or in metropolitan areas (e.g. in Montreal, merged in 2002 in the framework of a compulsory merger policy of the province of Québec which was deconsolidated in 2004 following a referendum).
2. LocRef Network, 2013.
3. Counties as a self-governing entity were abolished in 1993 and transformed into State territorial administrations. Since then, proposals have been made to restore counties at a self-governing regional level in order to relieve municipalities of some responsibilities.

Chapter 3

Political economy of multi-level governance reforms: Insights for policy

This overview of past and recent multi-level governance reforms in OECD countries, with a special focus on Finland, France, Italy, Japan, and New Zealand, confirms that **public administration reforms are sensitive and difficult to conduct**. Policy makers face a **variety of challenges,** highlighted in the OECD "Making Reform Happen: lessons from OECD countries" framework (OECD 2010a). Firstly, governance reform processes are highly context-dependent and are framed by structural constraints including countries' specific features (geography, population, economy, historical and cultural context, constitutional arrangements and organisational patterns) and political conjuncture. Secondly, multi-level governance reforms confront policy makers with the problem of "reforming the reformer" since the public administration must indeed design and implement its own reform, often imposing measures which may be contested both at central and local levels. There is an increased administrative, financial and socio-economic interdependency between levels of government. In that context, multi-level governance reforms refer to reshaping and improving vertical as well as horizontal interactions between public authorities, i.e. between central and SNGs and also within SNGs. These reforms are complex as they involve several layers of government, elected politicians and non-elected officials, as well as various other stakeholders with sometimes conflicting interests. Thirdly, gaining citizen interest and public support is often a challenge: there is usually a lack of social demand. Citizens do not notice an efficient administration but tend to lose confidence in the government and in its capacity for reform when facing inefficiencies. Paradoxically, when citizens express an interest for multi-level governance reforms, public resistance is still often observed. Reforms tend to be perceived as threats to an existing social order and as a risk of loss compared to previous situations, as witnessed by the failure of several municipal mergers or regional reforms. As a result, the development of such reforms, from planning and design to implementation, project management and sustainability, is typically very slow. Reforms do not produce instant results and need adaptation, adjustments, and the introduction of complementary reforms.

The analysis of territorial, institutional and fiscal reforms in the OECD led to the identification of several key issues and challenges, sometimes similar across countries, in the design, the implementation and the sustainability of multi-level governance reforms. OECD countries adopted diverse solutions and tools in response, some successful, others not. . This concluding part seeks to recall and underline potential strategic levers for policy makers planning to introduce multi-level governance reforms.

The main challenge of multi-level governance reform is to understand and manage efficiently the relationships and the mutual dependence across levels of governance

OECD experience shows that there is no clear-cut rationale on whether or not decentralisation should be pursued. Opportunities and risks can differ from one country to another and even more or less identical decentralisation reforms may have very different impacts depending on the country. Therefore, there is no universal consensus on the optimal structure of multi-level governance and decentralisation.

There is a strong mutual dependence across levels of government. Decentralisation outcomes will depend to a large extend on how the complex relationships between levels of government are managed, and on how different challenges (vertical or horizontal "gaps") between levels of government are bridged. In this perspective, co-ordination across and within levels of government is key. OECD experience illustrates the crucial

need to set up formal and informal mechanisms to reinforce multi-level dialogue and foster effective and efficient co-ordination, such as dedicated structures (permanent inter-governmental committees or forums) or contractual arrangements (State-Region Planning Contracts or CPER in France, Italy, etc.). Several multi-level governance reforms have taken into consideration this requirement. The crisis highlighted the strategic importance of such instruments, in particular for fiscal co-ordination. However, setting a multi-level dialogue on a permanent basis is not an easy task and may face resistance, as illustrated by the difficulty to set up a High Council of the Territories in France.

An "open-system" perspective should be adopted when designing, implementing and assessing multi-level governance reforms and decentralisation processes

The linkages between the three core dimensions of multi-level governance reforms (political, administrative and fiscal) should be considered to ensure effectiveness, in particular with respect to decentralisation. All three dimensions are complementary and interdependent, and the outcomes will depend on how the different elements of the reform are connected and interact. Two major challenges arise: finding the right balance between these three dimensions, and finding the right sequencing. Multi-level governance reforms are also a learning process and are not set in stone. Continuous adjustments are necessary to correct potential deviations.

However, OECD country experiences show that this systemic approach and adequate sequencing are sometimes poorly taken into account, leading to unbalanced processes. In particular, the fiscal dimension of reforms may be underestimated due to political, technical or economical obstacles, leading to unfunded mandates, fiscal imbalances, lack of efficiency, strong disparities and inequity across SNGs and territories. Fiscal reforms are sometimes the "weak link" of multi-level governance reforms. One key issue, also often underestimated, is that of sub-national capacity. SNGs do not always have the managerial and administrative capacity to deal with the new responsibilities, tasks or challenges (preparing merger or co-operating) resulting from multi-level governance reforms. One key component of reforms should be capacity-building before and during the reform process.

Reforms should be approached in a multi-dimensional and comprehensive way in order to avoid negative and counterproductive outcomes

Territorial or decentralisation reforms concerns both SNGs and the central government, in particular, state entities operating at the territorial level. It is thus necessary to develop parallel and co-ordinated efforts to reform both central and subnational governments, especially on the local level, to avoid potential overlapping and confusion (e.g. France, Greece). In addition, a reform targeted at one specific SNG level (e.g. municipal) often has an indirect impact on other levels (e.g. regional or intermediary), thus requiring a systemic approach to territorial reforms. Any reform may also have an impact on satellite and subordinate functional bodies attached to SNGs, which should be taken into consideration in the reform process. Finally, territorial reforms often imply institutional and public management changes, e.g. a reorganisation of responsibilities and human, technical and financial resources across the different levels of government (decentralisation or recentralisation). These changes should be anticipated and considered in advance in order to avoid potential difficulties.

"Bundling" territorial, institutional and financial reforms can facilitate reform processes

Given the strong interrelations between the different categories of reforms, closely connecting municipal reforms to territorial changes at regional or intermediary levels can make the reform process smoother. Similarly, governments can benefit from connecting territorial reforms to institutional, fiscal and public management ones, transferring new responsibilities and resources to consolidated entities (Norway, Finland, France, New Zealand, Japan, etc.). Comprehensive packages may allow losses on one side to be compensated with gains on another. In particular, opposition to a reform may be reduced by packaging it with another more popular reform. In many cases, stakeholders who stood to lose from one of these reforms can gain from other elements.

Reformers can benefit from having a clear electoral mandate for reform…

Many territorial and institutional reforms follow a series of failed attempts, or even reform reversals. Such a context may create momentum and generate pressure for more comprehensive and conclusive reforms. In that process, a decisive national election or government reorganisation can provide the occasion to launch or re-launch a national debate on territorial or institutional reforms. Several large territorial and decentralisation reforms have been launched recently in OECD countries after such changes, illustrating the importance of electoral mandate.

Government can also can "seize the moment" in times of political or economic crisis to suggest and implement multi-level governance reforms. Crises can create important reform opportunities, both by demonstrating the unsustainability of the status quo and by disrupting the interest coalitions that have previously resisted reform (Tompson, 2009). There is a strong crisis-reform link, confirmed by the wave of reforms which have taken place since the global crisis in the OECD countries, for instance in France, Italy and Finland but also in Greece or Portugal.

Strong leadership is a *sine qua non* of successful reform. This is a particularly complex issue in cases of multi-governance reforms, as leaders need to take many stakeholders with diverging interests into account: central government structures and civil servants, local and regional governments, citizens and the civil society in general. Strong leadership and political commitment to the reform are necessary to develop a clear road map and follow (often narrow) reform paths. Determination and the capacity for persuasion are crucial to discourage opponents from seeking to delay or renegotiate terms of the reform. Nonetheless, flexibility is essential in order to adapt to changing circumstances, overcome obstacles, and identify circumvention strategies. In Italy, for example, momentum for reform was conserved after the change of government by keeping the same team in charge.

Reforms often build on previous steps but also pilot programmes, experiments and place-based approaches

Institutional and territorial reforms are often carried out step-by-step or through waves, such as in France, Japan or Belgium. Sequencing can be a good approach, especially for comprehensive reforms including territorial, institutional and financial components. Each step can create an impetus for further reforms.

Pilot programmes and regional experiments (free communes experiments in Norway, Finland, Sweden and Denmark, experimental regionalisation in Finland and Sweden,

France) also represent an interesting approach, as they can demonstrate the effectiveness of reforms and pave the way for change on a larger scale. France has recently adopted this type of innovative “asymmetrical” approach with the MAPTAM law based on "recognising the diversity of territories within the unity of the Republic". This reform aims at adapting organisational structures and policies to the distinctive characteristics of territories on an appropriate scale and also authorises experimentation. Former policies have instead relied upon a uniform approach for all territories (with the exception of overseas territories). Today, France aims at allowing each territory to develop according to its own characteristics and potential, while at the same time promoting balanced development and complementarity between territories. Italy is also following this trend, as provinces and metropolitan areas will have different statuses, organisation, responsibilities and financing schemes, which will be adapted to local needs. In Finland, all 18 future new regions will not be organised in the same manner, with 15 regions being responsible for their own social and healthcare services while the last three would organise such services in co-operation with other regions.

However, this type of experimentation might have drawbacks in terms of delays and costs. These asymmetric situations may create imbalances and possible tensions (for example, in terms of political organisation, responsibilities and financial resources). Examples of such asymmetries can be found in the United Kingdom, Spain, Portugal, etc., or countries having experimented in this approach as a bottom-up or “laboratory” process (Sweden). This asymmetry may become permanent and may entail certain risks, increase co-ordination costs and, indeed, generate a need for further reforms.

The use of contracts or agreements (partnership contracts in Poland and Portugal, various forms of contracts in France, "Free Communes" in Finland, etc.) may also help local governments to implement a reform.

“Prefiguration” tools, such as inter-ministerial task forces in France in the context of metropolitan reforms, can also be an innovative and useful way to prepare transitions and ensure that all stakeholders are on board.

Overcoming opposition from local governments through co-operation and consultations, incentives and good relationships with associations of SNGs

Opposition from local politicians to territorial reforms is a major issue encountered in several countries. This generates big challenges, in particular, in countries characterised by a relatively low level of political co-operation and consensus-seeking, but even to some degree in countries with a strong tradition of political co-operation (Nordic countries). In any case, a wide-reaching consultation with local representatives starting in the early stages of the reform is helpful, as opposition from them may be a major stumbling block for the introduction of multi-level governance reforms. Such opposition could, in turn induce potentially large modifications to reform projects. In France and Italy, opposition to reforms have led to intense debates and many amendments to the initial texts of law, leading to watered down reform plans, and thereby giving rise to inconsistencies in the final reform. Decision makers should be particularly careful about this specific challenge while planning for future reforms.

In the reforms analysed, opposition tends to crystallise around changes involving a decline in the number or power of local representatives. Municipal or regional mergers, the abolition of one level of government, the introduction of greater ceilings to be met by (inter-)municipalities (for instance in terms of inhabitants), the creation of metropolises, decentralisation or fiscal reforms, all involved some opposition from local politicians.

Particularly sensitive issues include the decline in the number of representatives, the modality of election of representatives in new entities, as well as the decline in responsibilities allocated to local authorities. Each type of territorial reform tends to generate different issues. Regarding municipal mergers, the typical problem encountered is the reduction in the number of representatives due to the change from several municipal councils to only one. The creation of metropolises (or inter-municipalities in major urban areas) tends to generate political friction linked to historical competition from participating municipalities for jobs, residents and enterprises that may impede the reform process. If new metropolises have an elected board, modalities of election can be a main source of opposition from local representatives. In France, the mere existence of direct elections at the metropolis level generated opposition from local politicians as they feared they would lose in legitimacy. The transfer of responsibilities from one level of local government to another also typically generates opposition (France, Italy), and leads to (often successful) attempts by representatives to annul some of these changes. Recently in Italy, the project of abolishing one level of government (provinces) led to fierce opposition from provincial politicians and, through lobbying at the parliament, to a significant watering down the of reform and indeed ultimately to its abandonment

Beyond organising consultations, multi-level governance reforms can be facilitated by associating local governments to the reform design and implementation, through negotiations with local associations and/or ad hoc commissions, at a preliminary stage and during the whole process. Other tools can be mobilised to "compensate losers" and offer trade-offs such as temporary transition funds or mechanisms in the case of fiscal reforms, fiscal incentives, provisional guarantees or political compensation.

Associations of SNGs are essential to public administration reform processes, as these intermediation bodies regroup information and provide stable negotiating partners for the government, hence helping to reduce substantial information asymmetries and high transaction costs. In Finland, the working groups in charge of drawing up the reform included members from the two coalition government parties and from opposition parties, as well as members from the Finnish Association of Local and Regional Governments. This allowed the reform to gain wide political support, despite a change of government during the reform process. The organisation, representativeness and capacities of such bodies, and the quality of the relationships and trust between them and the government are key to the process; in contrast, their fragmentation may generate difficulties. In France, the multiplicity of associations representing the interests of subnational governments at each level and within each level, whilst mirroring the diversity and vigour of local leadership, also makes it more difficult to build consensus and to rally potentially diverging interests to uphold common positions.

Mobilising and generating acceptance from central and local civil servants through incentives, compensations and training

Territorial and decentralisation reforms affect central government structures at ministerial and territorial levels (restructuration of state territorial administration). They can be perceived as a threat in terms of power over local governments and jobs (France, Japan, Korea, etc.), and civil servants from the central government may thus prefer the status quo. As a result, central administrative "structures" and officials can resist and slow down reform implementation. To be successful, reforms should take this dimension into account and aim to change public servants' attitudes and habits through putting in place incentives, compensation mechanisms, good communication practices training activities, whilst also endeavouring to develop a feeling of "ownership" for the reforms in question.

Difficulties can also arise from local civil servants' fear of losing their jobs (for example, in municipal and regional merger situations), hence generating opposition to the reform. Specific measures can be introduced to protect civil servants’ jobs in order to alleviate this issue. This was the case, for instance, in the context of municipal mergers in Finland, where it was guaranteed that there would be no lay-offs in merged municipalities during the five years following a municipal amalgamation. France and Italy adopted the same practice during their territorial reforms, so that resistance from civil servants could be overcome.

Gaining support from civil society through information, public debates and consultations.

Reforms can be met with resistance from the civil society. Sensitive issues include, in particular, the uncertainty of final reform outcomes, a fear of losing voice or a sense of identity, or to see an increase in bureaucracy and tax pressure. For example, citizens may oppose municipal mergers because they can induce a loss of territorial identity.

Policy tools used in the reforms analysed in order to gain support from the civil society include public debates, consultation requirements and referendums. In New Zealand, the Commission in charge of the 1989 reform consulted with the civil society, and the reform itself introduced further consultation requirements. However consultation with citizens has typically been weak in most of the cases analysed, with little consultation in the early stages of the reforms in Finland, France, Italy and Japan. In the current reform process in Finland, however, large-scale consultations have been planned with all stakeholders from spring 2016 onwards.

Citizen consultation mechanisms, such as referendums, which are used to show citizens support for reform, are particularly challenging in the context of municipal mergers or metropolitan reforms – as confirmed by the Finnish and Japanese examples, but also in Norway or Iceland. In France, referendums have historically been required before municipal amalgamations, and have often led to rejecting merger projects. Defiance of politicians towards referendums in this context is so significant that a recent reform has abolished this requirement. In cases of regional or metropolitan reforms, referendums might also result in a reform being rejected, as it has been the case in the United Kingdom, Portugal, Slovenia and Japan. This reinforces the idea that creating a new regional governmental tier should be considered only when there is a clear economic and institutional rationale as well as strong citizen demand. Other consultation mechanisms may be mobilised (roadshows, consultation roundtables, conferences, e-voting, etc.) to listen to different stakeholders views. In particular, tools for sharing information with the civil society and other stakeholders may rely upon physical and virtual communication tools (including internet tools). Some countries also seem to privilege the “White Paper Process”, such as Australia or the United Kingdom (England).

Gaining political adhesion across party boundaries through experts committees

Another challenge common to several of the reforms analysed is to gain political support across party boundaries. This may be especially crucial to keep the momentum for reform going despite changes in governments. In France, for instance, initial reform plans from the previous government were extensively changed (and mostly abolished and replaced) after the new government came into place. In Finland, a lack of political consensus may be one of the reasons of the failure of the 2013 municipality reform. Parliaments have an essential role to play in this respect, to reconcile different points of

view and reach consensus between different stakeholders. Ad hoc parliamentary committees to consult, prepare and monitor reforms' progress (and more rarely evaluate) can be key success factors. However, some practices may be an obstacle to the proper implementation of multi-level governance reforms. In France for instance, the *cumul des mandats*, in which politicians tend to combine local offices with seats in parliament, led to several conflicts of interest (OECD 2007c). Its elimination in 2017 should contribute to removing a sizeable obstacle to the pursuit of multi-level governance reforms (OECD 2014e).

Approaches to reach greater political support include consultation through permanent multi-level co-ordination commission or forums, but also the reliance upon ad hoc expert advisory committees in charge of drafting the reform (these committees may or may not be independent from the central government) : the CORA group in Spain, the independent Local Government Commission in New Zealand, decentralisation promotion committees in Japan (in charge of drafting successive decentralisation reforms under different names), expert committees in Sweden, Norway, Australia, etc.

The importance of guideline documents, expertise and technical support

Providing expertise, guidelines, and technical support to local governments and stakeholders in the context of the reform can help to achieve its objectives, in particular, regarding technical aspects for which local staff may lack capacity (mergers, inter-municipal co-operation, local finance reform). An effective implementation of reforms relies on subnational government capacities, including a sufficient level of expertise. This may also improve the homogeneity of reform outcomes. In Finland, for example, structural models have been used as a basis for the design of local and regional plans.

