



## **West Nordic municipal structure**

### ***Challenges to local democracy, efficient service provision and adaptive capacity***

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## 1 Introduction

The geographical structure of people's settlement in the West Nordic countries<sup>1</sup> is in itself a considerable challenge for the provision of municipal services. It can be argued, therefore, that this is a challenge for the democracy on the local level. Municipal structure varies in the three West Nordic countries and has gone through changes in the past decades. Geographically the three countries are different although the similarities are more obvious when we look at the economic structure – fishing and fish processing are the mainstay of the economy. The basic idea behind this project is that local communities in the West Nordic countries are facing a certain type of dilemma. On the one hand, decisions at local level need to be based on sound knowledge of local circumstances and conditions and taken in harmony with the local people, if they are to be sensible, successful and legitimate decisions. On the other hand, very small or “too” small local decision-making units often have problems mobilizing and providing the expertise needed to make rational decisions. This problem, or question, of the optimal size of a municipality – or should we rather say optimal smallness – is a relevant and emerging question in, for example, the larger Nordic countries. The difference between the West Nordic and the East Nordic situation in this sense is that the municipalities in the west are historically considerably smaller in population.

In 2005 the Nordic Council of Ministers published the report *Demokrati i Norden* (Democracy in the Nordic Countries) (Demokratiutvalget 2005). The research work behind this report was led by “The Democracy Committee” (Demokratiudvalget). Among issues like democracy in general, people's engagement in politics and information technology as a democratic instrument, there was a special chapter on *local self-government*. Based on the report, the committee brought forward its recommendations. Among those on local autonomy were suggestions for strengthening municipal autonomy in various ways – one of which was “structural reforms”. The committee proposed an impact study of every structural change in order to determine how each change affects the prerequisites for action of democratically elected bodies.

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<sup>1</sup> It is important to note here that the definition of Vestnorden is: Iceland, Greenland and the Faroe Islands. In some cases Vestnorden is defined along with the NORA-region, which also includes the west coast of Norway.

This, irrespective of structural change, is initiated at national or local level, or both. It was argued that it had come to be evident that structural changes and reforms in the relationship between the state and the local level had had unanticipated consequences for the local democratically elected bodies, sometimes by delegating political power over certain tasks to other levels and in some cases to private parts. It was also strongly argued that the heavy emphasis on effectiveness, but less on democracy and self-government in the Nordic countries, was a negative consequence of the structural changes and reforms. Instead, the role of a local politician should be looked at as a school in democracy, and therefore the number of elected representatives should rather be increased than decreased. By strengthening democracy, opportunities for the people of becoming more involved in decision making would increase (Demokratiutvalget 2005, p. 51-59).

These ideas on local democracy are to some extent relevant to the cases the authors of this report are investigating in this research project on the West Nordic municipalities, or *Vestnorden*. As we will see later on in this report, the emphasis in Vestnorden has been much the same as in the four big Nordic countries – effectiveness rather than democracy has been the key principle.

The central idea behind the this project reported here has been developed, not only by the researchers who write this report, but also by representatives from the federations of municipalities in the countries involved; from Føroya Kommúnufélag in the Faroe Islands, Mrs Sveiney Sverrisdóttir and from Kanukona in Greenland, Mrs Kisea Bruun. The researcher team consists of Dr. Grétar Thór Eythórsson, professor at the University of Akureyri in Iceland; Dr. Erik Gløersen lecturer at the University of Geneva in Switzerland and senior consultant at Spatial Foresight in Luxemburg; and finally Dr. Vífill Karlsson docent at the University of Akureyri and consultant at the Federation of Municipalities in West Iceland. It should me mentioned that the original idea was born in Reykholt, Iceland in 27. – 28. October 2011 at the final conference in the project “Vestnorden Foresight 2030” with participants from the municipal and the state level, together with researcher teams from all three countries.

The application proved to be successful and the team was granted some preparatory money for the project which was called *Västnordisk kommunstruktur: Utmaningar för*

*service-effektivitet och lokaldemokrati. Ett projekt om utbyte av kunskap och erfarenhet mellan Färöarna, Grönland och Island.*

The overall aim of the project is to collect knowledge on the local level in the three countries by mapping the situation and development, focusing on four aspects: *First*, to map development, debate and current situation of the municipal structure in the three countries. *Second*, to look into the democratic aspect – that is which consequences the structural development has had for local democracy – more specifically to try to identify which have been the main challenges for democracy, caused by the structural developments. *Third*, to map the service production capacity and effectiveness of the municipalities in the three countries and *fourth*, to try to map the municipalities' capacity to manage the development processes which often accompany municipal amalgamations – not least when looking at entrepreneurship in economic life as well as innovativeness in importing external management models. An overall research question for all parts can therefore be: *Which consequences have developments in municipal structure in the three countries had for democracy, local self-government and autonomy and the ability to manage the processes accompanying amalgamations?*

In this first phase of the project the intention is to write an overview report on the aspects listed above. The main method in this context is to collect and use all relevant literature, including research reports, articles, other kinds of reports and official accessible statistical data at local level. The websites of the statistical bureaus Hagstofa Íslands ([www.hagstofa.is](http://www.hagstofa.is)) for Iceland, Hagstova Føroya ([www.hagstova.fo](http://www.hagstova.fo)) for the Faroe Islands and Grønlands Statistik ([www.stat.gl](http://www.stat.gl)) for Greenland became highly useful to us. Additionally, the authors sought to deepen their insight through interviews with people working at, or linked to, local level in these countries. In the cases of Iceland and the Faroe Islands this was successfully achieved, but problems occurred when it came to recruiting people to do interviews in Greenland, as the budget did not allow for the travel expenses required. Consequently, email was to some extent used to collect information.

In chapter two we deal with the municipal structures in the three countries and their respective development. Here an attempt is made to provide an overview of the

municipal structures, not only as they are at present but also in a historical context. In chapter three we deal with matters of local democracy. The emphasis is on trying to illustrate the main current challenges to local democracy in each respective country. In chapter four the main focus is on a cross country comparison of the size of national and local government, and the efficiency of local administration. Chapter five provides a framework for the analysis of local strategies for economic development and adaptation in the West Nordic countries and presents some preliminary observations on current practices within this field of policy-making. In chapter six the main findings in the report are summed up with some guidelines as to the second phase of the project.

## 2 The municipal structure

Firstly, this chapter provides an overview of some theories and literature on municipal structure changes and their consequences. Secondly, the municipal structure is described, mapping its development in the West-Nordic countries. The historical context is outlined, as well as the main catalysts for developing or changing municipal structure. Furthermore, the division of competences between the state and local level is looked at, examining the extent to which tasks have been transferred from the state to the municipalities. In the past decades, such trends have mainly been in evidence in Greenland and Iceland.

### 2.1 Municipal territorial structure reforms: Research and literature

So far, only limited research exists on the consequences of structural reforms in the Nordic region or, or in other countries for that matter. Studies have been conducted in Iceland, however, and to some extent in Denmark. In 2002 an evaluation study on the impact of seven amalgamations implemented in Iceland in the 1990s was published in book form. In these 7 municipalities which were the result of amalgamations from 37 local councils between 1994 and 1998 some clear patterns emerged when looking at the consequences. People in former autonomous districts that did not obtain the role of “Central place of administration and services” in the new municipality were much more discontent with their current situation than those living in the part that now had the role of “Central place”. This had mostly to do with their democratic situation, their potential for influencing decisions and their possibilities of establishing contact with elected representatives. The democratic deficits were clearly apparent in the peripheral “territories”. The situation was not as dramatic with the municipal services – even though people in the “peripheries” were more discontented, their dissatisfaction was less severe than with regard to the democratic situation.<sup>2</sup> So, in the Icelandic case clear signs of more emphasis on effectiveness than democracy are found.

In 2006, just before the great municipal reform in Denmark, Danish political scientists published the anthology *Kommunalreformens konsekvenser* (Blom-Hansen, Elklit and Serritzlew eds., 2006). The results show a clear negative correlation between the size of a municipality and several indicators of democracy, such as trust,

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<sup>2</sup> Eythórsson & Jóhannesson 2002. A summary of the project can be read in Swedish in Ivarsson (ed.) 2011.



voting participation and attending political meetings (Juul-Madsen and Skou 2006).<sup>3</sup> In another study presented in this book Nørgaard-Petersen and Christensen did not find any correlation between municipal size and representation – that is, in bigger municipalities, voters in various social groups used their potential for participating in the democratic process (Nørgaard-Petersen and Christensen 2006). The Danish political scientist Kurt Houlberg has looked at economic consequences of the reform in Denmark. His results are mainly that the expected economies of scale gained by the extensive amalgamation reform were not at all realized three years after the reform. He gives four possible explanations: a) expectations were too high, b) the models used to calculate underestimated administrative costs due to a higher degree of decentralization, c) municipalities that are larger in size are in fact more expensive to run and d) trying to live up to all expectations around the reform, the municipalities built up administrative competences which turned out to be more expensive than anticipated (Houlberg 2011).

Lassen and Serritzlew (2011) conducted research on the correlation between jurisdiction size and local democracy. Using the Danish structural reform as a case they looked for evidence on internal political efficacy. By internal political efficacy they mean that citizens believe they are competent to understand and contribute to political decision making and by external political efficacy they mean that citizens feel government authorities are responsive to their demands so that participation is something worth struggling for. Among their findings was that in terms of population larger municipal units were necessary for economies of scale but at the same time larger size incurred cost with regard to the quality of democratic order (Lassen and Serritzlew, 2011).

These examples of research on structural reforms show that structural territorial reforming by enlarging municipal units is, at the same time, a question of the balance between economies of scale and local democracy. These studies have mostly shown us that too much emphasis on seeking economies of scale can have negative consequ-

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<sup>3</sup> The authors of this chapter use three indicators for municipal size: population, area and urbanization degree. The discussion of size here is restricted to population numbers.

ences for the local democracy. This is in line with what was argued already in 1973 by Dahl and Tufte that a correlation between size and democracy exists.

However, looking at the research examples from Denmark we have to realize that here the question was about much larger municipal units than in the case of the West Nordic countries.

## 2.2 The Faroe Islands

Originally there were 8 municipalities in the Faroe Islands – this was based on the system of parishes. These municipalities had, however, very limited tasks. The societal changes where the society was transformed from an agrarian to a fishing community led to demands for more activity on behalf of the municipal boards in terms of service provision. At the same time, people paying taxes in one village were not keen on that money being spent in other villages. This led to the establishment of new municipalities and at the peak of this trend in 1967 there were 51 municipalities in the Faroe Islands (Hovgaard et. al. 2004).

Already in the mid-twentieth century there were 49 municipalities in the Faroe Islands, an autonomous territory of 18 islands with a population of less than 50,000. This structure of numerous small municipalities, with more than half of them having a population of less than 1000, stayed the same all the way into the beginning of the 21st century. The Faroese municipal geography during this period is summarized by Hovgaard et.al. (2004) as following:<sup>4</sup>

- A capital area with almost 40% of the population
- Constantly improving conditions for commuting to the capital of Tórshavn have connected over 85% of the nation by road
- A rather peripheral island of Sandøym in the south with 1300 inhabitants and four municipalities
- The even more peripheral Island of Suðuroy, 2:15 hours ferry trip from Torshavn. On Suðuroy there are 7 municipalities with a total population of 4700
- Geographically remote small islands (municipalities) with low population and difficult communications

This is also graphically shown in the figure below:

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<sup>4</sup> Hovgaard et.al. 2004, p. 18-20



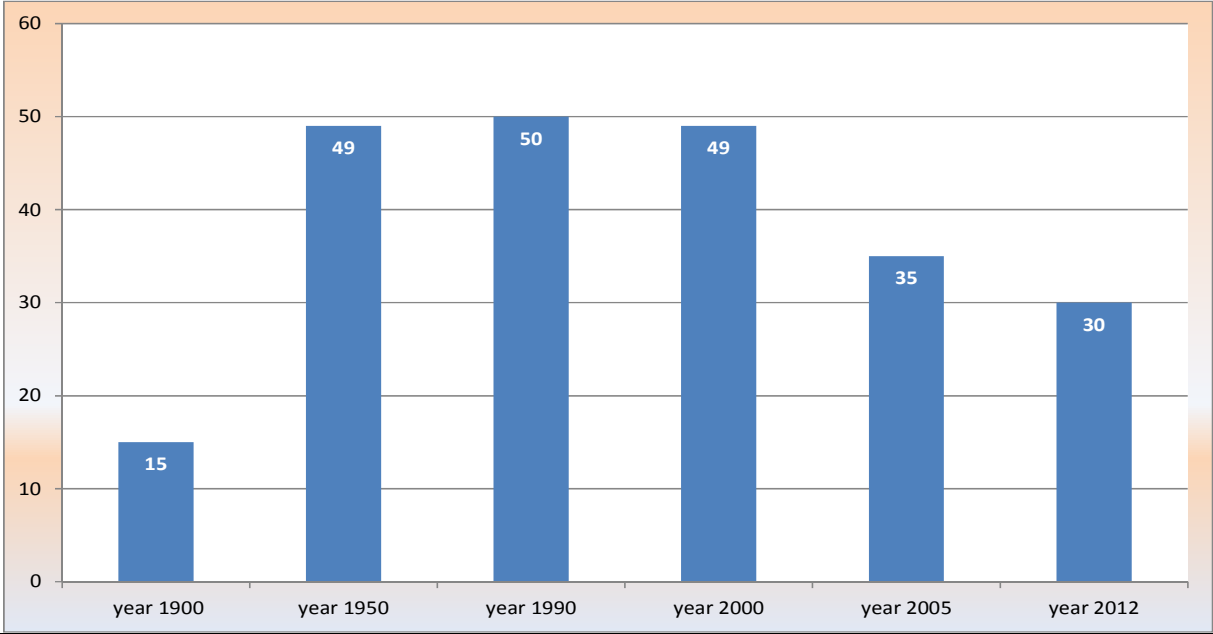
Figure 2-1. The municipal map of The Faroe Islands in 2012.<sup>5</sup>

In 1998 a commission on municipal reform (Kommununevndin) proposed in a report that the number of municipalities should be reduced to 7-9 through amalgamations. The municipalities should be allowed to amalgamate voluntarily by their own initiatives within a given time limit. Failure to do so would mean that an amalgamation by force from above should be implemented. These ideas and proposals met total resistance among the municipalities, political parties and in the Parliament and thus never went into a law making process. However, an *Act on voluntary amalgamations* was passed in the Faroese parliament in in May 2001. The act stated that municipalities could amalgamate voluntarily but they had to be geographically connected or/and by infrastructure. It was also expressed as desirable that a population of 2000 should be minimum size for a municipality. Further, it was stated that the government intended to decentralize by transferring tasks from the state to local level.<sup>6</sup>

<sup>5</sup> <http://en.wikipedia.org/wiki/File:Map-kommunur-foroya-2009.png>

<sup>6</sup> Based on Hovgaard et. al., 2004)

Despite massive resistance against law-enforced reform, voluntary amalgamations in the following years reduced the number of municipalities from 49 in 2000 to 35 in 2005. This is illustrated in the following figure which also shows how the municipal structure in the Faroe Islands has changed since 1950:



**Figure 2-2. The municipal structure in Faroe Islands 1950 – 2012.**

No extensive structural reform came about as a consequence of the laws in the beginning of this century but, as the figure shows, voluntary amalgamations reduced the number of municipalities by 14 until the year 2005.

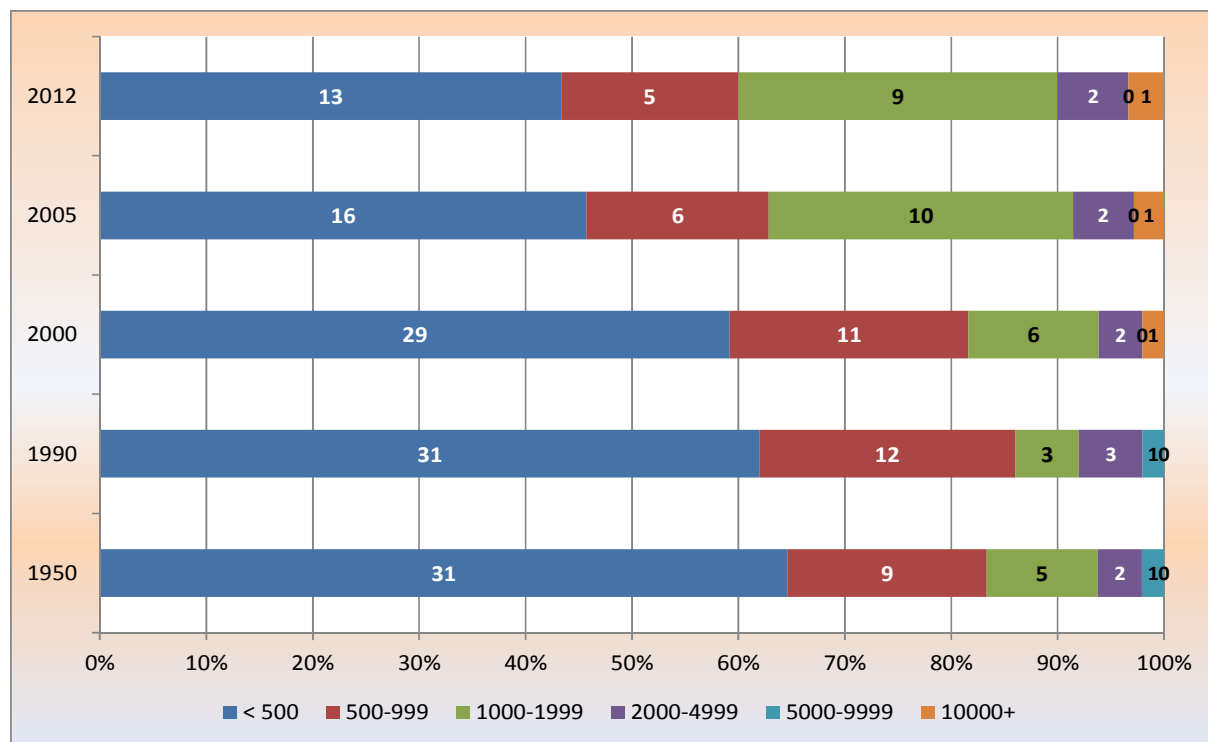
Early in 2008 a new government came to power in the Faroe Islands and the coalition paper contained clear statements on the municipal structure. “Regional development initiatives and changes in the municipal structure shall ensure fair and balanced opportunities for all areas of the Faroe Islands.” Furthermore, the coalition paper contained statements on deadlines by which municipalities should have grouped into suitable entities that were able to take over more tasks from the state government – and this would ensure even standards of services in the whole country (Aalbu et. al. 2008). Here, it was apparent that the new government wanted to put through an extensive structural reform at municipal level, in order to transfer tasks to the local level.

An even stronger and more precise statement on this was made by the Prime Minister Jóannes Eidesgaard, in his opening speech to parliament in July 2008, where he said that the government had decided to reduce the number of municipalities to 7 during the mandate period. He even set time limits for 1<sup>st</sup> January 2010 (Aalbu et. al. 2008). The government coalition broke up already in the autumn 2008 and these intentions have not yet become reality as other less interested parties have been in power since then.

The amalgamation issue was more or less put off in 2012 with a nationwide referendum on the people's will to amalgamate, with the potential result that the number of municipalities might have gone down from 30 to 7. With only 33 percent voter turnout, this proposal did not receive majority support in any of the 30 municipalities.

Today the number of municipalities remains at 30 - the radical intentions of 2008 government were never realised as the people of Faroe Islands refused. And people seem to think that this amalgamation wave of the first decade of the 20<sup>th</sup> century has come to an end. "*The referendum stopped everything*" and "*The reform is dead*" were the answers the authors of this report received from interviews with people from the two federations of municipalities in the Faroe Islands. However, if we look at what has happened since year 2000 we see a reduction of municipalities by almost 40% - so the change is noticeable even though the municipal structure remains the same.

Looking further at the municipal structure and examining the share of municipalities of different sizes in the whole, we note that the smallest municipalities are those which have been amalgamated to the greatest extent, internally or with larger ones. Figure 2.3 illustrates this:



**Figure 2-3. Municipalities in the Faroe Islands in different size categories 1950 - 2012.**

It is clear that after year 2000 more than half of the smallest municipalities (< 500) have ceased to exist – their share in the total number has gone from 59% in year 2000 to 43% in 2012. Municipalities in the category (1000-1999) have increased in number, so the major changes have been in these size categories. Municipalities with a population of more than 2000 remain as they have been through the decades. The characteristics of the Faroese municipal structure remain: Fewer *very small* and more *rather small* municipalities.

### 2.3 Greenland

The first elected municipal councils in Greenland came about in 1911. After WW2 the Danes reorganized them along Danish lines. Their functions expanded in line with the growth of the Danish welfare state from the 1950s to the 1970s. Later, when the home rule system was established in 1979 the municipalities acquired a more central role in the domestic welfare system taking care of social services, culture, education, housing, planning, fire brigades, water and electricity (Dahl, 1986; Børenholdt, 2007). In 2007 the Greenland Parliament directed the Greenland Home Rule to implement a new municipal structure for Greenland. This decision led to radical structural change when 18 municipalities were amalgamated to only 4. New municipal councils were elected

in spring 2008 and established from May 2008. The change was formally implemented 1st January 2009. The rationale behind this development was set by the Structural Committee (Strukturudvalget). The main purposes were:

1. To make all municipalities large enough to be able to take over more tasks from the Home Rule.
2. To ensure that the citizens in the municipalities received better and safer services.
3. To gain effectiveness and economies of scale in the municipal service provision.<sup>7</sup>

This revised division of tasks was to be implemented under the mandate period 2009 – 2013. The tasks to be transferred to the municipalities were: elderly care, handicap services, pensions, housing, labour market measures, family policies, harbours, water supply, communications and spatial planning sectors.<sup>8</sup> At the time of writing only one task has been transferred from the Home Rule to the municipalities; handicap services on 1<sup>st</sup> January 2011. According to the Federation of Greenland Municipalities (KANUKOKA) in 2011, two other tasks were to be transferred on 1<sup>st</sup> January 2012. These were a) psychological-pedagogic consulting and b) specialized retraining (KANUKOKA 2011).

