

# Inter-municipal cooperation in Hungary: The factors explaining cooperation in service delivery <sup>1</sup>

*Éva Margit Kovács (kovacseva@uni-nke.hu)*

*Assistant Professor of National University of Public Services, Former research fellow of Interior Ministry of Hungary*

*Paper presented by Tamás Szabó,  
Research consultant of Interior Ministry of Hungary*

## **Abstract**

Inter-municipal cooperation (hereinafter: IMC) is an important element of local government reforms across Europe. There is a growing attention both in academic literature and on governments' reform agendas to examine the forms and results of different IMCs. This wide-spread phenomenon did not avoid Hungary either. There has been a long discussion since the early 90s – the establishment of the current local government system including almost 3200 local governments with extremely broad scope of responsibilities – on the adequate forms of IMC. Despite of this permanent debate and the introduction of many government policies intending to stimulate the greater cooperation on local level, the rationalities behind IMC and the factors that might trigger local governments to engage in increased cooperation with their neighbors have not been systematically analyzed yet. Hence, this study aims to explore what factors explain the different levels of cooperation among local governments. There is strong evidence underlined also by previous studies that service delivery infrastructure (organizational factors), spatial factors and economic constraints are significant drivers (or barriers) of IMC. Our study presents an analysis explaining the effect of these factors on the actual number of formalized IMCs among Hungarian local governments in the field of service delivery. By this it provides a better understanding of the factors driving IMC. Based on the preliminary results of this study future empirical research should give more elaborated attention and a deeper understanding on how these factors might affect the cooperation arrangements and its results themselves.

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### **Inter-municipal cooperation in Service Delivery: a Spreading Phenomena**

Inter-municipal cooperation (IMC) in many ways and forms has been a wide - spread phenomenon of local government reforms in the last decades. The increasing cooperation in service provision on the local level was triggered by various contextual conditions. These included the growing pressure on municipalities including the declining fiscal conditions, the increasing, or at least transforming nature of service obligations required by central government, the increasing public needs, and inhabitants' expectations for better services and more effective government operations. Most often these factors forced local governments' political leaders and managers to search for new forms for providing public services. One of the possible solutions to replace the traditional "one town - one public service provider" is cooperating with other local governments. According to Hilvert and Swindell cooperation in service delivery might result a number of positive effects (Hilvert – Swindell 2013). These include cost savings by exploiting scale of economies, overcoming resource scarcity, the creation of opportunities for new and innovative ways to achieve high quality and less expensive service delivery, and, in the final analysis, enabling local governments to better meet citizens' expectation.

Local governments can cooperate in service provision in many different forms and with many different actors – either other local governments or corporate as well as NGO entities. But the cooperation between local governments, in particular, provides a form enabling them to avoid outsourcing the services to external provider. Academics identified two common forms of cooperation between local governments in public service delivery. These are, firstly, IMCs and, secondly, contracting out the provision of service delivery to other municipalities (cf. Spitzel 2015, Siegel 1999). In our study, we focus on the former groups that is IMCs, because recently the relevance of this issue in Hungarian reform agenda is growing. In the last years, the government has introduced new initiatives that enable to increase the mandatory and quazi mandatory cooperation between local governments.

According the definition of Council of Europe, IMCs involve two or several local authorities (local governments) "having a status of legal persons, endowed with competences, powers and resources in accordance with the European Charter of Local Self-Government" (Council of Europe 2013).

In our understanding the forms of IMC cannot be simplified to the commonly created legal entities. The forms of inter-municipal cooperation might be very heterogeneous.

With regards to its form, IMCs can range from the formal relationships – usually based on contractual relations –, through inter-municipal agreements prescribed by the law, to the more ad hoc, sometimes not even institutionalized informal cooperation forms (Teles 2016 :19-20). It also relevant to consider the direction of cooperation and the participants' level in the government structure.

Another classification of IMCs is based on the drivers of the cooperation. In some cases, local governments are required by law or central authorities to engage in IMCs. There are however voluntary forms of IMC too, in which case local governments' agreement to cooperate represents their mutual interest and negotiations.

The forms of IMCs can be classified according to the main tasks or aims for which they were created. Cooperation involving municipalities can spread from single purpose

to multipurpose arrangements. The main goals of IMC range from the exchanges of information through mutual consultation through to the more formal interactions between bodies, mutually making decisions, creating plans, and even municipalities working together to jointly operate public service infrastructures or to co-creation shared services.