In contrast, lack of guidance from the central government has been identified as a problem in several case studies. This was the case for instance in New Zealand concerning the technical shift to accrual accounting. The absence of guidelines from the central government was criticised and led to a too large heterogeneity in the financial documentation provided by local governments. In Finland, and despite the provision of the documents mentioned above, municipalities have expressed their desire for more guidelines from the central government to help them meet reform objectives and overcome knowledge capacity challenges.

Promoting municipal mergers and inter-municipal co-operation through diverse tools

When a municipal amalgamation reform consists of voluntary mergers, a key challenge faced by many countries is to promote amalgamations with success. Within the cases analysed, while several countries managed to carry out large-scale territorial reforms (Finland, Japan), in others only a small number of municipalities decided to merge (France).

Many policy tools have been used to promote voluntary mergers. They mostly rely on financial and political incentives but other approaches such as the introduction of a new specific status may be useful as well. The most widely used policy tool for promoting municipal amalgamations is based on financial incentives for merging municipalities (Finland, Japan, and France with the *Communes Nouvelles* reform). Another strategy employed to promote municipal mergers is the introduction of a new special status for larger cities (Japan with the "Core Cities"); there is some evidence that this strategy may have been successful in Japan.

Another incentive encouraging mergers – or facilitating their acceptance in cases of forced mergers - is to keep temporarily, or indeed definitively, the former municipal administration as a sub-municipal structure, i.e. as local deconcentrated units. Finland, for instance, introduced measures temporarily protecting representatives' positions. For municipalities merging early (over 2007-08), previous municipal councils merged into one large council, remaining in place until the 2008 municipal elections. In France, similar dispositions were introduced to gain local representatives' support within the *Communes Nouvelles* framework. In general, measures that allow a certain level of proximity to be kept, as well as local democracy through sub-municipal organisation and elected representatives, can facilitate the acceptance of the reform (Greece, Ireland, France, New Zealand, etc.).

Inter-municipal co-operation may provide an alternative to mergers or, at least a first step towards mergers. It offers a good compromise and clear benefits. Co-operation allows internalising externalities in service management, taking on functions that could benefit from economies of scale, while allowing municipalities to retain their identity and those functions that either do not require a larger scale of production or do not affect neighbouring municipalities. Diverse tools can be mobilised to promote inter-municipal co-operation. However, political, organisational and operational difficulties and risks can be significant with sometimes unclear outcomes, requiring adequate strategies during both the design and implementation phases.

Preserving homogeneity after metropolitan reforms

A recurrent issue in the context of metropolitan reforms (or mergers between larger central municipalities and smaller ones) is to avoid concentration within the central municipality and a parallel degradation of services in surrounding smaller local authorities. In the case of Japan, for instance, it was shown in several case studies of mergers that staff and infrastructures post- merger tended to be concentrated in the central municipality, and school, healthcare or public transport downsizing was typically observed in peripheral areas. There is some evidence to support this claim in other case studies as well. In France, the metropolitan reform specifically aimed to develop a "global architecture" of the territory, and the growth of cities was considered beneficial to their rural and "rurban" surroundings. However, one of the main criticisms of the reform of metropolises was that these new large agglomerations may attract all the financing, jobs, investments and economic activity in the territory in which they are located, hence having a potentially negative impact on neighbouring territories. Although the introduction of these *metropoles* is still under way in France, it is too early to assess their impact, there may be indications that this is a challenge within the Lyon area. In New Zealand, after the metropolitan reform of Auckland in 2010, some areas at the periphery have been complaining about the degradation of facilities in their territories.

None of the countries analysed in the case studies have implemented specific policy tools to tackle this issue. However, central/state governments can introduce specific financial schemes, for example, to increase equalisation and solidarity within the metropolitan area - a concern taken into consideration in France, for example. While planning for future metropolitan reforms, policymakers may consider including dispositions to preserve homogeneity and promote greater complementary and equity in the whole area.

The evaluation of reform outcomes should be promoted

The lack of evaluation of reforms, ex-ante and ex-post, is a striking common feature of most of the reforms analysed in this overview. Out of the five case studies, the only case that involved an in-depth evaluation was the PARAS reform in Finland. A five-year research programme (Evaluation Research Programme ARTTU) was established in 2007 to evaluate the reform project and its implementation. It involved, and was jointly funded by, the Association of Finnish Local and Regional Authorities, as well as 7 ministries, 7 universities, and 40 municipalities. These municipalities included merging municipalities, municipalities involved in inter-municipal co-operation, city region municipalities, and other municipalities. The ARTTU programme focused on the outcomes of the reforms in terms of finances, service provision, public servant and citizen satisfaction, etc., in merging, co-operating, and "regular" municipalities. Results from this programme should be useful in the context of future reforms in Finland.

Other examples of the above type of evaluation exist in OECD countries, such as Denmark or Iceland, but are not widespread. However, certain countries consider this lack of evaluation an important issue. Assessments may include an evaluation of reform costs, in particular, transaction costs. This type of evaluation is particularly important to avoid a reversal of the reform (except in cases where evaluation outcomes are detrimental). Reform implementation should be accompanied by regular assessments. The lack of evaluation can be addressed by creating an independent authority responsible for assessing reform progress and publishing assessments. In Austria, an independent unit will be in charge of monitoring the effective implementation of the current administrative reform. This unit will submit its reports to the parliament and the government.

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ANNEX A

Case studies: Finland, France, Japan, Italy, New Zealand

Case study 1 – Finland: from the PARAS reform to the 2015 local and regional reform

1. Brief description of the country – national context

Finland is a unitary country, with a local government system composed of 313 municipalities and one autonomous region (Aland). Finland is one of the most decentralised countries in the OECD. Local authorities are responsible for a very large share of public expenditure (41% of total public expenditure in 2014) and have wide responsibilities, in particular in the sectors of education, healthcare and social protection. Their functions include schools, hospitals, health centres, social welfare, water supply and sewage services, energy, etc. Local governments in Finland are also a crucial actor in terms of public investment, representing 54% of public investment in 2014. Apart from giving them wide-ranging responsibilities, the Finnish constitution and subsequent laws, grant municipalities a high degree of autonomy in terms of revenue and local management.

This is the result of a gradual decentralisation process. Finland has a strong and long tradition of local self-government (CoR, 2001). Local autonomy is guaranteed by the 1999 Constitution, which states that local government is founded on self-government by citizens. Several laws have been adopted to improve the local government framework, including fiscal matters. The decentralisation process was also motivated by the economic crisis of the 1980s and the need to make savings in the public sector.

Decentralisation was based on experimentations through the “Free Commune experiments” (also introduced in other Nordic countries). These experimentations permitted testing of the devolution of various functions to local governments, while increasing local discretion to influence policies (DCLG, 2006). The Free Commune Act was passed in 1988 and gave local governments the opportunity to acquire more powers. The experiment was launched in 1989 with the aim of strengthening local governmental self-rule, increasing local popular participation, adapting local governmental organisation to local conditions, using local resources more effectively, and improving local services (DCLG 2006). The experiment, originally intended to run until 1992, was extended for a further four-year period. Some measures involved all Finnish municipalities, while others were reserved to the 56 selected “free municipalities”. This experimentation served as a basis for permanent changes in legislation and in 1995 a new enabling Local Government Act gave local governments more freedom to organise their affairs, permitting greater diversity.

Over the years, the issue of municipal fragmentation has become a major concern in Finland, in a context of population ageing which generates pressure on the sustainability and quality of service provision. The population of Finland is ageing more rapidly than in most OECD countries and this is a huge challenge for pensions, healthcare and the welfare system. Municipal amalgamations, as well as the transfer of healthcare and social services to new autonomous larger regions (see below), are on the agenda in order to alleviate this particular issue.

2. Reform(s) description

The PARAS reform in Finland was a multidimensional reform, including municipal mergers, inter-municipal co-operation for service provision (in particular in the areas of healthcare and education), and better governance in urban regions. In merging or co-operating municipalities, the reform also had an impact on managerial practices (organisational restructuring, introduction of new practices, etc.). Decisions to merge or co-operate were taken on a voluntary basis.

Legislation to support the reform was enacted in 2005 and 2007 and the implementation of the first phase of the reform was planned over 2007-08. Municipalities and urban regions had to submit their reports and implementation plans to the central government by the end of August 2007. In 2008, the central government evaluated the reform progress, based on supplementary information submitted by municipalities.

The reform was implemented between 2009 and 2012. As decisions were voluntary, each municipality/urban region implemented (or not) its plans at its own pace. In 2009, the central government submitted a report to the parliament on the reform to restructure municipalities and services. At the end of the reform period, a questionnaire was sent by the central government to municipalities to find out what decisions they had taken within the framework of the reform. In 2011, amendments were made to the law regulating inter-municipal co-operation, giving the government the power to impose co-operation on the municipalities (co-management areas of social and health care) in case they could not take decisions by themselves within the time required by law.

3. Objectives of the reform(s) and key priority areas

The legislative framework for the PARAS reform was the Act on Restructuring Local Government and Services (169/2007). According to the Act, the objectives of the reform were to:

- Strengthen municipal and service structures
- Improve productivity
- Slow down the growth of local government spending
- Create a sound basis for local service provision

The Act stipulated that these objectives could be reached by three approaches:

- Merging municipalities
- Creating larger areas for service provision, through inter-municipal co-operation
- Strengthening operating prerequisites in the Helsinki Metropolitan Area and other city regions

The Act introduced quantitative thresholds to be reached for healthcare and education provision. A municipality or inter-municipality responsible for primary healthcare or associated services had to regroup at least 20 000 inhabitants. In a similar way, municipalities or inter-municipalities which were authorised to provide basic education services had to have at least 50 000 inhabitants.

4. Challenges and risks

A major challenge was to gain a broad consensus for the reform. Although most actors agreed on the necessity of reaching greater service productivity, an agreement had

to be reached on how to implement the reform. For instance, the Centre Party was traditionally in favour of co-operation areas, while other major parties such as the Social Democratic Party and the National Coalition Party were in favour of municipal mergers. Many civil servants feared to losing their position. A key challenge was to reach a consensus for the reform without making it devoid of substance.

Moreover, as municipal mergers and inter-municipal co-operation areas were voluntary, an effective implementation of the reform relied on municipal capacity. Another main challenge was for municipalities to have a sufficient level of expertise to successfully implement the reform.

5. Reform characteristics

Municipal mergers were voluntary and relied on municipal plans drawn at the beginning of the reform process. For municipalities merging over 2007-08, the previous municipal councils of merged municipalities were merged into one large council, which remained until the 2008 municipal elections.

Regarding inter-municipal co-operation (co-management areas, to reach the population thresholds set by the Act for healthcare and educations), the local authorities involved could agree that the functions of co-management areas would be conducted jointly or by one local authority on behalf of one or more other local governments.

Finally, in the Helsinki Metropolitan Area and other urban regions specifically mentioned in the Act (in particular urban regions with a growing population and economy), urban authorities had to design plans in order to alleviate problems linked to dispersion and insufficient co-operation for services, and for the organisation of transport and housing. Some municipalities also designed collaboration plans in parallel to regional plans.

6. Outline of the process

The PARAS reform was designed by the central government, in co-operation with the Association of Local and Regional Authorities. However, the real ownership of the reform is relatively unclear, which could indicate a weak leadership.

The reform relied on several tools for its implementation, including financial incentives, organisational, and consultation tools. Moreover, a five-year research programme (Evaluation Research Programme ARTTU) was established in 2007 to evaluate the PARAS project. It involved and was jointly funded by the Association of Finnish Local and Regional Authorities, seven ministries, seven universities, and 40 municipalities accepted in the programme. These municipalities included merging municipalities, municipalities involved in inter-municipal co-operation, city region municipalities, and other municipalities.

Financial incentives were used to promote municipal mergers. A merger grant was established for 2008-13; the size of the grant was determined by the population size of the merged entity and the number of merging municipalities. Moreover, the reform guaranteed that there would be no lay-offs in merged municipalities during the five years following a municipal merger.

Organisational tools were used in metropolitan areas, in the form of structural models to guide regional land use. These models were non-binding and aimed at establishing a

common framework for land use strategies in all regions. They could be used as a basis for the design of local and regional plans.

Moreover, the central government used letters of intent in order to increase the use of structural models and plans in urban regions. These letters of intent were agreements for implementing structural models, in particular, in areas such as land use, housing and transport. It is worth pointing out that these agreements were not included in the original legislation but were introduced later when a monitoring report presented to the government in 2009 revealed that co-operation had not made much progress, particularly in urban areas.

The working groups in charge of drawing up the reform included members from the two coalition government parties as well as opposition parties, and members from the Finnish Association of Local and Regional Governments. This allowed the reform to gain a large political support base, despite a change of government during the reform process. Research was carried out prior to the reform, in particular by the Government Institute for Economic Research; it pointed to the unsustainability of public finances, with projections of the rise in municipal expenditure and deficits.

Citizens were not consulted in the early stages of the reform. Referendums were used as consultation tools only in a small number (18) of municipalities. Each municipality was free to introduce (or not) a referendum.

The main policy tools used in the reform process are summarised in table 6.

Table 6. **Main policy tools used in the reform process in Finland**

Key challenges	Tools used
Creating political consensus	The working groups in charge of drawing up the reform included members from the two coalition government parties as well as opposition parties, and members from the Finnish Association of Local and Regional Governments. This allowed the reform to gain a large political support base, despite a change of government during the reform process.
Gaining support for the merger reform	Civil servants: the reform guaranteed that there would be no lay-offs in merging municipalities during the five years following a municipal merger. This helped to gain the support of trade unions. Citizens: Referendums were used as consultation tools but only in a small number (18) of municipalities. The results were not all favourable to mergers.
Promoting voluntary mergers	Financial incentives: a merger grant was established for 2008-2013; the size of the grant was determined by the population size of the merged entity and the number of merging municipalities. Local representatives: for municipalities merging over 2007-2008, previous municipal councils of merged municipalities were merged into one large council which remained until the 2008 municipal elections.
Evaluating reform efficiency	A five-year research programme (Evaluation Research Programme ARTTU) was established in 2007 to evaluate the PARAS project. It involved and was jointly funded by the Association of Finnish Local and Regional Authorities, seven Ministries, seven universities, and 40 municipalities accepted in the programme. These municipalities included merging municipalities, municipalities involved in inter-municipal co-operation, city region municipalities, and other municipalities.
Implementing organisational change in urban areas/metropolises	Structural models: non-binding documents used as a basis for the design of local and regional plans. They aimed at establishing a common framework for land use strategy in all regions. Letters of intent: agreements for implementing structural models, in particular, in areas such as land use, housing and transport. They aimed at increasing the use of structural models and plans in urban regions.

7. Gaps and obstacles

While a majority of referendums were in favour of mergers (10 out of 18), referendums could generate specific obstacles. In five municipalities, the voters were against a merger but local authorities decided to merge anyway.

In urban areas, co-operation and mergers progressed only slowly. According to ARTTU results, there was a significant lack of trust between city region municipalities, which have "historically competed over residents, enterprises and jobs". There were several disputes in regions participating in the ARTTU research; municipalities in these regions were also in competition to attract to attract home builders. Closer co-operation seems to have been impeded by a lack of political commitment.

Moreover, residents' support for the reform, as well as their perception of their ability to influence the reform process has declined over time. According to the ARTTU report, the share of residents with a negative view of mergers raised very significantly between

2008 and 2011. Moreover, residents in merged municipalities reported that their identification with their municipality weakened.

The establishment of quantitative thresholds in terms of population for healthcare and education services (see above) has been widely criticised ex-post. In urban regions, these thresholds may encourage wealthy "inner-rings" municipalities to co-operate with the central municipalities while actually maintaining their own services. This criteria may also induce "geographical blindness" and it has been emphasised that greater importance should be given to structural factors such as distances, accessibility, regionalisation and dispersion trends, etc. This explains why the legislation changed in 2011.

The central government was also criticised for a relatively low level of co-ordination across ministries, with problems of alignment for information, norms and resources.

Municipalities also expressed, sometime after the beginning of the reform, their desire for more guidelines from the central government to help them meet the reform objectives. There was a knowledge capacity challenge in many municipalities, probably enhanced by a weak leadership from the central government.

8. Reform outcomes

Mergers

In a majority of cases, mergers were not implemented: 144 mergers plans were initially drawn; of those, 77 did not lead to a merger. Only 67 mergers took place between 2007 and 2013, involving two or more municipalities. The number of municipalities in Finland declined by 111, from 431 in 2006 to 320 in 2013. Most mergers involved two municipalities but in some cases the number of merging municipalities was greater (up to 10). In 17 cases, there were successive (or chained) mergers.

Co-management

Co-management areas have been typically established either by groups of small municipalities, between small and large municipalities, or in urban regions either with or without including central urban municipalities. By late November there were 54 co-management areas for health care and associated services in Finland. Most new co-management areas (23) started operating in 2009. All of the plans for creating co-management areas were not implemented; at some point, there were 66 planned areas. Moreover, some co-management areas were disbanded as well; this was due to participating municipalities engaging in a merger, but also to a dissatisfaction of the results of the co-operation (in these cases municipalities transferred services back to their own organisations, or started new negotiations for creating a different co-management area). Co-management areas are very diverse in size and by the number of participating municipalities (from 2 to 8). Among the 54 co-management areas existing in late 2012, 21 were managed by joint municipal authorities, while a majority (33) was managed by a host municipality.