The number of municipalities was reduced in 2009 from 18 to the following 4 municipalities:

**Table 2-1. Municipalities in Greenland 2012 and their population.**

Municipality	Population
Øst – Vest (Kangia-Kitta)	20733
Nord (Avannaa)	18243
Midt (Qegga)	9685
Syd (Kujataa)	7787
Outside municipality	200

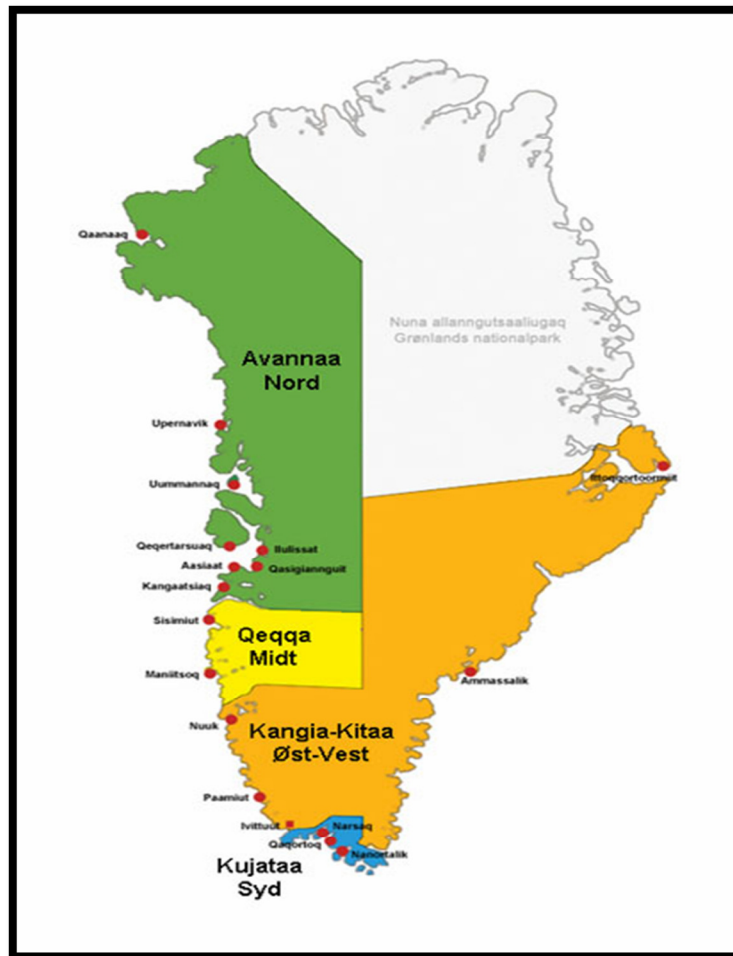
With the largest municipality of over 20,000 inhabitants and the smallest of little less than 8000 the structure has changed dramatically. At the same time the geographical

<sup>7</sup>

[http://dk.nanoq.gl/Emner/Landsstyre/Departementer/Dep\\_for\\_indenrigsanliggende\\_Natur\\_og\\_Miljoe/Indenrigs\\_kontor/Til\\_kommunerne/Struktureformen/Strukturudvalget.aspx](http://dk.nanoq.gl/Emner/Landsstyre/Departementer/Dep_for_indenrigsanliggende_Natur_og_Miljoe/Indenrigs_kontor/Til_kommunerne/Struktureformen/Strukturudvalget.aspx). (Downloaded on 25th April 2013). Aalbu (et.al.) (2008).

<sup>8</sup> Aalbu (et. al. (2008).

size of the two of the new municipalities, *Nord* and *Øst – Vest* has become enormous. This is clearly illustrated in figure 2.4.:



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Figure 2-4. The municipal map of Greenland after 2009.<sup>9</sup>

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In their report from 2008 *Administrative Reform – Arguments and Values*, Aalbu, Böhme and Uhlin map and analyze the municipal structures, structural reforms and the arguments and values behind them, in all eight Nordic countries. They conclude that no clear public opposition to the reform process in Greenland has emerged. Further, they conclude that in the debate around the reform, the main focus was on efficiency, accessibility and quality in local administration. Thus they think the main emphasis in the Greenland case has been on effectiveness and improved services, just as in the cases of Sweden and Denmark.

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<sup>9</sup> Taken from:

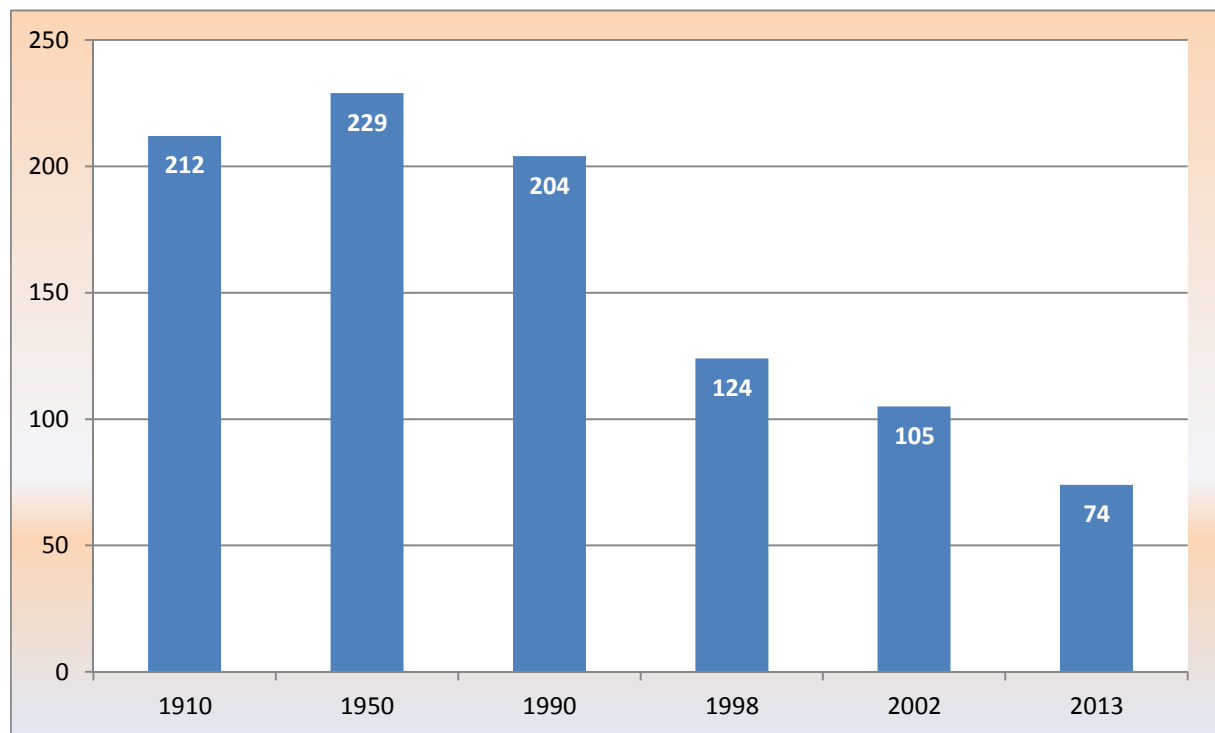
[http://dk.nanoq.gl/Emner/Landsstyre/Departementer/Dep\\_for\\_indenrigsanliggende\\_Natur\\_og\\_Miljoe/Indenrigs\\_kontor/Til\\_kommunerne/Strukturereformen/Kommuneinddeling%20i%20grafisk%20udgave.aspx](http://dk.nanoq.gl/Emner/Landsstyre/Departementer/Dep_for_indenrigsanliggende_Natur_og_Miljoe/Indenrigs_kontor/Til_kommunerne/Strukturereformen/Kommuneinddeling%20i%20grafisk%20udgave.aspx)



## 2.4 Iceland

Municipalities in Iceland have a long history - all the way back to the 11th century. When the Danes took control over Iceland in 1662, they whittled down most of the municipalities' autonomy and then totally abolished them by law in 1809. Later on, in the 19th century, when the Icelanders started asserting their rights for independence, the local government system was re-instituted by law in 1872. At the same time, the Danish government included a regional governmental level (Amt), similar to the former existing Amt structure in Denmark. However, the regional experiment was not very successful, and these were abolished by law in Iceland in 1904.

The main development pattern is that the number of municipalities increased slowly until the middle of the 20th century, and then began to decrease, especially after 1990. The main reason for the increasing number of municipalities until the 1950s was the industrialization of fishing, leading people to move from the countryside to the coast in order to work where there were better hopes of earning a decent income. This meant that new fishing villages emerged, and new municipalities were established.<sup>10</sup>



**Figure 2-5. The main patterns in the municipal structure in Iceland 1910 – 2013.**

<sup>10</sup> Based on Eythórsson (1998).

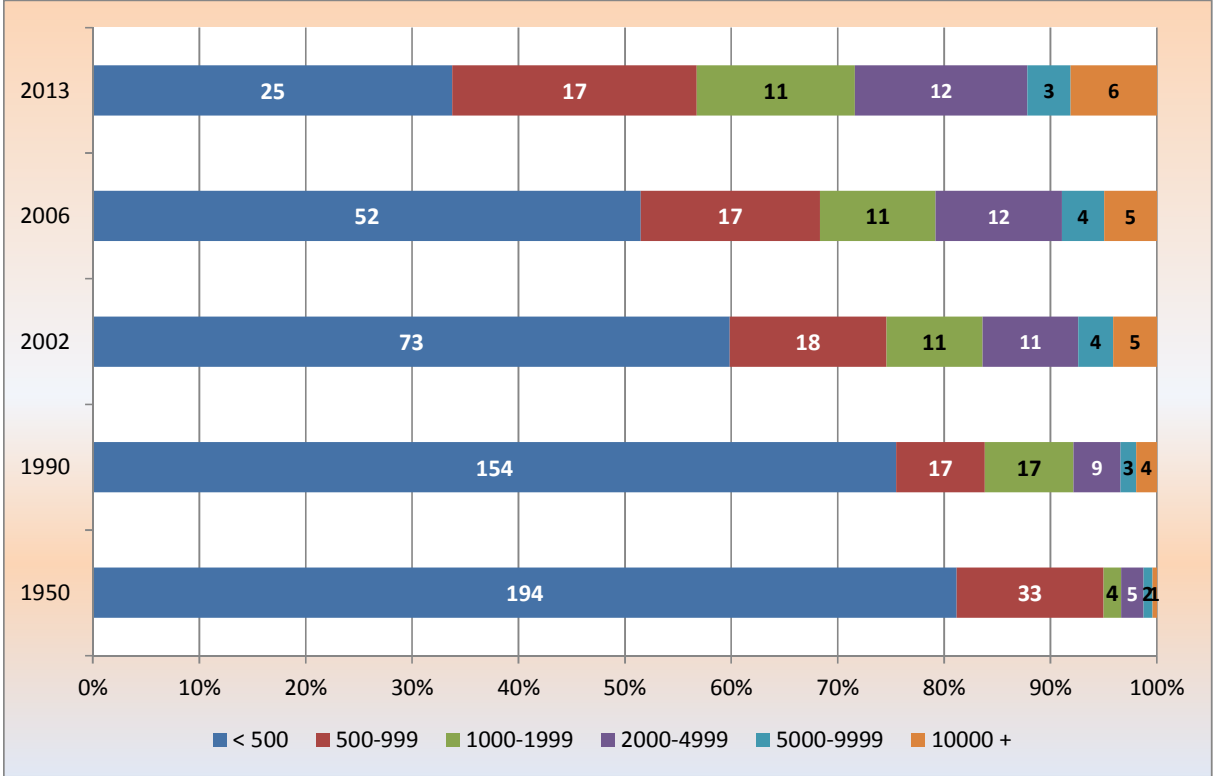
The slow decrease in the number of municipalities after the mid-twentieth century is mainly explained by two forces – a number of rural municipalities ceased to exist due to total depopulation; and some municipal amalgamations. The rapid changes since 1990 were indirectly facilitated by two referenda on municipal amalgamations - one in 1993 and the second in 2005 - and their implications.

Ideas on reforming the municipal structure in Iceland can be traced all the way back to the 1940s. The discussion has mainly focused on strengthening the municipal structure through amalgamations. Through the years, however, this never led to any changes until the 1990s.

In 1991, the Minister for Social Affairs, Jóhanna Sigurðardóttir, (Prime Minister 2009-2013), took the initiative to set up a Commission to start a process intended to result in a reduced number of municipalities, because larger administrative units were believed to have a better capacity to deliver appropriate welfare services in step with modern standards. All amalgamations would remain strictly voluntary; and all proposals for such changes were to be developed by the municipalities themselves, or recommended by representative mutual boards within the regions. In November 1993, referenda were held in 185 municipalities out of 196. Had all the submitted proposals been accepted, they would have meant a drastic reduction in the number of municipalities, down to 43. However, every proposal except one was voted down in these referenda. Only 67 out of the 185 municipalities involved voted for amalgamations. This only caused an immediate reduction of municipalities by 3, but nevertheless the ball had been set rolling and an amalgamation trend never known before had started. By the time of the local government elections in spring 1994, several voluntary amalgamations among those that had voted ‘yes’ in the November 1993 referenda had already reduced the number of municipalities to 171. By the next elections in 1998, the number was reduced further to 124 and was as low as 105 in the local government elections in 2002. Thus, a process was initiated in 1993 which had led to a reduction of municipalities by as much as 47 percent in only 9 years.

In 2003, the Icelandic Ministry of Social Affairs launched a reform project on the strengthening of the municipal level, in cooperation with the Federation of Municipalities. The main objectives were to strengthen municipalities so they would

be better able to provide their current level of services and eventually some additional ones. Bringing about such a change would make it possible to move certain public services from the state to the local level. This required both a revised division of tasks between state and local level, as well as a revision of local government finances. The cornerstone of the project, however, was to strengthen the local level by amalgamating smaller municipalities. Even though the number of municipalities had been reduced by almost 50 percent since 1993 the project commission argued that this had not changed the characteristics of the municipal structure. Still there were far too many small municipalities lacking the capacity to take over more responsibilities from the state. The following figure illustrates changes in the municipal structure in a historical context. In 2006, municipalities with a population of less than 1000 were almost 70 percent of all municipalities.<sup>11</sup>



**Figure 2-6. Municipalities in Iceland in different size categories 1950 - 2013.**

A referendum took place in 66 municipalities out of 97 in spring and autumn 2005. In these 66 municipalities, residents voted on a total of 17 merger proposals; so a ‘yes’ to

<sup>11</sup> Mainly based on Eythórsson (2009).

all proposals would have meant a reduction of 49 in the number of municipalities. The general commission on financial matters did not agree on its mandate in time, however, and many local leaders claimed that the interval for arguing the case was too short. Consequently the referenda were postponed until October. However, in one case the municipalities wished to move ahead right away, since they had completed all their preparations. These were 5 municipalities in the Borgarfjörður region; in April 2005, four of them voted yes in a referendum, which meant that the decision to amalgamate those four was confirmed. So, eventually, on 8th October, referenda were held in 61 municipalities on 16 different amalgamation proposals. The 16 different proposals were voted down in 41 municipalities and accepted in only 20. Only one proposal was accepted by a majority in every municipality in question – in East Iceland involving 4 municipalities in the area around an Alcoa smelter plant. This only meant an immediate reduction of the number of municipalities by three – from 92 to 89. In several cases, municipalities which had voted 'yes' continued a process voluntarily which ultimately led to some further amalgamations. At the time of the local government elections in May 2006, the number was down to 79 municipalities.

No serious or extensive attempts to reform the municipal sector have been implemented in Iceland since 2005. The Social Democrats (Samfylkingin), which is the political party historically most interested in an amalgamation reform, came to power in 2007 in a coalition government. One of their ministries was responsibility for municipal affairs. Soon, preparations for an extensive amalgamation reform were made – ideas on reduction down to 17-19 municipalities, possibly through law-enforced actions, were presented – but the coalition partner, The Independence Party, was reluctant, although not directly opposed. After the economic collapse in Iceland in 2008 a new coalition government of The Social Democrats and The Left-Green Party came to power after new elections in spring 2009. Already in 2010, the Social Democrats yielded responsibility for the Ministry of the Interior to their coalition partner which was not at all interested in amalgamation reform. So, municipal structure in Iceland has remained more or less unchanged since 2006 as shown in figure 2.6 above.

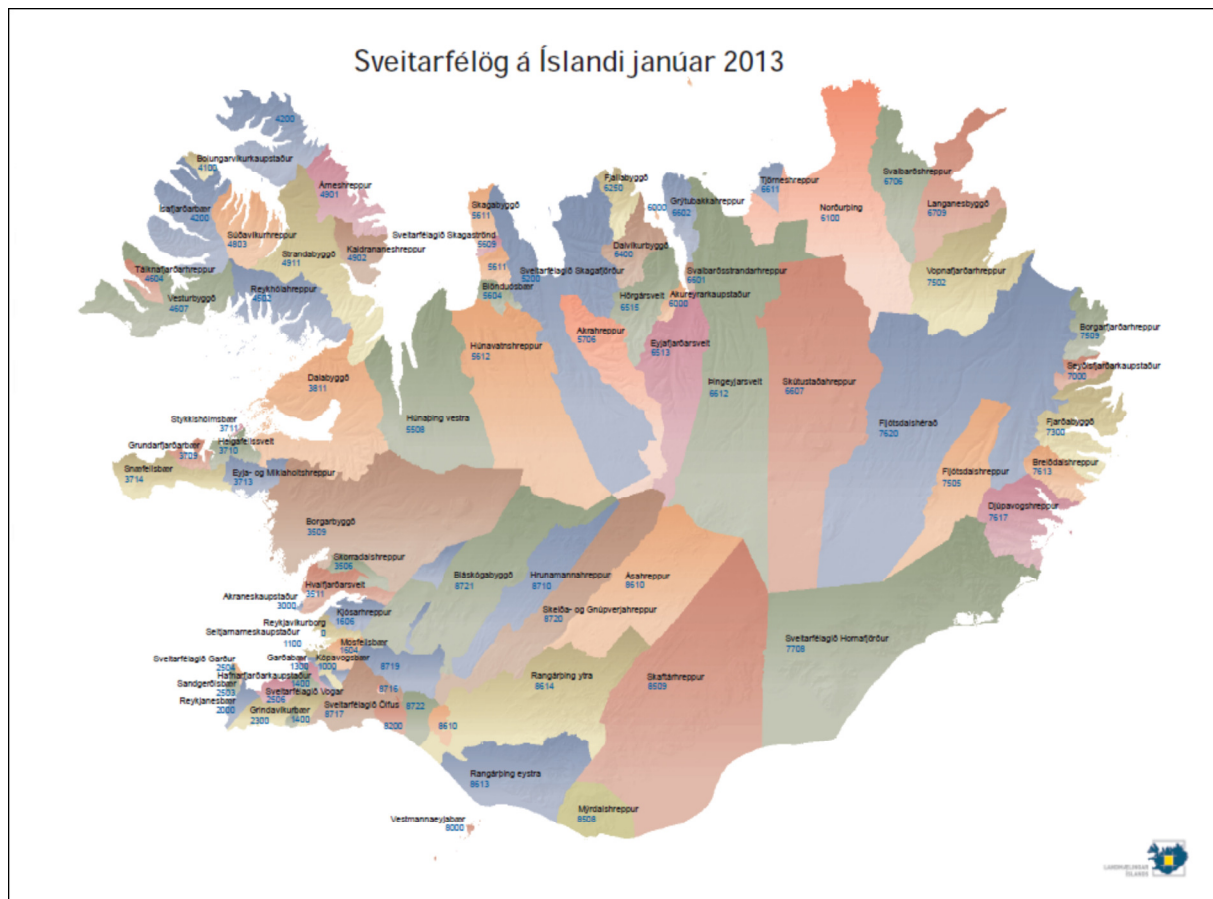
Besides, interest in further amalgamation reforms seems to be declining. Two surveys among local politicians and members of parliament in 2006 and in 2011 show this. Interest and belief in amalgamations as a measure to strengthen the municipal level is significantly less in 2011 than in 2006. There is, as earlier, no majority support for law enforcement with regard to amalgamations. Instead, local politicians seem to see increased inter-municipal cooperation as the way to go further and take over more responsibilities from the state government (Eythórsson & Arnarson, 2012).

At present the municipal geography of Iceland can be briefly described in terms of three characteristics, which, in turn, suggest a high rate of urbanization and concentration of population:

1. The capital area - Reykjavík, the capital with 119,000 inhabitants, followed by its neighbours Kópavogur (31,000), Hafnarfjörður (26,500) and Garðabær (13,000) contains some two-thirds of Iceland's total population. These are the largest municipalities in terms of population: only Akureyri in the mid-north is in the same size group (18,000).
2. Counting all the municipalities within commuting distance of the Greater Reykjavík area (that is, a radius of up to 75 km), one finds three quarters of the island's total population. Here are included municipalities such as Reykjanesbær (14,000), Akranes (6,500) and Árborg (8,000). An underwater road tunnel under the fjord Hvalfjörður was opened in 1998, shortening the distance from the north and west to the capital by over 40 kilometres, and having major impacts on nearby municipalities such as Akranes and Borgarbyggð (3,500) (Karlsson, 2004; Sigursteinsdóttir & Ólafsson, 2004).
3. Apart from Akureyri, only few municipalities outside the capital region have more than 3,000 inhabitants. These include Ísafjarðarbær in the north-west (3,800), Skagafjörður in the mid-north (4,000), Fjarðabyggð (4,600) and Fljótshálsa (3,400); in the east and in the south Vestmannaeyjar (4,200).

