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**THE NECESSITY OF AN
ADMINISTRATIVE-
TERRITORIAL REFORM IN A
COUNTRY: THE CASE OF
ESTONIA**

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The necessity of an administrative-territorial reform in a country: the case of Estonia¹

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Abstract

The goal of this paper is to analyze the theoretical, political and organizational bases of the territorial division of the country into municipalities and offer a research direction for identifying conceptual solutions to the development problems in Estonian municipalities. The paper focuses on the territorial organization of administrative issues, looking at the remaining administrative aspects only insofar as they relate to the territorial organization of public administration and services.

In order to accomplish the goal we tackle the following research tasks: systematize theories concerning the territorial division of the country into municipalities and analyze the possibilities and limitations for their application; discuss administrative-territorial reforms in Nordic countries, their causes and consequences; describe the development, nature and indicators of the administrative-territorial division of Estonia; empirically analyze the relationship between municipal size and capability and development indicators.

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The analysis of the theoretical approaches to municipal size pointed out that they are fragmented and incompatible. Some authors support small municipalities, and others large. The theoretical reasoning of both those directions is often strongly simplified and biased and a unified meta-theoretical approach has not been established. The empirical analysis revealed that there is no empirical evidence to confirm either the presence of significant size related advantages among municipalities or the existence of an optimal municipal size considering current municipal functions and financing.

The lack of theoretical and empirical evidence on the necessity for administrative-territorial reform means that merging municipalities alone cannot significantly improve the public service delivery capacities and economic and democratic development of Estonian municipalities. This means that future studies should focus on analyzing public services from the perspective of their economic efficiency, quality and accessibility, and in doing so, determine the optimal size of regions for providing the various public services.

JEL Classification: H11, H70

Keywords: optimal size of municipalities, local governments' financial potential, local political development, amalgamation, local government reform, local government efficiency

1. INTRODUCTION

The disputes over the administrative-territorial organization (division) of Estonia have run into a dead end. The established municipal system is being criticized by almost everyone for different reasons and purposes. It seems that the solution to Estonian regional imbalances and problems in rural areas would be to increase the size of the municipalities. There are some political forces recommending these problems be resolved by the central government enacting radical reform resulting in large municipalities; that means nullifying a substantial aspect of the communities people live in using raw command force. Fortunately, however, there has not yet been a majority in favour of that political decision. This article tries to show that it is more sensible to examine the causes of the administrative and services problems in municipalities and seek solutions by eliminating these causes.

Administrative reform can be associated with everything to do with reforming the public administration. Administrative-territorial reform, however, means changes to the public administration resulting from territorial changes (Teeväli 2009: 27). Administrative-territorial organization therefore represents the structural dimension of public administration, and must be compatible with the functional, organizational, decision-making and other dimensions of public administration (Kjellberg 1988: 8-13).

A solution to the different problems in the administrative system cannot therefore be achieved by changing only one dimension (e.g. the territorial division). Instead a coordinated reorganization of the various dimensions of the public administration is necessary. This paper focuses on the territorial organization of administrative issues, looking at the remaining administrative aspects only insofar as they relate to the territorial organization of public administration and services. By doing so, it is possible to analyze, how rational and effective it would be to focus solely on the territorial reform of public administration in Estonia.

The goal of this paper is to analyze the theoretical, political and organizational bases of the territorial division of the country into municipalities and offer a research direction for identifying conceptual solutions to the development problems in Estonian municipalities. We tackle the following research tasks to accomplish this goal:

- systematize theories concerning the territorial division of the country into municipalities and analyze the possibilities and limitations for their application;
- discuss administrative-territorial reforms in Nordic countries, their causes and consequences;
- describe the development, nature and indicators of the administrative-territorial division of Estonia;
- empirically analyze the relationship between municipal size and capability and development indicators.

The article consists of four parts. In the first part we investigate the theoretical bases of the administrative-territorial division of countries. In the second part we examine the experience of the Nordic countries in shaping their administrative-territorial division. The third part is devoted to problems associated with the administrative-territorial division of Estonia, highlighting indicators of municipal capability and development. In the fourth part we analyze empirically the relationship between the size of the Estonian municipalities and their capability and development indicators.

2. THE THEORETICAL FOUNDATIONS OF A COUNTRY'S ADMINISTRATIVE-TERRITORIAL DIVISION

There exist contradicting opinions about the optimal administrative-territorial division of a country, where some favour large municipalities and others small. There are four main arguments used by those who favour large municipalities (Relationship.....2001: 6):

- large municipalities are economically more efficient;
- in large municipalities the political processes are more democratic;
- large municipalities have more possibilities for promoting economic development;
- large municipalities will provide a better and fairer distribution of services, tasks and tax burdens.

The most widely used statement is that economic efficiency is dependent on the size of the municipality. Large municipalities are thought to be more efficient because of alleged economies of scale and scope.

Economies of scale refer to the reduction of unit costs that occurs as a result of increasing the production volume. This occurs when the long-term marginal costs of production are smaller than the long-term average cost (Bailey 1999: 25). If economies of scale occur, larger municipalities are able to provide more public services at the same level of expenditures or reduce the level of expenditures while retaining the volume and quality of public services. Economies of scale occur when there are fixed costs (associated with providing a service), when an increase in supply will promote workforce specialization and better division of labour or when discounts or other reductions of costs can be achieved through buying in large quantities.

The merging of municipalities and the possible spatial centralization resulting from this also has a negative side, in particular the reversion of rural areas. Moreover, it is more than doubtful whether the theoretical positions of economies of scale can be used to predict the efficiency of public service provision in municipalities, because according to Bailey (1999: 27), public services are not very standardized, the outputs are not clearly identifiable and quantifiable and unit costs are not measurable with sufficient accuracy due to the high proportion of fixed costs.

Consequently, economies of scale can occur only in a few public services. For some public services a larger municipality may instead lead to unit cost growth or in other words diseconomies of scale (Dollery, Crase 2004: 269). Byrnes and Dollery (2002: 393)

conducted a meta-analysis of various studies carried out in the United States and United Kingdom from 1951 to 2001 and found that 39 percent of the research papers showed no statistically reliable relationship between per capita expenditure and municipality size, and that diseconomies of scale characterized larger municipalities in 24 percent of the research papers.