In the educational sector, a very large majority of municipalities and co-management areas reached the population thresholds for vocational education at the end of the reform period. In this sector, the PARAS reform has clearly driven collaboration. However, a joint project launched in 2006 by the Ministry of Education and Culture and education providers to ensure a sufficient structural and economic basis for vocational education and training also played a key role in this trend.

The creation of co-management areas led to significant organisational changes. In terms of healthcare, most social security and healthcare committees were disbanded, and their responsibilities and decision-making powers transferred either to the committee of the host municipality or a committee in the joint municipal authority. Overall, according to the ARTTU report, decision-making structures have become more complex and have distanced municipal and co-management areas' decision-making.

Reforms in urban areas

As mentioned above, political obstacles have been encountered in particular in urban regions, and as a consequence, the reform did not achieve a significant increase in co-operation and mergers between city region municipalities. According to the ARTTU report, "the municipality-based approach to strategy work in urban regions remains unchanged, even though collaboration in economic development, structural plans and other corresponding tools of co-operation may have opened up new perspectives to regionalism". In some cases, there were improvements in regional planning; some regions have engaged in economic co-operation and joint services.

Results from the ARTTU research

The ARTTU research evaluated the impact of the reform on the perception of service quality, economic aspects, etc. However, these conclusions are drawn shortly after the introduction of the reform, and hence do not provide any indication of the long-term impact of the reform.

Impact on municipal management and structural integration

Municipal mergers, the establishment of co-management areas and operative development in regions led to changes in their management system in a large majority of municipalities surveyed, as well as in municipal corporations. Many municipalities adopted a purchaser-provider model, some have created purchase manager positions (in particular in large municipalities), and service unit managers have often become responsible for purchases (often in smaller municipalities). Municipalities also established new budget units or centralised services across municipalities such as payroll, information management, etc. Restructuring in municipal corporations were very significant as well.

Regarding structural integration, the PARAS reform has positively impacted the integration of municipalities' social welfare and healthcare services. Nearly all municipalities participating in the ARTTU research integrated social welfare and healthcare services in a similar organisational structure, hence harmonising local service provision at the national level.

Economic impact of the reform

While the PARAS reform did not seek to cut spending but to reach greater productivity and curb spending growth (in particular in healthcare and education), economic results are not very conclusive so far.

On the positive side, the number of municipalities in deficit has significantly reduced since the beginning of the reform. This is explained by the fact that most municipalities in a difficult fiscal situation have engaged in municipal mergers.

There is so far no evidence of curbing the growth in municipal spending, in particular, in merged municipalities. This may be explained by changes in operational procedures induced by mergers and co-management, and fusion costs such as wage harmonisation, consolidating information systems, etc. In particular, investments increased more in merged municipalities than in other municipalities.

In education, operating costs have been equal in all types of municipalities; there is no evidence that merged municipalities or co-management areas achieved greater efficiency in this sector.

Moreover, municipal debt has grown more rapidly since the start of the reform. While this is probably linked to the economic recession, debt has increased more rapidly in merged municipalities than in other municipalities. This strong increase may be caused by the fact that many merged municipalities had a weaker financial situation.

Resident satisfaction

Resident satisfaction with the quality of municipal services was greater in municipalities involved in co-management areas, and lowest in merged municipalities. Over the period of the reform, the perception of service quality increased in unchanged municipalities, increased by a lesser extent in municipalities involved in co-management areas, and decreased in merged municipalities.

Factors promoting mergers and co-operation

Surveyed municipalities report that the most efficient tool to promote municipal mergers is the use of financial incentives through merging grants. Other positive factors included past experience of co-operation, trust in the decision-making of neighbouring municipalities, etc. In contrast, factors having a negative influence on the reform included divergences in municipal interests; the opinion of local residents; and local media (as municipal decision-makers face of cross-pressure from many interest groups), etc.

Other tools perceived as either helping or impeding reform are listed in the table below:

Table 7. **Municipal decisions-makers' opinions on the factors that promoted or obstructed the PARAS reform the most in autumn 2010.**

Scrutiny by PARAS categorisation

	Municipalities of a municipal merger	**Municipalities pursuing deepening co-operation**	**Other municipalities**
Factors promoting restructuring the most	Economic incentives Local government officers 'opinions Opinions of business and industry	Local government officers' opinions Opinions of business and industry Previous inter-municipal co-operation	Local government officers' opinions Opinions of business and industry Elected officials' opinions
Factors obstructing restructuring the most	Solution of other municipalities Solutions of neighbouring municipalities Municipal residents'opinions	Solution of other municipalities Stands of the local media Solutions of neighbouring municipalities	Solution of other municipalities Municipal residents'opinions Solutions of neighbouring municipalities

Source: P. Meklin, M. Pekola-Sjöblom (2013): "The Reform to Restructure Municipalities and Services in Finland: A Research Perspective", Evaluation Research Programme ARTTU Studies No. 23.

9. Next steps: towards a global reform

Failure of a new municipal amalgamation reform

The PARAS reform was rapidly followed by other plans for municipal amalgamations. Another reform to restructure municipalities was introduced in 2011, and the Municipal Structure Act took effect in July 2013. Municipalities had to prepare a report presenting the pros and cons of possible mergers, take a decision (voluntary) by late 2013, and then implement the decision. In this process, the government envisioned forced municipal mergers in situations where municipalities were in economic crisis. The mergers themselves were planned for 2015-17.

Again, financial incentives were used in order to promote municipal amalgamations, to help municipalities investigate possible mergers and to support the merger process. Several criteria were taken into consideration, such as the municipal financial situation, the mobility of work force, the ability to provide basic services in small municipalities, and the proximity to an urban area. The aim of the reform was to reach greater efficiency for public services and strengthen municipalities.

However, this reform met strong resistance and the new Finnish government, which took office in May 2015, decided to end the process and adopt an alternative strategy, based on regionalisation (see below). Several explanations have been given to explain the failure of this reform. First, there appeared to be disagreements within the government regarding the organisation of the reform: while some politicians were in favour of reforming municipal borders first, others preferred to start with a reform of healthcare structures or local functions, before engaging in another round of amalgamations. Second, the fact that mergers were only considered on a voluntary basis (hence introducing a second round of voluntary mergers in a short time) may have been inappropriate to successfully implement the reform. The proposal for forced mergers between municipalities in urban regions was turned down, hence reducing the governments' leeway. Last, opposition from local decision-makers was greater than before and thus the planning of the mergers was characterised by a low level of political energy.

A large regionalisation reform

In its programme, the new government proposed a major regionalisation reform. This reform is to be based on the creation of elected self-governing regions, which would receive healthcare and social services transferred from municipalities. A compromise concerning the main components of the reform (the number of regions and the basis of regional financing) was reached in November 2015 after vigorous debates. The reform should come into force in January 2019.

This reform is part of a larger package of reforms, built around five priority areas: employment and competitiveness; knowledge and education; well-being and health; bio-economy and "clean" solutions; and digitalisation, experiments and deregulation. Reforms include the pension reform, the social welfare and healthcare reform, cutting municipalities' costs by reducing duties and obligations, the 'Municipality of the future' project (aiming at increasing municipal authority in areas such as promoting vitality, entrepreneurship and employment, as well as encouraging municipal mergers), and regional and central government reforms (simplification of regional and central administration). Each priority area is managed by a ministerial working group, with a

designated ministry assigned to each key project. The executive is in charge of active steering and monitoring.

Regarding the reform of healthcare and welfare, the aim is to reach similar objectives as those of municipal mergers, i.e. reaching greater efficiency for public services through up-sizing; reducing costs so as to bridge the EUR 3 billion sustainability gap; and reducing inequalities in service provision across the country. The financing system should also be revised and simplified (the aim is to introduce a single-channel funding system, in contrast to the multi-channel current system). In this context, the responsibilities for primary and specialised healthcare, as well as social services and other functions (see below), would be redirected from the municipalities to 18 large new regions.

The approved regionalisation project includes the creation of 18 new autonomous regions with 15 regions being responsible for their own social and healthcare services (the last three would organise services in co-operation with other regions). There have been intense debates about the number of regions, with proposals ranging from 5 large regions to 19. Finally, in the current project, the new autonomous regions are based upon the current division of the country into "regional councils" (corresponding to the joint municipal bodies). They will be led by a directly elected regional council and will constitute a new level of government – hence, Finland would pass from one to two levels of subnational government (autonomous regions and municipalities). In parallel, the number of inter-municipal groupings (for joint service provision) should be substantially reduced.

The legislative reform package is currently under preparation and will be presented in April 2016. A consultation round will be organised in spring 2016 to discuss a draft Act on the organisation of healthcare and social welfare services, and draft Acts on autonomous regions and their financing.

The transfer of responsibilities from municipalities to autonomous regions should come into force on January 1st, 2019. In addition to responsibilities in healthcare and social protection, autonomous regions should gain functions from current regional councils, from Centres for Economic Development, Transport and the Environment (mostly regarding regional development), rescue services, etc. (around nearly 190 different designated authorities). The legislation under preparation could include a special provision for autonomous regions with insufficient resources. New regions might seek approval from the central government and provide services in co-operation with another region; the resource capacities of each autonomous region should be assessed at least every five years. The central government should have primary responsibility for financing the regions.

The new organisation of health and social services should be decided by the central government in consultation with the regions themselves. In particular, the transfer of property and personnel from municipalities and joint municipal authorities is under discussion. A national joint procurement unit, as well as a national support services bodies owned by the autonomous regions, could also be created. The central government should be in charge of steering and monitoring, and disseminating best practices.

The reform plans to reach a more efficient management of resources through an integration of basic and specialised healthcare; a better procurement system; an increase in preventative care; and a reduction in institutional care. Moreover, the introduction of new digital service solutions should also be a significant source of savings.

This reform follows that of the regional-level state administration (ALKU reform). Initiated in 2007, and implemented in 2010, it merged regional offices, concentrating them in 15 larger regions. These state regional entities will also evolve with the creation of the self-governing regions.

10. Sources and bibliography

See main bibliography (above) and internet resources below:

- http://www.nordregio.se/en/Metameny/Nordregio-News/2015/Reforms-sweeping-over-the-Nordic-countries/Why-did-the-Finnish-local-government-reform-of-2011-fail/ (accessed 10 January 2016)
- http://www.reuters.com/article/2015/11/07/us-finland-government-idUSKCN0SV2ZL20151107 (accessed 10 January 2016)
- http://www.helsinkitimes.fi/finland/finland-news/domestic/13272-years-of-work-on-care-reform-down-the-drain.html (accessed 10 January 2016)
- http://alueuudistus.fi/etusivu (accessed 10 January 2016)
- http://alueuudistus.fi/en/frequently-asked-questions (accessed 10 January 2016)

Case study 2 – France: Act III of Decentralisation and the reform of the "*Communes Nouvelles*"

1. Brief description of the country – national and historical context

France is a unitary country with three tiers of local government: regions, "departments" (*départements*) and municipalities (*communes*). Until January 1st, 2016, there were 27 regions (22 in mainland France and five overseas regions - Guadeloupe, Guyane, La Réunion, Martinique and Mayotte), 101 *départements* (96 mainland and five overseas), and 36 681 municipalities (including 129 overseas). France also has a quasi-fourth subnational level composed of 2 145 inter-municipal co-operation structures, having their own sources of tax revenues.

While local expenditure in France represented only 20.5% of public expenditure in 2014 (lower than the EU and OECD figures of 33% and 40% respectively), SNGs represented 58.8% of public investment (higher than the EU average, and similar to the OECD average). Local governments are responsible for important functions such as education, social protection, infrastructure, economic development, spatial planning, and environment.

This is the result of major decentralisation reforms in 1982-1983 (Act I of Decentralisation) and 2003-2004 (Act II of decentralisation). These reforms transferred important responsibilities and resources to subnational governments, in particular, to the newly created regions and to the departments.

In the late 2000s, several analyses were launched by the government to improve the decentralisation framework and streamline the multi-layered and fragmented territorial organisation, caricatured as the *mille-feuille*. Proposals included a clarification of the role of regions and departments; the improvement of inter-municipal co-operation, in order to alleviate the "democratic deficit" of inter-municipal groupings and to streamline the inter-municipal map; etc. The government set up a committee run by Edouard Balladur, a former Prime Minister, to analyse potential "territorial reforms". The Balladur Committee published a report entitled "*Il est urgent de décider*" ("urgent decisions need to be made").

After this consultation process, the government passed an initial law in December 2010. The law aimed at clarifying the distribution of subnational responsibilities, in particular, by suppressing the *clause de compétence générale* (general clause of competence) for the départements and the regions. It also set up a new type of elected local representative common to the regions and départements: the "territorial councillor". The "territorial councillor", who would sit both on general councils and on regional councils from 2014 onwards, was seen a way to keep the département as an intermediary subnational government level while reducing the number of local politicians, pooling resources, and putting an end to duplication. This reform was accompanied by a reform of local taxation (which led to the loss of tax autonomy for local governments, particularly for regions and départements), of equalisation mechanisms, and of co-financing frameworks. Other changes included the direct election of inter-municipal councillors, the creation of a new status of *métropole* for the largest French cities (on a voluntary basis), and the promotion of amalgamations through the *Commune Nouvelle* framework.

With the new government formed in 2012, a new stage has been set towards a fresh reform of decentralisation. The programme of the government included the abrogation of

most of the provisions of the 2010 legislation and new proposals were made to launch an "Act III of decentralisation".

As a result, the 2010 law was partly revoked (e.g. abolition of the "territorial councillor"), and the government announced the launch of a new territorial and decentralisation reform process in 2013. The government proceeded in successive phases. Laws passed in 2014 and 2015 were dedicated to the creation of *métropoles*, to regional amalgamations, to changes in subnational responsibilities, and to the simplification of inter-municipal co-operation and municipal structures through the strengthening of the *commune nouvelle* framework. This series of reforms also concerned the territorial administration of the central government.

This reform package took place in a context of deteriorating public finances and pressure from European authorities to introduce structural reforms. It implied the need to rationalise and consolidate public finances, and expressly aimed at generating savings, both at the central and subnational levels. Reforms were implemented in parallel to significant cuts in transfers from the central government to local authorities, offset, however, by a reinforcement of equalisation for the poorest areas. The objective of including local authorities in the national effort to reduce public spending has always been clear, even since the early stages of the reform.

2. Reform(s) description

The government initially planned to carry out one large reform with different sub-chapters. However, following intense debates at the parliament, a more gradual approach was adopted and several proposals were made, covering both territorial and institutional issues (boundaries and responsibilities). The final reform package consisted of three parallel reforms introduced by the government (Act III of Decentralisation), as well as one reform initiated by local representatives. Another reform of the central territorial organisation, adapting regional *préfectures* to the new regional map, was also adopted by the central government. Some major measures considered by the government, such as the abolition of départements in 2020, have been abandoned thus far due to strong opposition in the parliament (discussion is postponed to 2020).

The reforms introduced by the central government are the following:

The first law for the Modernisation of Public Territorial Action and Metropolises (MAPTAM), voted in December 2013 and published in the official journal as of January 27th, 2014 (Law No. 2014-58), creates a status of *métropoles* for the 14 largest French agglomerations, with specific powers and functions (see below).

The second law relative to the Delimitation of Regions and Regional and Departmental Elections entered into force on January 16th, 2015. It introduced forced amalgamations for French regions (Law No. 2015-29).

Last, the law for the New Territorial Organisation of the Republic (*NOTRe*), entering into force on August 7th, 2015 (law nº 2015-991), reformed the allocation of responsibilities to each level of government with an increase in the functions assigned to regions in particular.

In response to the various reforms introduced by the executive, local representatives decided to be pro-active and proposed a reform to favour local mergers. This resulted in a modification of the previous *Communes Nouvelle* reform, with the publication in March

2015 of the law relative to the *Amelioration of the Commune Nouvelle* Framework, aiming at promoting local amalgamations on a voluntary basis.

3. Objectives of the reform(s) and key priority areas

According to the government, the different reforms meet three main requirements:

Strengthening local democracy;

Ensuring the proximity and efficiency of public services while reducing the tax burden and the public deficit, in a context of strong pressure on public finances at the central and subnational levels;

Allowing each territory to develop according to its own potential, and promoting balanced development and complementarity between territories.

Objectives of the regional reform

The objectives of the regional reform were to build larger and stronger regions in order to i) generate savings and reach efficiency gains; ii) build more homogenous regions from a socio-economic point of view; iii) grant regions sufficient weight to engage in international and inter-regional European co-operation.

The creation of larger regions was seen as a way of generating savings and reaching efficiency gains; an early argument aiming at reaching savings from 5 to 10% of current spending was however abandoned during the reform process.[1] Efficiency gains were also planned from the parallel reform of the state regional administration. The French central government started to adapt its own administration to the new regional map (seven regions with entirely redefined areas, and six unchanged regions).

Another stated major objective for regional amalgamations was the building of more homogenous regions from a socio-economic point of view. The initial regional division made in the 1950s and made a reality with the 1982 decentralisation laws was strongly criticised. The author of the initial regional map himself thought that French regional borders would be temporary, and that they should have evolved towards a clustering and a reduction in the numbers of regions to around 15. Since the creation of the regions, their delimitation has been subject to many debates, in particular in the cases of Bretagne, Pays de la Loire, Poitou-Charentes and the historic Normandy region (which was divided into two regions, upper and lower Normandy).

Finally, the last objective was to constitute stronger regions, granting them sufficient weight to engage in international and inter-regional European co-operation. From this perspective, the reform also aimed at introducing a clarification, and strengthening, of regional responsibilities (although this aspect was not included in the law on the delimitation of the regions enacted in January 2015 but afterward in the framework of the *NOTRe* law enacted in August 2015). It was also perceived as a first move towards more ambitious regional development policies.