But in spite of all attempts to change, the main characteristic of the Icelandic system stubbornly remains in the year 2013. More than half of the municipalities in the country have less than 1000 inhabitants and 1/3 have less than 500 – a trait which has been considered as the main problem through the decades; too many too small municipalities with limited capacity to provide modern services. A reduction from 196 municipalities to 74 in twenty years has only managed to change the main pattern to a

limited extent. As already mentioned, local leaders and state politicians seem to have begun to believe that the most realistic way to strengthen the municipal level so that it can continue taking over significant tasks from the state is by developing more cooperation projects. A form of surrender to voluntary amalgamations appears to have taken place. The following figure is the municipal map of Iceland for January 2013:



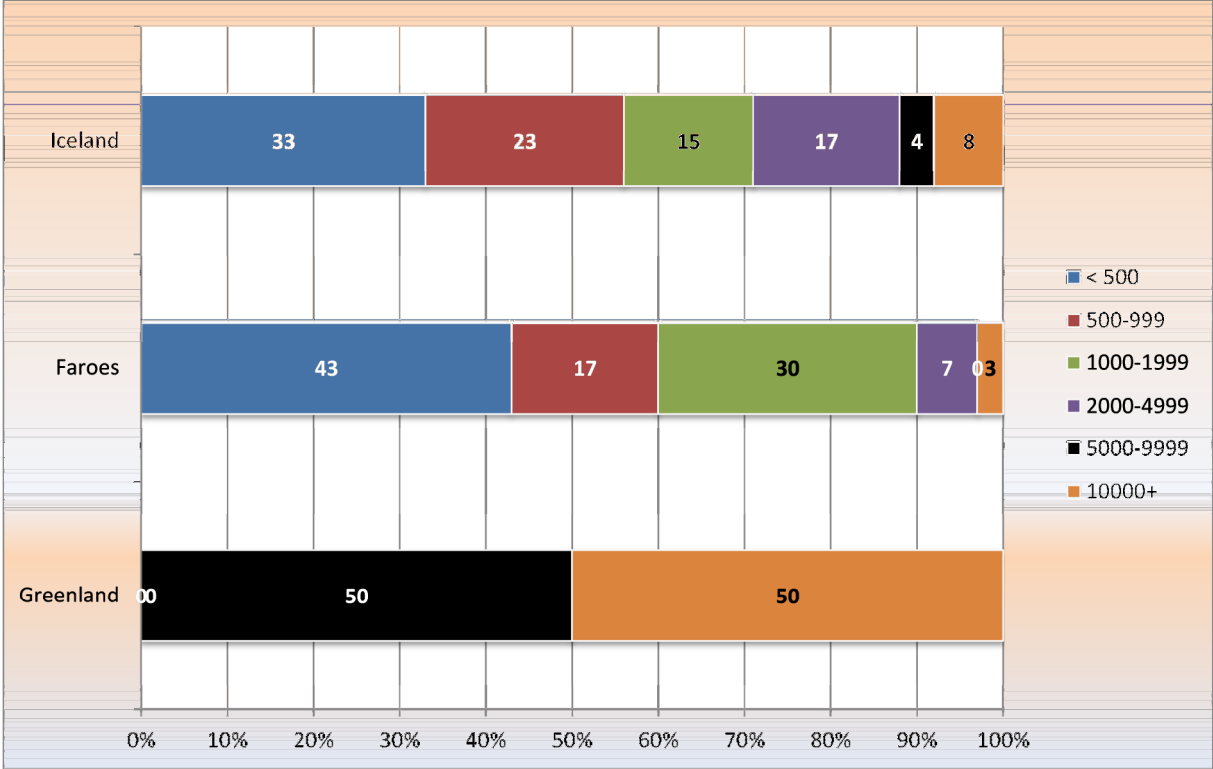
**Figure 2-7. Municipalities in Iceland in January 2013.**

## 2.5 The West Nordic municipal structure in sum

When attempting to sum up and compare the municipal structure in these three countries, the most striking fact is the dramatic development in Greenland, where the structure of local administration was changed after 2007 by amalgamating 18 municipalities to 4. In this respect, the Greenland structure differs significantly from that of the Faroe Islands and Iceland. Now, Greenland has few and large communes, both measured in population and areal – at least in West Nordic terms. Even though bigger steps towards reforming the municipal structure have been taken in Iceland than

in Faroe Islands, the characteristics are in principle the same. In both cases there are proportionally numerous very small municipalities with limited capacity to take over more welfare tasks and thereby provide modern services. In Iceland, however, there seems to be a will to strengthen the local level by other means than amalgamating.

The following figure illustrates the municipal structure in the three countries at present:



**Figure 2-8. Municipalities in the West Nordic countries in different size categories 2012.**

It is clear that the share of small municipalities; that is, with a population of less than 1000, is similar in Iceland and the Faroe Islands, 55-60 percent. At the same time municipalities of such limited size do not exist in Greenland anymore.

The following table provides an overview of some facts about the number of municipalities and their populations in the three West Nordic countries.

**Table 2-2. Municipalities and their population in the West Nordic countries in 2012.**

	<i>Faroe Islands</i>	<i>Greenland</i>	<i>Iceland</i>
<i>Total population</i>	48,296	56,648	319,575
<i>Number of municipalities</i>	30	4	75
<i>Average population</i>	1,610	14,162	4,261
<i>Median population</i>	626	13,964	889

There are, for example, significant differences between the three countries in the average size of municipalities. While Greenland has over 14,000, Iceland has over 4,000 and the Faroe Islands just over 1,600. However, the average for Iceland is strongly affected by the size of Reykjavík with its 121,000 inhabitants.



### 3 Local democracy

In this chapter we will try to give a brief overview of the status of local democracy in the three countries. This will primarily refer to the current circumstances. Also we attempt to outline the most prominent issues and problems in local democracy connected with the present situation in the municipal sector in each respective country. In the Faroe Islands the most pressing issue is connected to the content of local democracy since the many small municipalities have limited tasks. In Greenland the emerging issue is the geographical representation of small villages and communities after the great municipal reform. In the Icelandic case much of the discussion on democracy at the municipal level is about direct citizen democracy versus the more traditional representative democracy. Another emerging and upcoming discussion in Iceland is connected with trying to reinforce the municipal level by greater emphasis on municipal cooperation instead of municipal amalgamations.

#### 3.1 The Faroe Islands

The Faroe Islands have always had a two tier government system, the state level and the local level. However, there exist *sysler* (counties) but they are without any administrative or political significance. The municipalities are 30, and have historically been divided into two local authorities associations: *Førøya Kommunufelag* is the association of the smaller municipalities, consisting of 21 municipalities, and the other association, *Kommunusamskipan Førøya* consists of 9 of the larger ones. In December 2013 it was decided to merge these two associations into one, valid from 1<sup>st</sup> January 2014. In the local government elections in 2008, 208 representatives were elected, whereof 63 (30%) were women (Knudsen, 2009).

##### 3.1.1 Current challenges to local democracy in the Faroe Islands

The coalition paper published by the 2008 government in the Faroe Islands contained clear policy statements on enlargements of the municipalities in order to increase their service capacity and ensure even service standards in the whole country. This was emphasized by Prime Minister Eidesgaard in Parliament in summer 2008 where he announced that the goal was to reduce the number of municipalities to seven. He

underlined the democratic aspect in his opening speech to Parliament on the 29<sup>th</sup> of July 2008:<sup>12</sup>

*An important part of democracy lies in decisions being made as close to the citizens as possible, and this is one reason why more and more functions are being transferred to the municipalities.*

These arguments of attracting young people to the more peripheral regions by transferring challenging tasks to the municipalities from the state were central in his speech. By this, Eidesgaard was in fact saying that the municipalities were too many and too small and had too limited tasks. In other words, local democracy, even though formally present, lacked content to be effective.

This kind of argumentation has, for example, been presented in this context by Dahl and Tufte (1973) as well as by Harald Baldersheim (1987) who stated that it could of course be claimed that municipal amalgamations, which reduced the number of municipalities and thereby the number of local politicians, appeared to be a centralization of power. But such arrangements could actually prove to be a way to decentralize power, since an increased capacity for service provision also made local units capable of taking over more tasks from state level. If this is the case, steps towards decentralization have been taken through amalgamations and more power given to the local level. The Faroese political scientist Beinta í Jákupsstovu (with Eli Kjersem) has, however, criticised this type of argumentation by questioning to what extent this “reform theory” about large municipalities with considerable capacity holds. She calls this “imitating the organization in the neighboring countries” and questions how these ideas based on the principle of economy of scale, can be functional in the small Faroese case (í Jákupsstovu and Kjersem, 2007). But the idea of increasing efficiency and economies of scale in the municipal sector, and at the same time giving the democracy content – the representatives – a role, was central in the argumentation of the government which introduced the reform ideas in 2008.

But as we have read above, the coalition government initiating the structural reform broke up already in autumn 2008. Little has happened since then. Therefore, Eidesgaard’s democracy argument in support of structural reform still seems to remain

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<sup>12</sup> Aalbu et. al. 2008 p. 34.

the central issue in local democracy in the Faroe Islands. As in for example Iceland, local resistance has been strong and loud against amalgamation reforms. Until 2013 there were two federations for local government in the Faroe Islands, one for the smaller units (Føroya Kommunufelag) and another for the seven largest municipalities (Kommunusamskipan Føroya). That meant that the smaller communities have had their own organizational ground and can have their own voice in the public debate. And this voice has been strong in expressing the view that the smaller municipalities are sustainable units and are doing well. How this will develop with the merger of the two local authorities associations from the beginning of 2014 is too early to say, but a majority of 21 municipalities against 7 emerges from the earlier association of smaller communities. It is most likely that different views on local democracy in the Faroe Islands will remain.

## **3.2 Greenland**

Greenland has always had a two tier government system, state level and local level. Before the structural reform in 2009, there were local councils in each of the 18 municipalities and elected neighbourhood councils (bygdebestyrelser) as well in every neighbourhood (bygder). In the local government elections in Greenland 2005, 28.8 percent of those elected were women. This was a great increase since 1979 – 2001 the share of women had been between 10 and 19 percent (Poppel & Kleist, 2009).

### **3.2.1 Current challenges to local democracy in Greenland**

In his report to the Greenland Structural Committee (Strukturudvalget) in 2005 the Danish political scientist Ulrik Kjær from the University of Southern Denmark pointed out what the consequences of the reform would be for local democracy in Greenland. He raised a warning flag as to the form of geographical representation in the new extensive municipalities, not at least due to the many instances of very difficult communications between regions, villages and towns. In such a situation small and isolated places would suffer democratic deficits as peripheries in more than one sense. Kjær argued that it was very important, from a democratic point of view and with consideration to welfare services in the new municipalities, that smaller neighbourhoods should not lose all power within the new enlarged municipality (Kjær, 2005). Binderkrantz and Jacobsen (2007) also raised similar questions about the

democratic aspect. According to them, increased costs, due to more travel between neighbourhoods in the new municipalities was to be met with a law on the use of videoconferences between isolated villages and neighbourhoods. A research project on the consequences of seven municipal amalgamations in Iceland in the 1990s showed that in some cases small and peripheral areas suffered democratic deficits and losses of services after having become part of a larger municipality (Eythórsson and Jóhannesson, 2002).

In the Annual Report 2011 of The Greenland Federation of Municipalities (KANUKOKA), local democracy is discussed in a separate chapter. It is stated that local democracy was not discussed broadly before the great amalgamations in 2009 – warnings from the scientists did clearly not get through. But in the report it is further stated that now, 3 years after, it is time to go deeper into that discussion. In the beginning of 2009 each of the four new municipalities was to establish a “geographical mandate” for every one of the former 18 municipalities. However, this was only to apply for the first four year mandate period. The annual report refers to hearings on experiences of this, conducted by the Ministry of the Interior. The hearing showed clearly that the mandate had had different practical significance in the four municipalities and that it seems that the municipalities had understood the term “geographical mandate” very differently.

In its schedule for structural reform the Greenland Structural Committee set the time period for negotiations between the Home Rule and the municipalities on transfer of tasks to the local level as 2007 - 2013.<sup>13</sup> As we have seen in the preceding chapter the transfers from the Home Rule to the municipal sector have not at all been extensive until now, but still things are moving in that direction. Strengthening of the local level by democratic measures to compensate for the effects of the great reform and strengthening democracy by increasing the services local communities are to have in their own power, has, so far only been partly implemented.

In a meeting of representatives held by the Greenland Federation of Municipalities (KANUKOKA) in June 2013 representatives from the municipalities formally

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[http://dk.nanoq.gl/Emner/Landsstyre/Departementer/Dep\\_for\\_indenrigsanliggende/Natur\\_og\\_Miljoe/Indenrigs\\_kontor/Til\\_kommunerne/Strukturreformen/Tidsplan.aspx](http://dk.nanoq.gl/Emner/Landsstyre/Departementer/Dep_for_indenrigsanliggende/Natur_og_Miljoe/Indenrigs_kontor/Til_kommunerne/Strukturreformen/Tidsplan.aspx)

expressed their evaluation of the impact of the 2009 structural reform, and there were some critical voices on both democracy and services.<sup>14</sup> For example Kelly Berthelsen from Kommune Kujalleq:

*Når man skal drøfte kommunesammenlægningens betydning for os, må det siges, at den økonomiske situation har givet os meget negative oplevelser. Forbedringerne, som skulle vise sig for befolkningen, har været vanskelige at få øje på. Reduktioner i servicen har været nødvendige. Også fordi forholdene indenfor kommunen har været forskellige. Dem, som har haft dårligere forhold, mærkede forbedringerne. Men dem som havde haft bedre forhold, har ved harmoniseringen oplevet forringelser – f.eks. er priserne for affaldshåndteringen nogle steder steget. Derfor har kommunesammenlægningens fordele været svære at få øje på hos befolkningen. Byer, som ikke fik tilfredsstillende repræsentation i kommunalbestyrelserne sidste valgperiode, har følt en forringelse i medbestemmelsen, og nogle bygder, som ikke fik indvalgt repræsentanter ind i de nye fælles bygdebestyrelser, har også mærket forringelserne. Dette er fortsat gældende i dag.*

And from the representative Asii Chemnitz Narup from Kommuneqarfik Sermersooq:

*I forbindelse med etableringen af storkommunerne mærkede byernes befolkninger i Nuuk, Paamiut, Tasiilaq og Ittoqqortoormiit, at den lokaldemokratiske indflydelse blev noget svagere. Der blev færre folkevalgte, og kommunalbestyrelsesmedlemmerne var nu for hele storkommunen. Bygdebefolkningerne har deres stadig egne folkevalgte bestyrelser. Disse bliver årligt samlet til møde af kommunalbestyrelsen. Men fordi bybefolkningernes medbestemmelse synes at være blevet reduceret, er vi nu ved at oprette lokale råd, som skal fungere som ydre gren for den kommunalbestyrelse, som nu er blevet reduceret fra 21 til 19 medlemmer.*

These two examples taken from the resume of this meeting in June 2013 clearly show that there are problems with the representation of the small villages all over Greenland in their new democratic order.

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<sup>14</sup> Referat. Delegeretmøde i KANUKOKA 2013.

### **3.3 Iceland**

Iceland has always had a two tier government system, except in the period between 1874 and 1904 when a median level, Amts, were functional. This was done under the Danish rule but abolished when Iceland obtained its first minister. In the local government elections in 2010, 204 (40%) women were elected out of a total of 512 seats in local councils.

#### **3.3.1 Current challenges to local democracy in Iceland**

Some research has been done on the consequences and effects of municipal amalgamations in Iceland. An evaluation study of seven amalgamations undertaken in Iceland in 1994 and 1998, where 37 municipalities were involved, showed evident signs of democratic deficits for the smaller and peripheral municipalities. Surveys among the citizens clearly indicated that people outside the central service and administration locations felt that they were now more distant from their politicians than before and thereby their opportunities to influence and lobby decisions were much more limited. Furthermore, the majority of the people living in the peripheral parts believed that political power was now concentrated in these ‘central places’ (Eythórsson & Jóhannesson, 2002). No other evaluation study has been done since and the results remain. There are some examples of discontent in former municipalities and attempts have been made to accomplish splits or breakouts. This has, for example, been done several times in Sweden since the municipal structural reform in the 1970s and seven such requests were accepted by the Swedish government between 1974 and 1985 (Erlingsson 2005). In the Icelandic case such attempts have always been rejected. The democratic consequences of amalgamations have not been high on the political agenda and can hardly be seen as an emerging problem. The evaluation project from 2002 also showed unmistakable signs of positive economic developments in many of the small municipalities involved in amalgamations, so there have been both positive and negative consequences (Eythórsson & Jóhannesson, 2002; Eythórsson, 2009).

Other local democratic questions have been on the Icelandic political agenda for the past ten years or so. An emphasis on increased citizen democracy was actualized in the new and revised Local Government Act of 2012. For the first time there was a chapter on citizen democracy – called “consulting with citizens”. In this chapter new topics

appear in this context. Clauses on citizen democracy, citizen congress, citizen meetings and local referenda were all found in the Act. Furthermore, a minimum percentage of voters required to enforce citizen meetings and referendums on issues, was defined (Eythórsson, 2012).

In a previous chapter we have seen that the earlier emphasis on strengthening the municipal level in Iceland by amalgamating and enlarging individual units seems to be fading out. Instead cooperation between municipalities appears to be practised to a greater extent. The transfer of services for people with handicaps from the state to local level in was completed in 2011. Only six municipalities in the whole country are administering this task by themselves and in nine cases it is run by inter-municipal cooperation projects (*byggðasamlög*) with two to thirteen municipalities involved. Since the Ministry of the Interior defined the minimum size for running handicap services as a population of 8000, the transfer could not comprise every individual municipality. So, tasks are being transferred from state level to local level without adapting the municipal structure to the increased administrative responsibilities. Instead, this is solved and made possible by cooperation projects around the country. There is a further interest for transfer of responsibilities from the state to local level among both state and local politicians (Eythórsson & Arnarsson 2012). A commission on stronger municipal level suggested in 2012 that the responsibility for elderly care, home nursing and health centres should be transferred in coming years. Upper secondary schools have also been mentioned in this context. Increased municipal cooperation will be necessary if this is going to come about. The commission also suggested in its paper from 2012 that regional federations of local authorities should be strengthened in the roles of coordinating, implementing and policy making. This raises important questions on democracy. Since there is no formal elected intermediate stage between state government and municipalities this would mean transfer of power from the elected representatives at the local level to a cooperative organ – not elected but under a board of directors comprising representatives from the municipalities involved. A delegation or endorsement of power, of that kind is likely to weaken local democracy rather than strengthen it.

In our interview with the Chairman of the Board of the Icelandic Federation of Municipalities he expressed his doubts about this eventual development on transferring more and more tasks from the state to local level merely to have them taken over by indirectly elected organs. He even cited the concept of effectiveness as an argument against it, since decision making in a board with representatives from several municipalities could be cumbersome and ineffective. In this case a formally elected median level would be a better solution, but he personally preferred amalgamations as the effective way if a further transfer of tasks were to be implemented (Halldórsson, 2013).

### **3.4 West Nordic local democracy in sum**

As we have seen, current municipal structure in these three countries is less similar than it used to be. After the great reform in Greenland the municipalities are not only largest in areal but also in population in the West Nordic comparative perspective. Table 2.2 above has shown us, however, that the Faroese and Icelandic municipal structures are quite similar compared with the situation in Greenland. The most emerging question about local democracy in Greenland is the geographical representation of small villages and neighbourhoods after the great reform. The concern, just before the amalgamations came into practice, was how these smaller and often very isolated neighborhoods could be democratically included in the new municipalities and have something to say or decide about their matters. In the Faroe Islands the big issue seems to be mostly connected to the content of local democracy, since the numerous small municipalities have limited tasks. This is, however, not the standpoint of the smaller municipalities which run their own federation and claim that they are doing well as they are. But recently, the two municipal federations were merged into one, so the possibilities for the smaller municipalities to act as such are perhaps at risk. In the Icelandic case much of the discussion on democracy on the municipal level is about direct citizen democracy versus the more traditional representative democracy. Increased citizen participation in decision making between elections seems to be a key word nowadays. This concern has been clearly emphasized in the Local Government Act of 2011. Another emerging discussion in Iceland is about local democracy and municipal cooperation. The greater emphasis on inter-municipal



cooperation instead of municipal amalgamations is believed to affect the power structure of local authorities involved, since the cooperation projects are run by boards which are not elected by the people.

## **4 Service production and effectiveness of the municipalities**

In this chapter the authors try to provide some cross national comparisons of government size, local government size, and the efficiency of local government. An attempt is also made to investigate whether the countries in question have experienced a reduction of expenses as a result of municipal amalgamations. In addition, the variety of municipal services addressed and compared between countries. Furthermore, some evidence for potential scale economies is suggested. Since classifications of municipal affairs are not fully identical between countries, the authors decided to use United Nations international classification of public expenditures (“Detailed structure and explanatory notes of COFOG,” 2013).

### **4.1 Research and literature**

It has been argued that urban population contributes to social benefit in terms of agglomeration economies. „In the presence of agglomeration economies, average production cost is generally lower, which in knowledge-based industries increases profits, returns to shareholders and the real wages of highly skilled labour“(Karlsson, 2012, pp. 125–126). Thus, agglomeration economies are similar to scale economies in being a source of economic growth and higher welfare. Urban population contributes to social cost as well, since an additional citizen fuels traffic congestion, air pollution etc. When the population grows the benefit increases regressively while the cost increases progressively and thus each community has a global maximum of net benefit with respect to local population.

Comparatively, a provision of public services is likely to generate scale economies in step with agglomeration economies and thus lower average cost. Rosen (2008) suggested that scale economies were present in public services such as in fire departments and libraries. Similar results were addressed in a general study for Britain, where this seems to be the case in provision of health care services, water supplies, and telecommunications (Burrige, 2008). Furthermore, scale economies are present in primary and upper secondary schools, both regarding overhead and teaching cost. However, diseconomies of scale became apparent in teaching when quality was taken into account. Similar results were found by Duncombe and Yinger (2007) and Duncombe et al. (1995).