Due to the diversity of public services, the economies of scale argument is not adequate to justify the merging of municipalities. To achieve economies of scale when providing a diversity of public services it is much more reasonable for municipalities to cooperate with each other in this field instead of merging (Friedrich, Reiljan 2010). In addition, services (or products) with the potential for economies of scale could be bought in from private companies or the rights to provide those services could be privatized. Alternative options (cooperation, buying-in services and products and privatization) make economic efficiency as a justification for large municipalities even more dubious.

The possible presence of **economies of scope** is a second major argument in favour of the alleged economic efficiency of large municipalities. As Dollery and Crase (2004: 269) write: “Economies of scope, refer to the economic advantages that occur by providing a broad range of goods and services in a single organization, like a municipality. In particular, economies of scope arise when the cost of producing a given set of services in a single organization is lower than the cost of those services being produced by a number of specialized organizations”.

Dollery and Fleming (2006: 276-279) conclude that there are three main sources of scope economies: jointness in inputs – one input can be used in the production of more than one output and thus inputs could be fully exploited; jointness in outputs – more than one output is produced from the same set of inputs (typically a main product and one or more by-products); and interactions between service provision and goods production processes – outputs from one process are inputs into the second process.

The economies of scope argument for justifying the need for large municipalities is also one-sided. For example, the diversity of

services might lead to their management becoming overly complicated resulting in a deterioration of management quality. The centralization of service delivery can also increase the cost of receiving the services (e.g. higher transport costs for residents); therefore, the costs to society as a whole could increase in large municipalities rather than decline.

The economic efficiency of municipalities is not the most important aspect in a country's administrative-territorial division, and therefore, economies of scale and scope should not be overstated. It should be remembered that a municipality is not a business focused on economic efficiency, but a government agency that has to ensure public administration and the development of a democratic society. Total costs and cost-effectiveness can only be a topic for discussion when the presence of public administration and democratic development are guaranteed (Reiljan, Timpann 2001: 433). A similar view is stated by Sootla et al. (2008: 21), who found that achieving scale and scope economies in diffusely populated Estonian municipalities is problematic, and that mergers would make sense only if a qualitative change in governance and relations between the local authorities and citizens, as well as local authorities and central government authorities would be achieved.

Another argument in favour of large municipalities is that political processes are more democratic. Linking the development of democracy to larger municipalities might seem like a contradiction because usually small municipalities are thought to be more democratic than large (Aalbu et al. 2008: 34). Reiljan and Timpann (2001: 434) emphasize that to develop democracy, it is important that the lowest level of public administration is situated closest to the citizen. The optimal distance between the people and the lowest level of public power depends on the level of democratic thinking among citizens and on the length of their democratic experience. The less people have an awareness and experience of democracy, the closer to the lowest level of public power they should be and the smaller the optimal size of a municipality should be. In Estonia, where the direct experience of participation in democratic processes is only twenty years old, municipalities should not be large, because the institutions of large municipalities are further from the people.

According to Sootla et al. (2008: 19), one vote from a citizen living in a large municipality counts relatively less in political decision processes than one vote from a citizen living in a small municipality. Therefore, increasing the size of municipalities decreases the influence of each vote and reduces each citizen's potential for influencing municipal decisions and their interest in participating in political processes. People living together in a certain area also tend to have common interests and a strong territorial identity, which is why they jointly select the representatives of the municipality (Aalbu et al. 2008: 35). It is feared that increasing the size of the municipality will result in people losing their territorial identity and their feeling of being involved in the decision-making, and therefore their interest in the activities of their municipality.

However, pairing greater awareness of democracy with small municipalities also has its problems. First of all, the suppression of political debate and dissidents is more effective in smaller municipalities, because it can be justified in terms of social and community-based unity (Newton 1982: 203; Sootla et al. 2008: 19; Relationship ...2001: 14). The suppression of dissent and the resulting stifling of one's opinions may occur especially in municipalities where political leaders are also economic leaders (i.e. the largest employers). In this situation a political difference of opinion may lead to a direct economic threat (e.g. job loss). In larger municipalities political and social structures are generally more diverse, and thus, the opposition has a greater chance to express their ideas more freely and safely. According to Sootla et al. (2008: 18), larger municipalities in Estonia may increase the diversity of political parties and reduce regional particularism. Larger municipalities may also have more citizens' associations and community groups (Newton 1982: 200), which are often an indirect means of expressing personal opinions and getting involved in the community. Another reason why smaller municipalities could have lower citizen participation is the limited scope of activities they are able to pursue. According to Newton (1982: 202), the less a municipality is able to do, the less its citizens will bother themselves about its affairs.

The third major justification for large municipalities emphasizes that larger municipalities have more opportunities to support economic development on their territories through larger investments and other policy measures (Aalbu et al. 2008: 41). For example, a bigger budget will ensure lower interest rates, so more and cheaper money can be invested in improving the standard of living for local citizens. A larger municipality could also deepen the specialization of its officials, which would lead to more professional management of government functions (Aalbu et al. 2008: 36). Of course, the implementation of highly skilled professionals depends on their existence in the labour market and on the competitiveness of the working conditions offered by the municipality. Estonia's problems include the lack of policy independent professional public officers and the resulting high dependence of public officers on policy fluctuations.

The fourth and last major justification for large municipalities says that larger municipalities are better able to ensure a fair and efficient allocation of public services and taxes. However, it does not actually matter how big the municipality is, but how the production of public services is divided between the central government and municipalities, and how effectively the intergovernmental financial transfer system functions.

In contrast to the one-sided and controversial justifications for larger municipalities there are approaches that emphasize the benefits of small municipalities. The theory most used for justifying the rationality of small municipalities is the theory of local expenditures created by Charles M. Tiebout (1956). This theory is based on competition among municipalities in designing the volume and structure of municipal revenues (charges, taxes) and expenses (services). People are thought to move to the municipality that best satisfies their personal preferences. The greater the number of municipality units (i.e. the smaller they are), and the more they differ from each other, the better the preferences of the people are satisfied (Tiebout 1956: 418). At the same time, the assumptions in the theory (Tiebout 1956: 419-420) clearly ignore the real situation:

- Consumer-voters are fully mobile and will move to the municipality where their preference patterns are best satisfied;

- Consumer-voters are assumed to have full knowledge of the differences between revenue and expenditure patterns and to react to these differences;
- There are a large number of municipalities in which the consumer-voters may choose to live;
- Restrictions due to employment opportunities are not considered;
- The public services supplied exhibit no external economies or diseconomies between municipalities;
- For every pattern of municipal services there is an optimal municipal size;
- Municipalities below the optimal size seek to attract new residents to lower average costs. Those above optimum size try to get rid of some residents. Those at the optimum try to keep their population constant.