Municipal cooperation structures also vary on the heterogeneity and numbers of participants involving small and large numbers of municipalities and including municipalities with various size and capacity or sometimes involving private or civil sector organizations and upper level government. (Hulst – Montfort 2007).

In most cases municipalities decide to cooperate on the basis of their internal characteristics. According to Bel and Warner's (2015) a meta- regression analysis based on the existing empirical literature explaining the rationalities behind the inter – municipal cooperation fiscal constraints, spatial, and organizational factors (Bel and Warner 2015) often referred and verified as significant drivers of cooperation. Recent researches (Gerber – Loh 2014, Carr, Gerberm, Lopher, 2009) suggest that fiscal pressures play a role in support for cooperation between local governments. Municipalities with lower property and lower tax bases may consider the inter- municipal cooperation as a potential way of cost savings and cooperation means a higher value for them in comparison with the wealthier communities (cf. Gerber – Loh 2014).

With regards to the spatial factor, the literature on local government often pays attention to the optimal size for service provision. The most common measure in the empirical literature for economies of scale is population. “When municipal boundaries do not match the service area, some form of municipal cooperation is a natural alternative to achieve both economies of scale and fiscal equivalence” (Bel - Warner, 2015). Most studies find that IMC is negatively related to the size of municipalities. (Arntsen - Dag Torjesen - Karlsen 2018, Hefetz - Warner - Vigoda- Gadot 2012; Bel- Fageda - Mur 2014). As an organizational factor - with some restriction - we are focusing on the availability of infrastructure (asset) that is necessary to deliver services. The possibility of joint production with neighboring municipalities is to some degree determined by the availability of the number of service delivery infrastructures. According to Bel and Warner (2015) inter-municipal “cooperation is typically found to be higher when services are more asset specific” in general.

These explanatory factors are closely related - however cannot be fully restricted (cf. Gargan 1981) – to the public service capacity of the local governments, which is usually understood as those institutional, financial, organizational, human resources that enable local governments to perform their given task effectively and on a sustainable basis and with reduced dependence on external resources (Nwankwo et al. ). Therefore, in this study the above mentioned three factors are investigated that likely affect the public service delivery capacities of municipalities.

### **Research questions, research design, data and method**

The aim of this study is to explore what factors explain local governments' varying degree of engagement in IMCs. In particular, we test the effect of three (above mentioned) potential explanatory variables: local government size (as measured by the number of their inhabitants), the economic and the infrastructural capacity of local government.

To do so, we constructed a database including all Hungarian municipalities (altogether the data base contains 3154 municipalities, this number excluding Budapest and its

districts)<sup>2</sup>. We measured the extent, to which a local government engages in IMC on the basis of dummies indicating the presence or absence of the following, main forms of IMC (these forms of IMC are further investigated in the following section):

- Joint municipal offices (Közös hivatal)
- Inter-municipal agreement on service delivery involving the creation of a new legal entity (Társulás)
- Cooperation in the LEADER local action groups (LAGs/ Helyi Akciócsoport HACS)
- Cooperation in short – term projects (Konzorcium)– running for 4-6 years – for improving service delivery in specific certain field of local services within the region. These projects are often funded by the European Union and beyond inter – municipal cooperation it requires further engagement of the civil society, NGOs, local entrepreneurs and an active consultation with local citizens.

Our actual dependent variable indicating the number of IMCs was created on the basis of the above indicators.

In Hungary there are no comprehensive data on IMCs. Therefore, our data were collected from different, publicly available government registers<sup>3,4</sup>. These data bases are restricted to formalized IMCs, therefore informal IMC arrangements – extending beyond the scope of the above typology – are not covered in our analysis.

Our database comprised also different independent variables<sup>5</sup> possibly influencing the number of IMCs. The set of explanatory variables that we analyzed were selected on the basis of theoretical concerns and observing the empirical findings of previous studies. We define our independent variables as follows:

- The infrastructural capacity in this research refers to the number of available organizations providing basic public services in the given municipality. As a public service infrastructure, we considered the nursery, kindergarten, elementary school, general practitioner's services, outpatient clinics, elderly care facilities, public transportation services, public utility, water supply services, sports center, fire station.
- The size of the municipality calculated on the number of inhabitants is identified as the second explanatory variable in our study.
- Fiscal scarcity is also seen as an important drivers of local government service delivery reform, particularly as a driver for greater cooperation. Therefore, we also analyze role of local governments' economic situation. This feature is often measured by the indicator based on the local tax on company sales per capita<sup>6</sup> in Hungary. Although the indicator based on the local tax on company sales per capita might provide a limited – sometimes also biased – picture of the actual economic situation of the municipality, it is the most widespread and major economic indicator in Hungary that has been taken into consideration during the allocation of central resources and benefits.

