

Chapter 8

The organization of the local welfare state

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Introduction

The welfare state in modern democracies is at least partly a local phenomenon. This is true in the sense that almost all welfare states leave some welfare functions in the hands of local governments. The extent of welfare decentralization varies across the globe from almost nothing (e.g. Malta) to including almost all core welfare areas (e.g. Denmark). However, some welfare functions, for example primary education, are decentralized almost everywhere (Boadway and Shah, 2009: 276). In other words, the welfare state in many countries and sectors is a local welfare state. There is therefore an interesting link between the welfare state and the local government system. However, the debate on the welfare state is rarely linked to the debate on the organization of local government systems.

In this chapter, we seek to establish this link. We focus on one fundamental aspect of any local government system, namely the size of local governments. The optimal size of local governments has been a hot topic in political science for centuries, if not millennia, since size arguably influences the way democracy works (Dahl and Tufte, 1973). The rise of the welfare state over the past 50-70 years has been 'the single most important transformation of advanced capitalist democracies in the post-World War II period' (van Kersbergen and Manow, 2020: 376). With this rise, the age-old debate of the optimal size of local government has gained renewed significance because it now affects the daily lives of ordinary citizens in important ways.

More specifically, we address how the size of local governments affects four core issues in the modern welfare state: expenditure on welfare programs, the effectiveness of welfare programs, the costs of running the political system, and local democracy. We provide empirical evidence from research on the Danish 2007 municipal reform, which represents an unusually promising quasi-experimental testing ground for examining these questions.

The chapter proceeds as follows. The next section accounts for the classic debate about the optimal size of local government. It includes an argument that this debate has gained added importance with the rise of the welfare state and the increased focus on local governments as service-providing jurisdictions. Next, we turn to the methodological challenges faced by researchers who want to bring empirical evidence on the impact of local government size. In this context, we introduce the Danish 2007 local government reform and argue that it constitutes an unusually strong empirical testing ground. We then present findings from four projects that use the Danish 2007 local government reform's quasi-experimental nature to address the relationship between size on the one hand and welfare programs, economy, and democracy on the other. We find that size does not matter much for the welfare expenditure and effectiveness, but that size is important for administrative costs and for democratic outcomes.

The debate on size and democracy

The question of local government size is a major classic issues within the discipline of political science dating back to Aristotle and Plato. As Dahl and Tufte (1973) explain in their influential book *Size and democracy*, fundamental democratic concerns are linked to jurisdiction size, although not in a straightforward way. Arguably, small jurisdictions facilitate citizens' participation in politics, enhance their trust in their own political competence, and breed civic consensus. They make politics less abstract and increase politicians' responsiveness to citizen views. They spread political power, further control over government, and increase political accountability. However, there are also important democratic arguments against small jurisdictions. Large jurisdictions allegedly facilitate diversity in beliefs and values, make politics more competitive and professional, and imply greater system capacity. They also have more organizational activity and thus more community groups, interest organizations, and political parties and therefore more serious media coverage of local politics (Blom-Hansen, Houlberg and Serritzlew, 2014; see also Dahl, 1967; Denters et al., 2014; Lassen and Serritzlew, 2011; Lewis, 2011; Newton, 1982; Sharpe, 1970; Treisman, 2007; Warren, 2011).

Economic dilemmas can be added to these democratic concerns. Dahl and Tufte (1973) discussed the relationship between jurisdiction size and factors like system capacity and citizen effectiveness. Economists have worked further with these questions and argue that small jurisdictions create the potential for welfare gains, because public services can be better tailored to local preferences (Oates, 1972: 31-63), or because citizens can move to localities that offer the ideal tax-service package (Tiebout, 1956). However, a counter-argument holds that large jurisdictions are more cost-effective due to economies of scale in the production of many public functions (Hirsch, 1959).