If these assumptions were valid, municipalities would be like companies that compete with each other – the country would be the market, the revenue and cost structure of municipalities (taxes and public services offered) would be the product and the residents would be the consumers. As in a normal market, the supply of and demand for public services would determine the basis of the prices and volumes, which ultimately would determine the number of municipal residents. Unfortunately, full mobility of people does not exist in reality, people do not have full knowledge of the differences between revenue and expenditure patterns and there is not enough diversity among municipalities to fully satisfy the people's preferences. However, competition between municipalities can be found (Oates 1981: 93-94). For example, people searching for a place to live consider different aspects which can be influenced by the municipality (e.g. the existence of kindergartens, schools, the crime rate, etc.).

Administrative decentralization and competition between municipalities, however, may lead to negative co-phenomena. Too much autonomy in municipalities and the lack of adequate coordination between the central and local governments allows municipalities to be inefficient in their spending and live beyond their revenues, leading to budget deficits and the appreciation of

municipal borrowing because of the risk premium (de Mello 2000: 366). These financial imbalances could jeopardize macroeconomic stability throughout the country.

The problems in proving the rationality of small municipalities are similar to the problems proving the expediency of large municipalities. Because they are conflicting concepts, it is often possible to criticize the weaknesses of one concept with the strengths of the other and vice versa. The situation cannot be resolved with empirical studies either, because the theories are based on formal, unrealistic assumptions.

One way to overcome this situation is to recognize that according to geographical, historical, demographic, cultural, social, legal and economic circumstances, a certain optimal size of municipality can be found. It is sometimes believed that Club Theory can be used to find the optimal size of a municipality, because of the similarities clubs and municipalities have. According to Sandler and Tschirhart (1997: 335), a club is a voluntary group deriving mutual benefits from sharing one or more of the following: production costs, member characteristics, or a good characterized by excludable benefits. The club offers services that are financed through taxes that are paid by its members. It is relatively easy to see the similarities between clubs and municipalities in light of such explanations. Club theory must answer two questions: how much of the desired benefits should be produced and how many members should there be in the club (Rosen 1995: 528). The optimal size of the club is found when the marginal benefits that a member secures from having an additional member are just equal to the marginal costs that the member incurs from adding a member (Buchanan 1965: 5). Unfortunately, Club Theory cannot be used to find the best administrative-territorial division either, because there is no straightforward relationship between the public services offered by the municipality and the tax burden that the residents could adjust according to their preferences.

The analysis of different theoretical approaches shows that both large and small municipalities have their own advantages and disadvantages. A meta-theory that would synthesize these contradicting approaches and help to determine the best size of a

municipality has not been developed yet. What is clear, however, is that an optimal size of municipality can exist only if municipalities provide public services with similar cost curves. In reality, the cost curves of public services are different, and therefore, the optimal production of various public services needs different sizes of municipalities. This means that a municipality of a certain size can be too small from the perspective of one public service and too big from the perspective of another public service. Thus, theoretically, there is no optimal size of municipality and, consequently, the search for an optimal administrative-territorial division of a country is an unsolvable pseudo-task. Changing the territorial division can improve the supply of some public services, but will inevitably worsen the supply of other services.

3. NORDIC EXPERIENCE IN SHAPING ADMINISTRATIVE-TERRITORIAL DIVISION

The above has shown that a theoretically justified best solution for a country's administrative-territorial division does not exist. In this case, investigating the experience of other countries may provide valuable information about a better administrative-territorial division. This approach relies on the assumption that the functioning administrative-territorial solutions of one country can be transferred to another country. Randma and Annus (2000) have written that such an assumption comes from the fact that the main administrative goals of municipalities in different countries are similar. However, this assumption ignores the fact that, in addition to the formal goals, the administrative organization of a country and its efficiency is impacted by cultural, geographical, historical, demographic, social and legal factors etc. Thus, the investigation of foreign experience must focus primarily on the study of different approaches, rather than copying solutions.

Next, an investigation of the administrative-territorial divisions and reform experiences of Nordic countries – Finland, Sweden, Norway, Denmark and Iceland – will be carried out. The investigation points out the characteristics and factors that could be

useful when solving the problems of administrative-territorial division in Estonia.

Finland, like Estonia, has two levels of government – central government and municipalities. The municipalities in Finland are relatively small. Therefore, they have created special co-operative organizations for the joint provision of specific services. Participation in those joint municipal authorities is mostly voluntary. However, there are some areas where membership is compulsory – services such as health care (21 regions) or regional development and planning (19 regions). (Aalbu et al. 2008: 19) In addition to the joint municipal authorities, there are six Regional State Administrative Agencies and 15 Centres for Economic Development, Transport and the Environment that started operating on 1 January 2010. These agencies and centres are engaged in the provision of “national” public services at the regional level (the Reform Project for ... 2010).

Despite the orientation towards promoting cooperation between municipalities, the number of municipalities in Finland has decreased by more than one third since World War II: in 1955, Finland had a total of 547 municipalities, in 1977 the figure stood at 464 and dropped to 455 by 1996, in 2007 the number of municipalities had decreased to 416 and as of January 2010 the number of remaining municipalities is 342 (Trends in the number of municipalities 2010; Finnish local government 2010). These mergers have not been the outcome of administrative-territorial reforms. Economic hardships, on the one hand, and the central government's support on the other hand, have led small municipalities to voluntarily join the larger and richer municipalities (Oitmaa, Rõigas 1998, 88-89).

In February 2007, a law was adopted in Finland that set two thresholds for the restructuring of municipalities and local services: a municipality must have at least 20 000 inhabitants to provide basic health services and 50 000 inhabitants to ensure vocational education. The impact of this law on the administrative-territorial division of Finland is not yet clear.

Sweden has two levels of sub-national government – municipalities and counties. Most local public services are offered by municipalities except health care services, which are mainly the responsibility of the county. The central government is represented at the regional level by the county administrative board and by the administrative authorities in various sector and regional organizations (Aalbu et al. 2008: 23). Swedish legislation places municipalities and counties on an equal footing, even though counties cover a larger geographical area than municipalities. Therefore, county councils are not superior authorities to municipal institutions (Local government in Sweden 2005: 4). According to Montin (2000: 3), the expansion of Swedish welfare state services can be reconceptualised as municipal welfare expansion.