Several studies have been performed regarding the direct impact of amalgamation of municipalities on their operational cost in providing local services. Grétar Þór Eyþórsson and Hjalti Jóhannesson (2002, p. 261) did not detect any change in municipalities' operational cost for service in the wake of an amalgamation in Iceland. They argued that a possible gain in terms of lower cost had been spent on improved service. Rouse and Putterill (2005) did not succeed when they tried to prove that amalgamation of municipalities resulted in efficient road maintenance. Tyrefors Hinnerich (2009) showed, however, that municipalities were likely run into higher debts in the antecedents of amalgamation and be free riders in the merged municipality. Moreover, the smaller the municipality (relatively) the more likely they would be to indulge in such behaviour. This is in line with Jordahl and Liang (2010). A related topic was presented by Dur and Staal (2008) where small municipalities become free riders due to their proximity to another larger urban area. If a small rural municipality is close to a city belonging to another municipality that offers a vast variety of both private and public services this would serve the inhabitants in both municipalities and the local government of the small municipality would not develop the services concerned due to lack of pressure from the local community. When or if those communities merge, the service level of the small community will still be low or possibly lower according to Eythórsson and Jóhannesson (2002, p. 261).

Several studies do not detect scale economies or any other evidence for lowered cost following the amalgamations of municipalities (Byrnes & Dollery, 2002; Dollery, Byrnes, & Crase, 2007; Dollery, Crase, & Johnson, 2006). Furthermore, a larger municipality is not necessarily more cost efficient and collaboration between municipalities is more likely to lower cost than amalgamation (Dollery et al., 2007). A new Danish study, based on a large amalgamation process in the year 2007 where the number of municipalities dropped from 271 to 98, suggested that larger municipalities are no more cost efficient than smaller ones (Houlberg, 2011). Note that, only overhead cost was included in the analysis, this being the type of cost where potential gain is highest (Karlsson & Jónsson, 2011).

Amalgamations of municipalities can bring other challenges. Dahl (1967) pointed out that the democracy was significantly weaker in larger communities than smaller

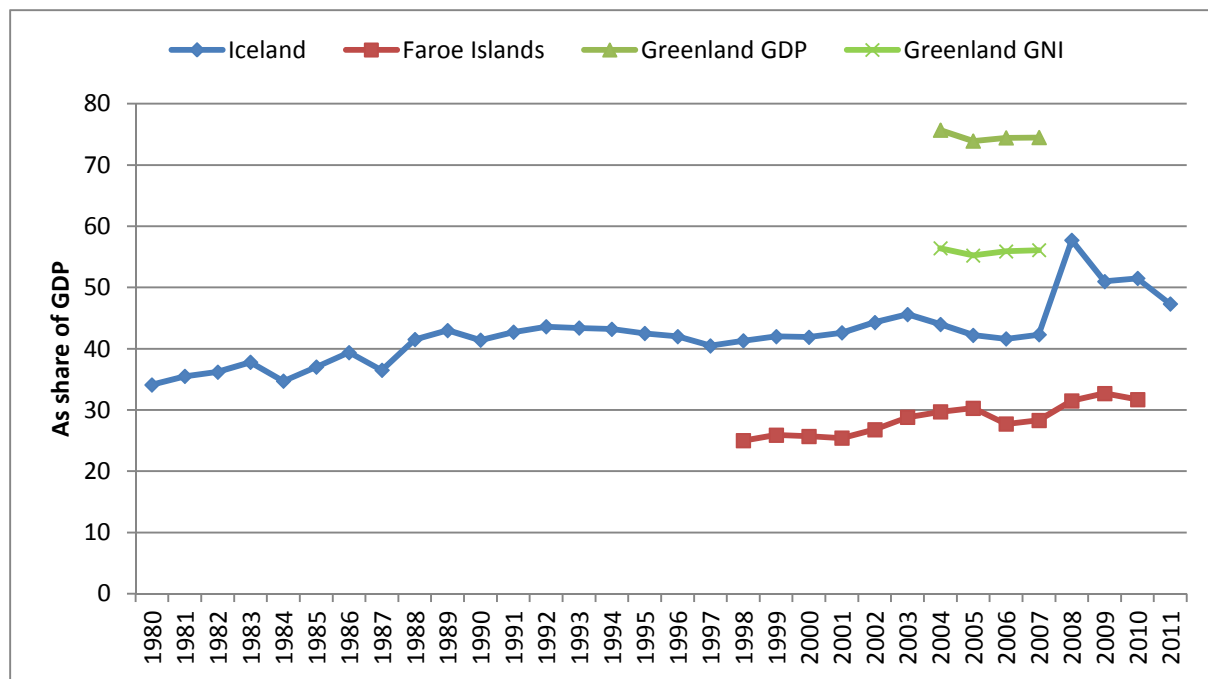
ones. If the amalgamation includes several populous municipalities the citizens would have considerably reduced access to the local authorities and thus democracy would be weakened. This is not in line with Newton (1982) who claimed that large units of government are no less democratic than small ones because large units are able to provide a wider variety of services than smaller communities. Thus, the civilians of smaller municipalities have to seek the missing services in other municipalities – services provided by a government that have been voted by others. Nielsen (2003), on the other hand, concluded that municipality amalgamation has a negative impact on democracy; it would be best to keep a size of a municipality limited to one dominant urban area. This research is based on data for municipality amalgamation in Sweden in the period 1952-1974.

## **4.2 Central and local government and cost efficiency**

This chapter provides a cross-national comparison of the government size, local government size, and the efficiency of the local government. Furthermore, the chapter also sheds some light on whether the countries under consideration have experienced a reduction in municipal expenditure following their amalgamations.

### **4.2.1 Government size**

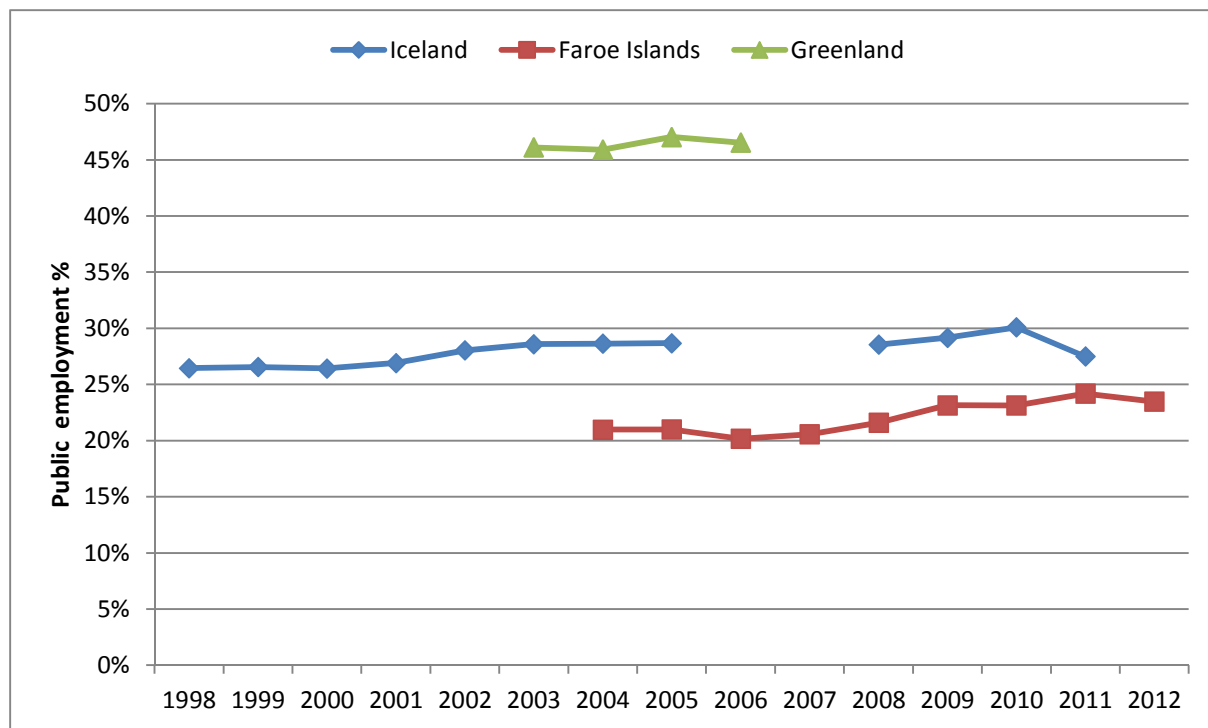
A comparison of government size in Iceland, the Faroe Islands, and Greenland will be explored before any analysis of local government is provided.



**Figure 4-1. Public spending as a share of GDP in the three countries**

For Greenland the numbers were also presented as a share of Gross National Income (GNI). Source: Statistics Iceland, the Faroe Islands, and Greenland

Public spending as a share of gross domestic product (GDP) differs significantly between the countries (Figure 4-1). In 2005 it was 30% in Faroe Islands, 42% in Iceland, and 74% in Greenland. Since gross national income (GNI) is considerably higher than GDP in Greenland due to grants from the Danish state the share becomes lower in terms of GNI, or 55% in 2005. Nevertheless, the share is highest in Greenland among those three countries. The trends are positive for all the countries, especially Iceland and the Faroe Islands – that is, public spending has been increasing with respect to GDP.



**Figure 4-2. Public employment as a share of total employment in the three countries**  
 Source: Statistics Iceland, the Faroe Islands, and Greenland

Accordingly, public employment is highest in Greenland as well (Figure 4-2). It was 46% in Greenland in the year 2004, 29% in Iceland, and 21% in the Faroe Islands. The trend has been rather positive for all the countries, apart from the last year in Iceland which relates to the recent economic crisis. It is, however, remarkable to see how much higher Greenland is compared to the other two. It is possible that larger part of the population live as hunters or farmers in Greenland than in the other two countries and therefore a larger part of their income is not accounted for in the traditional estimation for employment which leads to an overestimation of public employment.

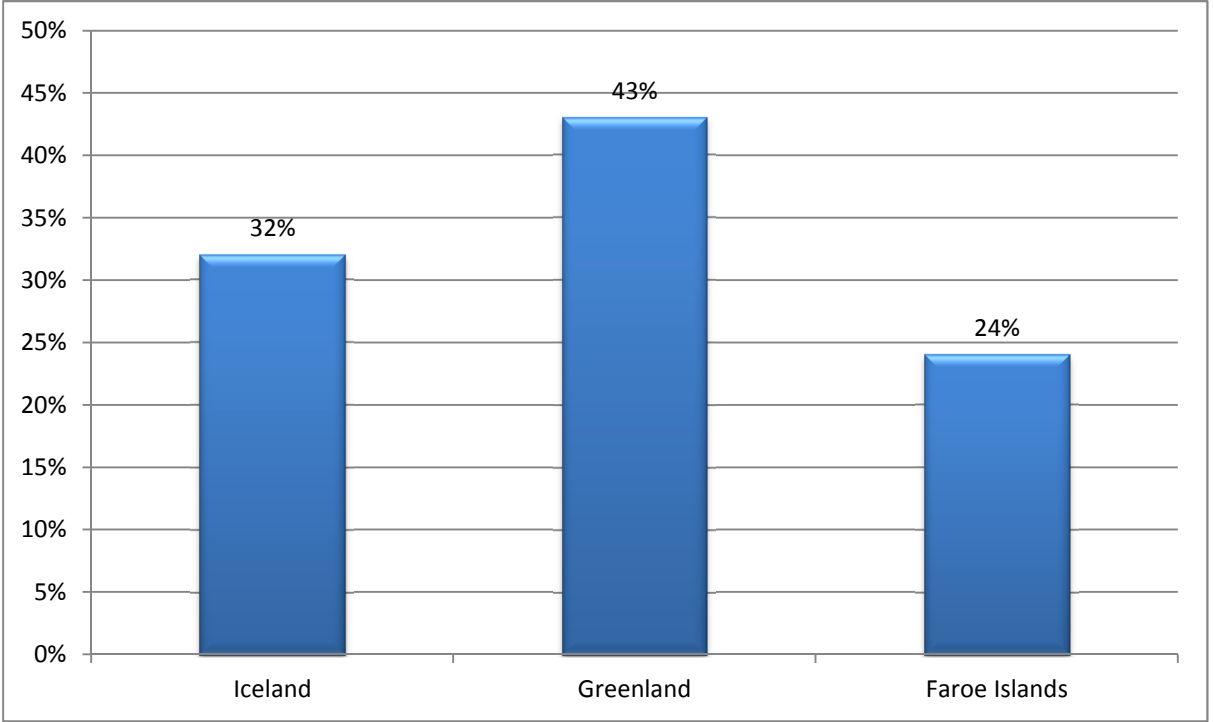
#### 4.2.2 Local government size

Government expenditure is close to 50% of GNP in Iceland. According to Statistics Iceland, local government in Iceland accounted for 35% of total public purchases in 2010 and had grown from 32% in 1998 to 37% in 2011.

According to Statistics Greenland gross domestic product was 11,063 million Danish kroner (MDK) in the year 2007 and total public expenditure was 8,239 MDK – that is 74% of GDP. However, available national income (GNI) was 14,687 MDK in that very same year, mainly because of grants from Denmark. Public expenditure is only 56% with respect to GNI. The same source reports that total public purchases

were 6,638 MDK in 2010, while the municipalities' purchases were 2,843 MDK. Thus, municipalities account for 43% of public purchases.

GDP was 12,942 MDK in 2010 in the Faroe Islands (Statistics Faroe Islands, 21.02.13). That year, public expenditure was 4,096 MDK or 31.7% of GDP. This share has been rising since 1998, when it was 25%, with a cutback in 2005 and 2010 (Figure 4-1). In 2010, total purchases of local governments only were 998 MDK, or 24% of public expenditure.



**Figure 4-3. Local government share in government purchases in 2010**  
Source: Statistics Iceland, Greenland, and the Faroe Islands

The relative size of local government is largest in Greenland and smallest in the Faroe Islands; that is, in Iceland 32% of public expenditure is spent by the municipalities, 43% in Greenland, and 24% in the Faroe Islands (Figure 4-3). This suggests that centralization is strongest in the Faroe Islands and by far the lowest in Greenland. In other Nordic countries the local government budget is approximately 2/3 of total government expenditure (Kristinsson, 2001, p. 46). This number also includes the purchases of individual counties as well. Among Nordic countries the two tier system is to be found in Iceland, Greenland, the Faroe Islands, Åland, and Finland, while a

three tier system (municipalities, counties, and the state) is the rule in Norway, Denmark, and Sweden.

**4.2.3 Cost efficiency of local government**

When the expenditures per capita were corrected for service level<sup>15</sup> Iceland delivered the lowest cost of them all and Greenland was the most expensive, or 51,000 DKK (Table 4-1). It is to be expected that the world’s most extensive municipalities – in Greenland - along with harsh terrain and expensive transportation will account for some of the difference.

**Table 4-1. National sample statistics for 2010**  
 Source: Statistics of Iceland, Greenland, and the Faroe Islands

Country	Total population	Number of municipalities	Municipalities median population	Local government purchases in MDK	Purchases per. capita in MDK	Purchases per. capita corrected for service level <sup>16</sup> in MDK
Iceland	317.630	74	893	6,42717	0.020	0.027
Greenland	56.247	4	13,713	2,843	0.051	0.051
Faroe Islands	48.621	30	629	998	0.021	0.037

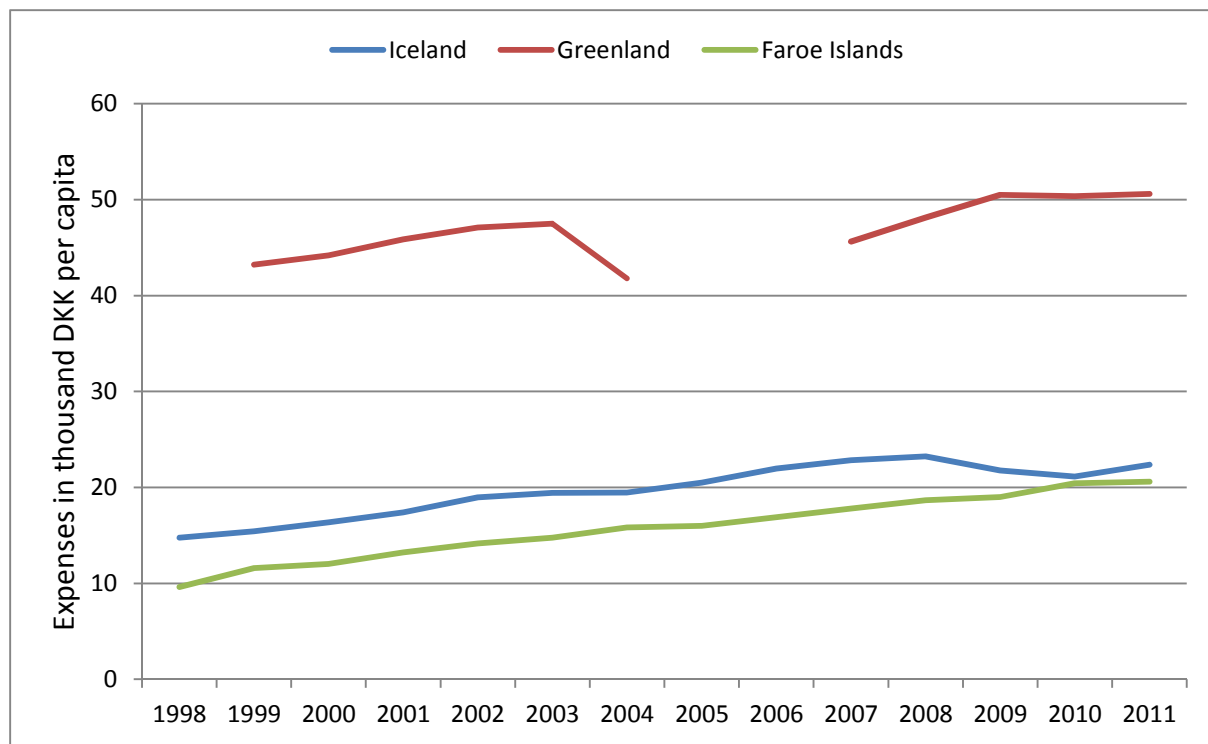
Note that there are only four municipalities in Greenland and the overall largest municipalities in terms of median population (Table 4-1). Iceland has the largest number of municipalities, while the cost per capita is the lowest there, when corrected for service level. The Faroe Islands have the smallest municipalities in terms of median population.

<sup>15</sup> Then we assume that the service level correlates perfectly with local government share in government expenditure (see figure).

<sup>16</sup> Purchases per capita multiplied by local government share in Greenland and divided by local government size for each respective country.

<sup>17</sup> It is 140,125 MKR at the currency value of 21.802 IKR per one DKK.





**Figure 4-4. The development of the municipalities' purchases per capita**

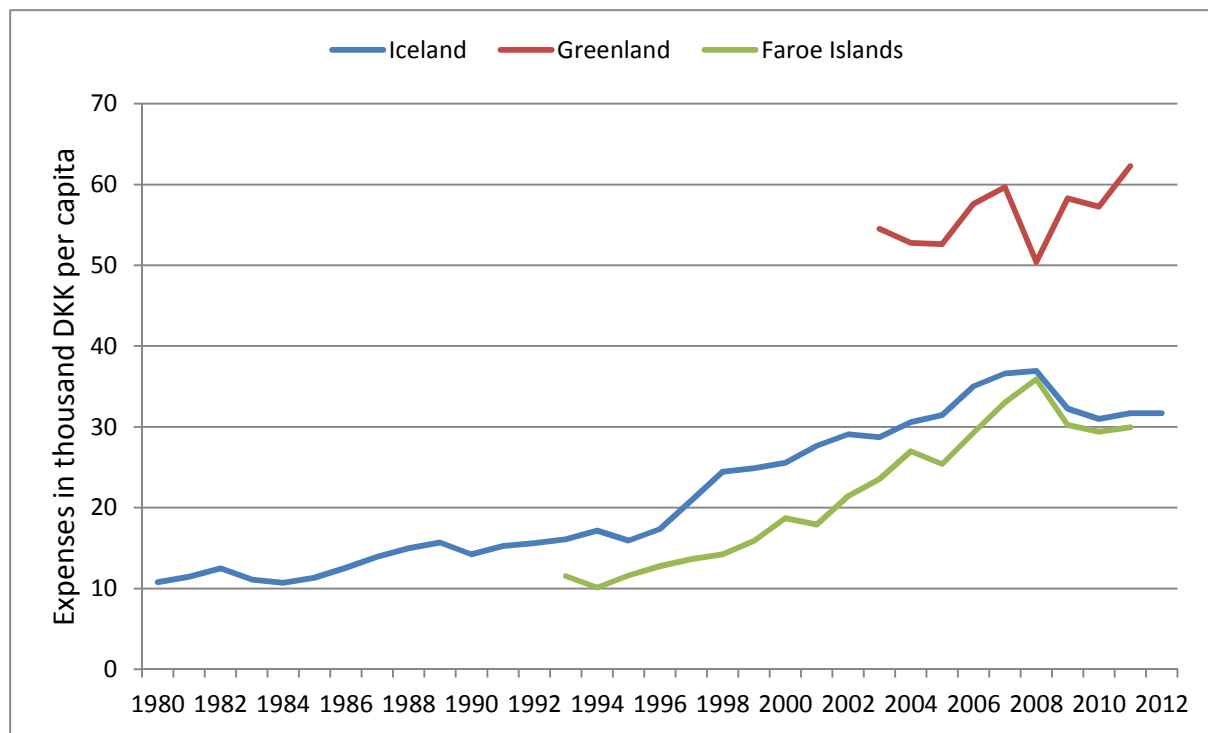
Amounts were corrected for national price indexes.

Source: Statistics of Iceland, Greenland, and the Faroe Islands

As noted earlier<sup>18</sup> Greenland municipalities merged into four in the year 2008 a change formally implemented 1st January 2009. No changes in municipality purchases were detected at that period of time in data from Statistics Greenland (Figure 4-4). Moreover, in a recent report (*Kommunernes økonomiske vilkår*, 2011) where the administration cost of Greenland municipalities was compared between the years 2008 and 2009, no cost reduction was noted. On the contrary, administration cost seemed to have increased following the amalgamation.

When the total expenses<sup>18</sup> of municipalities are investigated, those were found to have decreased in Greenland in 2008 by 16% in real terms, but returned back almost to the same amount the year after (Figure 4-5).

<sup>18</sup> Total expenses of municipalities differ from purchases since these cover all cost while purchases only comprise cost of direct service to clients. Interest payments exemplify an item not included in municipalities' purchases.