The rise of the welfare state over the past 50-70 years has given renewed value to the classic debate on democratic and economic concerns over local government size. According to Eurostat, local government expenditure averages 12% of GDP among countries in the European Union. There is considerable variation around this mean – from a low score of 1% on Malta to a high score of 35% in Denmark – but local government expenditure accounts for more than 10% of GDP in eleven EU member states.¹ What these statistical figures mean in practice is that when European citizens need the services of the welfare state, it is very often a local government official or a local government institution they need to contact. Local governments almost everywhere have turned into important providers of welfare services. In other words, the welfare state is largely a local government affair. Exploring the link between welfare services and the size of local governments is therefore a timely endeavor.

In the post-World War II period, a large number of countries have reformed their local government systems. Very often this has included changing the size of local governments. Given the number and validity of democratic, economic arguments for and against small jurisdictions, one might expect a great deal of variation in these reforms. However, the reform trend has been unidirectional: Changes of jurisdiction size have almost invariably led to larger units. The agenda has been to harvest scale effects by amalgamating local governments (Baldersheim and Rose, 2010; Fox and Gurley, 2006; Holzer et al., 2009; Swianiewicz et al., 2022).

¹ The cited statistics are 2020 values from Eurostat's digital database on General Government Expenditure by Function (COFOG).

Studying local government size: Methodological concerns and how the 2007 Danish municipal reform meets them

Studying the importance of the size of local governments is methodologically challenging. The main problem is that jurisdiction size is nonrandom. Size typically reflects a response to political problems. This means that while jurisdiction size may have an impact on factors like welfare expenditure, economy, efficiency, and democracy, the reverse may also be true. As such, jurisdiction size may be decided as solutions to problems related to these factors. For example, a local government facing economic problems may decide to amalgamate with neighboring local governments to solve these problems, or well-off districts in a large poor city may decide to secede to form their own local government to improve their own situation. The point is that there is a complex two-way relationship between the size of local governments and the factors we want to study. The researcher therefore faces potentially serious problems of endogeneity when studying this relationship.

The best solution to endogeneity problems is to turn to experimental methods (Blom-Hansen, Morton and Serritzlew, 2015). However, a true experimental investigation of the impact of jurisdiction size would involve a random distribution of jurisdictions of varying sizes across a political territory. Such a set-up would mean that not only is jurisdiction size exogenous, its effects are also uninfluenced by potential confounding factors. This would be a strong research design but practically – and ethically – very challenging, perhaps impossible, to establish.

If a true experimental design is not possible, the second-best solution is to use a quasi-experiment. Such an experiment resembles other experiments in the sense that there are experimental and control groups, an exogenous intervention, and measures of the effect of the intervention. However, unlike most types of experiments (but like natural experiments), the experimental intervention is not provided by the researcher but comes from the outside, for example from the political-administrative system. In contrast to all true experiments, however, assignment to experimental and control groups is not randomized in quasi-experiments, so active control for potentially confounding factors may be necessary.

A quasi-experimental investigation of the effect of jurisdiction size would require a large-scale reform of a country's local government structure, which includes some – but not all – local governments so that there is both an experimental group and a control group. Furthermore, the reform would need to be imposed upon the local government, for example by the central government, so that it is exogenous. Finally, controls for potentially confounding factors would need to be included in the analysis to deal with the nonrandom allocation of local government to treatment and control groups.

The Danish 2007 local government reform constitutes such a quasi-experimental set-up. The reform had two main ingredients. First, functions were redistributed among the three tiers of government: municipalities, counties, and the central government. This aspect of the reform involved all municipalities equally. Second, municipal amalgamations reduced the number of local governments from 271 to 98 new units (Mouritzen, 2010). The methodologically attractive aspect of the Danish reform is that not all local governments were amalgamated. 66 of the 98 new units were results of amalgamations of 239 old local governments, and 32 municipalities did not change. Couched in experimental language, the reform constituted a quasi-experiment in which a treatment group of 239 local governments received an external shock to their size, while a control group of 32 municipalities was left unchanged.

In the following sections, we present findings from four projects that use the Danish 2007 local government reform to investigate the relationship between jurisdiction size on the one hand and welfare programs, economy, and democracy on the other.² All four studies utilize a difference-in-difference design to compare the pre- to the post-reform development in the amalgamated municipalities with the control group of non-amalgamated municipalities.