Since the 1950s two administrative-territorial reforms have been carried out in Sweden. In 1946, the Swedish Parliament set 2000 inhabitants as the lowest limit for the size of a municipality (Gustafsson 1983: 28). As a result the number of municipalities fell from 2496 to 1037 by 1952 (Oitmaa, Rõigas 1998, 82). In 1964, the Swedish Parliament raised the minimum size of a municipality to 8000 inhabitants (Sandalow 1971: 773). The municipalities were given the right to decide for themselves whether or not a merger was necessary. As a result the number of municipalities decreased from 821 to 675 (Oitmaa, Rõigas 1998: 83). In 1969, the voluntary principle was cancelled because, despite the mergers, there were still municipalities whose population did not meet the required minimum (Oitmaa, Rõigas 1998: 83; Sandalow 1971: 773). Compulsory mergers reduced the number of municipalities to 278 by 1974 (Oitmaa, Rõigas 1998: 83).

Sweden is a useful example of how command mergers of municipalities carried out by the central government can lead to problems. During the last ten to fifteen years a number of municipalities have been partitioned into two or more units (Montin 2000: 3). One argument outlined for these separations was the need to develop democracy at local level, and it has been argued that the political activity of citizens is higher in smaller municipalities (Oitmaa, Rõigas 1998: 83). Therefore, the number

of municipalities has increased to 290 (Municipalities, county councils and regions 2009).

Another problem with the Swedish administrative-territorial reforms was the sharp decrease in the number of elected political representatives. In 1951, there were about 200 thousand elected political representatives, but by 1974 the corresponding figure had dropped to 50 thousand. The decrease in the number of elected political representatives reduced representation for various interest groups and the number of meetings with voters per representative also dropped. Different political measures had to be taken to increase the number of elected political representatives to 70 thousand by 1980. However, the reforms also improved the coherence of local policy with national policy (through intra-party relations and democracy), increased and deepened political debate over local issues and improved political awareness among citizens (Gustafsson 1983: 30-31).

Denmark, like Sweden, has two sub-national government levels – municipalities and regions. The regions are mainly responsible for the provision of health care services. Municipalities are responsible for basic education and other local services, and land planning (Aalbu et al. 2008: 16). There is no system of subordination between the regions and the municipalities, as they possess different tasks and responsibilities (The Danish Local Government System 2009: 4).

Denmark's central government has conducted two major administrative-territorial reforms since World War II. The administrative-territorial reform of 1970 decreased the number of municipalities from 1389 to 275 and the number of regions from 24 to 14 (The Danish Local Government System 2009: 3). With the second administrative-territorial reform, which ran from 2001–2006, municipalities were given more responsibilities and the number of municipalities was reduced from 271 to 98. At the same time the number of regions was reduced from 14 to 5 (Aalbu et al. 2008: 17-18). As a result the municipalities in Denmark are now significantly larger than in other Nordic countries.

Norway also has two local government levels – municipalities and counties. There are 430 municipalities and 19 counties and both have the same administrative status (Local Government in Norway 2008: 7). The Norwegian local and regional administrative-territorial division is characterized by stability, although there have been a few municipal mergers since 2000 (Aalbu et al. 2008: 21-22). Small changes at the regional level took place 1 January 2010, when the responsibility of the counties was increased. The largest single new task ascribed to the county authorities is responsibility for the national highways and the appurtenant ferry crossings (The county authorities... 2010).

Iceland has only one sub-national government level like Estonia and Finland. The population of Iceland's municipalities is often very small. The smallest municipalities are agricultural communities, whose population is in some cases within just 50 people. At the same time, Iceland is an urbanized country where the population of the capital region makes up nearly 75% of the entire population of Iceland (Aalbu et al. 2008: 25).

Iceland's government has repeatedly encouraged municipalities to merge. In 1950 there were 229 municipalities in Iceland, but by 1990 there were still 204. Currently there are 78 municipalities in Iceland, 14 of which have a population below 200 (Aalbu et al. 2008: 25-26).

The investigation of the developments of administrative-territorial divisions in the Nordic countries showed that experiences in shaping the national administrative-territorial division vary greatly. Denmark and Sweden have carried out compulsory mergers led by the central government, but the mergers in Finland, Norway and Iceland have taken place on a voluntary basis. The differences in the shaping of the administrative-territorial division may result from the different national visions for the role of the municipal sector in these countries. Sweden and Denmark had a strong central government and administrative systems long before the ideas of nationality began to spread. The municipalities in these countries are primarily aimed at achieving economic efficiency in public service provision and they should be viewed as extensions of the central government. Finland, Norway and Iceland, however,

acknowledged themselves as nationalities long before they could be declared independent states and the municipalities are therefore strongly related to local identity and carry with them the values of self-determination (Aalbu et al. 2008: 8).

Similarly to Norwegians, Icelanders and in particular Finns Estonians acknowledged themselves as a nation earlier than they were able to declare themselves as an independent state. Also, Estonia's central government has not been able to carry out a compulsory administrative-territorial reform and so far the mergers have been carried out on a voluntary basis. Opposition to the administrative-territorial reform in Estonia can therefore result from strong national and communal identity, and still relatively weak state identity (Ruutsoo 2002).

In addition to investigating the development of administrative-territorial divisions in the Nordic countries, it is reasonable to compare data describing their current administrative-territorial divisions (see Table 1).

The data shows that the most populous municipalities are in Denmark and at the same time Denmark has the smallest municipalities by area. This is due to the high population density in Denmark, where it is more than six times higher than in Sweden and seems even higher compared to the other countries. Low population density may be one of the main reasons why the population of the municipalities in other countries is lower than in Denmark. With low population density, larger population would mean larger municipalities in terms of area. Areas that are too large could make the management of municipalities more difficult and the provision of public services economically less effective or more difficult to use. Sweden and Norway are trying to balance the existence of less populous municipalities with larger regions, which are able to achieve economies of scale in the provision of their services. In Finland, municipalities try to achieve economies of scale through cooperation. In Iceland, where population density is extremely low and the population small, creating regions does not make sense and there the central government provides services that in other countries fall often within the competence of municipalities or regions.