**Figure 4-5. The development of the municipalities' total expenses per capita**

Amounts were corrected for the development of the national price indexes.

Source: Statistics of Iceland, Greenland, and Faroe Islands.

Furthermore, no services were delivered from the central government to the local government in Greenland (decentralization) that year. The affairs of handicapped people were the first task transferred to the municipalities in the beginning of the year 2011, two years after the amalgamation. Two more services, psychological pedagogical consultancy and special teaching in the upper secondary schools, were passed to the municipalities in January 2012. Presumably, these two projects are rather small with respect to budget. (Kanukoka, 2012, p. 8) So, a transfer of public services from the state to municipalities does not explain the fact that municipality purchases, total expenses, and administration cost failed to decrease after the amalgamations in 2009.

Only two functions have been handed out from the state to municipalities in the Faroe Islands; that is, kindergartens in the year 2000 and the affairs of children – i.e. children's protection – in 2005. Municipal purchases per capita have, however, been steadily increasing in the period 1998-2011 (Figure 4-4).

The municipalities' total expenses per capita in the Faroe Islands have not decreased during this time apart from the period after 2008 when the number of

municipalities went down from 35 to 30 – or by 17% between 2008 and 2011 (Figure 4-5).

The most likely explanation for the cost reduction in 2008 is the local government election that year. Local authorities tend to stretch the budget in their final year and thus deliver a low cash level to the next council majority. This is particularly true of public investment (“Ársrokskapirnir hjá kommununum fyri 2009,” n.d.). A slight cost reduction both in 2000 and 2004 supports this notion, since they vote every fourth year. Note, however, that the cost reduction in 2000 and 2004 only lasted one year while the cost reduction in 2008 still remains. This could be traced to the decentralisation in 2000 (kindergartens) and 2004 (children’s protection), but not in 2008. This suggests that the amalgamation of municipalities in the Faroe Islands might have returned some cost reduction.

In the Icelandic case, the development of municipal structure compared to the pattern of municipal expenditure shows no signs of change. Most of the massive amalgamations between 1994 and 1998 were voluntary, even though the government had initiated a reform with the referendum in 1993. The municipalities have received two tasks from the central government: The primary school in 1996 and the affairs of handicapped people in 2011 (Eythórsson, 2012).

Therefore, apart from the Faroe Islands, this simple descriptive analysis does not suggest that any improved efficiency has been achieved in the wake of municipality amalgamations. Furthermore, Iceland is the most efficient country in providing municipality services when correction has been made for the service level – even though it does not have the largest municipalities in terms of median population. Moreover, the budget of local government has been growing both in Iceland and the Faroe Islands for more than a decade while the situation in Greenland has remained more stable.

#### **4.3 The wide range of variety in local public services and implications for potential efficiency**

The purpose of the present chapter is to address the variety of municipal services and compare those between the countries in question. The chapter will also consider evidence for any potential scale economies which might indicate an average decrease

following a municipality amalgamation. The first section will be devoted to the variety of the projects for each country, their cost and scale economies, while the second compares the countries as a whole. Unfortunately, the categorization of services differs between those two sections, since national classification is not identical among the three countries. Iceland and the Faroe Islands have, however, implemented a classification according to international standards along with the local standards. Iceland has classified data by international standards for several years while the Faroe Islands have only done so for two years. We will use the local standards in the first section because they give us clearer information about project variety, while the international standards are better suited for the cross border comparison conducted in the second section. Moreover, since the data is not classified by international standards for every single municipality, data categorized by local standards was needed to look for any potential scale economies in the first section.

#### 4.3.1 Iceland

Services of the following categories are provided by local government in Iceland (Árbók Sveitarfélaga, 2012, p. 64):

1. Social services
2. Health care
3. Education
4. Culture
5. Sports and youth welfare
6. Fire department and public disaster protection
7. Hygiene
8. Planning and construction
9. Traffic and transportation
10. Environmental affairs
11. Industrial affairs

Since the bookkeeping of Icelandic municipalities has been more or less coordinated, financial statements from one of them will be used as a reference (“Borgarbyggð: Sundurliðanir ársreiknings 2011,” n.d., pp. 8–9) for further details of every single category. A public notification regarding the coordination will also be used as reference (“Um breytingu á auglýsingu nr. 414/2001 um flokkun og greiningu í

bókhaldi og reikningsskilum sveitarfélaga,” 2011) together with laws regarding this matter.

**Social services** are partly provided by local government. The objective of the social services provided by municipalities is to offer the citizens financial and social security, including provision of housing for the poor. It includes social and financial counselling and contribution. A provision of social home care, unemployment and employment services is included as well. Moreover, social services address the affairs of children, youth, the handicapped, the elderly, the homeless, alcoholics and drug addicts. (“Lög um félagsþjónustu sveitarfélaga nr. 40/1991,” n.d.1, 2).

**Health care** is mainly provided by the central government in Iceland which paid 87% of total health care expenses in Iceland 2010 (“Opinber fjármál,” n.d.). Municipalities, however, provide health surveillance (*Rekstur og stjórnun sveitarfélaga: starfsumhverfi, sveitarstjórnir, stjórnunarhættir, skatttekjur og verkefni og fjármál*, 1998, p. 100).

**Education.** Municipalities in Iceland offer primary schools and preschools while the central government runs upper secondary schools and universities. Primary schools are provided without demanding any tuition fee from parents while the parents are charged for the service of preschools which generates their total income. Parents pay a very limited amount for this service since preschool income is only 17.2% of their total operational cost and the rest is financed by local government (*Árbók Sveitarfélaga 2012*, 2012, p. 163). The primary school is mandatory in Iceland. One could say that it is an unofficial policy in many municipalities to provide preschool for all children that have reached 16 months of age and most of the municipalities manage this aim.

**Culture.** By law, all citizens of Iceland shall have access to a public library and it shall be provided by the municipalities (“Lög um almenningsbókasöfn nr. 36/1997,” n.d.1). This service is part of cultural affairs. Furthermore, municipalities provide cultural museums and community centres as well as arranging festivals which form part of the local culture. (“Borgarbyggð: Sundurliðanir ársreiknings 2011,” n.d., p. 8)

**Sports and youth welfare.** Municipalities, together with the central government, are obliged to support youth recreation such as sports and cultural activities in

collaboration with youth organizations (“Æskulýðslög nr. 70/2007,” n.d.3). This obligation includes running and providing playgrounds, youth centres, central baths, sports centres and sport arenas amongst other services of a smaller scale.

(“Borgarbyggð: Sundurliðanir ársreiknings 2011,” n.d., p. 8)

**Public safety - fire department and public disaster prevention.** Every municipality shall provide a fire department and fire control (“Lög um brunavarnir nr. 75/2000,” n.d.10).

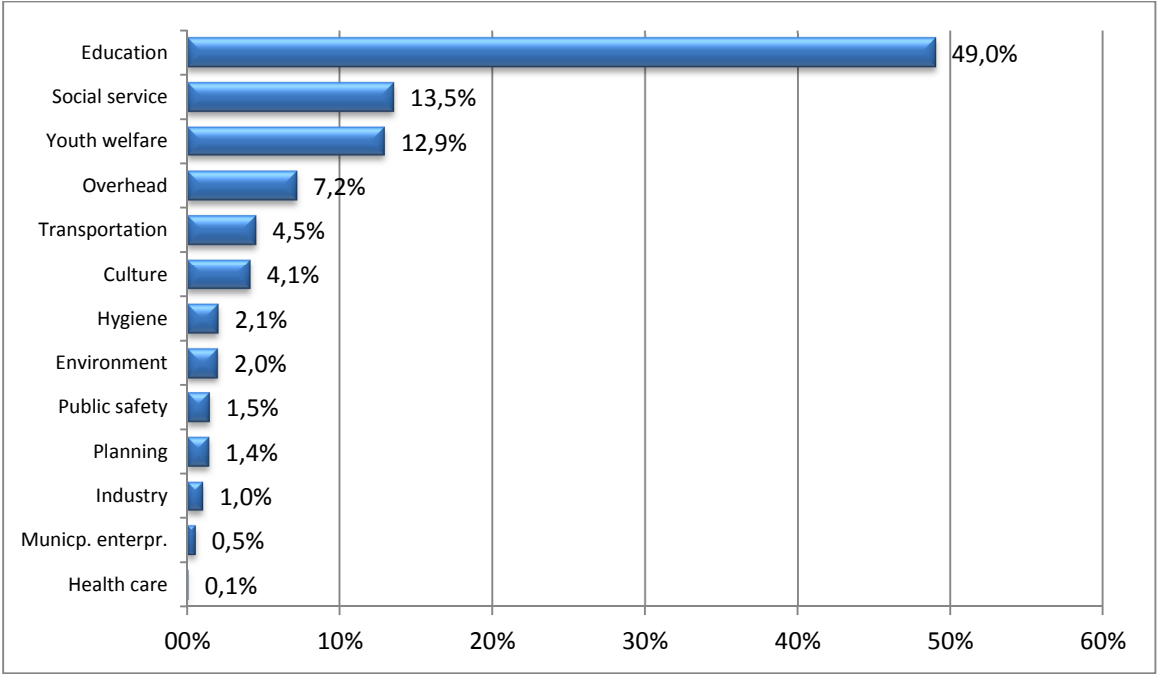
**Hygiene.** According to law, all municipalities shall implement a public health control and pay for its cost. The health control shall provide the citizens with healthy life conditions such as a low level of pollution, absence of vermin, housing conducive to good health, waste disposal, and related issues. The health control issues health licences for running selective types of businesses as well. (“Lög um hollustuhætti og mengunarvarnir nr. 7/1998,” n.d.1, 4, 10)

**Planning and construction.** Planning is the largest current category together with construction control. Construction control includes building security, energy efficiency, pollution, impact on human health, and housing quality amongst other things. The minister of the interior governs planning in Iceland through the Icelandic National Planning Agency (INPA). The municipalities shall, however, implement planning under the surveillance of INPA. INPA assists and consults municipalities in the planning process. (“Lög um mannvirki nr. 160/2010,” n.d.1, “Skipulagslög nr. 123/2010,” n.d.3, 4)

**Traffic and transportation.** Construction and maintenance of municipal roads falls under this category. Roads in Iceland are divided into state roads and municipal roads. Municipal roads are roads in urban areas which do not constitute part of the state road network whose function is to connect all urban areas in Iceland. State roads in urban areas are part of that connection. (“Vegalög nr. 80/2007,” n.d.3, 8, 9, 13) Construction and maintenance of traffic lights and sewers also comes under this category (Rekstur og stjórnun sveitarfélaga: starfsumhverfi, sveitarstjórnir, stjórnunarhættir, skatttekjur og verkefni og fjármál, 1998, p. 100) together with snow removal and de-icing of roads, footpaths and pavements (“Borgarbyggð: Sundurliðanir ársreiknings 2011,” n.d., p. 9).

**Environmental issues.** When it comes to environmental issues, municipalities run public parks, clean and cultivate road surroundings, and manage public decorations (“Borgarbyggð: Sundurliðanir ársreiknings 2011,” n.d., p. 9).

**Industry** (including public industrial support). Municipalities can choose to assist selected branches of industry if found to be necessary such as agriculture and tourism (“Borgarbyggð: Sundurliðanir ársreiknings 2011,” n.d., p. 9). The Icelandic Regional Development Institute addresses regional development issues in collaboration with the municipalities (“Lög um Byggðastofnun nr. 106/1999,” n.d.) – e.g. by running regional development offices.



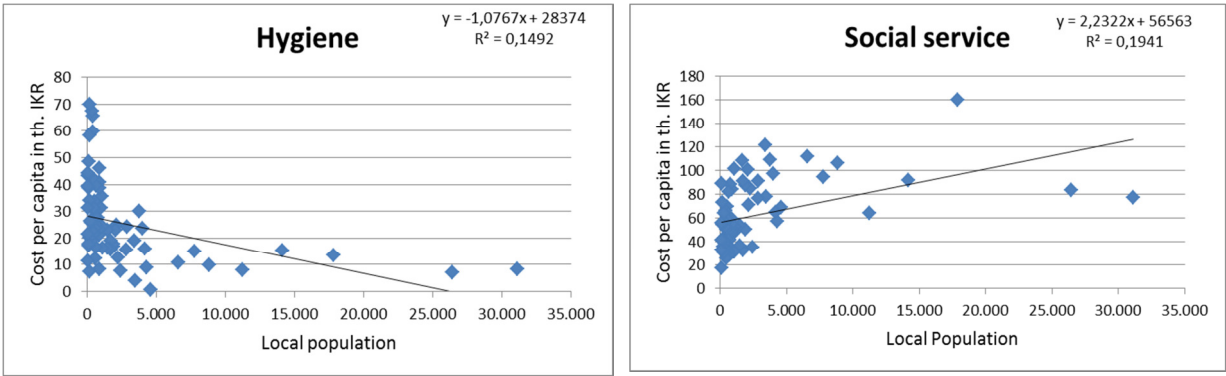
**Figure 4-6. Municipalities’ cost categories in Iceland and their share in total expenditure in 2010**

Source: The Association of Local Authorities in Iceland

According to data from the Federation of municipalities in Iceland, education, social welfare, overhead, and sports and youth welfare count for 83% of the local government budget (Figure 4-6). Thus, the remaining categories involve relatively low expenditure: transportation, culture, hygiene, environment, public safety, planning, industry, municipal enterprises, and health care.

The discussion of cost efficiency in municipalities often focuses on whether larger municipalities are more cost efficient than smaller ones – that is, whether average cost

is lowest in the most populous municipality. This might be the case in the supply of some of the categories addressed above. According to a simple scatter diagram analysis the trend is negative for them all except for social services (Figure 4-7). This suggests that the larger the municipality the lower is average cost for all categories except social services. The trends are strongest for hygiene and overhead cost.



**Figure 4-7. Cost efficiency in hygiene and social services in Iceland.**

This diagram presents cost per capita with respect to municipality size (local population) in hygiene and social services. The data refers to 2011. Source: The Association of Local Authorities in Iceland.

A simple trend line yielded only a weak indication. A more formal and robust estimation suggested that cost efficiency is present in overhead cost (Karlsson & Jónsson, 2011). The study also returned weaker evidence for the hypothesis that cost efficiency might also be present in the categories of hygiene, the public safety, and education. The cost-efficiency of the social services seemed to bear no relation to population.

When this estimation was repeated by a fixed-effect panel data model for Iceland in a recent study (Karlsson, Work in progress) using data from the period 2004-2011, the results suggested that average cost had become lower following amalgamations only in the categories of industry and the culture. Those groups, however, only generate approximately 5% of municipalities’ total costs. Accordingly, the impact of population is rather limited in terms of cost reduction. Moreover, larger municipalities have lower average cost than smaller ones in all categories except social services. A municipality amalgamation would, however, not necessarily return that disparity since it does not include migration and thus a denser population. Therefore, a presence of scale economies does not necessarily lead to lower cost following an amalgamation.



Moreover, the overall results suggest that the impact of an amalgamation on cost structure is rather mixed. Note that the results suggest that the overhead costs do not decrease following an amalgamation. That is in line with a recent Danish study (Houlberg, 2011).

Two experienced persons in matters relating to municipalities – both former mayors - were interviewed in summer 2013. Their opinions regarding cost efficiency and a significant cost reduction subsequent to an amalgamation of municipalities were as follows: Both claimed that overhead costs would be lowered in the wake of amalgamations. However, the total cost of the municipalities would not necessarily be reduced because the money would be spent on services – “which is good”. One of the respondents also claimed that it would take many years – even up to 12 years – to realize (harvest) the full benefit of an amalgamation in terms of restructuring and cost reduction.

So it is possible that a traditional regression analysis of the kind mentioned earlier does not capture all the possible benefits of municipality amalgamation – especially if it takes up to 12 years to be realized.

#### 4.3.2 Greenland

According to the Association of Greenlandic Municipalities (“De kommunale regnskaber,” n.d.) the affairs of the municipalities are classified into education and culture, social service, administration (overhead), technical issues, labour market and businesses, housing, and supply services.

**Administration** (overhead) relates to the expenses of government committees and the public offices. Grants and similar expense items are included as well.

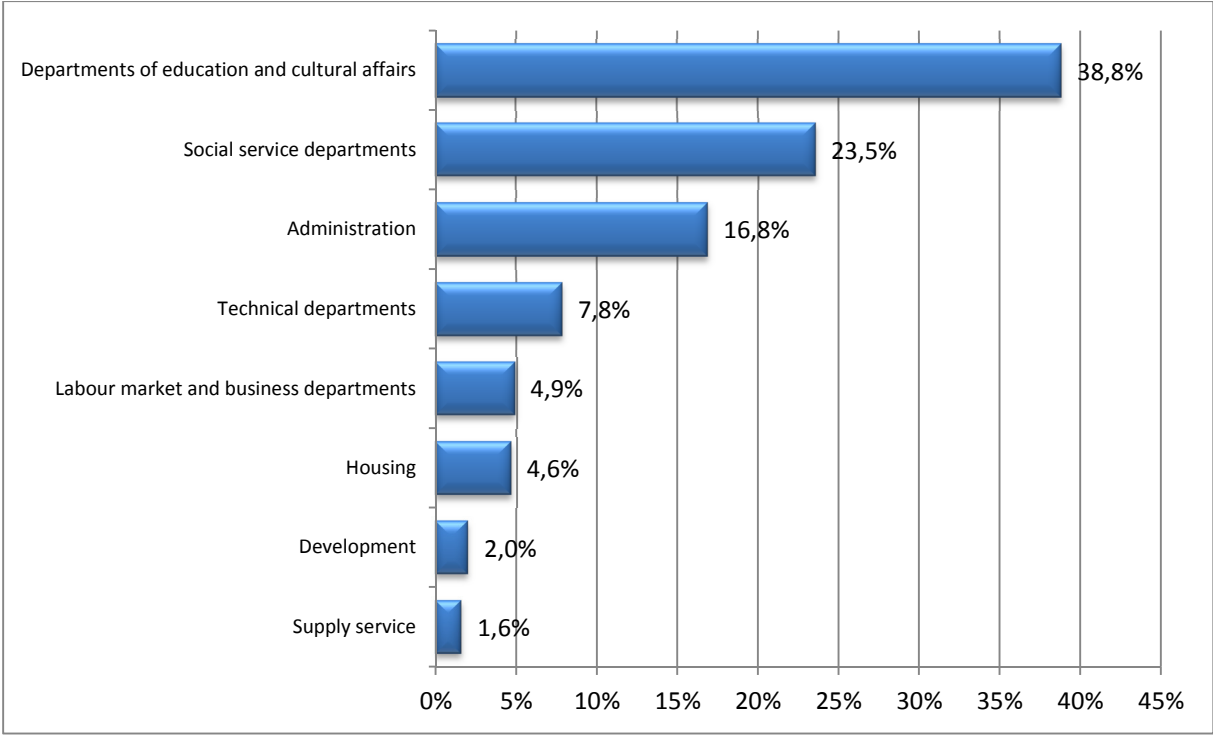
**Technical issues** include fire department, monuments, snow removal, cemeteries, water supplies, sewers, vermin control, and road networks.

**Labour market and business department** covers unemployment benefits and business and regional development costs. **Social services** comprise public housing, care for the elderly, handicapped people, health care, early retirement etc.

**Education and cultural affairs** cover expenses for primary school, preschool, youth centres, libraries, museums and other educational and cultural matters.

**Supply services** include renovation and maintenance of public facilities, central heating and matters of garbage, waste etc.

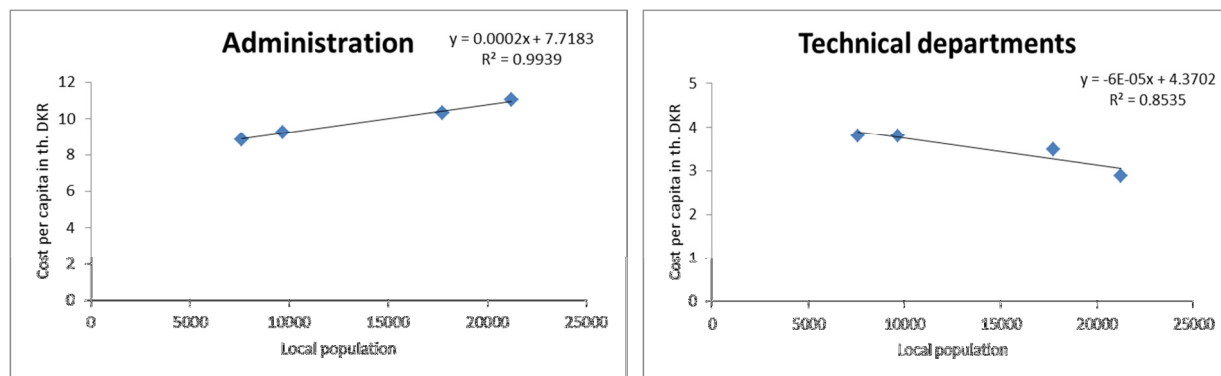
**Housing** covers all cost of public real estate (municipalities' housing) other than maintenance.



**Figure 4-8. Municipal affairs in Greenland and their share in total expenditure in 2010**  
Source: Statistics Greenland

The largest share (38.8%) of Greenland municipal expenses goes into education and cultural affairs. Social affairs are the second largest (23.5%) and then administration (16.8%). Other categories generate 21% of the municipalities' total cost: technical departments, labour and businesses, housing, development, and supply services.

A simple scatterplot analysis suggests that cost efficiency could be present in technical departments, labour market and business affairs. However, indicators for cost inefficiency were current administration, housing, supply services, and education and culture.



**Figure 4-9. Cost efficiency in hygiene and social services in Greenland.**

This is presented as cost per capita with respect to municipality size (local population) in administration and technical departments. The data is from 2010. Source: The Association of Greenlandic Municipalities.

These indicators are weak and unreliable as such, since there are only four municipalities and the study is limited to one year. The indicators were strongest for the administration cost and technical departments.