In order to investigate the relationship between the number of IMCs (dependent variable) and these three explanatory variables we used bivariate correlation analyses.

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<sup>2</sup> Budapest and its districts were excluded from the further analyses because of their special geographical and legal status that effects their behavior on co-operation.

<sup>3</sup> Hungarian State Treasury (Magyar Államkincstár) register on inter-municipal agreements on service delivery; Hungarian National Statistical Office

<sup>4</sup> New Hungarian Rural Development Program Website (Új Magyarország Vidékfejlesztési Program) - LEADER local action groups (LAGs)

<sup>5</sup> Data collected by the Hungarian National Statistical Office

<sup>6</sup> In Hungarian: "Egy főre jutó adóerőképeség"

([http://www.allamkincstar.gov.hu/files/2014\\_szamvitel/2014\\_02\\_25/AD%C3%93K\\_TAX.XLSX](http://www.allamkincstar.gov.hu/files/2014_szamvitel/2014_02_25/AD%C3%93K_TAX.XLSX)) The calculation method: local tax on company sales per capita x 1,4.

## **The Hungarian local government system. Basic characteristics, structural features and responsibilities**

The Hungarian administrative structure comprises three levels: the central, the territorial (county) and the local level. The current Hungarian municipal system was established in 1990, immediately after the transition. The municipalities were granted a large degree of discretion in their own actions. Decentralized self-government operates on two levels: on the territorial level one can find 19 county local governments and the local government of the capital city, Budapest. On the lower level there are 3178 local governments. These local governments operate in towns and villages with a relatively broad scope of competences in providing services. They are responsible for a broad variety of public services, including municipal development, kindergarten services and education (until 2012), social and childcare services, basic health care services (GPs), cultural services (library, support of art and theatre etc.), local environmental and nature protection, water supply management, housing management, disaster management, coordination of public employment programs in their towns or villages financed and created by central government, supporting local businesses and tourism, supporting sport activity and promoting youth policy, handling minority and ethnicity policy issues, waste management, and maintaining district heating services. In addition – until 2013 – the chief administrative officers exercised a broad variety of administrative tasks delegated to them by the central government.

In the light of the fact that the Hungarian municipal system is dominated by very small villages with a population of less than 1000 inhabitants (more than 50% of the municipalities are in this category) and endowed with very restricted resources, one would find this broad scope of task portfolio very contradictory. Throughout the post-transition years there were some legislative acts<sup>7</sup> enacted with the intention of stimulating IMC. They created additional financial incentives for IMCs. Still, no significant changes were achieved until 2011.

The historically stable and seemingly inalterable scope of local governments' autonomy and authority – both on the territorial and local level – underwent significant changes from 2012. This overarching administrative reform was triggered not only by power related motives. “The harsh external (macroeconomic, financial and social) conditions set, from 2008 onwards, by the economic crisis and the related requirements of the EU and IMF with regards to the containment of public deficit and debt posed a serious additional challenge” (Hajnal – Kovacs 2013). The major root causes of the problems can be tracked back to the structural and operational features of local government system:

Firstly, every municipality had the right by the Constitution to create its self-government<sup>8</sup>. Around 3178 local governments were created by the establishment of local government system. This system was highly and permanently criticized for the inefficient manner of service provision, being rigid in adapting central government initiatives and ineffective to cooperate. The system often referred as “difficult to manage both from administrative and financial aspects” (Dobos 2014).

Secondly, the phenomena of significant decentralization of tasks from the state to local level started in 1990 was not followed rationally and consciously by the decentralization

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<sup>7</sup> The Act CXXXV of 1997 on the Associations and Co-operation of Local Governments and the Act CVII of 2004 on Multi-Purpose Associations of Local Governments in the region

<sup>8</sup> Although a small restriction was introduced in 1994, which allowed the establishment of new local governments only in communities of more than 300 inhabitants, the ageing society produced lots of villages where less than 100 people lived. (Dobos 2014)

of financial resources to the municipalities. It became quite common for municipalities to use loans for the daily operation. As a consequence of the combination of small size and resource scarcity of local governments with the broad task portfolio many local governments used loans for maintaining their day-to-day service provision.