Table 1. Indicators of administrative-territorial division in Nordic countries

	Finland	Sweden	Norway	Denmark	Iceland
Population (people)	5 326 314	9 256 347	4 799 252	5 511 451	319 368
Area (km ²)	338 145	450 295	323 802	43 094	103 000
Population density (people per km ²)	16	21	15	128	3
Number of municipalities	342	290	430	98	78
Average population of municipalities (people)	15 574	31 918	11 161	56 239	4 094
Average area of municipalities (km ²)	989	1 553	753	440	1 321
Number of regions	- ⁴	21	19	5	-
Average population of regions (people)	-	440 778	252 592	1 102 290	-
Average area of regions (km ²)	-	21 443	17 042	8 619	-

Source: Eurostat 2010; CIA – The World Factbook 2010, Aalbu et al. 2008: 16-26, Finnish local government 2010; authors' calculations.

The population of Estonia is 1 340 021 in 2010 (Enim...2010) and the surface area 45 227 km², which makes Estonian population density 30 people/km². Estonia has 226 municipalities which means, that in 2010 the average number of inhabitants per municipality was 5 929 and the average area of a municipality was 200 km². The average population of the Estonian municipalities and the average area is therefore significantly lower than in Nordic countries (except Iceland). Therefore, there could be room for municipal mergers in Estonia's administrative-territorial division.

⁴ Finland operates on a regional level through various institutions, e.g. joint municipal authorities, Centres for Economic Development, Transport and the Environment, Regional State Administrative Agencies. Because their numbers, sizes and functions are different, general indicators for the regional level can't be given.

When comparing the sizes (especially the average populations) of municipalities, the tasks assigned to them have to be taken into account. A large number of tasks require an adequate municipal size to cope with the challenges, but few tasks enable the existence of small municipalities. In this aspect Estonia is better suited for an administrative-territorial division with smaller municipalities, where joint municipal authorities should be established for some services (following the example of Finland).

4. THE DEVELOPMENT OF ESTONIA'S ADMINISTRATIVE-TERRITORIAL DIVISION AFTER REGAINING INDEPENDENCE

The transition of Estonia's municipalities to the current arrangement began on the 8 August 1989, when the Supreme Soviet of the Estonian SSR endorsed the principles of administrative reform with the goal of restoring a democratic society. At that time, under Moscow, this was possible mainly at the local and regional level. Sections of the 1938 Constitution of the Republic of Estonia concerning municipalities were taken as the basis for the new municipalities. The principles of the European Charter of Local Self-Governments were also taken into account. On 6 December 1989, the Supreme Soviet of the Estonian SSR adopted the decree for the creation of a self-governing administrative system, in which the Soviet administrative units were changed to municipal units without any territorial changes. During the period 1990–1993, 242 towns and parishes received municipal status (Uuet 2002: 231).

On 28 June 1992, the new Constitution of the Republic of Estonia was adopted by a referendum (RT 1992, 26, 349), which stipulated the nature of Estonian municipalities. The Constitution created a legal basis for the development of Estonia's municipal structure to its modern form. On 12 May 1993, the Parliament adopted the Local Government Organization Act. Under this Act, Estonia's local government adopted a single-level system. The introduction

of a single-level local government system was made so that administrative authority would be as close as possible to individuals to ensure the democratic development of society (Reiljan, Timpmann 2001: 424).

In 1995, the Territory of Estonia Administrative Division Act (RT I 1995, 29, 356) was adopted, which established the regulations for changing the number, size and names of municipalities. That Act regulated the merger of municipalities until 24 July 2004. Since the Act did not provide specific information on the issue of modifying the administrative-territorial division, the Estonian Parliament (*Riigikogu*) adopted the Promotion of Local Government Merger Act on 28 June 2004, which substantially modified the Territory of Estonia Administrative Division Act and the Local Government Organization Act. Since 1996, there have been 22 municipal mergers in Estonia, in which 51 municipalities have merged (Ligema 2007; Haldusterritoriaalse korralduse...2009).

When Estonia regained its independence, sudden changes in the administrative-territorial division were avoided. The deepening of regional inequalities has increased, despite the political discontent in this regard. Despite several administrative-territorial reform projects by the central government, the administrative-territorial division of Estonia has not changed significantly because of strong political and social opposition. Here we see the analogy with Finland that local identity is worth preservation in the eyes of the people.

The problem of regional inequalities, however, still needs to be dealt with. Since the main focus in Estonia has so far been on creating larger municipalities, it is reasonable to analyze, whether the size of Estonian municipalities causes their current problems. To do that, indicators that characterize the situation of Estonian municipalities have to be found.

Municipalities have to organize and manage local life based on the needs and interests of the population, and taking into account the specific development of the municipality. On the one hand, this requires a good knowledge of local conditions, which in theory should offer an advantage to small municipalities. At the same

time, the needs and interests of the population may require such financial and administrative capacities that in theory are inherent to large municipalities. From the perspective of administrative division it is therefore important to identify which is the best size for municipalities to be able to organize and manage local issues.

The first group of indicators used in this study therefore will characterize the public service delivery capabilities and dynamics of Estonian municipalities:

- the position of the municipality in the Estonian municipality capability index (EMCI) ranking (Sepp et al. 2009: 13-16) – reflects the capability of a municipality to deliver public services;
- the position of the municipality in the territorial development index (TDI) ranking (Sõstra 2009: 53-57) – shows the development potential of a municipality;
- the municipality's score according to the development index of Enterprise Estonia (DIEE) (KOV finantsraport 2009) – shows the development dynamics of a municipality compared to last year.

An analysis of the relationships between the indicators listed above and the parameters describing the size of a municipality will show whether the size of a municipality affects its capability to provide public services and its pace of development and further development potential. The analysis should also reveal whether it is possible to find the best administrative-territorial division from the perspective of capabilities and development.

The second group of indicators consists of financial performance and capability indicators, as adequate financial potential is needed to ensure the provision of public services and the development of the municipality. The group consists of the following indicators:

- the municipality's score according to the financial index of Enterprise Estonia (FIEE) (KOV finantsraport 2009),
- the debt reserve of the municipality and (Kohalike omavalitsuste võlakooormus 2009),

- the free to use revenue⁵ and gross revenue ratio of the municipality (Kuuaruanne 2009).