Jurisdiction size and democracy

The local welfare state serves economic as well as democratic purposes. Political control of welfare production at the local govern-

² These sections draw – sometimes verbatim – on Lassen and Serritzlew (2011); Blom-Hansen, Houlberg and Serritzlew (2014, 2021); and Blom-Hansen et al. (2016).

ment level allows citizens to influence how their own schools, day-care centers, libraries, etc. operate, where they are located, how they are run, and how well they are financed. State-level welfare services are, of course, also governed democratically, and citizens can influence policy but not the welfare institutions they use. National politics is by nature much more abstract and almost never about specific institutions in citizens' own local area. In contrast, local politics is concrete and often about the very school that your kids attend or the roads on which you drive. This affects how democracy works. Dahl and Tufte (1973) point at two mechanisms: One is a democratic strength of the local level, and one is a limitation. The big strength of local democracy is that ordinary citizens typically have better opportunities to understand, participate in, and influence politics at the local level. This may lead to better democratic outcomes on indicators such as turnout, internal political efficacy, trust, political confidence, and satisfaction with democracy. However, the limitation of local democracy is that some policy areas cannot easily be controlled by local government, particularly if they are small, and that organized political participation may be hard or impossible because not all interest groups and parties exist at the local level.

The democratic strengths and limitations of local government are, of course, closely tied to jurisdiction size. It is due to the relative smallness of local government that politics can become more accessible but less potent. In very small jurisdictions, politics is very close to citizens, and in large jurisdictions, it is further away. One consequence is that political discussions may be quite different in large and small jurisdictions. In a study of local agendas, Mortensen et al. (2022) find that political agendas in smaller jurisdictions are simpler and shorter. Thus, jurisdiction size of local government may influence democratic indicators.

Using the Danish 2007 reform, Lassen and Serritzlew (2011) examine how jurisdiction size affects internal political efficacy. Internal political efficacy is a measure of citizens' political self-confidence, which is important for whether they believe that they can participate in politics or whether it is worth their while. A high degree of internal political efficacy is therefore a good measure of the quality of a democratic system. It turns out that jurisdiction size influences internal political efficacy. In larger jurisdictions, citizens tend to

have lower political efficacy. Studies of other democratic effects following the reform suggest that larger jurisdiction size leads to lower turnout in elections, lower trust in politicians' responsiveness, and lower satisfaction with local democracy (see the overview in Hansen, 2016). The effects are typically limited, particularly in the long term (Pedersen et al., 2022). However, it seems safe to conclude that the effects of jurisdiction size on a range of democratic outcomes are more likely to be negative than positive. Studies of local democracy in other countries (Gerring and Veenendaal, 2020) draw similar conclusions about negative effects on factors such as turnout, internal and external political efficacy, political confidence, and satisfaction with democracy (DeHoog, Lowery and Lyons, 1990; Lapointe, Saari-maa and Tukiainen, 2018; Denters et al., 2014; Denters, 2002).

Hence, jurisdiction size is likely to be important for democracy. However, the big trade-off here is that the potential benefits of small jurisdictions may come at an economic cost. We now turn our attention to three aspects of this question.

Jurisdiction size and the costs of running the political system

Blom-Hansen, Houlberg and Serritzlew (2014) use the Danish 2007 municipal reform to investigate whether the argument of scale effects is really so powerful that it trumps other arguments on municipality size. They start by clarifying how to design a proper test of this argument. First, in line with Hirsch (1959), they argue that large units cannot reasonably be expected always to produce with lower unit costs than small ones. It is more likely that the municipal cost curve initially exhibits increasing returns to scale, since some production costs are constant and unrelated to size, and since increasing production allows for more division of labor into more specialized functions. However, after a certain level of production is reached, decreasing returns to scale begin to emerge due to problems of communication and coordination.