[1] This estimation was abandoned because of the high costs of the reform, which made any attempt to set precise quantified objectives somewhat risky. In fact, some critics said the reform could have even increased spending in a first step (reorganisation costs, construction of new buildings, alignment of statutory staff, etc.).

Objectives of the metropolitan reform

The objective is to improve governance in large urban functional areas in order to enhance co-ordination of public policies in key sectors (transport, economic development, spatial planning, etc.), to reach efficiency gains, to favour financial solidarity and to assert large cities' role as engines of growth and attractiveness of the territory. This reform is based on a dual strategy. First, to integrate all actors involved at the metropolis level (all local governments present within the *métropole* territory, but also central government authorities) in order to develop more coherent policies for the whole metropolis. Second, to introduce a degree of diversification across French territories: metropolises will be granted more functions than other municipalities or inter-municipalities, which is justified by their larger size and urban nature. Moreover, the larger metropolises (Paris, Lyon and Aix-Marseille-Provence) which already have a specific status since the 1982 PLM law (see above), will have ad hoc different status i.e. different organisation, responsibilities and resources. This "asymmetrical" approach is relatively new in France and it is based on "recognising the diversity of territories within the unity of the Republic" or, in other words, adapting modes of organisation and policies to the distinctive characteristics of territories and on an appropriate scale, as well as authorising experimentation. In the past, policies were instead based upon a uniform approach for territories (except for overseas territories).

Objectives of the municipal and inter-municipal reforms

The objective is to reduce municipal fragmentation in order to reach economies of scale and greater efficiency. In fact, the level of municipal fragmentation in France is one of the most significant in the OECD (average municipal size of 1855 inhabitants against 9 570 in the OECD; 86% of municipalities under 2 000 inhabitants).

In the past, this sensitive issue has not been addressed in a frontal way (via compulsory municipal mergers,) as populations are particularly attached to this level of proximity. The mayor is often the only representative of the Republic in the territory and the *commune* is the guarantor of local democracy and social cohesion, working in close connection with local NGOs. This explains why policies encouraging inter-municipal co-operation have always been preferred. In fact, inter-municipal co-operation allows for economies of scale and solidarity while ensuring proximity and respecting local identity owing to the preservation of small municipalities.

However, despite the numerous positive outcomes of inter-municipal co-operation, the way it was implemented resulted in the creation of a dual municipal layer, generating an unnecessary proliferation of inter-municipal structures and duplication of services and staff.

The perception of municipal mergers seems to evolve slowly. According to the president of the French Mayors' Association, responsible for initiating the reform, the "*commune nouvelle*" formula may be a response to the current financial context, and aims at pooling both human and financial resources.

As a result, the objectives of the current reform at local level are twofold: i) to reduce the number of inter-municipal co-operation structures while reinforcing their responsibilities; ii) to favour municipal mergers by improving the *Commune Nouvelle* legislative framework adopted in 2010.

4. Challenges and risks

Regional reform

As the regional reform will be accompanied by a change in local authorities' responsibilities, a major challenge is to reach an adequate allocation of functions to each level of government, and this without underestimating the costs induced by the changes in these functions. Another important challenge will be to provide the new regions with the necessary financial resources to perform their new role and responsibilities.

Metropolitan reforms

A major challenge of the introduction of the new *métropoles* and their strengthening is that these new large agglomerations may attract and concentrate the majority of financing, jobs, investments and economic activity in the territory in which they are located, hence having potentially a negative impact on neighbouring territories. Although the introduction of these *métropoles* is still underway and it is too early to assess their impact, there might be indications that this is effectively a challenge within the Lyon area. However, it should be recalled that the metropolitan reform specifically aimed at developing a "global architecture" or design of the territory where the growth of cities would benefit their rural and "rurban" surroundings. The reform aims at fostering solidarity and complementary between the different territories.

The future relationships between the new metropolis and their respective regions may be challenging. There is, in particular, a risk of overlapping in terms of responsibilities (e.g. economic development, innovation) and competition.

Municipal and inter-municipal co-operation reforms

The question is whether this framework will fundamentally change the municipal landscape. The topic of the municipal fragmentation in France remains a sensitive issue. For many politicians and the population, having 36 000 communes constitutes an asset for France.

Inter-municipal co-operation bodies should become the main player at the local level, reshaping the municipal landscape. However, one initial objective of the reform was to reinforce these structures by allowing direct elections of their representatives and thus reducing the "democratic deficit". This proposal did not withstand the negotiation with the Senate and was abandoned.

5. Reform(s)' characteristics

The MAPTAM law of 27 January 2014 on the modernisation of territorial public action and affirmation of metropolitan areas

Fourteen *métropoles* have been planned to this day. Eight of them were created by law in January 2015. They are referred to as inter-municipalities, with more than 400 000 inhabitants and urban areas composed of more than 650 000 inhabitants. Two of these eight *métropoles* (Brest and Montpellier) had the choice of joining the metropolitan framework. The three largest *métropoles*, Paris, Lyon and Aix-Marseille-Provence, have a different status, i.e. different type of organisation, responsibilities and resources. The *Métropole* of Lyon was created in January 2015, and those of Paris and Aix-Marseille-

Provence in January 2016. Political representatives for the *métropoles* will be elected through direct suffrage from 2020 onwards.

Métropole du Grand Paris: a new inter-municipal authority encompassing the city of Paris and three *départements* from the closer inner suburbs (Hauts-de-Seine, Seine-Saint-Denis and Val-de-Marne), will regroup about 6.7 million people across 131 municipalities.

Métropole d'Aix Marseille Provence: a new inter-municipal authority encompassing the six existing inter-municipal groupings in three existing *départements* (Bouches-du-Rhône, Var and Vaucluse), will amount to about 1.8 million people across 93 municipalities.

Métropole du Grand Lyon: unlike Paris and Aix Marseille Provence, Lyon has a special status as a metropolitan level of government, which will merge the responsibilities of the existing inter-municipal grouping of *Grand Lyon* and those of the *département du Rhône*, regrouping around 1.3 million people (the only one of its kind in France).

Each metropolis will be administered by a metropolitan council, composed of one metropolitan councillor per member municipality, plus one more councillor (for each municipality) per 25 000 inhabitants (with exceptions for Paris). For the initial creation of the metropolitan council, councillors will be elected by the municipal councils of member municipalities. They will later be directly elected from 2020 onwards. The President and vice-presidents of the council will be elected by the councillors. In addition, there will be a sub-metropolitan organisation based on "territorial councils" (*conseils de territoire*), mostly issued from previous inter-municipal co-operation bodies.

The responsibilities of *métropoles* are being extended. While the *métropoles* replace the inter-municipalities previously in place, they are granted greater functions than these inter-municipalities. These additional functions include planning for territorial cohesion, housing, and train stations. *Métropoles* also have the opportunity to take over responsibilities from the regions and/or the departments, within their territory, through conventions passed with them. For instance, it was decided that the metropolis of Lyon will take over all the responsibilities of the region (including secondary education) from 2015 onwards.

In parallel to the introduction of the metropolis, the MAPTAM law also modifies the inter-municipalities in the Ile-de-France area. An objective to reach inter-municipalities of at least 200 000 inhabitants has been stated, but has encountered a lot of resistance from local representatives, and may thus be slightly modified.

Moreover, in order to clarify the allocation of responsibilities to each level of government (although the *clause de competence générale* was shortly re-established – see below), the MAPTAM law also stipulates that each level of subnational government is primarily responsible for organising and assuring the cohesion of some responsibilities within their territory. For instance, regions are responsible for the organisation of territorial planning, support to secondary education, and research, etc. in their territory.

A Territorial Conference for Public Action has also been introduced at the regional level. Chaired by the president of the regional council, it aims at regrouping all local representatives within a region (from the region, départements, communes, inter-municipalities, etc., present within the regional territory) in order to improve co-ordination in terms of responsibilities, co-operation and communication across local actors. The Conference can result in establishing territorial agreements to delegate

responsibilities to another local government level or perform jointly some tasks in a rational and efficient way (to avoid cross-funding). It means that the distribution of responsibilities across subnational government levels can now differ from one region to another.

Last, the law introduces the ability for the central government to delegate responsibilities to any local authority (including inter-municipalities) that asks for greater functions. Such delegations of responsibilities have to be decided at the central level and formalised within a decree and a convention between the central government and the local authority.

The regional reform

Change in regional boundaries

In January 2016, the number of regions decreased from 22 to 13 regions in mainland France. Seven regions have entirely redefined areas. Generally, two regions merged but there was an instance of with the merger of three regions. Six regions remained unchanged. The main criteria for delimitating the new regions was population size (there is no region under 2 million inhabitants), the surface area, the presence of a metropolitan city, economic vitality, and cultural cohesiveness. It was decided to merge regions "block by block" without detaching *départements* to avoid further difficulties. *Départements* within regions have a theoretical possibility to switch from one region to another between 2016 and 2019, but in practice the conditions to do this in practice are harsh and hence it seems highly improbable.

The first regional elections took place in December 2015. The number of regional councillors remained unchanged. The regional councils of the newly amalgamated regions will have to decide on the name of the new region and its capital before October 2016. There have been a few exceptions to this rule; the merger of the regions Champagne-Ardenne, Lorraine and Alsace, for instance, led to strong discontentment of local representatives of Alsace and it was subsequently decided that Strasbourg would become the regional capital.

Last, it is planned that from 2018 onwards, Corsica will become a local authority with special status, in place of the Territorial Authority of Corsica, and the *départements* of South Corsica and High Corsica (which will merge).

Another major change introduced by this law is the abolition of the obligation for merging local authorities to conduct a local referendum.

Clarified and strengthened regional responsibilities (NOTRe law)

The general clause of competence, deemed to generate overlapping and duplication of spending (Box 36), was abolished for the regions (and the départements) while it is maintained for the municipalities. It means that they are now confined to exercising the powers granted by the law.

The Law *NOTRe* defines the responsibilities for each level, resulting in a strengthening of the regional responsibilities while the départements lost several functions transferred to the regions, such as school and inter-urban transportation (but less than initially planned in the first version of the law as departments finally keep secondary schools and roads. In addition, regions may choose to delegate school transportation back to departments). The département remains the competent community to promote social

solidarity and territorial cohesion, having a major role of supporting rural municipalities and intermunicipal groupings with fewer capacities (expertise and technical assistance). In particular, regions gained greater responsibilities and powers regarding regional economic development, and will be in particular the only body responsible for defining aid schemes to small and medium enterprises in the region. Regions will also be in charge of territorial planning and environment protection planning. Regions now also have a regulatory power allowing them to adapt national legislation to the local context.

Box 36. **The issue of the general clause of competence or "subsidiarity principle"**

The *Clause de Compétence Générale* in France is a provision that allows local authorities to be active in all areas. This means that there is no strict delimitation of responsibilities across levels of sub-national governments; while some functions are allocated to specific levels of governments by law, each local authority can choose to provide other functions in addition.

This clause, initially introduced in 1884 for municipalities only (municipal law), was extended to départements and regions in 1982 (decentralisation law). It has been strongly criticised, as it may generate duplication of spending, as well as create greater inequalities in service provision across the country. The costs associated to this additional spending are estimated to be large. For instance, a report by Queyranne, Demaël and Jurgensen (2013) estimated excess spending linked to overlaps and cross flows of funds between SNGs to EUR 5.7 billion. Lambert and Malvy (2014) found that that each region had an average of 75 bodies in charge of economic development.

The clause was initially abolished for regions and départements under the previous government with the 2010 territorial reform. However, the MAPTAM law enacted in January 2014 reintroduced it before it was again abolished by the *NOTRe* law enacted in August 2015 (municipalities are still concerned by this provision).

This (re-)deletion of the clause for regions and départements aims at clarifying the allocation of functions assigned to different levels of subnational government ensuring a more intelligible territorial organisation. It allows avoiding duplication of actions and contributes to more transparency and accountability for citizens Municipalities will remain the only local level which benefits from the general clause of competence. It gives municipalities explicit freedom to act in the best interests at local level, allowing them to respond to the day-to-day needs of local citizens.

Source: Authors' own elaboration.

New planning requirements have been introduced for regions. Regions will have to draft a regional plan for economic development, innovation and internationalisation (*schéma regional de développement économique, d'innovation et d'internationalisation* or SRDEII), to set strategic objectives over the next five years. Regarding territorial and environmental planning, regions will have to publish regional plans for sustainable territorial development (*schéma régional d'aménagement, de développement durable et d'égalité du territoire* or SRADDET) covering subjects such as territorial planning, transport, air pollution, energy, housing, waste management, etc. These schemes replace all other existing ones. The novelty is primarily due to their mandatory and prescriptive character vis-à-vis the decisions of other authorities. It means that authorities shall take into account the general guidelines of SRADDET in the development of their own planning document (e.g. SCOT). The same applies for the SRDEII, except concerning the metropolises. Metropolis obtained derogation on this point allowing them to adopt their own policy document in case of disagreement with the Region. They will have only to take into account the regional scheme and will not have to comply.

Municipal and inter-municipal co-operation reforms

This law modifying the *commune nouvelle* framework, passed in March 2015, aims at introducing voluntary municipal mergers through the modification of the previous *Commune Nouvelle* reform of 2010. Under this framework, the status of "associated municipalities" allows merged municipalities to remain and retain some particularities such as a delegate mayor, a town hall, an advisory council, etc. In response to the failure of the 2010 reform (only 12 merger plans were carried on over 2010-15, a small number compared to the more than 36 000 municipalities in France), the rules for the creation of these new municipalities have been relaxed. Moreover, strong financial incentives for small municipalities creating *communes nouvelles* were introduced (see below).

Merging municipalities must belong to the same inter-municipality. The new rules aim in particular at reducing opposition from local representatives: each mayor from the pre-merging municipalities will become a deputy mayor in the amalgamated municipality, there is greater flexibility regarding the composition of municipal councils over a transition period, etc.

The *NOTRe* law also aims at reinforcing inter-municipalities. They will be organised around functional areas. The minimum population threshold for inter-municipalities will pass from 5 000 to 15 000 inhabitants (20 000 in a previous version), to be attained before 1 January 2017. Exemptions were introduced to adjust to the diversity and reality of specific territories (sparsely populated areas, mountain areas, recently merged groupings and islands). All municipalities will have to integrate an inter-municipal co-operation structure, on a compulsory basis. The number of inter-municipal syndicates (single or multi-purpose and without taxing power) will also have to be reduced.

To clarify the distribution of responsibilities between the inter-municipal structure and its member municipalities, departmental schemes for inter-municipal co-operation will have to be prepared in 2016, including an inventory of the distribution of responsibilities of existing groups. IMC will be strengthened, as municipalities will have the obligation to transfer some additional responsibilities to their "communities of municipalities" and "town communities".[2] These responsibilities include water provision and sanitation, waste, tourism, reception of travellers, commercial activities, and other optional responsibilities have been added by law (e.g. creation of public services centres). The transfer of responsibilities regarding economic development, however, is no longer considered. In addition, provisions for pooling services and personnel have been improved by law to avoid duplication.

6. Outline of the process

There has been little formalised consultation with the civil society in the design implementation of these reforms, except in some cases (e.g. metropolitan reforms). The suppression of mandatory local referendum for local mergers shows a certain defiance towards public consultation regarding territorial reforms. This may be linked to previous episodes where such referendums showed opposition of local residents to mergers (in Alsace, Corsica, Guadeloupe). Large consultations with associations of local governments took place. However, the multiplicity of such associations in France,

[2] As far as urban communities and metropolis responsibilities are concerned, they have already been reinforced by the MAPTAM law in 2014.

sometimes defending diverging interests, may be an obstacle to reach a consensus and facilitate the reform process.

While the central government has kept a fundamental leadership role, it has adopted a less top-down approach than usual in the case of the reform of metropolises. In this particular case it has adopted a role of arbitrator, assuring co-ordination across local actors involved. In the case of Paris and Aix-Marseille Provence, a new approach was adopted through the creation of an Inter-ministerial Task Force for the Metropolitan Project, in charge of implementing the reform in a transition phase. The two task forces (headed by the respective prefects, who represent the central government) are responsible for implementing the transition and gaining support from all stakeholders (citizens, local authorities, the private sector, and civil society). In the case of Aix-Marseille Provence, this task force is composed of national civil servants and experts, seconded by partners (municipalities, chambers of commerce, the port, and other public enterprises), and seeks to launch the metropolitan authority and prepare the substance of its strategic role (OECD, 2013).

Regarding the *Communes Nouvelles* reform, financial incentives were introduced to promote municipal amalgamations for municipalities merging before January 1st, 2016. These incentives take the form of the safeguarding of transfers from the central government in a context of large cuts in transfers to non-merging municipalities. Amalgamated municipalities are also guaranteed to receive the sum of the main transfer from the central government (*Dotation Globale de Fonctionnement*, DGF) of all former municipalities. Moreover, for merged municipalities of greater sizes, the DGF will be enhanced over three years ("Financial Pact").

The table below summarises the main policy tools used in the reform process.

Table 8. **Main policy tools used in the implementation of the reform**

Key challenges	Tools used
Gaining political support	Reform of the regions: regarding the merger of the regions Champagne-Ardenne, Lorraine and Alsace, following a strong discontentment of local representatives of Alsace, it was decided that Strasbourg would become the regional capital. Municipal mergers : each mayor from the pre-merging municipalities will become a deputy mayor in the amalgamated municipality; there is greater flexibility regarding the composition of municipal councils over a transition period; etc.
Promoting voluntary mergers	Financial incentives: financial incentives were introduced to promote municipal amalgamations for small municipalities merging before 1 January 2016. These incentives take the form of the maintenance of transfers from the central government during three years for the new municipality, in a context of large cuts in transfers to non-merging municipalities. The new municipality must be under 10 000 inhabitants. Amalgamated municipalities are also guaranteed to receive the sum of the main grant from the central government (Dotation Globale de Fonctionnement, DGF) of all former municipalities. There is a bonus of 5% of the same DGF if the new municipality group more than 1 000 inhabitants (while remaining always under 10 000 inhabitants in order to avoid larger municipalities engaging in a subsidy race).