Thirdly, the other often mentioned problem of Hungarian municipal system is the absence of a strong middle level (local) government system. Originally the county local governments were established to coordinate the complex regional development projects and to provide regional level public services. In spite of this initial idea in practice the middle level remained a ‘missing tier’ (Zongor 1999) in Hungary so that finally it was not able to achieve a better coordination of local service delivery.

In the realm of the overarching government reform started in 2010 – following the sharp political change in the national political landscape – numerous local governmental reform measures were motivated by the intention of consolidating municipalities, balancing the scope of duties with their actual capacities, spreading a higher “paternalistic” central control over the operation and budgeting of municipal system. The mayor elements of the post-2010 local government reforms are the following:

- Refinement of central government finance on local service delivery and introducing the task-based financial system.
- Restrictive central regulations on taking loans by local governments and a Local Government Debt Consolidation program was introduced between 2012 and 2013.
- A major element of the local government reform was the re-division of tasks and powers of municipalities and increasing the role of the state in local service provision. The majority of public administrative functions – delegated by the state to local government – were taken over of by the newly established district (“járás”) level centrally supervised structures, the so-called government administrative offices. Also certain field of the health care services got centralized and taken over by the government administrative offices.

### **An overview on the most common forms of formalized inter- municipal cooperation in Hungary**

In Hungary the legal framework for local government allows a relatively large freedom and broad scope of cooperation to choose how and in what forms they will provide services.<sup>9</sup> It allows for the local governments a greater flexibility to make a choice about their engagement in any cooperation arrangements, choose the appropriate implementation form taking into consideration their available resources and capacities and being aware for their citizens’ needs. In Hungary the local public services can be delivered by local governments themselves (in- house service provision), through different forms of IMC, or in cooperation with other external actors such as civil, and religious organizations or with private firms. It is a common practice, in Hungary that IMCs involve a formal agreement establishing coordination arrangement or formal procedures.

One of the wide- spread forms of mandatory IMC is the creation of joint local government offices (közös hivatal). The primary function of the joint local government office is to support the work of the local government committee by preparing and implementing the local regulations and providing administrative services in those cases are delegated to the scope of authority of the mayor and the chief executive officer. Based on data gleaned from 2017 there are 738 joint offices across Hungary and 2633

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<sup>9</sup> According the Article 32.1 (c) paragraph of the Fundamental Law (Alaptörvény) the local governments are enabled to manage their tasks and duties by themselves in the frame of obeying the essential rules.

municipalities - 82.8 percent of the total 3178 municipalities- are members in one of them. For municipalities with a population under 2000 joining a joint local government office is compulsory since 2011.<sup>10</sup> The rationality behind this IMC structure is that the small municipalities are unable to maintain their own administrative apparatus due to their scarce resources.

The other most common, but voluntary form of cooperation is the creation of single- or multi- purpose IMC agreements and local government partnerships (társulás). The Hungarian Local Government Act allows, and based on other sectoral legislation, even incentivizes local governments to create agreements with other local governments in order to implement any of their tasks. These IMCs might comprise only one specific purpose, but it is more common to make an agreement on delivering more than one public services jointly. These agreements also create a formalized organizational structure (a partnership) that enable the co-decision making among the local governments involved. According to the register of the Hungarian State Treasury (data from February 2017), there are 1517 local government partnerships in Hungary. These associations comprise more than 10765 memberships.

The third form of IMC is the cooperation in Local Action Groups (LAG). LASs are created in order to qualify for applying for the European Union's LEADER funds aiming to support rural development projects, the revitalization of rural areas and to create jobs. LAGs are created to implement the Local Development Strategy within a certain region. An interesting feature of this cooperation structure that it has to comprise both public – mainly local governmental - and private organizations from villages in order to guarantee a broad representation of different socio-economic actors. This network type of local government cooperation extended to the entire territory of Hungary. 96 LAGs operate across the country encompassing 3020 municipalities out of the 3178. LAGs can be seen as a form of wide-range cooperation either in terms of their territorial scope and also in terms of the heterogeneity of the actors. A typical LAG encompasses 20-40 municipalities and beyond the large number of local governments cooperating in the group, a wide range of social actors (local businesses, NGOs) are also involved in the cooperation.

The fourth form of IMC covered by our investigation is cooperation forms for supporting short-term projects for improving service delivery. In these cases, cooperation between local governments are motivated by economic incentives. This category might include consortia created in order to submit a bid to tenders announced for government / EU funds where one of the major condition for application might be creating cooperation across municipalities and integrating a large number and broad scope of public organizations and social actors. In our database there are two types of such short term cooperation: the Children's Chance Programs (CCP), where 473 local governments participating in one of the 24 consortia and the "Developing territorial cooperation programs for local governments in convergence regions" where 1744 municipalities were involved in 83 regional programs.