The cost curve is, therefore, expected to be U-shaped. This suggests that there is an optimal jurisdiction size at the trough of the curve. However, since the optimal size is likely to vary across different tasks, it does not make much sense to try to estimate a general optimal size when dealing with multipurpose local governments. The optimal jurisdiction size for, say, sewerage production is like-

ly to be different from, say, education. Since the functions of local governments vary across countries and time, the search for a general optimal jurisdiction size is probably futile. This may explain the mixed evidence in the literature on scale effects in local government (Gendźwiłł, Kurniewicz and Swianiewicz, 2021; Tavares, 2018). Blom-Hansen, Houlberg and Serritzlew (2014) therefore argue that the argument of scale effects must be tested on the costs of running the political system. Any local government is a political system, and running it involves administrative costs. Globally, any other task can be – and is – placed in different tiers of government.

Blom-Hansen, Houlberg and Serritzlew (2014) use the Danish 2007 local government reform to test whether amalgamations reduce the costs of running the local political system. To compare local governments before and after the reform, they impose the post-reform structure on the pre-reform situation, that is, pre-reform municipalities that were amalgamated in 2007 are aggregated to their post-reform size. In a series of difference-in-difference analyses including appropriate controls, they then investigate how administrative costs per capita developed in amalgamating and non-amalgamating local governments in the period 2005–2011, that is, two years before the reform and five years after.

The results consistently show statistically significant scale effects. They took a few years to fully materialize, but five years after the reform, the savings amounted to 10% of average administrative costs. In other words, at least within the empirical range of jurisdiction size in the Danish local government sector, the costs of running the system decrease with unit size. Although the savings are far from trivial, it is still a relevant question whether this gain trumps other concerns of local government size. We return to this question in the conclusion.

Jurisdiction size and welfare expenditure

As noted in the introduction, the welfare state in modern democracies is at least partly a local phenomenon. This is nowhere more true than in Denmark, which, according to the Eurostat statistics discussed earlier in the chapter, has the largest local government sector in the EU. This is the result of decentralization of important welfare functions, including childcare, elementary schools, care for children

with special needs, eldercare, and labor market activities. Denmark is therefore an interesting case for investigating the link between the welfare state and the local government system.

This is what Blom-Hansen et al. (2016) do, continuing the work by Blom-Hansen, Houlberg and Serritzlew (2014) discussed above. The analysis from 2014 focuses on the costs of running the local political system, which amount to approximately 10% of total local costs; the study from 2016 investigates whether jurisdiction size affects local government expenditure spent on delivering policy to local citizens, which is the lion's share of local expenditure at approximately 90%.

Blom-Hansen et al. (2016) start by arguing theoretically that a strong relationship between welfare expenditure and the size of local governments cannot be expected. The reason is that most local welfare services are delivered by institutions within local governments such as schools, kindergartens, and nursing homes. Changing the size of local governments does not automatically change the size of these institutions. In other words, scale effects may be real, but they are likely to be located at the level of welfare institutions, not at the jurisdiction level. As in private production, firm size is different from plant size (Boyne, 1995). If true, this would mean that, at least as far as expenditure goes, there is no link between the welfare state and jurisdiction size.

The Danish 2007 local government reform again functions as empirical testing ground, and the analytical strategy is similar to the previous study. Blom-Hansen et al. (2016) compare local governments before and after the reform by imposing the post-reform structure on the pre-reform situation. Using a difference-in-difference design including appropriate controls, they investigate how expenditure per user in eight policy areas develops in amalgamating and non-amalgamating local governments in the period 2003-2014, that is, four years before the reform and eight years after.

The results confirm the theoretical expectations of no size effects. In all areas where welfare services are provided by institutions below the jurisdiction level – schools, childcare, and eldercare – jurisdiction size is unrelated to expenditure levels. For two non-welfare areas with services provided at the municipal level – roads and administration – increased jurisdiction size is related to lower expenditures. In only one welfare area – labor market activities, which

are not provided by institutions below the jurisdiction level – is there a link between expenditure levels and jurisdiction size, but the relationship is *positive*. In other words, large local governments spend *more*, not less, than small ones in this area. For total expenditures across eight policy areas, no significant effect of jurisdiction size is found. This result echoes findings from a study of Dutch municipal amalgamations (Allers and Geertsema, 2016). In sum, in most welfare areas, there is no direct link between the welfare state and the size of local governments, at least as measured by local expenditure on welfare services within the empirical range of Danish local jurisdiction sizes.