7. Gaps and obstacles

The main obstacle met by the different reforms was a strong opposition from local elected representatives and representatives of the parliament (in particular the Senate), which led to modify the initial reform projects. The intense discussions at the parliament from 2013 to 2015, and during the process of passing legislation between the two chambers, led to adopt many amendments that significantly changed the initial governmental proposals. This reflects the vitality of French representative democracy allowing reconciliation of different points of

view to reach consensus. However, it also illustrates the negative impacts of the *cumul des mandats*, a French particularity in which politicians tend to combine local offices with seats in parliament. This practice may be an obstacle to the proper implementation of decentralisation, especially because it may lead to conflicts of interest (OECD 2007c). Its elimination in 2017 (law enacted in February 2014) should contribute to remove an important obstacle to the pursuit of multi-level governance reforms (OECD 2014e).

Another obstacle is the high number of associations representing the interests of subnational governments at each level (regions, departments, municipalities, inter-municipal co-operation bodies) and within each level (metropolis and large cities, medium-sized towns, small towns, rural municipalities, mountainous municipalities, etc.). Although it mirrors the diversity and vigour of local leadership, it makes it more difficult to build a consensus among subnational governments and to rally potential diverging interests to uphold common positions.

In particular, the abolition of one level of government (départements) mentioned at some point by the executive has been abandoned so far, with discussions reported to 2020. Moreover, while the initial reform consisted in one coherent text of law, following political opposition it was divided in three, plus an additional text on the reform of the regions. This disconnection made the reform process riskier and more complicated, as region boundaries were drawn without having information on regions' responsibilities, still under discussion.

The Senate (composed of many mayors and local councillors) modified the responsibilities initially transferred to regions; functions related to junior high schools, road transport, and road networks, which were supposed to be transferred from departments to regions, will remain at the level of département.

Opposition from politicians has also been high regarding the election processes associated to the new territorial entities. For instance, the fact that councillors in *métropoles* will be elected from 2020 onwards has been strongly criticised by local representatives, in fear that the representatives of each municipalities composing the *métropole* would lose some legitimacy and power. In the case of the Paris, opposition to the modality of elections of the metropolitan council led some representatives to refer the issue to the Constitutional Council in July 2015, leading to changes in the initial project. In the case of the metropolis of Aix-Marseille-Province, local politicians have also criticised the modalities of elections (they considered that too many seats were granted to Marseille in comparison to other municipalities), and seized the *Conseil d'Etat* on this matter.

As far as inter-municipal groupings with own-source tax (EPCI) are concerned, the principle of direct elections of their members before January 1st, 2017, aimed at reducing the "democratic deficit" and which would have had a major impact on the smooth reconfiguration of the municipal landscape, has not withstood the negotiation with the Senate and was abandoned.

In addition, the first bill provided for the creation of a High Council of Territories. This forum, headed by the Prime Minister, aimed at establishing a permanent multi-level governance platform for dialogue between government and local governments, but was rejected in the last version of the text by the Senate.

Overall, the large amount of pressure generated by local representatives and all the related changes made to the initial reform projects following parliamentary debates and

amendments, may have led to a loss of clarity in the reform, and to lower, in some cases, the reform outcomes compared to their initial objectives.

8. Reform outcomes

At this stage, it is difficult to analyse the outcomes of these different reforms. They are very recent and are still in the implementation phase. In addition, some steps are planned over the next years.

The new incentives for the creation of the *Communes Nouvelles* (and in particular the financial incentives described above) seem to be quite effective, even if they have not changed fundamentally the municipal landscape. The number of amalgamation projects was greater than for the 2010 reform. On January 1st, 2016, 308 new municipalities were created, resulting in the elimination of 1 019 municipalities. In fact, many of these *communes nouvelles* come from previous inter-municipal co-operation structures. This reform has created an awareness of municipal fragmentation and started a rather positive movement. Financial incentives will be renewed in 2016.

Regarding *métropoles*, eight *métropoles* were created by law in January 2015 but the planning of their future organisation is still underway, and an analysis of the outcomes of the reform will only be possible at a later date. Changes may be more significant and challenging for Paris and Aix-Marseille than for Lyon and the other *métropoles*, which already had the status of “urban communities” (*communautés urbaines*) since 1966 (for them, the main changes is the enlargement of responsibilities as their area should not evolve). The effective implementation of Grand Paris and Aix-Marseille still raises great challenges because of strong local resistance. Indeed, it has already given a rise to administrative appeals in the case of Aix-Marseille-Provence: in January 2016, the Marseille Court of Justice cancelled the election of the head of the newly created metropolis. This state should be transitory however, and should be settled by a decision from the Constitutional Court.

Changes introduced by the reform of the regions and the *NOTRe* law will only take place from 2016 onwards, and there are no outcomes so far. Regions should be strengthened but not as much as initially planned, as the *départements* remain relatively untouched, with most of their responsibilities being confirmed.

9. Next steps

The implementation of the metropolitan reform, which has just begun, is as crucial as the content of the reform. The effective implementation of Grand Paris raises great challenges, related to the future relationships between the new metropolis, the city of Paris and the Region Ile-de-France. There is in particular a risk of overlapping in terms of responsibilities (e.g. economic development) and competition, due in particular to the derogation obtained by the metropolis concerning their compliance to the regional plan for economic development, innovation and internationalisation (SRDEII). The relations between the metropolis and the central government, still in charge of important responsibilities at the level of the metropolitan area (e.g. *Société du Grand Paris* in charge of building the automatic metro), can be also a source of tension.

The metropolitan reform must seek to avoid reigniting conflicts in the metropolitan area. The decision to keep the *Conseils de territoire* (previous inter-municipal co-operation bodies) has introduced an additional level of complexity, as it created an intermediary level between the municipalities and the metropolitan body. This should be closely monitored in the future.

Regarding regional amalgamations, as they will have consequences on the organisation of regional bodies, a process of evaluation and re-organisation has been started in regions concerned by the mergers. The key challenge of regional financing remains: regional financial resources should be adapted to the new responsibilities, in a context of reduction of central government's transfers and reform of the main general-purpose grant (DGF – *Dotation Globale de Fonctionnement*). One concern for the regions is the future of their taxation system. In June 2015, the government announced a doubling (from 25% to 50%) of the share that regions receive from the CVAE (*cotisation sur la valeur ajoutée des entreprises*).

The future of the *départements* over the medium term remains uncertain and the different hypotheses of their possible transformation are still valid. Discussions concerning the future of the departments, in particular in urban areas, are postponed to 2020.

In parallel to reforms concerning subnational government levels, the central government has started to adapt its own administration to the new regional map. In addition, the central government launched in a Review of State Missions in September 2014, aiming at identifying key public expenditure to be prioritised in a context of declining public spending. Although it has been presented as independent from the territorial reform, it introduces a review of expenditure at all levels of government, and may have impacts on local spending in the future.

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Case study 3 – Italy: from the 2009 fiscal federalism reform to the 2014 metropolitan and provincial reform

1. Brief description of the country – national context

Italy has three tiers of local government, including 8 047 municipalities, 107 intermediary governments (provinces and metropolitan cities), 20 regions (15 ordinary regions and 5 regions with special status) and two autonomous provinces (Trentino-Alto Adige / Südtirol and Trento and Bolzano / Bozen). Special status regions have wider powers (including greater financial autonomy), as a result of their multi-lingual status and location on the national borders. Although Italy is formally considered as a unitary country, it has evolved towards more federalism over the last decade, in particular, through the constitutional reform of 2001 and the fiscal federalism law of 2009. It is now considered as a regionalised unitary country. Subnational governments were responsible for 28.7% of total public expenditure in 2014, and 54.9% of total public investment.

Subnational responsibilities include several key expenditure areas. Regions are responsible for healthcare (60% of their budget), transport, town and country planning, etc. Municipalities' responsibilities include town planning, social housing, local police, local public transport, road maintenance, etc. Healthcare in particular represents the bulk of subnational government spending (47% in 2014). Provinces, which have been transformed into inter-municipalities bodies with the 2014 reform and may be abolished in the years to come (see below), were in charge of transportation, roads, environmental protection (sewerage, waste disposal, etc.), territorial management, etc. - until 2014.

The reform takes place in a context of greater decentralisation and changes to the intergovernmental framework in Italy over recent years. In particular, in 2009, relations between levels of governments, as well as the functions of SNGs, were reshaped through a framework law (Law No. 42). This aimed at increasing the efficiency and accountability of SNGs and enhancing the level of public services across the country.

This fiscal federalism law No. 42 of 2009 (implementing the article 119 of the Constitution) set a milestone for Italy in its gradual move towards decentralisation and federal institutions. It focused on fiscal matters but also included several various other components (transfer of state property to municipalities, legal status for *Roma Capital*, definition of services standard costs). In fact, the objectives of the reform were to increase the fiscal autonomy of subnational governments, increase both the efficiency and accountability of SNGs, and ensure adequate levels of subnational services across the country. It included several elements: i) spending responsibilities should be covered by own taxes or by shares in national taxes, resulting in the replacement of a portion of central government grants by tax revenues; ii) spending obligations should be clarified, i.e. a distinction should be made between compulsory services and all other services. For these compulsory services, minimum standards should be defined by the central government (for the others, SNGS are free to set their own standards and spending levels; iii) Review of the equalisation system, with the introduction of a new system based on covering the costs of essential public services and equalising tax-raising capacities. iv) a process for harmonising accounting principles across regional and local governments was started (Blöchliger and Vammalle, 2012).

However, as in the previous cases, Law 42 set down the principles for reform but left their implementation to a set of 8 legislative decrees (and around 70 concrete measures)

which were expected to be adopted before 2016. The implementation process has been slowed down by the economic and public finance crisis. All decrees were adopted in 2010 and 2011. However, due to the 2008 global financial crisis, the central government started to cut revenues and expenditure at the local level (as well as the central level). The reform of the Italian provinces in particular is directly in line with this trend (see below), although the abolition of this intermediary level has been on the table for several years.

2. Reform(s) description

Italy is carrying out major territorial and institutional reforms. These reforms initially contained two major components. First, they established the transfer of responsibilities from the provinces to regions and municipalities. The aim was to completely abolish provinces through a revision of the Constitution (as provinces are enshrined in the Constitution and cannot be abolished directly); in the meantime, provinces would keep some transitory functions. After many changes to the initial projects of law (see below), provinces have been transformed in inter-municipalities, non-elected directly, and cannot be considered as a level of government anymore; their complete suppression through a modification of the Constitution is still on the agenda.

The second major aspect of the reform was the creation of metropolitan cities, which correspond to the territory of the provinces in which the city is located.

3. Objectives of the reform(s) and key priority areas

The reform of the provinces is not new in the agenda. It has been a recurring debate, as Italian provinces were established by Napoleon Bonaparte on the model of French *départements,* and are thus considered as obsolete. The main initial objective of the reform of the provinces in 2011 was directly linked to the consolidation of public finances. The first decree-law planning for the abolition of provinces was passed within Mario Monti's *Salva Italia* decree, which introduced measures to cut public spending by EUR 13 billion, and increase public revenues by EUR 17 billion to restore public finances in the context of the European financial crisis.

Regarding metropolitan cities, the objective of the reform was to stimulate the emergence of inter-municipal co-ordination in the major metropolitan areas, in particular in the areas of strategic planning, service delivery, and managing infrastructure and communication networks across the whole metropolis. The introduction of metropolitan cities is seen as a way of introducing integrated service delivery and planning at the metropolitan level, hence reaching a greater quality of services and better cohesion across the cities composing the metropolis.

This reform of metropolises, proposed by the central government, gave a new momentum to metropolisation in Italy, after failed attempts over several decades. In 1990, a law was passed offering the possibility for ten large Italian cities to become "metropolitan cities" and gain additional responsibilities. The implementation of these measures relied upon the enactment of regional laws, with a provision stipulating that the central government could intervene if these laws were missing. However, regions often were against the reform, and no serious action was taken either by regions or the central government to introduce "metropolitan cities". The few instances of local attempts to establish *città metropolitane* remained unsuccessful (e.g. Bologna in the 1990s, Rome and Turin in the 2000s). As a special case, Rome was given different responsibilities from

all other Italian municipalities in Law No. 42/2009, Art. 24 (*Roma capitale*). Hence, in 2012, the central government decided to tackle this issue directly, and presented a draft law in 2013 creating *città metropolitane*, which would leave no possibility for the regions to oppose it. The implementation of metropolitan cities will be supported by the national operational programme for Metropolitan cities (PON Metro) within the 2014-2020 EU Structural Funds programming.

In parallel to these reforms, other measures regarding municipal mergers and inter-municipal co-operation were taken in Italy. Municipal mergers are promoted by incentives such as state and regional financial incentives.

Moreover, following the Law 56/2014 on Municipal Unions, participation to municipal unions has been made mandatory for municipalities with less than 5 000 inhabitants. These municipal unions (inter-municipalities) must reach a minimum of 10 000 inhabitants (3 000 in mountainous areas) and co-operative functions have been extended, to now include all basic municipal functions.

4. Challenges and risks

As the reform initially envisaged a direct abolition of the provinces, provincial representatives would clearly lose from its implementation, and fierce resistance from provincial politicians was to be expected. Even the watered-down reform proposals (see below) planned for a much reduced number of representatives at the provincial level, and for a suppression of compensation for provincial council members.

Opposition to the reform among provincial representatives was indeed very strong. This led to several delays, watered-down reform proposals, and even at some points, the total abandonment of the reform. Details on the obstacles encountered are given below.

5. Reform(s)' characteristics

After a long and difficult legislative process (the law was cancelled by the Constitutional Council), the Italian Parliament finally passed Law No. 56/2014 in April 2014. This law set a roadmap (up to 31 December 2014) to establish the *città metropolitane*. In an effort to avoid the vexed question of how to identify the boundaries of those metropolitan areas – which had proven to be a major obstacle to the emergence of metropolitan structures in the past – the government decided to take the territories of the corresponding provinces. However, it left to each territory the freedom – and responsibility – to decide the depth and breadth of inter-municipal co-ordination. The law also provided for the possibility of changing provincial boundaries and of striking specific agreements between the metropolitan cities and individual contiguous municipalities or clusters of municipalities. Nonetheless, the complex political-administrative procedure required in order to expand the boundaries of metropolitan cities may be regarded as an obstacle discouraging this option (OECD, 2015).

Each metropolitan city should have a president, represented by the mayor of the area's primary city. Metropolitan cities have as general institutional purposes:

- Strategic development of the metropolitan area
- Promotion and integrated management of public services, infrastructure and communications networks of interest to the metropolitan city

- Institutional relations, including those with municipalities and metropolitan areas in Europe.

The abolition of the provinces will be based upon the results of a referendum planned for 2016 (see below).

6. Outline of the process

The abolition of Italian provinces was first envisioned in six projects of law examined in May 2009 at the Assembly. These projects did not gather a large support base: discussions were suspended in October 2009, resumed in January 2011, before ultimately being abandoned in July 2011. However, the context of economic turmoil and pressure on governments' finances in Europe, and in Italy in particular, gave a new momentum to a territorial reform, met (again) by political reluctance. Political lobby led to watered-down propositions, encompassing fusions of provinces rather than their abolition.

A first decree-law passed in December 2011, aiming at reducing overall government spending and increasing public revenues. An article of this decree was devoted to provinces; provincial governing bodies were limited to ten members, with their legislative and executive structures merged, and no longer directly elected (they were elected instead by the mayors within each province's jurisdiction). Moreover, provinces lost most of their responsibilities, which were transferred either to regions or municipalities (as well as their staff); the only remaining competence was co-ordinating municipal activities. Provinces were not abolished through this decree as, since they are enshrined in the Constitution, a constitutional revision was necessary for their suppression. Modifications to the Constitution to this end were envisioned.

Opposition to these changes was strong, in particular from provincial politicians. Political pressure led to the publication of a series of three decree-laws between July and November 2012, which significantly watered down the modifications induced by the first decree. In particular, provinces regained some important functions such as roads, territorial planning, transportation, etc. The abolition of provinces was no longer considered, but replaced by eventual amalgamations (the number of provinces would be cut from 86 to 51 and the provinces must have reached at least 350 000 inhabitants or 2 500 km^2.), and, in some cases, by the transformation of provinces into "metropolitan cities". However, the governing bodies of provinces remained significantly smaller than previously, and non-elected.

In particular, the third decree stated that members of the provincial councils would no longer receive any compensation for their work. It also included the first organisation principles for the delegation of some responsibilities from provinces to municipalities. However, following a change of government in late 2012 (see above), these changes were never translated into a law. Recourse in front of the Constitutional Court also led to the abolition of all articles approved by law (see above).

However, the new government led by Enrico Letta, as well as the following government led by Matteo Renzi, was also in favour of a territorial reform, so the momentum for reform remained. The reform process remained purely top-down, being entrusted to Enrico Letta's Minister for Regional Affairs, Graziano Del Rio (who remained in charge of the reform after the change of government) and who benefited from the strong support and leadership of Matteo Renzi on this topic. A project of law was approved by the Assembly in December 2013, in a similar line as before – including changes to the repartition of functions, metropolitan cities, etc., as well as the project of

the abolition of provinces through a revision of the Constitution. It also included a new framework for inter-municipal co-operation. This project of law was slightly amended in February 2014 and the law was finally passed in April 2014.