## **Findings**

In this section we will present the results of our correlation analysis. We calculated bivariate Pearson correlation coefficients between the number of IMCs a local government is involved in (dependent variable) and our three explanatory variables the service delivery infrastructure, the size of municipality and economic capacity (Local tax on company sales per capita) that might significantly affect and drives the local governments to cooperate with their neighbors. The three factors – that were

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<sup>10</sup> Act CLXXXIX of 2011 on Local Government of Hungary (Mötv.)

operationalized in the above section – are used as the explanatory variables in the correlation analysis, which aims to quantify the strength of relationship between the cooperation behavior of local governments and those factors that might affect the public service delivery capacity of municipalities. Spearman rank correlation is used to measure the degree of association between the different explanatory factors and the number of IMCs (dependent variable). The variables are measured at a ratio scale.

First, we analyzed the correlation between the number of inter – municipal cooperation and the public service infrastructure capacity of local governments. The correlation between the two variables is, albeit statistically significant, only relatively weak and negative, so that the higher the public service delivery capacity a municipality has, the lower lever of the local government’s cooperation activity is and vice versa, the lower public service infrastructures the municipality has, the higher number of inter-municipal co-operation it is engaged.

*Table 1 – Analysing correlations between the public service infrastructure capacity and the number of formalized inter- municipal cooperation*

		Public service infrastructure capacity	Number of formalized IMC
Public service infrastructure capacity	Pearson Correlation	1	-.139**
	Sig. (2-tailed)		.000
	N	3153	3153
Number of formalized IMC	Pearson Correlation	-.139**	1
	Sig. (2-tailed)	.000	
	N	3153	3154

\*\* . Correlation is significant at the 0.01 level (2-tailed).

Secondly, we calculated the correlation between the number of inter – municipal cooperation and the size of municipality. The correlation between the two variables is, again, statistically significant, weak and negative, so the higher number of population a municipality has, the lower level of the local government’s cooperation activity is. And also, municipalities with smaller size are usually cooperating in more IMC arrangements, than those with larger size.

*Table 2 – Analysing correlations between the population (size of the municipalities) and the number of formalized inter-municipal cooperation*

		Number of formalized IMC	Population 2015 (municipalities)
Number of formalized IMC	Pearson Correlation	1	-.114**
	Sig. (2-tailed)		.000
	N	3154	3153
Population 2015 (municipalitis)	Pearson Correlation	-.114**	1
	Sig. (2-tailed)	.000	
	N	3153	3153

\*\* . Correlation is significant at the 0.01 level (2-tailed).



Thirdly, the correlation analyses between the local tax on company sales per capita and the number of engagements in IMC also indicates significant negative correlation.

*Table 3 – Analysing correlations between the economic capacity and the number of formalized inter-municipal cooperation*

		Local tax on company sales per capita (2017)	Number of formalized IMC
Local tax on company sales per capita (2017)	Pearson Correlation	1	-.029
	Sig. (2-tailed)		.100
	N	3154	3154
Number of formalized IMC	Pearson Correlation	-.029	1
	Sig. (2-tailed)	.100	
	N	3154	3154

\*\* . Correlation is significant at the 0.01 level (2-tailed).

According to these results, it seems that those local governments that have adequate public service capacity are less open to deliver their public services in cooperation with other local governments. While the municipalities where the local governments have modest capacity are more likely opened for joint service delivery and willing to cooperate with their neighbors because they might have not even the necessary resources to provide the basic local public services independently or they could only provide these services with lower efficiency or lower quality than in a cooperation with other local governments.

### Conclusion

According to the Hungarian case, there have been different strategies initiated to solve the problems of the increasing resource scarcity and decreasing service delivery capacity of municipalities. From 2012, a revision and redistribution of tasks and responsibilities between the central government (and its lower level bodies) and local governments have started. The centralization and the transfer of responsibilities for the provision of education services, certain health and social services, state administrative services to upper level government were part of the overarching government reform. On the other hand, the delivery of most of the local services are still remained the local governments' duties. Increasing the number of IMCs is another way to dealing with challenges. It has a clear advantage over the territorial reorganizations of local tasks, because it provides more flexibility to take special needs and characteristics of the municipalities into consideration. According to the literature "IMC is much easier to adapt to new circumstances and developments" (Hulst - van Montfort 2007).

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