Jurisdiction size and the effectiveness of welfare programs

The hope that larger jurisdiction size will lead to better economic outcomes can be fulfilled if costs are lower. Based on the results just presented, this seems not to be the case. But the hope can also be fulfilled if higher quality is obtained in larger jurisdictions. For constant costs, a higher quality would mean that welfare services can be produced more effectively in larger jurisdictions. This means that one important question remains unanswered: Is jurisdiction size related to the quality of welfare services? Similar arguments apply. Larger jurisdictions may enjoy economies of scale due to increased specialization and the possibility to recruit competent staff (Dahl and Tufte, 1973: 110-117). The counter-arguments are similar: Larger jurisdictions entail less competition, and larger jurisdiction size does not automatically imply larger firm size. Even the methodological problems of endogeneity are similar and can be addressed with the same quasi-experimental design. In addition to this, welfare service quality is elusive, either because quality is hard to define or simply hard to measure. This problem of defining welfare service quality particularly applies to wicked problems (Rittel and Webber, 1973), such as welfare services for children with special needs and special education, and many other welfare services where solutions are not always known, and it is unclear whether a problem has been – or can be – solved. But even when means and ends are known and uncontroversial, systematic accounts of quality are rare.

To address these problems, Blom-Hansen, Houlberg and Serritzlew (2021) focus on the effectiveness of public schools in municipal-

ities before and after the Danish amalgamation reform. The reform is used as a quasi-experiment as described above, and public schools are selected because they devote many resources to measure quality in the form of school exams. School exams cover most pupils, they focus on outcomes, are measured independently of the organization (thanks to external examiners), and measure learning, which is of course one of the main goals of schools. Hence, it is possible to obtain good measures of quality for public schools.

The results show that grades have increased in Danish public schools after the reform. However, the increase is almost identical in public schools located in amalgamated and non-amalgamated municipalities. This indicates that the larger jurisdiction size does not affect quality in public schools. Similar analyses of another measure of school quality, namely completion of upper secondary education, show the same result. Combined with the result that costs remain similar for amalgamated and non-amalgamated municipalities, it becomes clear that jurisdiction size is not related to effectiveness of welfare services, at least when it comes to public schools.

Conclusion

Local government plays an important role in welfare states. Many services are provided at the local level, although with considerable variation among countries. Local welfare service provision can make sense both from an economic and a democratic perspective. At the local level, it is possible to tailor services to local demands and needs. This can potentially entail an economic welfare gain that is infeasible if the service is provided at the national level. Service provision at the local tier of government can also have implications for economies of scale. Furthermore, local service provision allows for local political control of welfare service. This brings important political questions close to citizens, and this again can have implications for democratic participation and political efficacy.

A very fundamental aspect of how local government is organized is size. Local government can be fragmented with many small municipalities, and local politics can be close to citizens but with limited potential for economies of scale. Or local government can be consolidated with larger municipalities and more potential for economies of scale but also a larger distance between citizens and politicians.

We have explored, based on the Danish local government amalgamation reform of 2007, how the size of local governments affects the effectiveness of welfare programs, the costs of running the political system, and local democracy. When it comes to welfare expenditure and effectiveness, the effects are limited. This suggests that economies of scale play a limited role since local welfare provision takes place at the 'plant level', that is, at local institutions such as schools and daycare. Increasing the size of local government does not automatically increase the size of local welfare institutions. We also see limited effects on effectiveness. However, local political systems are affected by size. On the one hand, the costs of running them are higher in smaller municipalities, so here we do see evidence of economies of scale. On the other hand, smaller municipalities tend to perform better on democratic outcomes.

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