The latest planned modifications to provinces and regional responsibilities corresponds to a Constitutional reform approved by the Senate in October 2015, which should be subject to a referendum in 2016 (see below). This reform could suppress the provinces from the Constitution, a condition required in order to abolish them.

Moreover, the revision of the Constitution will lead to significant changes in the allocation of responsibilities between the central government and ordinary regions. Shared expenditures between regional and central governments would be suppressed, and many responsibilities would therefore have to be distributed between responsibilities allocated exclusively to regions and responsibilities allocated exclusively to the central government. This aims to avoid the duplication of services. For instance, the central government would gain exclusive competence regarding transport networks. Moreover it would gain new responsibilities such as the co-ordination of public finance and taxation, the standardisation of public sector labour rules, etc. Regions would gain exclusive responsibilities in all matters not explicitly allocated to the central government, including regional planning, the organisation of sanitation and social services, the organisation of support to companies and vocational training, etc. Regions should gain more autonomy from the central government, with the condition that their budget remains balanced.

Both ordinary and special regions will be in charge of participating in the different phases of the EU decision-making process. The financing of both regions and municipalities should be based on standardised indicators of costs and financial needs.

The Constitutional review should also introduce a “supremacy clause” enhancing the ability of the central government to act in the field of regional responsibilities, for the purpose of maintaining the national interest, or the legal or economic unity of the Republic.

Other major changes induced by the Constitutional reform but not directly affecting local governments include the suppression of the Council for Economy and Labour, and major changes to the country’s institutional framework. In particular, the Senate would no longer be elected and would lose a large share of its powers, hence ending the bicameral tradition in Italy. Senators would be elected indirectly by regional councillors among their members (with five members appointed by the President), and their number would be greatly reduced. Hence the Chamber of Deputies should have the upper hand and should mostly be in charge of relationships with the government, political control, and legislative decision making.

Policy tools used in the reform process are summarised in the following table.

Table 9. **Main policy tools used in the reform process in France**

Key challenges	Tools used
Promoting the creation of Metropolitan Cities	The law gives each metropolitan area the freedom to decide on the system of inter-municipal co-ordination they wish to adopt.
Promoting municipal mergers	Financial incentives: from both the central and regional governments. Moreover, the Stability Law 2015 introduces additional incentives such as the exclusion of merging municipalities from limitations set for hiring personnel.
Addressing political opposition to the suppression of provinces	Provisional "consensus": transforming provinces in non-elected inter-municipalities with fewer functions. The final removal of provinces from the Constitution (necessary for their abolition) will be decided by referendum.

7. Gaps and obstacles

The two main obstacles encountered were strong opposition from local politicians and successive changes to government.

In particular, political lobby from provincial politicians, through their connections to representatives in the Parliament, led to significantly water down, and even abandon, some reform proposals. The initial decree-law of 2011, as mentioned above, was modified drastically over 2012, with provinces getting back several important functions. Even after the law was passed in April 2014, there still was some opposition on the role of provinces. Moreover, the first decree-laws relative to the reform of provinces were subject to several recourses in front of the Constitutional Court and the Regional Administration in 2013, which led to the abolition of several law articles adopted until then.

Moreover, the government changed three times over 2011-14, which may have slowed down the reform process. However, as the reform of provinces and metropolitan cities was high on the agenda of all governments, the reform was still able to go through (although it is still not finalised regarding the abolition of provinces). The fact that Graziano Del Rio remained in charge of the reform project after the end of Enrico Letta's government may have helped to achieve these results.

8. Reform outcomes

Following the reform, provinces were transformed into inter-municipal co-operation entities and are no longer considered as self-governing entities e. According to the law approved in mid-2014, regional administrations are in charge of determining which functions should be transferred from provincial to regional or municipal governments within their jurisdiction. Hence, the implementation of the reform relies on the enactment of regional rules. In the meantime, provinces retain provisional functions in the areas of education, provincial roads, territorial planning, etc.

However regional governments appear relatively reluctant to introduce these transfers of functions. This may be linked to the large potential cost of the reform for the other levels of governments, since regions and/or municipalities will be responsible for former provincial staff expenditure (there are at least 8 000 employees of provincial administrations in the country). Moreover, Italian provinces are on average heavily indebted (provincial debt amounted to EUR 10.2 billion in early 2015), and the reassignment of their assets and liabilities is an intricate question. These potentially costly changes need to be implemented in a current climate of expenditure cuts and budgetary restriction, which may explain the slow progress made by regional authorities in the

implementation of the reform. After the law came into force, regional governments had six months to prepare agreements on these matters. Most regional governments however seem to have delayed the publication of these agreements; in contrast, some regional governments (six in late July 2015) such as Tuscany, started to implement the reform and regroup activities at the regional level. The pace of reforms accelerated in late 2015, and in December 2015, 15 regions had adopted such agreements.

Another major component of the 2014 law is the creation of ten metropolitan cities, which became operational in January 2015. The territory of metropolitan cities coincides with that of the province in which the city is located; they receive the patrimony and staff of the province. According to the law, the aim of creating metropolitan cities is to extend strategic development at the level of the whole metropolis and reach an integrated promotion and management of public services, public infrastructure and public communication networks. The Law establishes specific functions for metropolitan cities (art. 44). These functions include strategic planning (municipalities must in particular draw an annual plan for territorial planning at the metropolitan level over the next three years), planning regarding the communication, service and infrastructure networks of metropolitan interest, the co-ordination of public services across the metropolis, transportation, the promotion and co-ordination of economic and social development, the promotion and development of ICT frameworks at the metropolitan level, etc. Moreover, other responsibilities may be delegated by regional governments. Metropolitan cities are led by the mayor of the capital city, and a committee elected by the councillors of participating municipalities. Rome was granted a specific status.

The law leaves to each metropolitan area the freedom to decide the system of inter-municipal co-ordination to adopt.

Overall, the number of draft laws passed over the last years to reform provinces and the various amendments, even the abandonment of some of them, have resulted in confusion about the delegation of provinces' responsibilities to other levels of government and the repartition of provincial staff and patrimony. Although the fact that the responsibility of decision making was left to regions helped to build a consensus for the reform, in the end it may have had a negative impact since only a small number of regions took rapid steps to implement the reform.

9. Next steps

The next step in the final abolition of the provincial level of government is the revision of the Constitution, as provinces are enshrined in the Constitution. This revision has been announced, but is still not implemented.

As mentioned above, other than the abolition of provinces, the Constitutional reform will induce deep changes to Italy's institutional system, abolishing in particular the Senate as an elected chamber and reducing its power (senators would be replaced by regional representatives and mayors, and their number would be greatly cut). The Constitutional reform would also modify the repartition of responsibilities between the central government and regions (see above). The Prime Minister announced in December 2015 a referendum on the Constitutional reform, which should be held in October 2016.

In parallel, the central government is continuing its attempt to rationalise public finances, with wide implications in term of spending cuts for all levels of government, in particular through the successive Stability Laws. For example, the Stability Law 2015 mandates the reduction of 50% of the provincial authorities' employees, and 30% of the

Metropolitan authorities' employees (with a transition period up to 2019). It also plans for wide cuts in subnational expenditure (EUR 4 billion for regions for instance, in particular regarding the healthcare sector).

Moreover, the Stability Law 2015 introduces additional incentives for municipal amalgamations, such as the exclusion of merged municipalities from limitations set for hiring personnel.

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Case study 4 – Japan: From the Decentralisation Promotion Reforms to the 2014 local autonomy law

1. Brief description of the country – national context

Japan is a unitary country consisting of two tiers of local governments, both of equal status: 47 prefectures and 1 741 municipalities (as of 2015). Municipalities include cities (*shi*), towns (*machi),* special wards (Tokyo) and villages (*mura).* There are four different statuses for cities: ordinary cities; special cities (cities with more than 200 000 inhabitants); core cities (cities with more than 300 000 inhabitants, although there are exceptions for some cities in the 200 000-300 000 range); and designated cities (cities with more than 500 000 inhabitants). According to their status, cities have different responsibilities (core and designated cities have greater functions than ordinary cities).

Local governments are key actors in public spending in Japan. In 2014, subnational expenditures represented 40% of public expenditures, and SNGs were responsible for 77% of public investment. Prefectures are responsible for education (22% of total prefectural spending in 2012), public welfare (15%), civil engineering work (11%), support for commerce and industry (9%), general administration (6%), support for agriculture, fishery and forestry (5%), sanitation (4%), etc. Municipalities have similar functions, although the share of spending allocated to each function differs from that of prefectures. Municipalities' main responsibilities include, by order of magnitude: public welfare (34% of total expenditure in 2012), general administration (14%), civil engineering work (11%), education (10%), etc.

The first 1995 Decentralisation Promotion Reform took place in a context of serious economic downturn. The reform aimed at increasing the effectiveness of local government as well as increase local government accountability.

Another push for the reform was dissatisfaction with the agency-assigned function system. According to this system, the central government was able to allocate functions to local governments, which were mandated to carry them on without any legal authority over the tasks performed. These agency-assigned functions were hence used to relieve the central government's administrative load; they grew at a very high pace and, in the mid-1990s, they reached more than 50% of municipal expenditures.

2. Reform(s) description

In the mid-1990s, Japan started to introduce a major reform of local government. The initial Decentralisation Promotion reform was a broad reform encompassing changes to local governments' functions, an increase in local authorities' autonomy, and a revision of local governments' financing (with an emphasis on fiscal sustainability). It was carried out through several steps:

- The first resolutions for decentralisation were taken by the Parliament in 1993.
- The first Decentralisation Promotion Law was enacted in May 1995 and led to passing the Omnibus Decentralisation Law (see below) in 2000.

- Discussions regarding the financial decentralisation reform started shortly after, in 2002, and led to an agreement in 2004-05, the Trinity reform, which reviewed the financing system of local authorities.

- The second Promotion of Decentralisation Reform Law was enacted in 2006, and came into force in 2007.

3. Objectives of the reform(s) and key priority areas

A Decentralisation Promotion Committee was appointed by the government in July 1995. Its mandate was to make recommendations on the possible abolition of agency-assigned functions, on the reduction of the control of the central government over local authorities, on the increase of local own revenues, etc.

According to the Decentralisation Promotion Committee in charge of the implementation of the 1995 reform, this reform aimed at alleviating the following issues:

- The centralised system was suffering from system fatigue and needed to be redesigned.

- Decentralisation would help to better respond to a dynamic international society.

- Decentralisation would correct the excessive concentration in Tokyo.

- The reform also aimed at addressing issues linked to an ageing population and a decreasing birth rate.

- Greater autonomy for local governments would help them to achieve better local efficiency.

In contrast, the objectives of the Trinity Reform were purely on the financial side. The Trinity reform ("a package of three components") aimed at i) rationalising the national treasury subsidy system ii) change the national obligatory share system and iii) reform the local allocation taxation, with an emphasis on both central and local financial sustainability.

Last, the second Decentralisation Promotion Reform (2006), complementing the first reform wave of 1995, aimed at reaching similar objectives: granting further authority to local governments, rationalising their functions and the power of the central government over local authorities, and consolidating local administrative systems through municipal mergers. The reform also considered the abolition of regional branch offices of central ministries, whose authority was to be dispersed at the prefectural level, with in particular an integration of regional staff and budget at the prefectural level.

4. Challenges and risks

Friction between the Decentralisation Promotion Committee and the central government regarding the contents of the reforms were a major challenge. Regarding the first Decentralisation Promotion Reform, various interest groups tried to shape the outcome of the recommendations, and the largest pressure by far came from central authorities. The reform was implemented at the same time as another reform of the central government which reduced the number of ministries from 22 to 12; in this context the Decentralisation Promotion Reform was perceived by some as another loss in central

power. Negotiations between the Committee and central authorities led to agreements and the publication of the final version of the reform.

As far as the Trinity Reform is concerned, there was a strong opposition to some of the reform content (such as the abolition of the national treasury obligatory share of education expenses) by central ministries and agencies. This problem was solved by introducing negotiation rounds between the actors concerned, which led to an agreement for the reform.

The second Decentralisation Promotion Reform also encountered a large resistance, in particular from central government bodies. In particular the abolition of regional branches offices of central ministries and the removal of restrictions on specific grants, perceived as important resources to affect policy implementation at the local level, was strongly opposed by central ministries.

5. Reform(s)' characteristics

First Decentralisation Promotion Reform

The major piece of legislation corresponding to the first Decentralisation Promotion Reform was the Omnibus Decentralisation Law, enacted in July 1999 and implemented in April 2000. This law was extensive, introducing revisions to more than 475 anterior laws. The major changes introduced by the Omnibus Decentralisation Law were the following:

- The abolition of the Agency Delegated Function system;
- Modifications to the framework for control and monitoring of local authorities by the central government;
- A clarification of the responsibilities of each level of government;
- A transfer of authority to local governments;
- Modifications to mandatory obligations for local authorities' organisation.

In parallel, the Law for Exceptional Measures on Municipal Mergers (Great Heisei Consolidation) promoted the merger of municipalities on a voluntary basis.

The implementation of the Trinity Law, which aimed exclusively at reviewing the system of financial transfers to local governments and local taxes, focused on the rationalisation on modifications to local government financing system. In particular, the reform aimed at increasing the share of own revenues in local governments' budget and decreasing reliance on inter-governmental transfers. However, fiscal consolidation may have been an objective as well, as total revenue sources for local governments declined after the reform was implemented (see below).

Second Decentralisation Promotion Reform

Regarding the second Decentralisation Promotion Reform, a set of laws was adopted in March 2010:

- One bill, aiming at promoting regional sovereignty, introduced a Regional Sovereignty Strategy Council. This bill also allowed local authorities to pass bylaws regarding the setting of operational standards for public housing and child welfare facilities.
- A second bill introduced a forum of deliberation between the central and local governments.

Moreover revisions to the Local Autonomy Law were passed, aiming to increase local governments' freedom over their structure and management operations. This bill included for example the abolition of the upper limit set for the number of local assembly members, an expansion in the number of items covered by local assembly resolutions, the authorisation for creating joint establishment of government organs, etc.

In parallel, in 2004 the Law Concerning Special Measures for the Merger of Municipalities (New Merger Law) was enacted. This law aimed at promoting municipal mergers after the former law (Great Heisei Consolidation) came to expiration.

6. Outline of the process

First Decentralisation Promotion Reform

The Local Government System Research Council (*Chiho Seido Chosakai*) created in the 1950s in order to analyse and revise reforms taken under the Occupation, was in charge of formulating the main points of the Law for Decentralisation Promotion, under the direction of Osamu Uno. Shortly after the law passed in 1995, the Committee for the Promotion of Decentralisation was formed. The Committee, composed of members from the private sector, local government, academia, etc., was charged with drafting recommendations for the reform, to be submitted to the Prime Minister. The Committee was empowered with the ability to conduct investigations and deliberations, and could request information from both local and national authorities.

The implementation of the reform was hence "top-down"; however, the Committee consulted extensively, in particular with heads of local governments.

The Committee published an interim report and Decentralisation Promotion Plans. These recommendations were discussed with the central government, and some alterations were made (see below). The proposals were then implemented within the Omnibus Decentralisation Law.

Trinity Reform and the 2nd Decentralisation Promotion Reform

In 2001 a new committee was created in relation to the Trinity Reform: the Council for Decentralisation Reform (successor to the Committee for the Promotion of Decentralisation). However, major discussions took place within the Council of Economic and Fiscal Policy (CEFP) in the Cabinet office. The CEFP announced the reform in 2002, and most decisions were taken at the CEFP level. In contrast, the Council for Decentralisation Reform only submitted opinion papers to the Prime Minister on the content of the reform. The Prime Minister asked the six major regional government associations to propose plans for reforming national transfers to local governments.

Following the adoption of the law in December 2006, a new Decentralisation Reform Promotion Committee was established. The Committee issued three sets of recommendations over 2008-09. These recommendations were used in particular for discussion with the central government. In November 2009, the Committee published its final set of recommendations. These final recommendations were based on four essential

points: transferring authority from the prefectures to municipalities, relaxing the obligations and frameworks imposed to local governments, reviewing the system of central government branch offices, and amending the local tax and financial system.

Moreover, the Local Administration and Finance Examination Council was created in January 2010 in order to examine the review of the Local Autonomy Law.

The main policy tools used in the implementation of the reform are presented in the table below.

Table 10. **Main policy tools used for the reform process in Japan**

Key challenges	Tools used
Gaining support for the reform	The Japanese government relied on independent Committees for the elaboration of each reform. First Decentralisation Promotion reform: the Decentralisation Promotion Committee was in charge of making recommendations for the reform. The Committee was composed of members from the private sector, local government, academia, etc., and was charged with drafting recommendations for the reform, to be submitted to the Prime Minister. The Committee consulted extensively, in particular with heads of local governments. Trinity reform: the Council for Decentralisation Reform submitted opinion papers to the Prime Minister on the content of the reform. Moreover, six major regional government associations were asked to propose plans for reforming national transfers to local governments. Second Decentralisation Promotion Reform: a new Decentralisation Reform Promotion Committee was established. The Committee issued three sets of recommendations over 2008-09. These recommendations were used in particular for discussion with the central government. In November 2009, the Committee published its final set of recommendations.
Promoting municipal mergers	Financial incentives were used during the whole period of the Great Heisei Consolidation (1999-2006).

7. Gaps and obstacles

During the early stages of the first Decentralisation Promotion Reform, initial recommendations from the Committee were significantly modified and watered-down, in particular through the opposition of the central government. Some members of the central government feared an erosion of the power of central authorities. The Committee was criticised for yielding to the pressure from the central government.