These indicators help to investigate the claim that larger municipalities have greater financial opportunities and better economic management. The analysis of the relations between the indicators listed above and the parameters describing the size of a municipality will show whether the size of the municipality has an impact on the quality of financial management in the municipality, the borrowing opportunities of the municipality, the financial autonomy of the municipality, and which kind of administrative-territorial division would be economically most efficient if significant relationships exist.

The study of different theories and approaches pointed out that the democracy argument can be used simultaneously for justifying the rationality of both large and small municipalities. The third group of indicators therefore consists of indicators characterizing the development of democracy in the municipality. The indicators are taken from the municipal council elections which took place in October 2009. The indicators used in this study are as follows:

- voter turnout,
- the number of candidate lists for election,
- the number of mandates and the number mandates per inhabitant,
- the total number of candidates and the number of candidates per inhabitant.

The total number of candidates shows the number of election options the inhabitants have and the number per inhabitant characterizes how active inhabitants are in running for election. The number of mandates shows the possibility for various interest groups to represent themselves in the council, the number of mandates per inhabitant indicates the ability of residents to participate in municipal governance, and the number of candidate

⁵ The free to use revenue consists of the following types of revenues: tax revenues, revenues from selling goods and services, and other revenues.

lists can be considered as an indicator of political diversification in the community.

As pointed out earlier, increased cost-effectiveness is one of the most commonly used arguments for justifying the rationality of large municipalities. The fourth indicator group is intended to analyze this claim. However, overall cost-effectiveness cannot be proven because the content and quality of public services differ among municipalities. The only comparable costs among municipalities are the (general administrative) costs of governance for the municipality per capita.

The population size and the area of the municipality together with population density are indicators that are used to characterize the size of the municipality.

5. EMPIRICAL ANALYSIS OF THE IMPACT OF MUNICIPAL SIZE

The empirical analysis covers all the municipalities of Viljandi County and also the municipalities that share a common land border with Viljandi County⁶. Therefore, the analysis covers a total of 32 municipalities – 6 towns and 26 rural parishes. As towns and rural parishes provide different qualitative life and public service conditions for their inhabitants, we have to assume that the relationship between municipal size and indicators for characterizing the capability of municipalities is qualitatively different in these groups of municipalities. Therefore, towns and rural parishes are analyzed separately.

The relationships between municipal size and municipal capability are analyzed quantitatively in both groups – towns and parishes – based on the following assumptions about qualitative similarity:

⁶ This data originates from the master's thesis (Ülper 2010) that had the objective of creating a optimal administrative-territorial division plan for the County of Viljandi.

- population needs and interests do not differ significantly among municipalities;
- the provision of public services is guaranteed in all municipalities by law at least to a minimal quantity and acceptable level of quality;
- the democratic election mechanism ensures that the needs and interests of residents, and the laws are respected, otherwise citizens would choose other people to run the municipality.

The strength of the relationships is found using correlation analysis. The strength will be evaluated on the basis of the following classification: the correlation coefficient r is less than 0.3 – weak relationship; r is 0.3 to 0.7 – moderate relationship; r is over 0.7 – strong relationship.

Correlations between the indicators describing municipal size and the indicators describing public service delivery capabilities, development levels and dynamics, financial capabilities, development of democracy and cost of general governance in municipalities are presented in Table 2. The upper numbers in Table 2 are the correlation coefficients and the lower numbers in italics are the characteristics of the statistical significance.

Given the correlation coefficients presented in Table 2 alongside the partial correlation coefficients (Ülper 2010: 108-118), it can be concluded that:

- There is no relationship between the size of the municipality and its place in the TDI ranking;
- There is a moderate negative relationship between the population size of the municipality and its DIEE score when the effects of the other indicators are eliminated. In a real situation where the DIEE score is also affected by other indicators, population size has no relationship with the DIEE score of the municipality;
- Population size and density have both moderate negative relationships with the place of the municipality in the EMCI ranking. However, when eliminating the effects of other indicators, population size and density show no relationship with the place of the municipality in the EMCI ranking. It can

be assumed that a larger population size alone does not affect the place of the municipality in the EMCI ranking, but together with higher population density a relationship exists.

Table 2 shows that none of the size indicators have a statistically significant correlation with the FIEE score. There are also no statistically significant partial correlations between the size indicators and the FIEE score (Ülper 2010: 111). Thus, the argument outlined in the theory that the financial management of large municipalities is better than small municipalities can be refuted. There are also no correlations or partial correlations between the size indicators and the free to use revenue and gross revenue ratio. This means that small municipalities are not more dependent on government grants than large municipalities. The argument that larger municipalities have greater financial capacity due to the greater volume of loans they can apply for can also be refuted because there are no statistically significant correlations or partial correlations between the size indicators and the debt reserve of municipalities. The results above show that the financial capacity indicators of a municipality cannot be used to justify the proposals for improving the administrative-territorial division. However, the municipal debt burden and ability to take loans are figures that must be taken into account when planning an administrative-territorial reform because the municipal debt burden can be very different. An overly high debt burden can prevent a municipality from making significant investments from the perspective of development. Merging with a municipality with a low debt burden is one way to improve this situation. A merger carried out with the aim of reducing the debt burden, however, may not be in the interests of a municipality with a small debt burden, because its borrowing (and hence investment) ability could be reduced.

Table 2 shows that voter turnout has no statistically significant correlation or partial correlation (Ülper 2010: 114) with size indicators. These results refute the arguments made in the theory that larger municipalities reduce voter turnout because of the decreased influence of single votes and the loss of local identity.

Table 2. Correlations between the size of municipalities and indicators describing the socio-economic, financial and political development of municipalities

	Population	Area size	Population density
Correlations with development level and dynamics indicators			
Place in the EMCI ranking	-0,56 0,00	-0,32 0,11	-0,45 0,02
Place in the TDI ranking	-0,07 0,74	0,08 0,71	-0,30 0,14
DIEE score	-0,19 0,36	-0,10 0,63	0,03 0,88
Correlations with financial performance and capability indicators			
FIEE score	0,09 0,62	-0,10 0,58	0,07 0,71
Debt reserve	0,15 0,40	0,21 0,25	0,06 0,75
Free to use revenue and gross revenue ratio	0,16 0,38	-0,11 0,57	0,05 0,77
Correlations with democracy development indicators			
Voter turnout	-0,27 0,13	-0,27 0,14	0,05 0,80
Number of candidate lists	0,42 0,02	0,02 0,90	0,30 0,10
Number of independent candidates per inhabitant	-0,20 0,26	-0,09 0,62	-0,10 0,60
Total number of candidates	0,81 0,00	0,26 0,16	0,32 0,07
Total number of candidates per inhabitant	-0,44 0,01	-0,27 0,13	-0,14 0,44
Number of mandates	0,89 0,00	0,21 0,26	0,46 0,01
Number of mandates per inhabitant	-0,67 0,00	-0,40 0,02	-0,18 0,31
Correlations with economic efficiency indicators			
Costs of governance per inhabitant	0,65 0,00	-0,02 0,92	-0,14 0,43

Source: Rahvaarv...2009; KOV finantsraport 2009; Sepp et al. 2009: 13-16; Sõstra 2009: 53-57; authors' calculations.