It is informative to address the inhabitants' opinion regarding the matter: What do the inhabitants of Greenland think of the social- and economic impact of the large reform in 2009? The following information is based on a memo from a meeting of the delegates of the National Union of Greenlandic Municipalities (KANUKOKA) 13-14 June 2013.

The municipalities should be able to provide better, simpler and more flexible services because of the reform in 2009. Those have, however, not been delivered yet, but work is still in progress and there is no reason to lose faith in the project. (Jørgen Wæver Johansen, p. 6) However, until now, both negative and positive effects have been detected.

Increased administration cost (Asii Cheminitz Narup, p. 12) is one of the **negative** effects. This, however, does not apply to all municipalities as noted later. The amalgamation seems to have had a negative impact on the municipalities' economic and operational viability and improvements are not been easily detected. Those communities which suffered poor services prior to the reform have reported improvements while others have experienced a worse level of service (Kelly Berthelsen, p. 14). Increased decentralization<sup>19</sup> was one of the means to improve the

<sup>19</sup> Here decentralization refers to the act when the state transfers tasks or functions to the municipalities.

municipalities' viability. This has, however, turned out to be a slower process than anticipated. The administration of only three projects has been transferred to the municipalities and people are becoming impatient (Asii Cheminitz Narup, p. 13; Hermann Berthelsen, p. 9). Democracy has to some extent been weakened following the amalgamations. (Asii Cheminitz Narup, p.13). Many communities, that did not gain a member in the local parliament, experienced a weakening of democracy (Kelly Berthelsen, p. 14).

Some **positive** implications of the reform have been detected as well, one of which appears to be improved coordination of public services. This means that the municipalities provide comparable service [for the same price] irrespective of their location. (Asii Cheminitz Narup, p. 12; Kelly Berthelsen, p. 14). It was noted, however, that the coordination has not been completed in all parts of the country (Jens Kristian Therkelsen, p. 14). Service levels regarding family matters have been upgraded. Schools and sport services, leisure activities, assistance to families with children, and programmes for alcoholics have been improved. (Asii Cheminitz Narup, p. 12) According to a representative in Qaasuitsup municipality social services have been enhanced following the amalgamation. Some progress has been made regarding the coordination of primary schools. Several new offices have been constructed in order to upgrade family-related services (Jess Svane p. 15).

One municipality (Kujalleq) states that they were forced to reduce administration cost; it currently has the lowest administration expenses among municipalities in Greenland. It has also been found that, because of the reform, the municipalities have been able to run seminars and courses devoted to employment skills and industry – for example on mining and off-shore security. It was noted, furthermore, that the relationship between the municipalities and the “state” has improved. (Kelly Berthelsen, p. 14) If so, it apparently was unsatisfactory at an earlier stage, since some of the municipalities claim that central government has been absent in matters that followed the amalgamation of the municipalities (Jess Svane, p. 10).

Perhaps the structural reform has mostly been devoted to improving public services where performance has been inadequate and failed to address cost efficiency

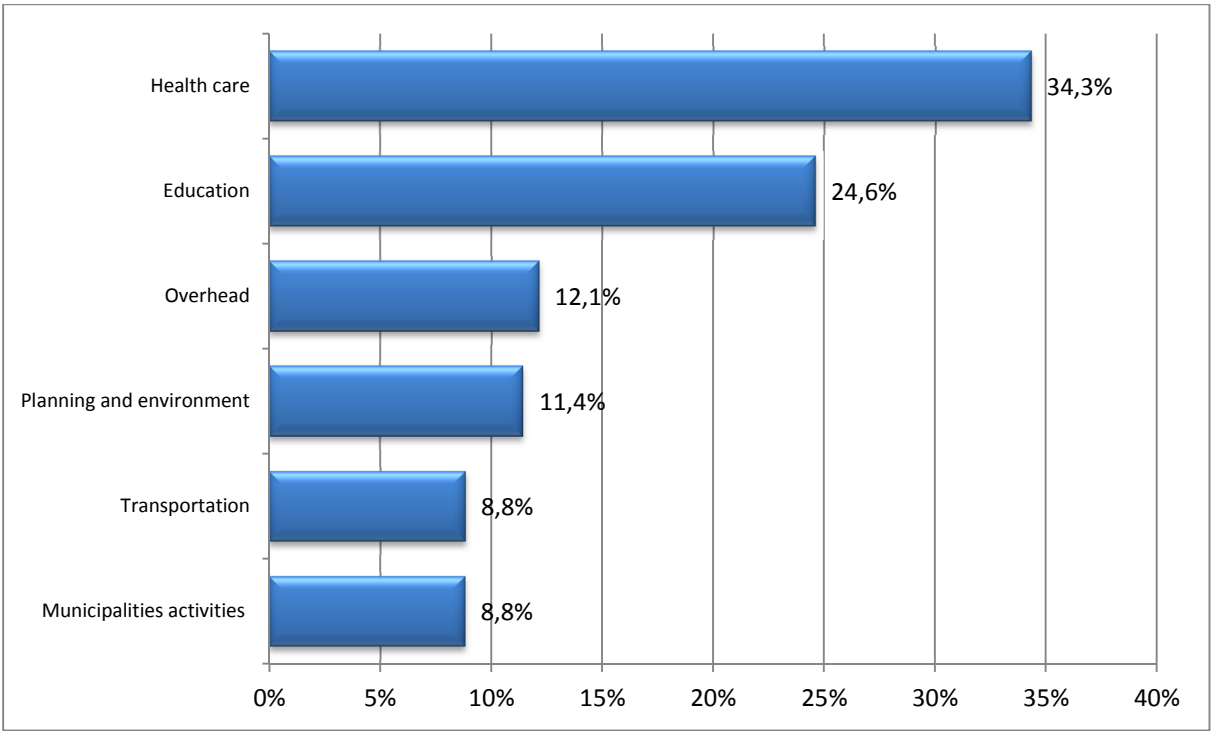
questions. This could be the reason why efficiency in terms of lower overhead cost or lower average cost is not easily detected.

### 4.3.3 The Faroe Islands

According to the ministry of finance in the Faroe Islands (“Kommunali Kontustrongurin,” n.d.) the affairs of the municipalities are classified as overhead, health care, children and youth, teaching, leisure, technical issues, and municipal activities.

**Overhead** relates to the expenses of government committees and public offices. **Municipal activities** include maintenance, fire department, harbours, public transport (busses), and parking lots. **Technical issues** cover expenses regarding sewers, road networks cemeteries, environmental matters, and water supplies.

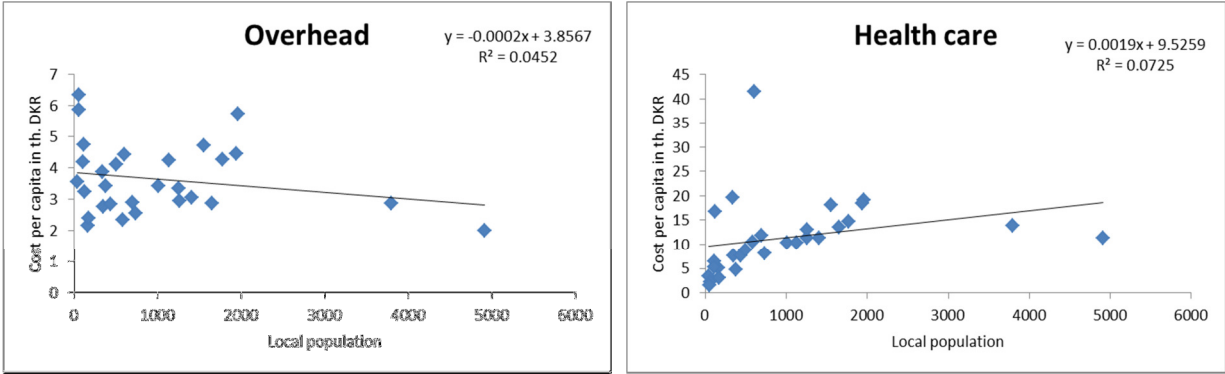
**Leisure** covers libraries, central-baths, and sports centres as well as non-compulsory education such as conservatoire and adult learning. **Teaching** comprises the cost of running primary schools. **Children and youth affairs** include preschool and youth centres etc. **Health care** covers the expenses of the health centres, dentists, assisting the elderly, and childcare.



**Figure 4-10. Municipal affairs in the Faroe Islands and their share in total expenditure in 2009.** Source: Statistics Faroe Islands

In order to make the comparison between central and local government the Statistics for Faroe Islands uses a slightly different classification: Overhead, health care, education, municipal activities, transportation network, planning and environment. Here education includes children and youth, teaching, and leisure. Health care is the largest category with respect to share in total expenses (34.3%). Education is the second largest (24.6%) and the administration is in third place (12.1%). Planning, transportation, and municipal activities comprise approximately 30% of the budget.

A simple scatterplot analysis suggests that cost efficiency could be present in overhead, municipal activities, and transportation network. However, indicators of cost inefficiency were detectable for health care and education. The trend for total cost suggests inefficiency as well.



**Figure 4-11. Cost efficiency in hygiene and social services in the Faroe Islands.**

This is presented as cost per capita with respect to municipality size (local population) in overhead and health care. The data is from 2009. Source: Statistics Faroe Islands.

These trends are insufficient to do any estimation and can be misleading as well. Thus, they must be tested formally by more robust methods. However, those trends that return the most robust estimates - despite their weakness - are for overhead and health care.

According to Sverrisdóttir and Christiansen – those who were interviewed in the Faroe Islands – there appear to be some scale economies but those have not been realised yet. Sverrisdóttir pointed out that primary schools have not yet been restructured following the amalgamations, since by law parents must vote for any suggestion of reform in primary schools. The potential benefit in administration cost is not significant either since its earlier share in total cost was relatively small.

According to Christiansen many of the amalgamations in Faroe Islands have been necessitated by lack of economic resilience or by the bankruptcy of a municipality. However, they seem to have led to an increased service level, for example improved water quality and sewage treatment, especially for the smallest municipalities and there are still margins for additional benefits. Moreover, in larger municipalities employees of higher competence (highly educated specialists) have been hired. Note, however that there are examples of lack of improved services following municipality amalgamation.

So, according to our respondents, municipality amalgamations in the Faroe Islands do not appear to have had significant impact on average cost, but in some cases the quality of local public services has improved.

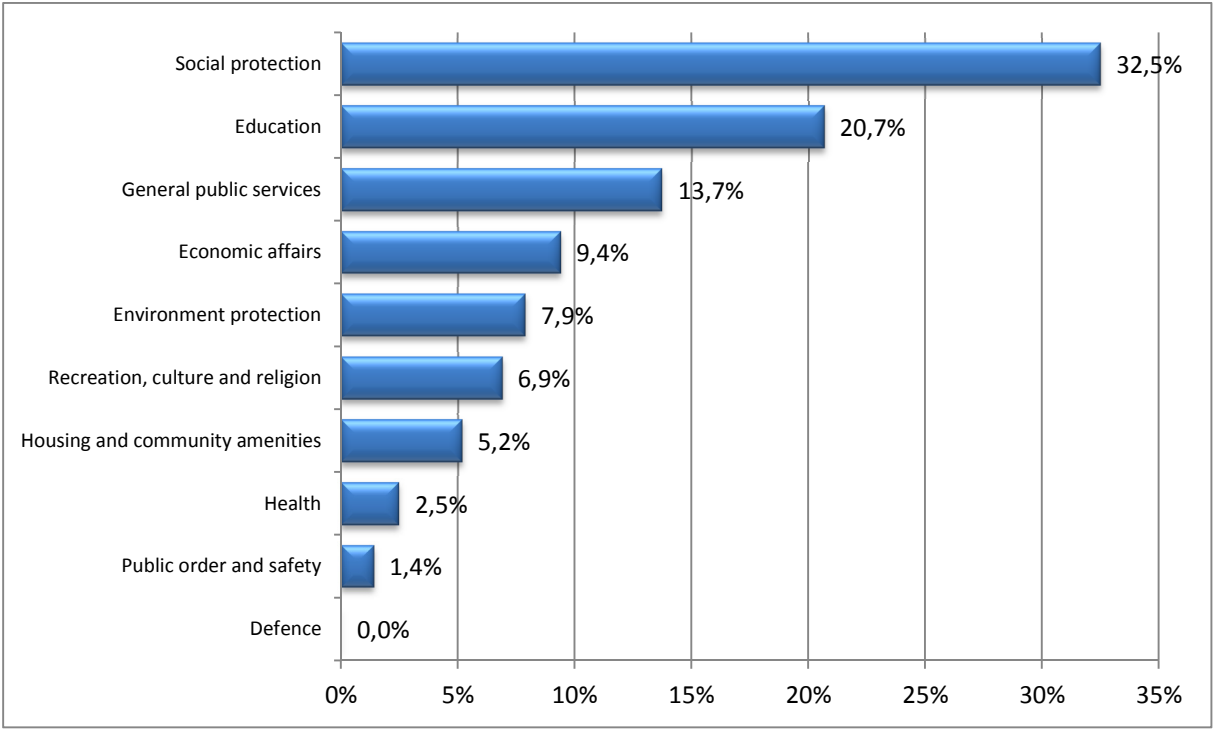
#### 4.4 More uniform country comparison

##### 4.4.1 The internal weight of municipal affairs

As mentioned earlier, previous classifications of municipal affairs vary among the countries concerned. The United Nations offers international classification of public expenditures (“Detailed structure and explanatory notes of COFOG,” 2013). The expenditures are classified in ten groups. First there are:

**General public services.** This includes executive and legislative organs, financial and fiscal affairs and external affairs. The category covers issues such as foreign economic aid, general services, basic research, public debt transactions, and transfers of a general character between different levels of government. **Defence** is the second category and contains military defence, civil defence, and foreign military aid. The next is **public order and safety** which includes police services, fire-protection services, law courts, and prisons. **Economic affairs** are the fourth category, representing general economic, commercial and labour affairs, agriculture, forestry, and fishing and hunting. Moreover, fuel and energy, mining, manufacturing and construction, transport, communication, and other industries are also included in economic affairs. **Environmental protection** is the fifth group, comprising matters like waste management, waste water management, pollution abatement, and protection of biodiversity and landscape. The sixth is **housing and community amenities** which comprises housing development, community development, water supply, and street

lighting. **Health** is the seventh category, covering hospital services, public health services, outpatient services, medical products, and appliances and equipment. The eighth group is **recreation, culture, and religion**, representing issues like recreation, sporting, cultural matters, broadcasting, publishing, and religious and other community services. **Education** is the ninth category and includes pre-primary and primary education, secondary education, post-secondary non-tertiary education, tertiary education, education not definable by level and subsidiary services to education. Finally, the tenth category is **social protection** which relates to sickness and disability, old age, those requiring rehabilitation family and children, unemployment, and housing.



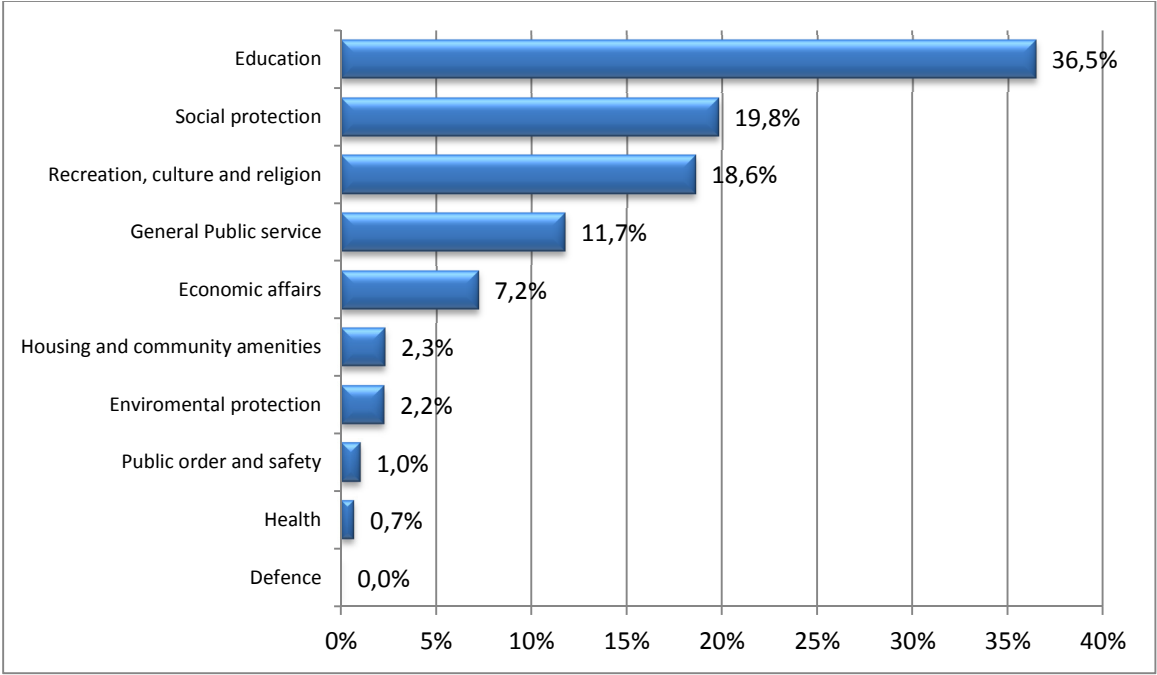
**Figure 4-12. Municipal affairs in the Faroe Islands and their share in total expenditure in 2010.**

Affairs by COFOG classification. Source: Statistics Faroe Islands

Only data from the Faroe Islands and Iceland were available based on the COFOG classification. According to this evidence it becomes apparent that education is the largest category in Iceland while social protection is largest in the Faroe Islands. The second largest category in Iceland is social protection and education takes this place in the Faroe Islands. The third largest category is general public services in the Faroe



Islands while it is recreation, culture, and religion in Iceland. The category of recreation, culture, and religion is the sixth largest in the Faroe Islands. So, even though there are differences between those two countries, they share education and social protection as the largest categories which are responsible for more than 50% of total expenses.



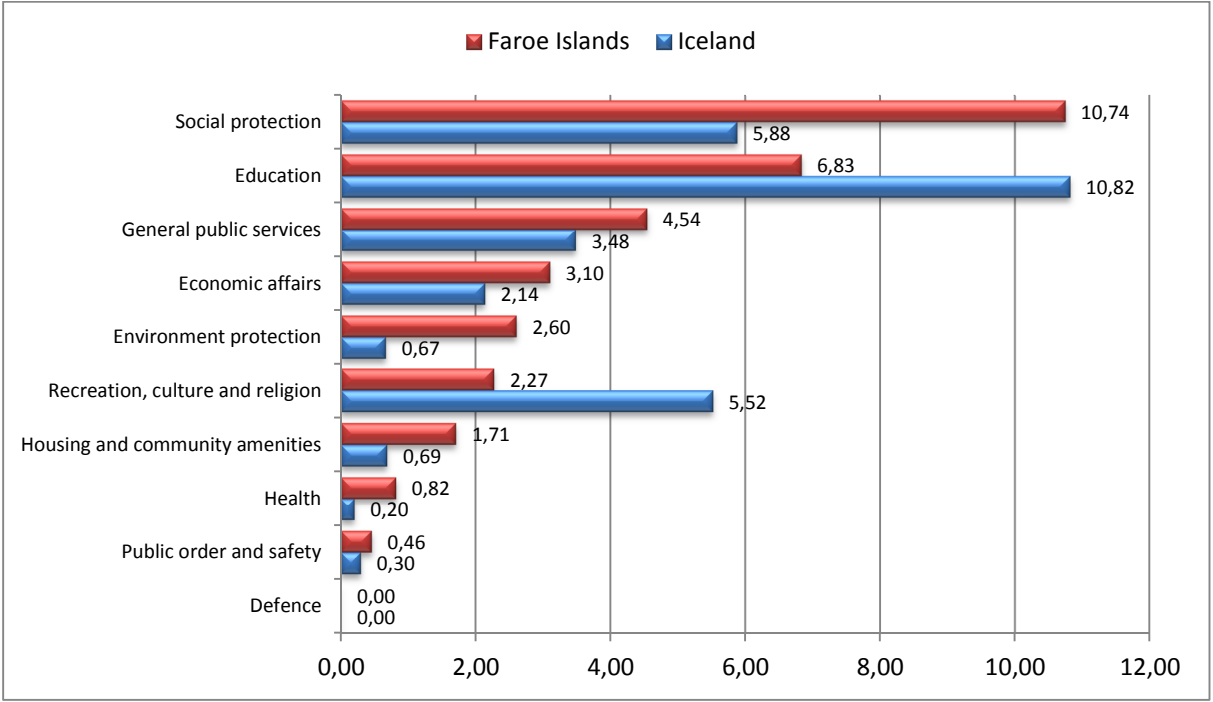
**Figure 4-13. Municipal affairs in Iceland and their share in total expenditure in 2010**  
 Categories by COFOG classification. Source: Statistics Iceland

It is hard to compare Greenland and the other two countries. We see, however, that education and cultural affairs is the largest group in Greenland where it is the source of 38.8% of total expenses (Figure 4-8). Social services comprise the second largest category and administration is in third place. Thus it seems that the structure in Greenland is more comparable to Iceland than the Faroe Islands. However, all three countries share the same two largest categories which give rise to more than 50% of total expenses.