Regarding the second Decentralisation Promotion Reform, a major challenge was a change in government in September 2009. However, decentralisation was also a priority for the newly elected Democratic Party of Japan, which even made bolder efforts than the previous government towards decentralisation. This change in government however induced several modifications to the reform process. In particular, the former Decentralisation Reform Promotion Headquarters (chaired by the Prime Minister and comprising all the cabinet members) was abolished; in November 2009 the Regional Sovereignty Strategy Council was established to replace the Decentralisation Headquarters.

8. Reform outcomes

First Decentralisation Promotion Reform

One of the major outcomes of the first Decentralisation Promotion Reform was to successfully abolish the much criticised system of agency-assigned functions, which required local governments to implement public policies decided at the central level. The suppression of this system led to revise more than 350 laws; the functions undertaken within this framework were abolished, transferred to the central government, or conserved at the local level but with a much larger autonomy of local authorities.

Secondly, the control of the central government over local authorities was reviewed; in particular, the elimination of the agency-assigned system meant that governors and mayors no longer had to serve as regional representatives of the central government, and the supervisory power of central authorities within this framework was abolished. The Local Authority Law strictly reduced the possibilities for central intervention in local matters; moreover, it established a committee in order to settle disputes between central and local authorities. However, the central government retained the ability to intervene in local administration function through the issuance of ministerial instructions.

Another major change introduced by the revision to the Local Autonomy Law was the creation of a third tier of special status cities (besides special and designated cities, which correspond to cities with more than 200 000 and 500 000 inhabitants respectively), "core cities". This concerned cities with more than 300 000 inhabitants, an area greater than 100 km², and considered as key employment centres in the region (although this last requirement was not mandatory for large cities of more than 500 000 inhabitants). Twelve core cities were approved in 1996. They gained administrative and service authority greater than ordinary cities. One of the aims of the central government for introducing this new status was to encourage municipal mergers, by pushing municipalities to amalgamate in order to gain this new status.[3]

The allocation of responsibilities between the central and local levels was clarified; moreover, the Omnibus Decentralisation Law gave local authorities gained greater authority over 64 functions (such as forestry, city planning, child rearing allowances, etc.). The repartition of responsibilities between prefectures and municipalities was also clarified; bylaws from prefectures aiming at imposing tasks on municipalities were abolished. Moreover, mandatory requirements for the organisation of local governments were abolished, hence granting local authorities' much more autonomy over their organisation (for instance, the introduction of the "designed manager" system in the Local Autonomy Law allowed local governments to entrust the management operations of public facilities to private-sector organisations).

The Decentralisation Promotion Reform also intended to promote voluntary mergers (the Great Heisei Consolidation), through the Law for Exceptional Measures on Municipal Mergers. This law corresponded to a ten-year reauthorisation of the Special Law for the Promotion of Municipal Mergers (Law 6, 1965), used to carry out mergers in the past. The main motivations of municipal mergers were cost-efficiency, weak fiscal

[3] There is some evidence that this approach may have been successful: for instance in the case of designated cities, the cities of Shizuoka and Shimizu merged in 2003 right after the conditions for this status were loosened, becoming Japan's 14th Designated City in 2005.

situation of many small towns and villages, many rural municipalities considered below the critical size to provide public goods efficiently.

Mergers were promoted in particular through the use of financial incentive from the central government (grants and tax advantages), that were in place until the end of the law in March 2006 (initially March 2005 but it was postponed). Moreover, "special amalgamation bonds" were introduced to fund projects related to amalgamations. Residents could also take the initiative to propose mergers. Measures to mitigate the resistance to mergers were also taken such as the guarantee to maintain the seats of local assembly members, a local tax "freeze" and the use of new organisational structures to enhance local representation (OECD, 2006).

In January 2006 the number of municipalities had declined to 1 820 (from 3 232 in 1999), with some amalgamation plans still under consideration. However, there is some anecdotal evidence for some of the mergers of great increases in costs, in particular relative to wages, compared to pre-merger situations (C. Schmidt, 2009). This is in line with Suganuma (2006), who finds that these amalgamations have resulted in oversized assemblies and wage inflation.

Box 37. **The impact of municipal mergers in Japan**

The Great Heisei Consolidation mergers provoked resistance, as there was a perceived risk that smaller towns and villages would be treated as appendages of their larger neighbours if they merged.

In several case studies on Honshū in the late 2000s, Elis (2011) found that the cost-cutting that followed mergers did indeed come frequently at the expense of the smaller municipalities: staff and infrastructure tended to be concentrated in the central settlements. School closures, healthcare downsizing and even the cutting of loss-making public transport services were more apparent in the peripheral areas of the new municipalities. In many cases, this may well have represented a sensible rationalisation of investment and services – the motivation for the mergers stemmed in large measure from the fact that the smaller partners could not sustain the infrastructure and service obligations they were carrying and they were in most cases losing population. The mergers also led in some places to innovations in local governance, including the devolution of responsibilities to non-governmental institutions on the sub-municipal level. In some places, local volunteers receive lump-sum payments to work at the level of districts. This is driving a broader trend towards networked local governance in Japan, involving greater participation by local groups, associations and NGOs.

Source: OECD Territorial Reviews: Japan 2005, OECD Publishing, Paris.

The evolution towards municipal amalgamations continued after the end of the Great Heisei Consolidation. In 2004, the Law Concerning Special Measures for the Merger of Municipalities (New Merger Law) was enacted. This law aimed at promoting municipal mergers after the former law (Law for Exceptional Measures on Municipal Mergers) came to expiration.

The trinity Reform and the Second Decentralisation Promotion Reform

The Trinity Reform was "a package" of three components: the transfer of tax revenue sources from the central government to local governments; the reconsideration of the equalisation tax; and the abolishment and reduction of national grants.

Local own revenues were expanded starting in 2004, through the transfer of tax revenue sources to local governments. In particular, local authorities gained JPN 3 trillion in revenues from the personal income tax and individual inhabitant tax (although they did

not gain power to set tax rates or bases). In parallel, earmarked grants to local governments were reduced by JPN 4 trillion, as well as revenues from the local allocation tax (a block grant which corresponds to the main equalisation system) which declined by JPN 5 trillion.

There was however significant criticism regarding the implementation of the Trinity Reform, linked to the fact that the initial plans from the six associations of local governments, involved in the reform, were not respected, and that local financial autonomy and independence were not improved enough. Moreover, critics objected that the primary aim of the reform may have been fiscal consolidation rather than decentralisation. Transfers of tax revenue sources were insufficient to compensate for the cuts in grants, which led to financial deterioration at the local level and increased the gap between rich and poor local authorities.

Reforms to enhance local autonomy were passed in 2009/2010, in particular revisions to the Local Autonomy Law. In 2010, several bills were submitted to Parliament. The bill creating a forum of dialogue between the central government and local associations was adopted in 2011. Revisions to the Local Autonomy Law, and in particular expanding items covered in local assembly resolutions and abolishing the upper limit for the number of local government assembly members, were adopted in 2011 and 2012. However, the project to reform the local branches of central ministries, which had been a source of strong opposition (see above), was abandoned following a dissolution of the Lower House.

After the Great East Japan Earthquake, reconstruction became a priority and decentralisation reforms were less important for the central government. Substantial funding was made available for local authorities affected by the disaster and the central authorities launched a ten-year plan for reconstruction, in priority in the provinces of Fukushima, Miyagi and Iwate. Special Zones for Reconstruction were created in 2011; 277 municipalities located in the afore-mentioned provinces could propose the creation of special zones to central authorities, leading to tax deductions, financial transfers and relaxed regulation.

The main components these three waves of reforms are summarised below.

Table 11. **Components of decentralisation reforms in Japan**

Reform	Date	Contents
First Decentralisation Promotion reform	1995	Promulgation of the Law on Promoting Decentralisation, establishing the Decentralisation Promotion Committee.
	1995, 1999	Amendments to the Local Autonomy Law, reducing the possibilities for central government to intervene in local matters. Creation of a new status for large cities (Core Cities).
	2000	Omnibus Decentralisation Law: Abolishment of agency-delegated functions, which required local governments to implement public policies decided at the central level. Clarification of the responsibilities of the central and local governments. Local authorities gained greater authority over 64 functions. Clarification of responsibilities between provinces and municipalities. Abolition of bylaws from provinces aiming at imposing tasks to municipalities. Local authorities gained greater autonomy regarding their organisation.
Municipal mergers	1999	Law for Exceptional Measures on Municipal Mergers: Great Heisei Consolidation mergers (1999-2006). The number of municipalities declined from 3232 to 1820 over 1999-2006.
	2004	Law Concerning Special Measures for the Merger of Municipalities (New Merger Law): promotion of municipal mergers after the former law comes to expiration.

Table 11. Components of decentralisation reforms in Japan *(continued)*

Municipal mergers	2006	Basic Policy for Promoting Municipal Mergers" which reinforced previous measures.
	2011	Additional measures focusing on facilitation of voluntary municipal mergers have been taken.
Trinity reform	2002	From 2004 onwards: increase in local own revenues and decrease in earmarked transfers from the central government to local authorities.
	2006	Decentralisation Reform Promotion Law, enacted in December 2006.
Second Decentralisation Promotion reform	2007	Creation of the Decentralisation Reform Promotion Committee
	2009	Change of government; launch of the Regional Sovereignty Strategy Council in replacement of the previous Decentralisation Headquarters.
	2010	Submission of several bills to the Parliament: A bill creating a council in charge of resolving issues between the central government and the 6 associations of local authorities. A set of bills mitigating restrictions on local administrations. A bill reorganising the local branches of the central ministries. A bill introducing revisions to the Local Autonomy Law (expanding items covered in local assembly resolutions, abolishing the upper limit for the number of local government assembly members, etc.). These bills were adopted in 2011 and 2012 respectively, with the exception of the reorganisation of the local branches of central ministries, which was abandoned.

9. Next steps

While inter-municipal co-operation was not particularly encouraged in the past (amalgamations being the only option), Japan has started to promote it via a revision to the Local Autonomy Law, which came into force in 2014.

This amendment is centred on two key points:

- Partnership agreements: these agreements are a new type of contract, which aim at reaching economies of scale by mutualising the delivery of services across several municipalities. This also aims at providing more homogenous services in sparsely populated areas. The agreements concern functions such as healthcare, welfare, education, transportation, etc.
- The system to transfer service provision from one municipality to another has been amended, inducing greater flexibility, and greater protection for municipalities using it over the outcomes in their area.

Other reform proposals considered recently in Japan include greater transfer of authority from the central to local governments, the creation of a national system of inter-municipal co-operation, etc.

Metropolitan governance reforms

Concerning metropolitan areas, a legislative measure allowing Japanese metropolitan areas to form new urban governments was passed by Japan's parliament in 2012. The law enables large cities to reorganise themselves from 2015 into new special entities modelled on Tokyo's system of metropolitan governance (with a system of special wards), considered as a best practices. Osaka and nine other Japanese major cities with populations over 2 million (Sapporo, Saitama, Chiba, Yokohama, Kawasaki, Nagoya, Kyoto, Sakai and Kobe) are now able to introduce new metropolitan structures following approval by city referendum. Despite a strong support from local representatives and business communities, in 2015 Osaka's citizens rejected by referendum the proposal for a

new metropolitan government, which would have merged the existing 24 administrative subdivisions into five new elected municipal bodies with enlarged competencies.

The National Spatial Strategy

Moreover, the Abe administration has recently launched a Regional Revitalisation strategy, aiming at correcting over-concentration in Tokyo, alleviating population decline in rural areas, revitalising regional and rural economies, and strengthening the competitiveness of major metropolitan areas.

The National Spatial Strategy (NSS), adopted in August 2015, focuses in priority on the issues of depopulation, regional revitalisation, disaster resilience and environmental sustainability. The NSS is a horizontal initiative; discussions involved inter-ministerial co-ordination, as well as wide consultation with academic experts, representatives of the private sector, representatives of cities and prefectures, and others. Measures considered in order to reach this objective include the establishment of new grants for municipalities that local governments could use for fighting population decline and revitalise local economies, the establishment of tax incentives for companies transferring their head office from Tokyo to a regional area, etc.

The main instruments identified to address the challenges of population ageing and decline are collaborative core urban areas, compact city policies and small stations. The associated vision is centred on the concepts of "compact" and "networked". In order to reach a more effective provision of public services, the settlement of Japan should become more compact; the NSS acknowledges that some places will become depopulated, although the general aim is to sustain a broad settlement pattern at the national level. In cities with declining population, an emphasis will be put on improving connectivity in order to reach economic benefits linked to agglomeration. Cities with more than 100 000 inhabitants will be designated as "core cities" and functional urban regions will be established around these cities based upon travel times, using population grids and the road network.

"Small stations" will be created in rural areas. These "small stations" will be established and maintained by prefectures and municipalities, and will concentrate basic service delivery such as administrative services, healthcare, etc., in areas easily accessible for rural populations via transport networks.

In order to support competitiveness and the future development of the main urban centres, the NSS includes plans for the construction of the *Chūō Shinkansen* magnetic levitating train from Tokyo to Nagoya and Osaka, steps to improve innovation performance in cities, instruments to attract foreign investment, etc.

Moreover, a National Infrastructure Plan was approved in September 2015, aiming at increasing the effective use of existing facilities, maintaining efficiently infrastructures, planning for future public investment, and focusing in particular on infrastructures to enhance mobility for the elderly and disabled. This plan is implemented in co-ordination with the National Spatial Strategy, under the authority of the Council for National Infrastructure.

Changes to local finance

Local governments in Japan gained additional revenues in 2014 through increases in the rate of the national sales tax. Parts of these increased receipts were allocated to local

authorities, with an emphasis on funding healthcare, long-time care, childcare and pensions.

In parallel, the special funds available for local governments in order to face the recession linked to the 2008 global financial crisis should come to an end, hence reducing local governments' funding.

After the Trinity reform, another round of reforms affecting transfers to local government took place in 2011 and 2012. It involved the conversion of earmarked grants towards general-purpose grants, hence increasing the autonomy of local authorities over the use of funds. In particular a Local Autonomous Strategy Subsidy was created for public works, leading to less authority from the central government over transfers to local governments. However it was abolished in 2013 after the central government decided to allocate more funds to infrastructure maintenance and disaster prevention.

The National Spatial Strategy may lead to a new increase in general-purpose funding for local governments. The 2015 local finance plan included specific funds for local revitalisation, to be allocated to local projects maximising local initiative and autonomy. Funds for innovative projects will also be available, distributed on the basis of a cost/benefit analysis.

10. Sources and bibliography

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Case study 5 – New Zealand: From the 1989 reform of local governments to 2014 Local Government Act

1. Brief description of the country – national context

New Zealand is a unitary country with a two-tier system of local governments, composed of 11 regional councils and 67 municipalities referred to as “territorial authorities” (11 city councils, 50 district councils and 6 unitary councils). New Zealand is a relatively centralised country compared to other OECD countries, with only 11,3% of public expenditure taking place at the local level in 2013 (against 40% on average in the OECD). However, local authorities play a large role in public investment as they represent 39.6% of total national public investment.

The responsibilities of local governments are established by the Local Government Act 2002; however, they may change from one local authority to another, as they are approved through consultation with their communities. They typically include resource management, public transport, regional parks, water supply, etc. at the regional level, and roads, water reticulation, sewerage and refuse collection, town planning, etc. at the municipality level.

This case study will focus on the reforms of local governments introduced in New Zealand in the 1990s, on the Auckland metropolitan reform entered into force in 2010 and to conclude on more recent local government reforms focused on managerial aspects.

The reforms adopted in the 1990s took place in a context of significant economic deregulation at the national level, including for instance reforms for the abolition of control over exchange and interest rates. The aim of these successive reforms was to shift New Zealand towards a deregulated and market-based economy, in order to support economic performance. These reforms included changes to all levels of governments; in parallel to the reforms of SNGs analysed below, changes to the central government were introduced as well, such as greater corporatisation and a separation between policy-making and operations at the central level.

2. Reform(s) description

Many parallel reforms were introduced in the late 1980s/ early 1990s to reform local governments in New Zealand. These reforms included a restructuring of local authorities through a drastic reduction in their number, a separation between local policy-making and policy implementation, a move towards more corporatisation for local public services, and greater local government accountability.

As far as the reduction in the number of local authorities is concerned, “amalgamations” can be misleading, as the old authorities were replaced by new ones that did not always correspond to old boundaries.

The metropolitan reform leading to the creation of the Auckland Council in 2010, as well as the Local Government Act 2002 and its recent amendments are also presented below.

3. Objectives of the reform(s) and key priority areas

New Zealand went through a series of reforms in the late 1980s/early 1990s aimed at enhancing local governments' efficiency (in particular for service provision), increasing the accountability of local governments, separating policy making from policy implementation, enhancing consultation with the civil society, and achieving a greater corporatisation of government-owned commercial activities (often through privatisation – a similar trend was implemented at the central level).

According to the Government Economic Statement (1987), the 1989 restructuring of local governments in particular was based on five principles to guide the reform, ensuring that new arrangements would only be introduced if their benefits exceeded that of other options. These principles were the following:

- Allocate individual functions to local authorities representing the appropriate community of interest.
- Greater efficiency, although there are difficulties (less incentives for efficiency linked to a weaker accountability, greater costs generated by a larger size, etc.)
- Non-conflicting objectives, i.e. a separation between service delivery functions and regulatory functions (in particular regarding regulation responsibilities linked to potential commercial advantages, to reduce the impact of pressure groups on local authorities)
- More explicit and transparent trade-offs between objectives in order to preserve adequate accountability
- Encourage strong accountability mechanisms (electoral processes, mandatory information publications, contestability in the provision of services).