It is important to note the moderate negative correlation (-0.44) between population size and the total number of candidates per resident and the strong positive correlation (0.81) between population size and the total number of candidates. These two correlations show that although larger municipalities have more candidates in absolute terms, they have fewer candidates per resident than smaller ones. This means that people's interest in personally participating in elections in large municipalities is lower than in smaller municipalities. This result cannot be considered, however, unambiguous proof of the fact that people in small municipalities are more interested in the wellbeing and development of their municipality. Large municipalities may have more citizens and community associations, which represent different interest groups at the community development, and allow influencing local government action. This argument is supported by a moderate positive correlation (0.42) between population size and the number of candidate lists, which proves that in large municipalities we see more political competition than in small ones.

The strong positive (0.89) correlation between the number of mandates and population size can be explained with paragraph seven of the Local Government Council Election Act (RT I 2002, 36, 220), which outlines the procedures for determining the number of members in municipal councils. Thus, it is guaranteed by law to a certain level, that larger municipalities, where there are more interest groups, also have more council members. However, a moderate negative (-0.67) correlation between population size and the number of mandates per resident means that residents of large municipalities have relatively greater difficulty in gaining access to the council. Larger municipalities are probably conservative in determining the number of members on the council and draw on the minimum requirements specified by law, and ignore the opportunity to ensure a better representation of interest groups in the council.

As a result of the analysis of the democracy indicators it can be concluded that the relationships between democracy and size indicators are often conflicting and no firm conclusions on the relationship between municipal size and the level of democracy

can be made. A similar result appears in another study investigating the municipal mergers that took place in 2005 (Sootla et al. 2008: 48). The study found that the mergers had resulted in the distancing of the residents from public institutions (in terms of both cognitive and territorial distancing), but at the same time the residents believed that the problems of rural villages were still the focus of municipal authorities and the unity of communities had strengthened.

The last line of Table 2 shows that the reciprocal⁷ population size has a moderate positive correlation (0.65) with the costs of governance indicator. This means that municipalities with smaller populations have higher costs of governance per inhabitant. The last line of Table 2 also shows that there is no statistically significant correlation between municipality area and costs of governance per inhabitant. When the impact of other indicators, however, is removed (Ülper 2010: 118), municipality area and the costs of governance per inhabitant have a moderate positive (0.38) partial correlation, which means that a municipality with a larger area is more expensive to govern than a municipality with a small area.

The conclusion of the empirical analysis is that most of the indicators analyzed have no statistically significant correlation with the size of the municipality, and therefore, the use of those indicators to argue in favour of the necessity of an administrative-territorial reform cannot be justified.

Based on the results of the empirical analysis it can therefore be argued that there is no empirical evidence to confirm the presence of significant size advantages among Estonian municipalities. The lack of size advantages also means that with the current municipal functions and financing system an optimal municipal size cannot be found. The obtained results coincide with the conclusion made in the first part: it is not possible to define what the best

⁷ The reciprocal population size was used because its relationship with the costs of governance per inhabitant was more linear than population alone, and therefore, the correlation coefficient described the relationship better.

administrative-territorial division is, since both large and small municipalities have their own advantages and disadvantages.

The lack of size advantages and the lack of an optimal size of municipality means that there's no reason for territorial division reform in the form of mergers or changing borders. There is no good reference point to which the current municipalities could be compared. From the perspective of improving the current situation for municipalities, it is therefore not wise to focus on carrying out an administrative-territorial reform. Instead, a wide-ranging administrative reform should be carried out, with which, if necessary, the municipal functions, financing, management and possibly even size are changed.

6. SUMMARY

The analysis of the theoretical approaches to municipal size pointed out that they are fragmented and incompatible. Some authors support small municipalities, and others large. The theoretical reasoning of both those directions is often strongly simplified and biased and a unified meta-theoretical approach has not been established.

To get an overview of practical experiences, the administrative-territorial division of the Nordic countries and the administrative-territorial reforms carried out in these countries were analyzed. The analysis revealed that both the current division, as well as the reform experience is varies. In Sweden and Denmark, the central government carried out a number of statutory municipal mergers, but in Finland, Norway and Iceland, the municipal mergers have taken place on a voluntary basis. The differences may be caused by differences in the historical evolution of the countries and in the different vision of the municipal sector's role in society.

The comparison of the administrative-territorial division of the Nordic countries with the administrative-territorial division of Estonia pointed out that Estonian municipalities have a considerably lower average population than the municipalities in

the Nordic countries (except Iceland), and the area of Estonian municipalities is also much smaller. Therefore, it was concluded that there could be room in Estonia for municipal mergers. More interest, however, should be given to the experience of Finland, where instead of merging the municipalities (making them bigger) they have focused on the promotion of cooperation (sometimes organized by the central government) among municipalities.

In the empirical part we at first described the evolution of the Estonian administrative-territorial division during the last twenty years and then reveal the indicators by which the impact of the size of municipality on economic, financial and democratic development could be analyzed. The indicators used in this paper can be divided into four groups:

- indicators describing the public service delivery capacities, but also development level and dynamics of municipalities;
- indicators describing the financial capacities of municipalities;
- indicators describing the development of democracy in municipalities;
- indicators describing the economic efficiency of municipalities.

Correlation analysis was used to analyze the relationships between these indicators and the municipal size indicators (population, area and population density). The analysis revealed that there is no empirical evidence to confirm either the presence of significant size related advantages among municipalities or the existence of an optimal municipal size considering current municipal functions and financing. The lack of size advantages and the lack of an optimal size, in turn, means that the need to change (reform) the administrative-territorial division cannot be justified.