**4.4.2 Efficiency**

The above comparison has shown the weight of every single category – classified by COFOG standards. Now an attempt will be made to construct a single economic indicator for the efficiency of every single category and generate a cross national comparison. The indicator is expenditure per capita in each category. Here, however

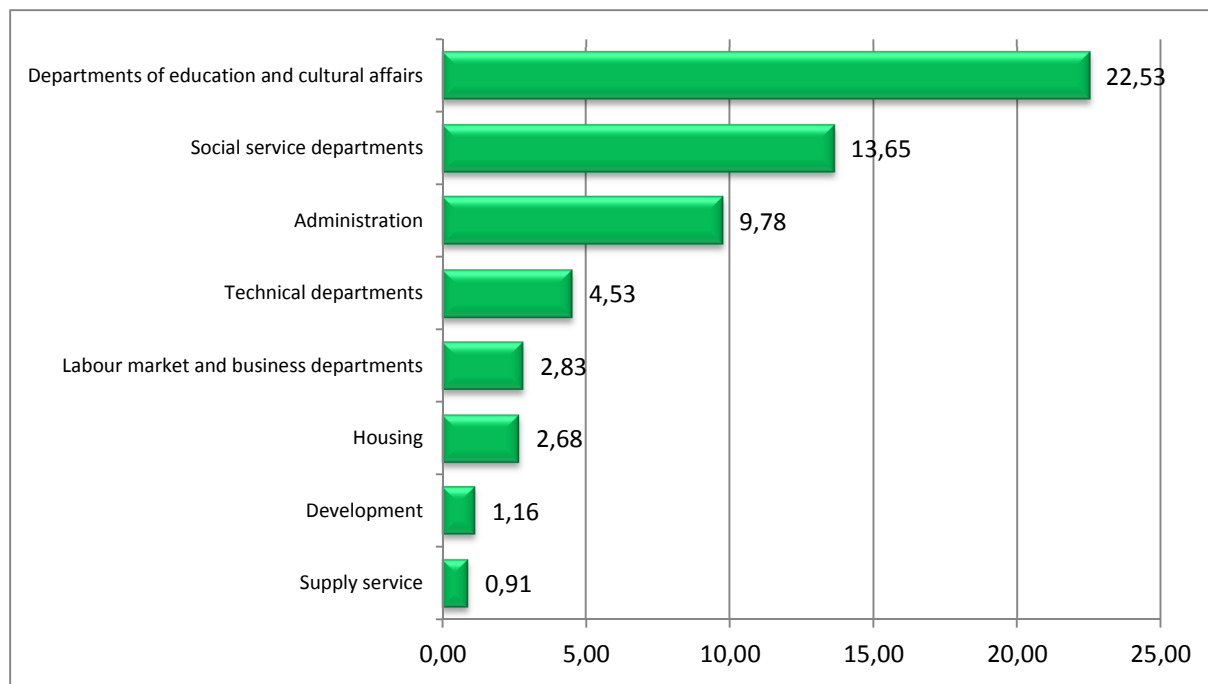
the problem is that Greenland does not provide data by COFOG standards, which will limit the analysis.



**Figure 4-14. Municipal affairs in Iceland and the Faroe Islands. Expenditure per capita in 2010.**

Numbers in thousand DKK. Categories by COFOG classification. Source: Statistics Iceland

When it comes to the efficiency of each category we see that the Faroe Islands are more efficient than Iceland when it comes to education and recreation, culture and religion. A significant difference between the two countries in social protection, education, environmental protection, health and recreation, culture and religion needs further investigation. As for health, in the Faroe Islands the municipalities run health centres, whereas this is not the case in Iceland.



**Figure 4-15. Municipal affairs in Greenland and their expenditure per capita in 2010**  
Numbers in thousand DKK. Source: Statistics Greenland

In Greenland, education together with culture has more than double the weight of education in Iceland and is almost four times larger than this category in the Faroe Islands. This cannot be explained by the presence of culture, so Greenland is the most inefficient when it comes to education. Social services are, however, comparable to social protection and this shows that Greenland is by far the most inefficient in the provision of those services if our assumption of a comparable level of need holds true. Administration has a similar definition as general public services and once again Greenland has the highest expenditure per capita among these three countries. In this case Iceland has the lowest cost of them all and is thus the most efficient country in the provision of administration. It should be noted that in Iceland administration cost fell by 9% in 2009 and 6% in 2010 due to necessary reforms and increased efficiency subsequent to the economic crash in 2008 (Karlsson, 2014). The labour market and business affairs for Greenland are comparable to economic affairs for Iceland and the Faroe Islands. In this case Greenland is closer to the expenditure per capita in the Faroe Islands than in Iceland. Housing for Greenland is not comparable to housing and community amenities in the other two countries. Other municipal affairs in Greenland are not so easily compared to the other countries.

The results, however, are in line with the previous conclusions for the entire countries where the Iceland was seen as the most efficient country, the Faroe Islands in second place, and Greenland last. The results were based on an attempt to include the service level in all calculations.

## **5 Local economic development and adaptation policies**

This chapter provides a framework for the analysis of local strategies for economic development and adaptation in the West Nordic countries and contains preliminary observations on current practices within this field of policy-making.

The first section presents some general considerations as to the reasons why policies for economic development and adaptation are considered necessary or useful. Why is it insufficient to adopt a “laissez-faire” approach, letting market forces and private initiatives determine the orientation of the economic development? What motivates measures to adapt local economic structures to changing framework conditions?

Section 2 focuses on the notion of “competitiveness”, which is increasingly considered as the central goal of economic development policies. The extent to which companies targeting international markets are created or continue to thrive tends to become the benchmark against which the success of economic development is measured. But does it always hold true that such procedures are a requirement for the balanced and harmonious development of local communities?

In section 3, a critical assessment of two other notions of economic development is proposed: entrepreneurship and innovation. Our objective is to demonstrate that even if the “entrepreneur”, or “gründer (founder)”, plays an important role in the economic development, one can design strategies that focus on the community as such. Such approaches, which are under the heading of “community led innovation” are an important component of current debates, and can be particularly well-adapted to small and isolated local communities.

On the basis of these considerations, the idea of “community led local development” promoted by the OECD and by the EU, is assessed in section 4. Section 5 draws up the status of local economic development policies in West Norden, while section 6 suggests perspectives for economic development and adaptation policies at the local level in the region.

## 5.1 The purpose and justification of local economic development policies

Preconditions for economic development and adaptation policies have changed dramatically over the past decades. Internationalisation has led to an increased exposure to international competition, at the same time as it creates improved export opportunities. Deregulation, combined with long periods of limited growth, has impeded the possibility of a pro-active public development policy. But perhaps the most important change is that the objective and purpose of “development” is less clearly defined. Post-Second World War reconstruction and welfare policies are not adapted to a series of new challenges. The following trends provide examples of these challenges:

- Social cohesion is threatened by the fact that economic growth does not necessarily create employment opportunities for the entire population, and that groups are excluded from the labour market.
- The awareness of environmental challenges linked to industrial production, intensive farming practices, increased mobility and a continuously increasing consumption of goods and services, generates scepticism towards the modernist view and its conception of “progress”.
- The focus on economies of scale leads to an intense centralisation, which creates fears of depopulation in many peripheral areas and challenges linked to demographic and economic over-concentration (“dis-economies of scale”) in many of the larger urban areas (Houlberg, 2011).

In parallel, forms of production and preconditions for value-creation are changing. There is an extensive literature on the information society and on the knowledge economy, which in general focuses on the key role played by urban areas in economic development. These areas concentrate higher education opportunities, research facilities and an increasingly important range of technical and economic development “brokers”. Furthermore, it is in these areas that the so-called “creative classes” (Florida, 2002) are congregated, and where access to advanced services and Information and Communication Technologies (ICTs) is the best.

An important challenge for small and isolated local communities is that the prevailing discourse on local economic development is generally based on such urban and

metropolitan examples of outstanding economic growth and “performance”. This tends to create a “development norm”, which implies that small and isolated communities appear as “less advantaged” by definition, insofar as they do not have the necessary preconditions to implement the corresponding type of development.

However, the OECD notes that rural regions have, on average, had higher growth than other types of regions in recent years, and that high demographic mass and easy accessibility do not necessarily trigger growth. The main challenge for regions with a lower development level is that their situation is so different in various parts of the World that their development and adaptation strategies need to be tailored to fit specific situations (OECD, 2012).

In its more general considerations on regional growth, the OECD notes that:

- Infrastructure is a necessary precondition for economic development, but not a sufficient one. Infrastructure investments only lead to economic development if the competence and capacity for adaptation and innovation exists.
- Competence and knowledge promotion is needed for economic development.
- Innovation, research and development promote development in the long term, irrespective of the sector considered.
- Proximity to markets and larger demographic concentrations have a more limited impact on the capacity to generate economic development than local factors such as human capital and innovation capacity. The strength of these local factors is, in turn, largely determined by the capacity to maintain a dialogue with neighbouring areas and to create networks.

## **5.2 The role of competitiveness and export oriented activities in local development**

Hovgaard (2001) uses the notion of “local coping strategies” when he describes development and adaptation strategies in Klaksvík on the Faroe Islands and in Båtsfjord in Norway. This implies that the main challenge for local communities such as these is to “cope with” an economic and political situation resulting from increased globalisation and deregulation. The challenge here is to differentiate between concrete challenges that need to be addressed to create the preconditions for a more balanced development on the one hand, and “mental barriers” generated by a globally prevailing

discourse on the purpose and objective of economic development policies and on the levers to be mobilised to trigger it.

Discussions on competitiveness exemplify the importance of differentiating between these two types of situations. It is frequently argued that internationally competitive companies constitute the cornerstone of local development. Different factors explain why these types of discourses prevail. On the one hand, there is a long tradition of differentiating between export oriented production activities that create the basis for local incomes, and other “induced” activity (e.g. Hoyt, 1954). The relation between the number of employees in export oriented production and in other activities, or so-called multiplying ratio of the export activity, then determines the size of the local economy.

On the other hand, globalisation and international deregulation has led to a focus on competitiveness because this is considered as a precondition to achieve a trade surplus. This focus has in many cases been uncritically transposed from national to regional and local levels. Different lines of argument can be invoked to illustrate why this is not justified: First, a local area or region does not have the same need to generate a balance between imports and exports as a country, insofar as it is not directly concerned by issues of monetary stability. Second, irrespective of the area considered, the bulk of economic activity is not export oriented, but related to the satisfaction of local demand for goods and services. A considerable proportion of the income that makes this consumption possible across the Western world comes from redistribution between local areas, e.g. through commuting, consumption far from the place of abode, fiscal transfers, pensions, unemployment, sickness and parental benefits. As a result, incomes from work in one local area can lead to consumption in a neighbouring locality or region. Finally, with the increased dependence on external investors, profits are to a growing extent channelled out of areas where production occurs. Together with the widening of individual mobility ranges and an ever-higher share of public expenses in GDP, this makes it increasingly difficult to predict the total economic activity of an individual local area based on the incomes generated by the export-oriented sectors.



It is, therefore, not purposeful to deal with local communities as “small nations” that would need to compete with each other creating the most attractive environments for internationally competitive companies. The belief that local export industries “generate” local service industries is, at best, an outdated vision. This view can, in some instances, be counter-productive, as it tends to encourage the development of industrial activities in sub-optimal locations, with lower productivity as a result.

A more systemic approach is preferable, considering the overall performance of networks of local communities, and promoting their combined balance, sustainability and resilience in the face of external shocks. Growth maximisation cannot be an objective for each local community taken individually. One needs to take into account the variety of functions of each local community: they can be living environments, contexts for social and cultural activities or daily environments for children and retirees, they can host educational and training institutions, research centres and production sites. All these functions are needed for a balanced and sustainable economic development. However, all of them do not need to be present in all localities.

This implies that while internationally competitive activities need to be present in a national or regional system of localities, they can be distributed in different ways. A concentration of these activities in main cities is only a problem insofar as this leads to continued demographic polarisation or other unsustainable demographic, social or environmental trends. Considering localities without internationally competitive activities as “subsidised” implies that one neglects all other functions needed for a balanced economic development.

Admittedly, this general stance may in some respects need to be nuanced in the West Nordic context. Commuting is often limited by the low population and isolation of many settlements. For the same reason, all services need to be provided locally, making it difficult to promote complementariness among neighbouring localities. The cost of maintaining these small and isolated settlements may be difficult to justify if there is not a sufficient production of goods or services for the national and international markets. By way of consequence, there are marked differences between development and adaptation processes in these local areas, compared to those that are

part of a wider functional region where commuting and daily mobility flows connect localities.

Compromises need to be found, therefore, when pursuing the parallel objectives of balanced territorial development, with limits to the centralisation of settlement patterns, and stable economic growth. The tension between these two parallel objectives is exacerbated by national strategies to reorient the economy towards a high productivity sector. Such a stance is for example advocated by the McKinsey Scandinavia (2012) report “Charting a Growth Path for Iceland”. The authors of this report point out that Icelandic productivity per worker is low in the largest part of the economy, including food production, other manufacturing, public sector, construction, wholesale and retail and agriculture. However, electricity and water, metal manufacturing and the fishing industry have high levels of labour productivity<sup>20</sup>. One can therefore roughly contrast a domestic sector providing local goods and services with low productivity, and an export-oriented sector with high productivity. At the same time, given the low Icelandic unemployment rates, possibilities of expanding the export-oriented sector are limited by the lack of qualified labour. McKinsey Scandinavia therefore considers that one should free labour in the domestic sector through efficiency gains, so as to improve the growth perspectives. However, this process also implies that a significant proportion of the Icelandic population would need to change their place of abode. The labour force currently employed in low productivity domestic sectors is not necessarily located in areas where new export oriented activities could be developed.

The implementation of such strategies at national level thus creates a need for local communities to position themselves. Depending on their local economic profile and development perspectives, they may either potentially host new economic activities and be the recipients of a potential inflow of workers, or be exposed to a reduction in employment opportunities and demographic decline. The territorial implications of economic strategies such as the one described above are seldom, if ever, considered at the national level. A dialogue with individual local authorities is therefore needed to establish how such abstract, a-territorial economic strategies can be concretely

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<sup>20</sup> Compared to other Nordic countries and the United Kingdom.

implemented “on the ground”. Municipal development strategies can serve as a basis for such a dialogue.

### **5.3 Entrepreneurship and innovation**

Innovation has come to be considered the key to growth. Consequently entrepreneurship and innovation have become mantras for development and adaptation processes at all scales. The entrepreneur is a central figure of the innovation process. Schumpeter describes the entrepreneur as a rare type of personality, characterised by willpower, alertness and ability to “think outside of the box”. According to Schumpeter, only a small proportion of individuals in any given society have the potential to become entrepreneurs (Schumpeter, 1928). From this point of view, betting on entrepreneurship can appear as a risky choice for small and isolated settlements, where the chances that there would be a “Schumpeterian entrepreneur” among the locals may appear rather slim. One also observes that many of the most resourceful and enterprising individuals leave these communities, as their ambitions can be met with hostility among local established elites, among whom conservative attitudes tend to prevail.

This Schumpeterian entrepreneur has often been compared to an economic “*Deus ex Machina*”. However, other approaches of entrepreneurship are currently discussed in the literature. Entrepreneurial initiatives can often be perceived as irrational by other actors, precisely because their logic is forward-looking and based on new ways of organising social interactions or production processes. Personal economic gain is not the only motivation that drives entrepreneurship. The desire of a community to create novelty and to achieve social recognition and prestige is equally important. From this perspective, some communities may be more successful than others in generating “entrepreneurs”. For example, communities that create a safe environment without excessive social control, in which open dialogues and debates play an important role, may create a favourable environment. Such considerations can form the basis for entrepreneurial policies in West Nordic rural environments.

In the Faroe Islands, the business incubator *Íverksetarahúsið* has been established to promote entrepreneurship and new economic activities. It is partly locally initiated, as the Municipality of Klaksvík (the second largest urban area of the Faroe Islands) has

funded it together with the Ministry of Trade and Industry and Eik bank. One of the activities of *Íverksetarahúsið* is to organise courses and seminars across all of the Faroe Islands. They can, therefore, improve each local community's ability to host and support entrepreneurial activities. In parallel, they support individual initiatives by providing mentorship and basic infrastructure during the first years.

By playing these different roles, *Íverksetarahúsið* is an illustration of how regional and local authorities can function both as promoters and as regulators of entrepreneurship. In a context where each individual citizen, company and organisation needs to relate to increasingly rapid exchanges of ideas, changes of economic framework conditions and technologies, public authorities can contribute to offer the stability needed for balanced and coordinated development. The figure of the “mythical entrepreneur” is from this perspective only one important actor among others in economic development and innovation processes. Change and novelty is generated by establishing the rules, approaches and institutional setups adapted to the possibilities and challenges one is facing (Harrisson and Vézina, 2006).

This type of approach places the emphasis on the community in innovation processes. This implies that authorities do not focus on supporting an individual entrepreneur, idea or technology, but rather seek to create favourable framework conditions for the emergence of new ideas and approaches, while contributing to the reflection on how they may benefit the community. This is a demanding form of development and adaptation policy, as it requires a holistic perspective on the functioning of the local community and its institutions, rather than presuming that a few resource persons and innovative companies would function as “growth and development motors”.

It is, however, consistent with the critique of the idea that balanced and sustainable local development derives from growth in export oriented companies. As described in section 2, a wide range of factors determine whether individual initiatives to develop innovative and competitive activities contribute to the prosperity and sustainability of the local community. Taking a “social innovation” perspective implies that one first considers the potentials and needs of the local community, and then identifies the types of initiatives and measures that would be best suited to address them.

Measures to promote entrepreneurship and innovation, therefore, do not need to be based on supporting entrepreneurs. It can be more appropriate to seek to understand the factors limiting the ability to implement new ideas within the local economy. Such an approach can raise awareness of local and natural resources that are not appropriately exploited due to these limiting factors. It can also make it possible to identify how those limiting factors reduce the resilience of the local economy and its capacity to adapt to external shocks and economic globalisation processes. A policy to promote entrepreneurship and innovation is first, therefore, based on an analysis in terms of identified failure and/or governance system failure. The underlying hypothesis is that a development without any form of public intervention would lead to a suboptimal exploitation of resources, or pose the risk of different forms of vulnerabilities in the short or long term. The second component of such a policy can be a project or vision for the local community, i.e. the expression of an ambition to promote a certain form of development or for the local community to reach a given state. This can, therefore, be based on what the EU and the OECD describe as “Community led local development”.

#### **5.4 Community led local development**

Community led local development designates policies seeking to achieve a higher degree of local embeddedness of development strategies and policies. The method has been applied in numerous regions and in a wide diversity of territorial contexts.

In the EU, community led development is one of the main buzz-words of the current 2014-2020 programming period. The method has already been applied in the LEADER programmes, and has demonstrated its potential when it comes to ensuring the successful implementation of local development strategies and projects, as well as stimulating local involvement and support.

Furthermore, the use of local development can be considered as a consequence of the shift from a government to governance logic in public policies, that is, the replacement of hierarchical and bureaucratic modes of intervention by methods based on dialogue and cooperation involving a wide range of public and private actors.

The present sections introduced the notion of community led local development, which can a priori be applied to all sectors of activity, but is here considered from the

perspective of economic and industrial development. It then describes how community led local development can contribute to changed attitudes and help involving a larger range of actors in the process of creating new economic development perspectives.

#### 5.4.1 General principles

Community led local development is based on the idea that local actors should be the main actors of local development processes. The objective is to increase the local sense of ownership with regard to development strategies, to contribute to the empowerment of the local population and to promote the integration of actors and policies within the framework of a multilevel governance system. Furthermore, community led local development can use local knowledge on development opportunities and potentials to a larger extent than other areas. To achieve these different objectives, local authorities need to play an active role in community led local development initiatives, but also seek to act as a catalyst for the involvement of other groups.

These general principles can be further specified as follows:

Local ownership of development initiatives is obtained by involving local communities in development initiatives, thereby improving local social cohesion but also enhancing the local embeddedness of development strategies and initiatives. This improved local embeddedness promotes their chances of successful implementation.

1. **Actor empowerment.** As already mentioned, empowerment is an important component of community led local development, and is considered as a catalyst for innovation and for the design and implementation of innovative projects. Empowerment presupposes that local actors acquire the competences needed to intervene in local development processes. This implies that they must have the ability to identify challenges and possibilities of local development, to participate in political decision-making processes and to contribute to the final implementation (Tordjman and Mahoul, 2012). Empowerment can be promoted through two mutually reinforcing processes. On the one hand, local empowerment can be approached as an objective in its own right, reinforcing the participation of the population in strategic discussions and development projects. On the other hand, empowerment can result from an increased

involvement in development processes. To facilitate these two parallel processes as part of community led local development, different types of measures need to be implemented. On the one hand, support needs to be provided to stakeholders to ensure that they all possess the required competence to participate in development processes. On the other, participation itself needs to be organised so that it is also a learning process.

2. **Local integration in a multilevel governance system.** The objectives pursued through community led local development are not confined to enhancing the qualities of the local communities and increased economic growth. It is also important to ensure the integration of local actors in multilevel governance systems. Such integration in political processes is, furthermore, designed to improve the quality of decisions made at higher levels. Ultimately, this therefore contributes to the final implementation of the strategies.
3. **Place based vs. place blind and local knowledge.** The community led local development rationale presupposes a policy-making context in which decisions are place-based rather than place-blind (Barca 2009; Barca, McCann and Rodríguez-Pose 2012). This type of approach is based on the assumption that territories have different potentials and challenges, which implies that “one-size-fits-all” types of solutions cannot be applied. Community led local development presupposes that such a logic is applied, as it is required to establish a meaningful and constructive dialogue between levels of governance.

“Smart specialisation” can be considered as an application of the “place-based” approach within the framework of EU regional development policies. In the smart specialisation approach, different regions should base their development plans on their unique sets of potentials. This implies that the extent of interregional competition should be limited, as all regions should develop different types of economic specialisations. At the European level, such regional strategies would contribute to increased territorial cohesion and resilience of the European economy in the face of external shocks (European Commission, 2013).

Community-led local development can contribute to the diversification of economic activities, as new ideas are developed through the involvement of a wider range of

actors with local knowledge. In rural areas, this typically implies identifying opportunities beyond the agricultural and fisheries sectors by formulating a vision for how the local economy could develop more diversified activities. A major challenge to be overcome is the influence of economic development fashions and trends on individual actors, which can influence their selection of local potentials to be exploited and limit the diversity of “smart specialisation” strategies.

#### 5.4.2 Implementation

The implementation of community led local development should be approached as a process in which strategies are progressively translated into concrete action. Torjman and Makhoul (2012) describe this as “an evolving process that involves the translation of aspirational goals into specific steps to be taken in respect of that vision.” (p. 17).

This process can take different forms. However, it is generally based on a bottom-up approach in which a broad range of local actors are encouraged to participate in decision-making processes on development strategies. Furthermore, development initiatives coming from the local community are promoted.