According to the Local Government Commission in charge of the 1989 reform, the objectives were the following:

- Reach a smaller number of local authorities
- Improved management and technical capacity in the new entities
- Create coherent entities with respect to service provision (not corresponding to historical communities of interest)
- Create efficient and effective entities
- Create multi-purpose capacity entities
- Create entities according to prospects of cost reduction and potential benefits in relation to functions.

4. Challenges and risks

Establishing political legitimacy for the reforms was a challenge. This was achieved by delegating the authority over the reform process to a Commission independent from

central authorities (the Local Government Commission), and by reaching across party boundaries (the chair of the Commission, Sir Brian Elwood, was a previous National party candidate, while the Minister in charge was from the Labour party). This helped building legitimacy for the reform process, and facilitated the adoption of local Orders.

5. Reform(s)' characteristics

The 1989 reform included a large restructuring of local governments and special-purpose bodies, by reducing significantly the number of local authorities. The Commission in charge of this restructuring was not bound by the previous structure of local governments, and could hence introduce drastic changes. In particular, some former councils could be divided across several new entities.

Besides this territorial reform, changes also aimed at enhancing accountability. Local governments were required to shift from cash to accrual accounting, to draft extensive annual plans for the next 12 months (and the following two years in outline – with public consultation), adopt a new consultation process ("special consultative process", with many requirements in terms of information provision and public consultation).

A new accountability regime for local governments was also introduced in a reform passed in 1996, with a focus on financial viability; this reform required local governments to draft a ten-year (or more) plan stating their future activities and funding sources (Long Term Financial Strategy), including financial forecasts, cash flows, and balance sheets. These requirements were initially not accompanied by any sanction or enforcing mechanisms. However this issue was addressed through a modification of the reform in the 2002 Local Government Act (the new long-term plan requirements focused less on the financial side and more on the promotion of community outcomes).

Another major component of this set of reform was a move towards greater corporatisation, either through privatisation or the creation of public (or semi-public) corporations.

6. Outline of the process

The task of restructuring local governments was delegated by legislation (Local Government Amendment Act 3) to the Local Government Commission. This aimed at isolating the reform process from political interference; all decisions were taken by the Commission, and not the government.

The Commission consulted extensively with the civil society, to build a stronger legitimacy. In particular, it worked in close co-operation with the association of local authorities (Local Government New Zealand), as well as with individual local authorities.

The reform was implemented very quickly, especially regarding local government restructuring. The rapidity of this implementation and the delegation to an independent Commission were seen by many as positive for the success of the reform (leading to less opposition to change).

The main policy tools used within the reform process are presented in the table below.

Table 12. Main policy tools used to implement the reform

Key challenges	Tools used
Creating political consensus	This was achieved by delegating the authority over the reform process to a Commission independent from central authorities (the Local Government Commission), and by reaching across party boundaries (the chair of the Commission, Sir Brian Elwood, was a previous National party candidate, while the Minister in charge was from the Labour party).
Gaining support for the reform	The Commission consulted extensively with the civil society, to build a stronger legitimacy. In particular, it worked in close co-operation with the association of local authorities (Local Government New Zealand), as well as with individual local authorities.
Promoting corporatisation	In the transport sector, the fact that subsidies from Transit New Zealand were only granted with compliance on competitive pricing procedures, led in many cases local authorities to corporatise their activities.

7. Gaps and obstacles

The Commission was not bound by the existing form of local government in New Zealand, and hence intended to vastly review the structure and functions of local governments. For this purpose it informed and consulted with local authorities by sending them information about the intended reform.

The government, in its attempt to reform other aspects of local governments, took a similar approach, but one of its core principles generated a widespread opposition. While the principle was relatively large (that local or regional government should be selected only where the net benefits of such an option exceed all other institutional arrangements), its interpretation was that local governments should only be responsible for service provision when such services are not more efficiently conducted by another means. Hence local government responsibilities would not include addressing the needs of their communities, regulation, etc. The principle was abandoned in face of this widespread opposition.

The question of completely separating authorities responsible for regulation and service delivery also led to a strong debate. In the end, the decision was taken to leave substantial regulatory functions to local governments.

The introduction of greater accountability for local governments generated specific problems. Regarding the shift to accrual accounting, there was some degree of confusion as the central government did not provide any guidelines to local authorities, resulting in a large heterogeneity in the documents provided by local governments. Moreover some requirements to report local authorities' "return on capital" were also poorly formulated, and this provision was repealed in the end.

Last, the choice to disregard old communities in the restructuring reform may have been costly. The previous political structures often did not disappear, but were transformed into boards or committees, which generated animosities and impacted on the effectiveness of the reform. It has been argued that a more bottom-up approach would have generated greater public support, in particular from the old political structures. Moreover, such a process would have helped to maintain greater identification with local communities.

8. Reform outcomes

The consolidation reform significantly reduced the number of local bodies. There were around 850 entities covering different areas (regional and local) and of different nature. They included around 200 local and regional authorities (counties, municipalities, independent town districts, district communities and around 650 elected "special purpose bodies" such as harbour boards, catchment boards, and drainage boards, etc.). Through the reform, the existing 200 local authorities were replaced by 12 regional councils (subsequently 11) and 75 city and district councils, referred to as "territorial authorities" (subsequently 67); a large number of special-purpose bodies were abolished. Restructuring was very heterogeneous, with some local authorities remaining unchanged, while others were formed from the amalgamation of several small authorities, or by portions from larger authorities. It appears that the regions were established by largely following the boundaries of drainage basins.

Policy making and implementation were effectively separated, by the introduction of Section 119C of the Local Government Act. According to the Section, councillors are excluded from policy implementation, which is a responsibility of a single (or a group of) chief executive officer(s) appointed by the Council.

Compulsory corporatisation was not fully achieved, with the exception of the transport and electricity sectors. However local authorities gained strong powers to use public corporate structures. In the 1989 Amendment Act, the Government made provision for other options such as, in particular, the creation of local authority trading enterprises (LATEs). In the transport sector, the fact that subsidies from Transit New Zealand were only granted with compliance on competitive pricing procedures led local authorities, in many cases, to corporatise their activities. Ports were also largely corporatised (although no major port was fully privatised). Regarding electricity, the Energy Companies Act of 1992 introduced compulsory corporatisation, which led to vast improvements in profitability for local councils that owned their local electricity distributor (McKinley 1998), and improved significantly local balance sheets.

Regarding the new accountability objectives, the reforms enacted in 1989/90 led to substantial changes. On the financial side, the shift from cash to accrual accounting, and the requirement to submit annual plans and reporting improved the quality and availability of local financial information. Moreover, new information requirements were introduced for local public enterprises (LATEs).

New consultation obligations were also introduced; revisions to the Local Government Official Information and Meeting Act and the new Resource Management Act granted larger access to local authorities' information, and introduced a right to attend meetings and make submissions on plans. However this reform led to unanticipated issues. While initially the public took greater interest and participated in the planning process, there were concerns that in the end this might contribute to greater public disillusionment. Moreover, it may generate specific difficulties and costs; for instance, local authorities may not be able to develop options in an informed manner before the information became available to the public.

Did the reform increase councils' efficiency?

Although there was no public audit or study to assess the impact of the reforms, a few independent studies have been conducted to assess their effectiveness.

Rouse and Putterill (2005) analysed highway service provision in New Zealand over 1982-1997, and tried to determine whether the efficiency of services improved following the reduction in the number of local authorities. Road construction has historically been one of the major activities of local authorities in New Zealand (with water supply, waste water, waste disposal, etc.). Their measure of efficiency is subdivided in two criteria: the presence of economies of scale in larger councils, and an improvement in technical efficiency (better performance). Regarding pre-amalgamation councils, the authors find no evidence of diseconomies of scale (i.e. smaller councils did not appear to be less efficient). Performance did increase after the reduction in the number of local authorities, but according to the study this was not linked to the amalgamation process. Instead, the most likely explanation for this greater efficiency is the outsourcing of services by small local authorities, linked to the parallel reform to increase corporatisation at the local level.

According to McKinley (1998), the reform successfully enhanced the capacity and operational efficiency of large local governments, but negatively affected smaller councils (with less than 20 000 residents).

Another study by TBD Advisory (2013), although not directly linked to the 1989 reform, tried to identify economies of scale in local councils in New Zealand. It analysed around 70 local authorities over five years, and considered 16 distinct functions. In line with international studies, the authors failed to identify a clean-cut relationship between efficiency and the size of local governments. However among the 16 functions considered, they did find evidence for economies of scale for five specific functions, mostly requiring large-scale capital investments (roads – in contrast to the study mentioned above -, water supply, solid waste, emergency management, and governance). Labour-intensive functions in opposition were likely to be characterised by diseconomies of scale; other approaches, such as the implementation of best practice management and operational techniques, may generate better results.

9. Next steps

Recent reforms affecting local governments in New Zealand include the introduction of the Local Government Act in 2002 and its successive amendments, territorial reforms (in particular in the Auckland area), as well as reforms affecting local finances.

The Local Government Act and its amendments

A large reform of local governments' functions came into force in 2002. The Local Government Act 2002 (LGA 2002) broadened and redefined local government's powers and roles and responsibilities. Its purpose was to provide democratic and effective local authorities. It was based upon a collaborative, citizen-centred approach and aimed at securing community well-being and sustainable development (Reid M, 2010).

The Act redefined the purpose of local governments, which is to:

- enable democratic local decision-making and action by, and on behalf of, communities

- meet the current and future needs of communities for good-quality local infrastructure, local public services, and performance of regulatory functions in a way that is most cost-effective for households and businesses

The Local Government Act 2002 introduced a new framework for local authorities, greatly increasing their autonomy by providing them a general power of competence. According to the Act, local authorities had “full capacity to carry on or undertake any activity or business, do any act, or enter into any transaction”. Since local governments were free to select activities to engage in, in consultation with their communities, this could lead to an asymmetry in terms of local activities and service provision across local authorities.

The Act also introduced additional requirements in terms of strategic planning and accountability. In particular, new requirements were set for local governments’ long-term plans, annual plans, and annual reports, with an emphasis on financial reporting. Regarding accountability, the Act introduced in particular new requirements for consultation with the Maori.

New requirements for communication and co-ordination across local authorities were also introduced, through triennial agreements aimed at avoiding the duplication of services or functions. A process to resolve conflicts across local authorities was created. In addition, local governments gained the ability to issue bylaws.

The Act was amended in 2010, with in particular the introduction of new financial reporting requirements, a standardisation of non-financial performance measures for infrastructure services to enable comparisons between councils, etc.

In 2014, the Act was amended again in the line of the “Better Local Government New Zealand” reform. This new amendment aimed to clarify and increase transparency for development contributions, increasing flexibility for local boards, encourage inter-municipal co-operation, clarify competencies between regional councils and territorial authorities, promote long-term planning, etc. Financial reporting requirements were also tightened (see below). The objectives of this reform were to encourage municipal co-operation and shared services, increase the efficiency of long-term and annual plans and simplify duplications across these plans. It also enabled the creation of local boards within new unitary authorities, as well as the creation of joint committees and council-controlled organisations within existing unitary authorities. This increased the ability of councils to participate in joint financing with the private sector, in particular regarding the provision of water services.

More specifically, the 2014 amendment to the Act introduced modifications to reviews of service delivery, consultation requirements, infrastructure strategies and development contributions. Regarding service delivery reviews, new requirements were introduced for the triennial agreement between councils belonging to the same region. The bill also specified that each local authority must review the cost-effectiveness of local infrastructure, public services, and performance/regulatory functions. Such review must be carried on in parallel to any significant change in service provision, within two years of expiration of any contract concerning the provision of infrastructure, service or regulatory function, or at any time considered desirable by the local authority itself (and at least every six years).

Local authorities in charge of drafting annual and/or long-term plans must consult on the content of each local board agreement planned to be included in the plan. Other

consultation requirements have also been introduced or simplified. Moreover, non-regulatory decision making powers may be delegated from councils to local boards (for the corresponding territory), and local boards may issue bylaws for its area.

Concerning investment, the Act introduced the obligation to adopt an infrastructure strategy (for a period of at least 30 years) as part of the long-term plan. It aimed at identifying key issues related to infrastructure and the main options available to manage them. It also (among other things) requires local governments to draw estimates of projected capital and operating expenditure linked to the management of infrastructure assets.

Last, the system of development contributions was modified and restricted. The Act states that development contributions should be charged only in the case of creation of new or additional assets, and should be set in coherence with the assets capacity life, hence avoiding over-recovery of costs. Moreover, local authorities should adjust these contributions in line with the Producers Price Index Ouputs for Construction produced by the National Statistical Institute.

Territorial reforms and the Auckland Metropolitan Reform

Regarding territorial reforms, a small number of case-by-case amalgamations happened since the end of the reform programme. Moreover, some councils were considering alternatives to amalgamation, in the form of inter-council co-operation, region-council co-operation, etc. In particular, the 2014 Local Government Act 2002 Amendment Bill encourages further intermunicipal co-operation and shared services between local authorities.

The major territorial reform that took place since the end of the 1989 changes was the creation of the Auckland Council in 2010. In the late 2000s the central government estimated that the large number of Councils and their difficulty to work together, combined to a weak regional government with limited powers, were hindering Auckland's progress. In 2007, it set up a Royal Commission on Auckland Governance (a Chair, two commissioners and a small office), to report on what restructuring should be done. The two main options considered were to create a stronger regional government, or to amalgamate all councils under one local authority. The Commission published several background research papers, and organised many study visits around the world. The Commission also organised public consultations, receiving over 3 500 written submissions, holding 27 public hearings throughout the region and hearing more than 550 submitters. The Royal Commission also held five meetings with the Māori, as well as workshops with Pacific and ethnic communities. In 2009, the Royal Commission submitted its report, Making Auckland Greater. The newly elected government subsequently announced that a "super city" would be set up to include the full metropolitan area under a single Auckland Council. This was done through a number of Parliamentary Acts. An Auckland Transition Agency was also created by the central government. Finally, the Auckland Council began operating on 1 November 2010, combining the functions of the Auckland regional council and seven territorial authorities. It is governed by a mayor, 20 members of the governing body and 148 members of the 21 local boards.

Several criticisms were made to the reform process. In particular, the fact that much of the advice and recommendations from the Royal Commission were not taken into consideration by the new government to design the metropolitan entity was criticised. Other controversies included:

- the selected area: many argued that the area was too big. As the boundaries of the region and the super city coincide, they include some rural areas.
- the choice of governance model (merger) and the organisational structure may have hindered local democracy (few powers and resources of local boards)
- the unbalanced situation between rural and urban wards
- the outsourcing of major functions to external independent agencies (council-controlled organisations or CCOs)
- the treatment of the Maori population.

Although the Auckland Council was only created recently, hence making ex-post evaluation difficult, there is anecdotal evidence of both positive and negative outputs. On the bright side, the Auckland Council reports savings in its early years of existence. The unification of regional planning and a more cohesive approach to planning and transport infrastructure may have been positive as well. The first-ever unified planning document (the Proposed Auckland Unitary Plan) was established regrouping development policies for the whole region and replacing the previous seven district plans. Auckland also gained greater resources with a unified tax system (over tax rates). On the negative side, observers have noted large transition costs, with in particular significant increases in wage expenditures. Some areas at the periphery are also complaining about the degradation of facilities on their territories. There are still key public concerns about transparency and accountability.

The reform is still in progress, and some stumbling blocks seem to be on the way to being solved (e.g. governance model with local boards). However, observers consider that an independent evaluation of the impact of the reform would be useful to grasp its effectiveness (Local Government magazine 2015).

Reforms affecting local finance

A recent initiative from both local and central governments was the creation of the Local Government Funding Agency (LGFA) in December 2011, which became operative in February 2012 (LGFA 2015). LGFA consists in a debt vehicle regrouping 47 member councils, which raises bonds on financial markets in order to lend to local governments at competitive interest rates.

One of the aims of the creation of this agency was to ensure continuity in the funding of infrastructure projects. More generally, the agencies' objectives are to increase the certainty of funding for local governments, reach more favourable funding conditions, and longer dated funding. The agency was granted a notation AA+ by two credit rating agencies.

LGFA analyses and monitors local authorities' financial performance closely, and issues regular reports. In November 2015, it had already lent over NZL 5 billion to 46 councils, through refinancing previous loans borrowed from banks, or funding new infrastructure projects.

New financial prudential requirements were introduced in 2011 and 2014, within the framework of the Local Government (Financial Reporting and Prudence) Regulations 2011 and 2014. These regulations aim at promoting prudent financial management by local governments:

- **Local Government (Financial Reporting and Prudence) Regulations 2011:** these regulations include additional information to be included in local authorities' financial statements, such as the specification of the sum of investments in council-controlled organisations, combined depreciation and amortisation expense within groups of activities, etc. It also requires councils to disclose balance sheet information for core assets (water, wastewater, storm water, flood protection, road) within local authorities' annual reports. The regulations also include directions for the preparations of funding statements (in terms of timing and balance), as well as some details on their form.
- **Local Government (Financial Reporting and Prudence) Regulations 2014:** the reform introduces new benchmarks and indicators for financial management. New reporting requirements have also been introduced: councils must include within their annual reports information such as the safety of drinking water, consumer satisfaction regarding drinking water, etc. (SLOGM 2014). Benchmarking was introduced around three main axes: affordability (rate and debt affordability), sustainability and predictability. Indicators associated include for instance the ratio of interest expense to operating revenue, which should not exceed 10% (debt servicing benchmark).

10. Sources and bibliography

See main bibliography (above) and internet resources below:

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