The lack of theoretical and empirical evidence on the necessity for administrative-territorial reform means that merging municipalities alone cannot significantly improve the public service delivery capacities and economic and democratic development of Estonian municipalities. This means that future studies should focus on analyzing public services from the perspective of their economic efficiency, quality and accessibility, and in doing so, determine the optimal size of regions for providing the various public services.

Knowing the optimal size of regions would make it possible to reform the current provision of public services, either by creating joint municipal authorities⁸ for services that require larger populations to be produced efficiently, or by creating smaller public service areas within current municipalities for services that need to be provided as close to the people as possible. The merging of municipalities, however, should be left for the municipalities themselves to decide.

Finding the best administrative-territorial division for a country is not a problem that can be solved with simple and quick municipal mergers. Forced merging of municipalities can be considered unconstitutional in Estonia, but the central government does have the possibility to intervene in the shaping of public services provision without undermining the autonomy of municipalities. Improving the situation, however, requires adequate analysis, not the application of force or intimidation.

⁸ The theoretical bases for designing collaborative public service areas have already been investigated in the field of Estonian general education (Friedrich, Reiljan 2010).

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KOKKUVÕTE

Riigi haldusterritoriaalse reformi vajalikkus: Eesti juhtum

Seniste riigi haldusterritoriaalse jaotuse muutmise kavade puudulikkuse tõttu analüüsiti teoreetilises osas erinevaid kontseptsioone riigi haldusterritoriaalse korralduse parandamiseks, otsiti empiirilisi tõendeid erinevatele kontseptsioonidele ning võrreldi Põhjamaade haldusterritoriaalset korraldust. Teoreetiliste käsitluste analüüsisel selgus, et need on fragmentaarsed ja ühildamatud. Ühed autorid pooldavad väikseid omavalitsusüksusi, teised aga suuri. Mõlema suuna põhjendused on enamasti lihtsustatud ja ühekülgised. Ühtset metateoreetilist käsitlust senini kujunenud ei ole.

Praktiliste kogemuste arvestamiseks analüüsiti Põhjamaade haldusterritoriaalset jaotust ning neis riikides läbi viidud haldusterritoriaalseid reforme. Need kogemused on väga erinevad. Kui Taanis ja Rootsis on keskvalitsus läbi viinud mitmed kohustuslikud omavalitsuste liitmiste voorud, siis Soomes, Norras ja Islandil on omavalitsuste liitumised toimunud eelkõige vabatahtlikkuse alusel. Erinevuste põhjuseks on riikide erinevad ajaloolised traditsioonid ja erinev nägemus munitsipaalsektori rollist ühiskonnas.

Eesti omavalitsusüksuste keskmine rahvaarv on oluliselt väiksem kui Põhjamaade omavalitsusüksustes (v.a Island) ning ka pindala poolest on Eesti omavalitsusüksused palju väiksemad. Seetõttu võib Eesti haldusterritoriaalses korralduses olla ruumi omavalitsusüksuste liitumiseks. Rohkem huvi pakub aga Soome kogemus, kus omavalitsusüksuste ühendamise (suurendamise) asemel on keskendutud nende koostöö edendamisele, sh keskvalitsuse poolt organiseeritud ühistegevuse vormis.

Empiirilises osas kirjeldati Eesti haldusterritoriaalse jaotuse kujunemist. Selle analüüsi põhjal toodi välja näitajad, mille abil saab analüüsida omavalitsusüksuste suuruse mõju nende majanduslikule, rahanduslikule ja demokraatlikule arengule.

Omavalitsusüksuste olukorda iseloomustavad näitajad võib jaotada nelja gruppi:

- avalike teenuste pakkumise võimekuse ja omavalitsuste arengudünaamika näitajad,
- omavalitsuste finantsvõimekuse näitajad,
- demokraatia arengu näitajad,
- omavalitsuste kuluefektiivuse näitajad.

Analüüsimetodina kasutati korrelatsioonianalüüsi, mille abil uuriti omavalitsusüksuste arengut iseloomustavate näitajate seoseid omavalitsuste suurust kirjeldavate näitajatega, milleks valiti omavalitsuse elanike arv, pindala ja rahvastikutihedus. Empiirilise analüüsi tulemusena selgus, et praeguste omavalitsuste ülesannete ja rahastamissüsteemi tingimustes puuduvad tõendid oluliste suuruseeliste esinemist omavalitsusüksustes ning omavalitsuse optimaalse suuruse olemasolu. Suuruseeliste ja omavalitsuse optimaalse suuruse puudumine ei võimalda objektiivselt põhjendada Eesti haldusterritoriaalse jaotuse muutmise (reformi) vajalikkust.

Haldusterritoriaalse reformi vajalikkuse teoreetiliste ja empiiriliste tõendite puudumine tähendab, et ainult haldusterritoriaalse reformi abil ei ole võimalik oluliselt parandada Eesti kohalike omavalitsuste avalike teenuste pakkumise võimekust ja majanduslikku ja demokraatlikku arengut. Tulevaste uuringute seisukohalt tähendab see eelkõige avalike teenuste analüüsimist nende majandusliku efektiivsuse, kvaliteedi ja kättesaadavuse aspektist, et teha kindlaks erinevate teenuste pakkumise optimaalse suurusega piirkonnad. Erinevate teenuste pakkumiseks tuleks luua väikeste omavalitsuste ülesed (nende koostööl rajanevad) teenuste pakkumise piirkonnad või liigendada suured omavalitsusüksused teenuste pakkumine osapiirkondadeks. Samuti oleks seeläbi võimalik analüüsida maakondliku tasandi taastamise otstarbekust Eesti haldus-territoriaalses korralduses mõnede avalike teenuste pakkumise optimaalse suurusega piirkonnana.

Riigile parima haldusterritoriaalse jaotuse leidmine ei ole probleem, mida omavalitsusüksusi liites ühe hoobiga lihtsalt lahendada saaks. Omavalitsusüksuste sunniviisilist liitmist võib Eestis lugeda põhiseadusvastaseks, samas on aga keskvoimul

võimalus ilma omavalitsuste autonoomiat kahjustamata sekkuda avalike teenuste pakkumispirkondade kujundamisse. Olukorra parandamine eeldab aga pakkumispirkondade kujundamisel adekvaatset sisulist analüüsi, mitte jõu rakendamist või sellega ähvardamist.