Torjman and Makhoul (2012) describe the process as one that is “guided by leading local actors”. Public authorities should have a supporting role and through this create an “enabling environment”. This is done by allowing public instances to assume three main roles:

1. **Model**, by defining legal, economic and ethical frameworks and being at the forefront when it comes to respecting the principles that are advocated. This could for example be done by implementing new environmental regulations rapidly after their adoption.
2. **Investor**, by providing economic support to initiatives or projects that promote a desired development. Support to local business through strategic procurements policies can also be envisaged when possible.
3. **Catalyst** that enables community-led local development. This may involve making contacts across disciplines and groups, organizing meetings and ensuring that a representative sample of the population is involved in community-led local development processes.



It is generally recommended that local action groups with representatives from private and public sectors should be established. These action groups contribute to the elaboration of local development strategies.

However, differences between the modes of participation of citizens and practitioners can create challenges, especially with regard to their mutual understanding of their respective competencies. This may lead to situations, for example, in which an evidence and knowledge-base is denounced as being either technocratic/scientific or anecdotal/based on subjective experience (Derkzen and Bock, 2007). A balance between practical knowledge and scientific expertise needs to be pursued, as the synergy between these two types of approaches is important for the successful implementation of community led local development.

In addition to these forms of knowledge, and awareness and understanding of political decision-making processes at regional, national and international levels within the local community is essential for a well-functioning community-led local development process. A lack of integration in a multilevel governance system, and corresponding isolation from other actors, limits dialogue with relevant decision-making instances. As a result, local perceptions of problems and challenges and local ambitions are not communicated to these instances, which limits the extent to which they can be taken into account in higher level policies. Senior officials and external experts can help establishing connections between local communities and other levels (Herbert-Cheshire and Higgins, 2004).

The balance between the different levels, and the efficiency of the dialogue between them, is a central prerequisite for meaningful community-led local development processes. As shown by the OECD analyses presented in section 1, one of the reasons why community-led local development is promoted is that external factors such as infrastructure and proximity to markets do not suffice to create growth and sustainable development. However, it is counter-productive to try to promote community-led local development in situations where the essential preconditions for such an approach (as described above) are absent. Many small and peripheral local areas in West Norden have suffered a population decline for many decades. The local communities, therefore, consider that they do not have the possibility to adapt to current economic

framework conditions, as they are shaped by globalising processes and national regulations and policies.

In situations where one experiences that there are fundamental obstacles limiting development perspectives or creating specific preconditions, it can be necessary to rethink the role of the local level in development and adaptation processes. The focus may, in a first phase, need to be on making national and regional authorities aware of possibilities and constraints, in order to encourage them to create framework conditions that would make it possible to address them. The promotion of local initiatives, for example within the framework of community-led local development, may then be envisaged in a second phase.

### **5.5 Status of local economic development policies in West Norden**

The diverse municipal structure of the West Nordic countries, as described in chapter 2, has obvious and major implications when it comes to local involvement in issues of economic development:

- In the Faroe Islands, most individual municipalities are too small to become involved in economic development issues. With the exception of Klaksvík's contribution to establishing the business incubator Íverksetarahúsið, local strategic actions for economic development have been very limited. Such actions are mainly implemented at national level. Interviewed stakeholders insist on regulatory constraints on local economic development initiatives, as it is illegal for municipalities to deliver services in lieu of private actors.
- In Greenland, all the new large municipalities have dedicated economic development units. Their activities and level of strategic planning vary from municipality to municipalities, but generally include some form of adult training. While the municipalities of Kujalleq and Qaasuitsoq still appear to be at the stage of defining objectives, with only limited strategy development and concrete actions, Sermersooq and Qeqqata are more advanced. Qeqqata has established an economic development council (Quqqata erhvervesråd / Qeqqani Inuutissarsiornermut Siunnersuisoqatigiit) which is a private association operating with support from the municipality. Both municipalities have

strategic plans identifying bottlenecks for the economic development and concrete actions to be implemented.

- In Iceland most individual municipalities are too small to address economic development issues. However, they have jointly established regional development centres across the country. These centres are financed through the national Regional Development Office, with a contribution from the municipalities. It is also through these regional development centres that regional growth agreements with the state are designed and implemented. However, the extent to which municipalities actively engage in the operation of the Regional Development Office to which they belong is variable and difficult to determine.

Overall, local involvement in economic development policies is limited. The main difference between the countries is that some have institutional arrangements and resources in place to allow for larger involvement. This is officially the case in Greenland, even though the slow progress beyond general statements of objectives could be an indication that there are structural obstacles to letting municipalities play an active, strategic role. The economic development units and elected representatives may, in some instances, need to grow into the role of strategic actors. It is also to be noted that Greenlandic municipalities should rather be considered as regions, with their large number of towns and villages functioning as separate economic units. Strategic discussions, plans and visions at the level of individual towns and villages are very limited.

In Iceland, the policy instruments in use suggest an adoption of the principle of a multi-level governance of economic development, based on bottom-up initiatives. In this setup, individual municipalities could play an active role bringing together relevant actors and protecting the general interest of their respective local communities. However, some authors suggest that policy practice is more top-down and sectoral. Analysing regional tourism policy, Huijbens et al. (2014) find that “industry clusters as promoted by the Icelandic government do not reflect an engagement with regional socio-spatial specificities”, especially after the end of the first growth agreement (2004-2007). They imply that since then there has been no real

engagement with local groupings of actors or a commitment to identify and use local development potentials. This suggests that the potential role of local authorities in the Regional Growth Agreements process is quite limited.

There is no formal framework for the involvement of Faroese local authorities in economic development issues and therefore the concrete situation is not very different from those observed in the other West Nordic countries. In all three countries, potential local contribution to multi-level governance of economic development and adaptation processes has been insufficiently conceptualised and framed. This implies that strategic actions which could meaningfully be implemented at local level have not generally been defined, and that corresponding policy levers are either not at the disposal of local authorities or not being used to their full extent.

## **5.6 Perspectives for West Nordic local development policies**

Different paths can be explored for the purpose of identifying how West Nordic local authorities could make a meaningful and efficient contribution to economic development and adaptation.

First, their role in these processes needs to be defined. Different hypotheses can be envisaged based on the policy notions and literature reviewed in the previous sections.

Local authorities can for example:

- Facilitate communication between actors, e.g. by creating forums for dialogue, exchanges of ideas and the identification of potential synergies;
- Promote the identification of different forms of market failures with regard to the exploitation of human and natural resources, taking into account local vulnerabilities, current social and environmental challenges and potential future risks;
- Coordinate the formulation of a vision or a project for the local community;
- Help identifying local development opportunities, and the precise reasons why these are not being identified and exploited by private actors;
- Support entrepreneurial initiatives, e.g. by providing training and mentoring, support during the first years, facilitate access to risk capital;
- Defend the interests of local communities in the dialogue with other levels of administration and with external actors, e.g. investors and corporations.

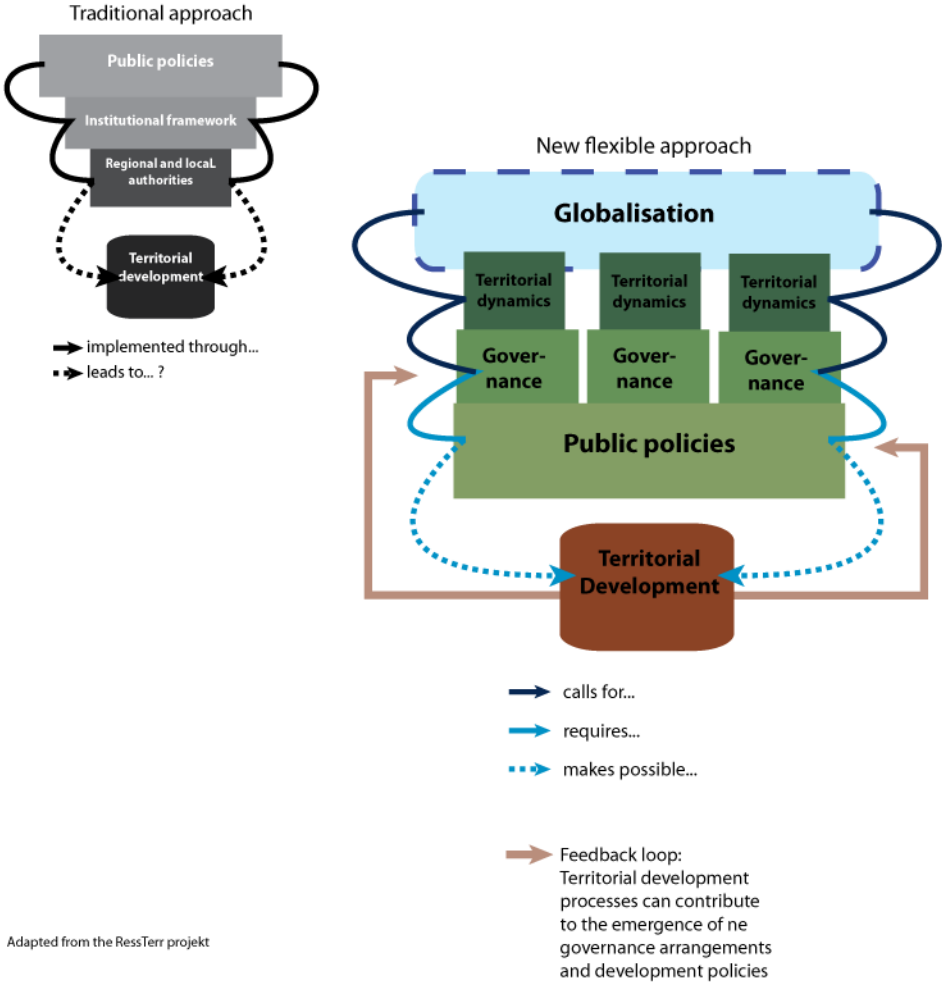
The relevance of these different roles can be different depending on the size, economic and development potentials of each local community. In many instances, one would come to the conclusions that only inter-municipal cooperation bodies could assume these functions, given the size and resources of individual municipalities. However, coordination costs are significant and need to be weighed up against foreseen benefits. It is also important to consider how decision-making in inter-municipal cooperation bodies can be democratically embedded, accessible to individual citizens and made accountable to local communities for their use of resources.

Municipal and inter-municipal strategy formulation and action in favour of economic development need to be considered as a component of multi-level governance. There is no elected regional level in any of the West Nordic countries. The main issue is, therefore, the division of responsibilities and mode of interaction with the national level. One may also in some instances need to consider the interaction with the sub-municipal level, typically in Greenland,

Exchanges between public authorities, on the one hand, and companies, entrepreneurs and investors, on the other, are central to economic development and adaptation policies. The so-called “triple helix” model (Leydesdorff and Etzkowitz, 1996) also includes research organisations in the group of actors to be involved in local/regional innovation and development processes. This has later been extended to a “quadruple helix” model, with proposals that the civil society could constitute the “fourth helix” (Arnkil et al., 2010). More generally, all actions for economic development and adaptation are necessarily collaborative, especially when meeting the needs and aspirations of local communities is the core objective.

Based on these two conclusions – the multi-level and collaborative nature of economic development policies - advocates of a territorially embedded development (Landel and Senil, 2009, Pecqueur and Gumuchian, 2007) have pushed further the idea of a revision of policy models. As illustrated in figure 5.1 below, they not only challenge the traditional top-down model of policy making whereby municipalities and regions are only a component of an institutional framework through which a general development policy is implemented. They maintain that the “governance” idea must be fully taken into account, and that public policies for economic development should be

implemented in reaction to existing territorial dynamics, as they emerge in a globalised economic context. Such an approach ensures that policies are implemented at the level which corresponds to the issues at stake, whereas the traditional model presumed that the existing administrative units would be appropriate. These authors therefore contend that the flexible model is more efficient.



**Figure 5-1. Traditional and flexible approach to public policies for territorial development**

The extent to which such a model could be applied to the West Nordic context needs to be critically considered. First, the mechanism whereby governance arrangements would emerge in response to territorial dynamics presupposes a framework of policy makers and senior officials at the appropriate level(s) and with the proper resources. This is not necessarily the case in the West Nordic context. Furthermore, in some particularly small and isolated localities, especially in Greenland, the assumption that

there would be territorial dynamics can be challenged. The North Atlantic Think Tank points out that there are Greenlandic villages where none of the inhabitants have paid work, and a number of localities where the only growth is in the public sector (Nordatlantisk tankesmie, 2012). However, in most parts of West Norden it could be useful to think in terms of framing and guiding the use of territorial resources bottom-up rather than seeking to implement “strategic objectives” top-down.

The recurring issue in these discussions is the small size and limited resources of individual West Nordic municipalities. The fact that many municipalities do not currently have any development strategy or vision is an obvious and major obstacle to their involvement in these types of issues. Further enquiries are needed into how a greater number of local communities could formulate a vision for their own development, based on a dialogue with the population.

The assets of small local communities should also be emphasized; they can, for example, more easily identify resource persons, who have the capacity to implement new ideas and mobilise local actors. Furthermore, a survey by the Norwegian trade union LO showed that business leaders in small and peripheral municipalities value the importance of municipal economic development policies higher than those based in large and centrally located areas. Furthermore, business leaders in small and peripheral municipalities have a better knowledge of municipal activities and initiatives (Moen, 2011). These patterns could be further investigated in the West Nordic context.

Municipalities with limited resources also need to be made aware of how their “basic” public services can become a lever in development processes. Childcare, schools and leisure activities for children can for example significantly increase the number of persons available for the labour market, in addition to creating new job opportunities. Regulatory plans developed in dialogue with local businesses can contribute to economic development and adaptation by taking their needs and expectations into account.

However, there are also obvious challenges to be addressed. First, interaction between small and peripheral local authorities and external companies and investors is often asymmetrical. These external actors may have larger financial resources and possess a wide range of specialist competences. It is, therefore, important that

municipalities should have access to appropriate counselling when needed, e.g. lawyers, financial experts and engineers. The mechanisms to gain access to such counselling in place could usefully be compared between West Nordic countries.

Second, while small local communities are characterised by a high degree of proximity between its inhabitants, some forms of social control and scepticism towards novel ideas are also observed. This obstacle to economic adaptation can be difficult to overcome. At the same time, there is generally a large local consensus about the need to actively counter the tendency of businesses and industries to agglomerate in only the largest urban centres. The question is, therefore, whether the shared sense of belonging to a challenged area can better be capitalised upon to promote innovation and development benefiting the community as a whole.



## **6 Summary and future research**

### **6.1 Main findings**

#### **6.1.1 Municipal structure**

The dramatic development in Greenland, where the municipal structure was changed after 2007 by amalgamating 18 municipalities to 4 makes the present situation and development in Greenland significantly different from the current structure in the Faroe Islands and Iceland. With its four big municipalities comprising an average population of more than 14,000, Greenland is significantly closer to the East Nordic structure pattern compared with Iceland with an average of about 4,300 and the Faroe Islands of 1,600.

Significantly larger steps towards reforming municipal structure have been taken in Iceland than in the Faroe Islands but the characteristics of the structure pattern are the same in both countries. There are proportionally many very small municipalities with limited capacity to take over more welfare tasks and thereby provide modern services.

#### **6.1.2 Local democracy**

As we have seen, the municipal structure in these three countries is nowadays not as similar as it used to be. After the great reform in Greenland the municipalities are not only largest in areal but also in population in the West Nordic comparative perspective. Table 2.2 above has shown us how the Faroese and Icelandic municipal structures are quite similar and the one in Greenland quite different. The emerging question about local democracy in Greenland focuses on the political representation of small villages and neighbourhoods after the great municipal reform. The concern just before the amalgamations came into practice was how people in these smaller, and in many cases severely isolated, neighbourhoods could be part of the democratic processes in the new municipalities and have something to say on or decide about their issues. In the Faroese case the main issues are related to the content and scope of local democracy, since the archipelago's numerous and small municipalities have limited functions – at least compared with the other two countries in the study. This is, however, not the standpoint of representatives of the smaller municipalities who have had their own municipal federation and claim that they are doing well as they are. But

recently, the two federations were merged into one, so the possibilities for the smaller municipalities to act as such are perhaps in question. In the Icelandic case the discussion on democracy at municipal level seems to be about increased direct citizen democracy and developing ways to modify the traditional representative democracy where politicians are elected every fourth year and left alone by the voters in between. Increased citizen participation in decision making between elections seems to be a key word nowadays. This has been clearly emphasized in the Local Government Act from 2011. Another emerging and to some extent increasing discussion in Iceland is about the effect of inter-municipal cooperation on democracy. The much greater emphasis on inter-municipal cooperation as a way to reinforce the municipal level instead of achieving this through municipal amalgamations is believed to affect the local authorities involved, since the cooperation projects are run by boards not elected by the people. This has its disadvantages, such as the agency-problem Ström (2000). In the cooperation projects extensive functions with high turnover are the responsibility of the boards of federations or the boards of single projects, but not the elected politicians in the municipalities. Thus these functions have been delegated to non-elected parties. The Danish political scientist Ulrik Kjær has also mentioned several “democratic potential worries” about inter-municipal cooperation. First, that the political minority is or can be undermined since it is usually a delegate from the majority who represents the municipality. Second, fewer possibilities of control to ensure that the interests of every municipality are taken care of and third, that the political responsibility is unclear. The voters have problems realizing exactly who within their municipality is responsible for the decisions taken this board (Kjær 2000, p. 11ff).

The changes of policies towards inter-municipal cooperation as a means to reinforce the municipal level in Iceland have not taken these above mentioned potential democracy problems into account at all. Effectiveness problems have, however, received some slight mention in a limited debate.<sup>21</sup>

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<sup>21</sup> See also in Eythórsson (2014).

### **6.1.3 Service production and effectiveness**

Among all West Nordic countries, the size of the government is largest in Greenland, second largest in Iceland and smallest in the Faroe Islands. This holds for the size of local government as well. Among all local government services the category of education and culture is the largest in Greenland, health care (or social protection) in the Faroe Islands and education in Iceland. Some statistics suggest that local government Greenland is also most inefficient in the provision of their services and Iceland most efficient. Another cross-national comparison shows that Greenland is the most inefficient country in the provision of education, social services and administration if the assumption of comparable service levels is valid in all countries. A thorough investigation of service level was not possible in this section of the research project. All the countries have had mergers of municipalities during the past two or three decades. Preliminary results indicate that these have had limited impact on the efficiency of the local government.

### **6.1.4 Local economic development**

West Nordic local authorities' involvement in economic development issues has generally been weak. There are few local economic development plans. When they exist, many of them list objectives rather than establishing a course of action to reach them.

The economic sustainability of many small isolated communities is challenged by a number of factors in a context of globalisation. As exposure to external competition and international market fluctuations increases, these communities are encouraged to increase their productivity and position themselves in “niches” that would generate a stable income and higher margins. However, national and local strategies do not necessarily converge in this respect. National measures to maximise growth by favouring the most productive and competitive sectors of the economy may encourage a geographic concentration of jobs and inhabitants. Furthermore, the uncritical transposition of national growth strategies from the national to the local tends to create an excessive focus on internationally competitive activities. Instead, a diversity of possible contributions to an overall balanced national economic development needs to be considered. In other words, high national growth does not imply that individual

local communities fare well. Similarly, even well designed and implemented local strategies to maximise growth do not necessarily create a balanced and stable economic development at national level.

How can these general considerations be transposed into concrete policy recommendations for individual West Nordic communities and for national and regional authorities seeking to promote growth and balanced development? First, a critical approach to the promotion of entrepreneurship and innovation is needed. While individual initiatives need to be encouraged and facilitated, small isolated communities cannot rely on isolated entrepreneurs as the main drivers of local development and growth. A more holistic perspective is needed, taking into consideration the potentials and needs of each local community. To this end, a collective identification of possibilities and aspirations is needed. This leads to a bottom-up approach seeking to achieve “social innovation”. This implies that innovation is collectively driven and is a lever for the achievement of community goals rather than an end in itself.

Such an approach could be developed in the more general framework of “community led local development”. This buzzword of OECD and EU policies covers a wide range of approaches and measures empowering local actors in development processes. In this context, local authorities can play different roles, e.g. as models, investors and catalysts. The preliminary overview of situations in West Norden shows that local authorities’ involvement is hampered by structural factors such as small municipality size and limited resources, legal constraints and by lack of awareness of the potential benefits of a more proactive approach to these issues.

## 6.2 Future research – The second phase of the project

With regard to this project the authors have begun with this report by collecting knowledge on the local level in the three countries and by mapping the situation and development focusing on four aspects: 1) Mapping development, debate and the current situation of municipal structure in the three countries. 2) Looking into the democratic aspect – that is which consequences the structural development has had for local democracy – more specifically trying to identify which have been the main challenges to democracy, caused by the structural developments. 3) Mapping the service production capacity and effectiveness of municipalities in the three countries and 4) mapping the capacity of the municipalities to manage the development processes which often accompany municipal amalgamations. The overall research question has been: *Which consequences has the development of municipal structure in the three countries had for democracy, local self-government and autonomy and the ability to manage the development processes which accompany amalgamations?*

In the next phase of the project the authors will attempt to develop and deepen their insight into these matters by undertaking a survey among all elected local politicians in all of the 108 municipalities in the three countries; 74 in Iceland, 30 in the Faroe Islands and 4 in Greenland. In Iceland there are 504 elected representatives, in Greenland 305 (including neighbourhood councils - bygderåd) and in the Faroe Islands there are 208 elected delegates. This means that 1017 elected officials will receive our netsurvey in the autumn of 2014. In this survey we are going to ask questions aimed at deepening our understanding of the problems and challenges facing the municipal level in the three countries, with a special focus on the findings in this overview report. How does the municipal structure affect service effectiveness and local democracy, and how do the municipalities manage the transformation connected to it? After having collected the results from the survey, these will be published in a special report.

This project will be concluded with a transnational seminar in Reykjavík focusing on the findings of this report as well as those from the survey report. The intention is to invite local and state politicians from all three countries and representatives from the federations of municipalities, as well as officials from the state institutions and ministries relevant to the issues in question. In this way the authors hope to be able to

invite people to meaningful discussions and comparisons on these issues which could be an important step in a mutual learning process for the people involved in the affairs of the municipal level in these countries.

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